

Economic Instruments And The Environment: Selected Legal Issues

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EXECUTIVE SUMMARY

This report examines several legal issues that should be addressed before establishing economic instruments for environmental protection. Economic instruments are tools created by law which either encourage improved environmental behavior or discourage environmentally damaging activities such as pollution. Many environmental organizations advocate improving Canada's existing environmental laws by using economic instruments such as deposit refund systems, subsidies and discharge fees in combination with traditional regulatory approaches.

Canadian environmental law currently consists largely of regulations and permits or licenses which prohibit industries from exceeding permissible levels of discharges. Breaches of these regulations are punished through fines and criminal law sanctions. This "command and control"

approach to regulation has successfully reduced pollution from many sources, but cannot overcome obstacles to effective regulation in areas where enforcement is difficult.

This report looks at three economic instruments which are intended to improve environmental protection:

- discharge fees.
- deposit refund systems.
- tradeable permit systems.

Also, administrative penalties and ticketing are examined.

The legal issues examined include: which level of government has the constitutional ability to adopt these instruments; what provisions must be included in statutes that establish these instruments; potential administrative and constitutional law challenges to economic instruments laws and implementation and how to prevent them; and challenges to economic instruments based on international trade law.

Constitutional Power to Establish Economic Instruments

Both federal and provincial governments have broad powers to establish economic instruments although neither level of government has an unlimited power to establish any form of instrument. Any law must be based on one of the subjects or "heads of power" listed in the *Constitution Act, 1867*. Municipalities and regional districts have whatever powers are delegated to them by provincial or federal law.

The provinces have a very wide power to establish economic instruments subject to only a few restrictions. Provinces can: establish discharge permit trading systems for any discharges within the province; establish revenue generating discharge fee systems; place charges on products that lead to emissions; impose a system of discharge fees or tradeable emission permits for vehicles; and establish a system of deposits and refunds for products or substances that are sold or produced within the province.

Although the federal government has a more limited power to establish economic instruments for environmental protection, its power is still significant. Economic instruments can be used by the federal government to help solve global, national or regional problems which need a coordinated national approach. A federal system of tradeable permits for pollutants that cause acid rain or global warming would likely be justified if the provinces show an inability to cooperate effectively in dealing with these issues. Deposit refund systems for persistent toxics, carbon taxes, tradeable permit systems for discharges into fish bearing waters, discharge taxes, and tradeable permit systems for the phase out of health threatening substances may also be justified under federal heads of power; however, these systems must be carefully designed if they are to be constitutionally valid.

A Common Approach to All Economic Instruments.

Regulations can be challenged on the basis that they go beyond what a Legislature or Parliament intended when they delegated a regulation making power. Enabling legislation for discharge fees, tradeable permit systems, administrative penalties and deposit refund systems should be sufficiently comprehensive to allow all necessary aspects of a working system to be established. Legislation should also establish basic principles that ensure environmental protection is the foremost goal of economic instruments. Enabling legislation for all instruments should ensure regulation making and administration of the systems is informed by an open discussion of public concerns.

Administrative Law Challenges to Economic Instruments

The decisions of administrators in exercising discretion given to them by statute or regulation can be challenged in Court if the discretion is exercised for an improper purpose or in an unfair manner. The degree to which any system of economic instruments can be challenged on either basis depends on the amount of discretion granted to administrative officials. For instance, discharge fees based on permitted discharges rather than actual discharges are difficult to challenge because there is little discretion left to individual administrators. There is more potential to challenge fees based on estimates of actual discharges. Appeals of discretionary administrative penalties and discretionary approvals of permit trades are also very likely. Appeals to the courts can, however, be limited by statutorily structuring the exercise of discretion, by creating a fair process for appealing decisions, and by following these processes.

Discharge Fees

Under a discharge fee system government sets a price on each unit of pollutant discharged, and the polluter pays to government an amount equal to the quantity of the pollutant discharged times the unit price. The unit price varies according to the toxicity or environmental effect of the pollutant. Comprehensive enabling legislation for discharge fees should provide:

- that discharge fees are not limited to recovery of administration costs;
- authority for discharge fee surcharges in environmentally sensitive or polluted areas;
- authority for fees being charged on the production, import or the use of products where production, import or use of a product will likely lead to a discharge;
- regulations defining methods of monitoring or estimating discharges;
- charges to be levied on different classes of polluters with provision for partial rebates where performance standards are met; and
- grant inspectors the power to enter on to any premises where emissions are occurring and inspect emissions, monitoring equipment and data.

While discharge fee systems could potentially be challenged in the Courts on the basis of the *Canadian Charter of Rights and Freedoms* (the "*Charter*") the chances of successful appeals are limited. The *Charter* generally does not protect economic rights or liberty to carry on business. Nor are equality provisions of the *Charter* infringed by discharge fees that apply unequally to different regions or businesses. Discharge fees will generally not be contrary to trade law.

Administrative Penalties and Ticketing

Two reforms of the existing system of command and control regulations are examined along with discharge fees: monetary administrative penalties and ticketing. While discharge fees are intended to encourage reduction of discharges below permitted levels, administrative penalties and ticketing are intended to ensure that there are meaningful incentives to reduce discharges below permitted levels. Ticketing streamlines the criminal process for minor offences so that prosecution of large numbers of minor offences is possible. Administrative penalties provide regulators with an enforcement option which may in some cases be more practical than criminal prosecution.

Enabling legislation for administrative penalties should provide that:

- administrative penalties are in addition to any criminal sentences;
- automatic penalties are payable whenever permit violations occur;
- polluters are liable to pay minimum fines regardless of fault;
- further discretionary administrative penalties may be levied where harm to the environment may have occurred or where the permittee was at fault; and
- provide that penalties be used for environmental purposes.

Enabling legislation for ticketing already exists for both the federal government and many provinces.

Automatic administrative penalties payable whenever a permit violation occurs are valid under the *Charter* and could probably be used in combination with criminal sanctions. The constitutionality of using discretionary administrative penalties and criminal prosecutions for the same offence is less clear; however, if legislation distinguishes between the role of administrative penalties and criminal sanctions, combined use of both should be permissible. Legislation should specify that the purpose of the fines is to encourage compliance with environmental regulations and permits, to compensate for environmental damage or potential damage, and to recover administrative costs related to the imposition and investigation of regulatory breaches.

Deposit Refund Systems

Deposit refund systems include relatively simple product deposits and refunds payable on the sale and return of beverage containers, car bodies, batteries, and pesticide containers. Product deposit refund systems such as these have been applied in Canada, the United States and some European countries. Product deposit refund systems for hazardous materials such as solvents and oils have also been proposed. Substance deposit refund systems -- where a deposit is paid when a substance is produced or imported and refunded when the substance is exported or properly disposed of -- have been proposed in Europe. In a substance deposit refund system the refund is paid despite substantial changes in the form of the substance.

Enabling legislation for product deposit refund systems should:

- include a broad power to implement deposit refunds for different products;
- provide for restrictions on when products are eligible for refund;
- provide for product charges and product bans;
- allow for regulation of labeling requirements; and
- include sufficient offence provisions to guard against refund fraud.

Some additional provisions necessary for substance deposit refund systems include:

- a power to define acceptable disposal by regulations and provide mechanisms to determine acceptable disposal;
- provision for import levies and export refunds in lieu of substance deposits and refunds; and
- provision for a central agency to delegate different functions to appropriate agencies. For instance, customs and excise officials are already trained to collect excise taxes on the primary production and import of substances such as alcohol and would be well suited to collect substance deposits and provide refunds on export.

Deposit refund laws will likely withstand any attacks based on the *Charter*. Even in the United States, where economic interests receive some constitutional protection, attacks by industry on deposit refund systems have failed. Such attacks are less likely to succeed in Canada where there is even less constitutional protection of business interests.

Challenges to deposit refund systems based on trade law are unlikely to succeed although there is some potential for challenges to measures related to deposit refund systems. For instance, labeling requirements, product charges and products bans may have more of an impact on foreign manufacturers than domestic manufacturers and could be challenged as non-tariff barriers. While governments should be wary of such challenges, successful challenges can probably be avoided by basing measures on a clear environmental rationale.

Tradeable Permit Systems

Under a tradeable permit system the government establishes a cap for total allowable emissions and distributes permits for this amount amongst polluters. Polluters that keep their emissions below allowed levels may sell their surplus permits to other firms. The number of permits which are distributed to polluters -- and the cumulative emissions allowed under all the permits -- are reduced pursuant to a schedule set out in legislation or regulations.

According to some economic theory, tradeable permit systems can place a limit on the total discharges of a particular substance and reduce this limit over time at the lowest possible economic cost. However, there are significant practical problems in actually implementing a system of tradeable permits. This is especially true for sources which do not have accurate discharge data and for discharges that may have localized effects. Any proposal for tradeable permit systems will have to be carefully examined to ensure that it will actually reduce pollution, at a lower cost than command and control strategies. Both draft legislation and draft regulations must be carefully analyzed with public input before any system is adopted.

The following are some of the salient concerns which should be addressed in any generally applicable enabling legislation. Some recommendations may not be necessary for enabling legislation aimed at a specific problem. Enabling legislation should:

- provide a broad power to establish systems governing a variety of products and discharges;
- allow regulation of trading between different areas and sub-areas;
- require a timetable for reducing permitted discharges in areas where environmental quality objectives have not been met;
- allow local area caps to be established for discharges which may have localized effects;
- allow permits to be allocated by a variety of means and require periodic auctions of permits with revenues dedicated to program administration and environmental remediation;
- if tradeable permits can be created by reductions at sources not mandatorily included in the tradeable permit system those creating the permits should bear the onus of proving that an actual reduction has taken place. Future rights to discharge attached to these permits should be automatically phased out with an accelerated phase out available where regulators believe the emissions may have been reduced in any event;
- provide for approval of trades to ensure that trade-offs in the same pollutants will not lead to a degradation of environmental quality and that actual emission reductions have occurred;
- generally require continuous emissions monitoring systems;
- provide substantial automatic minimum fines for permit exceedances and high minimum penalties for other offences; and
- permit delegation of functions to either local or multijurisdictional boards, but only permit interjurisdictional trading with jurisdictions that have equivalent legal provisions and administrative practices.

Finally, challenges or claims for compensation based on property rights in tradeable permits can be avoided by specifically stating that permits are revocable licenses.

In short, the validity of economic instruments for environmental protection under the *Charter*, the potential for administrative law challenges to administrators' discretion, and the potential for challenges under international trade law must be considered in designing legislation and regulations for economic instruments. However, these concerns can be largely dealt with through well planned legislation and regulations. Both federal and provincial governments have wide powers to establish economic instruments, which may prove to be useful regulating tools for environmental protection.



INTRODUCTION

The search for improved environmental protection -- and the urgency of the task -- challenges us to be ever alert to new or improved ways to accomplish our goal. Increasingly we recognize that our approach must encourage prevention rather than remediation of environmental degradation and that a variety of tools need to be used together to achieve this end.

This report examines the use of economic instruments: tools that attempt to take advantage of market forces to prevent pollution and influence behaviour. These tools are not viewed as a single solution to environmental ills. However, an appropriate mix of environmental regulations and economic instruments may accelerate our progress to better environmental protection.

Canadian environmental law consists largely of regulations or permits and licences which prohibit industries from exceeding prescribed levels of emissions, require industries to install certain abatement equipment or prohibit the use of substances for specific purposes. If a business exceeds permitted levels or breaches regulations it can be charged with an offence and, if convicted, it can be punished by a fine or jail sentence. This "command and control" system of regulation has been successful in some areas of pollution. Atmospheric lead concentrations in Vancouver have dropped dramatically in the last fifteen years; the frequency of carbon monoxide concentrations in the Lower Fraser Valley exceeding air quality objectives has declined in the same period; and the discharge of organochlorines in pulp mill effluent has been reduced substantially in only a few years. [(1) -- 1. See British Columbia, Ministry of Environment Lands and Parks, *State of the Environment Report for British Columbia* (Victoria: Ministry of Environment, Lands and Parks, 1993) at 14 to 24.]

However, there is a growing recognition that command and control strategies have limitations in terms of their ability to modify destructive conduct through enforcement alone.

To help address these issues, some environmental organizations and economists have advocated the use of economic instruments in conjunction with environmental regulations, to create incentives for compliance. Economic instruments include discharge fees, product levies, taxes, deposit-refund systems, subsidies and tradeable permit systems. This report examines three economic instruments that can be used to improve environmental protection: discharge fees, deposit-refund systems and tradeable permit systems. The report addresses some of the legal issues related to the use of these instruments. It examines which government bodies have the constitutional power to adopt these instruments and what potential legal challenges governments might face if economic instruments are implemented. The emphasis in this report is on the legal issues related to the implementation of economic instrument rather than a comprehensive analysis of their overall effectiveness.

The first crucial legal issue is to determine which level of government has the power to implement an economic instrument. [Chapter 1](#) deals with the constitutional powers of the Canadian federal and provincial governments to implement economic instruments.

[Chapter 2](#) discusses general legal principles that must be taken into account in developing and implementing legislation for economic instruments. It reviews various rules of statutory interpretation that will affect which issues should be addressed in legislation and which issues should be addressed in regulations. It also discusses some of the basic principles of

administrative law that will affect how statutes are drafted and how economic instruments should be implemented to avoid successful court challenges.

[Chapter 3](#) reviews discharge fees, administrative penalties and ticketing systems, all of which are intended to provide increased economic incentives for polluters to reduce discharges. Under a discharge fee system, a price is set on each unit of pollutant discharged, and the polluter pays to the government an amount equal to the quantity of pollutant times the unit price. Discharge fees should be used in conjunction with maximum limits on permitted emissions. If sufficiently high, discharge fees are an effective incentive to reduce emissions below permitted levels. [(2) -- 2. J. Opschoor & H. Vos. *Economic Instruments for Environmental Protection* (Paris: Organization for Economic Cooperation and Development, 1989).] Product charges are considered to the extent they may be the most effective means of placing charges on emissions. For instance, if fees are to be placed on carbon dioxide releases this will be most effectively and efficiently done by placing a tax on the carbon content of fossil fuels.

While emission charges also have the potential to improve the efficiency of the tax system by discouraging undesirable side effects of economic activity, they may, in some cases, have greater impacts on low income earners. These adverse distributive effects must be addressed.

[Chapter 3](#) examines the necessary components of enabling legislation and the potential *Charter of Rights*, administrative law and trade law challenges to discharge fees. Chapter 3 also examines these same issues -- *Charter*, administrative law and trade law challenges -- in relation to two policy options often associated with discharge fees: administrative penalties and ticketing. While discharge fees encourage reductions in emissions below permitted levels, administrative penalties and ticketing increase the costs to polluters when permitted emissions are exceeded. Administrative penalties allow either automatic or discretionary monetary penalties to be levied on polluters when they breach regulations or permits. Ticketing allows enforcement officers to charge offenders, bypassing the onerous procedure involved in most criminal charges.

[Chapter 4](#) discusses deposit refund systems. These systems can range in complexity from the simple bottle deposit system used for beer bottles in Canada to deposit systems used for particular substances such as lead, cadmium or chlorine. For bottle deposits, the charge is levied at the time of sale and refunded when the bottle is returned to a designated collection point. A substance deposit is levied when the substance is manufactured or imported and refunded when it can be proven that the substance has been exported or disposed of suitably. Deposit-refund systems are appropriate where the policy objective is not only to discourage the use of the product but also to encourage its proper disposal.

[Chapter 4](#) also examines specific legal issues relating to deposit-refund systems, including necessary implementing legislation, *Charter* challenges, trade law challenges and administrative law challenges. It raises issues that legislative drafters and administrators should consider before implementing deposit-refund systems rather than comprehensively analyzing whether or not they are an appropriate tool in any particular circumstance.

[Chapter 5](#) discusses one of the most complex economic instruments, a tradeable permit system. Under this type of system, the government establishes a cap for total allowable emissions and

issues permits for a specified level of emissions. Firms that keep their emissions below their allowed level may sell their surplus allotments to other firms. The number of permits which are allocated to polluters -- and the cumulative emissions allowed under all the permits -- are reduced pursuant to a schedule set out in legislation or regulations. Tradeable permit systems thus have the theoretical potential to achieve specific overall emissions reductions.

However, the potential and the reality may be quite different. Problems relating to monitoring and ensuring that traded permits represent actual reductions in emissions may negate the potential advantages of tradeable permit systems. Chapter 5 examines the elements of enabling legislation required to withstand legal challenges and to ensure that the environmental goals of tradeable permit systems are not abrogated by practical problems of implementation.

Many of the safeguards suggested in [Chapter 5](#) may affect the ability of tradeable permit systems to reduce emissions at the least possible cost. For example each of the safeguards necessary to ensure that a tradeable permit system for nitrous oxides and volatile organics actually reduces pollution may have an economic cost. The added administrative burden of a tradeable permit system and the reduced potential for savings on abatement costs may indeed make tradeable permit systems inappropriate for dealing with some environmental problems. This should be studied further before any tradeable permit system is adopted. Our purpose here is to explain rather than advocate the use of tradeable permit systems. Any proposed tradeable permit system must be carefully scrutinized to ensure that it will result in a cleaner environment. Further, the success of a tradeable permit system is entirely dependent on the adequacy of enabling legislation and implementing regulations.

We hope this report will be a useful addition to the growing body of literature considering the application of economic instruments for environmental protection in Canada.

Chapter 1 THE CONSTITUTIONAL CONTEXT

Both the federal and the provincial governments have wide powers to enact economic instruments for environmental protection, but neither level of government has an unlimited power to enact any instrument for any purpose. Governments must make decisions about possible solutions to environmental problems in the context of the constitutional limits to their powers. These jurisdictional limits relate to geographic and subject matter. Provincial laws apply only within provincial boundaries, whereas federal laws have national application. The division of powers between the federal and provincial governments regarding subject matter is based on the *Constitution Act, 1867* as interpreted by the courts. [(3) -- 3. *Constitution Act, 1867* (U.K.), 30 & 31 Vict. c. 3.] If the federal government's legislation goes beyond the subjects over which the federal government has jurisdiction, the law can be challenged.

Also, all Canadian governments are bound by constitutional rules that govern relations between government and citizen. Laws cannot limit rights protected by the *Canadian Charter of Rights and Freedoms* (the "*Charter*") [(4) -- 4. *Canadian Charter of Rights and Freedoms*, Part 1 of the *Constitution Act, 1982*, being Schedule B of the *Canada Act, 1982* (U.K.), 1982, c. 11.] unless the limitations are reasonable, prescribed by law and "demonstrably justified in a free and democratic society." [(5) -- 5. Section 1; Section 33 of the *Charter* permits provincial legislatures and the federal Parliament specifically to override a *Charter* right, but doing so is usually politically unacceptable.] If *Charter* rights are infringed by laws that create systems of economic instruments the laws can be struck down by the Courts.

This chapter deals with the constitutional limitations to establishing economic instruments and reforming environmental protection legislation. The focus is on the law relating to the division of powers between the provinces and the federal government, because the issues relating to the division of powers tend to be similar for all economic instruments. The provisions in the *Charter* which may be used to challenge economic instruments or law reform aimed at environmental protection are discussed briefly. Since *Charter* issues tend to vary from instrument to instrument, the chapters on specific instruments each include a more complete analysis of how the *Charter* might be interpreted .

The discussion of the division of powers in this Chapter does not deal with which level of government should establish particular economic instruments.

The Division of Powers

This section addresses federal, provincial and municipal authority to establish economic instruments for environmental protection. It is difficult to state with certainty which level of government has the jurisdiction to regulate a particular problem using a particular instrument because of the degree of overlap of federal and provincial jurisdictional powers. However, generally the provinces have a clear power to establish economic instruments for most purposes and the federal government has a broad power to establish economic instruments in many cases.

The lack of clarity surrounding the constitutional parameters of each level of government has often resulted in inaction: each level of government is wary of infringing on the jurisdiction of

the other, while at the same time each jealously protects its area of jurisdiction. The purpose of this section is to indicate the breadth of each level's jurisdiction for the purpose of reducing this constitutional inertia. Where there is government action in questionable areas of jurisdiction it will no doubt be challenged by polluters. Some jurisdictional issues may be clarified as a result -- a positive development in a country that is often plagued by considerable doubt regarding its constitutional division of powers.

The "environment" is not a subject specifically assigned in the constitution to either the federal or the provincial government. Both levels of government have limited powers to regulate the environment based on other subject matters, or "heads of power", [(6) -- 6. "Heads of power" is a term for the subjects listed in sections 91 and 92 of the *Constitution Act, 1867*. Provincial heads of power, listed in section 92, are the subjects over which the provinces have exclusive jurisdiction. Federal heads of power, listed in section 91, are the subjects over which the Federal government has exclusive jurisdiction.] over which they have exclusive authority under the *Constitution Act, 1867*. [(7) -- 7. See *Friends of the Oldman River Society v. Canada (Minister of Transport)* (1992), 7 C.E.L.R.(N.S.) 1 (S.C.C.) at 46 to 49.] Jurisdiction will "depend not only on factual matters such as the source, nature and consequences of particular ... pollution, but also on the precise form and scope of any law aimed at it." [(8) -- 8. Alastair R. Lucas, "Harmonization of Federal and Provincial Environmental Policies: The Changing Legal and Policy Framework," in O. Saunders, ed., *Managing Natural Resources in a Federal State* (Calgary: Carswell, 1986) at 34.]

The federal power to protect the environment is based on a number of federal "heads of power": fisheries; [(9) -- 9. Section 91(12), *Constitution Act, 1867*.] land reserved for Indians; [(10) -- 10. *Ibid.*, s. 91(24).] peace, order and good government; [(11) -- 11. *Ibid.*, s. 91.] criminal law; [(12) -- 12. *Ibid.*, s. 91(27).] federal undertakings [(13) -- 13. *Ibid.*, s. 91(29) and 92(10).] and federal public land. [(14) -- 14. *Ibid.*, s. 91(1).] The provinces' powers over the environment are based mainly on their authority over property and civil rights [(15) -- 15. *Ibid.*, s. 92(13).] as well as local matters. [(16) -- 16. *Ibid.*, s. 92(16).] The federal government has the power to levy both indirect and direct taxes [(17) -- 17. *Ibid.*, s. 91(3).] while the provinces only have authority to levy direct taxes. [(18) -- 18. *Ibid.*, s. 92(2).] Each of these subject matters is relevant to the use of economic instruments, but none of them gives an unlimited authority for either level of government to apply a particular economic instrument in any case.

Municipalities and other regional or local governments have no constitutional powers, as they are usually created by provincial and sometimes federal [(19) -- 19. Local boards can also be created by the federal government to deal with areas of federal jurisdiction.] legislation; but they can be delegated powers from either level of government.

To understand each level of government's authority, it is necessary to review some general concepts of constitutional law as well as each level of government's specific powers. This chapter discusses provincial powers first, because the provinces generally have the clearest authority in relation to environmental protection and economic instruments. Moreover, an understanding of the provincial powers in this field is essential to an understanding of the federal government's powers.

Double Aspect Doctrine and Paramountcy

It is important to understand a few basic aspects of Canadian constitutional law before examining the powers of each level of government. First, merely because the federal government has the power to regulate a particular subject does not mean that the provinces do not have this power and vice versa. Overlapping jurisdiction is a phenomenon of Canadian federalism. Under the double aspect doctrine a provincial law regarding a matter of provincial jurisdiction may validly affect a matter that comes within federal jurisdiction. [(20) -- 20. *Alberta Government Telephones v. Canada (Canadian Radio-Television & Telecommunications Commission)*, [1989] 2 S.C.R. 225 at 275.] However, the "dominant and most important characteristic" [(21) -- 21. See *Friends of Oldman*, above at footnote 7 at 45.] or "pith and substance" of a government's law must be in relation to one of its heads of power. These same rules apply to federal laws which affect a provincial area of jurisdiction.

Where there is an overlap, both provincial and federal laws apply unless there a conflict in operation, "as where one enactment says 'yes' and the other 'no', or compliance with one is defiance with the other," or unless there is a clash of purposes. [(22) -- 22. *Multiple Access Ltd. v. McCucheon*, [1982] 2 S.C.R. 161 at 163; *Bank of Montreal v. Hall*, [1990] 1 S.C.R. 121.] Where there is such a conflict the federal law will be paramount. [(23) -- 23. "Paramount" is a legal term meaning the federal law will prevail over the provincial law.]

Due to the double aspect doctrine and the need for express conflict in regulations the instances of application of the paramountcy doctrine are rare. Courts have generally allowed federal and provincial laws to operate concurrently if at all possible. For instance, a federal tradeable permit system for sulphur dioxide emissions would not necessarily conflict with provincial laws requiring permits for such emissions. The clash of purposes test or operational conflict test suggests that if both federal laws and provincial laws apply to a firm, the firm could not rely on its federal permit alone. As discussed in Chapter 5 on tradeable permits, the application of provincial regulations should be clearly dealt with in federal legislation. This would avoid uncertainty about the application of the paramountcy doctrine and ensure that regulations necessary for protection of the local and workplace environments remain in effect. Overlapping federal and provincial jurisdiction in which the citizen must obey the highest legislative standard may be most effective means of protecting the environment at both the local and national level.

Provincial Heads of Power

The provinces have a wide power to regulate the environment, based on their power over "property and civil rights." [(24) -- 24. *R. v. Lake Ontario Cement Ltd.* (1973), 11 C.C.C. (2d) 1 (Ont. H.C.).]

This section first discusses the breadth of environmental legislation which can be based on the "property and civil rights" head of power and some of the other provincial heads of power that may be relevant in the context of economic instruments. Second, it discusses the exceptions to the general rule that the provinces have the power to enact economic instruments for environmental protection. These exceptions include the inability of the provinces to establish economic instruments which are "in pith and substance" within an area of exclusive federal

jurisdiction, and the inability of the provinces to pass laws which apply outside of their territory. Third, this section discusses the limitation of provincial taxation powers to raising revenue through direct taxes in the province.

Breadth of Provincial Powers

The property and civil rights head of power is the constitutional basis for almost all provincial environmental initiatives. Provincial environmental assessment legislation, regulations restricting the production and use of ozone depleting substances, legislation requiring permits to introduce discharges into the environment and permits requiring certain monitoring devices and imposing reporting requirements are all based on the property and civil rights head of power.

There are several other provincial heads of power which are relevant to the authority to use economic instruments for environmental purposes. For instance, the provincial power to impose direct taxes is the basis for green levies charged under the B.C. *Social Service Act*. [(25) -- 25. See discussion in at footnote 274.] Also the provincial powers over municipal institutions and matters of a merely local or private nature in the province, [(26) -- 26. S. 92(16), *Constitution Act, 1867*.] combined with the "property and civil rights" head, form the constitutional basis for most municipal regulation of environmental matters. Municipalities, regional districts, and improvement districts such as the Greater Vancouver Sewerage & Drainage District are all created by the Province. The Province can by statute delegate any of its environmental regulation powers to regional districts and municipalities. [(27) -- 27. The federal government can also delegate functions to provincially created boards or municipalities; however, it is doubtful if such delegation could be forced unwillingly on a municipality or regional district.]

Provincial Powers and Federal Jurisdiction

Despite these wide ranging powers, there are some limits on provincial regulation of the environment. First, provinces cannot regulate any subject area which is a matter of exclusive federal jurisdiction. For instance, the province could not pass regulations aimed specifically at controlling discharges from federal lands, an area of federal responsibility. However, a provincial law will be valid so long as its "dominant and most important characteristic" comes within the very wide ambit of property and civil rights or some other head of provincial power.

This interplay between the provincial property and civil rights head of power and the federal heads of power is the most important limit on provincial powers over the environment. Most of the remainder of this part focuses on the federal powers, which may have an impact on the provincial power to regulate for environmental purposes where there is a direct conflict between the two levels of government.

The Provinces and local governments have been reluctant to regulate in the areas of federally owned land and federal undertakings to avoid interfering with federal jurisdiction. While the federal government has jurisdiction to regulate federally owned land, a number of Supreme Court of Canada cases have clearly stated that Indian Reserves and other federal lands are not enclaves from provincial regulation. [(28) -- 28. In both *Montcalm Construction Inc. v. Minimum Wage Comm'n* (1978), 93 D.L.R. (3d) 641 (S.C.C.) at 660, and *Cardinal v. A.G. Alta.* (1973), 40

D.L.R.(3d) 553 (S.C.C.) at 560 the court rejected the enclave theory.] Valid provincial legislation of general application will apply to federal land located within the province so long as it does not conflict with federal regulation and so long as it is regulation of activities on the land rather than regulation of the land itself. For instance, a provincial order requiring the preparation of a report on contamination of federal land was valid because it did not purport to regulate the use or ownership of the federal land. [(29) -- 29. *Canadian National Railway Co. v. Ontario (Director appointed under the Environmental Protection Act)* (1992), 8 C.E.L.R. (N.S.) 1 (Ont. C.A.). But see also: *Canadian Occidental Petroleum v. North Vancouver* (1986), 13 B.C.L.R. (2d) 34 (B.C.C.A.); *Delta v. Aztec Aviation Group* (1985), 28 M.P.L.R. 215 (B.C.S.C.); *International Aviation Terminal Inc. v. Richmond (Township)* (March 16, 1992) Van. Reg. CA01384, (B.C.C.A.); *Surrey v. Peace Arch Enterprises Ltd.* (1970), 74 W.W.R. 380 (B.C.C.A.) all of which involved provincial or municipal attempts to actually regulate use of federal land through zoning and building by-laws.] Similarly, provincial game laws have been held to apply to federal land. [(30) -- 30. *R. v. Harrt and Stewart* (1979), 94 D.L.R. (3d) 461 (N.B.S.C., App. Div.).]

It is expected that Courts would hold that provincial or local government pollution regulations and bylaws validly apply to federal lands such as ports and Indian reserves so long as the regulations do not conflict with federal regulation of the land. A conflict may exist where federal regulations or local port corporation bylaws regulate pollution and specifically allow emissions which are not allowed by provincial regulation. [(31) -- 31. See Jack Woodward, *Native Law* (Vancouver: Carswell, 1989) at 120 to 129 for discussion of application of provincial and municipal laws to Indian Reserves. Bands do not currently have an express power to regulate emissions although general regulations are in effect: s. 81, *Indian Act*, R.S.C. 1985, c. I-5; the federal government's current waste disposal regulations for reserves are unlikely to conflict in operation with economic instruments for environmental protection: see *Indian Reserve Waste Disposal Regulation*, C.R.C. 1980, c. 960. Although the *Canadian Environmental Protection Act*, R.S.C. 1985, 4th Supp., Part IV allows the federal government to pass regulations for federal lands no such regulations have in fact been passed.]

Further, the federal power to regulate federal undertakings, such as interprovincial and international transportation and communications businesses, [(32) -- 32. Note that a firm or individual who uses a vehicle to cross provincial or international boundaries from time to time does not become a federal undertaking: *Agence Maritime v. Canada Labour Relations Board*, [1969] S.C.R. 851.] does not mean that such undertakings are immune from provincial laws. [(33) -- 33. See s. 92(10) and 91(29) of the *Constitution Act, 1867*, and Hogg, *Constitutional Law of Canada*, 2d. ed. (Toronto: Carswell, 1977) at 321 to 329.] The only limit on the provincial power is that it must not "affect a vital part of the management and operation of the undertaking". [(34) -- 34. *Commission du Salaire Minimum v. Bell Telephone Co.*, [1966] S.C.R. 767. See also *Alberta Government Telephones*, above at footnote 22 at 275 and *Irwin Toy v. Quebec*, [1989] 1 S.C.R. 927.] Provincial environmental laws have consistently been held to apply to federal undertakings. [(35) -- 35. See *R. v. Canadian Pacific Ltd.* (1993), 10 C.E.L.R. (N.S.) 169 (Ont. C.A.); *R. v. Norris* (1992), 17 W.C.B. (2d) 160 (Ont. Ct. J. Prov. Div.); and *R. v. Nitrochem Inc.* (1992), 8 C.E.L.R. 283 (Ont. Ct. J. Prov. Div.).] Economic instruments are unlikely to infringe the "vital part" rule since discharges are unlikely to be viewed as a vital part of an undertaking.

The only exception is if a provincial law has a disproportionate effect on a federal undertaking, so that the federal undertaking is hampered in comparison to intraprovincial undertakings. Thus, a discharge fee system or tradeable permit system that charges interprovincial trucking firms for discharges outside the province might be invalid because it would hamper interprovincial trade, especially if enacted by more than one province. [(36) -- 36. See below at footnote 38.]

Extraprovincial Effect

Provincial law cannot have any extraterritorial effect. Thus, discharge charges could not be imposed on polluters in the Yukon or Washington discharging into a river flowing through B.C. [(37) -- 37. In *Interprovincial Cooperatives v. The Queen* (1975), [1976] S.C.R. 477 the Supreme Court of Canada held that a Manitoba law could not impose liability on an Ontario company who, with legal authority from Ontario, was polluting a river draining into Manitoba. The minority in *Interprovincial Cooperatives* characterized this extra provincial aspect of the Manitoba legislation as a valid incident of intraprovincial regulation. The majority decision is difficult to reconcile with *The Queen v. Thomas Equipment*, [1979] 2 S.C.R. 529; see Peter Hogg, *Constitutional Law of Canada*, 3d. ed. (Toronto: Carswell, 1992) at 13-11.]

Extraprovincial effects and mobile sources

The inability of the province to pass laws which apply extraprovincially raises the question of whether the province could establish an effective economic instrument system for mobile sources of air pollution. A provincial law requiring British Columbia drivers to pay a fee or purchase a permit based on miles driven during the year and Air Care readings or car specifications might be challenged on this basis. It could be argued that where a motorist's driving was not limited to British Columbia a fee was in effect being charged for emissions occurring in another province. Despite this potential challenge, it is likely that the province can successfully and effectively apply economic instruments to vehicles.

First, it would be possible to prevent this sort of challenge by allowing motorists to avoid paying charges for out of province driving. [(38) -- 38. Cases dealing with application of provincial sales tax are instructive in this regard. The *Constitution Act, 1867*, in S. 92(2), only allows provinces to levy direct taxes "within the province" (*Constitution Act, 1867*, S. 92(2)). The Courts have rejected provincial taxation of aircraft and of alcohol served in aircraft where the aircraft's only presence in the province is transitory -- for instance, where the aircraft is only flying over or landing in the province (*Manitoba v. Air Canada*, [1980] 2 S.C.R. 303, 111 D.L.R. (3d) 513; *Canadian Pacific Airlines Ltd. v. British Columbia*, [1989] 1 S.C.R. 1133; 59 D.L.R. (4th) 218.). Courts have, however, allowed the application of provincial taxes to aircraft or railway cars used partly in the province so long as the tax is applied in proportion to the amount of their use within the province and the provincial taxation does not place a "undue burden" on inter-provincial transportation firms or inter-provincial movement of goods (*Canadian Pacific Airlines Ltd. v. British Columbia*, leaves this issue open in the context of aircraft (at S.C.R. 1154); *Dow Chemical Canada Inc. v. British Columbia* (1992), 67 B.C.L.R. (2d) 145 (B.C.C.A.) decides this point in regard to railway rolling stock.)] For instance, if a fee or permit system were established for the Lower Mainland of British Columbia, and cars insured for use in the Lower Mainland were given an opportunity to claim exemptions for miles traveled outside that area there would

be only an incidental and, probably, unchallengeable extraprovincial effect. [(39) -- 39. This system would require some infrastructure to police but may be workable. For instance, offices at all arteries leading into and out of the permit trading area would have to be established to take odometer readings for vehicles claiming the exemption. Some sort of identification would be necessary to indicate when such exemptions are being claimed (for instance, different coloured license plate renewal stickers) so that cars claiming exemptions could not use exemptions while in the permit area. Claims for minor exemptions for short periods outside the province could be avoided by having an administration fee to cover the costs of exemption requests.]

Courts might uphold a provincial tradeable permit or discharge fee system for provincially licensed vehicle emissions even if there is no means to claim exemptions for out-of-province travel. The charges could be characterized as an aspect of "property and civil rights", payable solely due to a vehicle owner's decision to license the vehicle in the Lower Mainland. Liability for fees only occurs where a person has submitted to licensing in B.C. In this regard, the Courts have upheld the power of provinces to tax residents of the province taking into consideration "extraprovincial facts" such as the amount of property held outside the province. [(40) -- 40. Hogg, above at footnote 37, at 30-11; *Bank of Toronto v. Lambe* (1887), 12 App. Cas. 575.] It follows that they also should be able to take into account other "extraprovincial facts" such as miles driven outside the province.

Also, the Supreme Court of Canada has held that a New Brunswick wholesaler selling machinery to an Alberta retailer is bound to purchase back stock from the Albertan retailer pursuant to a generally applicable Alberta law requiring wholesalers to buy back unsold stock. [(41) -- 41. *The Queen v. Thomas Equipment*, above at footnote 37.] The Court stated, "If a manufacturer wants to have his farm implements sold here he must comply with the rules of the game, as it were, established by the Legislature in Alberta." [(42) -- 42. *Ibid.*] An analogous argument could be made for drivers licensing themselves in B.C.

However, cases on the application of provincial sales taxes [(43) -- 43. See footnote 38 above.] have expressed concern that provincial laws not be a barrier to interprovincial trade or federal undertakings. Thus Courts might be more likely to uphold application of provincially imposed economic instruments to mobile sources if some sort of proportionality is applied at least to federal undertakings, such as interprovincial or international trucking and shipping firms.

Indirect Taxation

The provincial government cannot raise revenue through indirect taxation. [(44) -- 44. *Constitution Act, 1867*, s. 91(3) and 92(2).] Many economists would argue that discharge fees are indirect taxation. However, since discharge fees are not charged on the basis of products produced or imported and will not be passed on to consumers where a product can be manufactured without causing pollution, they would likely be classified as direct taxation by the Courts. [(45) -- 45. See *Canadian Industrial Oil & Gas Ltd. v. Government of Saskatchewan* (1977), 80 D.L.R.(3d) 449 (S.C.C.) for a discussion of how courts distinguish between direct and indirect taxes.] Discharges resulting from the manufacture of a good are analogous to products purchased and incorporated into another product which is sold. Courts have held that taxes on

such products are direct. [(46) -- 46. *Cairns Construction Ltd. v. Saskatchewan*, [1960] S.C.R. 619, 24 D.L.R.(2d) 1.] The tax

"... is not related or relateable to any unit of the commodities which the company advertises and sells and cannot be regarded as a tax which clings as a burden to a unit of the commodity or its price.... The mere fact that the company may be able to shift the burden of the tax to the purchasers of its merchandise is not ... sufficient to make the tax an indirect one... [(47) -- 47. This quote is from the New Brunswick Court of Appeal unanimous decision on a case dealing with a tax on catalogues: *Simpsons-Sears Ltd. v. Provincial Secretary of New Brunswick* (1976), 71 D.L.R. (3d) 717 at 724, rev'd (1978), 82 D.L.R.(3d) 321 (S.C.C.). Although the Supreme Court of Canada was equally divided on this point, the decision of the New Brunswick Court of Appeal has been supported by G.V. La Forest prior to his appointment to the Supreme Court of Canada: G.V. La Forest, *The Allocation of Taxing Power Under the Canadian Constitution*, 2d ed. (Toronto: Canadian Tax Foundation, 1981) at 83.]

Similarly, discharge fees are analogous to business taxes based on the number of places of business a firm operates or the capital it employs. Courts have upheld these as direct taxes. [(48) -- 48. *Bank of Toronto v. Lambe*, above at footnote 40.]

A problem arises if "proxy discharge fees" are applied to a product that is likely to be resold. Use of charges based on carbon content of fuels or volatile organic content of solvents has been identified as a more efficient means of discouraging carbon dioxide production or VOC releases from consumer sources than applying discharge fees to measured releases. [(49) -- 49. Canada, *Economic Instruments for Environmental Protection: Discussion Paper* (Ottawa: Supply and Services Canada, 1992) at 34 to 35.] However, a tax on fossil fuels or solvents applied when they are first sold is clearly an indirect tax. [(50) -- 50. *British Columbia (Attorney General) v. Canadian Pacific Railway*, [1927] A.C. 934, [1927] 4 D.L.R. 113 (P.C.).]

A carbon tax or fee that is part of a larger regulatory scheme aimed at environmental protection may be valid since provincial charges will generally be valid as long as they are ancillary to a valid provincial regulatory scheme. [(51) -- 51. See *Re LaFarge Concrete Ltd and District of Coquitlam* (1972), 32 D.L.R.(3d) 459 (B.C.C.A.).] If carbon taxes or taxes on solvents were imposed on the import or production of these products as part of a larger provincial discharge fee system this might change the character of invalid indirect taxation into valid provincial regulation. This characterization would be supported by dedicating revenues to a purpose such as environmental protection, applying the charge under the same statute as other discharge fees, and allowing exemptions if the product is exported or if it can be proven that its use did not result in discharges.

Federal Heads of Power

The main federal heads of power that relate to environmental protection are:

- **Peace, Order and Good Government.** The so called "POGG" power may be the most important of the federal heads of power. It includes a power to regulate matters of national concern and

transboundary pollution. Although the exact limits of this power are uncertain it is the basis for many federal environmental initiatives.

- **Trade and Commerce.** This head of power may influence how the "Peace, Order and Good Government" power is interpreted and could arguably be a basis for many far reaching economic instruments.
- **Criminal Law.** This power may be important in the sphere of establishing economic instruments for dealing with discharges that threaten human health.
- **Any Mode or System of Taxation.** Federal taxation powers may support some forms of discharge fees and could certainly support "proxy discharge fees" such as carbon taxes or taxes applied to other products that lead to discharges.
- **Sea Coast and Inland Fisheries.** This power allows use of tradeable permits and possibly other economic instruments which are clearly aimed at protecting fish habitat.

Peace, Order and Good Government

The Courts have generally interpreted the POGG power narrowly, stating that the federal government only can rely on the power in order to deal with "matters of national concern" and matters not dealt with in the *Constitution Act, 1867* (the "residual power"). Nonetheless, this power is important in the environmental context.

Interprovincial Discharges

It is clear that pollution of interprovincial and international rivers and airsheds can be regulated under the federal POGG power. Some judges have justified this on the basis that it comes within the residual power of POGG; [(52) -- 52. *R. v. Crown Zellerbach Canada Ltd.* (1988), 3 C.E.L.R. (N.S.) 1 (S.C.C.).] others have based their decision on the national concerns test discussed below. [(53) -- 53. *Interprovincial Cooperatives*, above at footnote 37.]

In one case, a minority of the Supreme Court of Canada upheld the federal power over pollution of interprovincial rivers through an analogy with the federal power over trade and commerce, [(54) -- 54. *Ibid.*] which allows regulation of intraprovincial trade and commerce incidental to the primary purpose of regulating interprovincial trade. This suggests the POGG power will allow regulation of discharges within a province if the regulation is part of an attempt to deal with an interprovincial or international problem. One case even suggests that any regulation of air pollution would be justified by the POGG power. [(55) -- 55. See *Re: Canada Metal Company and The Queen*, (1982), 144 D.L.R.(3d) 124 (Man. Q.B.)] It is likely that any regulation of discharges that pose significant cross boundary problems would be justified, especially where interjurisdictional agreements deal with the problem.

The fact that the federal government has the power to regulate pollution of international or interprovincial waterways and airsheds does not mean that the provinces do not have powers to impose higher standards in their regulation of these waterways and airsheds. [(56) -- 56. In *R. v. Nitrochem Inc.*, above at footnote 35, the court held that provincial statutes which validly supplemented CEPA provisions for discharges into interprovincial waters valid. See also *TNT Canada Inc. v. Ontario* (1986), 1 C.E.L.R. (N.S.) 109 (Ont. C.A.).]

National Concern Doctrine

As noted above, the POGG power also allows the federal government to legislate over "matters of national concern." These can be matters which, although originally matters "of a local or private nature in the province" and thus subject to provincial jurisdiction, have grown to be matters of national concern. [(57) -- 57. *R. v. Crown Zellerbach Ltd.* above at footnote at 52; *Labatt Breweries of Canada Limited v. Canada (A.G.)*, [1980] 1 S.C.R. 914 at 944 to 945.]

The National Concern Test

A problem such as legislation of acid rain must fulfill several tests before the federal government can regulate it on the basis of the national concerns test. One aspect of the national concerns doctrine is that provinces are unable to effectively regulate a problem. The "provincial inability" test has been met where failure to deal with the intraprovincial aspects of a problem could have an adverse effect on extra-provincial interests. [(58) -- 58. *R. v. Crown Zellerbach Ltd.*, above at footnote 52. Other cases have expressed the provincial inability test in more demanding terms stating: "the most important element of national concern is a need for one national law which cannot realistically be satisfied by cooperative provincial action because the failure of one province to cooperate would carry with it grave consequences for the residents of other provinces:" *Labatt Breweries, Ibid.*]

One cannot assume that there must be an undivided jurisdiction in one or other level of government to deal with a subject. Also, in order to qualify as a matter of national concern a matter must have "a singleness, distinctiveness and indivisibility that clearly distinguishes it from matters of provincial concern and a scale of impact on provincial jurisdiction that is reconcilable with the fundamental distribution of legislative power under the Constitution." [(59) -- 59. *R. v. Crown Zellerbach Canada Ltd.*, above at footnote 52, at 32.] Finally, the federal government must use measures which are the least intrusive to provincial interests.

National Concerns Doctrine and the Environment -- the Crown Zellerbach Case

The national concern doctrine is discussed at length in the case of *R. v. Crown Zellerbach*. [(60) -- 60. *R. v. Crown Zellerbach Canada Ltd.*, above at footnote 52.] The defendant logging company had been charged, under the *Ocean Dumping Control Act*, with dumping waterlogged wood waste that it had dredged from provincial Crown property and disposed of in an adjoining area of provincial Crown property. The Supreme Court of Canada held, by a 5-4 majority, that the anti-dumping provision was constitutionally valid. Although both the decisions of the minority and the majority indicate that there are limits to the extent of the federal government's power under the national concern test, both found the federal government had a very substantial role in regulating pollution under this test.

The majority held that marine pollution, because of its predominantly extra-provincial and international character, could be distinguished from pollution of fresh waters or land and air. The majority's decision involved drawing an admittedly arbitrary line around discharges into marine water. Discharges into fresh water were excluded from federal jurisdiction under POGG. This made the subject of marine pollution sufficiently discreet to meet the requirements of singleness,

indivisibility and reasonable impact on provincial jurisdiction. The Court justified this distinction on the basis of the uncertainty involved in determining which marine pollution will cross provincial boundaries and different characteristics of marine pollution.

The minority focused on the fact that the substances regulated by the *Act* were not necessarily deleterious and might not cause pollution outside of the province. The minority agreed with the majority that the federal government had the ability to regulate extra-provincial ocean pollution by dealing with sources of pollution, including air, fresh water and groundwater pollution, that originate within the province.

However, the minority opinion stated that the federal regulations must be linked in some way to the basis for the federal power -- the control of extra-provincial pollution. It suggests that the necessary link could have taken the form of evidence that monitoring of all dumped substances is necessary to avoid ocean pollution (no such evidence was adduced) or a link in the wording of the statute. [(61) -- 61. See discussion below at footnote 91 on *R. v. Northwest Falling*.] The latter could be accomplished by prescribing pollutants which are potential cross boundary pollutants.

The minority opinion in *Crown Zellerbach* is important because it is reconcilable with the majority opinion. Neither rejected the federal government's power to regulate air or fresh water discharges and ground deposits that are somehow linked to cross boundary pollution.

The scope of the national concern test has been fleshed out in several other cases. In a 1992 unanimous decision, the Supreme Court of Canada stated that environmental control, as a subject matter, does not have the requisite distinctiveness to meet the test under the national concern doctrine. [(62) -- 62. *Friends of the Oldman River Society*, above at footnote 7, at 46.] This should not be seen as ruling out wide use of federal economic instruments based on the POGG power. The Court was referring to the environment in its broadest sense, including the social and economic environment. Moreover, many environmental pollution issues have the same degree of distinctness as marine pollution and it can be shown in many situations that intraprovincial sources of pollution must be controlled to deal with transboundary pollution.

Limits to the National Concern Doctrine? -- The Hydro Quebec Case

In *Attorney General of Canada v. Hydro Quebec*, [(63) -- 63. *Attorney General of Canada v. Hydro Quebec* (August 6, 1992), Shawnigan Reg. 410-36-000024-914 (Que. S.C.).] the Quebec Supreme Court held that regulations governing the release of PCBs made under the *Canadian Environmental Protection Act* ("CEPA") were unconstitutional. The Court found that environmental protection was too broad a subject for the national concern doctrine, and noted that CEPA did not merely regulate release but actual use. The Court did not accept Hydro Quebec's proposition that CEPA can only apply to localized releases if it is proven that they will inevitably spread to another province. Instead, it quoted from a lower Court decision which suggested that the main concern is whether release might have interprovincial effects and questioned whether the cradle to grave regulation of CEPA was necessary for regulating interprovincial releases.

Unfortunately the decision in *Hydro Quebec* is vague in its reasoning. It is currently under appeal. [(64) -- 64. Appeal date October, 1993. [Personal communication, Janet Davies, Environment Canada, Conservation and Protection Branch.]] While it raises some concerns it may not ultimately affect the implications of the decision in *R. v. Crown Zellerbach*.

Interlocking Legislation and Equivalency Agreements

The national concerns test depends in part on the potential for dealing with a problem through provincial cooperation and in part on the impact federal regulation of a subject will have on provincial jurisdiction. Three models of cooperative regulation should be considered when determining the provincial inability test and when considering the impact of federal legislation on provincial jurisdiction:

- Federal and provincial or multi-provincial statutes and regulations which interlock in a comprehensive scheme ("Interlocking Legislation");
- Federal legislation and regulations combined with provincial legislation that incorporates federal regulations by reference ("Referential Incorporation"); and
- Federal Legislation which applies nationally in the absence of equivalent provincial legislation ("Equivalency Schemes").

The first two models can be designed to effectively avoid any constitutional questions as to the validity of federal legislation. Thus, in areas where there is doubt as to the constitutional authority of either level of government there is a strong incentive for using Interlocking Legislation or Referential Incorporation. The Supreme Court of Canada has shown a great deal of deference to such Interlocking Legislation. [(65) -- 65. See text accompanying footnote 75.]

Unfortunately, both Referential Incorporation and Interlocking Legislation require a great deal of cooperation and may be thwarted by failure of one province to cooperate. However, since failure to reach a common approach may support application of the national concerns doctrine, where its application is unclear, Interlocking Legislation should be considered.

Equivalency agreements may also help ensure the validity of federal legislation. [(66) -- 66. CEPA includes provisions for equivalency agreements between the federal government and a province where the federal government agrees that provincial regulation of toxic substances is equivalent to a CEPA regulation.] First, equivalency provisions indicate that a statute is designed to minimize intrusion on provincial environmental jurisdiction, which may help support federal legislation based on the national concerns test. [(67) -- 67. This issue approach has yet to be considered by the Courts.] Second, the lack of equivalency agreements can be an indication of provincial inability. Finally, to the degree equivalent provincial regulations are in place the chances of challenges to the constitutionality of CEPA are reduced. [(68) -- 68. Alastair Lucas, "Jurisdictional Disputes: Is Equivalency a Workable Solution?" in *Into the Future, Environmental Law and Policy for the 1990s* (Edmonton: Environmental Law Centre, 1990) raises the issue of whether equivalency agreements undercut POGG because they indicate a provincial ability to regulate a problem. While this concern may be important in other contexts, it is not a problem with regard to most economic instruments for environmental protection, where the basis of the provincial inability test is the undermining of effective regulation by non-

cooperation of one or several provinces. In those circumstances federal legislation, whether or not it includes equivalency provisions, is aimed at overcoming provincial inability.]

In areas where application of the national concerns test is unclear, the federal government is well advised to attempt establishing Interlocking Legislation through forums such as the Canadian Council of Ministers of the Environment. If these attempts are unsuccessful, federal legislation, especially federal legislation with equivalency provisions, is more likely to be upheld by the Courts on the basis of the national concern doctrine.

Potential Application of National Concerns Doctrine

There are a number of potential applications of the national concern test under POGG for justifying economic instruments established by the federal government.

- Tradeable permits for NO_x and SO₂ possibly could be established along the lines suggested in the federal discussion paper ***Economic Instruments for Environmental Protection [(69) -- 69]*** Canada, above at footnote 49, at 27 to 30.

], with trading regions consisting of Western, Central and Atlantic Canada. The existence of a Canada-U.S. agreement on acid rain and the interprovincial nature of the trading areas support this being a distinct environmental concern of national importance. Even though not all SO₂ or NO_x crosses provincial boundaries, evidence may be presented to show that transboundary pollution requires a comprehensive application of legislation. While industries that are generally under provincial jurisdiction could argue that the program has a scale of impact on provincial jurisdiction not reconcilable with Canada's division of powers, the Court support for federal regulation of interprovincial pollution suggests that a SO₂ and NO_x trading program would be supported, especially if interprovincial cooperation is ineffective in dealing with acid rain.

- Tradeable permits for the production and import of fossil fuels, and carbon taxes could be established both on the basis of the global nature of climate change and on the basis that the federal government could effectively implement these schemes.
- Tradeable permits for solvent production and import as suggested in the discussion paper ***Economic Instruments for Environmental Protection, [(70) -- 70]*** Canada, above at footnote 49, at 35 to 36.

] or product charges for solvents, could potentially be justified on the basis that ozone pollution is a relatively discreet topic and that cooperative provincial regulation may not be a realistic alternative since failure of one province to cooperate would limit the effectiveness of the system. [(71) -- 71. Not only would it lead to problems associated with controlling inter-provincial transportation of solvents but also non-cooperative provinces could become pollution havens contributing to transboundary pollution.] Arguments in favour of the federal jurisdiction to impose such a system would likely be buttressed by the trade and commerce power.

- Deposit refund systems on toxic substances such as cadmium or pollution precursors such as sulphur likely would be justified both on the basis that there are transboundary problems with acid rain and that toxic substance contamination is a distinct subject with a transboundary

dimension. The difficulties inherent in provinces levying charges on imports into the province would help support the provincial inability test.

- Phasing out of toxic substances which pose a recognized human health hazard likely would be justified by the national concern test. For example, phase-out by tradeable permits analogous to that used for lead in gasoline and ozone depleting substances in the United States [(72) -- 72. See, Canada, above at footnote 49, at 23.

] could probably be justified by the national concerns test combined with the Criminal Power to prohibit releases that pose a significant and recognized threat to human health.

- Tradeable permit systems for ground level ozone precursors may be upheld on the basis of their transboundary effects and their health effect. While the federal government could try to justify regulation of NO_x/VOC in the lower Fraser Valley on the basis that some ozone may cross into Washington State, the Courts may see this as a "colourable" means of dealing with what is actually a local problem. On the other hand, a federal NO_x/VOC tradeable permit system might be valid for the Windsor/Quebec corridor where there is a larger transboundary dimension to ozone pollution. This would be especially true if Ontario and Quebec were unable to cooperate effectively in dealing with the problem.

Trade and Commerce

The federal power of trade and commerce and its relation to provincial powers over "property and civil rights" may be important in terms of the federal power to establish tradeable discharge permit systems.

Tradeable permit systems to control some discharges may be applied most efficiently to production and import of a particular substance such as VOC from solvents. [(73) -- 73. See Canada, above at footnote 49, at 27 to 30.] The issue is whether the federal government can regulate such manufacture and import under the trade and commerce power. Cases dealing with agricultural marketing boards indicate that federal legislation primarily aimed at interprovincial or international trade in a particular product will be valid, even if some regulated goods are manufactured, sold and consumed solely within a province. [(74) -- 74. *R. v. Klassen* (1959), 20 D.L.R. (2d) 406 (Man. C.A.) upheld application of the *Canadian Wheat Board Act* to intra-provincial grain works and trades and was approved by the Supreme Court of Canada in *Caloil v. A.G. Canada*, [1971] S.C.R. 543; *A.G. Manitoba v. Manitoba Egg and Poultry Assoc.* (1971), 19 D.L.R. (3d) 169.]

The trade and commerce cases have not held that where the market for a product is national in size, effective regulation can only occur at the federal level. However, federal action may be justified to impose a tradeable permit system for the manufacture or import of solvents on the basis of trade and commerce power in combination with the national concerns test. Since the federal government has some role in regulating import and manufacture of products, federal action under the national concerns doctrine is less problematic as it involves less of an intrusion on provincial jurisdiction.

One case, which upheld a federal marketing statute that applied to primarily intraprovincial markets involved an interlocking scheme of provincial and federal statutes. [(75) -- 75.

Agricultural Products Marketing Act, Re., [1978] 2 S.C.R. 1198.] Since the system encompassed interlocking legislation in the ten provinces, the Court's support of federal jurisdiction was probably out of deference to the unanimity among the jurisdictions. This sort of cooperation is ideal for ensuring the constitutional inviolability of any tradeable permit scheme. However, the practical difficulty of achieving this level of cooperation may require one or the other level of government to legislate on its own.

The federal trade and commerce power does not prevent provinces from exercising control over import and production of a particular product within the province. Cases generally support the notion that the provinces could establish a tradeable permit system for import or production of fossil fuels or solvents, as the Courts have upheld compulsory provincial marketing plans that apply to products imported into a province. [(76) -- 76. See *Carnation Co. v. Quebec Agricultural Marketing Board*, [1968] S.C.R. 238; followed in *Can. Indemnity Co. v. A.G.B.C.*, [1976] 5 W.W.R. 748 (S.C.C.); *Shannon v. Lower Mainland Dairy Products Board*, [1938] A.C. 708 (P.C.); and *Home Oil Distributors v. A.G. B.C.*, [1940] S.C.R. 444. Provincial schemes must not, however, be aimed at restricting inter-provincial trade disadvantaging out of province producers: see *A.G. Manitoba v. Manitoba Egg & Poultry Association*, [1971] S.C.R. 689 and Hogg, above at footnote 37 at 21-19.]

Finally, the federal government's power over interprovincial trade does not preclude a province's ability to adopt economic instruments which have the potential to impact on interprovincial trade. As long as the impact on interprovincial trade is not the intent of the legislation or regulation it should be immune from attack. [(77) -- 77. American cases which challenge deposit refund systems on the basis of their effect on inter-state trade have failed. American Courts have held that the commerce clause in the United States Constitution, which gives the federal government power to regulate interstate commerce, is not violated by deposit refund systems because the local benefits of these systems clearly outweigh any burden which might be imposed on interstate commerce: *Bowie Inn, Inc. v. Bowie*, 335 A. 2d. 679 (Md. 1975), *American Can Co. v. Oregon Liquor Control Commission*, 517 P. 2d. 691 (Ore. 1973). Courts have held that these laws are reasonably related to achieving the objective of environmental regulation and, even though the laws affect interstate commerce, the state is "under no obligation to maintain equal levels of competitive advantage for all producers regardless of their distance from the market.": *Midstate Distributing Co. v. Columbia*, (1981) 617 SW 2d. 419. Canadian Courts would almost surely come to a similar conclusion if a *bona fide* deposit refund system were challenged in Canada.]

Criminal Power

The federal government has exclusive authority to make criminal laws. While not every prohibition coupled with a potential jail sentence or fine can be justified as criminal law, the criminal power has been interpreted as allowing prohibitions aimed at protecting human health. [(78) -- 78. *Labatt Breweries*, above at footnote 57, at 934; *Section 5(a) of the Dairy Industry Act, Ref. Re.*, [1949] S.C.R. 1, aff'd [1951] A.C. 179.] Regulation of air pollution causing significant health effects has been upheld under the criminal law. [(79) -- 79. *Canada Metal Co. and the Queen, Re.*: (1982), 144 D.L.R. (3d) 124 (Man. Q.B.). There is some support for this decision in *Crown Zellerbach* above at footnote 52, at 44.]

This power could be used to justify enacting some types of economic instruments. For instance, it is possible to envisage a general prohibition against release of contaminants which pose health hazards, with an exception made for releases which are allowed by tradeable permits. Such a system should only be considered where it can lead to a faster phase out of a substance than command and control legislation.

The criminal law power can support a prohibition combined with exemptions so long as regulatory processes are used only to establish exceptions and not to define the offence. [(80) -- 80. For instance, in *Nova Scotia Board of Censors v. McNeil*, [1978] 2 S.C.R. 662 the Supreme Court of Canada held that film censorship was not criminal because it did not involve a prohibition and penalty. In film censorship the administrative process of the censorship board is necessary to determine when a film is banned. On the the other hand, in *R. v. Morgentaler*, [1976] 1 S.C.R. 616 and *R. v. Furtney*, [1991] 3 S.C.R. 89 a general prohibition was ascertainable without recourse to administrative processes, but exceptions from the prohibition could be made by administrative process.] While the federal government cannot justify a regulatory scheme as criminal law merely because it uses a penalty to enforce compliance, [(81) -- 81. In *Attorney General of Ontario v. Reciprocal Insurers*, [1924] A.C. 328, [1924] 1 D.L.R. 789 (P.C.). See also *R. v. Morgentaler*, [1976] 1 S.C.R. 616; and Hogg, above at footnote 36, at 18-24 to 18-26.] the use of a tradeable permit system for the phasing out of environmental contaminants that threaten human health could distinguish the system from other cases. However, any authority the federal government has to use tradeable permits based on its criminal law power is limited by several very important factors.

First, not all statutory prohibitions are based in the criminal law. The Courts have distinguished between "mens rea" [(82) -- 82. Latin for "guilty mind".] or criminal offences and regulatory or strict liability offences. The essence of criminal responsibility is that the accused must have intended the offence to occur. On the other hand, for regulatory offences a finding of guilt may be made even if the accused did not intend the offence to occur. To avoid conviction, the accused must not only prove lack of intent but also must show it exercised due diligence in trying to avoid the offence's occurrence.

Although the Supreme Court of Canada case [(83) -- 83. *R. v. Sault Ste. Marie*, [1978] 2 S.C.R. 1299.] which made the distinction between regulatory and criminal cases was not trying to determine the constitutionality of the offence, there is some authority that offences based on the criminal law power must be *mens rea* offences. [(84) -- 84. See *Hydro Quebec*, above at footnote 61, at 15-6; In *R. v. OMI International (Canada) Inc.* (1989), 4 C.E.L.R. (N.S.) 190 (Ont. Prov. Ct.) the Court rejected basing the *Transportation of Dangerous Goods Act* on criminal law power because it was a strict liability offence.] This is a problem in relation to economic instruments aimed at unintended discharges because the *mens rea* test cannot be met. However, the criminal law power might provide authority for regulation of discharges where the nature of discharges are known and emitters have clear control over the amounts emitted.

Second, there is some authority that the more elaborate the regulatory scheme the more likely it will be viewed as not being based on the criminal law power. [(85) -- 85. See Hogg, above at footnote 37, at 18-27. In our opinion the case referred to by Professor Hogg does not support this view point, although the proposition is probably true.] The air pollution regulations which have

been upheld on the basis of the criminal law power have been quite simple prohibitions. [(86) -- 86. *Secondary Lead Smelter National Emission Standards Regulations*, C.R.C. 1978, c. 412.]

Finally, despite these limitations the criminal law power may be useful in buttressing federal use of economic instruments under the national concerns doctrine. The Courts often consider the criminal law power in applying the national concerns doctrine. Presumably this is because the existence of some federal involvement in an area based on the criminal law power makes an extension of federal involvement in that area more reconcilable with the division of powers. This logic appears to be true even if the criminal law power alone would not justify the expanded role..

Taxation

Under the *Constitution Act, 1867*, the federal government has the power to raise revenue through both direct and indirect taxation. [(87) -- 87. Taxation is a very broad subject matter with much greater potential for use in relation to environmental protection than is dealt with in this report.] This potentially could justify federal imposition of some types of discharge fees. However, federal charges that are part of a system of regulation will not necessarily be valid merely because they generate revenue. [(88) -- 88. For instance, levies charged as part of an overall marketing scheme or unemployment insurance premiums to finance unemployment benefits cannot be supported under the tax power because they are tied with the regulatory scheme: see *Agricultural Products Marketing Act, Re* (1978), 83 D.L.R.(3d) 257 (S.C.C.) at 283; *Employment and Social Insurance Act, Re*: [1936] S.C.R. 427. A discussion of federal taxing power is found in G.V. La Forest "The Allocation of Taxing Power Under the Canadian Constitution" Toronto: 1981. The Canadian approach to the limits of the taxing power is much more restrictive than in the United States where a tax is valid even if aimed purely at regulation with negligible revenue generating potential: see for instance *United States v. Sanchez* (1950), 340 U.S. 42.] The taxing power cannot be used to indirectly control an area of provincial jurisdiction, but taxes of uniform application throughout Canada can be used to discourage activities. such as smoking and drinking. Extremely high taxes for foreign publishers of Canadian magazine editions aimed at protecting Canadian publishers have been upheld by the Courts. [(89) -- 89. *Reader's Digest Association (Canada) Ltd. v. Attorney General of Canada* (1967), 59 D.L.R. (2d) 54.]

Courts clearly would uphold some taxes aimed at discouraging pollution. For instance:

- An energy tax or a carbon tax applied either on the retail sale or production and import of fossil fuels almost undoubtedly would be valid federal legislation;
- A federal substance charge, such as a charge on chlorine or heavy metals, with potential exemptions where export or proper disposal can be proven, would also likely be valid if it is revenue generating; and
- Fees on discharges also might be justifiable if they are not seen as an attempt to usurp the role of provincial regulation. There is little guidance as to what factors the Courts would consider in this regard although the federal government could consider measures such as a nationally applied tax on a common and relatively easily measured type of discharge, for instance SO₂, NO_x or AOX. Revenue from such taxes should not be dedicated to particular programs if the tax is being justified as an exercise of federal taxation power. [(90) -- 90. See *Re: Agricultural*

Products Marketing Act above at footnote 73 and *Re: Employment and Social Insurance Act*, above at footnote 88.

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Fisheries

The federal "Sea Coast and Inland Fisheries" head of power provides the constitutional authority for federal laws protecting fish from degradation of their environment. However, the fisheries power is not a general power to prohibit or regulate water pollution. [(91) -- 91. In *R. v. Fowler*, [1980] 2 S.C.R. 213, 113 D.L.R. (3d) 513 the Supreme Court of Canada ruled that a prohibition against putting logging debris in water frequented by fish was beyond the scope of the federal fisheries power, because the offence was not tied to harm to fisheries and there was no evidence that all the prohibited deposits of logging debris would cause harm to fisheries. On the other hand, another section of the *Fisheries Act* prohibiting deposit of "deleterious substances" into fish bearing water, was held to be valid legislation in *Northwest Falling Contractors Ltd. v. The Queen*, ((1980), 113 D.L.R (3d) 1 (S.C.R.)) because it was restricted to deposits that threaten fisheries.]

Any use of economic instruments based on the fisheries power must be clearly linked to regulating deposits which alone or cumulatively threaten fish. In the same manner that regulations or legislation can prescribe substances as deleterious, [(92) -- 92. The *Fisheries Act*, ss. 34(1)(c) allows deleterious substances to be designated by regulation, thus avoiding problems relating to actually proving that a substance is deleterious to fish. We are not aware of any court consideration of this provision; however, we expect that it will be valid as long there is some justification for prescribing a substance as deleterious for purposes of fisheries protection. This ability to prescribe substances as deleterious is important for setting up any workable economic instrument system.] regulations or legislation can be used to establish a link between an economic instrument and fisheries protection. For instance, a tradeable permit system could be established whereby regulations would set limits on contaminants that can enter a fish bearing river system. So long as there is some justification for identifying a contaminant as a potential threat to fisheries, the system should be constitutionally valid. Similarly, a discharge fee system could be set up where the goal is to set fees for the discharge of deleterious substances.

Canadian Charter Of Rights And Freedoms

Just as the *Constitution Act, 1867* establishes the fundamental rules governing the relations between provincial powers and federal powers, the *Canadian Charter of Rights and Freedoms* [(93) -- 93. Above, at footnote 4.] establishes the fundamental rules governing relations between governments and individuals. Any system of economic instruments that breaches these rules will be invalid. [(94) -- 94. Charter arguments may be raised as a defence by polluters charged with an environmental offence.]

This part gives a brief overview of the main sections of the *Charter* which will be of concern in structuring economic instruments. Unlike the application of the division of powers to economic instruments -- where a very similar analysis applies to each instrument -- the application of the

Charter tends to be quite different for each instrument. Therefore, the analysis of whether a specific instrument breaches the **Charter** is contained in the chapters discussing those instruments, and issues which are relevant to all instruments are discussed in this part.

Section 7

Section 7 of the **Charter** provides:

Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice.

When applying section 7 to economic instruments legislation it is necessary to consider whether the legislation endangers someone's life, liberty or security of the person, and, if so, whether it has done so contrary to the principles of fundamental justice.

Because imprisonment is a clear loss of liberty, offence provisions which can be penalized by imprisonment must accord with the principles of fundamental justice. However, "liberty", has been interpreted as not including "economic liberties" such as a business' freedom to conduct business as it likes or to do what it likes with its property. [(95) -- 95. In *Irwin Toy Ltd. v. Quebec (A.G.)* (1989), 58 D.L.R. (4th) 577 (S.C.C.) the Supreme Court of Canada stated that generally economic rights do not come within the protection of section 7 and that a corporation's economic rights find no protection under section 7. Corporations can, however, raise a **Charter** defence in the context of a criminal prosecution. While the Court in *Irwin Toy* left open the issue of whether economic rights fundamental to human life -- such as rights to social security -- were included in section 7, it is clear that the Courts are extremely reluctant to extend section 7 to economic matters: see *Edwards Books and Art Ltd. v. The Queen* (1986), 30 C.C.C. (3d) 385 (S.C.C.) and *Sections 193 and 195.1(1)(c) of the Criminal Code, Reference Re: (Man.)* (1990), 56 C.C.C.(3d) 65 at 77.] This limitation on the meaning of liberty is important in designing economic instruments because it protects instruments from **Charter** attacks that the instruments are restrictions on business which have been imposed contrary to fundamental principles of justice. [(96) -- 96. This is discussed further in .]

If legislation creating economic instruments may deprive a person of liberty it will only be contrary to the **Charter** if the deprivation of liberty is contrary to the principles of fundamental justice. The principles of fundamental justice are the basic tenets of the legal system, including many procedural protections such as the right to silence and the right to a fair trial. Many but not all of these procedural guarantees are specifically referred to in other sections of the **Charter**. Section 7 also protects Canadians from infringements of their liberty that are fundamentally unfair. For instance, it disallows enactments which could lead to a person being jailed after the Court has found they are not in any moral sense at fault for an offence having occurred. [(97) -- 97. *Section 94(2) of the Motor Vehicle Act, Reference Re: (1985)*, 23 C.C.C.(3d) 289 (S.C.C.) The application of this rule is discussed further in .]

Section 11

Section 11 is important in the context of administrative penalties and ticketing, both of which are discussed in Chapter 3. Section 11 provides:

Any person charged with an offence has the right

(d) to be presumed innocent until proved guilty according to law in a fair and public hearing by independent and impartial tribunal;

(h) if finally acquitted of the offence, not to be tried for it again, and, if finally found guilty and punished for the offence, not to be tried or punished for it again;

Section 11 only applies to circumstances where a person has been "charged with an offence" or in the case of subsection 11(h) to someone who is being charged with an offence a second time. For instance, a polluter will only be able to argue that processes for ticketing or for levying administrative penalties deny the right in subsection 11(d) to a public hearing if these processes are considered to be proceedings in relation to an offence.

Offence proceedings in this context have been narrowly defined. Courts have held that something is only an offence for the purposes of section 11 if it is prosecuted in a process which is "by its very nature a criminal proceeding" or if it may lead "to a true penal consequence". [(98) -- 98. *Wigglesworth v. the Queen* (1987), 37 CCC (3rd) 385 (S.C.C.).] Normal provincial or federal regulatory offences, including environmental offences, are offences. [(99) -- 99. *Ibid.*] How section 11 applies to administrative penalties and ticketing systems, and how these systems can be designed to avoid challenge, is discussed further in Chapter 3.

Section 15

Section 15, the equality section of the *Charter*, is considered because of the concern that economic instruments might be challenged if they apply unequally to different sectors or in different geographic areas. This potential argument has little, if any, weight. Subsection 15(1) provides

Every individual is equal before and under the law and has the right to the equal protection and equal benefit of the law without discrimination and, in particular, without discrimination based on race, national or ethnic origin, colour, religion, sex, age or mental or physical disability.

Not every distinction or differentiation in treatment at law will violate the equality guarantee. Discrimination exists where a distinction based on grounds relating to personal characteristics of the individual group whether intentional or not, has the effect of imposing burdens or disadvantages not imposed on other members of society. [(100) -- 100. *Andrews v. Law Society of British Columbia* (1989), 56 D.L.R.(4th) 1.] Discrimination has been interpreted as discrimination on the grounds listed in section 15 or analogous grounds. [(101) -- 101. *Ibid.* See also .] Given these limits it will be difficult to argue that an initiative to implement economic

instruments is contrary to section 15 merely because it only applies to a certain industry or treats different industries differently. [(102) -- 102. Application of section 15 is discussed further in .]

Section 1

Section 1 is relevant to any analysis of the application of the *Charter* and economic instruments because enabling legislation which infringes any *Charter* right will still be valid if it can be justified under section 1. Section 1 states

The *Canadian Charter of Rights and Freedoms* guarantees the rights and freedoms set out in it subject only to such reasonable limits prescribed by law as can be demonstrably justified in a free and democratic society.

To justify a limitation on a protected right under section 1, the objective of the measure must be of sufficiently important to warrant overriding a constitutionally protected right. Also, the means chosen to reach that objective must be reasonable, based on a balancing of societal and individual interests. Thus, even if an economic instrument for environmental protection is found to breach one of the protected rights, it may be justified on the grounds that it is necessary given the importance of environmental protection or that the infringement is a necessary means of meeting an important objective.

Summary

Division of powers

Both the federal and the provincial governments have wide powers to enact economic instruments for environmental protection, but neither level of government has an unbridled power to enact any instrument for any purpose. The provinces and the federal government have limited powers to regulate the environment based on "heads of power" over which they have exclusive authority. However, as long as the laws' "dominant and most important characteristic" is within the heads of power of the level of government passing the law, a provincial law in relation to a matter of provincial jurisdiction may validly affect a matter that comes within federal jurisdiction and a federal law may impact on an area of provincial jurisdiction. Municipalities and other regional or local governments have no constitutional realm of power, but can be delegated powers from either level of government.

Provincial Powers

The provinces have a wide power to use economic instruments for environmental protection subject only to a few exceptions. In particular the provinces could:

- establish discharge permit trading systems for any discharges within the province;
- establish discharge fee systems which generate significant revenue without infringing the rule against indirect taxation; however, they can likely only use "proxy discharge fees" applied to products that will be resold if they do so in the context of a broader discharge fee system; and

- impose a system of discharge fees or tradeable emission permits for vehicles especially if these instruments are only applied to international or interprovincial trucking firms in proportion to the discharges of those firms in the province.

Federal Powers

While federal powers in relation to environmental protection are not as clearly established as those of the provinces there are a number of federal heads of power on which economic instruments for environmental protection could be established:

- **Peace Order and Good Government.** The most important basis for federal involvement in environmental matters is the POGG power under which the federal government has the authority to establish economic instruments for controlling pollutants that may cross provincial boundaries. It also empowers the federal government to deal with intraprovincial aspects of an environmental problem if provincial inaction may have adverse extraprovincial results. However, the POGG power must be used in a way which is reconcilable with the Canadian constitution's division of powers and does not unnecessarily entrench on provincial powers.
- On the basis of the POGG power the federal government could likely establish economic instruments to deal with problems that have substantial interprovincial elements. Economic instruments which would probably be justified under POGG include:
 - a) tradeable permits, emission fees or product charges for sulphur dioxide emissions and fossil fuel production or import;
 - b) deposit refund systems on persistent toxic substances or pollution precursors which lead to interprovincial pollution;
 - c) tradeable permits for solvent production and import or product charges for solvents; and
 - d) tradeable permits for ground level ozone precursors from both stationary and mobile sources to the ozone problem.

Federal action is more likely to be upheld in areas where there is a significant transboundary dimension to the problem and where there are inherent difficulties with provincial governments regulating a problem, for instance, in imposing product charges for solvents and products containing solvents or in establishing a substance deposit refund system. Because there is some doubt as to the application of POGG in areas which often been seen as provincial jurisdiction, the federal government should make some attempts to establish the above systems through Interlocking Legislation. However if negotiations are unsuccessful it should move unilaterally.

- **Trade and Commerce.** The combination of the POGG power and trade and commerce may be important in allowing the federal government to regulate interprovincial trade in products which are sources of pollution and in tradeable emissions permits.
- **Taxation.** The federal taxing power could justify carbon and other substance charges and could potentially justify discharge fees applied on a nation wide basis.

- **Criminal Power.** Using tradeable permits to quickly phase out toxic substances which pose a recognized human health hazard would likely be justified by a combination of the national concern test and the criminal law power.
- **Fisheries.** Tradeable permit systems, to the extent they may be applicable to discharges into rivers, could be applied to discharges of substances deemed deleterious to fish.

Canadian Charter of Rights and Freedoms

The constitutional rules contained in the *Charter* govern relations between government and citizen. *Charter* issues relating to use of economic instruments for environmental protection are dealt with mainly in the following chapters, in the context of particular economic instruments. However, it is clear that the *Charter* has a limited role in protecting economic or property rights, and thus the effect of the *Charter* on how economic instruments are applied is minimal. In particular, equality rights enshrined in the *Charter* do not block governments from adopting economic instruments which apply differently to different geographic areas or to different sectors and businesses and the protection of liberty contained in section 7 does not protect businesses' ability to conduct their operations as they like.

Chapter 2 ADMINISTRATIVE LAW AND STATUTORY DRAFTING

This chapter discusses policy issues and rules of statutory interpretation that affect the content of enabling statutes, and rules of administrative law which can both influence the content of enabling statutes and determine the legal challenges governments may face in implementing economic instruments. This chapter also includes recommendations regarding the preferred approach for administrative and regulatory decision making in enabling statutes for economic instruments. These recommendations are based on the discussion of administrative law as well as our commitment to public participation in environmental protection.

Chapters 3, 4 and 5 discuss the specific content of enabling legislation for economic instruments and the potential challenges to enabling legislation, regulations and administrative action. Discussions of potential challenges to regulations and administrative action depend on an understanding of the law which regulates the conduct of administrative agencies. Similarly, our recommendations about the content of enabling statutes are designed to reduce the potential for administrative law challenges through careful statutory drafting. For this reason, the chapter will provide a concise overview of the basic principles of administrative law and statutory drafting as background to these subsequent chapters.

First it is essential to understand some fundamental principles of legislative interpretation and drafting. Legal requirements or powers can be imposed or granted in a number of different ways, including: by statutes passed by Parliament or the Legislature ("statutory" or "legislative" requirements); by regulations passed under the authority of statute by the Lieutenant Governor in Council, [(103) -- 103. The Lieutenant Governor in Council is essentially the provincial cabinet with automatic approval of the Lieutenant Governor; the Governor in Council is essentially the federal cabinet with the automatic approval of the Governor General.] Governor in Council or some other government body ("regulatory" requirements); and by orders or permits issued by government officials in an ad hoc manner under the authority of either statute or regulation ("administrative" requirements).

Administrative law constrains government action by setting limits on public officials in the exercise of their statutory and regulatory powers. The difference is that legislators may override the rules of administrative law if they do so expressly by statute. No statute can exclude the application of the Constitution. The rules of statutory interpretation are not laws per se; but they can have an important effect on how laws are applied in situations where the meaning of the law is not clear. Judges use these essentially grammatical rules to assist them in determining what is the intended meaning of a statute.

Statutory Drafting

As discussed above, the content of statutes will depend on a number of factors including:

- **Policy decisions about which subjects should be covered by statutes and which by regulations.** Governments need to consider a number of competing factors that influence the content of

statutes. Relevant factors include the need for certainty or flexibility, government's commitment to democratic process and principles of environmental protection, and the time it has available to debate detailed legislation.

- **Rules of statutory interpretation governing the necessary language in statutes required to authorize government action.** The power of government bodies to pass regulations or of government administrators to make orders or decisions affecting individuals must be based in a statute. Courts have developed a number of rules of statutory interpretation which they apply in deciding whether a particular regulation or administrative action is permitted by legislation.
- **Rules of administrative law governing how decisions by government administrators can be made.** When statutes give government administrators certain powers, these powers must be exercised in a way which is fair and consistent with the purposes of the legislation. Administrative law deals with how decisions are to be made: rules of procedural fairness and appropriate exercise of discretion. Persons opposed to a particular administrative action can ask the Courts to block the action if these rules have been breached. Where statutes provide a specific process for government administrators to follow in decision making, these decisions will be less susceptible to successful attack in the Courts as long as the process is followed.

Policy Issues

The following are some of the central policy issues which influence our recommendations about the content of enabling statutes for economic instruments:

Commitment. Enshrining a principle in legislation rather than leaving it to regulation or administrative action shows a government's commitment to that principle. Foremost in legislation aimed at environmental protection must be a commitment to positive environmental purposes and to promoting sustainability. For instance, to shield program administrators from pressure to approve monitoring systems which are open to abuse, drafters of tradeable permit legislation could specify that monitoring systems must provide a continuous accurate record of emissions that is not prone to tampering.

Flexibility. Legal requirements in regulations can be amended more quickly than those in statutes. Therefore, requirements that will need to change from time to time should be put in regulation. For instance, the acceptability of specific emissions monitoring systems in a discharge fee system may vary with rapidly changing technology. This is an appropriate subject for regulations.

Certainty. Including a particular requirement in legislation rather than regulation will give the persons regulated a greater security that the provision will not be changed. For instance, certain rules as to how tradeable permits will be dealt with may be enshrined in legislation to give permittees the confidence necessary to engage in trading.

Democratic Process and Accountability. Adopting a dramatically new way of governing emissions, such as a tradeable emissions permit system, may be viewed as undemocratic if the system is based on a cursory statutory reference that does not allow the debate of important aspects in Parliament or the Legislature. Detailed legislation allows for fuller debate in a legislature accountable to the people. Moreover, detailed legislation is often less open to political attacks based on unfounded fears.

Control. Legislatures or Parliament may want to enact detailed legislation in order to exercise control over the bodies it empowers to pass regulations. This is especially true where a body independent of government is given regulation making authority. For instance, if the province delegated to the Greater Vancouver Regional District the authority to set up a tradeable permit system for NOx and VOC it is likely the legislature would want to have a great deal of control over the details of the system.

Many of the recommendations in Chapters 3 to 5 about the content of enabling legislation are influenced by these factors. The recommendations do not necessarily follow from rigid legal analysis but instead from weighing competing policy concerns.

Presumptions of Statutory Interpretation

One of the most important arguments in favour of detailed legislation over general legislation is to ensure that the legislation gives a legal mandate to implement all the necessary aspects of an economic instruments system. Courts will only uphold regulations where they find that there is a statutory mandate to pass them. For instance, the Manitoba *Environment Act* allows "marketing of pollution allowances." [(104) -- 104. C.C.S.M.E-12, s. 45.] This probably would not provide the necessary authority for a system where permits or allowances are initially allocated on a historic emissions basis. While Courts in Canada have been relatively liberal in broadly interpreting statutory mandates to pass regulations, in some circumstances Courts may require very specific statutory mandates in order to uphold certain types of regulations. [(105) -- 105. See *CKOY Ltd. v. The Queen*, [1979] 1 S.C.R. 2 and John Keyes, *Executive Legislation: Delegated Law Making by the Executive Branch* (Toronto: Butterworths, 1992) at 181-187.] In particular, there are a number of "presumptions of statutory interpretation" which require very specific statutory authority before certain actions are taken:

Presumption Against Delegation. There is a general presumption that when Parliament delegates to the Governor in Council power to pass regulations, the Governor in Council cannot subdelegate its authority to a third party. For instance, if the power to pass administrative penalty regulations were delegated to cabinet, cabinet would need specific statutory authority to pass regulations that created a tribunal to adjudicate penalties. [(106) -- 106. See *Steve Dart Co.* (1974), 46 D.L.R. (3d) 745 (F.C.T.D.).] The more the authority delegated involves discretion the more likely it cannot be delegated without statutory authority. [(107) -- 107. *Dene Nation v. The Queen*, [1984] 2 F.C. 942 (T.D.), and Keyes, above at footnote 106 at 253-to 267.]

Presumption Against Transformation of Power. This presumption is closely related to the rule against delegation. Courts will generally presume that where a power to make regulations is delegated, the delegate must exercise that power through regulation-making rather than ad hoc administrative decisions. For instance, if the Greater Vancouver Regional District were given the power to make regulations establishing discharge fees it would probably not be able to pass a regulation giving administrators the power to set per unit fees on an ad hoc basis. [(108) -- 108. See *Brant Dairy Company v. Milk Commission of Ontario*, [1973] S.C.R. 720 for an analogous situation of allotment of marketing board quotas for milk.]

Presumption Against Imposition of Liability. Regulations cannot impose liability, either criminal liability for an offence or liability to pay an emission fee tax or an administrative penalty, unless there is clear statutory authority to do so. [(109) -- 109. See Elmer Driedger, *Construction of Statutes*, 2d ed. (Toronto: Butterworths, 1983) at 318 and Keyes, above at footnote 105 at 166.]

Presumption Against Absolute Liability. Specific statutory authority may be required to pass regulations which create absolute liability offences. Absolute liability offences are those in which an accused will be found guilty whether or not they intended the offence to occur or were negligent in allowing it to occur. [(110) -- 110. See *R. v. Sault Ste. Marie*, [1978] 2 S.C.R. 1299; See also discussion accompanying footnote 52 to 54 in .] This is relevant in the context of administrative penalties which may be imposed on an absolute liability basis.

Limiting Access to Courts. Specific statutory authority is needed to limit the public's ability to have administrative decisions reviewed by the Courts. [(111) -- 111. See *Re Kendrick and Ontario (Milk Control Board)*, [1935] O.R. 308 (C.A.).]

Presumption Against Discrimination. Some cases state that there must be statutory authority to apply different legal obligations to different classes of people (for example, excluding emitters under a certain size from a system of tradeable permits) or different locales (for example, applying a tradeable permit system to the lower Fraser Valley alone). [(112) -- 112. See Keyes above at footnote 106 at 227-229; see also *R. v. D'Entremont* (1987), 34 C.R.R. 255 (N.S. Co. Ct.).] The "presumption against discrimination" will be especially strong where it has an impact on someone's ability to carry on business. [(113) -- 113. Keyes, above at footnote 105.]

Interference With Existing Rights. There is also some authority that regulations may not interfere with rights created by the statute under which the regulations were passed or by the regulations themselves. For instance, in one case a new limitation on the transfer of milk production quotas was not allowed even though the quotas themselves had been established by regulations. [(114) -- 114. *Ackerman v. Nova Scotia* (1988), 47 D.L.R. (4th) 681 (N.S.S.C.T.D); British Columbia courts have declined to follow the reasoning in *Ackerman*: see *Sanders v. Milk Board* (1991), 53 B.C.L.R. (2d.) 167 (B.C.C.A.). In our opinion *Ackerman* was wrongly decided (see at footnote 415 to 420).]

These policy factors and rules of statutory interpretation will influence how legislation is drafted. In addition, rules of administrative law will affect how legislation is implemented by government officials and regulation makers. The remainder of this chapter discusses these rules and various statutory provisions which can help to ensure that legislation is implemented in a fair and effective manner.

Administrative Law

Administrative law governs the exercise of powers granted by legislation, including the exercise of the power to pass regulations, the exercise of the discretion given to officials, and the exercise of powers by tribunals. Implementation of economic instruments may involve all these functions. The rules of administrative law will govern cabinet passing regulations that establish a tradeable

permit system, conservation officers approving a permit trade or a monitoring system, and appeal boards hearing appeals of administrative penalties. However, the application of these rules will vary substantially depending on the power exercised and the authority exercising it.

The following review of the principles of administrative law is only a brief summary of an extensive body of law. [(115) -- 115. Further discussion of administrative law can be found in Sara Blake, *Administrative Law in Canada*. (Toronto: Butterworths, 1992); David Jones & Anne DeVillar, *Principles of Administrative Law*. (Toronto: Carswell, 1985); Robert F. Reid & David Hillel, *Administrative Law and Practice*, 2 ed. (Toronto: Butterworths, 1978); Sir William Wade, *Administrative Law* 6th ed. (Oxford: Clarendon Press, 1988).] Administrative law is extremely complex and cases depend largely on the individual circumstances. This is only a thumbnail sketch aimed at raising awareness of the areas of administrative law which will affect the implementation and design of economic instruments. If officials are alerted to principles of administrative law, they will usually be able to avoid challenges to their exercise of power by acting in accordance with these principles and seeking legal advice when they are in doubt as to how a power should be exercised.

Discretion

There are two important components relating to how legislative power is exercised: the considerations affecting how powers are exercised and the procedure followed in exercising power. We will consider the factors that can influence discretionary powers before turning to issues of procedure.

Arbitrariness and Proper Purpose

Government bodies must exercise discretionary powers in accordance with the purposes of the legislation that gives them authority and in a manner that is not completely arbitrary or capricious. [(116) -- 116. *Roncarelli v. Duplessis*, [1959] S.C.R. 121 at 140.] This means that powers must be exercised in good faith. It follows that government administrators, in making decisions, should not take into consideration facts or evidence irrelevant to statutory purpose and must not refuse to consider facts that are relevant to the statutory purposes. [(117) -- 117. *Oakwood Development Ltd. v. St. Francois Xavier (Rural Municipality)* (1985), 61 N.R. 321 (S.C.C.).]

Regulators generally are given a relatively broad discretion to consider relevant factors. For instance, in granting environmental emission permits or approving trades regulators can take into account both whether a facility meets technical standards under the environmental legislation as well as broader policy issues related to pollution prevention and maintaining of environmental quality. [(118) -- 118. *Wimpey Western Limited v. Alberta (Director of Standards and Approvals of the Department of Environment)* (1983), 28 Alta. L.R. (2d) 193 (C.A.).]

Indications of arbitrary behaviour or bad faith will include decision makers acting surreptitiously or, for no apparent reason, singling out an individual for different treatment than others. [(119) -- 119. Blake, above at footnote 115 at 89.] These indications will tend to make the Court look closely at motives but will not necessarily be sufficient to quash a decision.

Discrimination is acceptable as long as it is discrimination for valid policy purposes related to the statute. [(120) -- 120. See *Aluminum Co. of Canada Ltd. v. Ontario (Ministry of the Environment)* (1986), 1 C.E.L.R. (N.S.) 1 (Ont. Div'1 Ct.).] For instance, discriminating in monitoring requirements depending on the potential effects of permit exceedance is acceptable. Discrimination to reduce economic impacts of a regulation on a particular producer may also be acceptable. [(121) -- 121. *Ibid.*]

Fettering and Consistency of Discretion

Discretion must not be fettered in scope. Courts and academics have recognized the value in administrative bodies developing policies to help them apply their discretionary powers and to make decisions predictable. [(122) -- 122. *Capital Cities Communications Inc v. Canadian Radio-Television Commission*, [1978] 2 S.C.R. 141; Davis, K.C. "Discretionary Justice" in J.M. Evans *et al.*, *Administrative Law* 3d ed. (Toronto: Emond Montgomery Publications, 1989).] However, regulators must not rigidly follow such policies and must be open to submissions that these policies not be followed in a particular case. [(123) -- 123. *Maple Lodge Farms Ltd. & Government of Canada, Re:* (1982), 137 D.L.R. (3d) 558 (S.C.C.).] For instance, a board empowered to levy administrative fines can develop policies as to the appropriate level of fines, but it must not consider itself bound to follow these policies in every case. Similarly, a tradeable permit agency empowered to issue permits could not consider itself bound to follow directions from cabinet, unless the statute authorized binding directions.

On the other hand, inconsistency of policy may be an abuse of discretion in some circumstances. Where there is a reasonable expectation that a policy announced by government will be followed, tribunals should not vary the policy without giving some warning or notice to parties affected. [(124) -- 124. *Bendahmane v. Canada (Minister of Employment and Immigration)*, [1989] 3 F.C. 16 (Fed. C.A.).] What constitutes sufficient notice is discussed further below.

Bias

Decision makers must not be biased. Clearly they should not have any personal monetary interest in the outcome of a decision. They also may be required to conduct themselves so as to not lead an impartial observer to think they were biased. In some cases, such as where a Court-like tribunal hears appeals of administrative fines, decision makers must approach a decision without strongly held preconceptions. In other cases, such as where a board passes bylaws or regulations, or rules on matters of policy, they can have a clearly held position so long as they are open to submissions and changing their minds. [(125) -- 125. *Save Richmond Farmland Society v. Richmond (Township)* (1990), 75 D.L.R. (4th) 425 (S.C.C.); *Newfoundland Telephone Company Limited v. Newfoundland (Public Utilities Board)*, [1992] 1 S.C.R. 623.]

Bias will be acceptable if it is obviously condoned by statute. For instance, where a statutory body is empowered to investigate allegations and then hold hearings into the allegations, its combined investigatory and judicial role can be taken as an acceptance of bias by the legislature. [(126) -- 126. *Brosseau v. Alberta Securities Commission*, [1989] 1 S.C.R. 301.] Therefore, departmental administrators levying administrative penalties can show some bias, but the tribunal to which the penalties are appealed would probably be expected to act in a relatively

neutral way. There may be some bias if the same Minister that employs the administrators names the members of the tribunal, but it may only be permissible if it is clearly what was intended by statute.

Review of Regulations

All regulations must be clearly based on a statutory power to enact that type of regulation or to enact regulations on a particular subject. Generally, decisions of the Lieutenant Governor in Council or the Governor in Council are not reviewable by the Courts on the basis of what motivated enactment of regulations or whether cabinet considered sufficient material to determine what was in the public interest. [(127) -- 127. *Thorne's Hardware Ltd. v. The Queen* (1983), 143 D.L.R. (3d) 577 (S.C.C.); *MacMillan Bloedel v. British Columbia (Minister of Forests)* (1984), 4 Admin. L. R. 1 (B.C.C.A.).] The Court will likely only strike down regulations which are contemplated by legislation where the regulations by their very terms are clearly based on factors unrelated to the purpose of legislation or where there is strong evidence of some improper purpose. The Courts will not, for instance, review regulations made by the Lieutenant Governor in Council to see whether or not it had sufficient information to make an informed decision. [(128) -- 128. *Ibid.*, *MacMillan Bloedel.*]

Courts have upheld regulations passed under environmental legislation which allowed the use of non-refillable steel cans but delayed the introduction of aluminum cans. This was done to allow the steel industry time to develop a lightweight steel can and to protect employment in the steel industry. These regulations were permitted by the environmental legislation despite the fact that aluminum cans were considered to be superior to steel from an environmental viewpoint. The majority of the Court found nothing unreasonable in cabinet concerning itself with job protection when implementing regulations, in spite of the fact that the statute was aimed at environmental protection. [(129) -- 129. See *Aluminum Co. of Canada*, above at footnote 120.]

Cases such as this give regulators wide discretion in developing regulations. So long as regulations implementing tradeable permits, deposit refund systems or emission charges are made for the purpose of environmental protection, they cannot be challenged merely because they take into account other factors such as job protection or equity.

Procedural Fairness

The second major area of administrative law addressed in this part is the procedure that must be followed in imposing regulatory or administrative restrictions. The central rule of administrative law is that a person exercising a power or discretion must "act fairly." This is obviously a vague standard. Generally, it means that before a decision adverse to a person's interests is made, the person should have the right to be informed of the facts on which the decision is based and should be given an opportunity to respond by stating a position and giving useful information to the decision-maker. [(130) -- 130. *Nicholson v. Haldimand-Norfolk Regional Board of Commissioners of Police*, [1979] 1 S.C.R. 311.] The procedure, rather than the actual decision, must be fair. [(131) -- 131. *Chief Constable of North Wales Police v. Evans* [1982] 1 W.L.R. 1155 (H.L.).] The exact content of the duty of fairness will vary depending on the circumstances: the nature of the decision-maker, the nature of the decision being made, and the effect of the

decision on the person claiming a right to fairness. In deciding what constitutes the right to procedural fairness, Courts are well aware of the need to make most decisions quickly, inexpensively and without protracted hearings.

The Right to Notice

In the context of environmental protection, a polluter's right to fair participation in the decision making process will vary. The right to notice can vary from verbally notifying a person of the gist of the case against her [(132) -- 132. *Bennett v. Wilfrid Laurier University* (1983), 43 O.R.(2d) 123 (Ont. Div'l Ct.), aff'd (1984), 48 O.R. (2d) 122 (C.A.).] to being able to review evidence. [(133) -- 133. *Re: Toronto Newspaper Guild and Globe Printing*, [1953] 2 S.C.R. 18; *Re: County of Strathcona No. 20 and Maclab Enterprises* (1971), 20 D.L.R.(3d) 200 (Alta. S.C., App. Div.).] If a tentative decision were made to substantially change the terms of a discharge license -- for example, changing requirements for monitoring equipment after substantial sums had been spent on a different system -- the permittee would probably need to be informed in advance of any meeting with regulators at which the changes are discussed. A vague statement that the permittee's operations would be discussed in a general fashion would be insufficient. [(134) -- 134. See *Baiton Enterprises Ltd. v. Liquor Licensing Commission*, [1985] 1 W.W.R. 186 (1984, Sask. Q.B.) for an analogous case on liquor licensing.] Similarly, if policies had been developed on when emissions trades should be approved or what administrative fines should be levied in particular circumstances, these should be publicly available and persons applying for trade approval or being fined should be informed of them. [(135) -- 135. In *Griffin v. Canada* (1989), 26 F.T.R. 185 the refusal of Agriculture Canada to certify a potato crop for sale was overturned because the farmers applying for certification had not been apprised of the standards for certification.]

Where regulators have in the past acquiesced to a practice by a permittee or committed themselves to a particular policy there may be a need to give some notice if the practice is deemed no longer acceptable or the policy is changed. [(136) -- 136. See for instance *Douglas Lake Cattle Company Ltd. v. Minister of Environment and Parks*, [1988] B.C.J. No. 489 (B.C.S.C.).] Thus, if regulators start considering fugitive releases [(137) -- 137. Fugitive releases are emissions from equipment due to leaks in seals and valves. They contrast with end of pipe releases.] in calculating allowable emissions, after having discounted such releases for years, they may have a duty to notify affected parties.

The Right to be Heard

The right to be heard can vary from a formal court-like proceeding to an informal telephone conversation. The type of hearing that is necessary will depend either on the circumstances or the rules laid out in statute. The nature of the hearing will vary according to its importance and whether rights are being taken away or granted. Administrative decisions which may force a company out of business or take away some existing right invoke a more extensive right to be heard than decisions which deny an application. [(138) -- 138. See Blake, above at footnote 13, at 10-12; *Re Webb and Ontario Housing Corporation* (1978), 93 D.L.R.(3d) 187.]

If an emissions permit was cancelled or a major administrative fine levied, other than an automatic, absolute liability, fixed fine, the permittee would probably have a right to a relatively formal hearing and may even have a right to be represented by a lawyer at the meeting. [(139) -- 139. *Baiton Enterprises*, above at footnote 134.] Similarly, if a permit was being cancelled because of failure of the permittee to abide by its terms, the permittee would have the right to make extensive representations to the decision-maker. [(140) -- 140. *Prysiazniuk v. Hamilton Wentworth (Regional Municipality)* (1985), 51 O.R.(2d) 339 at 344 (Div. Ct.).] On the other hand, if a tradeable permit transfer were denied, the applicant may only have a right to an informal hearing, an exchange of letters or even just a telephone discussion. [(141) -- 141. *McInnes v. Onslow Fane*, [1978] 1 W.L.R. 1520 (Eng. Ch. D.).]

Procedural requirements usually will be lower if a decision can be appealed and the body hearing the appeal has the right to consider all the merits of the decision. For instance, an administrative fine may be levied or a license suspension ordered without an oral hearing so long as there is a body to which the decision can be appealed. [(142) -- 142. *Theriac v. Nova Scotia Marketing Board* (1981), 48 N.S.R. 116 (N.S.S.C., T.D.).] Where statutes have given the right to appeal decisions to a tribunal, the tribunal generally will have to hold a full hearing.

Procedural requirements will vary according to the nature of the decision-maker. The Court's supervisory powers over cabinet decisions is extremely limited and there is generally no right to a hearing for cabinet decisions. [(143) -- 143. *Islands Protection Society v. Environmental Appeal Board* (1988), 32 Admin L.R. 36 (B.C.S.C.); See also *Gray Line of Victoria v. Chabot*, [1984] 2 W.W.R. 635 for a case involving court review of cabinet process.]

Procedural requirements are relaxed or non-existent for decisions which are "legislative in nature, affecting the community as a whole rather than particular individuals, and if based on policy rather than findings of fact, the duty to act fairly is unlikely to be imposed." [(144) -- 144. See *MacMillan Bloedel v. British Columbia (Minister of Forests)* (1984), 4 Admin.L.R. 1 (B.C.C.A.).] Thus, in the absence of legislation to the contrary, where generally applicable regulations are developed by cabinet, a regional district or an environmental agency, there will be no right to procedural fairness.

However, where regulations are adopted by a regional district or agency and involve a dispute that affects a few individuals or one individual more than others there may be a need to consult. [(145) -- 145. *Township of South-West Oxford v. A. G. Ontario* (1983), 44 O.R.(2d) 376 (H.C.).] For instance, a special board given the power to make regulations for the approval of permit trades, likely could pass -- without any consultation or notice -- generally applicable regulations disapproving of a certain type of trade. However, it might not be able to pass such regulations in the same way if they applied only to a single transaction.

Structuring Legal Powers

Based on the principles of administrative law and principles of fair and open government, we recommend that statutes enabling the use of economic instruments clearly set out how regulatory and administrative powers are to be exercised.

The potential for successful administrative law challenges to regulatory powers can be reduced by statutorily defining a process for the exercise of these powers and by following this process. If legislation clearly specifies the form of hearing and notice which must be given in different circumstances, the Courts will not strike down decisions made in accordance with the legislation. [(146) -- 146. Even if a process is biased or contrary to procedural fairness, courts will accept it if it is clearly allowed by statute. See *Law Society of Upper Canada v. French* (1974), 49 D.L.R. (3d) 1 (S.C.C.).] Moreover, a statutorily defined process will give much more guidance to administrators than the vague principles of administrative law. In defining this process in enabling legislation for economic instruments it is essential to provide for adequate public involvement.

Public Involvement and Administrative Law

We recommend a strong role for the public in the exercise of regulatory and administrative processes. In part, this is to avoid laws being challenged due to a breach of the public's rights to procedural fairness. However, the law has generally not allowed interested members of the public to make representations on decisions that affect them unless they have some direct interest (other than as a concerned citizen) in the outcome of the decision. We strongly support public participation in environmental regulatory or administrative decisions particularly where they affect the public interest.

Public Involvement in Regulation Making

There are many reasons supporting public participation in setting regulations that implement economic instruments. [(147) -- 147. This section is adapted from "Public Access to Environmental Justice," Franklin Gertler, Paul Muldoon & Marsha Valiante, in *Sustainable Development in Canada: Options for Law Reform*, The Canadian Bar Association Committee Report, September 1990 (Ottawa: Canadian Bar Association, 1990) at 94-95.] Regulations developed with public input will lead to decisions that are more informed and accepted. Interested groups and individuals can challenge the data upon which the proposed regulations are based, test the regulatory assumptions employed, and provide a new or different perspective. Public participation ensures a fairer process, since those who must bear the risk of the decisions will have input into the process. The public is essential in helping define the public interest through direct representations to regulators. Also, increasing public participation may well increase the public acceptance of a decision.

The Canadian Bar Association Sustainable Development Committee recommended in its 1990 report on options for law reform for sustainable development in Canada that:

The federal government should initiate a formalized rule-making process for the development of environmental regulations These processes should include the following elements:

- a. public notice that the regulations are being developed or considered;
- b. release of sufficient background information and technical documentation;

- c. provision for public comment, with the time to comment to be specified in regulations;
- d. a written response by the government to the public comments;
- e. the opportunity to request a public hearing;
- f. criteria for refusing a hearing should be established and, where the request for a hearing is denied, written reasons for the denial should be issued; and
- g. funding for public interest intervenors or participants.

We wholeheartedly endorse these recommendations and note that this approach has been largely adopted in the Ontario *Environmental Bill of Rights, 1993*. [(148) -- 148. Bill 26, 3d Session, 35th Legislature.]

Public Involvement and Appeal

We also recommend statutory processes which ensure a right to public involvement in the exercise of administrative powers. Entrenching a public right of involvement and provisions for public notice may help avoid Court challenges based on individuals claiming that their rights to procedural fairness have been denied by administrators applying an ambiguous standard. The same reasons which dictate public involvement in regulation making dictate that there should be meaningful public involvement in administrative decisions.

Privative Clauses

We also recommend that drafters of environmental protection legislation seriously consider restricting the ability of the Courts to review the decisions of administrators and appeal boards through what is known as a privative clause. [(149) -- 149. One of the reviewers of this report suggested that, as an alternative to a privative clause, review of administrative and appeal board decisions by the Courts could be restricted by requiring that appeals be filed within a limited time and only with the leave of the Court. This limits the potential for use of judicial review as a stalling tactic since the Courts could only allow those calls for review which have substantial merit to proceed. At the same time the role of the Courts in overseeing the fairness and legality of administrative decisions is preserved. We do not recommend this approach because tight time frames for appeal will tend to have a greater restrictive effect on public access to judicial review as public interest groups seldom have quick access to legal resources. Second, with regard to requiring leave to review administrative decisions, it is our experience that most Courts in Canada are reluctant to limit appeal rights and that seeking leave to appeal could merely create a new procedural step delaying final decisions.] Many specialized decision making structures limit the ability of the Courts to review decisions. For instance, decisions of labour relations boards and human rights boards cannot be reviewed by the Courts unless these bodies step out of their area of statutory jurisdiction.

This helps ensure that decision makers familiar with economic instruments for environmental protection are responsible for implementing the legislation. It also avoids administration becoming mired in extensive appeals to the Courts.

The Court's role in ensuring appeal boards stay within their areas of jurisdiction includes the ability to ensure appeal boards abide by the rules of natural justice and that they interpret their legislation in a way that is reasonable, even if it is not the way the Court would have interpreted it. On the other hand, it means that the traditional legal rights of a party to challenge a tribunal's interpretation of the law in front of an independent and impartial Court is limited. While restrictions on this right should not be made lightly, we note that it may be appropriate in some circumstances to lessen the prospect of litigation aimed at delaying action and intimidating decision-makers.

Summary

Administrative law and the rules of statutory interpretation govern what actions are permitted by statute and how statutes are implemented. An understanding of this body of law, as well as an understanding of the policy factors which influence the content of enabling statutes, is essential to understanding the recommendations in Chapters 3, 4 and 5 about what should be included in enabling legislation and what legal challenges might be made to economic instruments.

Enabling legislation for economic instruments should include sufficient provisions to allow all necessary aspects of a working economic instrument system to be adopted. This may include the authority to impose absolute liability for certain offences, a clear authority to discriminate amongst different sectors, and possibly the authority to subdelegate functions to suitable agencies. Enabling legislation should also contain provisions which show a commitment on the part of government to using economic instruments for environmental protection.

The principles of administrative law also will influence enabling legislation. Governments may wish to partially shield certain functions from administrative law appeals by delegating them to bodies like cabinet that are not subject to most of the constraints of procedural fairness. Regulations made by any body will be harder to attack on administrative law grounds if they are generally applicable rather than being focused on an individual situation.

Administrative decisions and tribunal decisions will always be subject to some oversight by the Courts. The Courts' main role is to ensure that decisions affecting an individual are made with the individual's input and to ensure powers are exercised for valid purposes such as environmental protection.

Privative clauses could be used to minimize the potential for Court challenges to administrative decisions. A statutorily defined process for both regulatory and administrative decision making can also reduce the potential for Court challenges if it is followed. A statutorily defined process also may ensure decision making is informed by an open discussion of public concerns.

Chapter 3 DISCHARGE FEES, ADMINISTRATIVE PENALTIES AND TICKETING

This chapter examines three environmental policy initiatives. The first initiative, discharge fees, is aimed at encouraging polluters to lower their discharges below levels set by regulation or permits. The last two initiatives, ticketing and administrative penalties, are aimed at increasing the economic incentives for polluters to comply with regulations and the terms of their discharge permits.

Discharge Fees

Under a discharge fee system, the government sets a price on each unit of pollutant discharged and the polluter pays to the government an amount equal to the quantity of pollutant times the unit price. The unit price for different pollutants varies according to their toxicity or environmental effect. The basic rule is that the more harmful the pollutant discharged is, the more the polluter pays. The less discharged, the less the polluter pays. Companies are still prohibited from exceeding discharge levels allowed under the waste discharge permits. [(150) -- 150. Some economists have suggested that limits on discharges could be eliminated if discharges fees equal to the environmental damage caused by a unit of a pollutant were established; they argue this would lead to a societally optimal level of pollution: see D.G. McFetridge, "The Economic Approach to Environmental Issues" in Bruce G. Doern, ed., *The Environmental Imperative: Market Approaches to the Greening of Canada* (Ottawa: C.D. Howe Institute, 1990) at 83. This approach incorrectly assumes a political and scientific ability to measure the environmental costs of pollution or to determine what levels of fees are necessary to reduce discharges to desired levels. There is ample evidence that scientific studies attempting to measure the negative impacts of discharges unavoidably and consistently underestimate these impacts: see Randall Peterman & Michael M'Gonigle, "Statistical Power Analysis and the Precautionary Principle," (1992) 24 *Marine Pollution Bulletin* 231. Basing fees on the estimated costs of abatement is problematic because of unknowns relating to these costs: see United States General Accounting Office, Report to the Chairman, Subcommittee on Deficits, Debt Management and International Debt, Committee on Finance, U.S. Senate, *Environmental Protection: Implications of Using Pollution Taxes to Supplement Regulation*, (Washington, D.C.: U.S. General Accounting Office, 1993) at 28. A number of jurisdictions which have considered charging discharges fees equal to estimated social costs of pollution have rejected this approach because of uncertainty: see for instance, Hans Bressers, "Use of Economic Instruments for Environmental Management: The Role of Effluent Charges in Dutch Water Quality Policy" in H. von Gunter Schneider & R. Sprenger, eds., *Mehr Umweltschutz f'ur weniger Geld* (Munich: Ifo-Institut fur Wirtschaftsforschung, 1984) at 324 to 325 and Gjalt Huppes & Robert Kagan, "Market-Oriented Regulation of Environmental Problems in the Netherlands" (1989) 11 *Law and Policy* 215 at 217-218. Dependence on discharge fees is unacceptable given these uncertainties and biases. Discharge fees are also unable, by themselves, to protect local ecosystems or communities.]

Discharge fees combine the benefits of command and control regulations with economic incentives: encouraging both economic efficiency and an improved environment. [(151) -- 151.

British Columbia, Ministry of Environment, Lands and Parks, *Revising British Columbia's Waste Discharge Permit Fee System: A Discussion Paper* (Victoria: Ministry of Environment, Lands and Parks, 1992).] One study suggested that, where sufficiently high, the discharge fees component of a combined permit and fee system may have been more effective than the permit component of the system in encouraging abatement of emissions. [(152) -- 152. Bressers, above at footnote 150, at 335 to 336 suggests that this may be true without reaching any firm conclusions.] The main criticism of discharge fees has been that charges are generally too low to reflect the full social cost of emissions or to be an effective incentive. [(153) -- 153. J. Opschoor & H. Vos, *Economic Instruments for Environmental Protection* (Paris: Organization for Economic Cooperation and Development, 1989) at 113; Remiand Barre & Blaire Bower, "Water Management in France, with special emphasis on Water Quality Management and Effluent Charges," in *Incentives in Water Quality Management in France and the Ruhr Area* (Washington, D.C.: Resources for the Future, 1981) at 205; Gardener M. Brown & Ralph W. Johnson, "Pollution Control by Effluent Charges: It Works in the Federal Republic of Germany, Why not in the U.S." (1984) 24 *Natural Resources Journal* 929, at 943; but see also Bressers, *Ibid.*, at 334 to 336.]

While discharge fees have the potential to improve the efficiency of the tax system, by discouraging undesirable side effects of economic activity, [(154) -- 154. United States General Accounting Office, above at footnote 150, at 22.] discharge fees may have undesirable effects on distribution of income. [(155) -- 155. An analysis of anticipated distributional effects of a carbon tax in the United States found that the tax, while it cannot be called progressive, may have less effects on lower income earners if revenues are used to replace revenue from very regressive taxes: Repetto, Robert et al. *Green Fees: How a Tax Shift Can Work for the Environment and the Economy* (Washington, D.C.: World Resources Institute, 1992).] If discharge fees are used adverse distributional effects must be addressed.

As noted above, the object of this report is to look at selected legal issues related to the implementation of discharge fees, rather than their effectiveness or their distributional effects. Thus, Chapter 3 looks at necessary components of enabling legislation and examines potential **Charter**, administrative law and trade law challenges to discharge fees.

Ticketing and Administrative Penalties

Chapter 3 also examines these same issues -- components of enabling legislation, **Charter**, administrative law and trade law challenges -- in relation to administrative penalties and ticketing. While these two initiatives are often not classified as economic instruments, they are examined in this report because they are a means of effectively implementing the polluter pays principle -- of ensuring that there is a cost associated with discharges. Like discharge fees, administrative penalties and ticketing are intended to provide a more powerful incentive to reduce discharges. While discharge fees are a means of encouraging the reduction in emissions below permitted levels, administrative penalties and ticketing are a means of increasing the economic incentives to comply with permitted discharges.

The need for better incentives is based on poor levels of compliance with environmental regulations. Low levels of compliance frequently are due to inadequate enforcement. However,

even if expenditures on enforcement were increased the criminal court system is often not an adequate deterrent for many offences because of low levels of prosecution and fines. [(156) -- 156. See T.M. Rankin & R.M. Brown, *Persuasion, Penalties and Prosecution: The Treatment of Repeat Offenders Under British Columbia's Occupational Health and Safety and Pollution Control Legislation*, September 1988 [unpublished] at 38-41. See also John Swaigen, *Regulatory Offences in Canada: Liability and Offences* (Scarborough: Carswell, 1992) at 213-235.] The cost of using the criminal process; the need to prove guilt beyond a reasonable doubt; and the rules of criminal evidence all tend to inhibit laying of charges under the criminal system. [(157) -- 157. *Ibid.*] Existing administrative penalties, such as cancellation of discharge permits, are often equally unwieldy. Permit cancellation for minor violations will seldom be a viable option. Expanding administrative penalties to include monetary penalties and reforming the criminal process have both been suggested as ways to overcome the barriers to enforcement associated with the criminal process. [(158) -- 158. Swaigen, above at footnote 156, at 213-235, suggests that reforms to the criminal process, such as ticketing, reduced burdens of proof, specialized environmental prosecution units and changed rules of evidence may be as effective as administrative penalties in providing a cost effective credible deterrent to non-compliance with environmental laws.]

Monetary administrative penalties could be levied on permit violations or other minor environmental offences. This report focuses on expanding the range of administrative penalties, rather than on the existing administrative penalties. In some circumstances, penalties can be set by regulation and made automatically payable. [(159) -- 159. See 42 U.S.C.S. §7651j (a) (*Clean Air Act*).] In other circumstances, both the amount of the penalty and its imposition are at the discretion of regulators or, alternatively, either the amount or the imposition is discretionary. [(160) -- 160. 33 U.S.C.S. §1319(g) (*Clean Water Act*) requires the administrator to levy a penalty when they become aware of a violation, but the amount of the penalty is up to the discretion of the administrator.]

Incentives for compliance with environmental regulations also can be increased by reforming criminal procedure so that prosecutions are a viable alternative for minor offences. Ticketing is one of a number of potential reforms [(161) -- 161. See Swaigen, above at footnote 156, at 213-235, for a discussion of other potential reforms.] that facilitates increased numbers of charges being laid. Under a ticketing system a conservation officer can issue a ticket. The party charged can plead guilty and pay a pre-set fine without appearing in court. Alternatively, the accused can request a trial or do nothing. If nothing is done, the court has the power to convict without hearing evidence. This system allows large numbers of charges to be processed through the courts at minimal cost, while preserving the safeguards of the criminal process for those who wish to raise a defence.

Our support for the use of administrative penalties and ticketing is qualified by our strong support for the continued application of criminal sanctions applied through the normal criminal procedure. Appearing before the criminal courts has a strong stigma effect and is an expression of society's disapproval of an act. [(162) -- 162. Dianne Saxe, *Environmental Offences: Corporate Responsibility and Executive Liability* (Aurora, Ontario: Canada Law Book, 1990) at 40 to 41.] Economic incentives and penalties do not have the aura of moral culpability associated with the normal criminal process. While economic incentives are strong modifiers of behavior,

there is a danger that penalties and ticket fines may be seen as a cost of doing business and reliance solely on administrative fees may weaken the stigma associated with being a law breaker. Much of the discussion of potential challenges to administrative penalties is focused on ensuring that criminal sanctions continue to be available if penalties are imposed.

Discharge Fees

The essence of a discharge fee system is a fee charged for each unit of a specified pollutant that is released. A charge can be placed on permitted discharges, actual charges or a mix of the two. Per unit charges can be lowered where polluters have installed best available technology or undertaken other pollution prevention steps. Also, charges can be placed on products whose use will eventually lead to an emission. For instance, a charge placed on carbon in fossil fuels is an effective proxy for a charge on carbon dioxide in emissions and could be an efficient and effective way of dealing with global warming. [(163) -- 163. Roger Dower & Mary Beth Zimmerman, *The Right Climate for Carbon Taxes: Creating Economic Instruments to Protect the Atmosphere* (Washington, D.C: World Resources Institute, 1992).]

Implementing Legislation

Discharge fees have been applied in British Columbia, [(164) -- 164. *Waste Management Permit Fees Regulation*, B.C. Reg. 299/92.] the United States, [(165) -- 165. M. Stone, *Pricing Pollution: Revising British Columbia's Waste Discharge Permit Fees* (Victoria: B.C. Ministry of Environment, 1990) at 23.] Ontario, [(166) -- 166. M. Fortin & B. Mitchell, *Water and Wastewater Charges for Ontario: The User Pay Principle* (Mississauga: Ontario Sewer and Water Main Contractors' Association, 1990) at 14.] Quebec [(167) -- 167. *Regulation Respecting Industrial Depollution Attestations*, Quebec Gazette, March 4, 1992; In force for pulp and paper mills only as of September 13, 1993: personal communication with Cecile Geadrealt, Quebec Ministry of Environment.] and extensively in the European community. [(168) -- 168. J. Opschoor & H. Vos, above at footnote 153, at 58.] In British Columbia the **Waste Management Act** allows the Lieutenant Governor in Council to make regulations:

requiring persons to whom a permit ... is issued under this Act ... to pay to the government charges in respect of the permit ... , establishing the amount of those charges or the method of their determination and requiring that they be paid yearly or otherwise, [(169) -- 169. Section 35(2)(d).]

This minimal statutory provision is sufficient to establish a system of discharge fees such as the system authorized by the **Waste Management Permit Fees Regulation**, [(170) -- 170. Above at footnote 165.] but it may not be sufficient for a more comprehensive system of discharge fees. For instance, the language in the **Waste Management Act** referring to "charges in respect of the permit" could be interpreted as not allowing discharge fees which do more than recoup the costs of administering permits. [(171) -- 171. A number of cases in other contexts have distinguished between permits fees aimed at recouping administration costs and fees which raise revenue: see for instance *Attorney General of Canada v. Registrar of Titles*, [1934] 4 D.L.R. 764 (B.C.C.A.); See also section 35(4) of the *Waste Management Act*.]

We recommend that any federal or provincial law under which discharge fees are imposed include the following provisions:

- Clarify that permit fees are a regulatory tool not limited to recovery of administration costs and not limited to permitted sources. Legislation should provide clear authority to set fees at any level deemed advisable by regulators taking into account the estimated societal costs of discharges and the level of fees necessary to ensure substantial improvements in discharge levels. In the case of federal legislation where the federal government does not have a clear authority to regulate emissions, the power to charge fees should be linked to revenue generation and be a part of tax legislation. [(172) -- 172. See discussion of the federal government's taxation powers in , at footnote 87 to 90.

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- **Provide authority for discharge fee surcharges.** Surcharges could be used for environmentally sensitive or heavily polluted areas to provide a further incentive to reduce emissions. This approach has been used in France: effluent charges are increased where local ambient objectives are not being met. [(173) -- 173. Barre & Bower, above at footnote 154, at 203.

] Specific provision for surcharges would avoid arguments that legislation is not intended to allow fees which discriminate between different regions or different emitters. [(174) -- 174. See , text accompanying footnote 112-113.] In addition to allowing surcharges we strongly recommend the use of a standard minimum fee structure rather than a fee structure that varies from region to region or is individualized according to assimilative capacity. Reasons supporting a standardized minimum fee structure include:

- administratively and politically it is more difficult to establish effluent emissions which are a realistic incentive to pollution reduction where the fee schedule is being negotiated on a site by site or regional basis; [(175) -- 175. See Brown & Johnson, above at footnote 154, at 960.]

- a consistent provincial fee schedule avoids the danger of luring dischargers to pristine areas; [(176) -- 176. *Ibid.*, at 959.]

- the concept of assimilative capacity is problematic, given scientific uncertainty and the fact that assimilative capacity can ignore both local and global effects; and

- wherever they locate, dischargers are utilizing a portion of the local assimilative capacity of the environment.

- Provide authority for fees being charged on the production, import or the use of products where production, import or use of a product will likely lead to release of a substance into the environment. Often the only means of applying charges to emissions is to apply charges to a product which likely will lead to a release. For instance, a carbon tax has been suggested as a proxy for carbon dioxide emissions. [(177) -- 177. J. A. Cassils, "Exploring Incentives: An Introduction to Incentives and Economic Instruments for Sustainable Development," (Ottawa: National Round Table on the Environment and the Economy, 1990) at 17.

] Taxes on ozone depleting substances have been used in the United States and proposals have been made for excise taxes on import or production of virgin chlorinated solvents. [(178) -- 178. Molly Macauley, *et al.*, *Using Economic Incentives to Regulate Toxic Substances* (Washington, D.C.: Resources for the Future, 1992) at 31-40 and 61-64.]

- Provide for regulations defining methods of monitoring or estimating emissions for the purposes of levying charges. There should be clear statutory powers allowing regulations that establish acceptable means of estimating emissions -- including materials accounting. This is essential if fees are to be based on actual emissions rather than permitted emissions. There will likely be numerous challenges to emissions measurements, if monitoring systems are not clearly defined by regulation. There will be a need for an independent and impartial tribunal for appealing permit provisions and fee assessments if monitoring systems are set by permit, or if emissions are estimated by administrators.

Allow charges to be levied on different classes of polluters with provision for partial rebates where an individual polluter has established that it meets certain performance standards or has installed pollution reduction technology. This provides an incentive for meeting higher environmental standards and is necessary for dealing with emissions from small sources where effective monitoring is expensive or technologically unfeasible. [(179) -- 179. This approach has been applied in the Netherlands to unmetered effluent dischargers: M. Stone, above at footnote 166, at 29-30; J. Opschoor & H. Vos, above at footnote 153, at 58.

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- **Allow revenue neutral charges.** The government may wish to consider providing for the return or partial return of emission charges to the sector from which they are collected, in accordance with a formula that rewards clean production. For instance, Swedish charges on nitrous oxide emissions from large energy generation installations are put into a fund and returned to plants in proportion to the useful energy they produce. [(180) -- 180. See Sus Andersson & Peter Hanneburg, "First Refundable Pollution Charge," (November 1991) 12 *Enviro* 10.

] While this may not provide a full internalization of environmental costs and may not fully accord with the polluter pays principle, there are circumstances where it could be a useful regulatory tool. [(181) -- 181. Sweden implemented the refundable charge because it was not practical to apply charges based on continuous emissions monitoring to small units, and it did not want to give small, less environmentally friendly plants an economic advantage.]

- Grant inspectors the power to enter on to any premises where emissions are occurring and inspect and verify the emissions, monitoring equipment and data. Existing legislative provisions for inspection [(182) -- 182. Section 21 of the *Waste Management Act*.] may not allow testing of monitoring equipment or testing, examination and auditing necessary to verify estimates of emissions based on material accounting. Also, legislation should ensure that regulators have the right to conduct routine searches and inspections of laboratories relied on to analyze emission samples or other materials. A 1993 report of the U.S. General Accounting Office found that self-reported emissions monitoring results were statistically unrepresentative and open to substantial fraud both in sampling of emissions and in testing. [(183) -- 183. United States

General Accounting Office, *Environmental Enforcement: EPA Cannot Ensure the Accuracy of Self-Reported Compliance Monitoring Data*, GAO/RCED - 93 -21 (Washington, D.C.: United States General Accounting Office, 1993).] The report found a high level of fraud amongst both emitters and independent laboratories. [(184) -- 184. Commercial laboratories may falsify emissions monitoring with or without the knowledge of facility operators in order to save money or handle more work; in some instances falsification has been a routine part of major commercial laboratories' operations: *Ibid* at 51 and 56-7. Instances of fraud by emitters have included plant managers persistently over a period of at least nine years directing workers to falsify results: *Ibid.*, at 53.] Legislation could require permittees to provide consents to spot audits and inspections from any independent laboratories used to conduct emissions testing.

Legal Challenges to Discharge Fees

Government may be reluctant to adopt high discharge fees that these fees for fear of challenges in the courts by firms who argue that a charge is unfairly high or results in an adverse economic effect. While the potential for challenges always exists, the potential for successful challenges to discharge fee systems is very limited so long as enabling legislation gives a wide authority for appropriate regulations and, where necessary, administrative discretion.

Administrative Law Challenges

As discussed in Chapter 2, the abuse of any discretionary power can be challenged. Therefore, regulations which implement a system of discharge fees could be challenged if implemented for some ulterior motive unrelated to the purposes of the enabling legislation. There is no right to procedural fairness in the context of regulation setting, although thorough consultation will help ensure both the legitimacy and quality of regulations. Regulations adopted under clear statutory authority are difficult to attack on administrative law grounds. On the other hand, a right to procedural fairness arises in the context of decisions by individual regulators. If the enabling statute does not establish a process for making such decisions, the content of the right to procedural fairness will vary according to the decision and its implications.

Regulations can be challenged as not being authorized by legislation. The components of enabling legislation discussed above are aimed at avoiding any successful challenges. In particular legislation should give ample authority for setting high fees to avoid arguments that regulations are not authorized because the statute only contemplates recouping administrative costs. The law should state clearly that fees can be set at any level deemed advisable by the regulator.

The potential for challenges to administrative actions will depend on the structure of the discharge fee system. The British Columbia *Waste Management Permit Fee Regulation*, which bases fees on the amount of discharge allowed under regulations or permits, provides virtually no potential for challenge. There is no individual discretion in relation to the fees charged per unit or the measurement of units emitted; therefore, no rights to procedural fairness arise. Since the fees are charged on permitted emissions rather than actual emissions, permittees have acquiesced to the permitted amounts. The only situation where a permittee could challenge the fees would be

if regulators insisted on the permit having a higher permitted discharge than the permittee thought necessary -- an unlikely scenario.

However, as more discretion is involved in the application of discharge fees there will be a greater potential for challenges based on administrative law. If discharge fees are based on actual emissions measured by individually approved monitoring systems, permittees can challenge administrative decisions relating to the approval of systems. For instance, in appropriate circumstances a permit holder might argue that regulators did not grant it a hearing before insisting on a particular monitoring system or that they fettered their discretion in insisting on following past practices relating to required systems. These types of challenges currently can be made to conditions in waste management permits. However, there is no basis for challenging administrative actions merely because they lead to particularly high costs for an industry.

Establishing a system for appeals of administrative decisions to an impartial and independent tribunal, with provision for fair hearings, either written or oral, would help protect against court challenges to administrative decisions. The right to appeal decisions on monitoring systems or estimates of emissions to an independent tribunal will reduce the potential for appeals to the courts.

Charter Challenges

As discussed in Chapter 1, there is little basis for arguing that a system of discharge fees is contrary to section 7 of the *Charter* merely because it limits the liberty of a firm by making it economically impossible to carry on operations. Nor can discharge fees infringe the equality provisions of the *Charter* because they only apply in one area of the province or Canada, or set higher fees in one area of a province than another.

Section 7

Section 7 of the *Charter* provides that a person's liberty will not be taken away except "in accordance with the principles of fundamental justice". Economic rights, except to a very limited extent, are not protected by this provision and a corporation's economic rights find no protection under the section.

For example, a court rejected, without hearing evidence, arguments that excessive taxation of tobacco products breached section 7 because it unreasonably deprived or restricted tobacco farmers of their right and ability to carry on their livelihood. [(185) -- 185. *Cosyns v. Canada (Attorney General)* (1992), 88 D.L.R.(4th) 507 (Ont. Div'l Ct.).] Similarly, a regulation which temporarily outlawed the use of non-refillable aluminum cans was not contrary to section 7 merely because it denied aluminum manufacturers the right to market aluminum cans. [(186) -- 186. *Aluminum Co. of Can. v. Ontario (Ministry of Environment)* (1986), 1 C.E.L.R.(N.S.) 1 (Ont. Div'l Ct.).] Other cases have held that conditions on liquor licenses, or the revocation of such licenses, cannot be challenged under section 7 because the right to hold such licenses is an entirely economic interest. [(187) -- 187. *R.V.P. Enterprises Ltd. v. British Columbia (Minister of Consumer and Corporate Affairs)* (1988), 50 D.L.R.(4th) 394 (B.C.C.A.).] The same reasoning would apply to discharge fees.

There has been one case in which the right to carry on a profession, which is arguably an economic right, was found to be protected under section 7. However, it is extremely unlikely that this case would be followed by the courts if a polluter challenged a system of discharge fees. [(188) -- 188. In *Wilson v. British Columbia (Medical Services Commission)*, (1988), 53 D.L.R.(4th) 171 (B.C.C.A.) the B.C. Court of Appeal held that regulations denying doctors the right to practice where they chose were contrary to section 7. The Court held that the right to choose a profession and where to practice, subject to reasonable restrictions imposed by the state, came within the meaning of liberty. This case has been criticized by members of the Supreme Court of Canada (see *Ref. Re: ss. 193 and 195.1(1)(c) of the Criminal Code*, at 99 to 101) and has not been followed by Ontario Courts (see: *Cosyns*, above at footnote 186).]

Section 15

The equality rights guaranteed by section 15 are equally unlikely to provide fruitful grounds for challenging discharge fee systems. The Supreme Court of Canada has held that section 15 only applies if there is discrimination based on grounds relating to the personal characteristics of an individual or group. This discrimination must have the effect of imposing burdens, obligations or disadvantages on the individual or group not imposed on others. [(189) -- 189. *Andrews v. Law Society of British Columbia*, [1989] 1 S.C.R. 143; 56 D.L.R. (4th) 1.] The purpose of section 15 is to protect groups who suffer social, political and legal disadvantage in society. In applying this the courts will consider whether the person complaining of discrimination belongs to a classification which has been treated differently on the basis of personal characteristics listed in section 15 or analogous to those listed. In particular, the court will consider if a person comes from a minority which has suffered from stereotyping and vulnerability to prejudice.

The courts have held that neither tobacco farmers nor the tobacco industry were groups of the sort protected by section 15, [(190) -- 190. *Cosyns*, above at footnote 186, at 522 to 524.] and upheld distinctions in taxation between tobacco products and other products without even considering if the higher tobacco taxes were justified on the basis of health or other effects. [(191) -- 191. *Ibid.*] Other cases have held that occupational class is not the sort of classification to which section 15 applies. [(192) -- 192. *Lister v. Ontario (A.G.)* (1990), 67 D.L.R. 4th 732 (Ont. H.C.J.)] Therefore, it seems clear that there is no basis for arguing that section 15 would protect against discharge fees which target a particular industry or business.

Similarly, courts have held that inequality in the application of the law in different geographic areas is not contrary to section 15. [(193) -- 193. See *R v. Turpin* (1989), 48 C.C.C.(3d) 8 (S.C.C.); *R. v. C.L.P. Canmarket Lifestyle Products Corp.*, [1988] 2 W.W.R. 170 (Man. C.A.).] Thus, section 15 will not protect against differential application of discharge fees in different provinces or in different parts of a province.

Trade Law Challenges

It is difficult to imagine a situation where discharge fees would be contrary to Canadian international trade obligations. Except for a few rare instances, discharge fees will not pose a barrier to trade. For instance, a fee charged on import or production of solvents as a proxy for emissions of VOCs from solvents might have different effects on imported solvents. Likewise, a

fee charged on mobile sources might have the effect of increasing the price of imports because transportation might be a larger component of costs for imports. [(194) -- 194. A global road user charge was found by the European Court of Justice to be contrary to European Community law because it was considered discriminatory. However, this decision was based on provisions peculiar to the E.C. and the case has been criticized: see Eckard Rehbinder, "Environmental Regulation Through Fiscal and Economic Incentives in a Federalist System" (1993) 20 *Ecology Law Quarterly* 57.] However, these trade effects would be permissible so long as the environmental measures are genuine and do not exclude goods which meet Canadian environmental goals. [(195) -- 195. See *NAFTA* Article 904.4; *GATT* Article XX(b) and discussion in .]

The only exception would be if Canada attempted to charge taxes on imports based on the emission of a pollutant during foreign production. For instance, the United States applies its ozone depleting chemical fee to products which use ozone depleting substances in their manufacture. [(196) -- 196. See Canada, *Economic Instruments for Environmental Protection: Discussion Paper* (Ottawa: Supply and Services Canada: 1992) at 60.] According to the reasoning of a recent GATT dispute panel this would be contrary to GATT; however, that panel ruling has yet to be adopted by GATT as a whole. [(197) -- 197. See *United States -- Restrictions on Imports of Tuna*, *GATT Doc.* DS21R/R (September 3, 1991) as cited in Eric Christensen & Samantha Griffen, "GATT sets its net on Environmental Regulation: the GATT Panel Ruling on Mexican Yellowfin Tuna Imports and the Need for Reform of the International Trading System" (1992) 23 *The University of Miami Inter-American Law Review* 569 at 570.]

Administrative Penalties

While regulators in Canada are familiar with the use of discharge fees for environmental purposes, they are less familiar with the use of administrative penalties for environmental purposes. Nonetheless, this approach is well established in other regulatory areas in Canada and is an important part of American and some European nations' environmental law. [(198) -- 198. For examples of Canadian use of administrative penalties see *B.C. Workers Compensation Act*, *Canada Income Tax Act*; the *Canadian Aeronautics Act* and the *Canadian Employment Insurance Act*. For examples of administrative penalties for environmental offences in the United States see footnote 160 and 161 above. Environmental offenders in Sweden are subject to both criminal sanctions and administrative penalties: see Lidgren, Karl, "Use of Economic Instruments in the Environmental Policy in Sweden" in H. von Gunter Schneider & R. Sprenger, eds., *Mehr Umweltschutz, fuer weniger Geld* (Munich: Ifo-Institut fur Wirtschaftsforschung, 1984).] As with discharge fees, many potential legal challenges to the use of administrative penalties can be avoided by drafting enabling legislation that sets a clear framework for the application of administrative penalties.

Enabling Legislation

Legislation authorizing the use of administrative penalties will need to clearly specify the differences between penalties and criminal sanctions. The exact contents of legislation will depend to a large degree on the government's intentions as to the relationship between penalties and criminal sanctions. Alberta, for instance, simply provides:

(1) Where the Director is of the opinion that a person has contravened a provision of this Act or the regulations that is specified in the regulations, the Director may, subject to the regulations, by notice in writing given to that person require that person to pay to the Government an administrative penalty in the amount set out in the notice for each day the contravention continues.

(2) A person who pays an administrative penalty in respect of a contravention may not be charged under this Act with an offence in respect of that contravention. [(199) -- 199. S. 223, *Environmental Protection and Enhancement Act*, C.C.R.S.A., c. E-133.]

Regulations can prescribe offences subject to administration penalties and can prescribe penalties of up to \$5,000. Further provisions allow appeal of penalties to the Alberta Environmental Appeal Board. [(200) -- 200. *Ibid.*] These provisions have a limited ability to provide a strong deterrent to potential law breakers. Legislation containing the following provisions would allow regulations which provide a stronger deterrent to polluters while maintaining fairness for all members of society. The legislation should:

- Provide that administrative penalties are in addition to any sentences imposed by courts for breach of an offence. Even if discretionary administrative penalties are available for offences, there is a need to retain the criminal court system for serious offences. There may be a greater stigma attached to being found guilty of an offence in the criminal court due to its moral connotations and the media exposure given to criminal penalties. [(201) -- 201. Rankin & Brown, above at footnote 156, found that there were more frequent fines under the administrative penalties system used by the B.C. Workers Compensation Board than under the court enforcement approach used for *Waste Management Act* violations; however, this study was completed prior to the Waste Management Branch adopting a vigorous prosecution policy. See also Saxe above at footnote 163. Swaigen, above at footnote 156, questions many of the assumptions behind administrative penalties being more effective deterrents than criminal prosecutions.

] The courts have distinguished between punitive function of criminal sanctions and the deterrent function of administrative penalties. It is essential that criminal sanctions remain an option for punishing significant environmental offences. Environmental legislation in a number of other jurisdictions provides for combination of administrative penalties and criminal sanctions. [(202) - - 202. See Lidgren, footnote 198 above.]

- Provide that an automatic penalty is payable to the government whenever a permit exceedance occurs. Legislation should specify that whenever monitoring systems indicate that a permit exceedance has occurred, the permittee shall pay to the government an amount equal to the amount by which the permit has been exceeded, multiplied by the per unit discharge fee for that pollutant and further multiplied by a factor such as 10 X, which penalizes the permit exceedance.
- Provide for the imposition of minimum fines on an absolute liability basis. For environmental offences tried in the criminal court system, courts will generally assume that there must be some degree of fault before the accused is found guilty. If the accused can show that it was reasonably diligent in avoiding the offence, it will not be found guilty. [(203) -- 203. *R. v. Sault Ste. Marie* (1978), 40 CCC (2d) 353 (S.C.C.).

] This type of offence is referred to as a strict liability offence.

In contrast, fault need not be proved for an absolute liability offence. The imposition of absolute liability for minimum penalties is justified because it may cause some business people to institute more safeguards than if they knew they could avoid conviction by setting up a "reasonably good system". Absolute liability also will allow for an increased application of penalties. If polluters can avoid penalties by introducing evidence of due diligence, investigators will need to contradict this evidence. This constrains taking legal action in many cases where administrators are aware that an offence has occurred.

Although absolute liability is undesirable in the criminal context where there is a potential for imprisonment, courts will be more open to it in the context of administrative penalties. [(204) -- 204. See L.S. Fairbairn, "Administratively-Imposed Civil Monitoring Penalties: Feature, Opportunities and Constraints" prepared for the Canadian Bar Association Continuing Legal Education Committee, May 15, 1992.] The traditional objection to absolute liability -- that it is inappropriate to penalize a morally innocent person -- is less applicable to administrative penalties for permit exceedences.

Courts have long recognized that where people engage in activities that may cause harm to others, they should sometimes be liable even if they neither intended the harm nor were at fault in allowing it to happen. [(205) -- 205. For instance under the common law, a person may be liable for the escape of hazardous substances from their land: *Fletcher v. Rylands* (1865), 159 E.R. 737 and John Fleming, *The Law of Torts*, 7th ed. (Sidney: Law Book Company, 1987). Similarly, employers will be liable for the negligence of their employees done in the course of the employees' duties, even though the employer is not at fault. See Fleming at 339-342.] Permit violations will often involve environmental degradation. Because of the difficulty in quantifying these costs in monetary terms, [(206) -- 206. See Randall & M'Gonigle above at footnote 150, for a discussion regarding the near impossibility of quantifying environmental harm.] civil liability for degradation is not practical in many cases. Absolute liability represents a means of ensuring that the costs of degradation, or an estimate of such costs or potential costs, is borne to some degree by the polluter. Even if the polluter was not at fault in allowing an emission to occur it has an obvious moral responsibility for degradation, and it, rather than society at large, should be responsible for these costs.

- Provide that further discretionary administrative penalties may be levied where harm to the environment may have occurred or where the permittee was not diligent in avoiding an occurrence of the offence or taking corrective action. There should be potentially higher fines to compensate for actual harm caused or to encourage compliance with regulatory standards. In the United States regulators have developed a number of policies which encourage reporting of offences and take into consideration actual and possible harm, the culpability of the offender and the seriousness of the offence. [(207) -- 207. See Fairbairn, above at footnote 204, at 10 and 14, for a discussion of administrative penalty policies developed by the U.S. Nuclear Regulatory Commission and the U.S. EPA.

] Similar policies could be adopted by Canadian regulators, specifically stating that the intent of additional penalties is to compensate and deter, rather than to punish. This would help ensure that penalties do not foreclose the possibility of criminal sanctions. As

is discussed further below [(208) -- 208. See text accompanying footnote 212 to 231.] if penalties are characterized as being punitive, the use of criminal sanctions in relation to the same offence may be foreclosed.

- Provide a process for imposing and appealing penalties. A clear statutorily defined process for imposing penalties may help avoid administrative law challenges to penalty assessments and can ensure that assessments are imposed with an awareness of all applicable facts. Appeal processes should be simple and speedy to ensure that the advantages of administrative penalties over the criminal process are realized. As discussed in Chapter 2, privative clauses could be used to help ensure the process does not become subject to frivolous appeals.
- Provide that penalties be used for environmental purposes. The courts will consider this an indication that the penalty is not retributive in nature, but is intended to correct damage rather than punish. This will help ensure that the penalty does not foreclose criminal proceedings in appropriate circumstances.

Challenges to Administrative Penalties.

Administrative Law Challenges

Regulators will need to establish a system that provides a fair process in levying fines because, the duty of procedural fairness applies to decisions to levy penalties against an individual or corporation except when the application and amount of the fine is automatic. [(209) -- 209. See Sara Blake, *Administrative Law in Canada* (Toronto: Butterworths, 1992) at 10 -12.]

The British Columbia Workers' Compensation Board uses a process that avoids administrative law challenges to administrative fines by building procedural fairness into the system [(210) -- 210. This process is described in Rankin & Brown, above at footnote 156, at 62 to 63.] The penalty process begins with a letter sent to an employer who has breached WCB regulations, describing the violation and possibly the employers' compliance history. The letter proposes a penalty and invites the employer to state why there should not be a penalty. Some employers pay the fine at this stage and the matter is concluded. If the employer objects, the objection is forwarded to inspectors and regional officials for their comment. Oral hearings are granted if requested. Final decisions by the Board can be appealed to the Commissioners of the Board.

If defined by legislation, a penalty assessment process is unlikely to be successfully challenged in court. Legislation also can limit the potential for appeal of decisions to the courts. "Privative clauses" [(211) -- 211. See .] in legislation or other limits on review of administrative decisions by the Courts could help to ensure that decisions are made by a body familiar with environmental regulatory issues. They also could help reduce the potential for parties seeking judicial review of penalties on the basis of factual issues or questionable legal interpretations.

Charter Challenges

The two largest potential challenges to administrative penalties relate to the ability to impose a penalty with no trial under section 11(d) of the *Charter* and the imposition of both administrative fines and criminal sanctions under section 11(h) of the *Charter*. Another potential argument is that absolute liability for administrative offences violates section 7 of the *Charter*. While these

challenges are realistic concerns they will likely be unsuccessful if enabling legislation is properly drafted.

Section 11

As discussed in Chapter 1, section 11 of the *Charter* protects against being charged twice with the same offence. It also guarantees the right of someone charged with an offence to be presumed innocent until proven guilty in a fair public hearing before an independent tribunal. If a polluter receives an administrative penalty, prosecutors will be prohibited from proceeding with criminal charges if the administrative penalty process is viewed as being charged with an offence. Similarly, a polluter could argue that the administrative penalty process -- which does not necessarily involve a public hearing -- is contrary to s. 11(d).

What constitutes an offence in this context has been narrowly defined. Courts have held that an offence is only an offence for the purposes of section 11 if it is a matter that is prosecuted in a process which is "by its very nature a criminal proceeding" or because it may lead "to a true penal consequence". [(212) -- 212. *Wigglesworth v. the Queen* (1987), 37 C.C.C. (3rd) 385.] Normal provincial or federal regulatory offences, including environmental offences, are invariably subject to section 11. On the other hand, an administrative penalty system can probably be designed and administered so that it is not criminal in nature and does not involve "true penal consequences".

Proceedings which are Criminal in Nature

The Courts have distinguished between matters which are intended to promote welfare within a public sphere of activity and matters which are intended to regulate conduct within a limited private sphere of activity, stating that "proceedings of an administrative nature" instituted for the protection of the public in accordance with the policy of a statute are not the sort of "offence proceedings to which section 11 is applicable". [(213) -- 213. *Ibid.* at 401.] Although administrative penalties are intended to protect the public, they are private in the sense that they are aimed at maintaining adherence to the set of environmental protection rules which industries accept when they enter a business. [(214) -- 214. See *R. v. Wholesale Travel Group Inc.* (1991), 67 C.C.C. (3d) 193 (S.C.C.) which distinguishes between regulations applying to the general public and those regulating a specific industry or sphere of activity.]

Recent decisions of the Supreme Court of Canada have stated that the question of whether proceedings are criminal in nature is dependent not on the nature of the act giving rise to the proceedings, but on the "nature of the proceedings themselves". [(215) -- 215. *R. v. Shubley* (1990), 52 C.C.C. (3rd) 481 (S.C.C.) at 493.] The exact same facts can lead to both a criminal offence and a non penal based penalty. [(216) -- 216. For instance, making fraudulent income tax returns can be the basis both for a fine from Revenue Canada and criminal proceedings: *R. v. Yes Holdings* (1987), 40 C.C.C. (3rd) 30 (Alta. C.A.).]

In considering the nature of the proceedings the court will look at whether an offender has been asked to account to society in general and face punishment or whether the proceedings are intended merely to be a deterrent to breach of a regulatory code. Informal and private

proceedings will generally not be criminal in nature. [(217) -- 217. *R. v. Shubley*, above at footnote 215, at 494.] Proceedings which have been held to not be criminal in nature include Revenue Canada penalties for false statements in income tax returns, [(218) -- 218. *Lavers v. B.C. (Minister of Finance)* (1989), 41 B.C.L.R. (2d) 307 (C.A.); *R. v. George's Contracting Ltd.* (1987), 15 B.C.L.R. (2nd) 240.] prison disciplinary hearings, [(219) -- 219. *R. v. Shubley*, above at footnote 215.] police disciplinary hearings, [(220) -- 220. *Wigglesworth v. the Queen* above at footnote 212.] and environmental clean-up orders. [(221) -- 221. *Eagle Disposal Systems Ltd. v. Minister of Environment* (1987), 9 C.C.C. (3rd) 501 (Ont. H.C.J.).]

In contrast, a person charged with a traffic ticket violation has been deemed to be charged with an offence [(222) -- 222. *Randall v. The Queen* (1989), 49 C.R.R. 368 (B.C. Co. Ct.)] and military court martial proceedings have been considered to constitute being charged with an offence. [(223) -- 223. *R. v. Genereux* (1992), 133 N.R. 241; 8 C.R.R.(2d) 89 (S.C.C.)] However, traffic ticket processes and court martials are significantly different from administrative penalties. The court martial process is an extremely formalized criminal court like process and can be used in relation to any offence under the *Criminal Code*. [(224) -- 224. *R. v. Genereux, Ibid.*, at 103 to 104.] The ticket process is closely related to the normal criminal process, involving a hearing before a judge and related court procedures if the person pleads not guilty. Although administrative penalties would likely involve a right to appeal to an open tribunal, the penalty initially would be levied in a private proceeding whether or not it was contested by the accused. [(225) -- 225. We note that one provincial court case decided shortly after the introduction of the *Charter* suggests that levying administrative penalties under the *Aeronautics Act* amounts to being charged with an offence. This case clearly gives a much wider meaning than was later given to it by the Supreme Court of Canada: see *R. v. B & W Agricultural Services* (1982), 3 C.R.R. 354 (B.C. Prov. Ct.)]

These cases indicate that so long as an administrative penalty process is carried out in a largely private manner as opposed to involving a court hearing where a finding or fine is disputed it will not be considered criminal in nature.

True Penal Consequences

Whether or not an administrative penalty would constitute a "true penal consequence" will depend on the circumstances. The Supreme Court of Canada has stated that penalties to which section 11 applies include imprisonment or fines which by their magnitude would appear to be imposed for the purpose of redressing a wrong done to society at large. [(226) -- 226. *R. v. Wigglesworth*, above at footnote 212, at 402.] This is distinct from fines which are merely intended to deter people from breaching a regulatory code. [(227) -- 227. *Ibid.*] The Courts have clearly stated that fines will not necessarily be considered true penal consequences. [(228) -- 228. *Ibid.*] It should be noted that very significant penalties have been considered non-punitive. For instance, the courts have said that confining inmates to solitary cells and losing parole rights are not penal consequences. [(229) -- 229. *R. v. Shubley*, above at footnote 215.] Forfeiture of pay, loss of a liquor licence, paying an extra levy on income tax, and deportation have also been held to not be "true penal consequences". [(230) -- 230. *Rio Hotel Ltd. v. New Brunswick (Liquor Licence Board)* (1987), 44 D.L.R. (4th) 663 (S.C.C.); *Trimm v. Durham Regional Police Force*,

[1987] 2 S.C.R. 582; *Burnham v. Metropolitan Toronto Police*, [1987] 2 S.C.R. 572; *Hurd v. Canada (Minister of Employment and Immigration)*, [1988] F.C.J. 945.]

One issue that arises from the Courts' definition of what constitutes a true penal consequence is whether an administrative penalty aimed at compensation for potential or actual damage done to the environment would be a fine "intended to redress a wrong done to society at large". Although the Courts' decisions are ambiguous, it appears that compensation for damages or potential damages is distinct from "fines intended to redress a wrong done to society at large". First, in other contexts the law has always distinguished between punitive and compensatory damages. For instance, in contract law parties are permitted to provide for fines which are intended to compensate one party for breach of a contract but cannot establish contractual fines intended to punish a party. [(231) -- 231. *Dunlop Pneumatic Tyre Co. Ltd. v. New Garage and Motor Co. Ltd.*, [1915] A.C. 79 (H.L.)] Thus, there is well established distinction between penal and compensatory fines.

Second, while the word 'redress' can mean both compensation and punitive retribution, the reference of the Court to redressing a wrong done to society at large appears to be in reference to punitive retribution. The "redress a wrong done to society as a whole" test was formulated in the context of a case involving an assault by a police officer on a prisoner. In this context "redress to society at large" appears to mean punishment for a morally unacceptable act rather than compensation to the specific individual for his pain and suffering. Thus, in the context of administrative penalties for illegal discharges, administrative penalties do not become "true penal consequences" merely because they attempt to approximate actual or potential harm to the environment.

A fine directed toward a special purpose is less likely to be seen as a "a true penal consequence" than a fine directed towards consolidated revenue. If fines collected by administrative penalties are directed towards a particular fund, such as the Sustainable Environment Fund in British Columbia, they will more likely be seen as non-punitive.

Application of Section 11 to Administrative Penalties

We expect that automatic administrative penalties imposed on an absolute liability basis will not be contrary to section 11 nor will they block prosecutions if the penalties involved are based on multiplying applicable discharge fees by a specified factor. The combination of a private process for penalty assessment and the tying of penalties to otherwise applicable civil liabilities should ensure that the penalties are not considered to be offences.

Administrative penalties levied in a discretionary manner likely will not be considered offences for the purposes of section 11 if the process involved for imposing such fines is relatively informal and private and the purposes of the penalties are clearly distinct from the purposes of criminal law. Because there is some uncertainty as to the exact distinction between criminal sanctions and administrative penalties which are neither "criminal in nature" nor "true penal consequences", it is recommended that legislation should clearly distinguish between the nature and purpose of administrative penalties and the nature and purpose of criminal sanctions. Specifically, legislation should provide that the purpose of fines is to encourage compliance with

environmental regulations and permits, to compensate for actual or potential damage to the environment and to recover administrative costs related to imposition and investigation of regulatory breaches. Legislation could specifically provide that the purpose of fines is non-punitive. Given the limited purposes of such fines and the need to continue to treat some environmental offences with the full weight of the criminal law, environmental enforcement officials should continue prosecuting offences in the courts in appropriate circumstances.

Section 7

As discussed in Chapter 1, section 7 protects citizens from being deprived of their liberty except in accordance with the principles of fundamental justice. A polluter [(232) -- 232. We note that the ability of a corporate polluter to raise a section 7 argument may be limited. The courts have held that since corporations cannot be deprived of "life, liberty or security of the person" they cannot raise section 7 in legal proceedings unless they are charged in "penal proceedings" with an offence that contravenes section 7: see *R. v. Wholesale Travel*, above at footnote 214; *Irwin Toy Ltd. v. Quebec (Attorney General)* (1989), 58 D.L.R. (4th) 577; *R. v. Big M Drug Mart Ltd.* (1985), 18 D.L.R. (4th) 321 (S.C.C.). It is likely that so long as administrative penalties are not considered to be penal for the purposes of section 11, a corporation may not have standing to raise section 7 issues.] could argue that administrative penalties have the potential to deprive the polluter of its liberty contrary to section 7.

In *Re: British Columbia Motor Vehicle Act*, [(233) -- 233. (1985), 23 C.C.C. (3d) 289 at 312.] the court concluded an absolute liability offence would be contrary to section 7 if it allowed for imprisonment. The court specifically left open the question of whether section 7 would be violated by an absolute liability offence which used fines as a penalty but left imprisonment for nonpayment of the fine as a possibility.

If penalties are a civil debt the possibility of imprisonment will be negligible and there will be no unjustifiable breach of section 7. Although there is still a potential for imprisonment in a collection of a civil debt, this will only apply where a debtor has, without any reasonable excuse, ignored a court order for payment. [(234) -- 234. See, for instance, Rule 42 (35) of the British Columbia Rules of Court.] This would distinguish the administrative penalties from the cases in which the combination of absolute liability and the potential for imprisonment were considered to infringe the *Charter*. [(235) -- 235. In *R. v. Grey* [1989] 1 W.W.R. 66 (Man. C.A.) the court considered whether an absolute liability offence was unconstitutional when combined with provisions for imprisonment in default of fine payment. The statute challenged stated that the court could set a period of imprisonment in default of payment and if no alternative imprisonment sentence was specified the jail term would be five days plus one day for every ten dollars of the fine not paid. The court held that because the prospect of imprisonment was highly remote the provision would be justified under section 1 of the Charter. A bench of the B.C. Court of Appeal has adopted this reasoning (*R. v. Smith* (1989), 14 M.V.R. (2d) 166 (Y.T.C.A.); see also *Yellowknife City v. Boyd* (February 19, 1993) (Terr. Ct. N.W.T.). Courts in a number of other provinces have held that almost identical provisions are contrary to sections 7 and cannot be justified under section 1: *R. v. Burt*, [1988] 1 W.W.R. 385 (Sask. C.A.), *R. v. Sutherland* (1990), 55 C.C.C. (3d) 265 (N.S.S.C. App. Div.)] In these cases the probability for imprisonment

was an important factor in deciding whether absolute liability and the potential for imprisonment were unconstitutional.

As discussed in Chapter 1, it will not be viewed as an infringement of the *Charter* to impose fines or restrict economic liberty on an absolute liability basis.

Use of Mandatory Reporting for Administrative Penalties

Despite at least one recent case restricting the use of self monitoring data, requiring polluters to submit monitoring data and spill reports and using such data to impose administrative penalties likely is not contrary to the Charter. [(236) -- 236. In *R. v. Weill's Food Processing Ltd.* (1991), 6 C.E.L.R.(N.S.) 249 (Ont. Ct. J.). Ontario Court of Justice held that using mandatory spill reports as evidence would be contrary to an accused's "right to silence".] The "right to silence" is considered to be a part of section 7 of the *Charter* and specific aspects of it are protected by sections 11(c), 11(d) and 13. [(237) -- 237. *Thompson Newspapers Ltd. v. Canada (Director of Investigation and Research, Restrictive Trade Practice Commission)* (1990), 67 D.L.R.(4th) 161 (S.C.C.)] None of these sections would apply to the use of mandatory reporting data so long as there is no potential for loss of liberty, life or security of the person, and so long as the administrative penalty process is not an offence for the purposes of section 11. As discussed above, there is unlikely to be an unconstitutional deprivation of life, liberty or security of the person where the only potential sanction is a fine levied as a civil debt. [(238) -- 238. Furthermore, at least one case has said that the use of mandatory reporting provisions is not contrary to the *Charter*: See *R. v. Courtalds Fibres Canada*, [1992] O.J. No. 1972 (Ont. Prov. Court).] Moreover, administrative penalties can be designed in such a way that they do not constitute an offence.

Ticketing

While administrative penalties are an alternative to the criminal system, ticketing is a procedural reform to the criminal system intended to facilitate increased numbers of charges being laid. The normal criminal procedure [(239) -- 239. The criminal process in fact involves many more procedural possibilities than discussed here. The description is intended to give an idea of the typical process for minor offences.] is cumbersome. Informations alleging an offence has been committed are sworn by police in front of a justice of the peace. An appearance notice or summons is issued requiring the accused to appear in court and charges are drafted by crown prosecutors on the basis of information provided by police or investigators. The first court appearance may involve the accused entering a guilty plea. In that case the Crown must be prepared to make submissions on appropriate sentencing. Alternatively, the matter can be held over for several weeks or a trial date can be set. Often trial dates are set and arrangements made for all witnesses and investigators to attend the trial only for a guilty plea to be entered at the time of trial.

This process involves substantial and expensive time on the part of the courts, prosecutors and investigators, as well as involving substantial inconvenience to the accused. Because of the costs and inconvenience involved, investigators aware of a minor offence may decide not to initiate a prosecution.

Ticketing is intended to streamline the process for minor offences so that more charges can be laid. In a ticketing system a conservation officer first issues a ticket. There is no need to swear an information or draft charges. The party charged can plead guilty and pay a pre-set fine without appearing in court. Alternatively the accused can request a trial or do nothing. If nothing is done, the court can convict without hearing evidence. This system allows large numbers of charges to be processed through the courts at minimal cost, while preserving the safeguards of the criminal process for those who wish to raise a defence.

The ticket system is an important tool for enforcement officers since it allows them to take some action beyond a mere warning without invoking the whole process of the criminal court system. Even though fines for ticketed offences are generally quite small, [(240) -- 240. Currently the maximum ticket fine for *Waste Management Act* offences is \$200: *Violation Ticket Fines Regulation*, B.C. Reg. 434/90: In our opinion ticketing could also be used for more substantial fines.] they may provide a substantial deterrence because large numbers of tickets can be issued and the registration of a conviction will leave a party more open to substantial penalties if there is a subsequent conviction. It would be useful to combine ticketing systems with other reforms of the criminal process. For instance, there is no reason why the legislature could not provide that persons charged with an environmental offence will be guilty on the basis of the "balance of probabilities" standard rather than the "beyond a reasonable doubt" standard; indeed courts already adopt a flexible standard of proof depending on the significance of a finding of guilt. [(241) -- 241. See Swaigen above at footnote 156, at 232. It is clear from a number of cases that the standard of proof varies according to the magnitude of an offence and the circumstances that flow from a conviction: See *Bater v. Bater*, [1950] 2 All E.R. 458 at 459 (C.A.) approved in *R. v. Oakes* (1986), 26 D.L.R. (4th) 200 (S.C.C.); *Re Beckon* (1992), 9 O.R.(3d) 256 (Ont. C.A.); *Continental Insurance Co. v. Dalton Cartage Co.*, [1982] 1 S.C.R. 164; *Coates v. Ontario (Registrar Motor Vehicle Dealers and Salesmen)* (1988), 65 O.R. (2nd) 526, (Div'1 Ct.) at 536. Some statutes have also reduced the burden of proof and reversed the onus of proof in relation to proof of negligence in regulatory offences. For example, see *Canadian Environmental Protection Act*, R.S.C. 1985, c. 16 (4th Supp.), s. 125.]

Enabling Legislation for Ticketing

British Columbia, [(242) -- 242. *Offence Act*, R.S.B.C. 1979, c. 305.] Ontario, [(243) -- 243. *Provincial Offences Act*, R.S.O. 1990, c. P. 33.] Alberta [(244) -- 244. *Provincial Offences Procedure Act*, S.A. 1988, c. P-215.] and the federal government [(245) -- 245. *Contraventions Act*, S.C. 1992, c. 47.] provide means for ticketing minor offences, including environmental offences. In British Columbia, provision is already made for using these general ticketing provisions in the context of *Waste Management Act* violations. [(246) -- 246. See *Violation and Ticket Administration Regulation* B.C. Reg. 423/90, schedule 2.] No further statutory provisions are necessary for using ticketing as a means of prosecuting environmental offences.

Although it is beyond the scope of this report, both the provincial and federal governments should consider further amendments to the criminal process which would facilitate environmental prosecutions: these could include changes to the standard of proof necessary to convict polluters and the use of absolute liability for offences where conviction does not involve a potential for imprisonment. Any such provisions should give prosecutors and enforcement

officers a choice between prosecutions requiring lower levels of proof, absolute liability and relatively low fines, and prosecutions requiring high levels of proof, strict liability and more punitive penalties including imprisonment.

Challenges to ticketing

Several cases have challenged the legality of ticketing itself, as opposed to the legality of a particular, improperly completed ticket. These cases have challenged the use of ticketing on the basis that it contravenes the right to be presumed innocent until proven guilty. The argument advanced is that, since convictions can be entered without any proof of guilt, even though the accused can require a trial, ticketing is contrary to Section 11 (d) of the *Charter*.

In all of these cases, the courts have upheld the application of ticketing for minor traffic offences. The courts have stated that ticketing is justified because of its value in alleviating inconvenience, costs and hardship to those charged and because it provides procedural protections to those who wish to contest a charge [(247) -- 247. *Grant v. British Columbia* (1986), 40 M.V.R. 56 (B.C.S.C.); *R. v. Greckol* (1991), 79 Alta. L.R. (2nd) 272 (Alta. Q.B.); *R. v. Carson* (1983), 41 O.R. (2nd) 420 (C.A.); *Kindersley v. Boisvert*, [1986] 6 W.W.R. 636 (Sask. Q.B.); *Yellowknife (City) v. Boyd* [1993] N.W.T.J. No. 5 (Terr. Ct.); *R. v. Randall* (1989), 49 C.R.R. 368 (B.C. Co. Ct.)]. In at least one of these cases challenging ticketing the court specifically referred to the application of ticketing procedures to environmental concerns and upheld this application [(248) -- 248. *R. v. Greckol, Ibid.*, at 282-283.]. Given these cases, ticketing is very unlikely to be challenged under the *Charter* unless it is used for serious offences.

A criminal process which uses ticketing is subject to most of the defences available in criminal proceedings. [(249) -- 249. Some defences are not available because of changes in procedure. For instance, since no information is sworn, the information which serves as a basis for a charge cannot be attacked.] Tickets must enable the accused to know the offence with which it is charged and the circumstances to which the charge relates, except to the extent these rules have been changed by the laws establishing the ticketing system. [(250) -- 250. The rules relating to sufficiency of the description of an offence are often altered in a ticketing system: see for instance, *Offence Act*, R.S.B.C. 1979, c. 305, section 14(6)]. There is a large body of criminal procedure law which relates to these topics, but it is beyond the scope of this work. However, it is unlikely these defences will be raised in a ticketing regime because polluters are less likely to challenge technicalities when the penalties involved are relatively low. [(251) -- 251. See Swaigen, above at footnote 156, at 217.] Also, these technical defences are not something peculiar to ticketing and, so long as inspectors are given adequate instruction in completing tickets, there is no reason why improperly completed tickets should be a more frequent occurrence than improper informations in the normal criminal process. Indeed, if these rules have been specifically addressed in a ticketing system the likelihood of successful challenges on technical grounds may be reduced. [(252) -- 252. See footnote 156 and 100 above.]

Summary

Discharge fees, monetary administrative penalties and ticketing are all instruments intended to increase the economic incentive either to reducing emissions or to comply with environmental permits and regulations. In this sense all three instruments are economic instruments.

We strongly endorse the use of discharge fees in combination with regulatory controls as a means of applying the polluter pays principle and encouraging reductions in emissions below permitted levels. The weakness in discharge fees in British Columbia and other jurisdictions is that they have not been broadly applied and are set too low to reflect the full cost of environmental degradation caused by discharges or to be an effective incentive to reducing discharges.

A number of legislative reforms, such as clarification that fees are not merely intended to cover administration costs and authority to apply higher fees in environmentally sensitive areas, would enable discharge fees that are effective incentives to discharge reductions. Enabling legislation also could ensure broader application of discharge fees by providing for fees applied to classes of businesses with rebates available where environmental performance is demonstrated, and by providing for proxy discharge fees applied to products on their import or manufacture. Other reforms are necessary to ensure effective enforcement and administration.

The potential for challenges to discharge fees will vary according to the details of the system. Administrative law challenges are probable in any system involving substantial discretion, but the likelihood of success for such challenges can be limited by establishing an appeal process in legislation. Neither *Charter* challenges nor trade law challenges pose any significant threat to discharge fee systems.

Monetary administrative penalties are a useful tool for encouraging compliance with discharge permits and environmental regulations. Automatic absolute liability penalties payable in the event monitoring data indicates a polluter is out of compliance or in the event monitoring systems are not functioning would operate in a manner analogous to discharge fees, but should be high enough that they are never viewed as merely a cost of doing business.

If automatic or discretionary administrative penalties are used, they should not foreclose prosecution in the criminal court system. Continued availability of criminal sanctions is essential both to ensure that administrative penalties are not viewed as a cost of doing business and to stress the importance society places on compliance with environmental laws. If administrative penalty legislation is properly drafted, penalties should not foreclose the additional use of criminal sanctions. Similarly, so long as administrative penalties are only a civil debt the combination of absolute liability and the slim potential for imprisonment is not contrary to the *Charter*.

Ticketing also is a useful tool for encouraging compliance with discharge permits and environmental regulations. Ticketing facilitates prosecutions for minor offences, and so long as fines for ticketed offences are significant, the increased potential for prosecution and imposition of fines should be an economic incentive to increased compliance. Traditional criminal process and higher fines should still be available for more significant offences. *Charter* challenges to ticketing have been rejected throughout Canada on the basis of the significant utility to ticketing

and the fact that ticketing retains all the procedural safeguards of the criminal process for those who wish to defend a charge or make submissions on the appropriate sentence.

In summary, we support the use of discharge fees and the availability of administrative penalties and ticketing so long as there is continued reliance on the normal criminal system for any significant offences. There are no major legal barriers to establishing any of these systems.

Discharge fees, Administrative Penalties and Ticketing

DISCHARGE FEES, ADMINISTRATIVE PENALTIES AND TICKETING This chapter examines three environmental policy initiatives. The first initiative, discharge fees, is aimed at encouraging polluters to lower their discharges below levels set by regulation or permits. The last two initiatives, ticketing and administrative penalties, are aimed at increasing the economic incentives for polluters to comply with regulations and the terms of their discharge permits.

Discharge Fees

Under a discharge fee system, the government sets a price on each unit of pollutant discharged and the polluter pays to the government an amount equal to the quantity of pollutant times the unit price. The unit price for different pollutants varies according to their toxicity or environmental effect. The basic rule is that the more harmful the pollutant discharged is, the more the polluter pays. The less discharged, the less the polluter pays. Companies are still prohibited from exceeding discharge levels allowed under the waste discharge permits. [(253) -- 253. Some economists have suggested that limits on discharges could be eliminated if discharges fees equal to the environmental damage caused by a unit of a pollutant were established; they argue this would lead to a societally optimal level of pollution: see D.G. McFetridge, "The Economic Approach to Environmental Issues" in Bruce G. Doern, ed., *The Environmental Imperative: Market Approaches to the Greening of Canada* (Ottawa: C.D. Howe Institute, 1990) at 83. This approach incorrectly assumes a political and scientific ability to measure the environmental costs of pollution or to determine what levels of fees are necessary to reduce discharges to desired levels. There is ample evidence that scientific studies attempting to measure the negative impacts of discharges unavoidably and consistently underestimate these impacts: see Randall Peterman & Michael M'Gonigle, "Statistical Power Analysis and the Precautionary Principle," (1992) 24 *Marine Pollution Bulletin* 231. Basing fees on the estimated costs of abatement is problematic because of unknowns relating to these costs: see United States General Accounting Office, Report to the Chairman, Subcommittee on Deficits, Debt Management and International Debt, Committee on Finance, U.S. Senate, *Environmental Protection: Implications of Using Pollution Taxes to Supplement Regulation*, (Washington, D.C.: U.S. General Accounting Office, 1993) at 28. A number of jurisdictions which have considered charging discharges fees equal to estimated social costs of pollution have rejected this approach because of uncertainty: see for instance, Hans Bressers, "Use of Economic Instruments for Environmental Management: The Role of Effluent Charges in Dutch Water Quality Policy" in H. von Gunter Schneider & R. Sprenger, eds., *Mehr Umweltschutz fuer weniger Geld* (Munich: Ifo-Institut fur Wirtschaftsforschung, 1984) at 324 to 325 and Gjalt Huppel & Robert Kagan, "Market-Oriented Regulation of Environmental Problems in the Netherlands" (1989) 11 *Law and Policy* 215 at 217-218. Dependence on discharge fees is unacceptable given these uncertainties

and biases. Discharge fees are also unable, by themselves, to protect local ecosystems or communities.]

Discharge fees combine the benefits of command and control regulations with economic incentives: encouraging both economic efficiency and an improved environment. [(254) -- 254. British Columbia, Ministry of Environment, Lands and Parks, *Revising British Columbia's Waste Discharge Permit Fee System: A Discussion Paper* (Victoria: Ministry of Environment, Lands and Parks, 1992).] One study suggested that, where sufficiently high, the discharge fees component of a combined permit and fee system may have been more effective than the permit component of the system in encouraging abatement of emissions. [(255) -- 255. Bressers, above at footnote 151, at 335 to 336 suggests that this may be true without reaching any firm conclusions.] The main criticism of discharge fees has been that charges are generally too low to reflect the full social cost of emissions or to be an effective incentive. [(256) -- 256. J. Opschoor & H. Vos, *Economic Instruments for Environmental Protection* (Paris: Organization for Economic Cooperation and Development, 1989) at 113; Remiand Barre & Blaire Bower, "Water Management in France, with special emphasis on Water Quality Management and Effluent Charges," in *Incentives in Water Quality Management in France and the Ruhr Area* (Washington, D.C.: Resources for the Future, 1981) at 205; Gardener M. Brown & Ralph W. Johnson, "Pollution Control by Effluent Charges: It Works in the Federal Republic of Germany, Why not in the U.S." (1984) 24 *Natural Resources Journal* 929, at 943; but see also Bressers, *Ibid.*, at 334 to 336.]

While discharge fees have the potential to improve the efficiency of the tax system, by discouraging undesirable side effects of economic activity, [(257) -- 257. United States General Accounting Office, above at footnote 151, at 22.] discharge fees may have undesirable effects on distribution of income. [(258) -- 258. An analysis of anticipated distributional effects of a carbon tax in the United States found that the tax, while it cannot be called progressive, may have less effects on lower income earners if revenues are used to replace revenue from very regressive taxes: Repetto, Robert et al. *Green Fees: How a Tax Shift Can Work for the Environment and the Economy* (Washington, D.C.: World Resources Institute, 1992).] If discharge fees are used adverse distributional effects must be addressed.

As noted above, the object of this report is to look at selected legal issues related to the implementation of discharge fees, rather than their effectiveness or their distributional effects. Thus, Chapter 3 looks at necessary components of enabling legislation and examines potential **Charter**, administrative law and trade law challenges to discharge fees.

Ticketing and Administrative Penalties

[Chapter 3](#) also examines these same issues -- components of enabling legislation, **Charter**, administrative law and trade law challenges -- in relation to administrative penalties and ticketing. While these two initiatives are often not classified as economic instruments, they are examined in this report because they are a means of effectively implementing the polluter pays principle -- of ensuring that there is a cost associated with discharges. Like discharge fees, administrative penalties and ticketing are intended to provide a more powerful incentive to reduce discharges. While discharge fees are a means of encouraging the reduction in emissions

below permitted levels, administrative penalties and ticketing are a means of increasing the economic incentives to comply with permitted discharges.

The need for better incentives is based on poor levels of compliance with environmental regulations. Low levels of compliance frequently are due to inadequate enforcement. However, even if expenditures on enforcement were increased the criminal court system is often not an adequate deterrent for many offences because of low levels of prosecution and fines. [(259) -- 259. See T.M. Rankin & R.M. Brown, *Persuasion, Penalties and Prosecution: The Treatment of Repeat Offenders Under British Columbia's Occupational Health and Safety and Pollution Control Legislation*, September 1988 [unpublished] at 38-41. See also John Swaigen, *Regulatory Offences in Canada: Liability and Offences* (Scarborough: Carswell, 1992) at 213-235.] The cost of using the criminal process; the need to prove guilt beyond a reasonable doubt; and the rules of criminal evidence all tend to inhibit laying of charges under the criminal system. [(260) -- 260. *Ibid.*] Existing administrative penalties, such as cancellation of discharge permits, are often equally unwieldy. Permit cancellation for minor violations will seldom be a viable option. Expanding administrative penalties to include monetary penalties and reforming the criminal process have both been suggested as ways to overcome the barriers to enforcement associated with the criminal process. [(261) -- 261. Swaigen, above at footnote 156, at 213-235, suggests that reforms to the criminal process, such as ticketing, reduced burdens of proof, specialized environmental prosecution units and changed rules of evidence may be as effective as administrative penalties in providing a cost effective credible deterrent to non-compliance with environmental laws.]

Monetary administrative penalties could be levied on permit violations or other minor environmental offences. This report focuses on expanding the range of administrative penalties, rather than on the existing administrative penalties. In some circumstances, penalties can be set by regulation and made automatically payable. [(262) -- 262. See 42 U.S.C.S. §7651j (a) (*Clean Air Act*).] In other circumstances, both the amount of the penalty and its imposition are at the discretion of regulators or, alternatively, either the amount or the imposition is discretionary. [(263) -- 263. 33 U.S.C.S. §1319(g) (*Clean Water Act*) requires the administrator to levy a penalty when they become aware of a violation, but the amount of the penalty is up to the discretion of the administrator.]

Incentives for compliance with environmental regulations also can be increased by reforming criminal procedure so that prosecutions are a viable alternative for minor offences. Ticketing is one of a number of potential reforms [(264) -- 264. See Swaigen, above at footnote 156, at 213-235, for a discussion of other potential reforms.] that facilitates increased numbers of charges being laid. Under a ticketing system a conservation officer can issue a ticket. The party charged can plead guilty and pay a pre-set fine without appearing in court. Alternatively, the accused can request a trial or do nothing. If nothing is done, the court has the power to convict without hearing evidence. This system allows large numbers of charges to be processed through the courts at minimal cost, while preserving the safeguards of the criminal process for those who wish to raise a defence.

Our support for the use of administrative penalties and ticketing is qualified by our strong support for the continued application of criminal sanctions applied through the normal criminal

procedure. Appearing before the criminal courts has a strong stigma effect and is an expression of society's disapproval of an act. [(265) -- 265. Dianne Saxe, *Environmental Offences: Corporate Responsibility and Executive Liability* (Aurora, Ontario: Canada Law Book, 1990) at 40 to 41.] Economic incentives and penalties do not have the aura of moral culpability associated with the normal criminal process. While economic incentives are strong modifiers of behavior, there is a danger that penalties and ticket fines may be seen as a cost of doing business and reliance solely on administrative fees may weaken the stigma associated with being a law breaker. Much of the discussion of potential challenges to administrative penalties is focused on ensuring that criminal sanctions continue to be available if penalties are imposed.

Chapter 4 DEPOSIT REFUND SYSTEMS

The public is familiar with deposit refund systems because of their wide use in North America for beverage containers. In this system, a deposit is paid on a soft drink or beer can or bottle. When pollution is avoided by returning the containers, a refund follows. [(266) -- 266. Organization for Economic Cooperation and Development, *Environmental Policy: How to Apply Economic Instruments* (Paris: OECD, 1991) at 17.] Consumers lose the deposit if they do not return the product, but are rewarded by the refund when the item is correctly returned. This type of economic incentive could be used more widely for a variety of products such as cars, batteries, refrigerators, other household appliances and containers of toxic pollutants such as paints and pesticides to obtain proper disposal of residuals left in the container.

Deposit refund systems for products are one way to reduce the amount and impact of packaging waste and discourage the use of some products and substances. Other waste reduction policies and laws are also needed, such as laws requiring local recycling programs, laws to reduce the use of heavy metals in packaging, bans on some types of non-recyclable packaging and voluntary packing reduction targets. Many countries are also asking or requiring industry to design solutions for waste disposal, often by requiring producers and distributors to take back waste. Making industry responsible for the costs of recycling and disposal provides an incentive for it to reduce waste and design reusable packaging. [(267) -- 267. J. McCarthy, "Recycling and reducing packaging waste: How the United States compares to other countries," (1993) 8 *Resources, Conservation and Recycling*, at 293-360.]

Deposit refund systems also are being studied for possible application to polluting or hazardous substances, such as heavy metals. A substance deposit is levied when the substance is manufactured or imported and refunded when it can be proven that the substance has been suitably disposed of or exported. [(268) -- 268. G. Huppes, *et al.*, *New Market-Oriented Instruments for Environmental Policies* (London: Graham & Trotman, 1992) at xvii.] Substance deposit refunds continue to apply despite substantial changes in the form of the substance; for instance, a deposit placed on production of lead ore may be refunded on export of a product which includes alloys using lead. Substance deposits have been suggested as an effective and efficient means for controlling the use of a number of substances in the European community. [(269) -- 269. *Ibid.*]

Deposit refund systems also have been suggested for oils and solvents. Part of the deposit could be used to impose a charge on unwanted uses of a product or on emissions. For instance, a deposit could be charged at the time of purchase of a solvent. If some of the solvent is released into the environment through leakage or burning or is incorporated into a new product, a refund could only be obtained for the amount of the solvent returned for recycling. This provides an incentive to reduce releases of solvents and their by-products in the same way as a discharge fee. Although this sort of system is similar to a substance deposit refund system, we classify it as a product deposit refund system since refunds are not available when the product, such as oil or solvent, has been transformed into another product, such as plastic or polyethylene.

Deposit refund systems are appropriate where the policy objective is to encourage proper disposal, encourage re-use or recycling, or discourage use altogether. Related measures, such as

"green levies," "advance disposal fees" [(270) -- 270. Alberta has just introduced this type of system for tires: *Tire Recycling Regulation*, Alta. Reg. 249/92; *Tire Recycling Management Board Bylaw*, Alta. Reg. 257/92; and *New Tire Advance Disposal Surcharge Bylaw*, Alta. Reg. 258/92. Florida has an advance disposal fee of one cent per container of all containers made of plastic, glass, plastic-coated paper, or other materials that are not recycled at a rate of at least fifty percent: Fla. Ste. Ann. 403.7197 (West Supp. 1990) cited in Peter S. Menell "Beyond the Throwaway Society: An Incentive Approach to Regulating Municipal Solid Waste," [1990] 17 *Ecology Law Quarterly* at 655-675.]or product bans, also may be necessary. For instance, Denmark has established a product ban on aluminum cans which are non-reusable to increase the environmental effectiveness of its beverage container deposit refund system. [(271) -- 271. J. Opschoor, *Economic Instruments for Environmental Protection* (Paris: OECD, 1989) at 86-87.]

Green levies can discourage the use of environmentally damaging products which compete with products regulated by a mandatory deposit refunds system. A mandatory deposit refund system for reusable glass bottles may encourage the use of containers that are neither recyclable nor reusable. This unwanted side effect can be countered by a green levy or ban on the use of the undesirable container. Norway has imposed a product charge on non-returnable containers to support its deposit refund system for wine, liquor, beer and soft drink containers. [(272) -- 272. *Ibid.*, at 84.]

Green levies also can be used to encourage business to voluntarily adopt deposit refund systems. For instance, a levy on the initial production or import of all beverage and food containers might encourage producers who want to avoid the levy to develop a deposit refund system for reusable containers. The potential for encouraging development of voluntary deposit refund systems may be limited. [(273) -- 273. Norway had hoped green levies on non-returnable food and beverage containers would lead to voluntary deposit refund systems, but few have actually been established: see Opschoor, above at footnote 156 at 60.] Although the British Columbia ***Social Service Tax Act*** [(274) -- 274. R.S.B.C. 1979, c. 388, section 2.4.] imposes green levies on tires and car batteries, it has not succeeded in encouraging businesses to set up deposit refund systems.

Green levies also can be combined with a refundable deposit. For instance, consumers could pay a 50 cent deposit on nickel cadmium batteries but receive only a 25 cent refund on their return. This discourages use as well as encouraging proper disposal. Alternatively, some jurisdictions give a greater refund than the deposit which is collected. [(275) -- 275. For instance, the refund for car bodies in Sweden is greater than the deposit: Opschoor, above at footnote 271.] In other circumstances, refunds alone have been used. [(276) -- 276. B.C. Hydro encourages the public to replace old energy inefficient refrigerators with new refrigerators by collecting old refrigerators and paying a \$30 bounty to the owner; B.C. Hydro then disposes of the fridges in a environmentally sound manner: telephone communication, B.C. Hydro Power Smart, Information and Marketing Services.]

Although the use of deposit refund systems could be greatly expanded, they are not a complete answer to diverting waste from landfills or avoiding toxic pollution. Other programs such as Germany's "Green Dot" program have been very successful in ensuring the return of packaging to manufacturers and ensuring high levels of recycling. [(277) -- 277. An excellent discussion of

the German program and a proposal for adopting a similar program in Canada is found in Zen Makuch & Mark Winfield's July 1992 draft paper, *Product Stewardship System for Ontario*, an unpublished paper of the Canadian Institute for Environment Law and Policy. The final version of that paper will be available shortly. The German *Ordinance on the Avoidance of Packaging Waste - Verpackungsverordnung*, German Federal Ministry of the Environment, Bonn, Germany, June 12, 1991, requires that all packaging be made of reusable or recyclable materials and that packaging be recycled or reused. Manufacturers, distributors and retailers are required to accept packaging for return. Retailers can get an exemption from this requirement if they participate in a privately funded collection system that guarantees recycling rates. If retailers do not participate in a private program, deposits are imposed on sales packaging. As a result of the ordinance German retail and industrial sectors have formed a company which funds a collection and sorting program. To participate, companies pay a licensing fee and guarantee to accept and recycle their packaging. In return they avoid deposits and can mark their products with the green dot symbol. For a more detailed discussion of this program and other programs based on this model in France and Belgium see Paula Vopni, *Dual System Deutschland*, background paper for Canadian Institute for Environmental Law and Policy (undated); see also "Stage Two of Germany's Packaging Ordinance Begins" (August 1992), 34 *Warmer* 16.] Programs such as the green dot system, as well as green levies, labeling requirements, virgin material taxes, user pay systems, waste collection and product bans should be considered along with deposit refund systems as part of an integrated effort to reduce municipal waste and toxic pollution. [(278) -- 278. See: Canadian Institute for Environmental Law and Policy, "A Nine-Point Plan for Municipal Waste Diversion in Ontario" (March, 1992).]

Enabling Legislation

As with the other economic instruments already discussed, the necessary elements in enabling legislation for deposit refund systems will depend significantly on the context. Recent amendments to British Columbia's *Waste Management Act* authorize regulations requiring the establishment of deposit refund systems for any products, product containers or packaging. [(279) -- 279. S.B.C. 1982, c. 35(2.1)(b).] For many product deposit refund systems, little more is necessary in enabling legislation. However, to establish substance deposit refund systems, the enabling legislation should be expanded. Some additional provisions could be useful for product deposit refund systems as well.

Product Deposit Refund Systems

The following components are necessary, or should be considered, in enabling legislation that allows for deposit refund systems on a variety of products:

- **Broad power to implement deposit refunds for different products and substances.** Legislation should provide for deposit refund systems for a variety of products and substances and for the levels of deposits and refunds to be prescribed by regulation. The provisions in B.C.'s *Waste Management Act* likely would not support substance deposit refund systems. [(280) -- 280. Since substance deposit refunds involve deposits on different products from those on which refunds are granted.

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- **Provide for restrictions on refunds.** Legislation should authorize regulations to restrict the conditions under which refunds are available. For instance, if deposits were paid on returned waste oil or waste solvent, regulations could provide that a refund would be paid only when the retail container is returned along with the product. This would help control illegal dilution.
- **Provide for product charges.** Enabling legislation should allow government to establish product charges by regulation. Charges could be used to ensure that deposit refund systems do not cause consumers to choose competing non-reusable products. Charges also could be used to encourage voluntary deposit refund systems. B.C.'s *Social Service Tax Act* now limits green levies to tires, car batteries and products deemed by regulation to be hazardous. [(281) -- 281. See above at footnote 274; no products are currently deemed hazardous under this provision. Also s. 35(2.1) of the *Waste Management Act* allows product levies to be imposed.

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- **Provide for product bans.** Product bans may be an important tool in a deposit refund system. The enabling legislation should include the power to establish a ban on products which will undermine the purpose of a deposit refund scheme. [(282) -- 282. For instance subsection 35(2.1)(d) of the *Waste Management Act*, S.B.C. 1982, allows a ban of product containers.

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- **Power to impose labeling requirements.** The enabling legislation should include the regulatory power for mandatory labeling of products. [(283) -- 283. See for instance subsection 35(2.1)(c) of the *Waste Management Act*.

] Labels or marks indicating that deposits have been collected on products helps curb fraudulent refund claims and ensures consumers are aware of the potential refund.

- **Provide for return of uncollected deposits to government.** The legislation should clearly state the government's power to claim any unclaimed refunds, to use either to pay for administering the system or to fund other environmental activities such as through B.C.'s Sustainable Environment Fund. In the absence of any legislative direction about unclaimed deposits, a "fair inference" is that they belong to the bottlers and distributors, and not to the government. [(284) -- 284. *Massachusetts Wholesalers of Malt Beverages Inc. v. Attorney General* 567 N.E. 2d 183 (Mass., 1991). Statutes should clearly allow regulations requiring return of uncollected deposits to government. Some American beverage distributors have argued that allowing undaimed deposits to revert to the state amounts to an unconstitutional expropriation without compensation of their property: *Maine Beer & Wine Wholesalers Association v. State*, 619 A.2d.94 (Ma., 1993); *Massachusetts Wholesalers of Malt Beverages Inc. v. Attorney General*, above. See Container Recycling Institute, "What Happens to the Deposits that are Not Redeemed by Consumers?" February 1992. This type of provision would have to have a clear basis in statute to avoid legal challenges in Canada.

] Authorizing the government to collect unredeemed deposits removes the incentive for producers and distributors to keep return rates low. [(285) -- 285. British Columbia, Ministry of

Environment, *Beverage Container Recovery System - Private Sector Ownership Structure*, (Victoria: B.C. Ministry of Environment, May 1991) at 29.]

- **Offence provisions.** The Organization for Economic Cooperation and Development has pointed out that deposit fraud may take many forms: false invoices, misrepresentation of goods, faulty classification of products, altering of import specifications, and smuggling from third countries. [(286) -- 286. Huppel, above at footnote 268, at 46.]

] Where refunds are available on the return of a used product, such as oil or solvent, it should be illegal to dilute that waste product. A high deposit provides an incentive for entrepreneurs from neighbouring jurisdictions to bring bottles, cans, etc. across the boundary to collect the deposit. In the absence of national laws, a provincial law should include provisions to deal with out-of-province redemption. Provisions such as these are included in at least one American bottle deposit refund law. [(287) -- 287. Massachusetts passed a law in May 1992 to penalize businesses that collected containers sold out of state and then knowingly returned these for refunds in Massachusetts. A recycler was successfully prosecuted for redeeming containers which had already been refunded in Maine. Container and Packaging Recycling Update, Container Recycling Institute, Washington, D.C., February, 1992.]

Substance Deposit Refund Systems

Substance deposit refund systems are substantially more complex than product deposit refund systems. Legislation allowing substance deposit refund systems will need to grapple with a number of significant issues. The law should:

- **Provide for regulations defining acceptable disposal and mechanisms to determine acceptable disposal.** The law must provide for regulations defining what constitutes acceptable disposal. [(288) -- 288. Huppel, above at footnote 268, at 133.]

] Determining acceptable disposal may also require significant discretion. The constraints on an administrator's exercise of discretion is discussed in Chapter 2. [(289) -- 289. See under the *Administrative Law - Discretion* heading.]

- **Provide for import levies and export refunds in lieu of substance deposits and refunds.** The legislation should include the regulatory power to collect or refund set fees on the import or export of products that contain a small quantity of the regulated substance. These fees would be based on general estimates of substances contained in a product, rather than actual measurements. This may be the only administratively viable way of collecting deposits for these products. Fees and refunds collected on this basis should be necessary only for imports and exports since it will be much easier to measure the primary production or disposal of a substance within the jurisdiction. [(290) -- 290. Huppel, above at footnote 268, at 47-48.]

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Provincial fees and refunds must be clearly associated with a larger substance deposit refund system. Importers or exporters of a substance should be able to opt, at their own expense, for actual measurements of the amounts of a substance exported or imported in their products. So

long as it is clear that the import levies and export refunds are intended as non-discriminatory means of avoiding the administrative difficulty of measuring small amounts of substances present in products the provisions should be constitutionally permissible. Otherwise they may risk being characterized as an unconstitutional provincial tariff.

- **Provide for administration fees.** Substance deposit refund systems can entail significant administrative costs, although these have been estimated as less than the significant environmental benefits that result. Legislation should provide for administrative fees that fully recover administrative costs. [(291) -- 291. *Ibid.*

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- **Further offence provisions.** It should be an offence to misrepresent quantities of the regulated substances that are produced, disposed of, imported or exported.
- **Enforcement Provisions.** The legislation should provide regulators with all the powers granted to excise tax collectors to carry out inspections, tests and audits.
- **Provide for sub-delegation.** It may be appropriate to delegate different functions to different agencies. For instance, customs and excise officials are already trained to collect excise taxes on the primary production and import of substances such as alcohol and would be well suited to collect substance deposits and refund the appropriate amount of deposits on export. [(292) -- 292. *Ibid.*, at 35-40.

] Other agencies would be better qualified to determine appropriate disposal of regulated substances.

- **Provide for a central agency with a power to direct delegated functions.** Since substance deposit refund systems are likely to involve different functions being carried out by different agencies, perhaps even different levels of government, a central agency should be created to coordinate these different functions, with the power to issue binding directives to different delegates. [(293) -- 293. *Ibid.*, at 30.

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- **Specify or allow regulations specifying financial arrangements.** It will be necessary to define the responsibility of various agencies for administrative costs and refunds and specify which agencies keep the proceeds from deposits. Legislation should allow for innovative financial arrangements which provide an incentive for competent administration. For instance, a report on the use of substance deposit refund systems for the European Community suggested that the party responsible for the refund portion of the system should have the refund payments deducted from its budget; this gives the administrative body a financial incentive for competent administration and fraud prevention. [(294) -- 294. *Ibid.*, at 29.

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Possible legal challenges to the use of deposit/refund systems

Manufacturers, distributors and retailers may challenge new deposit refund laws using constitutional, administrative or trade law arguments. Since beverage container legislation is one of the oldest forms of economic instruments in use, there is a history of mostly unsuccessful cases from which to learn.

Constitutional Law

As discussed in 1 Chapter 1, the Canadian provinces have a clear authority to impose deposit refund systems. This includes the power to collect deposits on imports into the province and pay refunds on exports of products from the province so long as these amounts are equal to deposits and refunds on intraprovincial production and export. The federal government also may have some authority to impose deposit refund systems in limited situations, such as for the regulation of toxic substances.

Charter Challenges

Chapter 3 addressed the potential for challenges under the *Canadian Charter of Rights and Freedoms* (the "*Charter*") to systems of emission fees. Many of the same issues arise in the context of potential challenges to deposit refund systems. For the reasons discussed in Chapter 3, challenges to deposit refund systems based on the *Charter* are unlikely to succeed. [(295) -- 295. See at footnotes 36 to 44.]

This conclusion is supported by the history of challenges to deposit refund systems in the United States, where distributors and retailers have mounted a number of constitutional challenges against mandatory deposit regulations or laws. The Courts have rejected the majority of these challenges. [(296) -- 296. See below at footnotes 298, 299, and 300 and in under the *Trade and Commerce* heading.] For instance, Courts have held that the equal protection clause of the U.S. Constitution, [(297) -- 297. Amendment XIV, Section 1 of the U.S. Constitution says "No state shall ... deny to any person within its jurisdiction the equal protection of the laws."] which is roughly similar to the *Charter's* section 15, was not violated because soft drink and beer containers were regulated differently from milk cartons and fruit juice cans, since there were many reasonable grounds which could justify the classification. [(298) -- 298. *American Can Co. v. Oregon Liquor Control Commission* 517 P 2nd 691, (Or., 1973); *Anchor Hocking Glass Corp. v. Barber* 105 A 2nd 271, (Vt., 1950); *Midstate Distributing Co. v. Columbia* 617 SW 2nd 419, (Mo. App., 1981)] In addition, the American Courts have held that the equal protection clause does not require government to attack all aspects of a problem at the same time. [(299) -- 299. *Ibid.*] The outcome of challenges such as these would be even clearer in Canada where soft drink or beer producers would not be recognized as the type of group which section 15 is intended to protect. [(300) -- 300. See , footnotes 40 to 44.]

American Courts also have rejected arguments based on provisions similar to section 7 of the *Charter of Rights*. Both the American "due process" constitutional guarantee and section 7 of the Charter have been interpreted as not allowing overly vague prohibitions if these are subject to criminal penalties. Industry in the United States has argued that due process was violated because deposit refund regulations were unconstitutionally vague. One Court found that the definition of "soft drink" in the law would give a person of ordinary intelligence fair notice as to

which beverages were within the deposit requirements. [(301) -- 301. *Bowie Inn, Inc. v. Bowie*, 335 A 2d 679, (1975).] Courts in Canada probably would come to a similar conclusion. [(302) -- 302. See *Canadian Pacific Ltd. v. Ontario* (1993), 10 C.E.L.R.(N.S.) 169 (Ont. C.A.).] American Courts also have rejected arguments that due process was violated because deposit refund laws imposed a heavy, or unequal, burden on those who must comply. Given the legitimate purpose of this legislation, arguments based on the cost of compliance simply did not warrant a due process analysis. [(303) -- 303. *Dana Distributors Inc. v. Dept. of Environmental Conservation* 532 N.Y.S. 2d 351, (N.Y., 1988); *Midstate Distributing Co. v. Columbia* 617 above at footnote 298.]

Administrative Law

Challenges to Regulations

Chapter 2 addressed limited potential to challenge regulations because of an improper or unreasonable use of discretion. Several American cases involved challenges to deposit refund laws on the basis that they went beyond the powers of the states that implemented the laws. These cases involved issues similar to challenges to regulation based on abuse of discretionary power. The failure of these challenges is a further indication that challenges to Canadian legislation or regulations are very unlikely to succeed as long as the legislative mandate is sufficiently broad.

For instance, in the United States, states have a police power which may be exercised on matters which bear real and substantial relation to the public health, morals, safety and welfare of the citizens. The exercise of that power by the legislature will not be interfered with unless it is shown to be exercised arbitrarily, oppressively, or unreasonably. Courts have held that there is a clear relation between a mandatory deposit requirement and the objective of reducing litter, and that a law designed for that purpose was not arbitrary and did not violate due process. [(304) -- 304. *Bowie Inn, Inc. v. Bowie*, cited above at footnote 301.]

Challenges to Administrators' Discretion

Straight deposit refund systems with a fixed fee for all or various classes of beverage containers provide little potential for challenge, since there is no individual discretion exercised which would give rise to a right to procedural fairness. Deposit refund systems for hazardous products containers or substance charges would involve the exercise of more discretion by regulatory officials and, therefore, would be potentially open to more challenges in Court . [(305) -- 305. See discussion in - *Discretion* heading.] Once again, clear statutory provisions for appealing decisions on the amount of deposits or refunds should exist where regulators have some discretion in determining these amounts.

Trade Challenges

Deposit refund systems and other measures [(306) -- 306. As well as the Canada - U.S. beer dispute and the Danish Bottles case discussed below we note that the German Green Dot program was challenged by France and Britain under EC law prior to France adopting a program

modeled on the Green Dot program: see Makuch, above at footnote 12, and Michael Rose, "The German Waste Packaging Ordinance: Recycling Uber Alles?" (November, 1991), 31 *Warmer* 13.] which require recycling or discourage use of non-reusable containers have been challenged under trade law because they may impose a greater cost on imported goods. Potential challenges to deposit refund systems and associated measures such as product bans, labeling requirements and green levies may arise under trade agreements such as General Agreement on Tariffs and Trade ("GATT"), the North American Free Trade Agreement ("NAFTA"), if and when implemented, or the Canada United States Free Trade Agreement (the "FTA"). [(307) -- 307. A complete discussion of trade and the environment is beyond the scope of this report.] These trade agreements place a number of restrictions on a country's ability to adopt regulations without facing trade sanctions from affected countries.

The Relevant Trade Agreements

General Agreement on Tariffs and Trade ("GATT")

GATT provides that any laws, charges or regulatory requirements applicable to imported products must also be applied to domestically produced products. [(308) -- 308. Article III, see also Julian Lew & Clive Stanbrook, *International Trade: Law and Practice*, Vol. II (1990).] Bans on importing products are also generally contrary to GATT. [(309) -- 309. Article XI. This is subject to a number of exceptions in Article XI as well as those Article XX exceptions discussed below.] Thus, a ban on import of goods in non-reusable containers might be contrary to GATT unless it comes within one of the exceptions to this rule. Moreover, the ***Technical Barrier to Trade Code***, to which Canada is a signatory, provides that countries will undertake to administer regulations relating to products so as to minimize unnecessary restrictive effects on imported goods. [(310) -- 310. Lew, above at footnote 308 at 111.]

These restrictions are subject to two exceptions listed in paragraphs (b) and (g) of Article XX of the Treaty.

1. Measures necessary to protect human, animal or plant life or health; and 2. Measures relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption. [(311) -- 311. At the time GATT was drafted, protection of the environment was not a matter of international concern, and consequently no specific mention is made of the environment.]

These provisions are generally seen as being the main basis for upholding environmental protection measures that have negative trade effects. [(312) -- 312. Frank Stone, *Canada, The GATT and the International Trade System* 2d ed. (Montreal: The Institute for Research on Public Policy, 1992) at 251.] Article XX provides that restrictions on trade justified under paragraph XX(b) and XX(g) must not be "arbitrary or unjustifiable".

Canada -- United States Free Trade Agreement (the "FTA")

The provisions of the FTA which relate to deposit refund systems are essentially the same as those in GATT. The FTA preserves the general obligations in Article III of GATT. [(313) -- 313.

Article 501, FTA.] With respect to beverage containers, parties are obligated not to introduce any specifications in relation to packaging and labeling that would constitute an arbitrary, unjustifiable or disguised restriction on trade. [(314) -- 314. See Articles 708(2) and 711.] However, this is subject to the exceptions found in Article XX of GATT. [(315) -- 315. Article 1201.] Technical specifications for other products that might be subject to deposit refund systems are valid if they are demonstrably designed to achieve a legitimate domestic objective, which is defined to include protection of the environment. [(316) -- 316. Articles 603 and 609.]

North American Free Trade Agreement ("NAFTA")

NAFTA's fate is currently uncertain, due to substantial opposition in the United States Congress and the upcoming Canadian federal election. If NAFTA is passed, it will incorporate GATT obligations and exceptions. [(317) -- 317. Article 103.1.] Whether additional obligations in NAFTA relate to deposit refund systems and related measures depends on whether the systems or measures are considered to be "standards related measures". A standards related measure is defined to include regulations on "goods' characteristics ... or their related operating methods..." [(318) -- 318. Article 915.] It is not clear whether a deposit refund system would be considered a standards related measure. Arguably a deposit refund system might be an "operating method" relating to goods. Also, labeling measures taken in conjunction with a deposit refund system are clearly standards related measures and thus would be subject to NAFTA.

Even if either deposit refund systems or related measures are considered standards related measures they will be valid under NAFTA so long as their demonstrable purpose is a legitimate objective, defined to include environmental protection, and they do not exclude goods of another party which meet that objective. [(319) -- 319. Articles 904 and 915.]

The Potential for Trade Challenges

It is necessary to consider whether deposit refund systems could be challenged as unnecessarily restricting trade and whether measures taken in conjunction with deposit refund systems -- such as levies or bans on non-reusable beverage containers -- could be challenged under these trade agreements.

Based on decisions made under GATT, reports by GATT committees and decisions made under other trade agreements, it appears that deposit refund systems are unlikely to be successfully challenged. However, environmental levies or bans on products may be problematic under trade laws, especially if they have a disproportionate effect on imports.

Deposit Refund Systems

GATT's Group on Environmental Measures and Trade recently reported that:

"...sales taxes on products that can create pollution (those containing chlorofluorocarbons, for example), deposit refund schemes for recyclable waste (bottles, scrap cars), or favourable tax treatment of environmentally friendly products (lead-free gasoline, solar panels for home heating) and other nondiscriminatory measures ensuring a pattern of domestic consumption that

minimizes pollution would not normally be open to challenge." [(320) -- 320. *Trade and the Environment*, February 1992, at 7, quoted in Miren A. Letemendia, "Packaging Initiatives as International Trade Barriers," Paper prepared for the 13th Annual Conference of the Recycling Council of Ontario, Ottawa, October 7-9, 1992, at 5.]

Similarly, a recent report from the European Community recommends expanding deposit refund systems from beverage containers to batteries and more complex apparatus such as cars and televisions. [(321) -- 321. European Community, Working Group of Experts from the Member States "Report of the Working Group of Experts from the Member States on the Use of Economic and Physical Instruments in EC Environmental Policy" (1991) 14 *Boston College Int. and Comp. L. Review*, at 447.]

While there seems to be general support within trading regimes for deposit refund systems, due to concerns about Canada's trade obligations, it is worth examining the interpretation of GATT in order to affirm the conclusion of the Group on Environmental Measures and Trade.

Any attack on a deposit refund system likely would be based on GATT. Article XX(b) is generally seen as allowing measures to protect the environment [(322) -- 322. Steve Charnovitz, "Exploring the Environmental Exceptions in GATT Article XX", (1991) 25 *Journal of World Trade* 37 and Kyle E. McSarrow, "International Trade and the Environment: Building a Framework for Conflict Resolution", (1991) 21 *Environmental Law Reporter* 10589.] so long as the measures adopted involve the least inconsistency with the trade objectives of GATT. [(323) -- 323. *Thailand -- Restrictions on Importation of and Internal Taxes on Cigarettes*, (1990) GATT Doc. DS10/R.] For example, a ban on cigarette imports imposed supposedly for human health reasons is not valid if there are no restrictions on domestic production. [(324) -- 324. *Ibid.*]

The exception in Article XX(g) is for measures relating to the conservation of natural resources. Arguably deposit refund systems are aimed at conservation of natural resources, such as land for landfill. [(325) -- 325. Deposit refund systems may also be aimed at conservation of natural resources consumed in production of imported products on which deposit refunds are placed. However, Article XX(g) has been interpreted by one GATT panel as not allowing measures aimed at preservation of natural resources in other countries: see *United States -- Restrictions on Imports of Tuna*, (1991) GATT Doc. DS21R/R as cited in Eric Christensen & S. Griffen, "GATT sets its net on Environmental Regulation: the GATT Panel Ruling on Mexican Yellowfin Tuna Imports and the Need for Reform of the International Trading System," (1992) 23 *The University of Miami Inter-American Law Review* 569, at 570.] If so, they will be valid under Article XX(g) as long as they are "primarily aimed at" conservation. [(326) -- 326. *Canada - Measures Affecting Exports of Unprocessed Herring and Salmon*, GATT Doc. L/6268.] A measure will be considered primarily aimed at conservation so long as the GATT panel finds that a government would have adopted it for its own purposes. [(327) -- 327. *In the Matter of Canada's Landing Requirement for Pacific Coast Salmon and Herring*, (1989) Canada - United States Trade Commission Panel, at 31-32.]

Although Articles XX (b) and (g) have not been considered in the context of deposit refund systems, it seems likely that the minimal trade effects of deposit refund systems would be considered acceptable if a deposit refund system were challenged. A case decided under

European law -- which places greater limits to restrictions on trade than GATT, NAFTA or the FTA -- upheld a Danish deposit refund system on the basis that the effects on trade were not disproportionate to the positive environmental effects. [(328) -- 328. *European Commission v. Denmark*, [1989] 1 C.M.L.R. 619.] In the Danish Bottles case, the European Court of Justice held the deposit refund system was

...an essential element of a system aiming to secure the reuse of containers and therefore appears to be necessary to attain the objectives of the disputed regulations. In view of this finding, the restrictions which they impose on the free movement of goods should not be considered as disproportionate. [(329) -- 329. *Ibid.*, at 624.]

Challenges to Related Measures: Product Bans and Environmental Levies

The European Court of Justice did not uphold all aspects of the Danish Bottle Law. Other parts of the Danish regulation limited the quantities of beverages which could be imported in containers not previously approved by Denmark, even where the importer could ensure the return of the containers. These were found contrary to European Community law as the quantitative restriction was judged to be disproportionate to the legitimate objective of environmental regulation. This portion of the judgment has been criticized because the reuse regulations were more environmentally beneficial and ecologically superior to the recycling requirements that the deposit refund system encouraged. [(330) -- 330. Stephen Shrybman, "Trading Away the Environment," in *The Political Economy of North American Free Trade*, Grinspun & Cameron, eds., (Montreal: McGill - Queens University Press, 1993) at 271-294.] Thus, there are some limits to the measures that can be taken in conjunction with deposit refund systems.

One limit may be the use of product taxes to encourage the use of reusable containers over the use of recyclable or non-recyclable containers. As part of an ongoing trade dispute between Canada and the United States over measures in both countries that favour domestically produced beer, in July of 1992 the United States Trade Representative (the "USTR") imposed a 50% duty on all beer brewed in Ontario. One of the major reasons cited for the tax by the USTR was an environmental levy of ten cents a container that Ontario placed on non-refillable alcoholic beverage containers. [(331) -- 331. An earlier GATT decision in the U.S. - Canada beer wars did not rule on Canada's right to impose environmental taxes: *Canada -- Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies*, (March 1992) 4 World Trade at 114.] Although the dispute was settled by an agreement on beer pricing between the United States and Canada which allowed the environmental levy to remain in effect, [(332) -- 332. Canada - U.S. Memorandum of Understanding on Provincial Beer Marketing Practices, August, 1993.] it still indicates a potential challenge to environmental levies.

The United States government and the aluminum manufacturers argued that the environmental levy was a thinly disguised tariff barrier, because the levy was not applied to soft drinks, only alcoholic beverages. American beer is primarily sold in cans, which makes it more competitive than bottled beer. The levy was, they argued, designed to make American beer less competitive. The American challenge to the Ontario levy should not be mistaken as an indication that the Ontario levy -- or green levies in general -- are contrary to international trade law per se. Problems arise because of the potential for environmental levies to be used improperly as a trade

barrier. The challenges that have been raised against green levies are based on the argument that the primary purpose of the responsible government is to protect its own producers from competition, not to save the environment. Thus, the American case points to the fact that the levy is limited to beer as proof that its real purpose is to discriminate against U.S. beer products, not to protect the environment; otherwise, other beverage containers would be included. The United States case would lose almost all its force if the Ontario levy were more widely applied. GATT panels have held that non-discriminatory environmental taxes were GATT legal. [(333) -- 333. In *United States -- Taxes on Petroleum and Certain Imported Substances*, (1987) GATT Doc. L/6175 the GATT panel upheld taxes on imported hazardous substances but rejected taxes on imported petroleum products on the basis they were discriminatory.]

Deposit refund systems in other jurisdictions.

A number of product deposit refund schemes exist and a number have been proposed. No substance deposit refund schemes yet exist, though several have been proposed. The existing regimes apply to products as varied as car hulks in Norway and Sweden, [(334) -- 334. Opschoor, above at footnote 271 at 87.] car batteries in Rhode Island, Wisconsin, Minnesota and Washington, [(335) -- 335. Michael Stone, *Environmental Excise Taxes: Options for British Columbia* (Victoria: B.C. Ministry of Environment, 1990). The laws are: Rhode Island, R.S. 23-60-1; Maine, Title 38 M.R.S., 1604; Wisconsin, R.S. Section 159.18.] and commercial-size pesticide containers in Maine. [(336) -- 336. Senators T. Wirth & J. Heinz, *Project 88--Round II, Incentives for Action: Designing Market-Based Environmental Strategies* (Washington: the Project, 1991) at 8.] The most common systems in place relate to beverage containers.

Beverage Containers

Although the percentage of beverage containers in the overall composition of the municipal waste stream is relatively small, the problem of improper disposal has been obvious and easy to solve in relation to other waste reduction or disposal issues.

British Columbia was the first North American jurisdiction to legislate a deposit refund system for beverage containers. The system is most successful with beer containers, where return rates for glass beer bottles exceed 95% and for aluminum cans exceed 90%. B.C.'s soft drink system is not as effective. [(337) -- 337. British Columbia, Ministry of Environment, *Beverage Container Recovery System*, (Victoria: Ministry of Environment, November, 1991) at 1.] The Ministry of Environment, Lands and Parks is currently considering expanding the system to include other beverage containers such as bottled water, fruit juice and drink, wine and spirits, milk, and eventually all beverages. [(338) -- 338. British Columbia, Ministry of Environment, *Beverage Container Initiative - Policy Options* (Victoria: Ministry of Environment, 1992).] A multi-stakeholder review is taking place to provide policy input on the design of a new system. An expanded deposit refund system which would encompass products other than beverage containers, as well as hazardous or polluting substances should be enacted. The proposed ***B.C. Environmental Protection Act*** could include the authority for such an expanded system. [(339) - - 339. British Columbia, Ministry of Environment, *New Approaches to Environmental Protection* (Victoria: Ministry of Environment, 1992). This legislation discussion paper released by the

Ministry about this proposed new Act contains a chapter devoted to market based incentives, but does not discuss deposit-refund systems.]

Similar systems operate throughout North America. Nine of the twelve provinces and territories have deposit refund systems for beverage containers and the B.C. Government Employees' Union has produced draft legislation for a *National Beverage Container Act*. [(340) -- 340. British Columbia Government Employee's Union "Act on Reduction of Pollution and Waste Through the Reuse of Beverage Containers," (1993).]

Three provincial systems stand out. New Brunswick's *Beverage Containers Act* [(341) -- 341. S.N.B. 1991, c. B-2.2.] applies to almost all containers under 5 litres other than milk. All containers must be approved on the basis of an acceptable plan for redemption and recycling or reuse. The *Act* provides an economic incentive for the consumer to use reusable containers over recyclable containers. The deposit is the same for either reusable or recyclable containers. The consumer, however, receives the full refund only on refillable containers and 50% of the refund on recyclable containers. [(342) -- 342. *Ibid.*, s. 5; *General Regulation - Beverage Containers Act*, N.B. Reg. 92-327, s. 9 and s. 15.] The 50% of the deposit which is not refunded is divided between distributors to cover handling costs and the province's Environmental Trust Fund, where it is allocated to environmental education, and administration of the Beverage Containers program. [(343) -- 343. *Ibid.*, *General Regulation*, s. 15 and s. 19.] The New Brunswick Act also provides authority to ensure that pricing does not eliminate the incentive to purchase refillable containers. [(344) -- 344. *Beverage Containers Act*, above at footnote 342, s. 12.]

Nova Scotia's *Litter Abatement Act* [(345) -- 345. S.N.S. 1989, c. 8.] allows the government to require approval of all types of packaging for any products. Regulations [(346) -- 346. *Beverage Container Regulations*, N.S. Reg. 246/90.] under the Act apply to virtually all alcoholic and non-alcoholic beverages requiring deposits and either reuse or recycling of returned containers. Deposits are generally higher for non-refillable containers in order to provide an incentive to reuse rather than recycle.

Manitoba's *Waste Reduction and Prevention Act* [(347) -- 347. S.M. 1989-90, c. 60.] and *Beverage Container and Packaging Regulation* [(348) -- 348. Man. Reg. 137/92.] do not require manufacturers or distributors of sealed beverage containers to establish deposit refund plans. However, they effectively encourage plans by requiring manufacturers and distributors to produce waste reduction and prevention plans and by assessing them with a charge if their sector does not achieve recycling and reuse rates of as high as 95% for some types of containers. [(349) -- 349. *Ibid.*, s. 4 and 5. Target rates for non-refillable glass containers are the lowest at 71.25% by 1995.] The government may require deposit refund systems if these measures are ineffective.

At least eleven states have laws in place and nineteen other states are considering introducing legislation. [(350) -- 350. *Container and Packaging Recycling UPDATE* (Washington D.C.: Container Recycling Institute, December 1992).] In addition, a national beverage container law has been proposed in the United States [(351) -- 351. *The National Beverage Container Reuse and Recycling Act* of 1992. Under the bill, a state would be exempt from the national legislation if it had a 70% recycling rate for containers or had legislation substantially identical to the Act. National beverage container legislation has been proposed in every Congressional session since

1971: "Container Deposit Legislation" (1986) 11 *Columbia. J. Environmental Law* 353.] The United States Environmental Protection Agency requires beverage containers sold at federal facilities to be made returnable with a \$.05 deposit.

Deposit refunds systems for beverage containers are also common in European and other countries. Countries have devised systems to incorporate deposit refunds in coordination with product bans or product taxes. A brief description of some of the European systems is found in Appendix 1.

Other Existing Deposit refund Laws

Deposit refund systems for batteries now exist or will operate soon in Manitoba, Minnesota and Denmark. [(352) -- 352. A mandatory deposit refund system (DRS) is planned for batteries in Manitoba: ERL 217. Minnesota has a statutory \$5 DRS on car batteries, cited in Calvin Sandborn, "Harnessing the Market Place to Reduce Hazardous Waste" May 29, 1991. A Danish battery mandatory DRS was scheduled to be passed in 1991; a voluntary system now been agreed. 10-50 DKr battery: ERL 206.] A system of deposits and refunds for nickel-cadmium batteries has also been proposed in Sweden. To ensure high returns of batteries, the Swedish Environmental Protection Agency has recommended refunds of 10% to 40% of the purchase price of the batteries. Cadmium in rechargeable nickel/cadmium batteries accounts for more than half of the cadmium usage in Sweden. Its use should be discouraged due to the well documented environmental and health risks. [(353) -- 353. Swedish Environmental Protection Agency, *Nickel-Cadmium Batteries: Cadmium in Phosphorus Fertilizers: Economic Instrument of Control in Environmental Policy* (Stockholm: Swedish Environmental Protection Agency, 1991).] Car batteries in Rhode Island, Wisconsin, Minnesota and Washington are subject to deposit refunds, [(354) -- 354. Michael Stone, above at footnote 335. The laws are: Rhode Island, R.S. 23-60-1; Maine, Title 38 M.R.S., 1604; Wisconsin, R.S. Section 159.18.] as are commercial-size pesticide containers in Maine. [(355) -- 355. Wirth & Heinz, above at footnote 336.]

Germany's packaging law requires 50% reduction of packaging waste by 1993. At the beginning of this year, a deposit was placed on packaging for a wide variety of products such as soaps, detergents, paints and beverages. Retailers will be responsible for establishing a collection system. [(356) -- 356. James McCarthy, "Waste Reduction and Packaging in Europe," *Resource Recycling*, July 1991, at 58.]

Car bodies are subject to a deposit refund system in Norway and Sweden. The objective is to promote the reuse of materials and discourage the disposal of vehicles out of doors, important since cars include many toxic components including lead and mercury. The initial system for Swedish car bodies worked poorly because the deposit was too low. The deposit of \$49 (U.S.) was increased to \$81 in 1988; the system raises 14M\$ annually and is used for a vehicle scrapping fund. [(357) -- 357. Opschoor, above at footnote 271, at 86.] In Norway, the deposit refund system for car and passenger van hulks has been very successful with a return rate of 90% to 99%. Most of the revenues are used for refunds, while a portion is devoted to financial assistance for collection, transportation and scrapping facilities. [(358) -- 358. *Ibid.*, 84.]

Germany has recently introduced a draft ordinance on automotive waste, requiring car manufacturers to take back post-consumer cars to drain, dismantle, and separate the cars. Manufacturers and dealers will be obliged to reuse or recycle the parts and specific recovery quotas have been established. No deposits are proposed yet, though there is authority under the *Waste Act* to require such deposits. [(359) -- 359. Jan Bongaerts, "German Ordinance on Automotive Waste," [February 1993] *European Environmental Law Review* 31.]

Proposed Deposit Refund Systems

Policy makers in the U.S. and the European Community have been urged to expand deposit refund systems in recent years.

A proposal in the European Community for a comprehensive deposit refund scheme on pollutants such as nitrogen, phosphorus, sulfur, carbon, cadmium and some organic chlorines was the result of a major research study on the use of economic instruments as tools for environmental protection sponsored by the Commission of European Communities. [(360) -- 360. Huppel, above at footnote 268.] The object of the study was to describe the potential value of financial instruments in contributing to the solution of some of the major environmental problems of the European Community such as acidification, climate change and pollution. Seven types of pollutants responsible for some of the environmental problems were chosen for study: nitrogen, phosphorus, sulphur dioxide, carbon dioxide, methane, cadmium and organic chlorines. Many economic or financial instruments were examined to determine their usefulness in reducing the use of the substances under study. Two economic instruments were found to have the broadest application based on two key criteria: the instrument had to conform to the "polluter pays" principle and the instrument had to lend itself to equal treatment of equal emission, throughout various sectors or countries. The two financial instruments that met both these criteria were the emission tax and the substance deposit system.

The substance deposit system was described as basically a tax on the import or primary production of every unit of a given substance and a refund upon export or "acceptable disposal" of every unit. A substance deposit, either alone or in conjunction with an emission charge, was found to be theoretically a useful way to control nitrogen and phosphorus emissions, sulphur dioxide and carbon emissions and cadmium and organic chlorines.

This study details the administrative and economic aspects of using a substance deposit across the Single Market of the European Community. Border control would be required for the import and export flows. A central agency would be responsible for administrative implementation of the substance deposit system, delegating its functions of deposit payment and refund at the outer borders of the European Community to existing customs and excise offices. The administrative apparatus necessary for dealing with substances like nitrogen and phosphorus, commonly used in agriculture, is already in place in the form of the structure used for the Common Agricultural Policy in the Community. The analysis assumed a uniform economic and environmental policy for the whole of the European Community, but since that unanimity does not now exist, the authors of the study propose that one country take the lead in introducing these financial instruments for environmental control. Two or more additional countries could then develop the same policy and administrative controls of the substances could be abolished for trade between

the participating countries. As more countries become involved in the program, the European Community could provide some informal guidance about the appropriate administrative setup as well as the correct level of taxes and deposits.

The long term effectiveness of these instruments is estimated to be very substantial: reductions of emissions in the order and magnitude of 50% are feasible and dynamic cumulative effects could be much higher. [(361) -- 361. Huppes, above at footnote 268, at 185.] The cost effectiveness of these instruments is also estimated to be substantially higher in the long run than that of traditional command and control techniques.

Project 88, a non-partisan research project on economic instruments to protect the environment, sponsored by two American Senators, proposed a deposit refund system for containable hazardous waste in a 1988 report. [(362) -- 362. T. Wirth & J. Heinz, *Project 88: Harnessing Market Forces to Protect Our Environment* (Washington, D.C.: Project 88, 1988).] This problem was estimated by the Congressional Budget Office to be about 30% or 80 million metric tonnes of 1983 industrial hazardous waste. Half of that amount was potentially recyclable after a reclamation or re-refining process.

A deposit refund system for this type of waste was proposed because of three positive features. First, the administrative agency would have the comparatively easy task of checking product refunds, rather than preventing illegal dumping. Second, this system would produce an incentive to recapture substance loss from the production process. Third, it would also provide an incentive to look for non-hazardous substitutes for the substances regulated under this scheme.

Project 88 continued its work with a second report produced in 1991. [(363) -- 363. Wirth & Heinz, above at footnote 336.] This report pinpointed three potential applications for deposit refunds: lead acid batteries, lubricating oil and industrial solvents, chosen because of the very high costs of improper disposal. The system for lead acid batteries contemplated a deposit collected when manufactures sold the batteries to distributors, retailers or original equipment manufacturers. Retailers would collect deposits from consumers at the time that the battery was purchased. Deposits would be received from redemption centres who would in turn collect the deposits from the manufacturers. For lubricating oil, the report proposed that consumers pay a deposit to retailers for each quart of oil purchased in return for a refund received on return of the used oil. The example of chlorinated solvents was used in the discussion on deposit refunds on industrial solvents. Again, a deposit would be paid on each unit of solvent purchased and a deposit recovered by returning the used solvent to a designated redemption or recycling facility. Solvents incorporated into products would be regulated by a front-end tax, discouraging the use of these products and encouraging firms to seek out substitutes. The Project 88 authors recognized the difficulties of administering this type of system, including verification problems, dilution of liquids, and detecting counterfeits.

A deposit refund system has been proposed for sales of refrigerator units containing chlorofluorocarbons, to ensure the proper return and disposal of such chemicals. [(364) -- 364. Peter Bohm, *Deposit-Refund Systems: Theory and Applications to Environmental, Conservation, and Consumer Policy* (Baltimore: Johns Hopkins University Press for Resources for the Future, 1981) at 129-169.] The Canadian Automobile Association has proposed that deposits "or other

means" should be used to ensure that automobile parts generally are returned and recycled. [(365) -- 365. Canadian Automobile Association, News Release (26 June 1991).]

Summary

Deposit refund systems are a well established tool for waste reduction. More use of the systems should be encouraged, for hazardous substances as well as products. There are precedents available for enabling legislation, as well as a body of mostly American case law which provides additional guidance for drafting statutes to avoid legal challenges.

Trade law has the potential for legal challenges to deposit refund systems, but the challenges are unlikely to succeed. Challenges based on the *Charter* and administrative law are also unlikely to succeed in overturning deposit refund laws.

The growth in the number of jurisdictions using this type of economic incentive, the number of products covered by these laws, and the additional products and substances proposed to be covered by the laws shows the great potential use of this tool to reduce waste and to encourage environmentally preferable behaviour.

Appendix

Beverage Container Deposit Refund Systems in Other Jurisdictions

The State of South Australia has had a compulsory deposit refund scheme since 1977. Austria has a mandatory deposit refund system on refillable plastic beverage containers combined with a product tax on non plastic beverage containers. [(366) -- 366. Environmental Resources Limited, *Economic Instruments and Recovery of Resources from Waste*, (London: HMSO) 1992, at 203.] The deposit is 4 schillings (\$0.37 U.S.). [(367) -- 367. J.E. McCarthy, "Recycling and reducing packaging waste: How the United States compares to other countries," (1993) 8 *Resources, Conservation and Recycling* at 293-360.]

Denmark has a deposit charge on beer and soft drink containers. This charge is backed up by a ban on nonrefillable beverage containers that are domestically produced, as well as a sliding scale of product taxes on packaging for liquids to encourage the use of returnable containers for recycling and reduce consumption of disposable packaging. [(368) -- 368. Environmental Resources Limited, above at footnote 366, at 205, *Ibid.*, at 307.]

Finland has a combination of deposits and taxes on non-returnable beer and soft drink beverage containers. [(369) -- 369. Environmental Resources Limited, above at footnote 366 at 207; Organization for Economic Cooperation and Development, *Environmental Policies in Finland* (Paris: Organization for Economic Cooperation and Development, 1988) at 177-172; McCarthy, above at footnote 367, at 310.] The Finnish market is dominated by refillable containers as a result of these measures.

Germany has a mandatory deposit refund scheme on plastic beverage containers except milk and liquid containers larger than 0.2 litres. The return rates for returnable beverage container systems

is at least 72%, whereas the exempt containers have much lower return rates, such as 17% for milk. [(370) -- 370. Environmental Resources Limited, above at footnote 366, at 209.] In Japan, some local governments have a mandatory deposit refund scheme on aluminum and steel cans; problems arise because the deposit is an obstacle when buying from a vending machine. [(371) -- 371. Environmental Resources Limited, above at footnote 366, at 138.]

The Netherlands has a deposit on glass beverage containers backed up by a product tax on non-refillable plastic beverage containers. It also has a voluntary deposit refund scheme on refillable PET bottles. [(372) -- 372. Opschoor, above at footnote 261, at 4-85.] Refillable PET containers are now replacing both non-refillable PET and refillable glass bottles. [(373) -- 373. McCarthy, above at footnote 367, at 316.] Norway has a combination of deposits and taxes on beverage containers: the deposit rate is set by the government and applies to all companies opting for deposit refund systems rather than product tax. Norway has return rates of 90% for beer and soft drinks, 70% on wine. [(374) -- 374. Environmental Resources Limited, above at footnote 366 at 217, McCarthy, above at footnote 102, at 317-318.]

Sweden has a deposit refund system for glass beverage containers as well as for aluminum cans. An increase in the deposit on the cans in 1987, from US \$.05 to \$.09, has led to the current return rate of 85%, the highest rate for these cans in Europe. Sweden has also prohibited the use of non-refillable PET containers as of July 1, 1991, and is considering bans on other plastic packaging. [(375) -- 375. Environmental Resources Limited, above at footnote 366, at 221, McCarthy, above at footnote 102, at 319.] Sweden requires producers of plastic bottles to establish deposit refund systems and establish that 90% of the plastic bottles can be recycled or reused. [(376) -- 376. Makuch, above at footnote 277, at 8.] The Swedish parliament is currently considering an extension of this requirement to importers. [(377) -- 377. *Ibid.*]

Switzerland has a mandatory deposit refund system for refillable beverage containers backed up by a statutory requirement for reduction of beverage containers tonnage in waste and a product tax on beverage containers. [(378) -- 378. Environmental Resources Limited, above at footnote 366 at 222.] Plastic containers are also banned unless their disposal meets standards for safe disposal of five hazardous substances. [(379) -- 379. McCarthy, above at footnote 367, at 319.]

Chapter 5 TRADEABLE PERMIT SYSTEMS

In the simplest form of a tradeable permits system the government establishes a limit on total allowable emissions of a given pollutant. It then either sells or assigns permits to industries that emit the pollutant until the limit is reached. Each permit allows the release of a given amount of pollutant during a specified time period. Polluters can buy and sell these permits so that those with the lowest abatement costs can reduce emissions and sell their permits to those with the highest abatement costs.

A tradeable permit system has three basic elements:

1. the government established a limit on total allowable emissions of a given pollutant within a defined geographical area;
2. the government then sells or assigns permits that fix the level of allowable emissions per company to emissions producers until the limit for total allowable emissions is met; and
3. if the system works, it will trigger a permits market among emissions producers, because companies whose emissions are already below the allowable limit or who have low pollution abatement costs will seek to profit from selling their excess emissions to companies whose emission levels are above the limit and cannot afford the cost of abatement measures. In this way, businesses are given a financial incentive to clean up their act.

Tradeable permit systems usually require reductions in the total allowable discharges over a certain period although they can be used to maintain environmental quality in areas that meet ambient objectives. Tradeable permit systems are distinct from current approaches to environmental protection which often do not impose an upper limit on total discharges from a particular source [(380) -- 380. Limits are often based on levels of production and concentration of pollutants.] and have no legal limits on the total permitted discharges from all sources.

This chapter discusses specific elements that are necessary and advisable in implementing legislation for tradeable permit systems aimed at environmental protection. The chapter also identifies potential legal challenges to systems of tradeable permits. In particular, it considers whether permit holders can claim compensation for regulatory changes that reduce the value of their permits.

We do not advocate adopting tradeable permit systems for pollution control in all situations. As with any complex regulatory mechanism, a poorly planned and executed tradeable permit system is worse than no system at all. The following extensive discussion of the elements of legislation required for tradeable permit systems to improve the environment shows that these systems are difficult and perhaps expensive to operate. Many of the restrictions on trading and requirements for regulatory oversight, which are necessary to ensure environmental goals are not sacrificed, may make the systems less effective in reducing the emission control costs of industry. Command and control regulation without tradeable permits may be both more effective in moving to a clean environment and more efficient. The feasibility of tradeable permit systems needs to be studied on a case by case basis.

This chapter focuses on tradeable permits or allowances, such as those used in the United States for the reduction of sulphur dioxide emissions, rather than emission reduction credits. Both are often referred to as emissions trading. Under a tradeable permit system all emitters must have tradeable permits in place before they pollute, while under an emission reduction credit system existing sources that meet command and control requirements do not require the credits to operate. Emission reduction credits are created when emissions are reduced below levels that are legal under existing command and control regulation. Acquisition of these credits is necessary for new sources to begin operation or for existing sources to modify or expand. Emission reduction credits can also be used in a tradeable permit system in order to create new permits. [(381) -- 381. For more discussion on the distinction between emission reduction credits as a part of a tradeable permit system and emission reduction credits as part of a command and control system see footnote 418 and accompanying text.]

The phrase tradeable permits can refer to different things. For instance, a permit could mean a permit which lasts for a number of years enabling the release of a certain number of units of a pollutant in the first year, less units in the second year, even less in the third year and so on. Alternatively, separate permits could be issued for each year with one less permit being issued each year. The terminology used in this chapter assumes that a permit is for a specific unit of pollution in a specific time period, although it could potentially be used in later time periods. We refer to the right to receive a permit in later years, once an initial permit is held, as allocation rights.

Throughout this discussion it is important to remember that tradeable permit systems still involve the use of some command and control regulation.

Implementing Legislation

There are a range of approaches that can be taken in enabling legislation for a system of tradeable permits, from the grant of a general power to establish a system to an extremely detailed description of the system. There are examples of both approaches in North America. On the one hand, title IV of the United States *Clean Air Act* [(382) -- 382. 42 U.S.C.S. §7651.] includes 40 pages of legislation solely devoted to establishment of a tradeable allowance system for sulphur dioxide and nitrous oxides from power plants. On the other hand, section 13 of Alberta's *Environmental Protection and Enhancement Act*, [(383) -- 383. S.A. 1992, c. E-13.3.] merely states that the minister may:

in accordance with the regulations, establish programs and other measures for the use of economic and financial instruments and market based approaches, including without limitation

(a) emission trading ... for the purposes of ... protecting the environment, achieving environmental quality goals in a cost effective manner and providing methods of financing programs and other measures for environmental purposes.

Manitoba similarly has a brief enabling provision for tradeable emission permits providing:

The Lieutenant Governor in Council may, where it is consistent with established environmental quality objectives, market units of allowable emissions of specific pollutants, in accordance with the regulations, and the revenue so generated may be held in trust by the Minister of Finance as an environmental contingency fund, to be used at the request of the Minister in the event of any environmental emergency. [(384) -- 384. Section 45, *Environment Act*, S.M. 1987-88, c. 26.]

Neither the Manitoba nor Alberta legislation give specific regulation making authority beyond the power to pass regulations for the purposes of establishing these systems. [(385) -- 385. *Environmental Protection and Enhancement Act*, S.A. 1992, c. E-13.3, s. 35(c); *Environment Act*, S.M. 1987-88, c. 26.] The difference between the American approach and the approach of Alberta and Manitoba reflects not only differences in legal tradition between Canada and the United States, but more importantly the degree of commitment of the three jurisdictions to tradeable permit systems.

The enabling provisions in Alberta and Manitoba legislation have limited what types of tradeable permit systems these provinces can establish and the mechanisms they can put in place to enforce those systems. The presumptions of statutory interpretation discussed in Chapter 2 indicate that the Courts might interpret the sort of general provisions found in Alberta and Manitoba legislation in such a narrow manner that effective tradeable permit systems might be undermined. For instance, if legislation similar to Alberta's were adopted in British Columbia, it is questionable whether the government could delegate regulation making to a local agency such as the Greater Vancouver Regional District or a Fraser Valley Air Quality Management District.

This chapter suggests terms of enabling legislation that allows for a tradeable system that will protect the environment, withstand legal challenges and provide certainty.

Our recommendations are directed at the legal requirements for designing a proper tradeable permit system; and they are generic in the sense that they are basic to any permit system regardless of the emission to be regulated. The design of a permit system to deal with a specific emissions problem will require legislation and/or regulations that are tailored to suit that situation. In practice, the success of any tradeable permit system will depend upon its use in the proper circumstances as much as the quality of the design.

Our recommendations address both the substantive and procedural issues that must be dealt with in implementing legislation to create an efficient, legally sound system that will maximize environmental protection. The substantive issues are: first, the core elements of a tradeable permit system; second, provisions relating to allocation of permits; and third, the statutory provisions required to operate the system, such as enforcement, trade approval and creation of credits. The procedural issues are: provisions aimed at ensuring fairness and openness; provisions necessary for efficient administration; and provisions allowing coordination with tradeable permit systems in other jurisdictions.

Core Elements of a Tradeable Permit System

Power to Establish Tradeable Permit Systems

The central provision of any enabling legislation will be a general mandate to establish a tradeable permit system and pass regulations for such a system. This core section will establish the scope of tradeable permit systems allowable under the legislation. In this regard we recommend that:

1. The power to establish tradeable permit systems should not be limited to permits for emissions, but also extend to permits for production and import of a product and permits for the use of a process or equipment which is expected to lead to emissions. For instance, if a tradeable permit system were established to control carbon dioxide emissions from fossil fuels, it would be much easier to issue permits for the import and production of fossil fuels based on their carbon content rather than measure actual emissions. [(386) -- 386. Canada, *Economic Instruments for Environmental Protection* (Ottawa: Minister of Supply and Services, 1992) at 39 to 40.] Similarly, tradeable permit systems have been used to govern the emission standards newly manufactured cars must meet [(387) -- 387. U.S. EPA rules for vehicle manufacturer permit trading are found at 40 C.F.R. 86.090-15 (1991).] and have been proposed or used for the phase out of hazardous substances such as cadmium and lead, based on production, import or use in a particular application. [(388) -- 388. Macauley *et al.*, *Using Economic Incentives to Regulate Toxic Substances* (Washington, D.C.: Resources for the Future, 1992) at 101 to 103.]
2. In order to avoid legal challenges to regulations based on discrimination between polluters in different areas or between different classes of polluters, the enabling legislation should allow regulations which apply only to designated areas and prescribed classes of polluters.
3. The enabling legislation must include the power to regulate trading in permits, including the power to regulate terms of trade between zones and subzones, and the ability to use permits in different time periods. These types of regulations can help avoid geographic concentration of pollutants and avoid releases at times when they are more likely to exacerbate pollution problems. Regulating transfers by means of generic trade rules rather than case by case approval generally fosters greater trading and more cost effective control of pollutants. [(389) -- 389. Brennan Van Dyke, "Emissions Trading to Reduce Acid Deposition," (1991) 100 *Yale Law Journal* 2707 at 2724.] The need for specific approval of some types of trading is dealt with below. [(390) -- 390. See footnotes 442 to 447.]

These recommendations apply if either the province or the federal government establish a tradeable permit system. However, additional considerations apply if the federal government decides to enact a tradeable permits system. Federal legislation should also establish the constitutional basis for the permit systems, since it might be attacked on the basis that the legislation is not confined to areas of federal jurisdiction. There is strong authority that courts should not consider the breadth of authority granted under statute as a basis for invalidating regulations made under the statute without considering whether the regulations themselves keep within areas of federal jurisdiction. [(391) -- 391. *Central Canada Potash v. Saskatchewan*, [1977] 2 S.C.R. 134 at 149.] Courts nonetheless often judge legislation unconstitutional on the basis of broad enabling provisions even though the regulations themselves may be quite narrow. [(392) -- 392. *Attorney General of Canada v. Hydro Quebec* (August 6, 1992), Shawnigan Reg.

410-36-000024914 (Que. S.C.); See also Rand, J. in *Saumur v. City of Quebec*, [1953] 2 S.C.R. 299 at 333.] Federal enabling legislation should specify that the power to establish tradeable permit systems is for the purposes of regulating substances which may cross provincial or international boundaries, may be a threat to human health, are a matter of national concern, may be deleterious to fish, or are emitted by federal undertakings or from federal land.

Total Emission Reduction Schedule

One of the key reasons that tradeable permit systems have gained support is that they are a means of establishing a cap on total emissions from a particular class of sources which can be reduced over time. It is essential that enabling legislation require regulations to include a mandatory schedule for reducing the cap on emissions or, where air quality objectives have been met, establish a fixed cap for emissions. This not only assures the public that there will be some improvement in the environment but also allows firms to anticipate the future value of their tradeable permits. If a schedule for reductions is not clearly set out in regulations, firms may be reluctant to trade permits for fear that the value of their permits may be suddenly reduced.

Establishing a schedule for emission reduction does not rule out acceleration of that schedule. Knowledge and scientific understanding of pollutants and their impacts on health and the environment progresses continuously. Therefore, any program must be able to accommodate changes in requirements and rules based on new knowledge or changes in values society puts on a clean environment. [(393) -- 393. Canadian Council of Ministers of Environment, Emission Trading Working Group, *Emission Trading: A Discussion Paper* (Winnipeg: CCME, 1992).] However, the legislation should clearly state that if emission reduction targets are accelerated, the units of pollution allowed by any permit will be reduced equally as compared to all other permits within the same zone or sub-area. This would assure permit holders that permits which are held for future use or sale would not be specifically targeted for confiscation or reduction in value if air emission reduction targets are redefined.

We also recommend that legislation require that schedules and caps be set to achieve desirable air quality objectives. In particular, air quality objectives could be defined as ambient concentrations identified as desirable air quality objectives under the *Canadian Environmental Protection Act*. [(394) -- 394. See Canada, Order in Council P.C. 1989/1482.] A statutory commitment to certain ambient standards will aid in reaching consensus on appropriate cap levels.

An emission reduction schedule can be used in conjunction with a system that allows for the opting in of new sources or the creation of emission reduction credits. While the total number of permits in circulation might increase, the reductions from sources initially included would be specified. Sources that opt in would acquire allocation rights which decrease with time so that reduction goals from sources initially included in the system are not diluted by being spread over a wider range of dischargers.

Local Area Caps

The enabling legislation should allow regulations to establish local area caps on some pollutants such as NO_x and VOC that may have impacts which are more localized than the areas in which a trading system for these pollutants would likely be established. [(395) -- 395. CCME Working Group, above at footnote 393, at 26, recommends that trading ratios and limitation of trading distances be used to avoid local clustering of heavy emitters or other local inequities.]

Avoiding local effects of emissions is problematic since restrictions on trading between areas may reduce the potential for both economic and environmental gains. The balancing of competing local and broader interests has led to litigation in the United States. [(396) -- 396. *Environmental Defence Fund v. Environmental Protection Agency* CA DC, No 93-1214, cited in "New York Sues to Limit Acid Rain Trading" (March 19, 1993) *Environmental Reporter* 3024.] New York state and New York environmental groups argue that restrictions on trading between the Midwestern states and other regions are necessary to ensure that sulphur dioxide emission reductions are made in the Midwest and that areas harmed by midwestern emissions, such as many parts of upstate New York, receive a net benefit. A national organization, the Environmental Defence Fund, and the U.S. Environmental Protection Agency argue that emission trading will encourage Midwest utilities to speed up emission reductions, providing quicker relief for the acid rain ravaged Northeast. They argue that, if trading is burdened with additional restrictions, incentives for early reductions will be weakened and prospects of early reductions in Midwestern emissions may be reduced. [(397) -- 397. *Ibid.* See also Joseph Goffman, "To Halt Acid Rain, Reward Innovation" (New York: Environmental Defence Fund, 1993); Joseph Goffman, "Learning to Love Emissions Trading" (New York N.Y.: Environmental Defence Fund, 1993).] While this type of challenge is unlikely to succeed in Canada [(398) -- 398. Typically challenges to EPA regulations will be much easier because there is more room for arguing that particular regulations passed by the EPA do not reflect Congress' intent.] it indicates the difficulty in identifying how to deal with trading between locales.

To avoid these disputes and to protect local air quality standards, caps could be placed on the volume of discharges which can occur within any particular sub-area within the system. Local area caps represent the maximum number of permits that can locate in that sub-area, while overall caps represent the total number of permits in existence in the large area at any time. Regulation of trading ratios would attempt to avoid the limits on local area loading being reached, but the existence of a local area cap would help ensure local inequities do not develop and allow flexibility in trading. To ensure air quality, local area caps should be somewhat dependent on the number of permitted emissions in an adjoining local area.

For instance, if a tradeable emission system existed for VOCs and NO_x in the lower Fraser Valley and lower mainland of British Columbia, one local area might represent the Port Moody area. Trading ratios could be set to encourage the migration of VOCs and NO_x production away from Port Moody which already has a high concentration of VOC and NO_x emissions. However, an absolute limit on permits allowed in the Port Moody area would provide greater assurance that there will be no localized effects.

We also recommend that legislation require local area caps be reset after the transition phase at a level necessary to meet desirable air quality objectives. To the extent that this is a feasible means of ensuring no significant local adverse impacts of trades, local area caps would partially replace the need for case by case approvals of trades. However, as discussed below, in some circumstances there will be a continuing need for some case by case approval of trades.

Avoiding Litigation Based on Claims of Property Rights in Tradeable Permits

A common concern about tradeable permits is whether they create property rights. The specific concern is whether, when a reduction schedule is accelerated or regulations are amended, polluters are able to claim compensation for "expropriation" of these "property rights". This type of claim would likely fail. However, the potential problem can be avoided by specifically stating in the enabling legislation that tradeable permits and allocation rights are not property rights but are merely a revocable licence to emit pollutants in accordance with the law.

In Canadian law there is a strong rule of statutory interpretation that compensation is payable for the taking or expropriation of most types of property. [(399) -- 399. *Attorney General v. De Keyser's Royal Hotel, Limited*, [1920] A.C. 508 at 542.] Statutes can, if their intent is clear, provide for expropriation without compensation although most governments have shied away from doing so. Expropriation is not available for the taking of non-property interests. Courts have distinguished property from revocable licences. Revocable licenses merely allow someone to do legally what they otherwise could not do; compensation is not payable on the revocation or change in the conditions of a revocable license. [(400) -- 400. See *Sanders v. Milk Board* (1991), 53 B.C.L.R. (2d) 167 (B.C.C.A.) at 175 and *National Trust Co. v. Bouckhuyt* (1987), 61 O.R. (2d) 640 (Ont. C.A.).]

As noted above, enabling legislation could specifically provide that tradeable permits are not property, but merely a revocable licence to emit a specified amount of some pollutant. This approach is taken in the U.S. *Clean Air Act* to avoid claims for compensation based on the constitutionally entrenched right in the U.S. to compensation on expropriation. [(401) -- 401. 42 U.S.C.S. §7651 b(f).] Such a provision would overcome any argument that permittees should receive compensation if the pollution allowed by their permits were to be revoked.

Claims for compensation probably would fail even in the absence of this sort of provision. In *Sanders v. Milk Board* [(402) -- 402. *Sanders*, above at footnote 389.] the B.C. Court of Appeal held that valuable statutorily created tradeable quotas created under the *Milk Industry Act* [(403) -- 403. R.S.B.C. 1979, c. 258.] were not property but were revocable licences. The characterization of the quota as a revocable licence defeated the milk producer's claim for compensation when regulations mandatorily reduced his quota.

Similarly, the B.C. Court of Appeal has held that mining under the authority of mineral claims located in a provincial park can be prohibited without compensation because the mineral claims were statutorily created and neither the mining nor the parks legislation showed any intent to compensate claim owners. [(404) -- 404. *Cream Silver Mines Ltd. v. British Columbia* (1993), 75 B.C.L.R. (2d) 324.] The Court found that the claims were property, but relied on the fact that

they were not an interest in land and were not an interest which existed at common law. Tradeable permits are also statutorily created interests.

Finally, compensation is only available for the taking of property, not the regulation of property. Courts have distinguished between the regulation of property, for instance by zoning, and the taking of property, suggesting that taking only occurs where value is added to a government asset. [(405) -- 405. *The Queen v. Tener* (1985), 17 D.L.R.(4th) 1 (S.C.C.) held that prohibiting mining in parks was a taking of mineral claims because a public asset, the park, gets the benefit from no mining taking place. *Tener* involved a different type of mineral interest from *Cream Silver*; in *Tener* the claim was an interest in real property which existed at common law. See also *Hartel Holdings Co. Ltd. v. Calgary*, [1984] 1 S.C.R. 337.] Since reductions in overall emissions do not specifically benefit a government asset they should not be a basis for compensation.

Since there are cases holding that statutorily created rights are property, it is advisable to specifically state that tradeable permits are merely revocable licences. In *Ackerman v. Nova Scotia* [(406) -- 406. (1988), 47 D.L.R. (4th) 681 (N.S.S.C.T.D.)] the Nova Scotia Supreme Court held that milk production quotas created by milk marketing board regulations were a form of property and that clear authority would be required to take a portion of this property without compensation. *Ackerman* was considered but not followed by British Columbia courts in *Sanders*, and the reasoning in the case is problematic. The milk quotas, like a system of tradeable permits, were created by regulation and would not have existed but for the regulations. Therefore, they should have been subject to changes in regulation or repeal of the regulations. [(407) -- 407. The *Ackerman* case was appealed to the Nova Scotia Appeal Court where the Court specifically refused to affirm or reject the argument that the quotas were property.]

However, while milk marketing quotas are closely analogous to a system of tradeable permits, it may be possible to distinguish the two systems and argue the need for compensation depends on the specific inferences of legislation. [(408) -- 408. Specific aspects of the legislation were important in *Cream Silver* and *Sanders* as well as in an Ontario case looking at the nature of milk quotas: *National Trust Co. v. Bouckhuyt*, above at footnote 389.] It may be possible to distinguish tradeable permits from the marketing board quota cases, for example if the statute does not require approval of trades.

While on the basis of *Sanders* and other cases it may not be necessary to specifically state that tradeable permits are revocable licences, for the sake of certainty we strongly recommend including this specific provision in the enabling legislation. An express legislative statement should remove any concern regarding claims for compensation based on property rights in permits.

Allocation of Permits

This part examines the creation and allocation of permits by government. This includes:

- allocation of permits when a system is established;
- different allocation rights given to different polluters depending on their compliance with acceptable environmental standards;

- subsequent distribution of permits by government conducted auction; and
- creation of tradeable permits through emission reduction credits and pollution reduction credits.

Initial Allocation of Permits

The three main means of initially allocating permits are through auction, according to historic emissions, or according to quantities an emitter would release if it met some criteria such as best available technology. [(409) -- 409. CCME Working Group, above at footnote 393, at 33-39.] The Discussion Paper on Emission Trading by the Working Group of the Canadian Council of Ministers of the Environment (the "CCME Discussion Paper") recommends an initial allocation based on an average of emissions in recent years. The United States sulphur dioxide program, on the other hand, allocates allowances on the basis of production levels and good practices. Allocation systems also can be combined. For instance, under the United States sulphur dioxide system, utilities receive less than their full allocation of allowances. Therefore, they are forced either to reduce emissions or acquire allowances to come into compliance. Withheld allowances are available through auctions and direct sales. [(410) -- 410. See 42 U.S.C.S. §7651 c(a), 7651 i(b); 7651 d(b); Barakat & Chamberlin, *Study of Atmospheric Emission Trading Programs in the United States: Final Report* (Winnipeg: Canadian Council of Ministers of the Environment, 1991) at 48.]

The political acceptability of one system of allocation or another will vary greatly from case to case and may vary according to the pollutant. If enabling legislation is intended to authorize a number of different tradeable permit systems it should allow allocation of permits by any means, taking into consideration certain basic principles such as fairness and minimization of economic dislocation. The legislation also should specifically provide that the total amounts permitted under the initial allocation should be no greater than amounts estimated to be released from affected sources under existing regulation.

Moreover, where initial allocation is made on the basis of historic emissions, the relevant criteria should be the lower of actual or permitted emissions. [(411) -- 411. This is the approach used in the U.S. *Clean Air Act* for sources other than electrical utilities: 42 U.S.C.S. §7651 i(c).] These qualifications are extremely important. Often permitted emissions in British Columbia and the Greater Vancouver Regional District are significantly higher than actual emissions. Allowing permitted but unutilized levels of emissions to be sold and utilized would damage the environment, as well as being an unfair windfall for emitters with lax permits. Many of the recommendations which follow in this chapter are aimed at avoiding this problem of converting unutilized permitted emissions into actual emissions.

Transitional Reductions

The CCME Discussion Paper recommends that initial allocation of permits be made on the basis of historic emission levels. This tends to reward companies which have lagged in reducing their emissions and are in a position to reduce emissions cheaply and sell excess permits, but avoids an economic shock to firms not in compliance with best practices. To partially overcome this unfairness the CCME recommends reducing allocation rights for firms which do not comply

with acceptable standards or have not applied best available control technology [(412) -- 412. For definition of best available control technology, see text at footnote 413.] at a faster rate than the reduction in allocation rights for firms that do comply with best available technology.

An accelerated reduction could be achieved in two ways. First it could be achieved by requiring firms which are furthest out of compliance with acceptable standards to reduce emissions at a faster rate, so that the allocation rights of all firms would be equal to emissions achievable through best available technology within a fixed transition period, such as five years. Second, it could be achieved by reducing rights at the same accelerated rate for all firms not in compliance with acceptable standards, while allowing a longer transition period for firms that are the furthest from compliance.

We recommend the first option. Where historic emission levels are the basis for initial allocations, legislation should specify that firms out of compliance with standards achievable through best available control technology receive allocation rights that are reduced to levels achievable through best available control technology within a specified period, such as five years. This approach achieves faster overall reductions in emissions and reduces the potential for recalcitrant polluters reaping windfall profits.

A difficulty inherent in accelerated transition for firms out of compliance with best emissions standards is defining what levels of emissions are achievable by any standard such as best available control technology. There is a strong incentive for polluters to argue that the lowest emissions achievable through best available control technology are relatively high; doing so would give polluters greater potential to sell allocation rights on the market because they would be more likely in a position to reduce emissions below the defined level.

To partly overcome this difficulty legislation should include a strong definition of what is meant by best available control technology ("BACT"). We recommend adoption of the definition of BACT used in a recent British Columbia government discussion paper on environmental protection:

"the currently available state-of-the-art control technology which is proven to be successful at reducing waste discharges and has been applied for at least one year in similar facilities in the province or in other relevant jurisdictions. Control technology refers to all of the following: raw materials, fuels, process technology and pollution control equipment or devices used to minimize both generation and discharge of wastes." [(413) -- 413. British Columbia, Ministry of Environment, Lands and Parks, *New Approaches to Environmental Protection in British Columbia*, (Victoria, B.C.: Ministry of Environment, 1992).]

Legislation should allow regulations to specify what emission levels constitute best achievable emissions. As discussed in Chapter 2, if specified by regulation these emission standards would be less susceptible to legal challenge. Setting these emission standards by regulation is preferable to setting these standards by administrative process, since successful appeals of administrative decisions could undermine adherence to discharge caps. If regulations are used, dischargers and the public should be given an opportunity to comment on the content of draft regulations which establish allocation rights dischargers will receive for the period following transition.

Subsequent Auctions

Enabling legislation should provide for a system of periodic auctions of permits whereby each emitters' allocation rights would be reduced by a certain percentage for the purpose of being auctioned off. Reduction in allocation rights in order to obtain permits for auctions would be in addition to reductions in allocation rights aimed at reducing overall discharges. Auctions could be conducted to raise revenues for the government agency responsible for the system or on a revenue neutral basis. In the revenue neutral case, the revenues generated would be returned to polluters in proportion to the permitted allocations taken from them and sold in auctions. The advantages of periodic auctions include: [(414) -- 414. These advantages are discussed in Van Dyke, above at footnote 389, at 2718.]

- overcoming psychological barriers against trading;
 - reducing any incentives for permit holders to hoard their permits;
 - lowering transaction costs;
 - ensuring that permits are not used by one firm to exclude competitors from the local market;
 - if regulators are given a portion of revenue generated by auctions, providing a strong incentive to ensure compliance since strict enforcement would ensure higher permit prices and hence higher revenue; and
-
- **if auctions are revenue generating obliging polluters to compensate society for the costs imposed upon it by their polluting activities. Revenue generating auctions would be more in keeping with polluter pay principle . Revenue generated which is not allocated to administration could be held in a special fund for environmental remediation.**

For these reasons we recommend that legislation require periodic revenue generating auctions. [(415) -- 415. The CCME Discussion Paper, above at footnote 393, endorses discharge fees. Revenue generating auctions would fulfill similar purposes as well as encouraging trading.] The CCME Discussion Paper has endorsed the concept of emission fees which act in a manner similar to revenue generating auctions.

There may be some value in giving administrators the authority to refuse to sell permits to the highest bidder where the administrator has reasonable grounds to believe that the highest bidder is purchasing the permits for the purpose of excluding bidders from the market. As an adjunct to this power the administrator could have powers to require bidders to provide information as to their abatement costs. Information that marginal abatement costs are significantly lower than permit prices would be an indication that the purchaser is attempting to exclude competitors from the market. [(416) -- 416. Some economists have suggested a rule requiring demonstration that marginal abatement costs exceed the price rights as a precondition of approval of purchases: See Walter S. Misiolek and Harold W. Elder, "Exclusionary Manipulation of Markets for Pollution Rights," (1989) 16 *Journal of Environmental Economics and Management* at 156.] The power to block sales and the power to require such information would need to be grounded in specific statutory provisions.

Opting In and Creation of Emission Reduction Credits [(417) -- 417. The discussion above on emission reduction credits was limited to their use in a tradeable permit system. There is a much more extensive history of the use of emission reduction credits in the United States as an adjunct to traditional command and control technology. In the United States emission reduction credits have been used to reduce compliance costs related to traditional command and control technology.

With some simplifications the four elements of the U.S. EPA's emission reduction credits policy are as follows:(a more complete description can be found in Robert W. Hahn & Gordon L. Hester, , "Marketable Permits: Lessons for Theory and Practice," (1989) 16 *Ecology Law Quarterly* 361 at 370 to 375. *Offsets*. The offset rule requires new and modified sources in heavily polluted areas to offset their increased or new emissions with emission reduction credits from other sources in the same area. These sources are still required to meet stringent emissions limitations;(Lowest Achievable Emissions Rate in areas that do not meet clean air objectives, Best available technology in areas that meet objectives). *Netting*. Netting allows a modified source to avoid the most stringent emission limitations that would be applied to the modification by reducing emissions from another source within the same plant. *Bubbles*. Bubbles allow existing sources to vary the levels of emission control applied to emissions from different sources as long as the aggregate limit is not exceeded. The sources included within the imaginary bubble do not have to be within the same firm. *Banking*. Banking allows firms to reduce emissions at one time to use at a later date. There is no reason in law why any of these elements could not be included as a matter of policy in existing permit systems. For instance, the Greater Vancouver Regional District could require offsets for any new or expanded source in the area. *Fisheries Act* pulp mill regulations could similarly be amended to allow banking. As a matter of policy, however, we are strongly opposed to the use of emission reduction credits (with the exception of offsets where there is a continuing requirement for stringent emissions) unless all the safeguards discussed below are in place. If the government considers use of emission reduction credits in the context of the current command and control regulation we recommend that there be legislation allowing emission reduction credits that commits the government to those safeguards and protects regulators from pressure to allow questionable emission reduction credits. The problems we have identified with regard to emission reduction credits in a tradeable permit system are even greater in a command and control system where there is no overall reduction in the cap to compensate for the difficulties inherent in emission reduction credits.]

Opting in of sources and creation of emission reduction credits is another means of creating tradeable permits in relation to initial allocations.

The CCME Discussion Paper notes that tradeable permit programs can be broadened to cover polluters through

- adding new participants by category,
- allowing voluntary opting into the program by emitters, or
- by allowing participants to reduce emissions from sources within their plant or firm or from third parties that are not part of the system. These reductions from non-participating sources would count as credits that could be exchanged for permits and allocation rights. For example, the California South Coast Air Quality Management District's "Beater Buy Back" program

allowed several oil refineries to gain emission allowances by purchasing and destroying old automobiles with high exhaust emissions. [(418) -- 418. See Environmental Defence Fund and General Motors Corporation, *Mobile Emissions Reduction Crediting: A Clean Air Act Economic Incentive Policy Proposal for Retiring High Emitting Vehicles* for a description of the SCAQMD program and for a similar proposed national program.

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The last two options are essentially the same, merely representing different ways of creating tradeable permits by reducing emissions from sources that are not required by law to take part in the tradeable emission permit system. We refer to these together as creating tradeable emission reduction credits.

Generally speaking, emission trading systems will likely be more effective if covering a broader base of emitters. However, there are several significant problems with creating emission reduction credits that, if not adequately compensated for, could easily subvert the success of any program. Emission reduction credits have been subject to a number of court challenges in the United States based on the argument that they subvert the purposes of the *Clean Air Act*. [(419) - - 419. *Natural Resources Defense Council, Inc. v. Gorsuch*, 685 F. 2d 718 (D.C. Cir., 1982); reversed sub nom *Chevron U.S.A. Inc. v. Natural Resources Defence Council* 467 U.S. 837, 81 L. Ed 2d 694 (1984). In the *Gorsuch*, case the U.S. Court of Appeal held that application of the netting (see footnote 417) to non-attainment areas was contrary to the purposes of the *Clean Air Act* to improve environmental quality in those areas. The U.S. Supreme Court overturned this decision only because it found that the EPA had to be given more room in implementing legislation than the Appeal Court had allowed.] Although there is much less potential for such litigation in the Canadian legal context, [(420) -- 420. Under the American system Congress passes relatively specific laws which the Environmental Protection Agency must implement through passing regulations. The EPA can be sued for not implementing regulations within the time mandated by Congress or for passing regulations out of keeping with the policies of statutes passed by Congress. Canadian legislation does not usually require action and is much less specific in terms of goals to be achieved etc. Because of this there is much less potential for litigation challenging the content of regulations.] the issues raised are important.

Claiming Credit Where Credit is Not Due

When emission reduction credits are created they will be based on claims that a non-participating source has reduced emissions by a certain amount. In practice it will be very difficult to measure actual emission reductions. For instance, an urban smog reduction program for the Fraser Valley initially would include mostly or all permitted point sources. Stack emissions from these sources are generally much easier to measure than pollution from the types of sources likely to create emission reduction credits, such as fugitive emissions [(421) -- 421. Fugitive emissions are emissions that escape unintentionally from a process, for instance VOC which escapes from car gas tank filler pipes rather than exhaust pipes, or gases that escape from leaks in pipes rather than emission stacks.] and non-point sources. Fugitive emissions can only be estimated, and often there is great uncertainty in predicting discharges from non-point sources. [(422) -- 422. David Letson, "Point/Non Point Source Pollution Reduction Trading: An Interpretive Survey," (1992)

32 *Natural Resources J.* 219 at 226.] It is very easy to overestimate emission reductions from sources that are not susceptible to monitoring. [(423) -- 423. See David Hawkins "Providing Economic Incentives in Environmental Regulation," (1991) 8 *Yale J. of Regulation* 463 at 490; Richard Liroff, *Reforming Air Pollution Regulation: The Toil and Trouble of EPA's Bubble* (Washington, D.C.: Conservation Foundation, 1986) at 74 to 95.] Indeed, in one American example, emission reduction credits were claimed for a supposed 20% reduction in emissions from command and control standards; these claims were initially approved by regulators. A subsequent reexamination of the figures and assumptions by the Natural Resources Defence Council concluded there would be a 36% increase in emissions. [(424) -- 424. Liroff, *Ibid.*, at 91 to 97.] When invalid emission reduction credits are used to increase emissions from other points, the result can be an actual increase in emissions.

Claiming Credit For the Inevitable

In many cases emissions that are the source of emission reduction credits may have been reduced even without the emission reduction credit program. For instance, a "Beater Buy Back" program in the Lower Fraser Valley might only buy back vehicles that would be taken off the road soon even without the program. While estimates can be made of the probable continued use of cars of a certain age, [(425) -- 425. See Environmental Defence Fund and General Motors Corporation, *Mobile Emissions Reduction*

Crediting: A Clean Air Act Economic Incentive Policy Proposal for Retiring High-Emitting Vehicles, (undated) at 12-13.] changing regulations can drastically accelerate the retirement of high emission cars. Many "beaters" would likely be taken off the road because of the implementation of Air Care regulations. If firms get credit for reductions that would have occurred anyway, overall progress in emission reductions will be less than if emission reduction credits were not available.

The Opportunity Cost of Emission Reduction Credits

There are only a finite number of easy, cheap, and technically obvious emission reduction opportunities. [(426) -- 426. Hawkins, above at footnote 423.] One reason for the current pollution levels is that regulators have difficulty identifying a sufficient number of inexpensive and attractive regulatory options. [(427) -- 427. *Ibid.*] Industry is often in a better position to identify these cheap options for reducing discharges. The problem is that if you create an incentive that lets industry identify emission reduction options and then apply the benefits to compensating for poorly controlled new units, you have skimmed the cream from attractive emission reduction opportunities that might have been identified by government regulators. [(428) -- 428. *Ibid.*] Instead of making progress towards an overall reduction in pollution, the benefit is applied to compensate for an emission increase that could have been avoided. [(429) -- 429. *Ibid.*]

Valuable Credits for Poor Performers

Providing for emission reduction credits also raises the same problems as distributing permits to a number of different sources, whose efforts to reduce or eliminate emissions have varied. Distributing permits on the basis of historic emissions tends to reward the worst polluters.

Increased Enforcement Demands

Emission reduction credits can place additional strains on enforcement. A U.S. Environmental Protection Agency review of emissions trading states

"It will increase the number of sources that must be monitored and thus may overwhelm resources available to assure adequate and continuous compliance with regulations. An examination of some of the early trades indicates that (emission reduction credits) will involve small and non-point sources not historically given much attention by the regulators.... Measuring emissions from these sources ... may be extremely difficult and expensive." [(430) -- 430. Eckard Reh binder & Rolf-Ulrich Sprenger, *The Emissions Trading Policy in the United States of America: an Evaluation of its Advantages and Disadvantages and Analysis of its Applicability in the Federal Republic of Germany* (Washington, D.C.: United States Environmental Protection Agency, March, 1985) at 116 to 119.]

These strains on enforcement would be added to strains placed by emission trading in general. [(431) -- 431. See under the heading "Enforcement" below.] The need to spend funds on increased enforcement must be taken into account when deciding on whether or not to implement a program.

Safeguards Against Negative Aspects of Emission Reduction Credits

Emission reduction credits are one of the prime concerns of environmentalists in assessing tradeable permit systems. In the U.S. these concerns have led to litigation. The State of New York and the Environmental Defence Fund contend that credits given to firms for improvements already made and for improvements they would have had to make in any event are contrary to the goals mandated by Congress. [(432) -- 432. "New York Sues to Limit Acid Rain Trading; EDF Suit Seeks to Close Credit Loophole" (March 19, 1993) *Environment Reporter* 3024.] While lawsuits of this type are unlikely to arise in the Canadian context, [(433) -- 433. The U.S. litigation is based on statutorily set emission reduction goals and much more extensive statutory direction than is likely in the Canadian context. This is due to the nature of the U.S. constitution where the administration of laws is independent from the legislature.] the American experience indicates the need to deal adequately with emission reduction credits if tradeable permit schemes are to be seen as legitimate.

Despite these concerns, emission reduction credits should not be rejected out of hand. In some cases they have helped accelerate emission reductions. [(434) -- 434. See Liroff, above at footnote 423, at 100 and 131 to 134, who concludes that bubbling for existing sources (see footnote 417) under the U.S. *Clean Air Act* has helped accelerate compliance in some cases.] If emission reduction credits are allowed, it is essential the enabling legislation include provisions

ensuring that there will be no increase in actual total emissions or a slowing of progress toward reductions in total emissions. We have a number of recommendations in that regard.

First, regulators should only have the authority to approve emission reduction credits from non participating sources or approve sales of allowances from opted in sources where it can be demonstrated that emissions were occurring at the rate claimed prior to reduction. Regulators must be required by statute to abide by the principle that emission reduction credits can only be given for reductions that would almost certainly not have occurred otherwise. [(435) -- 435. The South Coast Air Quality Management District, Rule 1309(1) requires that applicants for emission reduction credits demonstrate that they are real, quantifiable, permanent and enforceable.] As discussed below, [(436) -- 436. See "Public Involvement and Appeal".] the allocation of emission reduction credits should be subject to appeal by all interested parties including the public through a defined appeal mechanism.

Second, because sources of emission reduction credits tend to be poor environmental performers and have emission levels that are difficult to measure, emission reduction credits should only be available for reductions below the level of emissions achievable with best available control technology. The latter provision is found in many American tradeable permit systems. [(437) -- 437. For instance, South Coast Air Quality Management District Rule 1309(1) provides that applicants for emission reduction credits must prove that reductions are "not greater than the equipment would have received if operating with the best available control technology". Similarly, the American sulphur dioxide trading emissions program requires that any sources opting into the program only be allocated allowances up to the levels of emissions which would occur if the sources were in compliance with the best available control technology provisions of the *Clean Air Act*: 42 U.S.C.S. §7651 i(f).]

Third, there should be an automatic discounting of emission reduction credits. For instance, some American jurisdictions automatically discount any emission reduction credits by twenty percent. [(438) -- 438. South Coast Air Quality District, Rule 1303(b)(2).] Allocation rights based on emission reduction credits should be reduced at a faster rate than allocation rights of sources in compliance with best available technology. Indeed, we recommend that allowances for opted in sources be reduced by some minimum amount, such as 20 percent of their initial value per annum. The minimum amount should be supplemented by a higher rate at the discretion of regulators where they have reason to believe emissions from which credits are claimed would have been eliminated.

Finally, we recommend that where a source opts into the system, its allowances should be based on the lower of current emissions or their emissions prior to widespread discussion of implementing a tradeable permit system. This would guard against a source increasing its emissions for the purpose of opting in and then selling emission reduction credits based on its inflated emissions. The *Clean Air Act* in the United States uses this approach: sources which opt in to the sulphur dioxide emissions trading program have their initial allocation of permits based on production levels in the years 1985, 1986 and 1987, a period two to four years prior to introduction of the Clean Air Amendments into Congress. [(439) -- 439. 42 U.S.C.S. §7651 i(b).]

These safeguards against misuse of emission reduction credits might reduce the utility of emission reduction credits to industry to such a degree that they are not utilized. However, to allow the creation of tradeable permits from emission reduction credits without adequate safeguards is much like a government not protecting itself against counterfeit currency. While emission reduction credits have the potential to achieve some environmental gains, they also have the potential, if not properly implemented, to flood the market with counterfeit reductions.

In summary, emission reduction credits can broaden the scope and number of polluters taking part in a tradeable permit system and can create more tradeable permits. Unfortunately, they can also subvert environmental goals if not adequately regulated. Government must be aware of this risk when adopting a tradeable permit system.

Pollution Reduction Credits

Pollution reduction credits are similar to emission reduction credits, but are issued in exchange for activities that remove contaminants from the environment. Pollution reduction credits are usually discussed in relation to carbon emissions trading, giving credit for activities that will remove carbon dioxide from the air. However, activities for which credit would be given may only be a temporary or partial solution to the pollution problem. For instance, credits for planting of forests would allow increased carbon dioxide emissions in spite of the eventual release into the environment of the carbon temporarily absorbed by growing trees. [(440) -- 440. Canada, *Economic Instruments for Environmental Protection: Discussion Paper* (Ottawa: Minister of Supply and Services, 1992) at 40.] Due to the limited potential for pollution reduction after contaminants have been released, we recommend against statutory provisions for pollution reduction credits.

Operation of the System

Once permits are allocated or created from emission reduction credits, the day to day operation of a tradeable permit system presents a number of issues, including approval of trades by regulators, registration of trades, monitoring and enforcement. These are discussed below.

Trade Approval

The need for predictability in approving trades on the basis of clear and consistent rules has been underlined by a number of commentators. [(441) -- 441. See Barakat & Chamberlin, above at footnote 410, (Winnipeg: Canadian Council of Ministers of Environment, Emission Trading Working Group, 1991) at G-15; see CCME Working Group, above at footnote 393, at 45.] As discussed above, [(442) -- 442. See text accompanying footnote 406 to 410.] the power to set generic trade approval rules defining trading ratios and maximum concentrations of emissions within any area or sub-area can help ensure consistency and predictability. We recommend that generic trade approval rules be used as much as possible so that permittees become familiar with the rules and know when a permit is tradeable. However, any system will involve some case by case approval, to ensure actual reductions occur from the source selling the permit and to ensure that individual characteristics of the emission permitted do not cause harmful environmental effects.

Ensuring an Actual Reduction by the Vendor

There always will be difficulties in ascertaining that a reduction has been made where:

- the firm selling permits or allocation rights does not have continuous emissions monitoring systems ("CEMS") in place;
- where the firm selling the permit has opted into the system;
- where the firm selling the permit has increased its output in order to gain additional permits based on historical emissions;
- where the firm selling the permit would have voluntarily reduced its emissions or would have been forced to reduce its emissions in any case.

Generally applicable safeguards for permit transfers should include legislated requirements that legislators be convinced on demonstrable evidence that an emission reduction has taken place, and that this reduction would likely not have taken place in any event. Moreover, administrators should be required to discount by a minimum amount, traded permits from firms not having CEMS or from permits created through an emission reduction credit with the possibility of requiring further discounts to ensure that there is no increase in emissions. Once such emission reductions have been approved, the permits being traded could be certified to indicate that there will not be a need for further demonstration of actual reductions if those permits are traded in the future.

Review of Individual Effects

A review by the American Environmental Protection Agency of its emissions trading policy [(443) -- 443. The EPA review of the bubble policy allows a firm to increase emissions from one source above generally applicable standards in exchange for compensating by decreases in emissions from other sources.] states:

There are well-founded fears that equal trade-offs among the same pollutants may nonetheless degrade environmental quality because of the different physical and biochemical characteristics of the traded emissions

For example, particulates emitted from a stack might have a different size and chemical composition than fugitive dust from roads or storage piles within a plant site and therefore might have a totally different and more harmful impact on ambient air quality.

For trades involving non-reactive pollutants, such as SO₂, TSP, or CO [sulphur dioxide, particulate matter, or carbon monoxide], whose ambient effect may vary where the emission increases or reductions occur, ambient considerations are crucial. In addition to distance between sources, plume parameters (e.g. stack height, temperature and velocity of stack gases), pollutant characteristics, meteorology and topography will also affect the ambient impact of such a trade. [(444) -- 444. See above at footnote 430.]

In some cases the negative aspects of one trade may be balanced out by the positive aspects of another trade and in other cases the inability of emission impact modeling to make accurate

predictions of effect [(445) -- 445. *Ibid.*, at 122 to 122.] may limit the utility of case by case analysis. However, there clearly is a need for administrators, on a case by case approval basis, to ensure that trades do not lead to reduction of overall environmental quality or hot spots of pollution.

Public Registry and Banking

All permit trades, including allocations, sales and transfers, should be recorded in a public registry. A registry should have separate accounts for all sources. Trades would not be effective until recorded. Publication of data on firm emissions and permits in place would facilitate trading activity and tend to expose any firms who are hoarding allowances for anti-competitive purposes. [(446) -- 446. See CCME Working Group, above at footnote 393 , at 45 and Barakat, above at footnote 410, at F3 and G13.] A banking system also could be used to identify and register allocation rights or permits being held as surplus. Permits or allocation rights registered as surplus could then be utilized in the future or sold. [(447) -- 447. CCME Working Group, above at footnote 393, at 42.] Tracing of permits and emissions in different zones and local areas would ease public concerns over the concentration of emissions.

Enabling legislation should require a registry system with public access to data on emissions and permit holdings. It should also provide authority to regulate the banking of permits for future use. [(448) -- 448. The benefits of allowing permits to be banked for future use or sale have been identified by the CCME Working Group and others. See CCME Working Group, above at footnote 393 at 43 and Hahn, above at footnote 417, at 384-328.] Permit holders should pay the cost of the registry, including public access.

Liability of Purchaser for Vendor's Activities After Sale

We recommend that the legislation clearly set out when a purchaser of allocation rights or a permit will be penalized for the fact that the permit or allocation rights were improperly created by the vendor or earlier holders. While holding buyers liable for the legitimacy of their permits encourages buyers to scrutinize their purchases, too strong a "buyer beware" policy will make firms reluctant to trade permits. Under the United States sulphur dioxide emission trading program, if a permit allocated to an opted in source is sold and the opted in unit subsequently closes the permit is considered void.

We recommend that implementing legislation clearly set out that the purchaser will be responsible if, at the time of purchase, it is aware, or if it has reason to suspect after due inquiry, either that the vendor's emissions exceed its remaining allocation or that the emissions were created through some improper means such as the claimed reduction in emissions being greater than the actual reduction. This provision requires purchasers to exercise due diligence and make inquiries to avoid against dishonest transactions, while not adding significantly to transaction costs.

Sales of Permits from Firms that Close or Reduce Production

It also is necessary to consider how regulators approving trades should treat permits from firms that have reduced their emissions by shutting down or lowering their production rate. The U.S. bubble policy [(449) -- 449. See footnote 417.] has been criticized for allowing creation of credits that would last indefinitely from reductions by plants that would have closed their doors in a few years. Allowing trading of such permits can slow emission reductions in later years. [(450) -- 450. Rehbinder & Sprenger, above at footnote 441.]

We recommend that legislation prohibit sales where a firm is only in a position to sell permits because it has shut down or reduced its operations, unless the firm purchased those permits. Rewarding a firm for leaving the jurisdiction by allowing it to sell rights to a public resource which it acquired at no cost is indefensible and would be a serious impediment to public support for an emissions trading system. In keeping with this approach, the United States sulphur dioxide trading program prohibits the transfer of allowances from opted in sources who reduce or cease production. [(451) -- 451. 42 U.S.C.S. §7651 i(f).]

Monitoring

Accurate monitoring is essential for an effective tradeable permit system. This is true not only because there is greater incentive to cheat in a tradeable permit system but also because command and control approaches may offer alternatives to actual emissions monitoring that are not available under a tradeable permit system. [(452) -- 452. CCME Working Group above at footnote 393, at 50.]

Under the United States sulphur dioxide emission trading program, emitters are required to operate continuous emissions monitoring systems ("CEMS") on each stack. Alternative monitoring systems are only permitted where they can provide information with the same precision, reliability, accessibility and timeliness. [(453) -- 453. 42 U.S.C.S. §7651 k(a); see also §7661 (c) for monitoring requirements on ozone depleting substances.]

A general requirement for CEMS should be established in any implementing legislation. For small polluters CEMS may be prohibitively expensive. Administrators may need a power to approve alternatives to continuous emissions monitoring for emitters below a specified size. Legislation should provide that where an alternate system does not have the same precision, reliability, accessibility or timeliness as provided by CEMS, special requirements shall be imposed for approving any trades of permits from such sources. Legislation should include criteria for approval.

Reliability of emissions data is essential to the working of a tradeable permit system. A 1993 report of the U.S. General Accounting Office reviewing self-reporting of emissions monitoring results found that sampling was statistically unrepresentative and open to substantial fraud both in sampling of emissions and in testing. [(454) -- 454. United States General Accounting Office, "Environmental Enforcement: EPA Cannot Ensure the Accuracy of Self-Reported Compliance Monitoring Data" (Washington, D.C.: GAO/RCED, March 1993) at 21.] The result appears to be a very significant level of fraud amongst emitters and independent laboratories. [(455) -- 455.

Commercial laboratories may falsify emissions monitoring with or without the knowledge of facility operators in order to save money or handle more work. In some instances falsification has been a routine part of major commercial laboratories' operations: *Ibid.* at 51 and 56-7. Instances of fraud by emitters have included plant managers persistently over a period of at least nine years directing workers to falsify results: *Ibid.* at 53.] Even where programs are in effect to detect fraud in emissions monitoring, the chances of detecting fraud is often low. [(456) -- 456. *Ibid.* at 55.] As a result, self reporting of emissions monitoring should not be permitted if there is any potential for falsification of data. This may be a major constraint to the use of tradeable permit systems.

Enforcement

Commentators on tradeable emission permit systems consistently reiterate the need for strong enforcement. [(457) -- 457. Barakat & Chamberlin, above at footnote 410, at G-14.] Both inspection of facilities and prosecution of offences must be increased in a tradable permit system. There is an added incentive for polluters to exceed their permitted emissions in a tradeable emissions system as extra permits can be sold. This must be counterbalanced by a high probability or near certainty that offences will be penalized.

Inspection activities will need to increase because firms are less likely to operate substantially below their permitted emissions, as is now common, when they could sell excess permits for profit. [(458) -- 458. Reh binder & Sprenger, above at footnote 430, at 193.] As discussed above, [(459) -- 459. At footnote 441 to 443.] if emission reduction credits are allowed, demands on regulators will be exacerbated since there will be an increased number of hard to measure sources to inspect. Legislation should provide either for revenue generating auctions or emission fees to ensure inspectors are adequately funded. [(460) -- 460. See the headings "Subsequent Auctions" above, and "Ability to Charge Emission Fees and Administrative Fees," below.]

Penalties should significantly exceed the cost of acquiring permits. Penalties for administrative violations -- inaccurate records, tampering with monitoring devices -- must be sufficiently stringent that these violations are not used to disguise noncompliance. [(461) -- 461. Barakat & Chamberlin, above at footnote 410 at G-14 to G-15.] Under the United States sulphur dioxide emission trading program, an automatic penalty of \$2000 per tonne over permitted emissions is automatically levied every time a polluter exceeds its allowable emissions. [(462) -- 462. 42 U.S.C.S. §7651 i(j).] Firms that exceed permitted emissions also must offset future emissions by an amount equal to the exceedance. The fine is payable whether or not authorities take any action. Firms are liable for a further criminal penalty if they do not pay the automatic fine. [(463) -- 463. 42 U.S.C.S. §7651 j(d).] Firms out of compliance with monitoring requirements are assumed to be out of compliance with their permitted allowances. [(464) -- 464. 42 U.S.C.S. §7651 k(d).]

In the South Coast Air Quality Management District fines of up to \$25,000 per violation per day can be levied with the possibility of permit revocation as well as possible civil and criminal penalties. [(465) -- 465. Barakat & Chamberlin, above at footnote 410, at 53.]

We recommend that any implementing legislation impose high minimum fines for permit exceedances. Fines should be levied, as under the sulphur dioxide trading program, on the basis of X dollars per unit of a pollutant and should be levied automatically whether or not the polluter exercised diligence in avoiding the permit exceedance. The penalties should be automatically payable without any regulatory action if monitoring data indicates a permit exceedance. Failure to pay should constitute an offence. Legislation also should provide for substantial minimum criminal penalties where firms are not diligent in avoiding permit exceedances. All permit exceedances should be offset by future reductions in emissions.

Any implementing legislation clearly must grant the regulators power to enter on to any premises where emissions are occurring and inspect the emissions as well as the monitoring equipment. For tradeable permit systems enacted by the province, these enforcement provisions exist under section 21 of the *Waste Management Act*, although special consideration should be given to creating a specific authority to test and examine monitoring equipment. Also, if there is any self reporting of monitoring data legislation should give regulators the right to conduct routine searches, inspections and audits of laboratories relied on to analyze tests. [(466) -- 466. See above under enforcement.]

Implementing legislation also should include provisions similar to those in the federal *Canadian Environmental Protection Act* (CEPA) permitting concerned citizens to participate in enforcement, both in the administrative process and in the courts. Under CEPA, any two Canadian residents of majority age can require an investigation if they have reason to believe that an offence has been committed under the Act. The proposed Ontario *Environmental Bill of Rights* will permit any two residents of the province who are 18 years of age or older and who believe that a contravention a prescribed acts has occurred to apply to the Environmental Commissioner for an investigation by the appropriate Minister. The Minister would be required to investigate unless the application is frivolous or vexatious, the alleged contravention is not serious enough to warrant an investigation, or the alleged offence is not likely to cause harm to the environment. Otherwise, the investigation must proceed and both the people who laid the complaint and the Environmental Commissioner must be notified of the result within a specified period of time. [(467) -- 467. *Environmental Bill of Rights*, 1993, Bill 26, 3rd Session 35th Legislature, Ontario.]

When the responsible agency declines to prosecute an environmental offence, a citizen has the option of proceeding with a private prosecution. Private prosecutions have been a powerful tool in citizens' efforts to protect the environment. Implementing legislation should encourage private prosecutions by awarding citizens who initiate an action one half of any fine that is recovered. [(468) -- 468. Similar provisions exist for private prosecutions under the *Fisheries Act, Penalties, Forfeitures, and Proceeds Regulations*, C.R.C. 1978, c. 827.]

Process Provisions

This section discusses provisions in enabling statutes for ensuring a fair, open and effective decision making process.

Public Participation in Setting Regulations

In Chapter 2 we discussed the need for public involvement in the regulation making process. Meaningful public involvement in regulation making is especially important in the context of a tradeable permit system. Emissions now governed by a permitting regime that allows for public input and an appeal process would be subject instead to generally applicable regulations covering the tradeable permit system. Due to the decreased role for public input in individual cases, there is a greater need for public input into the general regulations.

Public Involvement and Appeal

In Chapter 2 we also discussed the potential for challenges under administrative law based on infringement of the rules of procedural fairness. A statute which lays out a procedure for making and appealing administrative decisions can provide a predictable process for decision making that ensures fairness and integrity in the process. Moreover, if grounded in statute, an administrative decision making process often will be less susceptible to intervention by the courts than an informal process.

A process set out in statute also can ensure a right to public involvement in issues that affect the public; the same arguments in favour of public involvement in regulation making support meaningful public involvement in administrative decisions. In the United States, involvement of environmental non-governmental organizations in the approval of emission reduction credits have revealed questionable assumptions and calculations as well as shortcomings in data which escaped the administrator's attention. [(469) -- 469. Liroff, above at footnote 423, at 101.] Because of the technical issues and the need for understanding the policy concerns in implementing a system of tradeable permits, we recommend that an independent agency with expertise in environmental matters responsible for appeals be responsible for appeals.

We recommend a defined process for public involvement and appeal by both public and other interested parties for:

- approval of emission reduction credits;
- approving trades from sources which do not have continuous emissions monitoring in place;
- administrative penalties;
- initial allocations of emission rights; and
- levels of emissions which must be achieved by the end of transition phases.

We also recommend legislation include privative clauses shielding administrative decisions from appeal.

Legal Remedies for Victims of Trading

The safeguards against concentration of emissions in a particular area should help ensure that hot spots of pollution do not occur as a result of trading. However, a concentration of emissions in particular areas does occur, the public should have legal recourse. The nuisance action is the most important common law remedy for persons who are adversely effected by pollution.

Nuisance is the unreasonable interference with the use of land by its occupier or with the public's use of a public right. [(470) -- 470. Allen Linden, *Canadian Tort Law*, 3d (Toronto: Butterworths, 1982) at 531.] An action in nuisance typically involves a consideration by the court of whether an activity such as polluting is reasonable in the circumstances. The courts will normally consider whether an emission is permitted by law in making this assessment. This consideration may be inappropriate in the case of emission trading because government has less control over the amount of emissions from any source.

We recommend that trading legislation specifically state that the holding of sufficient tradeable permits for an emission is neither a statutory defence to an action against a polluter nor a relevant factor in any such action. We also recommend reforming the law relating to nuisance to relax limits on the standing of the public to bring actions in nuisance. [(471) -- 471. See Ann Hillyer *et al.*, "Recommendations for the Proposed British Columbia Environmental Protection Act" (Vancouver: West Coast Environmental Law Association, June 22, 1993) [unpublished].]

Efficient Administration and Coordination

The efficiency and effectiveness of a tradeable permit system will depend in part on the ability of government to effectively delegate certain tasks and to work out arrangements with other jurisdictions whose cooperation may be necessary in dealing with a problem. Legislation also must clearly specify the relation between a tradeable permit system and other systems of regulation. This part considers these issues.

Interjurisdictional Trading and Equivalency Agreements

Both provincial and federal legislation should provide for equivalency agreements. Agreements should be permitted only with jurisdictions which have

- equivalent statutory provisions for enforcement and monitoring,
- equivalent enforcement practices,
- equivalent emission reduction schedules, and
- equivalent safeguards for emission reduction credits or no provision for emission reduction credits.

Where an equivalency agreement is in place, trading of permits would be permissible across jurisdictional boundaries subject to a requirement to abide by local caps on the maximum concentration of emissions within zones or sub-areas. It is essential that if interjurisdictional trading is allowed, there be an equivalency in the systems. Otherwise there will be a tendency for improperly created permits to flood the market in the jurisdiction with stricter controls and thus subvert environmental protection goals.

Where equivalency agreements are reached between the federal government and the provinces the result would be a partial withdrawal of federal authority in that province. The federal government would need to retain jurisdiction over interprovincial trading. There should be specific authority for regulations to govern interprovincial trading in these situations. The federal

government also will need to monitor interprovincial implementation of tradeable permit systems and resume control of the system where provincial enforcement and administration is weak.

Integrated Regulator and Authority to Delegate Functions

A trading permit system will function most effectively if most administrative functions are under the authority of a single regulatory body. On the other hand, often there will be a need for these administrative functions to be delegated to other departments or even other governmental bodies that are in a unique position to perform certain functions. For instance, if a tradeable permit system were established in the Lower Fraser Valley and mobile sources were included, regulators should be able to delegate the testing of mobile sources to Air Care branches. There are no constitutional impediments to delegating functions from a federal body to a provincial body as long as they are not delegated to the provincial legislature. [(472) -- 472. Peter Hogg, *Constitution Law of Canada*, 2d. (Toronto: Carswell, 1992) at 14-29.]

Any legislation should specifically allow for regulations allowing the delegation of functions to third parties. Where a statute gives a power to delegate, it also should provide that the delegation is subject to directions from the central regulator to ensure that functions are carried out in a coordinated manner and that there is satisfactory quality control. Where two jurisdictions act together in creating a tradeable permit system the statutory authority to delegate should allow delegation to a joint body which would coordinate the system in both jurisdictions.

Relation of Permit Trading Systems and other Environmental Regulations

It is essential that any tradeable permit legislation clarify the application of other legislation and regulations. For instance, the United States sulphur dioxide trading legislation provides that it shall not be construed as affecting the application of other provisions in the *Clean Air Act*, including provisions relating to national ambient air quality standards and state clean air implementation plans. Tradeable allowances only supersede emission limitations previously in effect under that part of the Act. [(473) -- 473. 42 U.S.C.S. §7651 b(f) and (g).]

Legislation should specifically provide that it does not affect any permit restrictions on the creation and discharge of toxic substances. This would help ensure that regulations limiting or prohibiting the production of a specific toxic substance are not overridden by tradeable permits allowing releases of a class of substances to which the specifically regulated toxic substance belongs. [(474) -- 474. See CCME Working Group, above at footnote 393, at 29-30.] For instance, restrictions on emissions of benzene should not be affected by permits to release volatile organic compounds; and permits for nitrous oxides aimed at acid rain reduction should not affect restrictions on emissions of nitrous oxides aimed at avoiding urban smog.

Ability to Levy Pollution Charges and Administrative Fees

Various commentators have underlined the need for the administrators of an emissions trading program to levy appropriate fees, noting that programs which lack resources for proper implementation will fail. [(475) -- 475. See Barakat, above at footnote 410.]. Recovering the full cost of administering the system is essential under the polluter pays principle, and any enabling

statute should give regulators the authority to levy administrative charges for processing transactions as well as the ability to levy discharge fees. Such fees should be statutorily dedicated to administration of the trading program. [(476) -- 476. See Barakat, above at footnote 410.]

Summary

According to some economic theory, tradeable permit systems can place a limit on the total discharges of a particular substance and reduce this limit over time at the lowest possible economic cost. However, the assumptions of economic theory may diverge from reality and, as this Chapter has discussed, there are significant practical problems in actually implementing a system of tradeable permits. This is especially true for sources which do not have accurate discharge data for discharges, and that may have localized effects. Any proposal for tradeable permit systems will have to be carefully examined to ensure that it will help in the reduction of pollution. Designers of tradeable permit systems also will have to consider whether the systems in practice will reduce pollution at a lower cost than command and control strategies. Both draft legislation and draft regulations must be carefully analyzed with public input before any system is adopted.

Tradeable permit systems for environmental protection can vary in complexity from a relatively simple national program to control carbon dioxide emissions through tradeable permits for fossil fuel import and production to a multijurisdictional tradeable permit system for the precursors of ground level ozone. This Chapter discussed general enabling legislation applicable to a wide range of environmental problems.

The following is a summary of concerns which should be addressed in any generally applicable enabling legislation. Some recommendations may not be necessary for enabling legislation aimed at a specific problem.

- Enabling legislation should provide a broad power to establish systems governing a variety of products and emissions. Legislation should allow for systems only applicable in limited areas and should allow regulation of trading between different areas and sub-areas.
- Enabling legislation should require regulations to establish a timetable for reducing permitted discharges in areas where environmental quality objectives have not been met.
- Enabling legislation should allow local area caps to be established for emissions which may have localized effects. These should be set to ensure air quality objectives are met in the local area in a specific time period
- Enabling legislation should specify that tradeable permits are revocable licences.
- Enabling legislation should allow permits to be allocated by a variety of means, taking into consideration basic principles such as fairness and minimization of economic dislocation.
- Allocation rights for polluters who are not in compliance with strict emissions standards should be rapidly reduced to levels achievable with best achievable control technology, and legislation should allow regulators to define these standards by regulation.
- Enabling legislation should require periodic auctions of permits with revenues dedicated to program administration and environmental remediation.
- If emission reduction credits or opting in of sources is permitted, those selling the credits or their permits should bear the onus of proving that an actual reduction has taken place. Credits should only be available for reductions in emissions from the lower of levels achievable with

best available control technology or levels prior to discussion of a tradeable permit system. Allocation rights of opted in sources or attached to emission reduction credits should be automatically phased out with an accelerated phase out available where regulators believe the emissions may be reduced in any event.

- Approval of trades should take place to ensure that trade-offs in the same pollutants will not lead to a degradation of environmental quality. Furthermore, trades should not be approved unless there is demonstrable proof that an emission reduction has occurred.
- Sales of permits which were not purchased by a firm should not be allowed where they are only available because a firm has reduced production levels or a firm has closed.
- Purchasers of tradeable permits should be required to inquire into the validity of their permits, and permits should be revoked if reasonably diligent inquiries were not made and the purchased permits were improperly created.
- A public registry should be established to indicate permit holdings, permits for sale and emission levels of participating firms.
- Participants in a tradeable permit system generally should be required to use continuous emissions monitoring systems. Alternatives to continuous monitoring should only be allowed for small sources. Special requirements such as discounting of trades from sources without continuous monitoring systems or their equivalent should be mandatory.
- Enforcement provisions including substantial automatic minimum fines for permit exceedances and high minimum penalties for other offences are essential. Provision should also be made for citizen initiated investigations and prosecutions.
- Processes for ensuring effective public participation in establishing regulations and making administrative decisions should be enshrined in legislation.
- Tradeable permit legislation should specifically provide that holding a tradeable permits is neither a statutory defence nor a relevant factor in any action against a polluter.
- Legislation should permit delegation of functions to either local or multijurisdictional boards and should permit interjurisdictional trading with jurisdictions that have equivalent legal provisions and administrative practices. If the federal government reaches equivalency agreements with provinces it should maintain a supervisory role and the right to resume control of the system if provincial administration and enforcement are weak.

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