



DAVID LYTTLETON

CRUNCH TIME

HOW FAR ARE WE ALONG THE ROAD TO THE UN CLIMATE CHANGE TALKS IN COPENHAGEN? ASKS
ALINA AVERCHENKOVA

This year is expected to become one of the most significant in the last decade for international climate change policy, if a post-2012 treaty is agreed in December. With only seven months remaining until the meeting in Copenhagen, the real negotiations are only just getting underway. Many critical issues are still only general proposals and lack the level of detail necessary to give the private sector guidance on their investment decisions beyond 2012.

The first session of this year's post-2012 negotiations was held in Bonn on 28 March–8 April. It was the first UN climate change meeting since the decision in Poznan last December to shift to full negotiating mode. Observing the meeting, it was clear that negotiations had indeed started, with the positions of countries on various issues firming up and, for the first time, talk of legal texts.

Under the Kyoto protocol, possible options for a post-2012

agreement were identified. These included: an amendment to the protocol; a new treaty under the UN Framework Convention on Climate Change (UNFCCC); simple decisions to be taken by the conference of the parties (the December meeting); or a combination of these proposals.

The most significant outcome of the talks was the request to prepare for the next sessions in June a draft amendment text under Kyoto on industrialised countries' emissions reduction targets and a legal negotiation text for other issues, such as the use of market-based mechanisms. This will coincide with the issuance of a negotiating text under the UNFCCC, making discussions more concrete and, in turn, refining and narrowing down options. The first proposed amendments were tabled in Bonn and many inputs for the negotiating texts have been put forward in April and early May.

However, the Bonn talks have not given much clarity to

the business community on the format of post-2012 carbon market. Uncertainty remains over which countries will take on emissions targets and at what level, which current market mechanisms will be accepted in the future, and what competition they will face from the new mechanisms that could be created. The list of options for proposed changes to existing carbon market mechanisms had some minor changes and will be up for negotiation again in June, but this time as part of a formal negotiating text.

Among the proposals on the table is a suggestion to limit the use of the carbon credits for compliance post 2012 from the clean development mechanism (CDM) depending on the host country, the technology used for the project, and/or the project size. Other proposals call for the creation of new mechanisms, such as sectoral or policy-based crediting (see *Trading Carbon*, May 2009, pages 30–35). There are also other discussions planned on large-scale reform of the CDM, which aim to make it more efficient, transparent and predictable, thereby making it more attractive to investors and reducing bottlenecks in the project approval pipeline.

One of the main hurdles to a rapid and successful conclusion to a post-2012 agreement is uncertainty over the US position. While US re-engagement under President Barack Obama, and the active stance of the new administration, has brought positive momentum to the negotiations, the statement by the US delegation in Bonn went no further than signalling a willingness to take the lead and support an agreement in Copenhagen.

There is much speculation in international political climate change circles about whether or not the US administration will have to wait until domestic climate change legislation is introduced before it can commit internationally. While some see it as a precondition, others have argued that waiting till the legislation is passed would lock US negotiators into a rigid position that limits their ability to negotiate effectively. The truth probably lies somewhere in-between. The US government would need draft domestic legislation to have, at least, gone through debates in both chambers of Congress, so that major concerns and flexibilities are clear.

Another factor that complicates post-2012 progress is the separation of negotiating tracks between the UNFCCC and the Kyoto protocol. The complexity of the process and the interconnectedness of crunch issues under both tracks is growing – that is, between the improvements to, and the role of, existing mechanisms (such as CDM) and the emissions reduction targets to be adopted post 2012 under the protocol, and the role of new market mechanisms, such as sectoral approaches, proposed under the convention. While officially these tracks are independent, none of the major issues can be agreed in isolation. Whether or not it will be politically possible to merge both tracks will determine the effectiveness of the negotiating process and the legal form of the final outcome.

Given strong public expectation and the commitments made this year at the highest political level to reach a post-2012 agreement, the Copenhagen talks have to deliver. The political uncertainties involved and the complexity of issues make the development of a comprehensive agreement in the remaining few months a great challenge. In informal

political circles, there is increasing talk of reaching a ‘framework’ agreement that defines the major parameters for post 2012, with the details to be finalised at a later date.

The minimum that Copenhagen must deliver are new commitments for industrialised countries, the mitigation actions that developing countries should take and how they will be supported by public and private finance, as well as action on adaptation. If the US is not ready to commit to a definitive reduction target by December, a potential fall-back option would be to agree on emissions reduction ranges for industrialised countries – similar to the conditional pledges made by the EU and Australia – which would need to be finalised later. While not providing full certainty on the demand side, such a signal would at least give some needed confidence to the carbon market and confirm a political commitment to the post-2012 era.

Getting agreement on the crunch issues is likely to require greater authority and flexibility to negotiate than environment ministers usually have at the climate talks. As time gets tight, other high-level processes, in particular ‘G-8 plus 5’, G-20 and the major economies forum, will be important to facilitate an agreement. A deal at the level of heads of state on the key parameters in advance of Copenhagen would go a long way to ensure success. So far, the G-20 has reaffirmed only a commitment to reach an agreement in Copenhagen, but has not touched upon the

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substance of this agreement. As we get closer to December, it is critical that these processes capitalise on their political power to broker a deal by resolving the differences between the main players and take it back to the UN climate change process for final agreement.

The remaining time in which the ‘rules of the game’ are defined for carbon investors is less than four years. With two years required on average for a new CDM project to be developed and registered, it leaves, at best, only two more years of secure carbon credit streams. Policy uncertainties coupled with the economic crisis are slowing already the growth of the CDM pipeline. The inflow of new projects to be validated in 2009 has fallen by around 30 per cent compared with 2008. Banks are reluctant to accept carbon credit contracts as collateral for new project financing and proposing a project for the post-2012 period is often received with even more doubt.

Getting firm signals on the future policy framework in Copenhagen is critical to the carbon market. Delaying key political decisions will lead to lost investment opportunities, further delaying the shift to a low-carbon economy and leaving millions of tonnes of greenhouse gases unabated. ●

Alina Averchenkova is a senior analyst at consultancy First Climate in Zurich
Email: alina.averchenkova@firstclimate.com