SUBMISSION BY THE THIRD WORLD NETWORK

1. Workstream II - Governance and institutional issues

Under the sub-workstream II.4 on Trustee arrangements regarding the relationship between the trustee and implementing institutions, particularly in relation to internationally accepted fiduciary standards, it is critical to ensure that measures are in place in ensuring that there would be no conflict of interest or a likelihood of such a conflict between the trustee and the implementing institutions, including the independent secretariat.

This would include the hiring of persons who have links or are connected to the interim or prospective trustee to provide services to the secretariat or implementing bodies.

2. Workstream 3 Operational modalities

On the methods to mobilize and leverage private sector finance and in creating a variety of instruments to achieve this, a key concern we have is the reliance on carbon financing and trading instruments.

As is noted in the draft background note on the overview of financing modalities, carbon finance is the generic name for revenue streams generated by projects from the sale of GHG emissions reductions or from trading in carbon permits.

1. Premature to discuss new carbon trading mechanisms

The only existing carbon mechanism between developed and developing countries is the CDM. Any discussion on new market mechanisms are still under discussions in the AWGLCA and remain contentious. Hence, it is premature for the Transitional Committee to design new instruments that have yet been agreed to under the AWGLCA and would also amount to a prejudging of the outcome the negotiations.

2. Issue of double counting.

Generating carbon credits in developing countries to offset the mitigation actions of developed countries cannot be regarded as climate financing for developing countries.

3. Derivatives trading, speculation, fraud etc.

(The following is adapted from the Submission by FERN and Friend of the Earth to the UNFCCC under the AWGLCA on market- mechanisms).

Carbon trading happens in two separate, yet linked parts of the market: (1) The first sale of a ‘good’ in a ‘primary market’ and (2) the onward trading of the ‘good’ or a product in a ‘secondary market’, which is often in the form of a derivative, a financial product which derives its value from the underlying good. In the textbook version, the carbon market is usually

described as being dominated by trading in the primary market, where permits or credits are sold only once and then retired by the buyer. It is primarily trade in the primary market which generates finance for the actual project, or mitigation activity. However, trading in the secondary carbon market has grown significantly in recent years, where carbon allowances and increasingly complex derivatives of carbon allowances are traded back and forth many dozen to hundreds of times before they are eventually used by a buyer to cover a greenhouse gas emission. This trading of the same carbon allowance or carbon derivative takes place mainly among financial speculators who profit from speculating on volatility of the price of carbon, not because they are subject to emission reduction targets or have an interest in climate mitigation.

This shift of emphasis of trading to the secondary carbon market has significant consequences for the environmental integrity of any emission reductions mechanisms based on carbon trading.

Carbon traders motivated by speculation will use their trading power to generate, exploit and profit from price volatility, as unpredictable price movements is how speculators profit.

Establishing new trading based on market mechanisms will most likely also increase the predominance of speculative trading in the carbon market. Establishing new trading-based market mechanisms will also increase the risk of 'regulatory arbitrage' and fraudulent trading

4. Land use sector and REDD are particularly ill-suited for a trading-based market mechanism

The assumption is that REDD could attract capital by offering quantified carbon in a commodity form, making forest carbon fungible and therefore tradeable with or without a derivatives style system akin to those used for commodities futures and options. There are many methodological flaws including in poorly defining assets in this regard.

More assessments are needed to understand such market mechanisms and it is too premature to promote these type of instruments without more review and evaluation when there are many uncertainties and risks involved.