Climate Markets & Investment Association

CMIA submission in response to para 85 of COP17 LCA Outcome (http://unfccc.int/files/meetings/durban_nov_2011/decisions/application/pdf/cop17_lcaoutcome.pdf)

Views on a market-based mechanism to enhance the cost-effectiveness of, and promote, mitigation actions

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The Climate Markets & Investors Association (CMIA) welcomes the opportunity to submit our views on the establishment of a market-based mechanism to enhance the cost effectiveness of, and to promote, mitigation actions, bearing in mind different circumstances of developed and developing countries, guided by Decision 1/CP.16 paragraph 80.

This submissions aims at recapturing CMIAs views on the establishment and development of a market mechanism framework that allows for the development of one or more domestic market mechanisms whilst taking into consideration national circumstances.

The key messages from experiences with existing mechanisms are:

- Market-based mechanisms are the most cost effective route to achieve the objective of the Convention;
- The global Carbon market has been highly successful and exceeded the achievements of all other approaches channeling 100 billion Euros per year into emission reductions, mostly from the private sector;
- The private sector needs a demand for emission reductions (targets), fungibility of efforts (tradability) and confidence in the longevity of the UN process-backed market-based approaches in order to invest – a lack of demand, restrictions in trade and loss of confidence in the system is currently limiting further investment;
- It has taken more than a decade to build up the infrastructure of the current system, other approaches need to utilize this infrastructure or face a similarly lengthy learning period;
- The limitations of the current mechanisms need to be addressed through both reform and expansion, and the development of new market-based approaches;
- While new mechanisms develop, it is of paramount importance to maintain continuity of the current market by adopting ambitious, clear and credible long-term commitments.
- The overarching architecture proposed by CMIA provides the common currency which gives the fungibility between the approaches and the global demand (targets).
- Greater capacity of the host country or sector allows the use of market-based mechanisms offering greater flexibility, thus achieving greater economic efficiency.

CMIA supports market-based mechanisms to mitigate greenhouse gas emissions, and believes that such mechanisms are the most cost efficient route to achieving the ultimate objective of the Convention. CMIA believes in a "carbon-constrained world" where global emissions need to be reduced and which requires an ever-greater proportion of those emissions to be covered under some market-based mechanisms placing a price on carbon emissions. Therefore, CMIA supports in principle the ultimate development of a global carbon market as one of the key means to effectively and efficiently incentivise appropriate mitigation actions.

We believe that there is considerable potential for the development of a new mechanism or new mechanisms, which in conjunction with the development of standardised baselines under a reformed CDM can expand the scope of GHG emission management while creating incentives to reduce emissions across a much larger proportion of the global economy. In order to reach the ambitious goals of limiting temperature increases, we need to define procedures and guidance that allow for flexibility in the implementation of mechanisms at the national and regional level that respond and function within national circumstances.

At present, only a very small proportion of the global economy is able to participate in the existing mechanisms of CDM and JI, due to the modalities and procedures of these mechanisms (costs and practicality of implementation, a project based approach, restrictive methodologies, limited approaches to additionality, etc.).

The primary objective of this submission is to reiterate our views of a possible framework that will facilitate provision of additional finance, transfer of technology and capacity building with the aim of enhancing the management and reduction of GHG emissions arising from more economic sectors, until ultimately, the entire global economy is under some form of GHG emission management that puts a price on carbon.

Interactions with existing mechanisms under Kyoto

The coverage of global emissions by the three existing market-based mechanisms under the Kyoto Protocol (Articles 6, 12 and 17) is currently limited, particularly as it refers to the participation of developing countries. Thus, there is significant potential for the expansion of the existing mechanisms as well as the establishment of new mechanisms in order to create incentives to reduce emissions across a much larger proportion of the global economy. Also, the Conference of the Parties (COP) decided to maintain and build upon existing mechanisms in the development of new market-based mechanisms. Therefore, the discussion on a new market-based mechanism or mechanisms does not stand on its own, but both the experience with and ongoing reform of the CDM, including the development of standardised baselines, should be taken into consideration.

CMIA believes that both the ongoing reform of the existing mechanisms under Kyoto and the development of new mechanisms under the UNFCCC are equally important. However, immediate and effective implementation of agreed reforms of the CDM and an ongoing standardisation to operate more efficiently, providing gradual evolution to enable far greater emissions reductions, will have an immediate impact on the potential for global emission reductions, and should therefore be implemented with the greatest urgency.

It has taken nearly a decade to build up the CDM to its current scale, including the infrastructure within the UNFCCC, the support industry such as third party auditors, technical experts and consultants. New mechanisms will be more complex to agree within the UNFCCC forum and require a greater involvement of national authorities and domestic entities. It cannot be expected that these new mechanisms would be operational, at any scale, within a shorter timeframe unless they utilise and build on the existing knowledge and systems to a large degree. Therefore, while new mechanisms develop, it is of paramount importance to maintain continuity of the current market by adopting ambitious, clear and credible long-term commitments.

The continuation and creation of new markets rest solely on governments. A major constraint to the development of any market mechanism is the lack of demand for credits from such mechanism. The current depression in demand is impacting strongly in the prospects for the CDM post 2012. It is unclear when the demand for CDM and new mechanisms will strengthen. Without continuity and clear commitment much of the investment and human capacity will be directed to other activities. This will delay implementation of GHG mitigation actions hence making mitigation and adaptation to climate change more costly.

Private sector involvement in the development of the current mechanisms has been substantial, growing the market to more than 100 billion Euros on an annual basis – a size beyond the possibilities for the public sector to achieve. However, the continued involvement of the private sector depends on demand being created. Similarly, the private sector involvement in the development of a new market-based mechanism or mechanisms is critical in order to be successful. However, this involvement will depend on three key aspects: (1) Demand for the resulting reductions, as without demand, there is no market. (2) Fungibility between reductions achieved through all the different actions that can be part of this mechanisms or mechanisms, as without such fungibility, the scope for involvement is too narrow and there can be no competition between approaches. And (3) confidence in the longevity of the UN process-backed market-based approaches, and thus that value can be derived from it, because without confidence that the UN process is honouring its historic commitments to market-based mechanisms, the private sector would not invest again. If the current mechanisms are not continued to be supported by the process, a decade of building and investing in capacity and infrastructure would be lost, and with it the credibility of the UN process as the basis for market-based approaches.

Architecture

CMIA has put forward an over-arching architecture for the management of GHG emissions in the global economy, with an increasing share of emissions covered overtime, which is elaborated in more detail in our submission of 21 February 2011, which is enclosed with this submission.

This architecture can be seen as the (singular) market-based mechanism defined by COP17, whereas the five levels of mechanisms described within the architecture can be different approaches within this market-based mechanism. The five different levels are proposed to be able to reach as far and wide as possible to cover the greatest share of global greenhouse gas emissions as possible, while being able to differentiate between appropriate measures in different countries and sectors. The overarching architecture provides the common currency which gives the fungibility between the approaches and the global demand.

CMIA agrees fully with the guiding principles (a) to (g) listed in decision 1/CP.16 paragraph 80 for the development of new mechanisms:

(a) Ensuring voluntary participation of Parties, supported by the promotion of fair and equitable access for all Parties;
(b) Complementing other means of support for nationally appropriate mitigation actions by developing country Parties;
(c) Stimulating mitigation across broad segments of the economy;
(d) Safeguarding environmental integrity;
(e) Ensuring a net decrease and/or avoidance of global greenhouse gas emissions;
(f) Assisting developed country Parties to meet part of their mitigation targets, while ensuring that the use of such a mechanism or mechanisms is supplemental to domestic mitigation efforts;
(g) Ensuring good governance and robust market functioning and regulation;

Further to the above CMIA would add important principles that should guide the establishment of any new mechanisms. Parties need to take into account the following:

1) Assist developing countries to manage their carbon assets such that they contribute to both the supply of credits and appropriate sovereign actions whilst avoiding double counting;
2) Be governed in an efficient and transparent manner, under the rule of law and by a full-time professional body (with its members being appointed according to required expertise rather than political appointments);
3) Generate emission reductions units or credits that are internationally fungible with Kyoto units and credits, and which are transferable;
4) Generated emission reductions shall comply with agreed international monitoring, reporting and verification standards;

5) Provide long term certainty and predictability, including for projects which have been implemented under pre-existing mechanisms;
6) Assist developing countries in their contribution to the objective of the Convention; and
7) Benefit from prompt start provisions and which allow for the participation of private entities.

The over-arching architecture for reducing global GHG emissions that CMIA has proposed consists of five levels of market-based mechanisms, building on the existing structure. The different levels have increasing stringency with regards to the level of emission reductions, monitoring and compliance, but also delivering increasing economic efficiency and reduced cost. Therefore, there can be a natural progression and incentive towards more stringent commitments, as will be required to achieve the objective of the Convention. Building on the existing mechanisms, and expanding from the current situation, the five levels of market mechanisms are:

1) Reformed/standardised CDM/JI (standardised baselines as agreed at CMP.6) (under development)
2) Benchmark mechanisms (incorporated in the Reformed/standardised CDM, or new mechanism)
3) Crediting baseline mechanism (new mechanism)
4) Cap and trade (new mechanism, unless as an implementation measure of economy-wide targets, e.g.
EU ETS)
5) Economy-wide targets (e.g. Kyoto targets)

Over time, the proposed architecture could cover an increasing share of global GHG emissions through one of the mechanisms in order to be able to achieve the objective of the Convention.

Participation in one or more of these mechanisms or to adopt, for example, sector caps or an economy-wide cap is at the discretion of host Parties. Nevertheless, it would be envisaged that stringency, both in terms of limiting emissions and monitoring and verification of emissions/reductions, increases from CDM through to economy-wide targets, but that the economic efficiency of the mechanisms also increases. It is essential to appreciate that different mechanisms require diverse levels of technical and institutional capacity. Therefore greater capacity allows greater flexibility thus achieving greater economic efficiency.

While the participation in these mechanisms itself will build capacity in the country or sector to reach the next level through learning by doing as proven in the CDM, dedicated capacity building may further speed up the expansion into the different levels.

However, the development of new mechanisms should not preclude the use of the existing mechanisms, for example CDM projects should not be forced to migrate to a new mechanism – but with lower transaction costs project participants may opt in voluntarily; also care needs to be taken so that projects/sectors are not refused the use of an existing mechanism before a new mechanisms is truly operational as that would jeopardise investments in the low carbon economy.

The CMIA is of the view that minimum eligibility criteria for a sector to participate at a given level is adequate institutional infrastructure to enable:

1) Access to accurate and transparent sectoral data;
2) Determination of a baseline;
3) Proof of additionality;
4) Implementation of accurate and transparent monitoring, reporting and verification for all sector participants; and
5) A national registry.

Under-developed sectors in an economy (i.e. economic sectors lacking basic infrastructure) can probably only participate in the CDM and the reformed CDM once operational. Sectors with access to sufficient verified performance data may engage via the benchmark mechanism (or reformed/standardised CDM), which should reduce the transaction costs compared to project-by-project CDM. Economic sectors with complete reporting are invited to participate in crediting baseline mechanisms with non-binding international targets, which should reduce the costs even further where a suitable baseline is agreed.

CMIA believes that there should be compatibility and coherence between nationally appropriate mitigation actions (NAMAs) and new mechanisms, while avoiding double counting. Thus CMIA believes that participation in these mechanisms could be registered as NAMAs at the discretion of the host parties, for example an emission standard could be introduced for a sector and used as the benchmark in the new mechanism (and vice versa, where a NAMA may be registered as a particular action in one of the mechanisms in order to obtain carbon finance, to pay for the implementation of the NAMA). CMIA believe this should enable more countries to implement such a standard early and/or at more ambitious levels. Therefore, there could be overlap between the 5 emission management levels and NAMAs.

Each of the 5 levels is described in detail in the annex to our previous submission on market-based mechanisms, which is enclosed with this submission.

Conclusions

CMIA believes there is significant scope for a new market-based mechanism or mechanisms in conjunction with the ongoing reform/standardisation and expansion of the existing mechanisms. For this to materialise the current ambition, demand and vision to incentivise private entities to reduce emission will have to be clear, coherent and credible.

New market mechanisms shall be open to all sectors of the economy, contingent technical capacity, institution infrastructure and eligibility to implement market mechanisms.

CMIA foresees that each successive mechanism is more powerful than the previous one, with the ability to attract more finance, deploy more technology, build greater capacity, have greater sustainable development benefits and contain a greater component of host country action.

CDM targets individual technologies in individual installations. A reformed/standardised CDM or a benchmark mechanism that use standardised baselines and may promote multiple technologies in individual installations or multiple projects using the same technology. A crediting baseline mechanism enables the deployment of macroeconomic planning and facilitates financing through the creation of a domestic market with links to international markets for the sale of additional emission reduction units or credits.

Within this architecture, each mechanism helps to build the technical capacity and institutional infrastructure necessary for the next mechanism. Transition through each mechanism may happen over a period of decades, giving ambition, capacity and development time.

Participation in the mechanisms is voluntary: there is no mandatory migration through the mechanisms, but reduced transaction costs should make successive mechanisms more attractive and ambitious. The mechanisms are open to all sectors of the global economy, dependent only upon national circumstances, institutional infrastructure and ability to implement the mechanism.

Once accepted within one mechanism, projects are grandfathered but may opt in if new mechanisms become operational, to ensure continuity and predictability for all stakeholders in these markets.

The ultimate long-term objective is the adoption of ambitious binding caps on sectors or economies, which break the link between economic growth and growth in GHG emissions. Without this it is likely that the ultimate objective of the Convention will not be met.

More detail explanation of the international architecture that CMIA is proposing was submitted to the UNFCCCC in response to the call for input on new market mechanisms (21 February 2011), and are enclosed here and also available at www.cmia.net.

CMIA expects that the COP fulfils its mandate to adopt procedures and modalities for a new mechanism or mechanisms at its eighteenth meeting, and looks forward to discussing these ideas in more detail at the workshop(s) to be organised, including at SB36.

For further information on this submission,

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About the Climate Markets and Investment Association

The Climate Markets & Investment Association (CMIA) is an international trade association representing firms that finance, invest in, and provide enabling support to activities that reduce emissions. CMIA's membership account for 75 per cent of the global carbon market .

Composed of businesses at the cutting edge of the services sector that work to reduce emissions through the market mechanisms of the United Nations Framework Convention on Climate Change (UNFCCC) and the Kyoto Protocol, CMIA was created to ensure that the progressive business voice is heard, and to promote market friendly climate change policy. Our members provide highly-skilled jobs and add value to the economy through services to, and capital injections into, the growing global carbon market.

CMIA's membership comprises over 60 companies including financial institutions, asset managers, investment and carbon funds, project developers, lawyers, accountants, verifiers, emissions brokers, and IT firms.

www.cmia.net