

K2S The Kyoto2 Support Group

October 2009

Comments on *Global carbon trading: a framework for reducing emissions*^{1,2}

Although the we are trying to raise the profile of the Kyoto2 proposals,³ our primary concern is to see a good system in place, and soon, drawing on good ideas wherever they may come from.

There is substantial common ground between what is proposed in this report (which we will refer to as “GCT”) and the Kyoto2 proposals (which we will refer to as “K2”) in that both sets of proposals envisage global carbon trading as a central plank in any new system, and both recognise that regulations and other policy tools will be needed to complement and support the objectives of carbon trading. That said, we feel that the balance of advantage lies with K2, for reasons which we will try to make clear.

Our main concerns about GCT are three-fold:

- It is a relatively complex system and that complexity can lead to problems in international negotiations, in administration, in costs, in opportunities for fraud,⁴ in fairness, and in the speed with which emissions can be brought down (next).
- In view of the urgency of the problem of bringing down emissions of greenhouse gases, we believe that what is proposed in GCT will be far too slow.
- Limitations on the scope of the GCT report (eg the exclusion of “leakage”, and the raising of revenues via auctions) seem to have led to missed opportunities.

These and more specific points are discussed in what follows.

¹ *Global Carbon Trading* is a report by Mark Lazarowicz MP for the UK government (Department of Energy and Climate Change), published by The Stationery Office (UK), and available online via http://www.decc.gov.uk/en/content/cms/what_we_do/change_energy/tackling_clima/emissions/emissions.aspx.

² An electronic copy of these comments (PDF, 46 KB) may be downloaded from http://www.mng.org.uk/gh/private/mark_lazarowicz_comments1.pdf.

³ See “Kyoto2 in brief”, http://www.mng.org.uk/gh/resources/kyoto2_in_brief3.pdf (PDF, 113 KB); www.kyoto2.org; and *Kyoto2: How to Manage the Global Greenhouse*, Oliver Tickell, Zed Books, 2008.

⁴ See, for example, “UK police join hunt for £1bn carbon credit fraudsters,” *The Observer*, 2009-10-04, <http://www.guardian.co.uk/uk/2009/oct/04/police-hunt-carbon-trading-fraudsters>.

Sovereignty

It appears that much of the relative complexity of GCT stems from certain assumptions related to “sovereignty”:

One option for expanding carbon trading would be to set up a single global emissions trading system with centralised governance. However, this approach has a number of disadvantages. It would reduce sovereignty over domestic policies and would be challenging to negotiate multilaterally. (p 28).

We accept that nation states have an important role to play, and that the principle of “subsidiarity” should be applied wherever it is appropriate. But putting national sovereignty centre-stage can create its own problems, described below.

K2 is based on the view that, because climate change is a global problem, a global perspective must be central to any solution (in much the same way that global standards and global systems are needed for the effective operation of international telephony, aviation and shipping, and the internet). But it also envisages that other initiatives may run in parallel, at regional, national and lower levels, depending on local needs and local conditions. There is plenty of scope in K2 for the exercise of national initiatives and national sovereignty, to complement and reinforce global mechanisms.

K2 recognises that it may not be possible to achieve a global system in one step and provides for the possibility that K2 principles may be applied in particular regions, pending a global solution. But we believe that it will be simpler, quicker and easier to achieve a global trading system by aiming for it directly, rather than trying to create such a system indirectly as envisaged in GCT (more below).

National targets for emissions

As regards the difficulty or otherwise of international negotiations (referred to in the quote above), *we believe that a focus on national targets for emissions is one of the main obstacles to progress.* It encourages each country to concentrate on the perceived “burdens” of cutting emissions and to try to minimise its own burden. By eliminating national targets, K2 reduces the temptation to indulge this kind of beggar-thy-neighbour approach to negotiations. And by creating a large fund to be spent on mitigation and adaptation, it shifts the focus on to how to share the benefits and opportunities of moving to a low-carbon economy.

National targets for emissions are more complex than they may seem. As Oliver Tickell has written: “If a product is made in China, by a company based in Singapore, using Australian coal, for a company in the UK, and exported to end users in the US, then which country should ‘own’ the emissions?”⁵ With national targets for emissions, trying to account for the fossil carbon that is embodied in traded products is likely to become unmanageable. But failing to account for that carbon will lead to anomalies and unfairness. A global cap on emissions, as is proposed in K2, sidesteps all those problems.

⁵ “Science says we need a 100% cut in carbon. Here’s how to achieve it,” Oliver Tickell, *Green Futures*, October 2008, p. 17.

Creating a global trading system from a range of national and regional systems, with “downstream” controls on emissions (see next), is likely to be very complex:

*Realising a long-term framework of global carbon trading will require a **period of transition and a roadmap** for: 1) expanding national targets with strengthened monitoring, reporting and verification; 2) developing a linked network of emissions trading systems (ETSs); 3) participation of developing countries through intermediary mechanisms; and 4) strong and effective international institutions. In the short and medium term, capacity building will also be needed to ensure that developing countries are well-prepared for participation. (p. ix, emphasis in the original)*

What is proposed in K2 is altogether simpler, and is likely to be quicker and easier to put in place.

“Upstream” versus “downstream” controls

A major advantage of K2 is that it applies controls over greenhouse gases “upstream”, as close as possible to their origins. In the case of oil, gas and coal, this would be close to where they are extracted from the ground. Because there are vastly fewer sources of fossil carbon than there are emitters of CO₂, this greatly simplifies administration, with corresponding reductions in costs, and it greatly reduces the opportunities for fraud.

Raising funds to pay for mitigation and adaptation

The way in which auctions may be used to raise funds is simply outside the scope of GCT (p. vii). But in K2, the sale of Permits to pollute would be used to create a large and continually-replenished ‘Climate Change Fund’ of about US\$1 trillion every year. This is a major strength of K2:

- It is a remarkably simple mechanism for raising the funds needed to pay for mitigation and adaptation.
- To our knowledge, it is the only proposal to date that would raise funds on the scale that is required.
- From the perspective of national governments, it has the attraction that the funds would be raised directly from the users of fossil fuels, without any call on national treasuries or taxpayers.
- In itself, it has a considerable measure of fairness because *per capita* contributions to the fund would be in proportion to *per capita* pollution of the atmosphere (more about fairness below).

In GCT:

*Recent estimates suggest that around **\$100 billion a year will be needed by 2020**. This will require strong and urgent international cooperation, and a combination of private and public finance. The carbon market will provide a significant proportion of finance by 2020. International public finance will also need to play a substantial role, and more advanced developing countries will be expected to fund some of their activities themselves. (p. viii, emphasis in the original)*

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We feel that this is too little, too late, and too complex. K2 would raise more money, more quickly, and more simply.

The need for speed

GCT envisages that a global system for carbon trading would evolve via the progressive linking of national and regional ETSs. But:

A notice period of several years should be provided prior to linking ETSs to allow time to negotiate common standards, give emitters and investors time to prepare, and smooth the convergence of prices in different systems. (p. xi).

Given those kinds of complexities, we believe that it is extraordinarily over-optimistic to suppose that a global system could be created within “the next five to ten years” (p. iv). It would be altogether quicker and simpler to aim directly for a global system, as proposed in K2.

*Current evidence suggests that to avoid the worst impacts of climate change, we should aim to **limit the global average temperature rise to 2°C**. This requires the international community to undertake immediate and substantial reductions in global greenhouse gas emissions in all sectors in line with the latest science. (pp. vii-viii, emphasis in the original)*

We simply don't have the luxury of waiting decades to achieve an effective global system for controlling emissions of greenhouse gases.

Dual-level carbon trading

GCT proposes a system of dual-level carbon trading, at emitter level and government level. The main reason seems to be because of the difficulties of controlling all emissions at emitter level and to “ensure governments take responsibility for limiting emissions in line with the latest science.” (p. iv).

With K2, since emissions are controlled upstream and there are no national targets, none of this complexity is needed.

Leakage

Although the problem of “leakage” of industries between countries is outside the scope of the GCT report, it is relevant to point out that, with a single global cap on emissions, as proposed in K2, the problem of leakage would disappear.

International aviation and shipping

The assumption that there will be national targets for emissions creates the problem of what to do about international aviation and shipping.

GCT proposes that “International aviation and shipping sectors should each have a dedicated transnational system to cap emissions.” (p. x).

In K2, none of that complexity is needed: the problem simply disappears.

Sectoral level trading and crediting

In GCT, a system of “sectoral trading” and “sectoral crediting” is proposed for developing countries, apparently as a successor to the Clean Development Mechanism.

In K2, none of this complexity is needed.

A reformed Clean Development Mechanism?

Developing countries not yet in a position to participate in government-level sectoral mechanisms should be assisted to take part in a reformed CDM. This should use benchmarking and a more rules-based approach where possible to increase the environmental integrity of CDM credits and minimise investor uncertainty. (p. xii).

K2 does recognise that there are potential benefits in retaining a reformed version of CDM (*Kyoto2: How to Manage the Global Greenhouse*, Chapter 6). But this is not an essential part of the proposals.

Dealing with loose targets of the past

In GCT:

*During the transition, an important challenge will be to address excessive surpluses of emissions allowances generated through loose targets under the first commitment period of Kyoto. Developed countries should commit to **cancel a substantial proportion of surplus allowances**. Other measures, such as **Green Investment Schemes**, should be considered, but only if emissions reductions are systematically measured and verified. (p. x, emphasis in the original)*

In K2, none of this complexity is needed. Countries that have allowed their emissions to rise will find that they are paying more into the Climate Change Fund than countries that have kept their emissions low.

What to do about diffuse emissions from such sources as deforestation, agriculture, and soils

With some kinds of emissions, there are problems:

Emissions from agriculture are problematic because of high levels of uncertainty in measuring emissions. (p. 36)

The uncertainties around methane production rates in the waste sector need to be reduced. (p. 36)

Accounting for carbon stock changes [in forestry] is currently problematic, given the challenge of distinguishing between anthropogenic and non-anthropogenic (particularly natural sink) effects. (p. 36)

and so on.

Despite these kinds of problems, GCT proposes that all kinds of emissions should fit into the Procrustean bed of national targets:

In future, national targets will need to be more stringent and will have to cover a broad range of sectors in order to meet global emissions targets. All domestic sectors – power supply, industry, domestic transport, waste, buildings, agriculture and forestry – should be included under national targets. (p. 104).

Because there would be similar problems in trying to control these kinds of emissions via the sale of Permits, K2 adopts a different approach:

As for diffuse land-based emissions from deforestation, agriculture and soils, these are excluded from the market mechanism owing mainly to the difficulty of measuring and monitoring them. (Kyoto2: How to Manage the Global Greenhouse, pp. 11-12).

In brief, K2 proposes that those kinds of diffuse and hard-to-measure emissions would be controlled by a combination of regulations, in the manner of the Montreal protocol, and funding for mitigation measures via the Climate Change Fund. We believe that this approach makes good sense.

Fairness, transparency, and vested interests

As mentioned above, the sale of Permits under K2 is broadly fair because, to a large extent, the money would come from the polluters. But this takes no account of historical responsibilities or pollution from sources not covered by the Permit system.

Any residual concerns about fairness may be resolved via the distribution of moneys from the Climate Change Fund. This is very much a matter for negotiation.

In that connection, the essential simplicity and transparency of the arrangements is an advantage for poorer countries that may not have the luxury of going into negotiations with the backing of large teams of lawyers and other ‘experts’. For much the same reasons, there is less scope for powerful vested interests to influence the outcome of negotiations.

By contrast, the relative complexity of GCT creates many opportunities for the rich and powerful to skew negotiations in their favour.

Conclusion

We very much endorse the idea that a global system for carbon trading should be a central plank in any system for controlling worldwide emissions of greenhouse gases, and we agree that regulations and other policy tools will also be needed. But we believe that, on a whole range of issues detailed above, the balance of advantage lies with the Kyoto2 proposals.