Carbon Markets & Investors Association™

Investors highlight options to enable the EC to lead climate change mitigation efforts

27 May 2010

The Carbon Markets and Investors Association (CMIA) welcomes the communication on 26 May 2010 from the European Commission (EC) and its proposed push for an accelerated greening of Europe's economy. Miles Austin, Director of the CMIA said "Within the proposals there is much to commend and we are pleased to see Europe positioning itself at the centre of efforts to combat climate change on the road to Cancun. There are, however, some points which should be improved to allow the markets to deliver larger amounts of private sector capital towards emissions reductions and at lower cost to European nations and their citizens."

Least Developed Countries (LDCs)

CMIA supports the Commission's desire, as stated in the communications, to help LDCs gain fuller access to the Clean Development Mechanism (CDM). It particularly support its clear definition of LDCs for the purpose of the EU ETS, and specification of project types that would be viewed favorably.

It notes however that there is still much work to be done on institutional capacity building not only within the realm of the CDM but also within the wider space of institutional reform and financial capacity building, which is not incentivised by the outlined proposals.

Further, with regard to project types specified, it is insufficient to encourage investment that has no regulatory basis. Austin says, "CMIA strongly urges the Commission to use the comitology process to set out a positive list of project types, as the communication does not remove the risk of projects in LDCs falling foul of the decisions of the comitology committee on offset standards (CCOS). There needs to be a clear process, with a set time frame, under which a positive list of project will be established."

Using lessons learnt from the CDM, CMIA urges the Commission and Member States to take the following additional steps to ensure the future expansion of the CDM in LDCs:

1. Specify clear and reasonable Terms of Reference (TORs) for the CCOS which define
    a. How often the committee will meet
    b. How long its decisions will stand for
    c. How often decisions can be revisited
    d. The establishment of an appeals process for actors that are negatively impacted by the decisions of the committee
2. At its first meeting, the CCOS should establish the principle of a safe list for project types that will remain unaffected by CCOS decisions for a given time period of time. We would propose ten years after first issuance.
3. Place all project types in all LDCs on the suggested safe list.

Discounting

The communication mentions the discounting of particular project types. CMIA warns that discounting will lead to increased costs and decreased investment and will be detrimental to the smooth functioning of the market overall for the following reasons:

1. It negates one of the basic principles of the carbon market, namely that one ton abated is equivalent to any other ton abated.
2. It introduces multipliers which will result in a high degree of fragmentation, and in turn decrease liquidity in the secondary certified emission reductions (CERs) market, which is already suffering from limited liquidity. Market liquidity is important as it helps to lower costs for participants but also for consumers and taxpayers.
3. It increases uncertainty over the value of projects which are currently being originated, leaving investors uncertain about the value of their investments post 2012. Greater uncertainty means reduced appetite for investment.
4. The decisions from the CCOS only apply to the EU ETS, so far from being a Europe wide measure, discounting will simply drive certain types of CERs toward government markets

5. As has been demonstrated recently, whilst all Member States will act within the letter of the EU ETS, some may not abide by its spirit. Discounting creates a clear risk for instance, of a Member State using two CERs for national compliance when it was handed these by an entity in exchange for one EUA. This will essentially be free riding and risking another round of negative publicity about loopholes in EC regulations. CMIA recognises that the Commission would like to avoid such situations and therefore urges it to put in place the appropriate regulations.
6. Very important questions are left unaddressed: will the number of multipliers vary through time, will their value be fixed or change?

Miles Austin reiterates "The multiplier proposal is increasing uncertainty and complexity at a time when investment in abatement is urgently needed but already held back by lack of clarity regarding the international process post 2012. With private sector expected to finance up to 85% of the cost of climate change mitigation, government must provide clear policy signals to allow the markets to deliver larger amounts of private sector capital towards emissions reductions and at lower cost to European nations and their citizens."

Sectoral Credits

In its communication the EC proposes additional restrictions on compliance entities within the EU ETS by demanding that they use "sectoral credits", i.e. credits that do not exist from a mechanism that does not exist. In our view this is an unworkable proposal.

When the EU ETS introduced CERs/ERUs as a compliance tools, CDM and JI were already established. Reserving a share of the offset cap for credits from a mechanism that has a very limited chance to exist in 2013 in effect means reducing the EU use of flexible mechanisms yet again, at a time when investment flows in the developing world are urgently needed.

It is not clear from the communication whether this applies only in the case of a 30% reduction target or also in the case of a 20% reduction target. In the case where the proposal is adopted under the current commitment of a 20% reduction, it entails another retroactive change to current rules, and therefore poses a considerable risk for investors and compliance buyers.

Austin says, "Using the offset limit in the EU ETS as leverage to get sectoral approaches off the ground is a blunt approach at best. Working with the private sector in the discussion of what these sectors might look like would be far more productive and has failed to happen to any meaningful degree to date."

ENDS

Notes to Editors:

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About the CMIA:

The Carbon Markets & Investors Association (CMIA) is an international trade association representing close to 50 companies that finance, invest in, and provide enabling support to activities that reduce emissions. CMIA's membership accounts for an estimated 75 per cent of the global carbon market, valued at USD 130 billion in 2009. Solely representing organizations that provide services to and invest in the environmental sector, membership does not include any entities with compliance obligations under cap-and-trade schemes. This results in a unique advocacy platform with emphasis on the environmental integrity of market mechanisms and climate change policies.