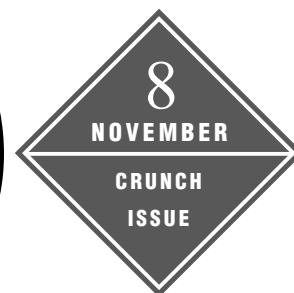


# ECO



## The Danger of Banking Sinks Credits

**All Parties have an interest in making sure sinks credits are not banked into future commitment periods. Making sure of this means designing watertight rules.**

With compliance unexpectedly settled and Ministers rolling into action, the sexily-labelled Article 7.4 looks like the big arena for COP7's showdown.

Article 7.4 governs issues such as the potential to substitute AAUs, CERs, ERUs and the all-new RMUs for each other (referred to as "fungibility"), as well as the freedom to carry such units over to future commitment periods, known as "banking".

The talks seem stalled on this core article, with familiar positions being taken by the Umbrella Group and G77 & China, with the EU hovering nervously in between.

All the 7.4 issues raise serious questions, but in this situation we have to sort out where the biggest dangers lie.

Banking of sinks credits into future commitment periods would be genuinely damaging. It would turn the hugely generous Annex Z allowances and other (uncapped) sinks provisions from a first commitment period fix (as was clearly intended in Bonn) into a lasting distortion of the Kyoto targets.

It would severely limit the CDM. Why invest in CDM projects when a country can simply grant itself bankable sinks credits including those from business as usual?

It would make it more difficult to bring in new Parties with targets in the second commitment period. New Parties – including the US were it persuaded to return to the fold – would be negotiating new targets on a very uneven

playing field, as the incumbent Annex 1 countries would be busy stashing away banked sinks credits. Hardly the kind of scenario to encourage these countries to get involved in an agreement rigged in favour of others.

These are very serious problems. They remove incentives for real emission reductions, severely limiting the CDM, and make life harder for other countries to take on targets in the future. Therefore, they require a watertight solution.

The G77 & China and the EU together are groping towards such a solution. The G77's suggestion of the new RMU unit will help identify the issue, but preventing banking of these units means more than saying "no".

A specific amendment is needed to prevent RMUs being traded for bankable AAUs or the structure will be meaningless.

The Umbrella Group should actually welcome such an amendment for the reasons described above.

It should go along with it. For the G77 & China, the advantages of preventing banking of sinks are clear.

The EU needs to support this stance if its environmental credentials are to remain intact. Let's focus on the issue that really gets us better results for the climate, for the integrity of the Protocol and for the interests of developing countries.

No negotiator should hold the Protocol to ransom when we are so close to wrapping up the deal from Bonn.

Parties must agree on clear rules that genuinely prevent banking of sinks credits into the second commitment period.

## Eligibility criteria a vital incentive

The mechanisms' eligibility criteria provide a built-in incentive for Parties to adopt the compliance regime and report accurately on their emissions and removals. Both are important if the Protocol is to operate credibly. They are especially essential for the carbon market to operate with environmental integrity and economic efficiency.

Unless Parties are bound by the procedures and mechanisms on compliance, the private sector will have no confidence in the Kyoto mechanisms. If there is no binding compliance regime, the effective default price for carbon is zero. For example, when faced with the choice between buying allowances or credits to meet targets or going out of compliance, a Party will inevitably choose the non-compliance option. A weak compliance regime would undermine the market.

This is widely recognised as a general phenomenon by governments in their domestic schemes (US Acid Rain programme, UK ETS, EU ET Directive, etc.), and by current and potential private sector participants from all branches of business and industry.

The importance of accurate and consistent reporting [eligibility criteria (f) and (g)] is also recognised by governments, businesses and NGOs. If Parties are not required to report on both sources and sinks on the same basis, then buyers, sellers, brokers and investors will face considerable uncertainty. This will raise transaction costs and the risk that units, subsequently found not to represent real emission reductions or removals, will be transferred or laundered. Equally important, if Parties are not required to report accurately on their sinks ac-

*—continued back page, column 2*

## Pandora's box

The infamous Appendix Z fixed the ceilings on capped 3.4 activities for Annex 1 countries. Playing with these numbers in favour of certain countries' was probably the price of agreement in Bonn. Having received by far the largest allotment in Appendix Z (17.63) MtC, Russia continues to argue it should receive 33MtC.

Mind you, the basic approach to calculating sinks in Russia involves estimating the mass of a tree and multiplying by the number of trees in the entire country. Not exactly the kind of sound science that allows a country to argue with much authority. Furthermore, Russia is awash in hot air and cannot even plead for the sort of unfounded mercy that Japan and Canada received in their extravagant sinks allotments.

Opening the Appendix for woolly "fixes" will lead down the slippery slope of claims from all and sundry, potentially blowing up the talks. Face it: the whole thing is dodgy – don't you wish you'd kept it simple and stuck to emissions reductions? So, approve a package and wait to follow the proper procedures to revisit the Annex Z numbers in due course.

## By road to Jo'burg

An overland travel itinerary to the World Summit on Sustainable Development (WSSD) in Johannesburg next year is currently being prepared by organisers of the climate trains to Kyoto and Marrakesh.

The aim is to offer an alternative non-air travel option to WSSD, with minimal climate impact.

Meetings will be arranged enroute to discuss environmental and development issues within local contexts, with the objective of taking messages from these dialogues to the WSSD.

A number of routes are currently under consideration. Project outputs and final routing will depend on participation and support.

Organisers claim the idea is already drawing substantial media, business and agency interest. Obtain details and keep track of progress on [www.chooseclimate.org/joburgcaravan](http://www.chooseclimate.org/joburgcaravan)

## CAN speaks

Representatives of the Climate Action Network (CAN) will make statements during the plenary meeting today. They will present a South and North perspective respectively.

The full texts of both presentations are posted on [www.climateactionnetwork.org](http://www.climateactionnetwork.org)

– *Eligibility criteria, from front page* activities before entering the market, it is highly possible they will be laundered through JI before they have been accurately verified.

The compromise text proposed in the negotiating group will solve this problem if, and only if, Parties are obliged to report all their sinks activities annually, as per the first part of paragraph 5 of the text on Article 7.1. The proposal by Canada (contained in square brackets in the second half of the same paragraph) must be deleted.

The other eligibility requirements – all just as important – have already been agreed upon and therefore are unlikely to be changed.

### Commitment period reserve

It is essential that it be mandatory for each Party to set aside at least 90 per cent of its assigned amount. Though imperfect, the commitment period reserve is the only solution to the problem of overselling units; otherwise parties could sell their allowances – including those needed to cover their emissions during the commitment period – and then either choose to leave the Protocol or not to abide by compliance rules. This would flood the market with credits not backed by real reductions.

This reserve must not be transferred out of the Party's registry until it has been demonstrated that it has reduced its emissions sufficiently to free them up (not before the end of the true-up period). The transaction log must flag any transfer if a Party does not maintain its CPR at the required level or causes the CPR to drop below this level. Such transfers could be blocked, as per current Paragraph 8 of the Annex to the Decision on Emissions Trading. This paragraph must be retained as it is now in the Chair's text.

## Abraham

Abraham was underwhelmed to find yet another plate of olives waiting for him at the Carbon Trust reception. A sad, cold meal of briny pitted fruit can hardly be meant to sustain a man through voluminous platitudes, especially when the wine is long gone. Oh, how the catering standards have fallen, now that the Protocol is out of the glare of the kleig lights. Fortunately the day's chit-chat was meaty, as Mr. Perellman was overheard thanking the US delegation for their "hard work for us over the past two weeks". Given their near silence until now, is it possible the bitter fruits of their labours have yet to ripen?

## Norway breaks ranks

On Wednesday, an article in Norwegian newspaper Dagsavisen quoted new environmental minister, Mr Borge Brende, saying he would speak in favour of a strong compliance regime in Marrakesh.

Another Norwegian newspaper, Dagbladet, on the same day quoted Mr Brende saying, "The US climate policy is a sorry chapter. I do not like the actions of the Bush administration",

Mr Brende followed through with his comments to the newspapers at COP7. During his speech at the plenary session yesterday, he said: "Those who break the rules must face legally binding, and not just voluntary, consequences".

This is a new development in Umbrella Group-member Norway's position during the final countdown to COP7. Prior to this, it had not spoken out against the proposal presented by Japan, Russia, Australia and Canada to remove compliance as an eligibility criteria.

## "Fossil of the Day" Award

Saudi Arabia was voted winner of the award for ensuring science played no part in the climate negotiations. When Parties agreed at the SBSTA meeting on Tuesday that a workshop will be held to discuss implications of the IPCC Third Assessment Report for future negotiations, Saudi Arabia insisted on bracketing uncontroversial text regarding the report. It insisted on removing any reference to the adoption of a decision at COP8 following the workshop.

The US earned second place for trying to delete references to climate change, the Kyoto Protocol and the Bonn Agreement from appearing in the Marrakesh Declaration as this would be brought forward to WSSD. Working behind the scenes, the US was trying to dilute the language to ensure it would not be isolated next September in Johannesburg.

## THANKS

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