THE MONTAGUES, THE CAPULETS AND THE CDM

What's in a name? That which the Kyoto Protocol calls the CDM would smell as sweet in the Paris agreement, writes Karl Upston-Hooper

Since its inception in 1997, in the form of Article 12 of the Kyoto Protocol, the story of the Clean Development Mechanism (CDM) has played out on the global stage, has involved a cast of thousands and has seen more highs and lows than a Shakespearean tragedy. Initial concerns about registration delays, the linking of the International Transaction Log with the EU's registry and categorisation of certified emission reductions (CERs) gave way to an explosion of participants and interest, double-digit prices and new carbon funds – all supported by a vibrant climate ecosystem of service providers.

Given the promise of the opening acts, the decline in the use of the CDM over the last few years has been surprising to many. However, the lessons learned and experience gained should endure: many tools, processes and approaches developed under the CDM can be used as a basis for facilitating investment into emissions reducing projects in a post-Paris world.

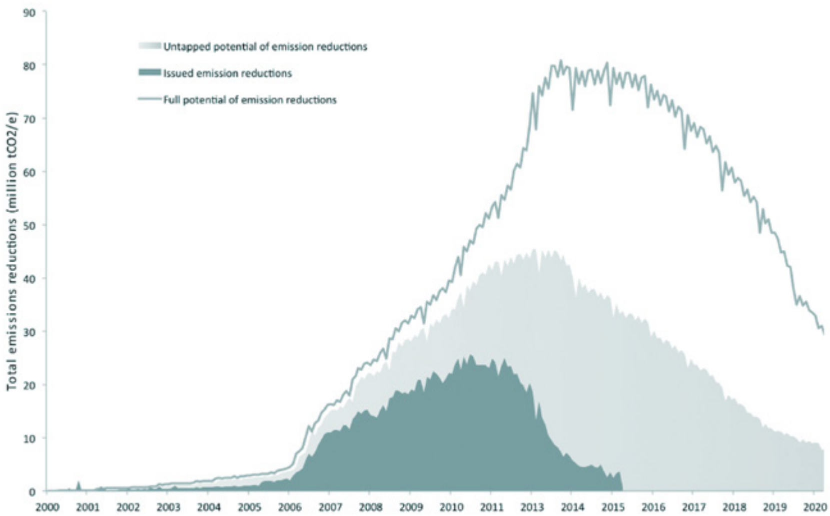
The passion that this innovative mechanism generated should be recalled. The CDM, through the use of price discovery by the market, enabled private investment into emission reduction projects on a scale that dwarfed existing public finance measures. By the end of the first Kyoto commitment period in 2012, 7,338 projects had been registered, a plethora of methodologies developed, more than $100 billion had been invested in emission reduction projects[1], technologies transferred, institutional capacity built in 110 developing countries and, perhaps most importantly, a emission reduction pipeline of 950 million tonnes of CO_2e per annum created.

Like many of Shakespeare's plays, the CDM has always meant different things to different people. For some it was aspirational, a tool to help developing countries skip to a low-carbon pathway. For others, it has always been about cost efficiency, the ability to discover the lowest cost abatement opportunities, maximising the bang for the buck and encouraging ambition in those with historic responsibilities. For many practitioners, the CDM was also an institution, a forum for developing, testing and contesting the nuts and bolts of project design and measurement, reporting and verification (MRV) – and accordingly has evolved into a global language that forms the basis of other policy tools such as Japan's Joint Crediting Mechanism (JCM) or the Gold Standard. Regardless of which side of the debate about issues like additionality or appeals you were on, a Montague or a Capulet, all would agree that the Paris Agreement must address the role of market mechanisms, and by implication the future of the CDM.

Just as Baz Luhrmann placed Romeo + Juliet in the MTV generation of Verona Beach, the modern context for the Paris negotiations is a world away from the Brazilian proposal for a Clean Development Fund that originally lead to the creation of the CDM. There are now many other carbon market travellers on the Road to Paris: the emissions trading systems of the EU, California and Québec, the Regional Greenhouse Gas Initiative, New Zealand, Korea, China, Kazakhstan; the innovative market systems in Mexico, Thailand and South Africa; the JCM; nascent programmes in Russia, Alberta and Chile, plus China's planned national ETS from 2017; and strong carbon taxes in much of Scandinavia. However, given the uncertain role that markets will play, based on the Intended Nationally Determined Contributions (INDCs) published to date, and the state of the negotiating text of the Ad Hoc Working Group on the Durban Platform (ADP), the Rime of the Ancient Mariner comes to mind: "Water, water, everywhere, but not a drop to drink".

Most observers are confident that, by the early hours of 12 December, there will be a Paris Agreement – but the $100 billion question is what role will markets be proscribed within this bottom-up world of nationally determined contributions (NDCs). Will meat finally be put on the bones of the discussions of future market mechanisms, or will the Brazilian proposal for CDM-plus be the new agenda item for the 2016 negotiations? Conceptually, delegates will have three (overlapping) options:

a. Continuing the use of carbon markets, although not necessarily in the form of the CDM, as a mechanism for achieving commitments/contributions made in Paris;
b. Relegating carbon markets to an implementation tool for climate finance initiatives; and/or
c. Acknowledge and encourage carbon pricing as a domestic instrument, albeit with international co-operation if possible.



Source: UNFCCC

As with the Montagues and the Capulets, these discussions occur in an environment lacking in trust and torn by disagreement over historic responsibilities and current realities. The CDM has some lessons in, if not overcoming, then navigating around these historic differences. Through standardising approaches to emissions monitoring and verification, providing clear process and procedures which can be used as a basis to disburse investment, and stimulating a network of co-operation and engagement between private sector actors, with government assistance, to put cleaner infrastructure on the ground. Although the CDM will not be the centrepiece of Paris Agreement, much of its institutional principles remain relevant. Price discovery through a market mechanism is efficient when properly regulated. There needs to be environmental integrity so that “a tonne is a tonne is a tonne”, as UNFCCC Executive Secretary Christiana Figueres – a former member of the CDM Executive Board – has taught us. Subsidiarity is common sense and good governance, but needs to take place within the confines of an international agreement. Trading works best where there is a common currency, previously the CER, but perhaps now a new International Compliance Unit.

Prior to the Paris Agreement becoming effective in 2020, the CDM can provide a platform for nations to continue to support emissions reduction projects and much of the institutional infrastructure, from host country authorities to parts of the UNFCCC secretariat, can be used to assist in operationalising INDCs. Already, the World Bank’s Pilot Auction Facility and the purchase programmes of the Swedish Energy Agency, the Nordic Environmental Finance Corporation and others are aiming to support the ecosystem that has evolved around the CDM. Although these measures provide some level of respite for disillusioned market participants and give confidence that a market mechanisms will persist, they would need to be scaled significantly to restore the confidence of the private sector: that is, investors need to see more demand for the end result (CER or another unit) before coming back. The Green Climate Fund implementing a results-based financing initiative, built around the CDM, would be one such mechanism to achieve a degree of scale.

During the course of the two weeks of negotiations in Paris, there will be more hostages, duels and victims (loss and damage, REDD+, response measures, CDM reforms, the Framework for Various Approaches, New Market Mechanism, IP rights for technology, voting rights, to name but a few candidates) than Shakespeare managed in Romeo and Juliet – and perhaps the CDM itself is one of them. If this is the case, then hopefully the lessons, principles, capacity and relationships that built the CDM are also not lost and find a place in the Paris Agreement, otherwise we are left with Juliet’s immortal words: *Parting is such sweet sorrow that I’ll say good night until tonight becomes tomorrow.*

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(1) According to the CDM Executive Board’s 2014 status report, at least $138 billion – “probably significantly more” – had been invested in the CDM over the nine years from 2005-14.