



From Copenhagen to Cancun

**a two track approach: a binding legal agreement
and a climate investment framework**

.

Allan Larsson

*Global Utmaning is an independent Swedish think-tank.
We are a qualified network from business, politics and academia focussing on the challenges
posed by a new world order regarding economics, environment and democracy.*

**From Copenhagen to Cancun
a two track approach: a binding legal agreement
and a climate investment framework**

Published by Global Utmaning
Stockholm, February 2010

Sveavägen 66 • 111 34 Stockholm • Sweden • www.globalutmaning.se

Executive Summary

This paper on the EU climate strategy, prepared by Global Utmaning, is a contribution to the discussions organised by BEPA on “Europe’s role in a new world order”¹.

Our starting point is that the failure to sign a legally binding agreement in Copenhagen has left “much of the business community confused about exactly how to interpret the meeting’s wider economic implications”. That means a loss of momentum in the investment process that is needed for the transformation of the old fossil economy to an economy based on renewables.

In this critical phase of the UNFCCC climate negotiations there is a need for a two track approach: on the one hand continue to work for a legally binding agreement and on the other hand also work for a sufficiently strong framework for sustainable investments. Such a framework could initially be established by the EU and a smaller number of countries with large emissions.

Therefore, we suggest that the European Commission takes the initiative to develop a trade, investment and growth strategy for climate mitigation, in accordance with the WTO fundamental goals on “sustainable development and protection and preservation of the environment”, a free trade agenda, with the long term aim of CO₂-free trade. Such a strategy could include the following elements:

- The establishment of a CO₂ price floor to provide incentives for re-investment
- Using Internal Markets tools to promote climate-smart goods and services - in Europe and globally
- Further developing the EU cap-and-trade regime
- A revision of the WTO Subsidies Agreement and a review of EU Member States’ subsidies with a substantial impact on GHG emissions and the climate.
- Better use of public procurement
- Elimination of tariffs and non-tariff barriers on climate-related goods

The G-20 would be a particularly useful arena for discussions on a climate investment framework, which does not need to include all the UNFCCC members. All efforts in 2010 must be directed to bring back momentum in the transformation of Europe’s energy systems by building a new framework for a sustainable investment process. Over time a successful investment framework may lead to a legally binding agreement.

¹ This paper is written by Allan Larsson with contributions from Peter Kleen, Måns Lönnroth, Håkan Jonsson and Staffan Laestadius.

1. The Copenhagen Accord: “confusion for investors”

The comments to the conclusions of the COP15 are mixed, from expressing disappointment” to welcoming the Copenhagen Accord as an “anchoring agreement” and to describing it as “a confusion for investors”.

The President of the European Commission, Mr. Barroso, noted in his first comment that *“the level of agreement is honestly not what we have been hoping for”*. Rajendra Pachauri, chairman of the Intergovernmental Panel on Climate Change (IPCC), said: *“We will have to make sure it moves quickly towards the status of a legally binding agreement and therefore I think the task for the global community is cut out”*.

Other commentators were more positive. Professor Anthony Giddens, writing for Policy Network in London, regards the Accord as *“one that carries promise, because it recognises core geopolitical realities and works with rather than against them”*... *If successfully elaborated over the next few months, the Accord can provide an anchoring agreement but will need in addition a diversity of bilateral and regional agreements and – yes – “coalitions of the willing”*².

McKinsey’s Jeremy Oppenheim says that *“what happened at Copenhagen, through all the noise, was that the agenda shifted from being about narrow environmental policy to being about broad-based economic transformation and a commitment by nations across the world—but, particularly, the biggest economies and the biggest emitters—to begin the process. And it will be a multiyear, multidecade process of economic transformation”*. However, the failure to sign a legally binding agreement in Copenhagen has left *“much of the business community confused about exactly how to interpret the meeting’s wider economic implications”*³.

That means a loss of momentum in the investment process that is needed for the transformation of the old fossil economy to an economy based on renewables. So far, the framework for

the investment process has been assumed to follow from the legally binding agreement. There are, however, no indications that the deep resistance encountered in Copenhagen to such an agreement can be overcome in time for Cancun. Therefore, the order between the investment framework and the agreement may have to be reversed. Without a binding global agreement it is now up to the most ambitious countries to take the lead and implement various measures in order to set the example and accelerate the process. The EU should therefore intensify its efforts to devise various tools for achieving efficient mitigation of carbon dioxide emissions. All efforts in 2010 must be directed to bring back momentum by giving clear indications on a new framework for a sustainable investment process. Over time a successful investment framework may lead to a legally binding agreement.

2. Follow up on the Copenhagen Accord: Emissions reduction pledges

The Copenhagen Accord includes provisions that governments should commit to implement emissions targets for 2020. By the end of January the United Nations Framework Convention on Climate Change (UNFCCC) had received submissions of national pledges to cut and limit greenhouse gases by 2020 from 55 countries. These countries together account for 78 per cent of global emissions from energy use.

The EU has pledged a reduction in relation to 1990 of 20-30 per cent reduction, Japan 25 per cent, Russia 15-25 per cent and Norway 30-40 per cent. The US, Australia and Canada have pledged reductions in relation to 2000 or 2005, which makes comparisons more difficult. However, the US pledge amounts to about 3 per cent when the baseline is 1990. China is pledging not a total reduction but a lowering of carbon dioxide emissions per unit of GDP by 40-45% by 2020 compared to the 2005 level.

“The commitment to confront climate change at the highest level is beyond doubt... but greater ambition is required to

2 Antony Giddens, [Big players, a positive Accord](#) paper for Policy Network, London, January 2010

3 Jeremy Oppenheim, *McKinsey Quarterly*, February 2010.

meet the scale of the challenge”, said Yvo de Boer, Executive Secretary of the UNFCCC⁴

World Resource Institute has made an analysis of the pledges. The WRI found that while developed country emission reduction pledges could have an important and potentially substantial impact, they will not be enough to meet even the lower range of emission reductions required for stabilizing concentrations of CO₂e at 450 ppm and certainly fall very short of goals to reduce concentrations below that level⁵.

While this outcome may seem disappointing – even if Europe, for one, can be proud of its pledge - it should be borne in mind that this is not unique. The first agreement under the Vienna Convention for the protection of the ozone layer was similarly regarded as woefully inadequate. The same held for the first protocols under the Geneva Convention for the protection against air pollution. Subsequent protocols, developed as the parties grew more confident about what could be achieved, narrowed the gap between agreements and the necessary. These experiences indicate that the role of the first agreement is not to solve all problems once and for all but to start the learning process that will take years if not decades to mature.

3. From Copenhagen to Cancun: what do we know about the road map?

The Copenhagen Accord includes a process leading to COP 16, a new Climate Summit in Cancun, Mexico in November 2010. A first international forum for a Post-Copenhagen discussion is the meeting of the Subsidiary Bodies of the UNFCCC, taking place May 31-June 11 in Bonn.

The EU Spanish Presidency presented in the beginning of 2010 an Indicative Roadmap⁶, giving the first signals on how the EU might act in the

4 UNFCCC press release, February 1, 2010.

5 WRI, Comparability of Annex I Emission Reduction Pledges, February 2010.

6 EU Presidency, Climate Change, Indicative Roadmap (post Copenhagen) January 5, 2010.

run up to the next phase of negotiations. The document states that the outcome of COP15 was below EU expectations. Still it represents a step forward: *“It has the virtue of providing for the incorporation of pledges for greenhouse emission reductions from most countries and, particularly, from the major emitter ones that were outside the Kyoto Protocol emissions reduction commitments. In this respect, the Accord paves the way for an efficient agreed action at international level. The EU should work for the adoption of a global binding agreement aimed at limiting and reducing the greenhouse gas emissions in order to support the adaptation efforts of the most vulnerable countries and to open the door to a future of environmentally sustainable growth”*

The Roadmap has been set up in cooperation with the European Commission *“with the objective of upholding EU global leadership”*. The Commission delivered a first assessment of the COP15 at an Informal Environment Council meeting 16-17 January and the Council discussed this assessment and the draft Roadmap. The Commission intends to present a Communication before the Environment Council March 15 and the European Council 25-26 March.

The BASIC countries - India, South Africa, Brazil and China - met in India January 24-25 to coordinate their work in the run up to the Cancun meeting⁷. The Ministers underscored in the conclusions of the meeting the centrality of the UNFCCC process and the decision of the Parties to carry forward the negotiations.

The Ministers called upon the COP President (Denmark) to convene meetings of the two negotiating groups — (AWG-LCA and the AWG-KP) – in March 2010 and to ensure that the AWGs meet at least 5 times before the Mexico conference. Furthermore, they underlined the importance of the Accord as representing a high-level political understanding among the participants on some of the contentious issues of the climate change negotiations. They expressed the hope that this would facilitate the two-track process of negotiation under the Bali Roadmap to lead to a

7 Joint statement issued at the conclusion of the second meeting of Ministers of BASIC group, New Delhi, January 25, 2010.

successful conclusion of ongoing negotiations in Mexico. Finally, the Ministers agreed to meet at the Ministerial level every quarter, next time in late-April, 2010, in South Africa.

The US position will be defined through the ongoing legislative process in Congress. In the meantime the US will take part in preparations of and in negotiations at the UNFCCC meeting in Bonn in May-June, and in the G-20 meeting in Canada in June 2010. The Chinese position will likewise be defined as the 12th five year plan is agreed and the succession of the present leadership is settled.

Our conclusion is that the EU has to develop a two track approach: on the one hand continue to work for a legally binding agreement and on the other hand also work for a sufficiently strong framework for sustainable investments by building “a coalition of the willing”.

4. A new EU-agenda: A climate related trade, investment and growth strategy

In the preparations for the Cancun meeting, the EU should intensify its efforts to devise various tools for achieving efficient mitigation of carbon dioxide emissions within the EU, making the climate strategy “the growth strategy”, as suggested by Professor Nicholas Stern. This will require a focus on those elements that are most relevant for a transforming investment process.

It is a matter of fact that all the important policy tools which are in force, planned or discussed for achieving mitigation in one way or the other affect the competitive situation of the firms concerned and thus also cross-border trade flows. The main starting point is that the climate policy and trade policy should be mutually supportive.

We suggest that the European Commission develops a trade, investment and growth strategy for climate mitigation, in accordance with the WTO fundamental goals on “sustainable development and protection and preservation of the environment”, a free trade agenda, with the

long term aim of CO₂-free trade. Such a strategy could include several elements:

- The establishment of a CO₂ price floor
- Using Internal Markets tools to promote climate smart goods and services
- A further development of the EU cap-and-trade regime
- A revision of the WTO Subsidies Agreement and a review of EU Member States’ subsidies with a substantial impact on GHG emissions and the climate.
- Better use of public procurement
- Elimination of tariffs and non-tariff barriers on climate-related goods

When choosing what policy tools or mix of tools are most effective and appropriate, the following considerations should be taken into account: 1) The measures chosen should be as effective as possible to achieve the mitigation required. 2) The measures should be implemented in line with EU:s international obligations in the WTO. 3) The measures/instruments should be devised in a way as to give enough incentives for others to follow. 4) The measures should be easy to implement and administer.

4.1 Both an emission-cap and a price-floor

We suggest that the European Commission, as a first step, broadens the agenda by complementing the emission-cap with the concept of a price floor policy within the EU, which can create the necessary incentives for new clean technologies.

It is, initially, not so important on what price level these policies are introduced. The important thing is to establish the tool box and to declare that the levels will be increased until the necessary GHG reductions have been reached. It is today at least not possible to give an exact price level where actors may succeed in reducing GHG emissions enough to keep temperature increase below 2°C. Instead of formulating an exact price we suggest

that a CO₂ price in the latitude of €40/tonne is set as a "working target" (as compared to the current EU ETS spot price of approx. €13/tonne). That price level will create conditions not only for most alternative fuels to be competitive with coal but also create the necessary incentives for CCS technologies to be developed. If coal is to be used in the future, CCS systems must be added to all power plants – and the price for doing that is significant according to all expertise in that field. Although the assumed price-span is wide, a CO₂ price of €40 is far from exaggerating the necessary level.

The tool box will have to include a combination of direct and EU-wide regulations and policies aiming to increase the price of GHG-emissions, i.e a CO₂ tax. Although non-price related policies should not be neglected we are, however, of the opinion that higher prices on GHG emissions is a necessary although not sufficient condition for creating the incentives for transformation of our society away from its carbon addiction. Focus should be on increasing the price of GHG emissions in general and CO₂ emissions in particular.

- CO₂ taxation may start with coal – which is the by far most problematic of fossil fuels. Taxation must successively be harmonized between different CO₂ emitting activities. This must not necessarily be done immediately - the important thing is that actors realize that this will happen within short, thus reducing their incentives to shift from one GHG-emitting behaviour to another. The commitment by the new tax Commissioner Mr. Semeta to make the energy taxation directive "one of my first priorities" is promising.

4.2 Using Internal Market tools to promote climate smart goods and services - in Europe and globally

We suggest that the European Commission makes the Internal Market a center-piece in the climate strategy by focusing on the global impact of EU

product legislation and standard setting, and by setting new ambitious targets in key areas.

Technical regulations and standards focus on technologies, processes or products, rather than the resulting emissions. They are probably more effective than price-related policy tools (like cap-and-trade and taxes) to achieve mitigation relatively quickly. They would encourage others to become climate friendly, to be able to sell to Europe.

Europe has the strength of being the most successful standard-setting and rule-setting political force in the world. This has been achieved by being swift and smart in devising our Internal Market rules, in a way that makes others want to follow. The Economist noted that "Europe is becoming the world's regulatory capital ... usurping America's role as a source of global standards"⁸.

Many recent examples underline this: European directives, in particular on safety and environmental issues, are today copied in part or in full in other major economies. The "New approach" Directives, and the European standards that follow them, are world-leading in many domains. Important technological leaps, such as the GSM standard for mobile telephones, have given Europe a competitive advantage.

Thus, Europe has strength in this standard-setting process that now could be used to set more ambitious performance targets for the implementation of the EU strategy in Europe and for making an impact in the rest of the world. Some sectors are of particular interest with respect to new smart regulations such as energy efficiency, resource efficiency and promoting services in the green sector.

- We suggest that the European Commission makes a review of the existing regulatory framework in these fields, to identify where new initiatives can be envisaged to encourage the development of climate-smart goods and services. Furthermore, the European Commission should identify performance targets to

8 The Economist, September 22, 2007,

achieve the necessary EU emission reductions for 2020 and beyond.

4.3 A further development of the EU cap-and-trade regime

One main field of action is the EU ETS scheme, the credibility of which has been seriously called in question and needs to be restored. The European Commission has to ensure that the new system is effective and sufficiently strong to include other developed countries to apply similar systems.

- Full auctioning of emission rights should be implemented as fast as possible to provide incentives for the energy-intensive industries to change to less carbon-intensive production methods. It is only when the EU forces the energy-intensive industries to pay the full price for acquiring the emission rights, that border measures might be considered to forestall possible “carbon leakage”. Such border measures that include importers in the emission trading system are already envisaged by the European Commission and in the bills presently considered by the US Congress.

An absolute condition for applying border measures of any kind is that they respect the two (and very reasonable) non-discrimination principles embodied in the WTO, namely national treatment and most-favoured nation treatment. In other words, the implicit (or explicit) taxes or other regulations must not be higher on foreign goods than on goods that are domestically produced and there must be no discrimination between different foreign suppliers. The Commission should therefore specify how the envisaged inclusion of importers into the EU ETS could be devised and implemented in order to meet these non-discrimination requirements.

4.4 A revision of the WTO Subsidies Agreement and a review of EU Member States’ climate subsidies

Another field of action is subsidies, which can play an important role in encouraging development and reliance on more environmentally sound practices. This applies both to the industrial and the agricultural sector. However, there is always the risk that subsidies are given for other more protectionist purposes. Two actions are needed:

- The EU should work for a revision of the WTO Subsidies Agreement to allow for expanding the definition of which subsidies should be termed “non-actionable” (i.e. not run the risk of meeting countervailing actions from other countries) and thereby including climate-related subsidies.
- The Commission should draw up a list of subsidies which presently are given by individual member countries for emission reduction purposes and make a judgment whether they are implemented according to the EU guidelines for state aid.

4.5 Better use of public procurement

Another field of action is public procurement, which could be a very effective tool in the mitigation tool-box.

- The Commission should undertake a study of how public procurement could be used as a policy tool in the fight against climate change. An EU policy for public procurement could act as an effective incentive for other countries to change their mitigation policies.

4.6 Elimination of tariffs and non-tariff barriers on climate-related goods

Finally, tariffs and non-tariff barriers for climate related goods should be eliminated, even if most tariffs on these products are very low, at least in developed countries:

- EU should pursue the initiative it took together with the US in Bali, December 2007 with regard to elimination of tariffs and

identifiable non-tariff barriers for environmental and climate-related goods.

5. The process: UN, G-20 or “Coalitions of the willing”

5.1 The UNFCCC-process: still the main avenue

The immediate reactions to the UNFCCC process after the Copenhagen meeting were negative and questions were made on the viability of the negotiation process.

A few weeks later there is broad support for a new round of negotiations. The BASIC group has asked Denmark to convene meetings in March 2010 and to ensure that the main group (AWGs) will meet at least five times before the Mexico conference. The EU is committed to work for the adoption of a global binding agreement within the framework of UNFCCC. Thus, the UNFCCC-process will continue to be the main avenue in the efforts to reach a legally binding agreement.

As proposed in this paper a two track approach is now urgent in order to create an international framework for sustainable investment processes. Such a framework would only need a limited number of participants in order to effectively change investment patterns and develop new and climate efficient technologies. It should be feasible to include this investments framework in a legally binding agreement as the UNFCCC process matures over the years.

5.2 The G-20 process: a new platform for negotiations

Leaders of the G-20 agreed at the Pittsburgh Summit in 2009 to make the G-20 “the premier forum for international economic cooperation”. G-20 will have several high level meetings in the next few months followed by a G-20 Summit in Toronto, Canada, at the end of June and a new Summit in mid-November in Seoul, Korea.

These meetings are opportunities to making sure that heads of state are involved and committed – not only environmental ministers. The meetings can and should be a platform for heads of state and government to resolve controversies and find compromises that can be included or added to a final agreement.

5.3 Coalitions of the willing: new opportunities for the EU

The EU focused in 2009 on the UNFCCC-process and did not seek to build alliances, “coalitions of the willing”, with other partners. In 2010 the process will be more open and EU could identify various issues to build coalitions around such as an investment framework, standards for climate-smart goods and services, sectoral agreements, agreements/treaties with groups of developing countries on adaptation, forestry (REDD) and the like.