

Beyond COP6: The Need for Extended Flexibility

Axel Michaelowa and Reimund Schwarze

1. Introduction

The climate summit at The Hague ended without any agreement and thus disappointed hopes that it could give a clear start for international activities to reduce greenhouse gas emissions. Still many observers believe - with some distance - that there was progress, and that a deal was only missed because of lack of time and diplomatic failure (Jepma 2000). We share this view and explain in this paper where, from our point of view, COP6 failed and where it succeeded, and how the failures of COP6 can be avoided at the follow-up meeting in mid-2001 (COP6/II). Specifically, we propose that European negotiators assume a more flexible approach to the "crunch issues" of The Hague (supplementarity and sinks) while standing firm on rules and modalities for the use of the Kyoto mechanisms. To give this strategy a chance of success, and to build confidence with the new negotiators of the Bush administration and to search new allies among the developing countries and countries in transition, the EU should initiate high-level political meetings to explore common ground *before* the meeting. The paper is organised as follows: In Section 2 we explain the role of COP6 within the Post-Kyoto process and discuss how the previous COPs and subsidiary bodies' meetings affected the discussions at The Hague. In Section 3, we provide an overview on the debate at COP6 and analyse President Pronk's proposal for a compromise, which was delivered two days before the break down of the conference. In Section 4, we draw some general lessons from the failure of COP6 and speculate how this failure could be avoided at COP6/II through extended flexibility and prior exploratory political meetings.

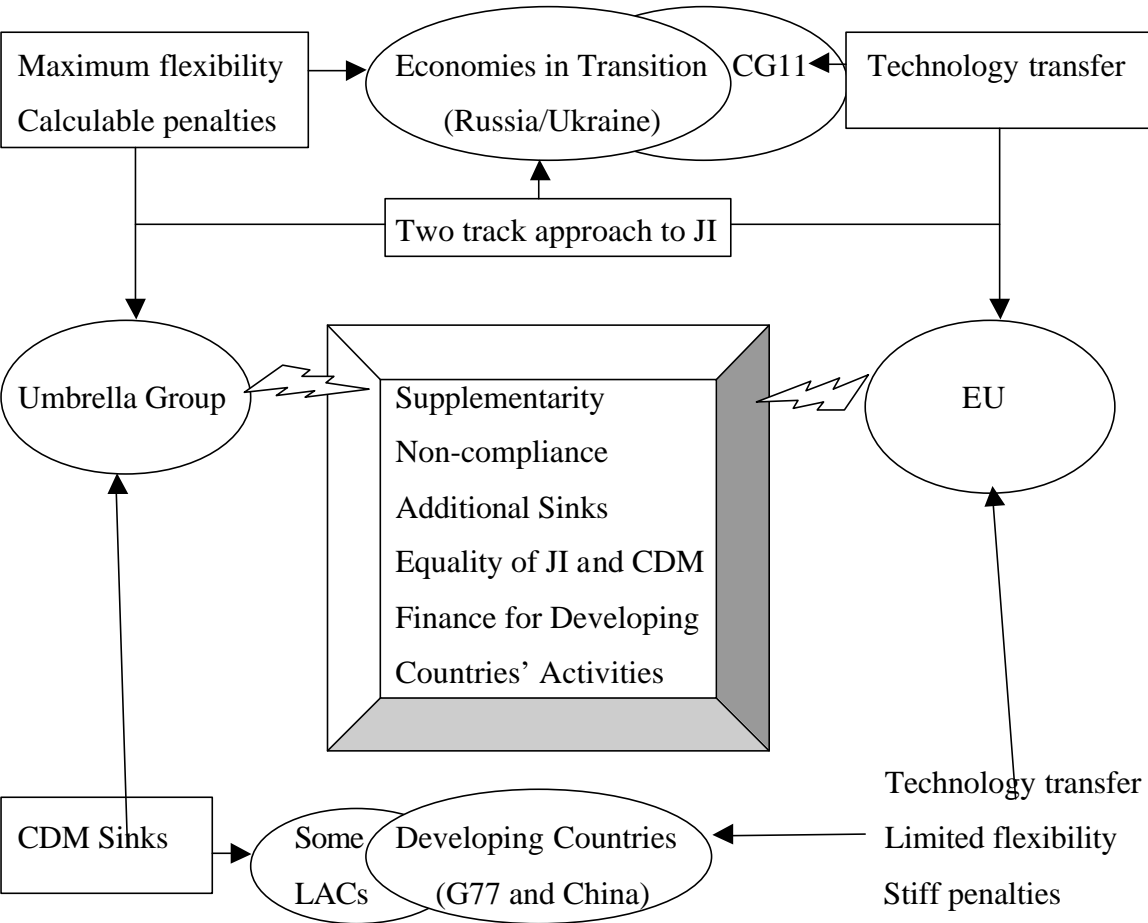
2. The road to COP6

Compared to the previous two conferences of the parties, COP6 was met with great expectations. It was intended to finalise the deal struck at Kyoto in 1997. The Kyoto Protocol sets legally binding emission targets for industrialised countries but allows them in principle

to use carbon sinks (forests and possibly soils), trade emission permits among themselves and to invest in emission reduction projects in other industrialised countries (Joint Implementation, JI) and developing countries (Clean Development Mechanism, CDM). However, the rules had not been defined in Kyoto. This consequently led to a wide-spread resistance among major emitters to ratify the Protocol. To speed up this process, the climate summit of Buenos Aires (COP4) decided that all outstanding rules of the Kyoto Protocol should be finalised at COP6.

To prepare this groundbreaking event, the UNFCCC Subsidiary Bodies (SBSTA and SBI) held four major sessions, and political negotiators met once in Bonn in 1999 (COP5). These rounds of talks did not produce many results. Instead they confirmed a deep political divide between the Parties on a number of technical issues. Figure 1 depicts the strategic frontlines of this divide.

Figure 1: The political frontlines at COP6



Major players in this debate were the US who, along with some non-European OECD countries such as Japan, Canada and Australia, form the so-called Umbrella Group. Its main opponent was the European Union (EU). Other players were the Economies in Transition (Russia, the Ukraine and some Central and Eastern European Countries, that formed a new negotiating group “CG 11”) and the developing countries (G77 and China). Within the latter group however, there were strong differences on some positions.

The Umbrella Group pushed for maximum flexibility in the design of the Kyoto mechanisms as well as for some creative accounting of sinks - domestically and as part of the CDM - in order to reduce their perceived economic burden. The EU, on the other hand, assumed the role of a "watchdog" for environmental integrity. It strongly pushed for domestic efforts to reduce energy consumption ("supplementarity") and limited accounting of sinks, both as part of the Kyoto mechanisms and domestic GHG accounting. The Economies in Transition, particularly Russia and the Ukraine, supported the Umbrella Group in their desire for unrestricted emissions trading, but the subgroup of Central and Eastern European Countries (notably Poland) joint the EU in their demand to restrict "hot air" trading and to focus the CDM and JI on technology transfer (energy efficiency and renewables). Many developing countries had changed their previously hostile attitude towards the CDM and other Kyoto mechanisms during the AIJ pilot phase. Especially many countries from Latin America (with the notable exception of Brazil) and forest-rich African and Asian countries recognised that they could benefit from the joint mitigation projects - including projects of sink enhancement such (afforestation and reforestation). Yet they agreed with the EU that the use of flexibility mechanisms should be somewhat limited. They also urged to have strict rules for compliance, specifically stiff penalties for non-compliance of Annex I countries. The Umbrella Group instead argued for calculable penalty schemes such as a cost cap (explained in Kopp/Morgenstern/Pizer 1997). Astonishingly, Russia argued against strong non-compliance rules. Developing countries also insisted on an equal treatment of JI and the CDM, specifically with regard to the adaptation tax of the Kyoto protocol, and demanded a larger funding of developing countries's climate change activities. Industrialised countries, on the other hand, argued that the CDM has already been given a competitive advantage over JI in that certified emission reductions (CERs) from CDM projects can, contrary to JI, be banked as of 2000. They also agreed to have two track-approach according to which JI projects would be eligible to a simplified verification procedure as long as the host countries comply with their reporting and inventory commitments. The issue of domestic accounting of “additional sinks” (agricultural soils and forest management) was mainly pushed by the US, but met

resistance by the EU and most other major players (except Russia). However, the whole issue of sinks remained largely undebated during the preparative sessions because of its difficult-to-understand technicalities and the expectation that these technicalities would be clarified by the IPCC special report on Land Use, Land Use Change and Forestry (LULUCF) that was released shortly before COP6 (May 2000). This report does, however, not give clear political guidance on this issue (it was actually never intended to do so!¹), but identifies "a range of options and discusses implications and interrelationships among options" (IPCC 2000, 3).

Missing any pressure to compromise on those issues, these sessions produced a "hotch potch" of proposals. Indeed, the final proposals submitted to COP6 negotiators were packed with mutually exclusive proposals (set in brackets) and covered 340 pages of legal text.² Thus, as a result of several years of in-the-air debate, COP6 did start with an untractable documentary basis for negotiations.

3. The discussions at COP6

The discussions at The Hague continued along the lines described above. After more than a week without significant progress, the President of COP6, Jan Pronk, finally but unfortunately too late³ took the lead and did away with the previous negotiation documents. He declared: *"The documents before us are too long and littered with brackets. To facilitate our negotiations this week, we must distinguish between outstanding issues of differing characters. Some are "crunch issues", i.e. questions on which clear political choices are needed for negotiations to advance. Others are more technical issues with political implications, which would fall into place when decisions on the "crunch issues" are made. There are also technical issues that require further negotiation, but not at a ministerial level. Finally, there are certain technical questions that could be set aside until after COP6. While recognizing the importance of all these issues before us, I focus on the "crunch issues" - those ripe for high-level decision making"*.

Instead, he proposed a few "issue clusters" (depicted as boxes) to be discussed in informal groups that contained the following topics (see table 1):

¹ As Robert Watson, the chairman of the LULUCF Special Report, made utterly clear in his outline: „This Special Report will be policy relevant, but will not be policy prescriptive“ (FCCC/CP/1998/INF.4)

² „All In Session Documents“ from www.unfccc.de (encompassing FCCC/CP/2000.CRP01-13 and FCCC/SB/2000/CRP.15 to CRP.23).

³ Some negotiators felt bored at the beginning of the second week as nothing was moving.

Table 1: Issue clusters at COP6

Box A	Capacity building, technology transfer, implementation of Articles 4.8./4.9, 3.14 of the Kyoto Protocol and finance
Box B	Kyoto Mechanisms
Box C	Land Use, Land Use Change and Forestry
Box D	Policies and Measures, Compliance, Accounting, Reporting and Review

Within this clustered approach negotiators achieved some progress. They agreed, for instance, on a fast-track approach for small-scale/renewables CDM projects. According to this approach, these projects would be subject to less stringent rules in terms of baseline determination (standardised baselines) and less institutional oversight. The political goal behind this decision was to jump-start the CDM with relatively uncontroversial projects at low transactions cost. Reconciliation seemed also feasible on the issue of supplementarity. The EU signalled (according to Environmental Minister Kawaguchi of Japan, who co-facilitated the informal discussion group⁴) that it could settle on a qualitative formula rather than a quantitative ceiling if other technicalities could be resolved satisfactorily.

To speed up this process and facilitate an agreement, President Pronk finally came forward with a proposal of his own - two days before the official closing of COP6. This proposal contained some bold suggestions (depicted in table 2) that reflected his personal view on the matters at hand.

⁴ Cited in Joint Implementation Quarterly, Vol. 6(4), p. 9.

Table 2: The Pronk Proposal

<p><i>Box A</i> contained a provision for additional funding of a very diverse bunch of developing country activities related to climate change such as capacity building, adaptation, emission reduction projects, forest protection, conversion of fossil fuel extraction-oriented economies. As part of this funding proposal it suggested an in-kind emissions tax based on emissions targets of the core industrialised countries (which could raise enormous revenues!). Another innovative proposal was the automatic kick-in of a (non-specified) tax on emissions trading and JI if less than one billion \$ of additional funding would be reached by 2005. On the other hand, it limited the adaptation tax on CDM projects to 2% which, according to some estimates, would amount to a few hundred million \$ per year only.</p>
<p><i>Box B</i> suggested a purely political Executive Board of the CDM to be elected in June 2001 that should be ruled by majority vote(which would slow down the decision process considerably!). Regarding project eligibility, it suggested a voluntary commitment by industrialised countries to “refrain” from nuclear power CDM projects. It also proposed a prompt start for small scale and renewable CDM projects that can use standardised baselines. No cap was proposed for CDM, JI and emissions trading, but a 70% reserve requirement to prevent overselling of permits (which would effectively limit the selling of permits to 30%!). A traffic light approach to JI would have established strong verification rules if the host country does not fulfil its reporting requirements (very much in line with the previously mentioned two track approach!).</p>
<p><i>Box C</i> allowed a broad range of additional sinks (agricultural land and forest management) for domestic accounting, but limited to 3% of the emissions budgets of Annex I countries. Afforestation and reforestation were eligible CDM projects, but not forest conservation (which would have been funded as part of the adaptation fund!).</p>
<p><i>Box D</i> stipulated a 50% penalty on any emissions above the target and an additional 25% for each target period in which the “debt” is not repaid.</p>

Indeed, the Pronk proposal would have been a relatively sensible comprise:

- The non-compliance penalties would have given a strong incentive to comply with emission targets (as the implicit interest rates are above 8% per annum!).
- Full international flexibility would have kept the cost of Kyoto low.
- Letting a limited amount of additional sinks in and allowing afforestation in the CDM would have led to a diversification of mitigation activity while incentives for avoidance of deforestation would have been provided by the adaptation fund.
- The quick start with small scale projects in the CDM could have allowed institutional learning while not unduly risking environmental integrity.
- The reluctance of industrialised countries to commit funds for developing countries would have been overcome by the threat of taxing emissions trading and JI alongside the CDM.

On the negative side, the proposal was lacking decisions on some critical CDM issues such as

- the distribution formulae for the funds for adaptation and other issues.
- the groundrules and institutional processes to derive baseline methodologies for CDM projects,
- the rules to prevent business-as-usual CDM projects (“investment additionality”),
- the participation of stakeholders in the CDM project pipeline.

The proposal was greeted by considerable scepticism from all interest groups, but particularly by the EU. The issue that finally led to the deadlock of The Hague was the threshold for additional sinks.

4. The issue of additional sinks

The issue of additional sinks came to the forefront of political debate as parties arrived at some definitional arrangements under Article 3.3 of the Kyoto Protocol. This article allows Annex I Parties to take account of certain human-induced activities in the land-use, land-use change and forestry sector (LULUCF) that remove greenhouse gases from the atmosphere, namely afforestation, reforestation and reduced deforestation. Conversely, it stipulates that any changes in these activities that lead to an increase of greenhouse gases in the atmosphere

(e.g. an increase in deforestation) will be subtracted from the assigned amounts of Annex I parties. Article 3.3, however, does not define exactly what "afforestation, reforestation and deforestation" means, and Parties could not agree on a common definition for these three terms. As these definitional problems could be partly resolved by the IPCC's Special Report of LULUCF (IPCC 2000), and Parties at SBSTA 13 (Lyon) seemed to compromise on the IPCC Definitional Scenario (according to which only forest to non forest conversion, i.e. land use change, triggers accounting under Article 3.3), it became clear that forest management activities (which increase the carbon uptake on *existing* stands), if at all, had to be included as additional activities under Article 3.4.

Several Umbrella Group countries, particularly the U.S., could generate heavy credits by including forest management. Some might have well been able to meet their Kyoto commitments without any action whatsoever. At the same time these countries faced considerable problems to get the Kyoto Protocol ratified at their domestic constituencies. Consequently, they fought for an extensive list of additional sinks, including forest management, to release the economic burden of Kyoto and smoothen the process of ratification. In the first week of COP6, Japan, the US and Canada proposed a concrete scheme for computing forest management carbon credits, which became known as the JUSC 3.4 proposal. This scheme consists of three different crediting intervals (see fig. 2, adapted from Greenpeace 2000, p. 9).

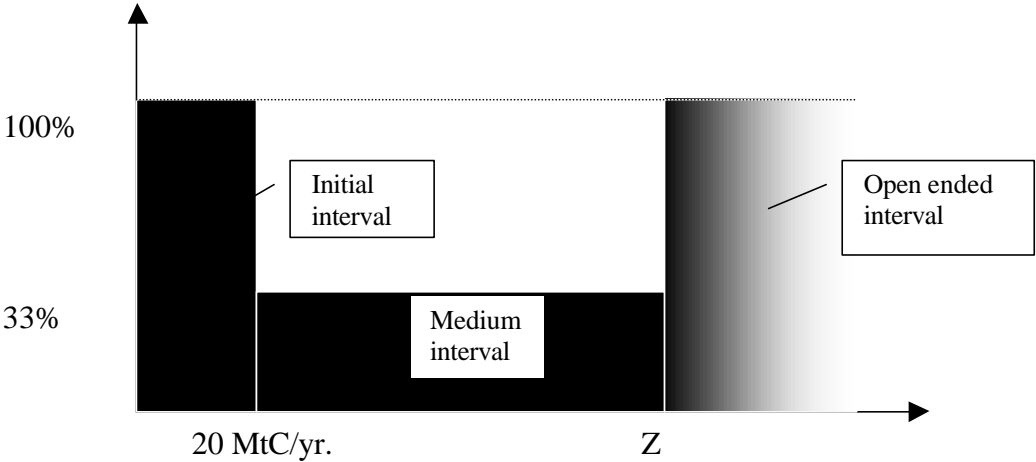


Figure 2: *The JUSC 3.4-proposal (Phase In-Approach)*

The initial interval offers full credits for net carbon removals from forest management for a portion up to 20 MtC/year. In the second interval, parties are offered credit up to an unspecified threshold (Z in figure 1) which will be discounted by a factor of 1/3. For those parties with a remaining sequestration potential (beyond Z) full credit will be given. As most

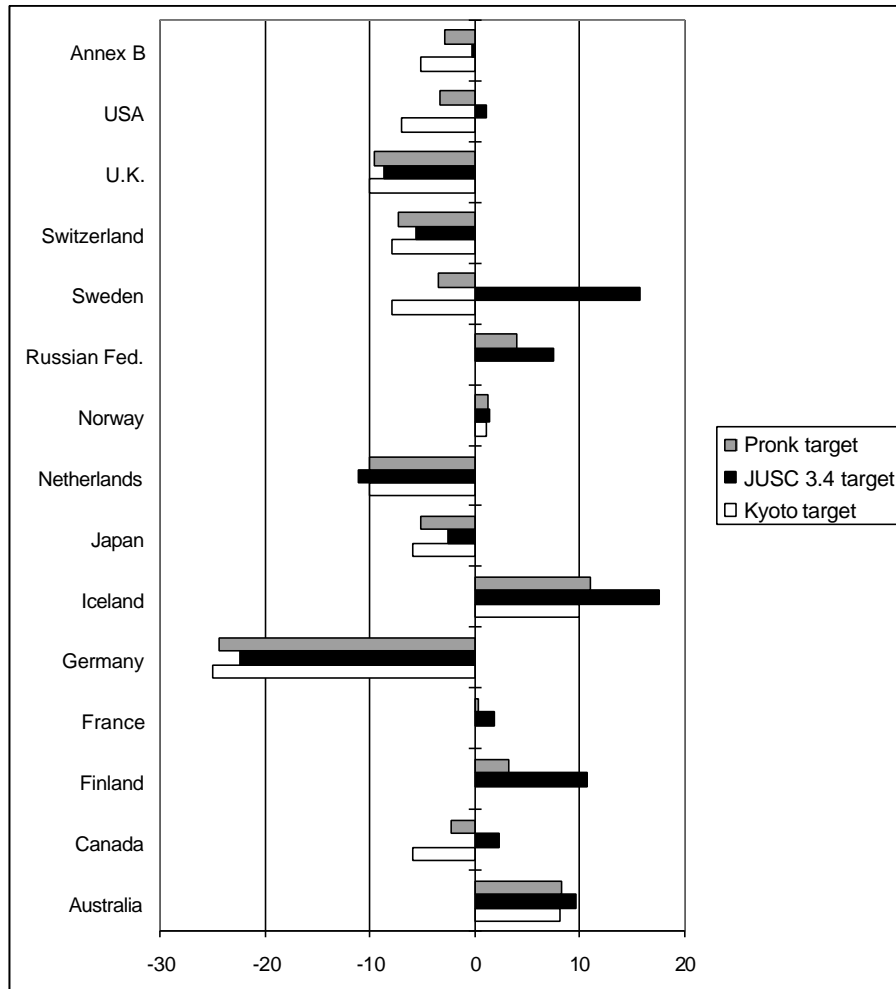
countries net removals from forest management are less than 20 MtC/year, this proposal would have implied full crediting for all their carbon removals due to forest management.

The following graph (fig. 3) illustrates the effect of the JUSC 3.4 proposal on Kyoto targets, assuming a scenario with no threshold. The white and black bars in this graph depict the percentage target changes for several Annex B countries and Annex B as a whole.

While the proposal seems to offer big target changes for some European countries, notably Sweden and Finland, the actual credits from forest management for these countries are comparatively small (i.e., - 4.4 MtC/yr and - 2.2 MtC/yr respectively). Massive gains, however, would result for the U.S. (-133 MtC/yr), Russia (-71 MtC/yr), Canada (- 13.7 MtC/yr) and Japan (- 11.4 MtC/yr). The overall Article 3.4 credits for Annex I countries from this proposal adds up to approximately 250 MtC/year, which would effectively wipe out the Annex B target of an overall reduction of 5,2% to an insignificant decrease of -0.4 % below 1990 levels.

This proposal met stiff opposition from the NGO community and the EU. The EU, at a Council meeting in Luxembourg June 22, had adopted a negotiating position that no additional sinks should be included until after the first commitment period of 2008-2012. As such differences between the Umbrella Group and the European Union began to dominate political discussions during the second week of COP6, President Pronk released a compromise plan of his own. The President's plan included a broad definition of additional activities (including forest management and agricultural soils), but curtailed the amount of credits under Article 3.4 to an upper limit of 3% of 1990 emissions. Furthermore, it stipulated a discounting of credits for forest management of 85% and for cropland/grazing land management of 30% exceeding a threshold of 30 MtC/yr.

The grey bars in fig. 3 indicate how this proposal would affect the Kyoto targets and how it compares the JUSC 3.4. proposal. Obviously, Pronk's plan would have significantly undercut the JUSC 3.4 proposal. The total Article 3.4 credits for Annex B countries would have been limited to 150 MtC/yr instead of 250 MtC/yr of the JUSC 3.4. proposal. Yet, it acknowledged the need of Umbrella Group for 'additional flexibility' by lowering the required reductions for the US by 56.7 MtC/yr, for Canada by 5.8 MtC/year and for Japan by 2.46 MtC/Year. More importantly, it helped to shift the focus of the debate from narrow technical matters (definitions, accounting procedures etc.) to a political level of bargaining on targets. Thus it levelled the ground for a series of last minute high-level political bargains.



Party	Kyoto target (%)	JUSC-3.4 proposal (MtC/yr)	% of assigned amount	Pronk proposal (MtC/yr)	% of assigned amount	JUSC 3.4 target (%)	Pronk target (%)
Australia	8	2.18	1.5	0.33	0.2	9.5	8.2
Canada	-6	13.73	8.2	5.79	3.7	2.2	-2.3
Finland	0	2.20	10.7	0.61	3.2	10.7	3.2
France	0	2.70	1.8	0.39	0.3	1.8	0.3
Germany	-25	8.45	2.6	1.50	0.5	-22.4	-24.5
Iceland	10	0.05	7.5	0.01	1.0	17.5	11.0
Japan	-6	11.44	3.4	2.46	0.8	-2.6	-5.2
Netherlands	-10	-0.69	-1.2	0	0.0	-11.2	-10.0
Norway	1	-0.04	0.3	0.02	0.2	1.3	1.2
Russian Fed.	0	62.37	7.5	33.00	4.0	7.5	4.0
Sweden	-8	4.55	23.7	0.77	4.4	15.7	-3.6
Switzerland	-8	0.34	2.4	0.09	0.7	-5.6	-7.3
U.K.	-10	2.71	1.3	0.54	0.3	-8.7	-9.7
USA	-7	132.48	8.0	56.70	3.7	1.0	-3.3
Annex B	-5.2	242.00	4.8	105.80	2.24	-0.4	-3.0

Source: WWF (2000) and Greenpeace (2000), p. 4. All values are derived from the submissions made by parties in August, 2000.

Figure 3 and Table 3: The effect of Article 3.4 on Kyoto targets

The most prominent bargain had been hatched, according to U.S. and British sources⁵, by a lengthy telephone discussion between US President Clinton and British Prime Minister Tony Blair in the night before the closing of COP6. Britain's deputy prime minister, John Prescott, stepped forward on November, 25th, with a compromise that called on the United States to restrict its use of the emissions trading scheme and reduce carbon credits from its forests and farmlands to 50 Mt (which would actually undercut the 56.7 MtC/yr of the Pronk proposal). He got the US delegation to agree to this compromise, however, he did not find approval for this proposal by the EU. Germany and Denmark said the it was intolerable and stood firm to their previous offer of 20 MtC/yr for the US. This led to the ultimate break-down of negotiations at COP6.

5. Lessons from COP6

What can be learned from the failure of COP6? At this early stage, we can only provide our very subjective judgement.

What we learned from COP6 was, firstly, that every conference has its own dynamics. If time pressure and late-night discussions helped to settle in Kyoto (as some commentators, e.g. Ott/Oberthür 2000, 16, suggested), it did not help in The Hague. In fact, we believe that COP6 could have been successful if negotiations on "crunch issues" would have started earlier at a political level. Given the range of issues and the potential for multiple settlements among parties, we conclude that a political deal would have been possible. Previous strategy talks and high-level political negotiations in any case would have reduced the bargaining agenda to "crunch issues" at which negotiators in The Hague arrived only at the end of their talks. Specifically, the "killing issue" of additional sinks could have been disarmed if packaged into an overall political deal, instead of assuming ad hoc positions during the closing days of the negotiations. Waiting for an expert solution to the problem, as most Parties did before, was a flawed approach since there is no scientific solution to a political problem - the IPCC special report is utterly clear on that from the outset! Thus to avoid repeated failure, we need high-ranking talks between *all* major players on all Kyoto issues *before* negotiators meet for the second part of COP 6. The meeting of environmental ministers in Ottawa (in December 2000) was an event in this spirit which needs to be followed by other such talks. The EU is in a perfect position to kick off such an initiative.

⁵ Cited from Washington Post as of November, 26th, 2000.

Secondly, we learned about the importance of the "principle of enhanced flexibility backed by transparency and responsibility" (Sugiyama/Michaelowa 2000) for the current Kyoto process. COP6 ultimately proved that the Kyoto protocol is different from all previous multinational environmental agreements in that it requires, at least for several countries, fundamental changes in energy consumption and lifestyles that imply high costs. Even if costs may be low economically, they will surely politically be high as powerful interest groups fight against emission reduction commitments. International negotiations thus have to acknowledge the sobering realities of political implementation at the domestic level. The slow process of ratification of the Kyoto Protocol and the failure at The Hague prove that ambitious quantified targets do not survive the fight of domestic interest groups, if these do not benefit from such targets. In order to prevent that such domestic backlashes destroy the whole Kyoto regime, we need extended flexibility.⁶ Extended flexibility implies to boil down the ambitious targets to symbolic, still important, hardcore issues ("crunch issues") and allow for political "horsetrading". Any deal should be possible such as: "If you accept x% of additional domestic sinks, I will agree on a de facto y%-cap on flexibility mechanisms or a maximum penalty for non-compliance of z \$/t" (in this respect we fully agree with Jepma (2000)). However, we should strive for consistency to avoid distortionary incentives. The only non-negotiables (and that¹ is where we disagree with Jepma) are transparency and accountability both at the level of policy making and at the level of implementation. We believe that public pressure can be the ultimate force to make countries adhere to the ultimate goals of the UNFCCC, but it requires transparency and accountability. Striving for perfectionism at an early stage instead produces negotiation deadlock such as the one at The Hague.

The failure of COP6 is neither dramatic, nor unique. It fits neatly into high-level summit failures such as the WTO summit in Seattle in 1999 or the temporary break down of discussions under the UN Convention on Biological Diversity in 1999 (Cartagena summit). It will have the greatest impact on the business community. Companies that have already started implementing climate change strategies may now scale back their activities and release their pressure on their respective government to provide a legal framework for early action. Business that had hoped for clarity concerning climate policy now faces even more uncertainty. In this situation, a lot depends on the willingness of some countries to take the lead, promote bilateral or regional agreements on climate change policy and shape the negotiation process at Bonn. The EU is in also in perfect position to assume this leading role, especially if it teams up with Russia and the developing world.

⁶ Extended flexibility corresponds conceptually to ordinary "flexibility" in others MEAs. We applied a new term

Literature

- Anonymous, Special JIQ Report on COP6, The Hague, Netherlands, 13-25 November 2000, Joint Implementation Quarterly, Vol. 6(4): 7-12..
- Greenpeace (2000), In Depth Analysis of the USA/CANADA/JAPAN Proposal for Sinks under Article 3.4, released on November, 22nd, 2000 at COP6.
- Intergovernmental Panel on Climate Change (2000), IPCC Special Report: Land Use, Land Use Change and Forestry, Geneva.
- Jepma, C. (2000), A Break in The Hague? Joint Implementation Quarterly, Vol. 6(4): 1.
- Kopp, R., Morgenstern, R., Pitzer, W. (1997), Something for Everyone: A Climate Policy that Both Environmentalists and Industry Can Live With", Resources for the Future, Washington D.C.
- Sugiyama, T., Michaelowa, A. (2000), What must and can COP6 decide? Extended flexibility backed by transparency and responsibility, Energy Policy 28, 571-574.
- The President of COP6 (2000a), Informal Note by the President of COP6, Submitted to COP6 participants on Monday, 20 November 2000, The Hague.
- The President of COP6 (2000b), Note by the President of COP6, Submitted to COP6 participants on Thursday, 23 November 2000, The Hague.
- WWF (2000), Implications of the Pronk Package on Article 3.4, released on November, 23rd, at COP6 (Analysis by Kevin Gurney, Dept. of Atmospheric Science, Colorado State University, for WWF).
-