

## "Kyoto Protocol's emission trading mechanisms could become redundant after 2020."

The next climate conference to be held in Madrid in December has the challenge of deciding how markets can be deployed in the service of climate. The Clean Development Mechanism (CDM), a product of the Kyoto Protocol, is one such market instrument that can help industry as well as climate. Alongwith China and Brazil, India is a leader in CDM since its inception in 2007. A number of small and medium projects in the field of energy efficiency and renewable energy, set up in India in the last two decades, owe their origin to the financing support available from CDM. Unfortunately, its future hangs in balance.

The situation may change in 2021 when market mechanisms mandated under the Paris Agreement come into operation. Most developed countries are strongly opposed to permitting the carryover of CDM projects and their credits into the Paris Pact's mechanisms. The credits lying unsold with the CDM projects could lose their economic worth. Besides, the CDM projects will have to go through the process of validation and registration again with the new mechanism. This will involve additional financial and administrative costs.

India has about 250 million Certified Emission Reduction (CER) units under CDM issued by the UN-FCCC, the global administrator of Kyoto mechanisms. The number of CDM projects registered in India is 1,376 (out of total 7,979 globally) and 89 per cent of these projects are still active. The demand in EU, which has been the largest market for CDM credits, has declined sharply over the last decade because of regulatory barriers. The unrealised value of CDM credits could be in the range of almost \$5 billion — estimated at a very conservative price of US \$20 per unit. India stands to lose substantially if the doors on the existing CDM projects and credits are closed in 2020.

What does one do to help CDM find a place in the post-2020 markets? This requires one to understand the arguments against CDM. There are three main concerns. One, it has failed to demonstrate environmental benefits in addition to the "business as usual" scenario, or provide technological benefits. Two, its transition to new mechanisms will have adverse impacts on carbon prices and investor sentiments in future markets. Three, double counting could compromise global ambition on reducing GHG emissions.

The argument on "lack of addition to the business as usual scenario" appears to be a contrived one. Credits for CDM projects are issued after their compliance with internationally approved criteria is ascertained. CDM proj-

ect proponents should be free to choose available cost-effective technologies as long as the objective of emission reductions is achieved. Moreover, “additionality” in CDM projects should not be judged solely on the criterion of technology; they are also about investments and overcoming market barriers. All CDM projects have passed these tests.

The argument that a full-scale transition of CDM credits may flood the market and lead to deterioration in the carbon prices in future markets is also over-stretched. Validation and registration of projects under the new mechanism may take at least three years. Assuming that all CDM units available globally till 2020 are traded immediately, they may be fully absorbed by 2024 — as demand for credits for meeting the Paris commitments increases. In fact, more than 60 per cent of the credits may be used fully even before 2022 if we take into account the demand from airline operators to meet commitments under CORSIA — an emission reduction scheme for international civil aviation effective from 2021.

The question of impact of CDM on global environmental integrity is, however, an important one. Environmental integrity is an objective of the market mechanisms under the Paris Agreement. Environmentalists believe that, in case of project/programme-based mechanisms, countries should make arrangements to prevent double counting of emission reduction units in their national accounts. The proponents of sustainable development, however, argue that difference in levels of development of countries requires that the adjustment principle should not be applied uniformly to developed and developing countries. The question, therefore, is: Should the pre-2020 CDM credits be discounted from the national emission reductions in case this principle is adopted for post 2020 credits?

Recent developments in the International Civil Aviation Organisation (ICAO) warrant an urgent examination of the issue. ICAO is actively considering a plan that seeks to limit the use of CDM credits to those issued after 2015. This could deal a body blow to CDM in the future carbon market. It may still be possible for the countries having a stake in CDM to influence the ICAO process if they negotiate the conditions for the long-term use of credits originating in their host country. It will be important for India to have a strategy that ensures that it does not get shut out of the CORSIA market even as ICAO enlarges the source of supplies from other countries. A pragmatic assessment of likely gains and losses from competing approaches to CDM transition into new mechanisms is the need of the hour.

It is time that we rethink the relationship between the project/programme-based emission reduction units and the national pool of emission reductions so as to establish a firm basis for access to future carbon markets. CDM has been a useful source of finance to industry and we may build a viable domestic carbon market in future on the foundations of industry interest as well as environmental protection.

### Expected Questions (Prelims Exams)

1. Consider the following statements and identify the correct statement.

1. The Kyoto Protocol is an agreement that obliges for the reduction of the emission of greenhouse gases.
2. The carbon emission limit has been fixed by the United Nations Framework Convention on Climate Change (UNFCCC).
3. Carbon trading means trading in carbon dioxide.
4. The carbon trading operates on the law of demand.

Code:-

- (a) 1, 2 and 3
- (b) 1, 3 and 4
- (c) 1, 4 and 2
- (d) 1, 2, 3 and 4

### Expected Questions (Mains Exams)

Q. 'Climate change is a battle whose the broader the financing is the easy it is to win.' Examine the utility of clean development mechanisms and other market-based resources in the context of this statement. (250 words)

**Note:** Answer of Prelims Expected Question given on 7 Oct., is 1 (c).