

28 October 2003

**UNICE POSITION PAPER ON LINKING THE KYOTO PROTOCOL MECHANISMS (JI AND CDM) WITH THE EU EMISSIONS TRADING SCHEME**

UNICE regards the proposed Directive<sup>1</sup> linking the Kyoto mechanisms (Joint Implementation - JI and Clean Development Mechanism - CDM) with the EU emissions trading scheme as an important tool that will provide a further opportunity to introduce more flexibility and to assist business in meeting its greenhouse gas emission reduction commitments in a cost-effective manner, thereby protecting EU international competitiveness.

We therefore support the Commission's objectives of contributing to global sustainable development and cost-effective emission reduction world-wide. Joint Implementation and the Clean Development Mechanism will be vital in the transfer of technology to both developing countries and countries with economies in transition (CEITs). Furthermore, they will generate funds that will assist developing countries in addressing climate change.

We believe that the following considerations should be taken into account:

- Flexibility would be reduced by introducing an artificial "cap" on the quantity of credits that can be converted to allowances

The introduction of emission credits into the EU Emissions Trading Scheme from JI and CDM projects should not be subject to artificial limits such as the "cap" on the number of credits recognised. We believe that recognition of credits should be based on the quality and not quantity of projects. The CDM Executive Board has proved itself very rigorous in its accreditation procedures. Such a "cap" will act as a disincentive to engage in sustainable projects due to the uncertainty in the convertibility of credits. This contradicts the Commission's objective of contributing to global sustainable development.

The "cap" will increase the costs to companies within Member States of achieving the reductions required under the EU Emissions Trading Scheme, which contradicts the Commission's objective of enhancing liquidity in the Emissions Trading Scheme. Furthermore, those companies within the scheme would be treated unfairly from those outside of it. We understand concerns have been raised that JI and CDM use will provide a disincentive to engage in domestic abatement measures. However, as the Commission admits itself, JI and CDM investment has been limited due to the uncertainties of the entry into force of the Kyoto Protocol; the potential transaction costs; the lack of capacity in many potential host countries as well as the overly complex procedures for the accreditation of small projects. Therefore the European Union should be looking to overcome existing barriers instead of imposing extra.

The setting of a "cap" is an attempt at steering the price of carbon on the EU market; this acts against the purpose of the Emissions Trading Directive which is to allow the free market to function and for companies to identify and develop the most cost-effective means to reduce emissions. It is also difficult to envisage how a European "cap" would be enforceable across

<sup>1</sup> Document COM 2003-403 final

Member States particularly if the “cap” was close to the limit and a determination had to be made as to which country was able to convert credits and which could not.

- The Linking Directive must not re-write the rules and modalities agreed under the Kyoto Protocol

The Directive must be consistent with the rules agreed under the United Nations Framework Convention on Climate Change, the Kyoto Protocol and the Marrakesh Accords that have been accepted by the EU. This particularly applies to project eligibility and the validity of credits. Deviation from the international rules would send a signal to the international community that would indicate that the EU was unwilling to conform to its internationally-agreed commitments. This could seriously affect the ratification of the Russian Federation and also the discussions of the Kyoto Protocol 2<sup>nd</sup> commitment period and the possible future commitments of developing countries.

- It should be possible to convert credits into allowances for the period 2005-7 or maintain the right to convert them in the 2<sup>nd</sup> period

Whilst it is not anticipated that there will any significant quantities of CDM certified credits available in the 2005-7 period, the use of these credits would provide extra liquidity to the EU emissions trading market. Furthermore, it would send a positive signal and could advance the development of future projects that would provide considerable environmental, social and economic benefits.

JI and CDM credits provide an important incentive to developing countries and CEITs to engage in projects that assist in combating climate change and promote sustainable development.

- The Linking Directive is an opportunity to encourage the ratification of the Kyoto Protocol

The European Union, through the introduction of this linking Directive, has an opportunity to encourage such developments and bring about the ratification of the Kyoto Protocol. The Directive also may contribute to minimising the costs of compliance for European business and help to maintain their competitiveness in international markets.

- Conversion of credits from the Kyoto project mechanisms shall be possible between countries which have ratified Kyoto Protocol prior to its entry into force

Emissions trading directive will be reality even if the Kyoto Protocol does not come into force. If credits from the project mechanisms are not available, the EU has taken only the reduction commitments of the Kyoto Protocol but not the flexibility that was built in to assist cost-effectiveness. Such a situation will be very harmful to the competitiveness of European industry. To avoid this situation, prior to the entry into force of the Kyoto Protocol, the JI/CDM Linking Directive should provide a mechanism for the conversion of credits from projects between countries that have ratified the Kyoto Protocol.

With the inclusion of the above points, UNICE supports the rapid passage of the Linking Directive through Council and Parliamentary procedures in order for it to enter into force in parallel with the EU Emissions Trading Directive.

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