Event Proceedings

Carbon Markets for the Poor: A Contradiction in Terms?
Panel Discussion and Public Debate

Tuesday 15th November 2011
UEA London Study Centre, 102 Middlesex Street, London

Event Overview
Ahead of the Climate Summit in Durban in November 2011, this event considered whether the commitment to carbon markets as a central response to climate change is the right approach. Discussion focused on the provision of sustainable development benefits in developing countries under the Clean Development Mechanism (CDM), and the role of governance from local to international level in determining the distribution of benefits from the CDM. The summary below reflects the fact that the event was conducted under Chatham House rules, to facilitate open and frank discussion. Comments are not attributed by name or institution.

Chair
Simon Maxwell, Overseas Development Institute

Panellists
Michael Grubb, University of Cambridge and Climate Strategies; Steffen Böhm, University of Essex; Emily Boyd, University of Reading; Adrian Rimmer, Gold Standard Foundation; Peter Newell, University of Sussex. Also present to comment: Martin Hession, Chair of the CDM Executive Board.

Introduction
It was suggested that this was a key time to reflect on these issues in advance of COP17 in Durban, the end of the first commitment period of the Kyoto Protocol in 2012, recent controversies that have shaken faith in carbon markets and the start of the CDM Executive Board's own policy dialogue on many of these issues. The key conclusions of the Governance of Clean Development Project were presented, based on findings in India, Argentina and South Africa and outlined in a project briefing *Governing Clean Development: What Have We Learnt?* Both the presentation and the project briefing can be viewed online at clean-development.com. The central research question was outlined: *Which features of the actors, institutions and policy-making processes involved in the governance of clean development are resulting in effective outcomes in terms of climate action and developmental benefits, which are not and why?...and what can be done about it?*

The presentation emphasised the links between process (who decides key decisions) and distribution (who gains and who loses from CDM projects). Key findings included the need for strong, independent and credible institutions at local, national and international level; the lack of attention to governance issues at the local level including consultations, monitoring and evaluation of project outcomes; how the range of policy tools that governments can utilise to secure development benefits from the CDM is restricted by the power they have to direct private investment; the often minimal role that the CDM currently plays in investment decisions and the need to create powerful coalitions of the 'winning' and 'willing' that have an interest in transforming the energy sector through carbon finance; the effect on the CDM's environmental integrity of the inappropriate use of CDM finance in indirectly supporting fossil fuel energy production; how the CDM can be aligned with and add value to more significant national policy initiatives; and the crucial role of governance reform in effectively meeting climate and development goals under the CDM and beyond as required by the mandate of the Kyoto Protocol.

Panellist and audience discussion:
Discussion began with a focus on the diagnosis of key problems and understanding of how the CDM market is currently functioning.

On adaption and the CDM
The need for the CDM to promote 'climate compatible' development was noted, but several contributors preferred to avoid what was seen as the mixing of distinct mitigation and adaptation objectives. While some proposed concrete ways of supporting adaptation projects through carbon finance, concern was also expressed as to whether market mechanisms are an effective or equitable way to achieve the aims of adaption, particularly for the poor who are most vulnerable to climate change.

On agriculture and the CDM
CDM finance for agriculture projects was discussed as a means to create greater 'pro-poor' benefits from the CDM, given how the large numbers of poor people that depend on agriculture for their livelihoods. But many difficulties were noted, many of which stem from attempts to apportion value to just one aspect of a complex agricultural system. Issues include the extra difficulty of proving additionality in agriculture projects; cases of displacement of people from land in favour of clean (or non-clean) energy or agricultural projects; and the (non)permanence of agricultural practices or forestry projects themselves. A further comment suggested that these difficulties are to be weighed against the potential gains of providing more sustainable financing than would otherwise be possible through public finance.

On collusion in carbon markets
Cases of collusion between Designated Operational Entities (DOEs) and project developers and the revolving door between government and private sector roles (trading, consultancy, project development, auditing etc.) in the CDM were described from one perspective as a result of the limited capacity of various CDM institutions and from another as a more simple case of corruption.

On local governance
The involvement of local people in project consultation and design was suggested as essential to ensure local benefits and to effectively reduce emissions. The deficit of knowledge on the engagement of local institutions with other carbon market actors and their role in determining the outcomes of CDM projects was noted and linked to a call for more research into local institutions under the CDM. It was also noted that there is a current lack of systematic evidence on the co-benefits of CDM projects, in part due to the lack of a requirement to monitor the sustainable development outcomes of CDM projects. Alternatively, it was suggested that carbon markets are being rejected as a legitimate response to climate change by local communities in both the North and South, and that a better approach would be to scale up existing low carbon practices.

On the record of carbon markets in reducing emissions
It was argued by one speaker that carbon markets have failed to meet emissions reductions goals, having been implemented over a period in which emissions have continued to grow in both developed and developing countries. This account was contested based on the findings of previous research on the role of carbon markets in driving low carbon technology development in developing countries, predominantly China and India. It was also suggested that the CDM is not intended to solve climate change alone and that many of the issues that have arisen are not unique to carbon markets but are instead problems of international capitalism and investment, such that the CDM itself has not caused many of the issues raised.

On trade-offs between emissions reductions and sustainable development outcomes
It was noted that many of the governance issues discussed arise from the difficult political space that the CDM occupies in attempting to meet large scale emissions reduction goal and promote sustainable development simultaneously. It was noted that increasing the demands on the CDM to demonstrate benefits to the poor increases costs. In this respect, emissions avoidance was described as the primary goal of the mechanism and that Executive Board activities predominantly focus on this aspect of the mechanism in responding to calls for governance reform. Also noted was the dependence of the Executive Board on political support from national

governments in order to drive governance reform. There were differing opinions over whether the CDM should strive to be a pro-poor mechanism, or whether an international market mechanism should be recognised as unsuitable for delivering social goals on a large scale.

On CDM sustainable development criteria

It was noted that international demands for stronger sustainable development criteria in developing countries would likely be perceived and experienced as financial conditionality in developing countries. Determining who could and who should make decisions on issues of better governance is therefore crucial. An alternative position suggested that sustainable development priorities could be assessed more broadly to include a wider range of stakeholders within developing countries such that CDM goals gain wider public support and benefit a larger number of people, many of whom are not represented in current CDM governance procedures. One contributor emphasised that additional checks (such as Environmental Impact Assessments) are required of CDM projects that are often not monitored when projects are financed by other means, such as Foreign Direct Investment. Alternatively, it was argued that the operation of the CDM market is (and will continue to be) determined by Annex 1 country demands for cheap emissions reductions, not the actions of developing country governments, who have no incentive to promote sustainable development in projects.

On labelled projects

The Gold Standard label was promoted as a means to meet the twin goals of the CDM more effectively. It was described by another commentator as a niche product that would remain marginal in a market driven by the pursuit of low cost emissions reductions. The voluntary carbon markets were suggested as a site of innovation from which many CDM methodologies originate and from which the CDM can learn lessons.

On 'pro-poor' CDM

It was suggested that it is legitimate to question whether markets should aim to serve the poor, as previous experience of market mechanisms suggests that a trade-off between emissions reductions and development is to be expected. Markets were described as amoral by nature, with their governance determining whether they are moral or immoral in practice. Several contributors noted the differing vision of various CDM stakeholders on what goals CDM finance should pursue. Support was expressed for the role the CDM has played in boosting renewable energy in India and China, while a counter position suggested that in most cases the CDM has provided the 'icing on the cake' of clean investment rather than being transformative. Examples of projects with negative outcomes for local residents were cited. In response, strong local governance was reiterated as essential to ensure that projects do not disadvantage local livelihoods.

On EU credit sourcing from Least Development Countries

The EU decision to restrict credits to Least Development Countries from 2013 received a mixed level of support, with some welcoming increased finance for poor countries and others noting the mitigation potential in middle income countries and the opportunities for pro-poor projects in countries such as India and Kenya. Governance challenges in countries with low institutional capacity were also raised as key issues in coming years.

On additionality and uncertain quantification of emissions reductions

It was suggested that more cost effective emissions reductions would always have most difficulty proving additionality and that the market needs to be adaptive enough to recognise technologies approaching commercial viability. The decision of the Executive Board to reject several Chinese wind projects was cited as an example of the Board responding in such a way to changing market conditions. Others drew parallels between the carbon market and the sub-prime financial crisis in the US, based on the questionable valuation of credits.

On gas flaring projects

The legitimacy of projects that reward oil companies in Nigeria with credits for reducing gas flaring was questioned due to the existence of national regulations that address the issue. This was described as additional income for transnational companies not complying with national law, thereby creating perverse incentives. In light of the long-term non-compliance of companies with local regulations, it was alternatively described as an environmentally beneficial project where baseline emissions would remain high in the absence of CDM finance.

On UK Carbon Budgets and offsets

It was suggested that the UK's carbon budgets are inadequate and that the CDM further reduces their effectiveness by allowing questionably quantified offsets to be used against commitments. Others felt that Annex 1 country targets should be higher but should also retain an offset component as a source of finance for low carbon development in developing countries. This point was contested in the case where polluting companies can use the Public Relations value of offsets to relieve pressure on domestic mitigation action.

A straw poll of the audience indicated the majority were sceptical about the performance of the CDM to date. The second part of discussion focused on why the market has come to take the form described in earlier discussion and ways forward.

On the causes of the uneven geographical distribution of CDM projects

Causes were suggested that included both investment-related factors and issues specific to CDM governance, including: the significance of institutional capacity and level of oversight from Designated National Authorities (DNAs); the existing physical, political and financial infrastructure of leading host countries such as China and India; the significant financial and institutional capabilities of domestic companies and public utilities in industrialising countries compared to Least Developed Countries; the perception of high risk investment environments in some countries; and the existing and changing networks of individuals and institutions that are important in shaping where investment flows.

On the role of political interests in shaping CDM outcomes

Several contributors noted that the current CDM is shaped by political interest groups whose current power to determine the structure and governance of the market – including their representation in key decision making forums – shapes the distribution of benefits from the CDM.

Suggestions for reform or next steps

Asked for ways that the CDM can improve on both environmental and social grounds, audience and panellist suggestions covered:

Potential immediate reforms included: creating a seat on the CDM Executive Board for an NGO representative and voluntary market representative; requiring DOEs to ensure sustainable development benefits of CDM projects; withholding a percentage of credits if sustainable benefits are not adequately demonstrated; and establishing independent DOEs, paid for through the Executive Board in order to address collusion in the validation and verification of emissions reductions.

Broader changes in procedures and governance included**:** greater attention to the local institutions involved in CDM governance; further systematic research on the impacts of the CDM on poverty alleviation; greater monitoring and valuation of the development benefits of projects outside of labelled projects; and retaining the separation of mitigation and adaptation goals in future forms of market mechanisms.

Suggested requirements for more fundamental changes in carbon markets and beyond included greater attention to the political institutions that shape how the market functions and the possibility of building a coalition of public and private institutions with an interest in reducing emissions, such that the CDM can become a significant lever for change in mainstream economies. Others favoured recognising the structural limitations of the CDM, abandoning offsetting and refocusing efforts on existing examples of sustainable living; consideration of the trade-offs inherent in the CDM and the limitations of agendas to pursue all goals simultaneously; and increasing Annex 1 emissions reduction commitments to deliver a 2 degree target at the UNFCCC.

Participants were encouraged to engage with the UNFCCC's current *CDM Policy Dialogue* process by submitting comments on the past and future of the CDM.