

## COPENHAGEN 2009: POLITICAL RISKS BRIEFING

### Summary

The effort to reach agreement on the next phase of the global regime to tackle climate change that will culminate in Copenhagen<sup>1</sup> in December this year is arguably the most complex international negotiation ever attempted. Its success or failure will have very far reaching consequences for human prosperity and security. These negotiations are taking place against a back ground of growing concern within the scientific community that climate change is occurring more rapidly, and that its impacts on humanity are sooner and greater, than previously anticipated. The gap between the action needed to avoid dangerous climate change and that yet being taken politically is widening.

Three political forces will shape the prospects for a successful outcome:

- > the pressure to arrive at an agreement that moves the world beyond the current regime in terms both of level of ambition and inclusiveness of participation by December;
- > the re-entry of the United States into the effort to construct a global regime to tackle climate change;
- > the impact on the politics of climate change of the depth and length of the global recession.

The interaction between these major political factors will add further complexity to already an already difficult process. Furthermore, there are five emerging tensions which could distract or derail the negotiations by further compounding the scope for

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<sup>1</sup> The fifteenth meeting of the Conference of the Parties (COP) to the United Nations Framework Convention on Climate Change (UNFCCC) will take place in December in Copenhagen. It will be preceded by several other important meetings which will play a significant part in shaping the outcome of COP 15. These include the G20 economic summit in London in April, the G8 meeting in Italy, a new version of the Major Economies Meeting convened (probably under a different name) by the US and a possible special summit to be convened by the Secretary-General of the United Nations. In addition there will be other important meetings between national leaders bilaterally at which climate change will be on the agenda, including those between the EU and China, the US and China and the EU and the US.

misunderstanding or mischief. The tensions generated by these issues are potentially highly disruptive to the focussed political effort needed to reach agreement.

These are:

- > the choice of carbon taxation or emissions trading as the preferred policy option;
- > an extension of the Kyoto Protocol or the negotiation of a new Protocol which might or might not include the Kyoto mechanisms;
- > whether to base climate policy on emissions targets or cumulative carbon burdens;
- > the primacy of mitigation or adaptation ( including geo-engineering ) as the focus for policy;
- > whether carbon burdens should properly be counted at the point of production or the point of consumption.

Together these three forces and five issues make up a political risk landscape that must be successfully navigated in order to reach a worthwhile agreement in Copenhagen. It will be important for political leaders to cut through this morass of issues to ensure that the three most essential elements of progress are achieved. These are:

- > the preservation and strengthening of the Kyoto mechanisms so that there continues to be a carbon price;
- > sufficient genuinely additional funding for adaptation and technology transitions in the developing world to ensure agreement;
- > an alignment of timetables so that the US can successfully rejoin the global regime.

## Science

The sense of urgency among climate scientists has grown consistently since the publication of the Fourth Assessment Report (AR4) of the Inter-Governmental Panel on Climate Change (IPCC) in late 2007. This is a consequence of increased knowledge of the climate system and its interactions with other global systems and of the impacts of those interactions on human well-being. In short, climate scientists now believe that

the climate is more sensitive to greenhouse gas forcing and that the response of other geochemical and ecological systems is stronger and faster than was thought in 2007<sup>2</sup>.

As a result the impacts of climate change on human well being will be greater and sooner than previously anticipated. The phenomena of most concern to the scientific community include:

- > the more rapid retreat of mountain glaciers threatening the water supply of billions of people;
- > the more rapid than projected melting of Arctic sea-ice in summer opening new flashpoints for resource conflict;
- > the increased acidification of the ocean threatening both reduce the oceans capacity to absorb carbon and to undermine the productivity of marine ecosystems;
- > the pole-ward expansion of the sub-tropical zone bringing droughts and fires to heavily populated areas;
- > the accelerated melting of the Greenland and Antarctic ice sheets increasing the rate of sea-level rise above that projected;
- > the increased intensity of hydrologic extremes increasing both: heavy rains, storms and floods, and drought and fires.

There are many other observations pointing consistently to the conclusion that the adverse impacts of climate change on human well-being are already detectable and are increasing more rapidly than previously thought. This reinforces the judgment of the EU that the primary goal of climate policy is to keep the eventual rise in global average temperature to below 2°C. There is now an emerging view within the climate policy community that avoiding dangerous climate change will require an 80% reduction of total global greenhouse gas emissions by 2050.<sup>3</sup>

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<sup>2</sup> 'the disruption and its impacts are now growing much more rapidly than almost anybody expected even a few years ago. The result of that, in my view, is that the world is already experiencing "dangerous anthropogenic interference in the climate system."' John Holdren, President Obama's Science Advisor, January 17th 2009

<sup>3</sup> Martin Parry, Climate Policy 2008. This is greater than the aspirational target of 50% of greenhouse gas emissions emanating from political agreements within the EU and the G8. It is often overlooked that an 80% reduction of total greenhouse gas emissions is tantamount to a 100% reduction in emissions from the global energy system because of the difficulty of reducing the emissions from agriculture, deforestation and land-use change which are roughly equivalent to the current capacity of the oceans and vegetation to absorb carbon.

This has led to a growing perception among scientists, climate policy analysts, the media and other opinion formers that **the gap between the action on emissions implied by our knowledge of the science and the political effort required to reduce emissions and re-stabilise the climate is continuing to widen.**

The current policy regime is essentially that constructed in the wake of the Kyoto Protocol. It was built at a time when climate change was still seen predominantly as an environment issue. It is still largely driven by environment ministers who have neither the political muscle nor the intellectual and financial resources to address what is now seen more clearly as a core prosperity and security issue.

These anxieties have been compounded by the speed and severity of the global recession that accelerated rapidly in the second half of 2008. Although this will lead to fall in the growth of emissions, it could also distract political attention and delay action to beyond the point at which there is any realistic chance of keeping the eventual rise in global average temperatures below 2°C.

### Politics

The politics of climate change in 2009 will be shaped predominantly by three forces: the drive to achieve a 'global deal' at COP 15 in Copenhagen; the re-entry into the global climate regime of the United States and the response by the international community to global recession. There is also a series of emerging issues that could distract, or even derail, efforts to reach the political and legal agreements necessary to respond to the growing urgency of the problem. These are: the choice of carbon taxation or emissions trading as the preferred policy option; an extension of the Kyoto Protocol or the negotiation of a new Protocol which might or might not include the Kyoto mechanisms; whether to base climate policy on emissions targets or cumulative carbon burdens; the primacy of mitigation or adaptation ( including geo-engineering ) as the focus for policy and whether carbon burdens should properly be counted at the point of production or the point of consumption.

## Copenhagen

The Copenhagen negotiations, guided by the Bali roadmap, are among the most complex ever undertaken. The goal is to achieve a so-called 'global deal' in which the industrialised world agrees to a second commitment period under the Kyoto Protocol and agrees to provide finance for adaptation<sup>4</sup> and the transfer of low carbon technologies in return for rest of the world undertaking 'monitorable, reportable and verifiable' commitments to reduce their emissions. In reality there are two main, and a number of related negotiations, including those on forestry, going on separately under the same umbrella without, as yet, a clear mechanism for bringing them all together.<sup>5</sup>

The political conditions for achieving such a deal at a level of ambition sufficient to avoid dangerous climate change do not yet exist. In other words, the internal alignment of key constituencies within the major economies is not such as to make it politically possible for them to agree such a 'deal'. This is as true within both the developed as developing world economies. The onset of the global recession has, in the eyes of many commentators, made the achievement of those conditions by the end of the year less likely.

National leaders are distracted by the need to engineer an economic recovery. They are increasingly unwilling to impose constraints on economic growth. Furthermore, public finances are already over-stretched by the loss of tax revenues and urgent need to finance economic stimulus packages. This considerably narrows the scope for agreement on the necessary funding for adaptation and technology transfer. Proposals for financing such capital flows rely heavily on a carbon price or permit auction revenues which are themselves dependent on the agreement by the industrialised countries to a second commitment period under the Kyoto Protocol.

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<sup>4</sup> Given that some degree of climate change is now inevitable and that its adverse effects are likely to fall hardest on those who have contributed least to its cause and who are least able to meet the significant additional costs of adaptation, it is difficult to see how agreement by some of the key developing countries, including very large countries like India and Indonesia, could be politically deliverable domestically without large flows of real and additional capital from the industrialised nations.

<sup>5</sup> The Annex 1 negotiations on the next round of emissions targets for the industrialised nations are being conducted under the Kyoto Protocol. The negotiations on additional commitments by the non-industrialised world and those industrial countries – principally the US – that have not ratified the Kyoto Protocol are being conducted under the Framework Convention itself.

There is thus a considerable risk of a chicken and egg impasse. The first commitment period under the Kyoto Protocol expires at the end of 2012. Two years is the time typically needed to go from reaching such an agreement to its binding commitments coming into force<sup>6</sup>. Delay beyond the end of this year therefore risks undermining the revenues flows needed to get agreement in the first place.<sup>7</sup>

While previous experience suggests that there is some margin to continue negotiating beyond the end of the 2009 this margin is small. In any case, **uncertainty as to whether or not there will be a second commitment period will lead to future carbon prices being discounted well before the negotiations conclude**. This would in turn lead to pressure for a more direct, but less politically deliverable, sourcing of the capital flows to the developing world needed for agreement on the 'global deal' to be reached.

Balanced against this gloomy prognosis is the re-entry of the United States into the constructive development of the global climate regime. The Bush Administration acted as a considerable brake on the development of the political conditions for effective action on climate change, both directly by creating friction within the international processes tackling the issue and indirectly by providing political cover for other nations seeking to impede an urgent response. There is no doubt, both from President Obama's campaign pledges, from the inclusion of a number of references to climate change in his inauguration speech, and from the number of climate related decisions announced during his first week in office, that his Administration will now play a full and leading part in addressing this issue globally.

However, this will not be an unmixed blessing and the re-engagement will need to be skilfully handled to avoid creating new problems as it solves those which are familiar. Politically, President Obama has pledged to reduce US domestic emissions to 1990 levels by 2020 and to aim for a reduction of 80% from present levels by 2050. This is an ambitious goal which converges on that of the EU albeit on a different trajectory. To

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<sup>6</sup> International agreements come into force only when a specified number of the parties to that agreement have deposited instruments of ratification with the United Nations. Methods of ratification vary between countries but often require parliamentary confirmation.

<sup>7</sup> The existing EU ETS commitments are legally binding within the EU whether or not there is an agreement to a second commitment period under the Kyoto Protocol. However, especially in the current economic circumstances, any failure to reach agreement on a second commitment period would inevitably lead to pressure to weaken those commitments. They would not, in any case, provide significant capital flow to the developing world.

deliver it will require very tough Federal legislation which a majority of commentators in the US think is unlikely to pass this year. There is also a widespread view that the US will not enter into binding international commitments until it has settled its domestic legislation. This would avoid the risk of repeating the Kyoto experience of negotiating an agreement in good faith only to be unable to achieve ratification by the Senate.<sup>8</sup>

**Should this prove to be the case, the US would not be in a position to join the other Annex 1 countries in agreeing to a second commitment period under the Kyoto Protocol in Copenhagen.** This is another reason for anticipating that reaching a final agreement might spill over into 2010. It is widely expected that a core condition for achieving agreement to a 'global deal' in Copenhagen by the major developing countries such as China, India and Brazil, will be US agreement to binding targets. Thus a successful 'deal' might require a difficult to accomplish alignment of timetables of the UN treaty process and US domestic legislative process.

### Stimulus

The depth of the global recession and the need for governments to agree stimulus packages of unprecedented size is also double edged. The scale of the economic crisis and its immediacy inevitably shifts political focus from the as urgent, but less immediate, need to tackle the intimately entangled challenges of energy and climate security. This reinforces an understandable political reluctance to impose emissions targets which put growth at risk<sup>9</sup>. This has emboldened those economic interests whose businesses would be subject to large scale change under pressure to reduce emissions and thus weakened the political conditions needed to support a sufficiently ambitious agreement in Copenhagen. These dynamics were already quite visible in the political effort to finalise agreement on the 20-20-20 package with the EU and are likely to grow as the recession deepens.

Conversely, as the Obama Administration has already indicated, the need for an unprecedented economic stimulus to the global economy has created an unlooked for

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<sup>8</sup> It is early days in the Obama Administration and a lot could happen to change these perceptions, either reinforcing or neutralising their impact on the US position in Copenhagen. Much will depend on the Administration's overall political success in this very difficult year.

<sup>9</sup> This will be particularly true in China where the current levels of urban unemployment are at a level which threatens political instability and current growth projections are well below those widely thought to be necessary to maintain political stability in China.

opportunity put the world onto a path to achieve economic, energy and climate security simultaneously. **Massive investment in a business as usual, carbon intensive recovery would not only undermine the prospects for Copenhagen, it would also put the recovery itself at risk.**

The sharp fall in the oil price, the difficulty and cost of obtaining capital and the uncertainty about the length and depth of the recession have frozen investment in oil and gas production. This increases the risk that a rapid recovery that is carbon intensive would be stalled by a sudden and sharp spike in the oil price as demand recovered far faster than was possible for production. An alignment of the global stimulus packages along a trajectory that reduced oil and gas dependence would both reduce carbon emissions and improve the political conditions for an ambitious agreement in Copenhagen. **This makes the G20 economic meeting in London in April and the processes that flow from it potentially an important part of the effort to reach agreement on climate change.**

The Obama Administration has already made clear its intention to design its \$800 billion stimulus package along such a path. It is also becoming clear from the latest economic analyses that this may be less than half the eventual size of the stimulus that might be needed for recovery of the US economy. Alignment of the EU and Chinese stimulus packages in a similar direction could lead to an overall global stimulus in its first phase of some \$2 trillion. Investing a significant proportion of this spend on increasing resilience of the global economy to oil and gas price shocks would go a long way to kick-starting the transition to a low carbon economy and thus to making an agreement in Copenhagen more possible.

It is difficult to imagine another opportunity of this magnitude arising in time to make the investments necessary to avoid dangerous climate change. **Such a failure would expose businesses everywhere to a much increased risk that when governments did act decisively on climate change they would do so more precipitously and at considerably greater cost than otherwise.**



### **Political Risk**

Travelling across this landscape of political risk and opportunity will be difficult enough if all that was involved was the successful harnessing of these three dynamics. Unfortunately, there is a series of emerging issues that threaten to complicate this picture further if they are not well understood and integrated successfully with the existing agenda.

### **Trade or tax?**

There is a growing debate about whether the world should rely primarily on a carbon trading or a carbon tax as a primary instrument of public policy on climate change. Carbon trading is the approach now embodied in the Kyoto Protocol and the EU.ETS, in Australia and many of the US legislative proposals. It has the benefit of a predictable – if not necessarily adequate – environmental outcome won at the cost of uncertainty about the carbon price and high transaction costs.

An increasing number of influential academic, business and political voices, especially in the US, are beginning to argue that a carbon tax would be a simpler, more predictable and more transparent policy tool. In practise, both approaches are over-reliant on a difficult to adjust carbon price to drive the high capital, long-life technology investments needed to drive down emissions in time to avoid dangerous climate change. There is a risk both that such a debate could further congest an already difficult negotiation and obscure the increasingly clear perception that a carbon price alone, at any politically deliverable level, will not be enough to drive the transition to a low carbon economy and will thus need much greater support from both regulatory measures and public expenditure.

### **Existing or New Protocol?**

There is also a debate emerging within the climate policy community, particularly in the United States, about whether what should be under negotiation in Copenhagen is the legally required second commitment period of the Kyoto Protocol or some wholly new treaty which would, in some as yet unexplained way, either incorporate or replace

the Kyoto mechanisms. Casual and inaccurate reporting in the media has created a widespread impression that the Protocol itself expires in 2012. This is not the case.<sup>10</sup>

Nevertheless, there is a growing debate about a replacement or successor to the Kyoto Protocol. Furthermore, there are a number of voices in the US and elsewhere beginning to argue that the approach embodied in the Protocol is too limited to achieve the goal of avoiding dangerous climate change. Rather than trying to seek difficult agreement about emissions reduction targets for all nations it would be better to recognise the big differences between nations and allow for a more variable geometry to the commitments they were asked to make. In this approach there would be agreement about the policies and measures to be adopted by groups of nations who would make a commitment to reach an agreed level of reductions within an agreed timeframe<sup>11</sup>.

There is a risk of confusion among the parties in Copenhagen about what exactly they are negotiating. This could be thought to be the required second commitment period to the Kyoto Protocol or a wholly new Protocol or an amended version of the Kyoto Protocol or some hybrid between the any of the above. This will allow considerable scope for misunderstanding, and possibly mischief, to impede progress.

### Emissions or cumulative carbon?

A debate is also growing within the scientific community about whether the effort to control annual greenhouse gas emissions uses the right metric for policies to tackle climate change. The relationship between levels of carbon emissions, with can vary with both the overall level of economic activity and the structure of that activity, and the increasing carbon burden in the atmosphere is complex and allows for a wide variety of emissions reductions trajectories to deliver a given climate outcome. What really matters is not so much the level of carbon emissions but, because of the long

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<sup>10</sup> The parties to the Kyoto Protocol undertook a binding obligation to negotiate a second commitment period after the end of the first commitment period in 2012. These negotiations are underway. They are not time limited and, in principle, could continue *sine die* if agreement is not reached. There is no specific requirement for the second commitment period to be contiguous with the first. The Kyoto Protocol remains in existence whatever the fate of the negotiations on the second commitment period and the parties to it remain bound by its obligations. They can, of course, amend the Protocol or withdraw from it.

<sup>11</sup> This is the so-called 'pledge and review' approach based around negotiating agreements on policies and measures rather than quantified emissions reductions obligations. It was the approach initially proposed by the EU for adoption in the Kyoto Protocol and opposed, successfully, by the United States.

lifetime of carbon in the atmosphere, the cumulative burden of carbon in the atmosphere.

The attempt to control emissions year on year is thought by some to be too indirect a way to manage the cumulative carbon burden in the atmosphere. In this view there would be a clearer and more effective link between climate policy and climate outcomes if policies were formulated around the allocation of a carbon budget shaped by the amount of additional carbon that could be allowed to accumulate in the atmosphere before remaining below a desired threshold, 2°C, for example, became unlikely.

Neither choice would remove the underlying political difficulty of reaching agreement on the relative effort to be made by different countries but it would change the terms of the debate. There are already tensions over how to deal with historic as well as current contributions to the total carbon burden. Some countries could come to see political attractions in framing the debate one way rather than another and thus complicate the task of reaching agreement.

### Mitigation or Adaptation?

There is already a mounting debate about the relative effort that should be applied to preventing a further rise in the concentration of greenhouse gases in the atmosphere ( mitigation ) and that to coping with the climate change to which the world is already committed ( adaptation ). Clearly, for those countries with low emissions but a high exposure to climate change, adaptation is a priority. For others, with relatively low exposure to a changing climate or higher capacity to adapt, mitigation in order to prevent longer term, and possibly unmanageable climate change, is a priority.

This dynamic has recently been reinforced by a developing current of opinion within the scientific community that it is already too late to prevent dangerous climate change by controlling emissions. Instead, some argue, effort should now be concentrated on developing technologies for removing, or off-setting, the carbon burden in the atmosphere. Particularly at a time when the financial and technical resources available to deal with this problem are under great pressure, there is a risk of this debate polarising opinion around false choices. **Choosing only to adapt runs a risk of climate change becoming unmanageable by even the most capable and**

**least exposed of nations. Choosing only to mitigate risks not being able to create sufficient unity within the international community to limit the danger.** Global efforts to both mitigate and adapt may not be ambitious and timely enough to avoid some future need for geo-engineering to retain some measure of manageability of climate change.

### Consumption or Production?

As China has become the world's largest current emitter of greenhouse gases it has come under increased pressure to act more aggressively to reduce its emissions. This pressure is largely unwarranted. The cumulative contribution of a nation to the total carbon burden has far more impact on the climate than current emissions. (On this measure Britain – as the birthplace of the Industrial Revolution - is still the largest contributor to the carbon burden.) In response, China has taken to pointing out that its high emissions are a consequence of the huge volume of trade it does with other countries.

This raises a much overlooked issue about whether the correct point at which to count carbon emissions is the point of production or of consumption. The Chinese view is consistent with the 'Polluters pay' principle that is the widely accepted basis for most national and international environmental law. On this view, responsibility for carbon emissions associated with the production of a good would be 'embedded' in that good and passed through to the final consumer in much the same way as VAT is passed through. It is likely that this argument will gain more prominence as the Copenhagen negotiations progress and the pressure for China to take on binding commitments increases<sup>12</sup>.

### Outlook

This combination of three intersecting forces and five emerging issues makes for a very difficult process to manage and a very high level of uncertainty about the outcome. It will be very important over the course of this year to manage expectations successfully. **The greater the gap between expectations and what can realistically be accomplished, the higher the risk of an outcome that works better in the**

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<sup>12</sup> The need for full Chinese participation has been a recurrent refrain in US discussions of the Copenhagen outcome. In the current economic circumstances this note is likely to grow louder.

**headlines than in the real world. This would be the worst of all worlds, undermining political momentum on climate change without compelling actions of sufficient ambition to secure a stable climate.**

There is a clear need to avoid an over-focus of effort on the negotiations themselves. All negotiations run the risk of becoming inward and obsessive leading to effort becoming confused with achievement. This is particularly true of negotiations as technically complex and politically difficult as those leading up to COP15. The scope of what it is possible to achieve in the negotiations will be determined by the success or failure of the effort to build the political conditions within each of the main economies. This will require a sustained effort, of the kind currently being undertaken by the UK, running parallel to the negotiations themselves.

Currently the range of possible outcomes stretches from significant breakthrough to complete collapse. Much will depend on how well the political leadership of the major countries understand the complexities of the problem and how effective they are at cutting through them to reach agreement on the essentials: preservation of the Kyoto mechanisms so that there continues to be a carbon price, sufficient additional funding for adaptation and technology transition in the developing world and successfully aligning timetables so that the US can again become a full participant in the global regime. This would not solve the problem, but it would keep open the door to their solution. Even so, getting to this point will require a concentrated drive by national leaders to use the stimulus packages to construct the domestic political conditions necessary for agreement in Copenhagen.

Tom Burke

London

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Tom Burke is a Founding Director of E3G and a Visiting Professor at Imperial and University Colleges, London.