

RECORD TYPE: PRESIDENTIAL (NOTES MAIL)

CREATOR: John D. Gibson (CN=John D. Gibson/OU=WHCCTF/O=EOP [WHCCTF])

CREATION DATE/TIME:21-JAN-1999 10:27:50.00

SUBJECT: Notes from diplomatic strategy meeting

TO: Todd Stern (CN=Todd Stern/OU=WHO/O=EOP @ EOP [WHO])

READ:UNKNOWN

CC: Dirk Forrister (CN=Dirk Forrister/OU=WHCCTF/O=EOP @ EOP [WHCCTF])

READ:UNKNOWN

TEXT:

Attached are a write up of my notes from Saturday's diplomatic meeting.

Let me know if you want them "processed" any further. jdg===== ATTACHMENT 1

=====

ATT CREATION TIME/DATE: 0 00:00:00.00

TEXT:

Unable to convert ARMS_EXT:[ATTACH.D91]MAIL41964812M.036 to ASCII,

The following is a HEX DUMP:

**NOTES FROM DIPLOMATIC STRATEGY MEETING
1/16/98**

Topics: Emissions Trading & CDM

Participants:

Todd Stern
Rosina Bierbaum
David Festa
David Gardiner
Bob Perciasepe
David Hales
Julie Anderson
Jeff Frankel
Melinda Kimble
David Doniger
David Sandalow
George Frampton
Frank Loy
Mark Mazur
Dirk Forrister
TJ Glauthier
John Gibson
Roger Ballentine
Beth Arner
Mike Orfini
Ron Minsk (invited -- attended?)

T Stern ("TDS"): Purpose of meeting is to identify our diplomatic objectives (on trading and CDM) and formulate plan to achieve them. Premise is that if we just repeat our talking points over the next two years in communications and at diplomatic meetings then we aren't likely to achieve our objectives.

F Loy: We also need to get to a 3rd point. Need to understand that the framework is not likely to change unless we contemplate positions we haven't. Need to try to get a breakthrough. It may be that we decide to simply bull our way through keeping our same positions, but right now we need to be creative and consider new positions.

M Kimble: Need to remember that we have an Umbrella Group position on trading. Important to realize that we will undermine the Umbrella if we shift our position w/o bringing them along. Example is liability -- Umbrella position is that seller should be liable.

D Sandalow: Most of our problems on emissions trading stem from lack of understanding. We need an emissions trading communications strategy, but also a constituency strategy for reaching out to various groups.

TDS: Are there any other issues that are important under these two broad categories (trading and CDM) that are not on the agenda? My assumption is where we butt heads most directly is on trading caps. Russian hot air follows from this. If there were no hot air we would still have a problem on caps but less so. Liability is also an important issue as is equity.

D Hales: Transfer tax also issue.

TJ Glauthier: Secretary Richardson also wants there to be a focus on process. There are lots of meetings happening -- bilats, regular meetings, trips to developing countries, etc. -- important for us to have a plan on what is going to be said/done at these meetings.

TDS: Yes, good point. But probably better to cover those concerns at the developing country strategy session.

G Frampton: Let me ask very simple question. If Russian hot air is the source of most hostility on trading, then if we are willing to accept limits of some type on how much hot air we will buy, is that inconsistent with our position on caps?

Group Response: Yes!

D Hales: There is an idea out there, however, for a tax of some type on emissions trading with the proceeds going into some type of fund.

G Frampton: It seems that free trading on allowances is the Holy Grail for us -- why?

M Kimble: We need to realize that if you talk about these issues in a vacuum w/o a discussion of monitoring, registries, etc. then it's a very frustrating conversation. If you address these issues then you can give some confidence to skeptics that you aren't double counting and go from there. Larry Summers has been emphatic -- "We need a source to buy from in the first budget period. Need to give time for the transition." Once you have monitoring and enforcement you can go from there -- it will give people confidence.

G Frampton: If you have this system, do we still say we need 60% from hot air? Can't we accept some cap like 25% or something? [unclear whether he meant that US gets 60% of its allowances from hot air or that US buys 60% of the hot air.]

TDS: What is the total % we need in the 1st budget period?

J Frankel: Our analysis shows that in the 1st budget period Russia and Ukraine are the big sellers. There are 3 interrelated issues here: 1 -- Assuming a system w/complete confidence, tough standards, etc., yes, no doubt U.S. needs those tons badly; 2 -- Russia hot air issue; 3 -- potential for abuse of the rules. These are 3 logically distinct issues.

We have talked about scenarios like an “empty tank provision” to keep Russia, for instance, from selling all its allowances in the 1st year. One disadvantage is that if you start talking about that it’s a real slippery slope.

G Frampton: Are there any other burdens we can agree to that wouldn’t affect us but would increase confidence. You’ve just named one.

F Loy: If you put some cap on Russian sales -- it’s recutting the basic Kyoto deal, but let’s assume you can do it -- is that really a slippery slope?

D Doniger: This is something to talk about at the end of the debate. It is best discussed after you’ve talked about and come to agreement on the integrity issues. It’s better to talk to the Russians about what they will do with the money -- an initiative, for instance, to get them to plow the money back into environmental projects. Only after you’ve had these conversations should we even discuss caps.

M Kimble: W/in Annex I universe there are a fixed number of tons. That is a supply issue. If we really achieve a 5.2% reduction by 2012 that will be a significant environmental accomplishment.

R Ballentine: What does it look like down the road? When both hot air and real tons are on line -- is there a point at which we can make real tons more attractive?

M Kimble: Need to remember that the term “hot air” is itself an EU rhetorical device.

J Frankel: 2/3 of Russian sales in the 1st budget period will be hot air. Beyond that it all depends on LDC participation; assumptions about the Russian economy; what the second budget period numbers are, etc.

R Ballentine: Couldn’t we have a phased-in cap?

D Doniger: What we want to happen is what happened with sulfur: tons are cheaper than we thought; overall solution is cheaper; therefore, people agree to tighter second budget period, more environmental success, etc.

D Forrister: Industry needs a free market signal in order to get going, but fact is, they will do stuff domestically (technology development, etc.). There is also a growing realization in the EU business community that they also need unfettered trading. Can we reach out to them?

D Hales: Keep in mind that the with respect to developing countries their position is that all things

are possible once we [US] show that we are really doing something at home.

D Sandalow: Have to keep in mind too that polling shows that our public is skeptical of trading.

TDS: Until you tell them the price! Then the numbers turn around.

G Frampton: Does EPA have a standard emissions trading briefing -- what I call a "Corps of Engineers" briefing?

Group Response: Yes, and EU and others are sick of it!

M Kimble: The word is spreading, however. UN is actually now using the EPA briefing.

D Gardiner: Need to appreciate link between trading and compliance. US stance on latter affects our credibility on the former.

D Sandalow: Hot air also an issue with the right wing. They see it as "paying Russia for doing nothing."

TDS: To sum up, our working proposition is no caps. It needs to stay that way until the 11th hour and then it gets changed only with a hi-level decision. Let me ask, will a 50% cap really bite?

J Frankel: Economic models say yes. It all depends on one's assumptions about technology.

TDS: Every week it seems like there's a technology announcement of some breakthrough. Impression one has is that there are real breakthroughs happening.

J Frankel: To some extent we are stuck with the models we have. And the fact remains that our emissions keep going up -- can't argue with the facts.

M Mazur: What does a 50% cap do though?

J Frankel: Let's just stipulate that it has a huge incremental effect in the cost.

D Hales: Let's remember too though that economic models also say that the cost of doing nothing is also very high.

TDS: So we know what we want. How do we get it? How do we avoid an 11th hour scenario?

1 -- We need to be leaders in monitoring, registries, etc. -- trading integrity issues.

2 -- We need to be leaders in pushing compliance.

3 -- We need to be leaders in pushing a deal w/Russia.

D Sandalow: We also need to be leaders in public communications on the international level.

G Frampton: And in targeted education of particular groups.

F Loy: I agree with all this, but is this the time to flesh all this out? We need a credible system, yes -- we can stipulate all that. But even if we do all this correctly, we will make progress, people will be better educated, etc. But the question is -- will we have a trading system at the end of 2 years? No. We need, in interim, something that developing countries can see sooner rather than later -- something they will like that will benefit them.

TDS: That's fine to skip ahead to CDM, but we will then have to come back to the game plan for trading.

G Frampton: I agree. This discussion has been useful in reaffirming the wisdom of pursuing our current position.

TDS: We need someone to do an outline of points that will set up the game plan meeting.

[Project assigned to D Doniger; D Sandalow; G Frampton]

[Beginning of CDM discussion]

M Kimble: The way the Kyoto Protocol is written, CDM is the one flexmechs that can come on line first -- almost right away. Certain issues are involved here and on emissions trading that can be resolved in SBSTA. CDM can start 11 months from now. Also important to realize that CDM can be very complex. Important to identify what issues are most important to resolve more quickly.

F Loy: There are 3 issues: 1) how far do we want to have elaborated before we start up? We could start as fast as possible or we could start only when all the loose ends are tied up, realizing that a sloppy start will set a bad precedent for trading. Regardless, there is a need for some international mechanism or body -- not yet set-up; 2) starting CDM opens us up to charge that we are implementing Kyoto -- to which I suppose our answer is: "so what?"; 3) must deal with argument that starting up CDM will lower appetite among developing countries to participate in trading (i.e. taking on a target).

D Sandalow: We should be so lucky that CDM works so well that it lowers appetite for trading. We can live with that.

TJ Glauthier: The 2 systems need to merge. CDM will always be small potatoes relative to emissions trading. We should get started as fast as possible to show benefits.

D Hales: For any country that makes a difference CDM will always be overwhelmed by emissions trading. Even if you have “whole sector” CDM. Need to move fast and demonstrate that with briefings.

J Frankel: I worry more that CDM will be so unsuccessful (additionality, transactions costs, etc.) that it will undermine trading.

D Doniger: There is a real potential for collusion in CDM -- could seriously undermine trading.

TDS: Have to make the best system we can. Key issue is additionality. We have to strike a balance between making it not so hard that no one can do it and not so easy that it is sloppy and we just have phantom reductions.

D Gardiner: Let's be really focussed. Example: the power sector in China. We know it is critical; we know a relatively lot about it. This way we enhance our credibility.

TDS: We also need the big picture on this though -- a whole vision. I.e., if you want to start a CDM which window do you go to?

D Gardiner: Focussing on specifics helps answer institutional questions. We are beginning to frame the important issues at the assistant secretary and technical level. Not really ripe to go much higher right now.

F Loy: We need answers to these questions more than we need answers on emissions trading. Would be enormously helpful to our efforts.

D Doniger: We need to pick off of the B.A. list and focus at the upcoming UN workshop.

TDS: How do we see this process playing out over the next 1 to 2 years. What are the points along the way. We have CDM work going on -- are there outside events driving us to certain conclusions by certain dates?

D Sandalow: Yes. March 1 -- submissions; March 31 -- submissions; April--workshop; June 10 -- SBSTA; October -- COP5.

M Kimble: UN has a CDM book that will shape a lot of thinking on these issues. Brazil is doing a lot of the legwork. Behooves us to influence this through the Brazilians. There is an Aspen Institute workshop w/Brazil in the spring. Brazil's legwork is proceeding on a project-by-project approach. Not so sure this is what we want.

D Hales: Sounds like we should upgrade our representation at the Aspen sponsored meetings.

D Gardiner: The project-by-project approach is the high transaction costs/high potential for collusion approach. The high ground would be to say “we want standards.”

TDS: Where are the tension points?

D Gardiner: The argument for caps on CDM is stronger textually than it is for trading. There is also the regional equity issue w/respect to CDM that needs to be addressed.

TDS: Where is the EU on this?

M Kimble: Their thinking is not that far along. Their basic point is that CDM will add tons to the system and they want to keep it small. They see it essentially as a way of going over your target.

D Doniger: We have this problem in the Clean Air Act. Simplicity vs. Quality control. There is a real debate about whether projects really result in reductions that wouldn't have happened otherwise.

D Hales: Additionality is really a system-boundary issue.

D Gardiner: EU will be for maximum quality control.

TDS: When will we have a paper or papers that will walk through the U.S. vision of this? Institutional structure; identification of issues on which we need resolution, etc. What is the schedule for producing this?

D Sandalow: 2-3 weeks (Gardiner and Mazur working); 4 weeks to get back to this group.

M Kimble: Need to factor in Umbrella meeting in Canberra in 1 week. Watch Canada on this one -- they are hosting a major ministerial.

D Sandalow: That's tactical -- need to get a draft text out there putting our vision forward.

TDS: I thought there was a big push in business not to move CDM and emissions trading except in tandem. Are we reconsidering that premise?

F Loy: Seems to me that the appetite issue (CDM discouraging participating in trading) is not real. On the other hand it seems to me that the model issue is real -- seems like we agree that we can't move too quickly; can't afford to be sloppy. Need to be reasonably rigorous because we can't afford to take hits on either the issue that these reductions are fraudulent or that we are therefore setting a bad example for trading.

TDS: Is it even reasonable to say that CDM could go first? Could it possibly start up before COP6?

M Kimble: The Kyoto Protocol says it can. In reality, we need to take 2 things to COP6: an emissions trading plan and a CDM plan.

D Doniger: But I want trading to really start after COP6. Not wait for 8 years.

D Gardiner: But there are things we can do over the next 2 years to get actual CDM projects ready.

F Loy: I think it will come out at the same place. But I don't want us to wait until COP6 to have a CDM plan. But it will take that long if we let it. Let's be able to have a plan that we can take -- even to anti-traders -- and get some momentum going.

M Kimble: The most important issues are establishing a benchmark and additionality. I also think it is key to move forward on trading and CDM in parallel.

D Forrister: Remember too though that we still have our hole card which is that we can do trading anyway -- we can do it legally among just the Umbrella.

TDS: Yeah, but playing that card has a high price -- could blow up on you.

F Loy: My point is that we should go as fast as we can to make CDM real. Let's have real discussions with people about how it would work because that is a very useful discussion for us to be engaged in. Don't let December 2000 date hold us up in having those conversations.

G Frampton: Seems like there is a need to accelerate, realizing that 1) a bad CDM is more of a threat to trading than trading is (at least emissions trading is self-limiting); 2) lots of anti-traders like CDM.

TJ Glauthier: We need to be as concrete as possible. Let's focus on power sector and, within that, maybe decide to focus on retrofits (less theoretical problems than new plants).

TDS: Can a developing country do its own CDM? Isn't that a hell of a hard additionality issue? If Brazil builds a good, clean power plant and says, "we wouldn't have done it anyway" -- yep, that's a tough additionality problem alright.

D Gardiner: Another issue: Lots of LDCs don't want sinks included in CDM because it doesn't involve technology transfer.

M Kimble: Our position is that yes, they are in and our position is that there should be no caps limiting CDM's usage.

F Loy: Concur.

TDS: To summarize: 1) In preparation for emissions trading game plan meeting, D Doniger and D Sandalow will do an outline; ready in 3 weeks;

2) Need substantive papers on CDM

a) outline issues -- tees up decisions on institutional issues

b) functional paper; "how to" guide

Papers on CDM ready in 4 weeks.