United Nations Environment Programme
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PROGRAMME DES NATIONS UNIES POUR L'ENVIRONNEMENT • PROGRAMA DE LAS NACIONES UNIDAS PARA EL MEDIO AMBIENTE
ПРОГРАММА ОРГАНИЗАЦИИ ОБЪЕДИНЕННЫХ НАЦИЙ ПО ОКРУЖАЮЩЕЙ СРЕДЕ

UNEP FINANCE INITIATIVES

CLIMATE CHANGE WORKING GROUP

Emissions Trading Position Paper

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Financial institutions are working to develop market solutions to address climate change (more than ever), particularly since the adoption of the United Nations Framework Convention on Climate Change (UNFCCC) in 1994. Indeed, signatories to the UNEP Finance Initiatives Climate Change Working Group support the Kyoto Protocol, with its flexible mechanisms like emissions trading, and advocate an effective long-term framework to tackle climate change.

Emissions trading is an economically efficient market-based instrument that encourages the transition to a more sustainable economy. Several European countries have already set up their own domestic trading schemes and the European Union (EU) intends to implement an EU-wide emissions trading system by 2005. In some regions of the US, emissions trading regimes have already existed for several years. We see domestic and regional trading as a positive first step. However only an international trading scheme, such as the Kyoto Protocol Flexible Mechanisms, offers the opportunity to capitalise on widely varying emission abatement costs.

These Flexible Mechanisms (International Emissions Trading, Joint Implementation, Clean Development Mechanism) are an effective way to reduce emissions at a lower cost. However, the efficiency of these flexible mechanisms depends largely on their design. The financial sector will play an important role in the operation of this international market and from the perspective of the financial services sector the following features are of utmost importance:

- **Scope and size:** The successful development of an emissions trading market depends on the *liquidity* of the market. An international emissions trading regime requires not only a broad range of sectors but also sufficient volume to ensure a sufficient diversity of contracts.
- **Market access:** Traders and financial intermediaries increase market liquidity and reduce volatility and are therefore a necessary component in an emissions trading scheme.
- **Market compatibility:** Fungibility of certificates across regional and national markets, and between Flexible Mechanisms for example, is an important condition for market liquidity and cost efficient emissions reduction.
- **Emissions reduction targets:** In such an international trading scheme absolute emissions reduction targets, as called for by the Kyoto Protocol for example, are an important prerequisite for credible, efficient and effective emissions trading.

For further information on this position paper or if you have any questions or comments please contact Sascha Lafeld, Dresdner Bank at Sascha.Lafeld@dresdner-bank.com or Nigel Baker, Swiss Re, Greenhouse Gas Risk Solutions at NigelAntony_Baker@swissre.com

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