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Review and Analysis COP-6

Overview

Parties to the United Nations Framework Convention on Climate Change (UNFCCC) held their sixth annual negotiating session (or Conference of the Parties, known simply as "COP-6") in The Hague from November 13th to November 24th. There diplomats sought to fill in unfinished details of the 1997 Kyoto Protocol, which would reduce industrialized countries' emissions of greenhouse gases (GHGs). Natsource personnel were present to participate in related meetings, and to observe progress in the negotiations. We provide the following review and analysis of the negotiations based on our observations and information gathered subsequently from a variety of sources.

Though progress was made on many key issues, negotiators from the United States (US) and the European Union (EU) ran out of time to reach a final agreement. They were unable to completely resolve differences over the most contentious issues, particularly limits on the use of domestic "sinks" to meet national emissions reduction obligations. So at 4 PM on the 24th, Conference Chairman Jan Pronk (the Dutch Minister of Housing, Spatial Planning and Environment) announced that Parties had agreed to "suspend" rather than "adjourn" the negotiations, and called for talks to resume before the October 2001 COP-7 meeting in Marrakech, Morocco. Formal negotiations are likely to recommence in May 2001, concurrent with an already scheduled technical meeting of the Subsidiary Bodies in Bonn, Germany.

For a moment, it appeared that a last-minute deal between the EU and the US was in hand. Early in the morning of the final day of COP-6, a provisional agreement was reached between the US, representing the "Umbrella Group", and Ministers from 3 European countries on a compromise package that limited use of domestic carbon sinks. It is rumored that the provisional agreement also addressed "supplementarity" and determined the compliance regime. The Ministers' excitement at the prospect of a broader agreement proved short-lived, however. Upon review of the preliminary agreement just before the final plenary session, some key EU Ministers found the sinks language to be unacceptable, and as a result the EU backed out of the agreement. The US is reported to have offered additional concessions on sinks before the doors closed at The Hague, but time had simply run out.

Despite the absence of a breakthrough in The Hague, there appears to be a consensus among Parties to continue negotiating and moving forward. At the time of this writing, technical staff from the US, the EU, Australia, Belgium, Canada, France, Germany, Iceland, Japan, Norway, the Netherlands, New Zealand, Russia, Sweden and the United Kingdom are holding a two-day meeting in Ottawa, Ontario. Prior to the Ottawa meeting, an EU source reportedly indicated that the meeting will focus primarily on narrowing the gap on sinks, but that the issue of "supplementarity" - limits on the use of emissions

reductions credits purchased abroad to meet national emissions reductions requirements -- could also be discussed. A briefing note from the International Institute for Sustainable Development expanded the list of topics to include the compliance regime.¹ According to other news reports, progress in the Ontario discussions could set the stage for a ministerial-level meeting tentatively scheduled for next week in Oslo, Norway.² Presumably, all of these efforts are aimed at consolidating the gains from The Hague talks in an EU-Umbrella Group agreement that could form the centerpiece for the COP 6, Part II.

The Pronk Paper

In the wake of COP-6, Part I (in The Hague), one key tool for assessing where the negotiations currently stand is a document referred to as "the Pronk paper," issued by Chairman Pronk on November 23rd and aimed at breaking an impasse between the US and the EU. The paper attempted to carve out middle ground in areas where the two could not come to terms, including supplementarity, the use of a compliance reserve, and specific aspects of the Clean Development Mechanism (CDM). Although few delegates were happy with the bulk of its provisions, the paper did become the de facto vehicle for negotiations on the final day of COP-6, forcing delegates to set aside the more detailed and technical conference papers they had been bargaining over for the past week. The Pronk paper has since been made a formal UN document, and will be the subject of written comments to be submitted by governments by January 15th. It is therefore central to all parties' assessments of where the negotiations were headed at the end of COP-6 Part I, and what the starting point for COP-6 Part II might be. This review of COP-6 provides a brief synopsis of provisions in the Pronk paper, with an emphasis on provisions that bear directly on compliance mechanisms and the creation of rules for international emissions trading.

Emissions Trading

Supplementarity

The EU and the Umbrella group disagreed prior to the COP-6 on whether a quantitative limit should be imposed on the use of the mechanisms for compliance with emissions targets. The EU supported a limit of 50% of total reductions, while the Umbrella Group opposed any

limit. The EU argued that such a constraint was necessary to prompt domestic action. The US argued that such a constraint would distort emissions trading markets and increase the costs of compliance, making it less likely that the Protocol would enter into force and discouraging future efforts. A member of the US delegation providing her personal views on the negotiations noted that the US expected supplementarity to be the biggest sticking point at The Hague.

The Pronk paper adopts the "qualitative" principle of supplementarity, but does not specify an explicit "quantitative" constraint on the use of the mechanisms for compliance [excerpts from the Pronk paper are presented in italics]: *Annex I Parties shall meet their emission commitments primarily through domestic action since 1990. Compliance with this principle will be assessed by the facilitative branch of the compliance committee on the basis of qualitative and quantified information, reported in national communications and reviewed under Article 8 [of the Kyoto Protocol].*

According to numerous sources, the US did not agree to a quantitative limit. In the personal view of an EU delegate, the EU still seeks a 50% quantitative cap, and the issue of supplementarity will be back on the table when negotiations resume. That said, the EU delegate suggested that the EU is learning quickly about the value of international trading for its own compliance needs, and that it will end up buying emission reduction credits from the US, where reductions are relatively less expensive. The European Commission, for example, has advocated pan-European emissions trading by 2005, and several countries such as the UK and Denmark already have plans for domestic emissions trading systems.

Liability

Parties sought to develop a rule that would assign liability for non-compliance to buyers and/or sellers of Assigned Amount Units (AAUs). The rule would address the question of who bears the responsibility when a nation sells too many AAUs and eventually misses its own target, falling into non-compliance? The EU supported a "buyer liability," which would create an incentive to buy only from nations with a high probability of meeting their targets. For the most part, nations comprising the Umbrella Group supported seller liability, believing it would prompt sellers to

¹Briefing note distributed to IISD's Climate Change Info Mailing List. See IISD website - <http://www.iisd.ca/linkages/>.

²"EU, US Meet in Last-Ditch Bid to Save Climate Deal," by David Ljunggren, Reuters, December 6, 2000.

be more responsible for assuring compliance while keeping the emissions market stable. Others supported blends of buyer-seller liability, hoping to get the best of both worlds.

The Pronk paper would require Parties to set aside 70% of their AAUs in a compliance reserve to better ensure that each country's estimated emissions would be covered by its AAUs: *Annex B Parties shall retain a portion of their assigned amounts in their national registries specific to that commitment period. This portion shall be 70 per cent of their assigned amounts, or the portion determined on the basis of projected or recent emissions. After the annual review of each Party's emissions data, the portion of assigned amount that must be retained shall be recalculated and, if necessary, adjusted.*

It is unclear whether the US and the EU are satisfied with the 70% compliance reserve/seller liability tradeoff - if that tradeoff was indeed agreed. From the US perspective, a 70% compliance reserve has the disadvantage of reducing liquidity in the international emissions trading market - though it is unclear how much. On the other hand, seller liability would greatly enhance buyer confidence and reduce transaction costs associated with buyers' assessments of seller creditworthiness. From the EU perspective, a 70% compliance reserve goes far toward limiting the extent of possible overselling. On the other hand, some observers worry that the choice of seller rather than buyer liability might increase the possibility that some AAUs sold on the international market will later turn out to be illegitimate.

Although the Pronk paper does not address buyer vs. seller liability, it is widely rumored that the US and EU agreed that AAUs in excess of the compliance reserve would be sold on a seller liability basis. Nevertheless, in their personal comments recently, an EU delegate and a US NGO representative contradicted this rumor, asserting that no agreement had been reached on seller liability.

Tax on international emissions trading (IET) and Joint Implementation (JI)

The Kyoto Protocol requires that a "share of the proceeds" from projects in the clean development mechanism be made available for emissions mitigation and adaptation efforts in poor and vulnerable countries. No parallel provision exists for IET and JI, which has disturbed some developing country delegates who are interested in maximizing adaptation and mitigation funding. As a result, these delegates have proposed that the "share of the proceeds" concept should be applied to IET and JI as well.

The Pronk paper addresses this issue by imposing an obligation on industrialized nations to increase climate change funding for developing nations by \$1 billion annually, backed by a levy on IET and JI that would apply if Parties fail to meet the funding target: *Parties agree to increase resources for climate change funding through other channels. They agree that the sum total should reach the level of one billion US\$ on an annual basis, as soon as possible, but not later than in the year 2005. If resources in 2005 are less than one billion US\$, Parties agree to apply a levy on Article 6 (Joint Implementation) and/or Article 17 (emission trading).*

Fungibility of Certified Emission Reductions (CERs)

The Pronk paper includes a provision pertaining to the fungibility of nations' AAUs and CERs generated under JI or CDM: *Parties note that emission reduction units (under Article 6) and parts of an assigned amount (under Article 17) could be added to, or subtracted from, the assigned amount of a Party. Parties agree that certified emissions reduction units (under Article 12) could be added to the assigned amount of a Party and could be used for the purpose of contributing to compliance with the quantified emission limitation and reduction commitments in Article 3 without altering that Party's assigned amount pursuant to its commitments inscribed in Annex B.* It is unclear whether the intent of the provision is to impose a real restriction on the use of CERs to meet domestic emissions reductions requirements, or simply to ensure that enforcement authorities know when CERs generated outside of the country are being used to meet domestic reduction requirements.

Participation in IET by private entities

The Pronk paper does not address this issue.

Compliance

The Kyoto Protocol requires the development of rules designed to deter non-compliance with treaty obligations. Entering The Hague, the US supported a mechanism by which Parties with emissions in excess of their AAUs must repay their overage - with interest -- out of the assigned amount from the next budget period. The EU supported financial penalties to deter non-compliance.

The Pronk paper assures compliance by subtracting overages from allocations in subsequent compliance periods. It sets a penalty rate of 150%, and increases the rate by 25% if a Party has not complied by the end of the

subsequent commitment period: *Parties decide that, if a Party has been determined as being in non-compliance with its commitments under Article 3.1, the enforcement branch should apply the following consequences: a) Subtraction of excess emissions from the assigned amount of the subsequent commitment period; b) A penalty rate, set at 1.5, and increased by 0.25 after the subsequent commitment period, if the Party concerned is not in compliance at the end of the subsequent commitment period.*

To prevent Parties from evading repayment of penalties, the Pronk paper requires emission commitments for the second commitment period to be adopted before the beginning of the first commitment period.

Joint Implementation

Under the Pronk provisions, JI would escape bureaucratic control and application of "additionality": *Parties decide that there is no need for stringent procedures on verification [of JI projects] if Parties meet reporting requirements. Parties note that, if Parties do not meet these requirements, they should follow the same rigorous procedure as provided for under the CDM procedures.*

Clean Development Mechanism

Project eligibility (other than sink projects), additionality, and baselines

Parties entered the talks with the goal of taking decisions to facilitate CDM projects. In particular, Parties sought to agree on terms that would provide certainty to project developers regarding project approvals while ensuring that emissions reductions were additional to those defined as "business as usual." The EU supported a positive list of preferred projects that would be provided automatic approval, with a focus on small renewable energy and energy efficiency projects. The US emphasized the need to ensure that developers of larger infrastructure projects gain certainty about approval processes. With regard to project eligibility, the US entered negotiations supporting the inclusion of nuclear projects in the CDM, which was strongly opposed by the EU. However, the US softened its position early in the negotiations, sending the signal that it would be willing to give up inclusion of nuclear projects in the CDM in exchange for concessions from other Parties.

The Pronk paper does not include a positive list for CDM projects: *Parties recognise that it is up to the Party's discretion to judge whether a project activity is in line with its national strategy on sustainable development. However, it does establish a preference for renewables and energy efficiency: The following activities should be given priority and will have expedited consideration within the rules, modalities and procedures of the CDM: (a) Renewable energy (inter alia small scale hydro); and (b) Energy efficiency improvements.* The Pronk paper also contains language that excludes nuclear projects from the CDM: *Annex I Parties will declare that they will refrain from using nuclear facilities for generating certified emission reductions under the CDM.* It is unclear whether the choice of the term "refrain" was intended to, or in fact does, provide a loophole for nuclear projects.

The Pronk paper calls for standardized baselines for small projects: *Standardised baselines, which are based on an appropriate Annex I average, may be used for small-scale projects (<XMw) and renewable energy projects (<XMw). The Executive Board is asked to elaborate, and make recommendations on, preferential treatment of these specific project types.* Size limits for eligible projects are not provided in the Pronk paper, but perhaps may be inferred from a conference paper from The Hague.³ The paper contains bracketed proposals for limits on small-scale fossil-fuel based projects, which are set at 1, 5 or 15 Mw, and on eligible non-fossil based energy production activities, which are set at 10, 15 or 50 Mw.

Definitions of additionality do not appear in the Pronk text. A US official has expressed personal regret that time constraints during the last-minute US-EU negotiations prevented a resolution on additionality.

Eligibility of Sinks Projects in the CDM

The issue of sinks remains extremely controversial (see discussion on the use of domestic sinks projects). The EU came into the negotiations opposing the inclusion of sinks projects in the CDM, as did a number of developing nations. The Umbrella Group supported the inclusion of sinks projects.

The Pronk paper includes afforestation and reforestation projects in the CDM, but excludes activities that prevent deforestation and land degradation. The paper also suggests that issues relating to inclusion of sinks

³ <http://www.unfccc.int/resource/docs/cop6/crpo2a01> -- see items 79 and 67.

in the CDM need further scrutiny: *Accounting modalities and definitions for Article 3.3 may need to be modified, and the issues of non-permanence, social and environmental effects, leakage, additionality and uncertainty should be properly addressed.*

In a recent panel discussion, an NGO representative indicated that environmentalists strongly disapproved of Pronk's text on sinks in the CDM. He also said he had heard that the US and EU would have deferred on this issue if they had come to agreement on domestic sinks. Other observers at The Hague heard similar reports.

Other CDM issues

Under the Pronk provisions, projects in least-developed countries (LDCs) would escape the adaptation levy (there are 40 LDCs⁴). This exclusion may also extend to small projects: *CDM projects in LDCs will be exempt from the share of proceeds for adaptation. The implementation of "small scale CDM projects" will also be promoted.*

To ensure a prompt start for the CDM, the Pronk paper calls for the election of the Executive Board at the next session of the subsidiary bodies. Lastly, the Pronk paper does not address the issue of participation in the CDM by private entities.

Domestic Sinks

Carbon sequestration or "sinks" was the most controversial - and most complicated -- topic discussed at the meeting. The Kyoto Protocol contains two provisions addressing sinks. Article 3.3 specifies that nations may include the net benefits of sequestration from afforestation, reforestation and deforestation in their national emissions inventories. Article 3.4 says that Parties may adopt a methodology for including the carbon sequestration benefits of additional activities, such as agricultural soils, land use activities, land use change, and forestry (presumably including forest management and conservation).

In The Hague, the Parties sought to agree on definitions of Article 3.3 activities as well as an approach for Article 3.4. The EU was strongly opposed to an initial US proposal to claim complete credit for its domestic sinks -- an amount equal to 50% of its emissions target. The EU argued that nations with significant forests should not be able to use reductions from sinks to avoid reductions from domestic emission sources. In the final hours of negotiations, the US and 3 European Ministers reached agreement on a formula that would have allowed the U.S. to claim credit for 75 million metric tons (Mt) of sinks against its emissions target each year-about a fourth of its original claim. However, the EU later changed course, rejecting this formula as too permissive. It was reported that the US made a last-second offer to lower the cap to 40 Mt/year, but this was insufficient to produce a compromise.

Annual cap during first commitment period

The Pronk paper acknowledges that domestic sinks may be used, to a degree, to change emission targets. To limit the impact of sinks on emission targets, the paper specifies that *additional activities under Article 3.4, towards meeting a Party's target in the first commitment period shall be limited to 3 per cent of that Party's base year emission.* Based on a 1990 US emissions baseline of 1,650 million metric tons of carbon equivalent, the Pronk paper limits US use of domestic sinks to about 50 Mt. As mentioned above, the provisional US-EU agreement would have capped use of domestic sinks at 75 Mt.

Definitions and eligible activities

The Pronk text adopts the IPCC definitions of afforestation, reforestation and deforestation. It identifies eligible domestic sinks activities as: *grazing land management, cropland management and forest management (broadly defined land management activities), revegetation (narrowly defined activity).*

Discounting of reductions from domestic sinks beyond defined threshold

The Pronk text seeks to address concerns about the uncertainty of reductions from domestic sink projects by incorporating a discount rate for emissions beyond a certain threshold. Accounting for domestic sinks activities would take place in two distinct intervals:

⁴ <http://www.unfccc.int/resource/docs/cop3/info3.htm>.

First interval

Parties recognise the unintended outcome of Article 3.3, namely that countries who have an overall increase in their total forest carbon stock may nevertheless have their assigned amounts reduced because of accounting and definitional conventions under Article 3.3. Therefore, Parties decide that Parties may fully account for carbon stock changes and net greenhouse gas (GHG) emissions in areas under forest management up to a level that is equal to carbon stock change since 1990 in that country compensates [sic] the net debit incurred under the provisions of Article 3.3. This first interval shall not be more than 30 Mt CO₂. [The Pronk text seems to have gotten jumbled in the scramble for an agreement. It appears that the intent was to establish a threshold for undiscounted emissions reductions at 30 Mt CO₂ below the 1990 baseline.]

Second interval

Parties decide that carbon stock changes accounted for in accordance with the provisions of Article 3.4 shall, for the broadly defined management activities, exclude the effects of: (a) Indirect nitrogen deposition; (b) Elevated CO₂ concentrations; (c) Other indirect effects; and (d) The dynamic effects of age structure resulting from management activities before 1990 (for forest ecosystems). Therefore, Parties shall apply a reduction of 30 per cent to the net carbon stock changes and net greenhouse gas emissions that result from additional cropland and grazing land management activities, and of 85 per cent to the net carbon stock changes and net greenhouse gas emissions that result from additional forest management.

Review of domestic sinks provisions

The Pronk paper stipulates that provisions addressing the treatment of domestic sinks will be reviewed before establishing emission commitments for subsequent commitment periods.

Significance of the Pronk Paper

Despite its importance, there is reason to question whether the Pronk paper addressed issues other than domestic sinks in terms that the EU and the US will both accept in May. First, according to accounts of the negotiations, haggling between the US and EU ministers centered mostly on sinks, and many topics in the paper were not dis-

cussed in any detail. Given the unpopularity of some of the compromises Pronk crafted, governments may resist negotiating from the Pronk text, and instead choose to work from the 14 more detailed, heavily bracketed, generally unfinished conference papers from COP-6 Part I. These papers are expected to be posted on the UNFCCC COP-6 website.

Second, US and European negotiators may well have revised some areas of the Pronk paper in arriving at their tentative agreement. As of this writing, the revised version of Pronk's paper has not been circulated.

Third, it is unclear whether the G77/China would have accepted an agreement based on the Pronk paper. Under the Pronk paper's formulation, Annex I countries would create three funds which would address adaptation, technology transfer, capacity building and other needs in developing countries, and would contain a minimum of \$1 billion/year. News stories and personal accounts of the conference suggest that opinions are mixed regarding whether \$1 billion would have been deemed adequate by the developing countries, and whether a compromise on the funding issue could have been brokered in the closing hours of the negotiations.

What's Next?

Although negotiations in The Hague were suspended on November 24th, activities aimed at achieving a negotiated agreement are continuing apace. Government comments on the Pronk paper are due to be submitted to the UNFCCC by January 15th. This week, the US and the EU will revive talks on the near-accord achieved in The Hague. Potentially, they could achieve a formal or informal agreement that could help jump-start COP 6, Part II in May 2001, when negotiations are scheduled to resume at the meeting of the subsidiary bodies in Bonn, Germany. We will be carefully monitoring any new developments in this area.

No one can be quite sure how close the Parties came to agreement in The Hague, nor how easily they can pick up where they left off. EU Ministers opposing the provisional agreement with the US reportedly took issue not only with the treatment of domestic sinks, but with provisions on supplementarity, the penalty for non-compliance, and the inclusion of sinks in the CDM. This would suggest a level of disagreement that could not be solved simply by adjusting the cap on the use of domestic sinks. Even if the industrialized parties had reached an accord, some observers believe that developing nations would not have

accepted the funding provisions and other aspects of the Pronk paper.

Other parties familiar with the negotiations take a brighter view. According to a New York Times story⁵, the US and the EU came within 20 million tons of agreeing on the use of domestic sinks - a trivial amount compared to total global emissions of 6 billion tons of CO₂ per year. If exhaustion and an excessive amount of number-crunching played a significant role in preventing agreement, as reported, perhaps a little more time was indeed all that was needed. And if the EU-US agreement had been secured, it may have created momentum for any concessions that may have been needed to reach agreement with the developing nations.

In addition to questions about where negotiations currently stand, no one can be certain of the impact of the presidential election in the US. If Governor Bush is elected President, it could take some time for the Administration to develop its position on the range of complicated issues at stake. It will take several months to have senior officials in place at the relevant agencies to even initiate interagency discussions on these issues prior to taking positions at upcoming negotiations. The only certainties if Governor Bush is elected appear to be (1) a reevaluation of US positions and (2) support for market based mechanisms to reduce emissions. Early in his campaign, Governor Bush stated his opposition to the Kyoto Protocol for failing to include serious commitments for developing countries. However, he later articulated his support for market mechanisms in his speech on energy policy in September. He also has a record of support for emissions trading (SO₂, NO_x) in the Texas electricity legislation. Some observers believe that, should a Bush Administration reach an international agreement on climate change, Bush would be well positioned to secure a successful Senate ratification vote. Others are skeptical that he would push hard for ratification, given his history on the issue.

If Vice President Gore emerges as the victor, there would likely be a prompt effort to resume the negotiations. His depth of experience on the issue, plus the experienced talent in the Clinton Administration that he could draw upon to complete the task, would likely assure that timely decisions could be made. There would be little doubt that the US would be ready to negotiate in May. Few doubt Gore's seriousness in wanting to address the issue, nor his commitment

to achieving a ratified treaty. However, some observers believe that his deep history on the climate issue - which some Senators view as extreme -- could cause serious problems in a Senate ratification vote.

Serious engagement by the Senate is critical to the long-term success of US action on climate change. In fact, for any treaty to become law, it must be ratified by 67 Senators, and thus would require a bipartisan majority. One of the most significant developments in The Hague was the emergence of new views on the part of key Republican Senators. For example, Senator Chuck Hagel indicated that if Governor Bush becomes President, the climate change issue would not be shelved. He also emphasized Governor Bush's commitment to a policy that includes limits on carbon emissions from electric utilities. Senator Larry Craig renounced his skepticism regarding climate change science, and said that it would not "be appropriate at this time" to bring the Protocol before the Senate with the intent of obtaining a rejection. He added that "we ought to stay engaged with the rest of the nations of the world."⁶ These developments follow a series of hearings held by Senator John McCain after his presidential campaign, where he heard frequent questions from audiences about his position on the climate issue. Although the Parties did not come close to creating an agreement that would meet the Byrd-Hagel condition of "meaningful participation" by developing countries, it is possible that the Senate's hostility to the climate issue - perhaps even to the Kyoto Protocol -- may have diminished somewhat. This term, the Senate appears evenly divided. Newly-elected Democrats will tend to focus more on environmental issues than the Republicans they replaced. But the key to ratification will be whether a bipartisan coalition emerges behind the compromises that may ultimately come out of the second half of COP-6.

One arena sure to get attention is power plants. After over two years of environmental campaigning by grassroots groups to further regulate power plants, both Governor Bush and Vice President Gore supported multi-pollutant power plant controls in their presidential campaigns. These proposals include four pollutants: CO₂, mercury, SO₂ and NO_x. There is bipartisan interest in pursuing this agenda on Capitol Hill, led by Senate Environment and Public Works Committee Chairman Bob Smith and Congressman Sherwood Boehlert, who is likely to become Chairman of the House Science Committee. There is a growing sense that there will be congressional action on the "four

⁵ "News Analysis: The Tree Trap," by Andrew C. Revkin, *The New York Times*, November 26, 2000 (<http://www.serve.com/commonpurpose/news/nytglobalwarming13.html>).

⁶ "Key Senate Republicans 'Less Skeptical' of Global Warming," by Chris Holly, *The Energy Daily*, November 27, 2000, ED Volume 28, Number 223: King Publishing Group.

pollutants" either as part of electric restructuring legislation or in an independent effort on power plant pollution.

Final Thoughts

In the aftermath of COP-6, Part I, there are several signs pointing to continued progress in the development of international emissions trading markets. Although the most controversial issues at The Hague received the most press attention, real progress was achieved in other important areas, such as monitoring and measuring emissions, capacity building, and policies and measures. The Pronk paper has helped focus attention on the most difficult issues and tradeoffs that Parties will need to confront in order to reach agreement. It also provides the US and the EU with an organizing framework, and perhaps the basis for a negotiated agreement, as they take steps in preparation for COP-6, Part II. In the meantime, the Kyoto Protocol will continue to drive progress toward the creation of domestic compliance regimes. As a result, interest on the part of companies and countries in finding cost-effective ways to meet emissions reduction requirements continues to grow. This is evident in the growing number of companies currently exploring opportunities to execute international emissions trades, as well as in the steps that the EU, the UK, Denmark, and other countries are taking to ensure that they will be ready for international emission trading when an agreement is hammered out.

Through the difficult challenges of a US election year and a tough set of international negotiations, it is important not to lose sight of the fundamentals shaping our future. As the year 2000 draws to a close, there is a powerful sense that climate change policies are coming, that emissions trading will be the centerpiece of the world's plan for addressing it, and that those best prepared for that future will be those gaining competitive advantage now - through early experience in managing emissions, building internal competency, and engaging in the emerging carbon market.