

article 17 was intended to allow trading in principle with rules to be negotiated. Environmentalists will continue to urge Canada to consider proposals for limiting hot air trading.

Cap on Trading.

While a cap on trading reduces the theoretical economic efficiency of a trading system, it is not clear that this is the case in a system that has considerable hot air. Moreover, a cap on trading sends an essential message to developing nations that the developed world does not see reductions in emissions as an unacceptable burden on their development. That demonstration of will is essential to securing meaningful commitments from G-77/China, and is in the best interest of the environment.

Clean Development Mechanism

To be effective the CDM will need to set baselines for CDM projects in a way which guards against credit for non-additional projects while at the same time encouraging no-regrets projects that would not otherwise occur. Canada should work with other nations in proposing detailed approaches. Some approaches which merit further attention include:

- using a matrix of technologies that can in different circumstances be presumed to be improvements on business as usual. The matrix would need to be set by international institutions;
- setting baselines based on production levels and internationally agreed benchmarks of carbon efficiency that represent practices at the top end of standard energy efficiency practices in the developing world;
- setting national baselines (possibly using dynamic baselines tied to economic growth) which can be subdivided into sectoral and/or project baselines by national government.

The latter approach has the advantage that it would be most conducive to the sorts of sectoral policy reforms that are likely to yield the greatest benefits. However, it would likely be perceived (quite rightly) as a backdoor means of establishing developing nation commitments.

In designing the institutional framework for CDM, it must be recognized that emission reduction credit trading places very high demands on regulatory agencies (in this case, operational entities and the Executive Board) and requires that such agencies be able to make independent judgments. The Executive Board must be independent and have a strong mandate. To ensure financial additionality it should also be independent of the GEF or the World Bank. Similarly, care should be taken in choice of operational entities. Operational entities must be able to make difficult judgments without fear of economic repercussions or political interference.

Other issues that need to be addressed in the context of CDM included discounting for uncertainty and ensuring that environmentally dangerous projects, such as nuclear power, are excluded from consideration.