



CIGI 

# THE END OF THE BEGINNING

Paris COP 2015

David Runnalls



## About CIGI

The Centre for International Governance Innovation is an independent, non-partisan think tank on international governance. Led by experienced practitioners and distinguished academics, CIGI supports research, forms networks, advances policy debate and generates ideas for multilateral governance improvements. Conducting an active agenda of research, events and publications, CIGI's interdisciplinary work includes collaboration with policy, business and academic communities around the world.

CIGI's current research programs focus on three themes: the global economy; global security & politics; and international law.

CIGI was founded in 2001 by Jim Balsillie, then co-CEO of Research In Motion (BlackBerry), and collaborates with and gratefully acknowledges support from a number of strategic partners, in particular the Government of Canada and the Government of Ontario.

Le CIGI a été fondé en 2001 par Jim Balsillie, qui était alors co-chef de la direction de Research In Motion (BlackBerry). Il collabore avec de nombreux partenaires stratégiques et exprime sa reconnaissance du soutien reçu de ceux-ci, notamment de l'appui reçu du gouvernement du Canada et de celui du gouvernement de l'Ontario.

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## Paris COP 2015

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The Paris Conference of the Parties (COP) is designed to produce the next round of climate change action. The commitments made at COP15 in Copenhagen in 2009 will expire in 2020, and given the time required for national parliaments to act, it is important to set commitments now for the period 2020–2030.

The French have brought their considerable diplomatic panache to bear on COP21. They have set out their goals quite simply:

- a universal legal agreement to establish rules and mechanisms to keep within the 2°C limit;
- national commitments covering control and reduction of emissions;
- the financial aspect enabling support for developing countries and financing the transition toward low-carbon economies; and
- the strengthening of the commitments of civil society and non-governmental stakeholders and the multi-partner initiatives of the Lima-Paris Action Agenda to begin concrete actions prior to the 2020 agreement.

The preparations by both the French government and the United Nations have been extensive and very public. Every effort has been made to involve national governments, but due to the scope and complex nature of the climate change problem, a number of other groupings have become energized during the process. Civil society, big city mayors, the private sector, and states and provinces have all been galvanized to take action. There is a clear sense that the world may well be approaching a tipping point on climate change.

The negotiations themselves, however, are a laborious process involving 195 countries plus the European Union, and all decisions are taken by consensus. This means that small groups of countries can slow the process to a halt. A failure to come to an agreement in Paris would stimulate more calls to move the real negotiations to a smaller, more manageable process.

Countries have been negotiating throughout 2015, but it looks as if major hurdles still remain. Recent “pre Paris” negotiations turned a reasonable 20-page text into the customary “forest of brackets” signifying disagreement. Are we facing a repeat of Copenhagen? The lukewarm references in the Group of Twenty (G20) communiqué from Turkey are not encouraging.

There are reasons to believe that the chances for success at the multilateral level are better now than they were before, but even under the most optimistic scenarios, Paris will not be the end of the negotiations. It is important, however, for the success of the UN climate process that Paris be a success. A failure would set back the whole process by a number of years.

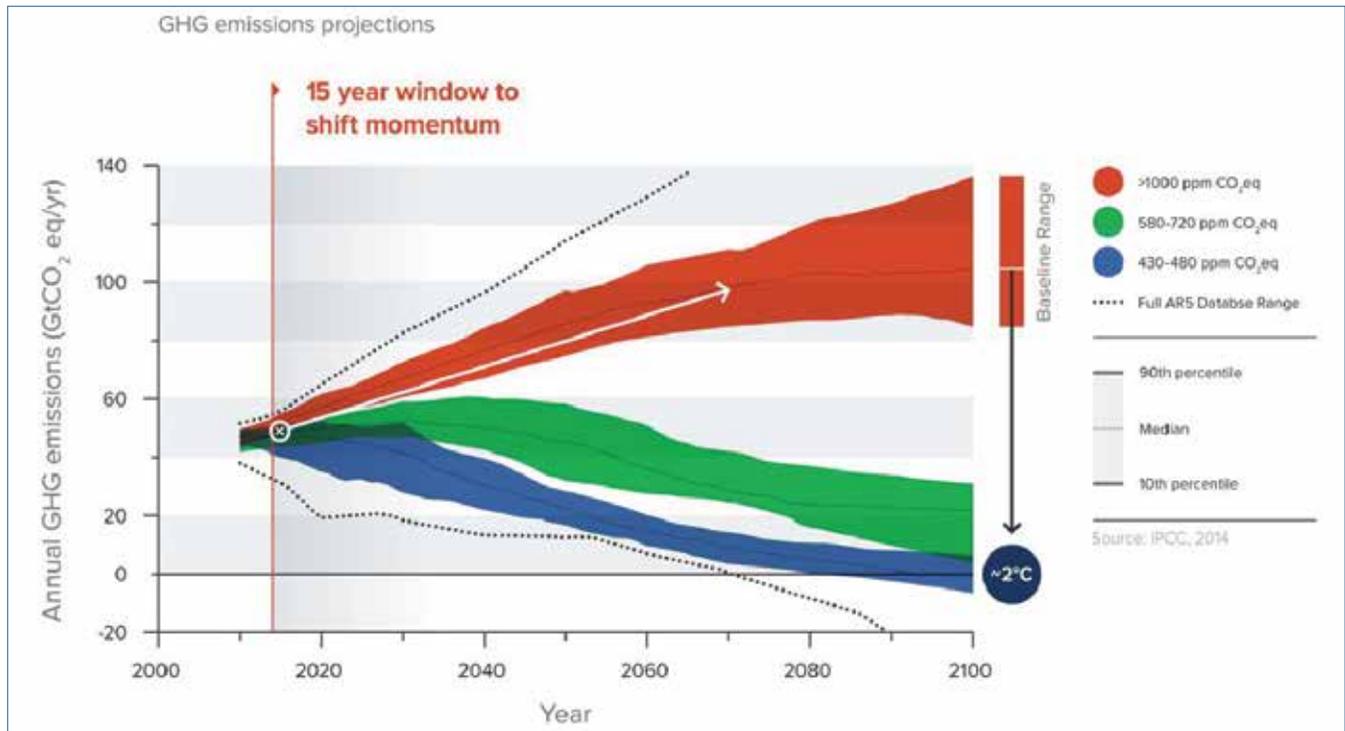
### The Science Is Alarming

Although a few climate change deniers still pop up from time to time, the consensus among climate scientists is hardening. At COP15 in Copenhagen, countries agreed to limit greenhouse gas (GHG) emissions to a level that would not result in an increase of global average temperatures of more than 2°C. There is still a great deal of debate about what that means in terms of concentrations of carbon dioxide (CO<sub>2</sub>) in the atmosphere, but it must not exceed 450 parts per million. We are already beyond 400 parts per million, leading many experts to suggest that only the most vigorous actions beginning immediately will get us to this level.

The costs of delay would be prohibitive. According to the White House, “an analysis of research on the cost of delay for hitting a specified climate target (typically, a given concentration of greenhouse gases) suggests that net mitigation costs increase, on average, by approximately 40 percent for each decade of delay” (Executive Office of the President of the United States 2014).

Perhaps the most frustrating part of the COP climate talks is to participate in a side event organized by scientists and see an increasing sense of despair among the experts, then to move to the negotiations where there appears to be little sense of urgency.

**Figure 1: Climate Performance OffTrack — Next 15 Years Critical**



Source: Global Commission on the Economy and Climate (2014) based on Intergovernmental Panel on Climate Change (2014, SPM, Figure SPM.4)

So, what indicators do we have that the world has reached that critical tipping point on climate change?

### The Economic Perceptions of Climate Are Changing

Climate change has traditionally been viewed as an environmental problem and most of the delegates in the room at COP summits have come from environment ministries. But the debate about climate change is really a debate about dysfunctional energy policies — and energy is at the core of the modern economy — making the problem a big ticket economic issue. Solutions, therefore, must be found by finance ministers, heads of government and CEOs, not just environment ministers and corporate social responsibility advisers.

Leaders of the International Monetary Fund (IMF), the World Bank and the Organisation for Economic Co-operation and Development (OECD) have all stated that climate change is the principal *economic* issue facing the world this century. And the IMF has gone a step further, now incorporating climate risks into its economic country reports, the most authoritative barometer for a country's economic prospects.

There is a growing realization among the world's economic decision makers that the shift to a low-carbon economy is not only a necessity, but also may be less costly than we believe,

and a source of profit for those who develop the technologies and skills necessary to make this transition. In addition, the recent report of the UN Environment Programme Finance Initiative, *The Financial System We Need*,<sup>1</sup> makes a compelling case for integrating the economic and low-carbon financing agendas.

The need to identify both public and private financing solutions is the greatest hurdle facing the Paris COP. It will be a real challenge to create the right kind of incentives and institutional change necessary to ensure a substantial flow of funds from large pools of capital to the transition to a low-carbon, greener economy in developing countries.

And there is evidence that much of this transition will be good business. The Global Climate and Energy Project at Stanford University calculates that in 2013, annual global climate finance flows totalled approximately US\$331 billion. While significant, this is not nearly enough. The Global Commission on Economy and Climate estimates that between now and 2030, the world will have to spend around US\$6 trillion annually on infrastructure alone. The total cost will be around US\$89 trillion if traditional infrastructure is built. If a lower-carbon, sustainable path is followed, the costs would rise to US\$93 trillion, and they estimate that most, if not all, of this would be met by savings in operating costs.

1 The full report is available at <http://web.unep.org/inquiry/publications>.

## The Integration of Financial Reform and Climate Change Agendas

On the broader macroeconomic front, there is a discussion of the integration of climate change into the global financial reform agenda. CIGI's research in this area concludes that that the financial sector faces challenges in coming to grips with the realities set out by the World Bank, the IMF and the OECD (Zou et al. 2015) and financial institutions are pivotal in addressing arguably the biggest challenge the world faces today — sustainable development (Weber and Adeniyi 2015).

Key takeaways from these two CIGI publications:

- Although crucial, classic climate policies — such as carbon pricing, emission standards and technology objectives — do not appear sufficient to address the challenges from climate change that the financial sector is facing. Policies affecting the demand side and supply side of finance, as well as instruments matching supply and demand, need to be aligned with climate objectives to efficiently shift investments toward a low-carbon, climate-resilient economy.
- The financial sector and its governance bodies should have an interest in integrating climate change issues into their risk and stability assessment frameworks, but seemingly differing mandates and the lack of institutional and intellectual links are hindering a timely and well-informed discussion.
- Once the link between climate change and the mandates of international financial sector governance and regulatory institutions is understood, the existing tool kits and processes of these institutions — common standards, principles and guidelines with various levels of legal force, country surveillance and technical assistance — present entry points to mainstream climate-related risks and opportunities into their core operations.
- Enforcement of codes of conduct is a major issue; they mainly focus on the business case of sustainability, rather than the impact on sustainable development, and codes of conduct are compromises that each financial institution can agree to without changing their business to move in a more sustainable direction.

## The Climate Change Issue Now Has Champions

One key takeaway from previous international environmental negotiations is that if the United States is opposed, little happens. US leadership on an issue can make a big difference. President Barack Obama has decided to make climate action one of his legacy issues and he has gone about as far as he can through executive action without Congressional approval. A number of other countries have also pledged serious action.



German Chancellor Angela Merkel and Vice Chancellor and Foreign Minister Guido Westerwelle follow debates after Merkel gave a government declaration on the Copenhagen climate summit at the Reichstag, the seat of the German Parliament (Bundestag), on December 17, 2009 in Berlin, Germany.

Climate change has become an important issue for President Xi Jinping of China because of domestic problems (most Chinese cities are suffering staggering levels of air pollution stemming from coal burning), and much of China is arid or semi-arid, leading to severe water shortages. China is making a deliberate attempt to reduce raw material use and to move to a cleaner economy, with ambitious renewable energy goals. The country has also pledged to stabilize its GHGs by 2030. This is critical to success, given that China now emits more GHGs than the United States and Europe combined. A recent CIGI publication, *How China Can Help Lead a Global Transition to Clean Energy*, states that China has underpromised and has already reached peak coal use, and it could actually reach stabilization of emissions in the early 2020s (Lin, Dong and Fuqiang 2015). So China's bilateral deal with the United States is meaningful.

The European Union has kept climate change as a prominent agenda item, despite the economic and refugee crises that have buffeted the European Union. German Chancellor Angela Merkel was the president of the first climate COP, and retains both an interest in and expertise on the subject. The European Union has by far pledged the most ambitious targets.

It is encouraging that a number of developing countries are taking the issue much more seriously than before. India has announced major targets for renewable energy production and has cut its fossil fuel subsidies dramatically. Brazil is in sight of ending net deforestation in the Amazon and has pioneered the use of alcohol produced from sugar cane as motor fuel. And other countries seem to be making serious commitments. This is an enormous contrast from Copenhagen, where the participation of developing countries seemed to be more reactive.

### Central Banks Are Now Involved

The Governor of the Bank of England, Mark Carney, has highlighted the issue of stranded assets in the British oil industry (principally BP and Shell) as a challenge to the stability of the British insurance industry. Carney is also the chair of the Financial Stability Board, and highlighted the issue at the G20 summit in Turkey. (The members of the G20 are responsible for over 80 percent of the global emissions of GHGs).

The active involvement of financial regulators is also the subject of two CIGI papers. *Central Banks Can and Should Do Their Part in Funding Sustainability* by Andrew Sheng (2015), former chairman of the Securities & Futures Commission of Hong Kong and a senior adviser to the Government of China, concludes that:

Central banks, when purchasing financial assets, should consider selecting assets that will promote sustainability, including climate change mitigation and adaptation. The amount of global investment needed for sustainable energy, for instance, is manageable in the context of the global supply of potential capital. Social impact investing is consistent with a central bank's mandate to maintain price stability. Central banks like to maintain their independence, but they are not independent of the societies that created them or Mother Nature. Central banks that are not yet ready to move in this direction should at least incentivize bankers and asset managers to invest in, or lend to, climate mitigation activities and low-emission growth. Central banks should also support a financial transaction tax, which could fund a new or established global fund for climate mitigation or adaptation or sustainable development more generally.

The second paper, *The Impact of Financial Sector Sustainability Regulations on Banks* by Olaf Weber and Olawuwo Oni (2015) determines that, first, mandatory guidelines have an impact on the sustainability performance of banks. Second, the inclusion of the banking sector into the development of financial sustainability regulations increases the success of the regulation. Third, activities to support the implementation of financial sustainability guidelines and supervising the

compliance with the guidelines are crucial for the success of financial sector sustainability regulations. Fourth, financial sector sustainability regulations have a positive impact on both the financial sector's financial performance and stability and sustainability performance. Finally, more research is needed to explore the impact of financial sector sustainability regulations on sustainable development.

### The Private Sector

There is clearly much greater sensitivity to the issues of climate change in the private sector and it is not all "greenwash" by any means. Until recently, companies managed climate change as a risk to their business. This is a perfectly prudent thing to do, and it carries costs, but now many companies are seeing it as a driving force behind future profitability. Profit centres obviously have more appeal than costs.

The most obvious industry in this sector is energy in general and electricity in particular. One of the popular paths to zero emissions begins with decarbonizing the electricity sector and then "electrifying" the transportation sector. There are virtually no new coal-fired power plants under construction in the Group of Seven countries, and investment in renewable electricity has exceeded conventional electricity in the OECD for a number of years. China's coal usage appears to have peaked. And China and India have issued very challenging renewable energy targets, as has the European Union, with Germany in the lead. Coal still remains an important fuel for many countries, and this will remain a challenge for the future.

Bloomberg New Energy Finance predicts that solar energy will be competitive with natural gas by 2020 in India, China and Europe. North America will take until 2030 or so. Wind is already competitive and will become more so with new developments in energy storage. Technology is another of the keys to success. Cleantech is now one of the fastest-growing sectors in the economy and there is no end in sight, especially if governments move to price fossil fuels properly and enact renewable-friendly policies.



Euro symbol in front of the European Central Bank.



A woman holds up a sign calling for a cut in carbon pollution at a rally held in Melbourne, Australia.

Technology transfer to developing countries is another of the keys to success in Paris and technology partnerships will be critical. What kinds of partnerships could facilitate coordinated climate-related action across several countries? Two CIGI papers by Arunabha Ghosh of the Council on Energy, Environment and Water in India have a number of suggestions.

The first paper, *Climate Technology Partnerships: Form, Function and Impact* (Ghosh, Vijayakumar and Ray 2015) analyzes the purpose, membership and governance of four partnerships: the Montreal Protocol; the Consultative Group on International Agricultural Research; the EC-ASEAN COGEN Programme; and the C40 Cities Climate Leadership Group. These illustrative cases reflect how different design elements could facilitate effective technology diffusion and also reflect diversity across issues (agriculture and environment), regional focus (European Union and ASEAN) and levels of governance (C40 focus on cities).

The second paper, *Fixing Climate Governance through Effective Technology Partnerships* (Ghosh and Ray 2015), discusses why climate technology partnerships are needed, especially in developing countries, which need to adapt to the impacts of climate change and mitigate future GHG emissions. Ghosh and Ray identify three obstacles that have impeded climate-friendly technologies: a lack of appropriate financing, intellectual property restrictions and insufficient or underutilized capacity. New partnerships could be designed to target these challenges and be more effective than previous efforts.

Another area of growth in this sector is environmental goods, which include the clean technologies that provide foundations for sustainable growth in a carbon-constrained world. *Growth, Innovation and Trade in Environmental Goods* by CIGI Senior Fellow Céline Bak (2015), discusses promising initiatives under way to remove impediments to global trade of environmental goods. Global exports in

manufactured environmental goods are now four times larger than global aerospace exports and two-thirds the size of global automotive exports, but there is an absence of trade reports on global trade in environmental goods. Reporting on global trade in environmental goods would provide a comprehensive lens into diversification that will be needed for the transition to low-carbon economies, help countries benchmark the shorter- and longer-term impact of policies such as regulation and fiscal stimulus targeted at green growth, as well as innovation, and strengthen the G20 leaders' commitment to inclusive and sustainable growth by providing visibility into the pace of investments to address climate change.

## Role of the Market and Prices

Although many in the environmental community worry about the commodification of the environment, carbon pricing is rapidly emerging as a preferred solution to the climate problem. There is a growing consensus on the need for a price on carbon. There is a loss of faith in the ability of old-fashioned command-and-control regulation on its own to reduce carbon emissions. There are several ways to price carbon, but the most common are a carbon tax, such as the one used in the Canadian Province of British Columbia and an emissions trading system similar to that of the State of California and Canadian provinces Quebec and Ontario (in 2016). The recent announcement by China of a national cap-and-trade system means almost 35 percent of the world's population will soon be under a carbon pricing scheme.

In September 2014, UN Secretary-General Ban Ki-moon held a climate summit in New York, at which more than 1,000 government, business, finance and civil society leaders signed a letter calling for a carbon price. When private companies agree to be taxed, the public policy challenge for governments becomes a bit easier.

However, a global price for carbon will not be agreed at COP21 in Paris. In fact, it may be a struggle to keep references to carbon pricing in the text. But it is growing in popularity as the primary tool for dealing with climate change. Look for the formation of a carbon pricing club among like-minded countries if there is not positive action at the Paris COP.

According to the IMF and the OECD, we have been paying the polluter to the tune of US\$500–\$600 billion per year in fuel subsidies. When the cost of damages to people and the environment are also added, the total rises to an astonishing US\$6.2 trillion. Many developing country governments have taken advantage of the drop in crude oil prices to eliminate or drastically reduce their subsidies, freeing up billions of dollars to invest in development. But far greater steps are needed to raise carbon prices to a level that covers the damage costs described in the IMF and OECD's figure.



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## About the Author



**David Runnalls** is a distinguished fellow and was formerly acting director of the Environment and Energy Program at CIGI. He also provided strategic advice and support for CIGI Chair Jim Balsillie's role at the United Nations High-level Panel on Global Sustainability. He remains a distinguished fellow at the IISD and a senior fellow at Sustainable Prosperity. David is chair of the International Centre for Trade and Sustainable Development.

# CIGI PUBLICATIONS

## ADVANCING POLICY IDEAS AND DEBATE

### Fixing Climate Governance Series



The Fixing Climate Governance project is designed to generate some fresh ideas. First, a public forum was held in November 2013. High-level workshops then developed a set of policy briefs and short papers written by experts. Several of these publications offer original concrete recommendations for making the UNFCCC more effective. Others make new proposals on such topics as how to reach agreements among smaller sets of countries, how to address the problems of delayed benefits from mitigation and concentrated political opposition, ways that China can exercise leadership in this arena and how world financial institutions can help mobilize climate finance from the private sector. These publications will all be published by CIGI in 2015.

#### **Policy Options Could Increase Ambition in the 2015 Climate Agreement**

*Fixing Climate Governance Policy Brief No. 1*  
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#### **Conducting Global Climate Change Negotiations: Harnessing the Power of Process**

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#### **Six Ways to Make Climate Negotiations More Effective**

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Pamela Chasek, Lynn Wagner and I. William Zartman

#### **Focus Less on Collective Action, More on Delayed Benefits and Concentrated Opponents**

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#### **How China Can Help Lead a Global Transition to Clean Energy**

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#### **Fixing Climate Governance Through Effective Technology Partnerships**

*Fixing Climate Governance Paper No. 3*  
Arunabha Ghosh and Sudatta Ray

# Financing Sustainable Development



## Voluntary Sustainability Codes of Conduct in the Financial Sector

*CIGI Papers No. 78*  
*Olaf Weber and Ifedayo Adeniyi*

This paper discusses the strengths and weaknesses of the financial sector voluntary sustainability codes of conduct. It concludes that enforcement of the codes of conduct is a major issue, that they mainly focus on the business case of sustainability, rather than the impact on sustainable development, and that the codes of conduct are compromises that each financial institution can agree to without changing their business to move in a more sustainable direction.



## The Impact of Financial Sector Sustainability Regulations on Banks

*CIGI Papers No. 77*  
*Olaf Weber and Olawuwo Oni*

This paper analyzes the impact of three financial sector sustainability regulations: the Chinese green credit guidelines, the Nigerian Sustainable Banking Principles and the Bangladesh Environmental Risk Management Guidelines. All three address the connection between financial sector activities and sustainable development, and develop guidelines for sustainable banking policies, strategies, practices, products and services.



## The Environmental Goods Agreement: A Piece of the Puzzle

*CIGI Papers No. 72*  
*Patricia M. Goff*

Can a trade agreement help achieve environmental goals? This paper explores the potential of the Environmental Goods Agreement (EGA) to produce a more positive outcome than previous attempts at environmental chapters within trade agreements. The EGA, while met with challenges, is an important piece of a complex environmental governance puzzle. The question is not whether the EGA will have an impact, but how much of an impact.



## Development of Sustainability and Green Banking Regulations

*CIGI Papers No. 65*  
*Adeboye Oyegunle and Olaf Weber*

Interest in sustainable and green financial regulations has grown in recent years due in part to increasing climate-change risks for the financial sector alongside a need to integrate this sector into the green economy. This paper recalls sustainability's course from fringe issue to central concern, and examines seven countries, all emerging and developing, where regulatory approaches have been implemented successfully.



## Growth, Innovation and Trade in Environmental Goods

*CIGI Policy Brief No. 67*  
*Céline Bak*

Reporting on global trade in environmental goods would provide a comprehensive lens into diversification that will be needed for the transition to low-carbon economies, help countries benchmark the shorter- and longer-term impact of policies such as regulation and fiscal stimulus targeted at green growth, as well as innovation, and strengthen the G20 leaders' commitment to inclusive and sustainable growth by providing visibility into the pace of investments to address climate change.



## Global Treaty or Subnational Innovation? Canada's Path Forward on Climate Policy

*CIGI Policy Brief No. 66*  
*Sarah Burch*

Canada's position on climate change is deeply contentious and constantly evolving, and presents a challenge of multi-level governance (across sectors, civil society and multiple levels of government). This policy brief describes examples of innovative climate change policy at the subnational level, articulates the roles played by different levels of government, and provides a series of recommendations on pathways to carbon-neutral, resilient communities.



## Global Sustainability, Climate Change and Finance Policy: A South African Perspective

*CIGI Policy Brief No. 65*  
*Penelope Hawkins and Olaf Weber*

One of the most important and topical discussions within the global multilateral arena is the challenge of meeting the world's climate finance needs in order to reduce carbon emissions to sustainable levels and support adaptation strategies. The mobilization of finance is key in supporting the transition away from traditional high-carbon or business-as-usual economic pathways toward low-carbon, climate-resilient economic systems.



## The Challenges of Counting Climate Change Risks in Financial Markets

*CIGI Policy Brief No. 62*  
*Jason Thistlethwaite*

Climate change has been identified in recent years as an investment risk, yet existing financial reporting standards do not adequately measure and communicate these risks to investors. A climate change risk disclosure regime has emerged in response, defined by a range of voluntary, regulatory and accounting governance initiatives. This policy brief describes the background for the climate change risk disclosure regime and the challenges that limit its effectiveness, and presents several policy recommendations to improve its capacity to measure and communicate climate change risks.

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