CDM Watch
Scrutinizing Carbon Offsets

Subject: Response to the call for inputs on draft revision of the Draft Modalities and procedures for the implementation of Article 6 of the Kyoto Protocol

31 August 2012

Dear Mr. Seidel, Members and Alternate Members of the JI Supervisory Committee,

We appreciate having the opportunity to provide input on the Draft Joint Implementation Mechanism (JI) Guidelines. We hope that our suggestions will contribute to the reform of the JI in a way that will ensure that JI will be a mechanism capable of delivering real, measurable and additional GHG emission reductions. Below we present our views on how the proposed Draft JI Guidelines can be further developed in order to improve the mechanism.

First we must put the future of the JI in context. The window of opportunity to prevent catastrophic climate change is rapidly closing. Several studies show that current pledges are woefully insufficient to keep warming below 2°C. Furthermore, they show that loopholes such as the surplus allowances (AAUs) from the first Kyoto commitment period (commonly referred to as 'hot air') could negate all current pledges and enable developed countries to meet mitigation targets while continuing with business-as-usual levels of emissions.[1] We are now on an emissions path that could lead to warming of 4°C or more.[2] In addition, impacts associated with even 2°C of warming have been revised upwards and are now considered "dangerous" and "extremely dangerous".[3] Maintaining a reasonable likelihood of limiting temperature increases to within 2°C will require much higher levels of ambition by all nations.

The insufficient current ambition levels also have led to a severe price decay in the carbon markets. At current price ranges, it is all but impossible to implement JI projects that are truly additional. Non-additional JI projects undermine mitigation goals, especially when they are implemented in countries with a large AAU surplus. A large supply of such ERUs will not only hamper climate goals but also severely undermine carbon markets.

MEMBERSHIP OF THE GOVERNING BODY

We support that the members *shall be nominated by the relevant constituencies and UNFCCC admitted non-governmental observer organisations*, as suggested in brackets in **paragraph 14**. The participation of NGOs is essential in JI policy making, as they can give impartial views and be fully independent of a particular Host or Investor Party.

HOST PARTY PARTICIPATION REQUIREMENTS

We support the suggestion that specific time limits should be established for the consideration of JI projects by Host Parties' DFPs (as bracketed in **paragraph 23b**), **as well as for providing information to the Secretariat by the Host Parties** (90 days as suggested in brackets in **paragraph 24**). This will increase the transparency and predictability of the timelines in the JI cycle.

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[1] UNEP (2011). Bridging the Emissions Gap. A UNEP Synthesis Report.

Kartha, S. and Erickson, P. (2011). Comparison of Annex 1 and non-Annex 1 pledges under the Cancun Agreements. *SEI Policy Brief.* Available at: http://sei-us.org/publications/id/424

Rogelj, Joeri, Julia Nabel, Claudine Chen, William Hare, Kathleen Markmann, Malte Meinshausen, Michiel Schaeffer, Kirsten Macey, and Niklas Höhne (2010). "Copenhagen Accord pledges are paltry." Nature 464, 1126-28.

Meinshausen, Malte, Nicolai Meinshausen, William Hare, Sarah C. B. Raper, Katja Frieler, Reto Knutti, David J. Frame, and Myles R. Allen (2009). "Greenhouse-gas emission targets for limiting global warming to 2°C." Nature 458, 1158-63. Available at: http://dx.doi.org/10.1038/nature08017.

[2] Betts R., Collins M., Hemming D., Jones C., Lowe J., Sanderson M., (2011). When could global warming reach 4°C? Phil. Trans. R. Soc. A 2011 vol. 369, 1934 p.67-84 doi: 10.1098/rsta.2010.0290

[3] Anderson K., Bows A. (2011). Beyond 'dangerous' climate change: emission scenarios for a new world. Phil. Trans. R. Soc. A 2011 vol. 369, 1934 p.20-44, doi: 10.1098/rsta.2010.0290

HOST PARTY ELIGIBILITY REQUIREMENTS

We agree that a Party wishing to host a JI project has to accept a legally binding QELRO for the second commitment period (CP2) of the Kyoto Protocol in order to be able to host JI projects that can generate ERUs post 2012, as proposed in **paragraph 27**. Furthermore, countries must have a reduction target for CP2 that is lower than their 2008 emissions. Only then will it be possible to avoid the laundering of the AAU surplus. Also, only countries with high ambition levels have an incentive to set their JI baselines realistically and stringently enough. **Requiring a CP2 commitment with emission cuts below 2008 emission levels is therefore the single most important measure that needs to be taken to ensure the environmental integrity of JI.**

VALIDATION AND REGISTRATION

The proposed procedure of the validation and registration does not include the option of a review of the project by the Governing Body. Registration is exclusively in the hands of a Host Party. The proposed modalities and procedures do foresee a review procedure at the stage of ERU issuance (**paragraph 38**), where it can be triggered by three members of the Governing Body. Without any influence on project registration, members of the Governing Body will not be able to provide their feedback regarding potential non-compliance of a project until the last step of the JI cycle.

If host countries have unambitious targets for CP2, it is in their interest to register many JI projects that could potentially help to indirectly sell AAUs, which shadow ERUs. Only with a strict QELRO requirement (see above) and with a review process by the Governing Body before project registration can the JI's environmental integrity be ensured.

We recommend that the review procedure by the Governing Body is included at the stage of validation (similar to the current Final Determination) or registration in addition to the review option at the stage of ERU issuance.

BASELINE SETTING, ADDITIONALITY AND MONITORING

The list of requirements regarding the baseline setting in **paragraph 2 of the Appendix** should be added with the following points:

- ***Taking into account autonomous (business-as-usual) improvements in efficiencies and regular technology upgrades.***
  The baseline has to become more stringent over time as business-as-usual improvements in efficiency can be expected. Such autonomous improvement factors have to be set according to the technology lifetimes and common practice in the relevant sector of the host country.
- ***Baselines have to be set in such a way that baseline emissions do not exceed historical emissions level of a respective installation.***
  If baseline emissions are allowed to be higher than historical emissions levels ERUs may be earned for business-as-usual emissions level or even for net emissions increase. This should not be allowed in the second commitment period because it does not help mitigate climate change, and only net emission reduction should be credited. The target of the Kyoto Protocol is to reduce net emissions from Annex-1 countries, as compared to a base year (i.e. cap is established on a historical basis). Thus the projects in Annex-1 countries should serve the same target - that is, to reduce emissions as compared to the historical levels.

  The following example can illustrate the problem with increasing baseline emissions. Some of the current JI projects involve the expansion of production that results in an increase of GHG emissions, but ERUs are claimed for lower emissions level per unit of product. The baseline of such projects is the production increase with a low-efficient technology, while the project scenario is the installation of a high-efficient technology. While such an approach could be acceptable under the CDM where the development and production expansion is inherent, it does not make sense in an Annex-1 country with a tight emission cap because it results in the net loss of assigned amount and contradicts the aim of the Kyoto Protocol.

Setting baselines correctly and conservatively is essential for maintaining environmental integrity (paragraph 3 of the Appendix) we therefore propose the following clarification: "*3. The baseline shall be validated by an AIE and approved by the host Party…*"

Baselines need to be regularly reviewed and updated. Baselines should be reviewed at the end of each commitment period or at least every five to eight years. Any review and update of the baseline must be validated by an AIE.

All JI projects currently registered must go through a review to renew their crediting period for CP2. The procedures for such a renewal of the crediting period must include an assessment of the baseline scenario.

Considering the issues raised about the environmental integrity of many registered JI projects as well as their potential to flood the carbon market with cheap non-additional ERUs, the continuation of ERU generation by them after 2012 would mean the carry-over of the same problem to the next commitment period. Even though many JI PDDs list emission reductions beyond 2012, it is hard to believe that post-2012 reductions were seriously considered in the investment analysis at the time of project decision-making. The prolonged uncertainty with the continuation of the Kyoto Protocol and then actual Parties' QELROs, which will define future demand and price of ERUs as well as other real or perceived risks of JI did not allow the business to rely on the future incomes from post-2012 ERUs. For this reason the additionality of the projects that claimed that post-2012 ERUs were crucial in their investment decision can be questioned.

Some of the projects that started in the first commitment period may still truly rely on JI as the critical source of income and would discontinue operation without JI[4]. Yet even those projects need to be reviewed to see for example if there was a change in legislation that impacts the additionality of JI projects.[5]

Thus we strongly recommend a procedure for the renewal of the crediting period for projects registered in the first commitment period that evaluates the baseline scenario and additionality claims.

We recommend that prior consideration requirements are made mandatory. These can be modelled on the procedures currently used in the CDM.

Prior consideration, ie. evidence that JI was taken into account at the planning stage of the project, can serve as one indicator that JI was instrumental in the implementation of an emission reduction activity. Proof of prior consideration should therefore be a mandatory requirement for the demonstration of additionality. The concept of prior consideration was discussed by the JISC in 2011 but consensus was not reached. Some members held that the concept of prior consideration would amount to introducing new requirements. This argument is not valid. Article 6 of the Kyoto Protocol stipulates that reductions need to be additional to any that would occur in the absence of JI. The concept of prior consideration is hence not a new requirement, it is a clarification of the existing requirements. The introduction of the requirement of prior consideration of JI should not hamper the development of new emission reduction activities under JI. It should prevent non-additional projects from taking advantage of retroactive crediting in JI in cases where JI didn't play a role in implementation.

Many JI projects that are currently being registered claim emission reductions starting from 1 January 2008 or even receive 'early credits'. **In order to restrict such abuse of retroactive crediting, JI projects registered in CP2 shall not be allowed to claim ERUs retroactively for the reductions that occurred in the first commitment period.**

MONITORING

We suggest adding to **paragraph 7 of the Appendix** that the procedure and methodology of the calculation of baseline and project emissions, leakage and emission reductions shall be consistent with the national inventories guidelines and methodologies applied in a Host Country's national GHG inventories, to the greatest possible extent. ERUs are converted from a Host Country's assigned amount, and emission reductions achieved in JI projects are accounted for in its national GHG inventory reports. Reported amounts of GHG emissions in national inventories eventually defines the number of AAUs to be retired. Thus it is important that the calculation of emissions and emission reductions on the project level is in line with GHG accounting rules at the country level.

[4] For example, landfill gas flaring is not profitable by itself as it requires some operational expenses which cannot be recovered without external support, unless it is mandatory due to legislation requirements.

[5] For example, 12 Central and Eastern European Countries (CEECs) countries joined the EU since 2004. These new member states must adopt the body of EU law and regulation, known as the acquis communautaire (acquis). Accession countries were given a "grace period" to implement these new laws. This grace period directly impacts JI projects. For example, the EU landfill directive requires that landfills receiving biodegradable waste must have a gas collection system. Yet there is a transition period for existing landfill sites. That means, once the grace period is over, CEECs should no longer be able to generate ERUs through landfill projects.