



Carbon Market Watch's briefing note for SBSTA 51 & COP25

Prepared for COP 25, December 2019

Carbon Market Watch encourages Parties to work towards an agreement for Article 6, while highlighting that a deal should not be reached at any cost, and that certain aspects related to environmental integrity and safeguards cannot be compromised upon. In addition, the selection of a number of issues to be postponed to a work programme, for further work in the future, must be dealt with very carefully, as it is unclear when - or even if - this work programme will eventually be completed. Giving the illusion of a strong set of rules for Article 6 by finding a partial agreement which does not establish the necessary level of environmental integrity could be more harmful than not finding any agreement.

Accurate accounting to promote environmental integrity

Accounting for units in a manner that truly reflects the transfers of *emission reductions* is paramount. While resolving all the existing uncertainties is necessary, finding the solutions to avoid double counting is of the highest importance.

This will require 1) transparent tracking of all credits through an international transaction log and national registries, 2) the application of corresponding adjustments at the point of first transfer/transfer for every carbon credit, and 3) the integration of international accounting rules to ensure that double counting is avoided across Article 6.2, Article 6.4, and CORSIA, as well as with any other mechanism and the voluntary carbon market. Corresponding adjustments should be applied to any credit or unit issued under Article 6, regardless of whether it is used by a Party or by another entity.

In addition to these crucial elements, Carbon Market Watch encourages Parties to further discuss the implications and risks of:

1. Recognising allowances transferred through linked emissions trading systems (ETs) as international transfers of mitigation outcomes (ITMOs) and counting such transfers under Article 6.2. The various ways of accounting for the transfer of allowances raise significant concerns about the environmental integrity of such accounting because allowances do not necessarily represent emissions when an ETS is oversupplied, or when banking and borrowing are allowed.
2. Accounting for the trade of ITMOs for Parties which have adopted single year targets. While there are several ways of accounting for transfers under such a scenario, many have significant shortcomings and are subject to gaming. This is the case in particular when the rules don't specify the shape of the emissions trajectory. A climate-friendly trajectory requires a rapid decrease in emissions today, rather than a slow transition and betting on rapid reductions in the future.

Going beyond zero-sum offsetting

Parties should adopt rules which deliver on the promise of the Paris Agreement to progressively increase ambition and to deliver an overall mitigation in global emissions through Article 6. The latter requires the application of a partial cancellation rate for every credit issued under Article 6. While conservative baselines are necessary for the environmental integrity of Article 6 (see below), they alone will not deliver an Overall Mitigation in Global Emissions (OMGE). Therefore, a partial cancellation should be applied to every transferred credit. OMGE requires that a proportion of the underlying emission reductions are not claimed by any entity. Simply setting conservative baselines would not deliver OMGE because the emission reductions which are not credited will still be captured in the host country's inventory, and counted towards demonstrating achievement of its NDC target. To achieve overall global emissions reductions, the reductions which are not claimed by the acquiring country should also not be claimed by the host country, and hence must be subject to corresponding adjustments by the host country.

In the spirit of the Paris Agreement, any form of perverse incentive against progress in the nationally determined contributions (NDCs) should be avoided. This will require that Article 6 credits/units can only be generated from sectors and gases covered by the host country's NDC. Should any units be issued outside the scope of an NDC, they should be subject to corresponding adjustments applied to emissions inside the NDC scope.

Promoting ambition in the carbon market also requires that baselines are set at a conservative level. Baselines should be set below business as usual. In particular, for countries which have hot air in their NDC, setting baselines at the level of the NDC target would not be sufficient.

Correct mistakes from the past

Carbon Market Watch urges Parties to prevent a full transition of Kyoto Protocol units and projects into the Paris Agreement markets. No Kyoto Protocol units should be eligible post-2020 (i.e. neither CERs, ERU, RMUs, nor AAUs), all projects should be re-assessed against stringent quality criteria, and existing methodologies should also be re-evaluated.

In addition, Parties must recognise the detrimental impacts which Kyoto Protocol mechanisms, including the Clean Development Mechanism (CDM), have had on local communities and the environment. In order to improve social and environmental safeguards, and protect and promote human rights, all mitigation projects must be required to consult local stakeholders before and during their implementation. Furthermore, a grievance mechanism must be established that is governed by an independent body. Such grievance mechanism must operate in a manner that is independent, rights-based, accessible, equitable, transparent, legitimate, and efficient. The work programme under Article 6 should include clear items to further define local stakeholder consultation rules as well as rules for the functioning of the grievance mechanism.

Prevent current challenges from materialising again in the future

In addition to recognising the environmental integrity deficiencies of Kyoto Protocol units, rules should be adopted to ensure that the situation we are currently in - i.e. large amounts of old units with

questionable environmental integrity threatening to undermine the future of climate policies - does not repeat itself in the future when transitioning between NDC periods. This means that Parties have to operationalise the principle of ensuring that “use of article 6 does not lead to an increase in emissions within or between NDC periods” (a principle currently included in several sections of the draft texts). A key requirement for this is to adopt measures to avoid the transfer and use of hot air credits or the eternal carry-over of old units. To this effect, measures are necessary to:

1. Set a cap on the transfer of ITMOs generated under article 6.2, e.g. in any NDC period, a Party may transfer ITMOs generated under article 6.2 up to a volume equivalent to 1% of its average annual emissions over the 2010-2012 period, multiplied by the number of years covered by that NDC period.
2. Prevent the banking across NDC periods of ITMOs generated under article 6.2, e.g. by requiring that acquiring Parties apply corresponding adjustments to a calendar year which is included in the same NDC period as the calendar year in which the mitigation outcome was achieved.
3. Limit the lifetime and/or banking of A6.4ERs, e.g. by limiting the lifetime of A6.4ERs to 5 years and/or allowing the transfer of A6.4ERs across NDC periods only up to a volume equivalent to 1% of the Party’s average annual emissions over the 2010-2012 period, multiplied by the number of years covered by its NDC period.

Key recommendations:

- Avoid double counting by requiring the application of corresponding adjustments for the transfer of every credit/unit under Article 6, and by establishing comprehensive transparency rules to connect Article 6 with the Transparency Framework.
- Do not allow any pre-2020 units for use towards NDCs, and re-assess all pre-2020 projects against stringent quality criteria.
- Establish a grievance mechanism governed by an independent body and require that stakeholders be consulted before and during the implementation of any Article 6 project.
- Adopt a partial cancellation rate for application to each Article 6 credit/unit.
- Adopt conservative baselines which prevent the issuance of any hot air credit.
- Set a cap on the transfer of ITMOs generated under article 6.2 in any NDC period.
- Prevent banking across NDC periods of ITMOs generated under article 6.2.
- Limit the lifetime and/or banking of A6.4ERs.

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