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UN negotiators search (yet again) for common ground on carbon markets

Paris Agreement Article 6 must reduce emissions fairly and effectively

Technical discussions at the UN climate body UNFCCC on the Paris Agreement carbon market mechanisms continue from 31 May to 17 June. Key outstanding issues in negotiations include whether problematic carbon credits from the Kyoto Protocol can continue to be used under the Paris Agreement and how market mechanisms should be designed to enable greater climate ambition.

For CMW's overall perspective on Article 6, see here. CMW has also been publishing a series of technical submissions, responding to a call for input from the UNFCCC: April, May, June.

On 31 May through 17 June, the UNFCCC will virtually host the first "sessional period" of the year, during which Party delegates will continue discussing technical aspects of the Paris Agreement in preparation for the UN climate conference COP 26 in Glasgow.

Guidelines on Article 6, regulating carbon market mechanisms, are one of the final major outstanding issues regarding the practical implementation of the Paris Agreement. Key decisions with considerable long-term consequences remain to be taken at the COP 26 later this year -- or in a future COP if no agreement is reached again this time around -- such as i) whether carbon credits created under the Kyoto Protocol will be permitted to transition to the framework of the Paris Agreement, ii) how double counting of emission reductions can be avoided, and iii) how market mechanisms can be designed to enable climate ambition, and crucially avoid watering down the Paris objectives.

Although these points are being hashed out yet again by negotiators, the way forward should be very clear, as Carbon Market Watch has long advocated.

Kyoto Protocol credits cannot be used under the Paris Agreement

The Paris Agreement's predecessor, the Kyoto Protocol, established the Clean Development Mechanism (CDM) allowing developed countries to buy emission reductions from developing countries in the form of carbon credits.[1] In theory, this type of development finance can be a

[1] For a full overview on carbon markets and on CMW's views on Article 6, check out our 2020 publication: "Carbon Markets 101: The Ultimate Guide to Market-Based Climate Mechanisms".

win-win to support important projects while also reducing emissions. However, in practice, the CDM lacked stringent safeguards against harm to the environment and to local and indigenous communities, and CDM finance often did not result in an extra reduction in emissions.

Companies were able to use CDM credits in emission trading systems, like the EU carbon market (EU ETS), to continue polluting instead of reducing their emissions. What's more, such credits did not necessarily represent actual "extra" emission reductions. Around 85% of CDM projects and 73% of potential credits from 2013-2020 in fact over-estimated their emission reductions.

If CDM credits are allowed to freely transition to the Paris Agreement era, as several Parties are advocating (e.g. Brazil, India), the market could become flooded with up to 4 billion junk credits. This would evidently be a significant loss for the climate, since such credits represent past emission reductions that in most cases would have happened even in the absence of the CDM (i.e. the projects did not need the revenues from carbon credits to reduce emissions). It also would negatively impact project developers, who would be selling credits in a vastly oversupplied market with corresponding low prices, which is already the situation today.

Carrying over any CDM credits poses too great a risk for the climate and for the proper functioning and credibility of the Paris Agreement's envisaged carbon market mechanisms to be permitted. This perspective is also publicly supported by 32 countries that signed the San Jose Principles for High Ambition and Integrity in International Carbon Markets.

Moreover, the UN body that manages the CDM confirmed in December 2020 that there is no clear basis for it to continue operation post-2020.[2] At the COP 26, it's thus up to Parties to officially confirm the same view, rather than lead a misguided effort to enable CDM credits to transition.

Markets must increase climate ambition - that means robust safeguards and meaningful emission reductions

Above all else, carbon markets are a means to an end. While they can play a role in lowering emissions -- when they are functioning well -- they can also be detrimental to climate action if credits substitute domestic action or lack environmental and social integrity.

[2] CDM Executive Board (2020): "Meeting report: CDM Executive Board 108th meeting", available at https://cdm.unfccc.int/EB/archives/meetings_20.html.

DATE 27/05/2021

While not all CDM projects should be painted with the same brush, many have ended up harming local communities and Indigenous Peoples instead of benefitting or empowering them. These impacts could have been avoided, or at the least mitigated, had there been more clearly defined social safeguards under the Kyoto Protocol framework, which need to thus be incorporated in Article 6 guidelines to avoid the same errors. These include embedding the need to protect, respect and promote human rights and the rights of Indigenous Peoples, requiring adequate public consultation processes and establishing a recourse mechanism in case of adverse impacts.

To ensure market mechanisms under the Paris Agreement enable ambition, first and foremost they must guarantee environmental integrity. Double counting, whereby two entities each claim the same emission reduction, must be avoided in all its forms by having strict transparency and accounting provisions, including applying a "corresponding adjustment": e.g. a country reduces its emissions by 100tCO_2e, sells 10 credits to another entity, and thus would need to report a reduction of only 90tCO_2e.

To go beyond the zero-sum game mentality that has so far beset carbon markets, credits under Article 6 of the Paris Agreement should be subject to an "automatic partial cancellation rate". In practice, this would mean that when a credit is first issued or transferred, a fixed share of the CO_2e reduction units embodied in the credit would be cancelled (i.e. redirected to a cancellation account in practical terms). Rendering a share of CO_2e "unclaimable" in this way would mark an important step in guaranteeing emissions are reduced overall rather than simply compensated.

Countries should reach mitigation targets through coherent domestic emission reductions, and only use the Paris Agreement's market mechanisms to disburse results-based climate finance. Developed countries are falling short of the 2020 target to annually mobilise $100 billion in urgently needed climate finance in developing countries. Carbon market mechanisms can play a role in this context, but it is crucial to ensure they deliver concrete, measurable contributions to sustainable development and climate mitigation, rather than cheap and potentially low-quality credits dubiously claimed as emission reductions. A balance should also be found between high measurement, reporting and verification costs and the need to measure results; carbon markets should certainly not be the only, nor even the main, channel for climate finance contributions.

To avoid the errors of the Kyoto Protocol, it is vital to guarantee that CDM credits do not transition to the Paris Agreement era and that greater ambition is embedded from the outset in the future market mechanisms. Better to correctly design these mechanisms from the start --

even if it means ultimately delaying a final decision on Article 6 to a future COP -- than to make dubious compromises only for the sake of finalising guidelines on Article 6 at COP 26.