CARBON MARKET WATCH[1] RECOMMENDATIONS TO THE CMP8 ON FURTHER GUIDANCE AND REVIEW OF JOINT IMPLEMENTATION (JI)

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INTRODUCTION

The future of the Joint Implementation (JI) has to be put 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. The insufficient current ambition levels have also 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. JI credits (ERUs) are shadowed by AAUs. If AAUs do not represent actual emissions reductions (ie are surplus "hot air") then JI credits can be used to launder hot air AAUs. A large supply of non-additional ERUs will not only hamper climate goals but also severely undermine carbon markets.

The large current oversupply is further increased by the large number of issued JI credits that come from clearly non-additional projects in countries with very weak pledges and large AAU surpluses. Such "hot air" laundering must be stopped immediately. This ongoing reform must turn the JI into a mechanism capable of delivering real, measurable and additional GHG emission reductions that serve the efforts to mitigate climate change.

RECOMMENDATIONS

This paper provides recommendations for CMP decisions for adoption at CMP8 and outlines key issues pertaining the JI. The recommendations refer to the provisional agenda item

- 8. (a) Guidance on joint implementation: *Annual report of the Joint Implementation Supervisory Committee (JISC) to CMP8* and
- 8. (b) Review of the joint implementation guidelines Issues relating to joint implementation.[2] *Revised set of key attributes and transitional measures and draft revised joint implementation guidelines*

Carbon Market Watch urges Parties to address the following JI related issues as a matter of priority:

1. **Host Party eligibility must depend on ambitious QELRO**
2. **No CP1 AAUs for JI Projects during the gap period**
3. **Require review procedure at registration stage**
4. **Strengthen criteria and review Procedures for Baseline Setting**
5. **Strengthen additionality requirements**
6. **Implement procedures to renew crediting period**
7. **Improve Public Input on Projects**

[1] Formerly CDM Watch

[2] CMP7 requested the Joint Implementation Supervisory Committee (JISC) to draft a revised set of key attributes and transitional measures dealing with possible changes to the JI guidelines, and to present them for discussion to the CMP8 in order to develop revised JI guidelines for adoption at CMP9: http://unfccc.int/resource/docs/2012/cmp8/eng/05.pdf

1. HOST PARTY ELIGIBILITY MUST DEPEND ON AMBITIOUS QELRO

A Party wishing to host JI projects to generate ERUs post 2012, must accept a legally binding QELRO for the second commitment period (CP2) of the Kyoto Protocol. Furthermore, Parties must have a reduction target for CP2 that is lower than their 2012 emissions. Only then will it be possible to avoid the laundering of surplus AAUs. 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 2012 emission levels is therefore the single most important measure that needs to be taken to ensure the environmental integrity of JI.** The appropriate language to this effect should be added to **paragraph 27** of the draft revised joint implementation guidelines.

2. NO CP1 AAUS FOR JI PROJECTS DURING THE GAP PERIOD

For each ERU sold, the host country has to retire one of its AAUs to avoid double counting. Since AAUs are tied to the Kyoto commitment period, it is not clear what will happen to the JI in the absence of a second commitment period, or what types of AAUs be used to "shadow" ERUs during the so called gap period, after the end of the first Kyoto commitment period and before a second commitment period will enter into force and Annex B countries under CP2 have received their AAUs.

In **paragraph 21** of the JISC annual report to CMP8 the JISC recommends that either AAUs from the first commitment period can be used or that future AAUs from the second commitment period be deducted from future emission reduction targets adopted by Parties hosting JI project.

Using AAUs from the first commitment period is highly problematic, as current experience under Track 1 shows: Countries with large amounts of AAU surplus have started to use JI Track 1 to convert a significant number of AAUs to JI credits. In other words, countries with large AAU surplus can use the JI for "hot-air laundering." This not only undermines environmental integrity but also threatens the viability of carbon markets.

The second option is also problematic in terms of preserving environmental integrity: **Given the uncertainty of future pledged and QELROS, it does not seem prudent to shadow ERUs during the gap period with future AAUs.**

The cleanest solution would be to only allow issuance of CP2 ERUs once CP2 AAUs have been issued. However, the issue of how to treat JI credit issuance during the gap period is less problematic if the recommendations to strengthening the environmental integrity of the JI as elaborated in this document are implemented.

Carbon Market Watch furthermore recommends that Track 1 ERUs from countries with large amounts of surplus AAUs should not be bankable.

3. REQUIRE REVIEW PROCEDURE AT REGISTRATION STAGE

The proposed procedure for validation and registration does not include the option of a review of the project by the governing body, who will supervise joint implementation under the guidance of the CMP. The current guidelines suggest that registration is exclusively in the hands of a Host Party. A review procedure is only proposed at the stage of ERU issuance (**paragraph 48** of the draft revised joint implementation guidelines), where it can be triggered by three members of the governing body. However, without any influence on project registration, members of the governing body will not be able to supervise compliance with essential JI requirements of a project until issuance of EURs, 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 surplus 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.

→ Carbon Market Watch calls upon Parties to

- ***Decide that the optional review procedure by the governing body is included at the stage of validation or registration in addition to the review option at the stage of ERU issuance.*** *A similar procedure to the one proposed in paragraph 48 during ERU issuance could be used for the review procedure during registration.*

4. STRENGTHEN CRITERIA AND REVIEW PROCEDURES FOR BASELINE SETTING

The proposed baseline setting rules as outlined in paragraph 30 should be strengthened to ensure the environmental integrity of the JI:

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that autonomous (business-as-usual) improvements in efficiencies and regular technology upgrades must be taken into account when baselines are set.*** *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.*

The proposed rules state in **paragraph 33** of the draft revised joint implementation guidelines that "the baseline shall be validated by an accredited independent entity and shall be approved by the host Party prior to the registration of the activity." Yet countries with weak emission reduction targets have an incentive to set weak baselines. This will lead to the over-issuance of JI credits.

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that baselines must be reviewed and approved by the governing body to avoid weak baselines and over-crediting.***

5. STRENGTHEN ADDITIONALITY REQUIREMENTS

Paragraph 30 of the draft revised joint implementation guidelines outlines the conditions that must be met for a project to be considered additional. Additionality is of vital importance in JI, especially in host countries with lenient reduction targets because otherwise JI can be used to launder surplus AAU, so called "hot air." Yet the current text does not include the concept of prior consideration. Prior consideration, ie. evidence that JI was taken into account at the planning stage of the project, is an important indicator that JI was instrumental in the implementation of an emission reduction activity. The concept of prior consideration is not a new requirement, but a clarification of the already existing requirements and fully in line with the Article 6 of the Kyoto Protocol which stipulates that reductions need to be additional to any that would occur in the absence of JI. Many JI projects registered only in 2012 claim emission reductions starting from 1 January 2008 or before. Such practices undermine the environmental integrity of JI.

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that proof of prior consideration should be made a mandatory requirement for the demonstration of additionality.***

Paragraph 32 of the draft revised joint implementation guidelines outlines that Host Parties may utilize positive lists of activity types that are automatically deemed additional. But the text is silent on how the environmental integrity of such lists is ensured.

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that positive lists must be reviewed by an independent auditor and approved by the governing body to uphold their environmental integrity.***
- ***Decides that positive lists are valid for up to 5 years and must be reviewed and updated thereafter.***

6. IMPLEMENT PROCEDURES TO RENEW CREDITING PERIOD

Paragraph 35 of the draft revised joint implementation guidelines outlines procedures on selecting and renewing crediting periods but the paragraph is silent on how existing JI projects will be treated. Carbon Market Watch is of the view that all existing JI projects should go through a process to renew their crediting period as outlined in paragraph 35. Many existing JI projects are no longer additional, given ongoing changes in industry and policy. It is possible that 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[3]. Yet even those

[3] 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.

projects need to be reviewed to see for example if there was a change in legislation that impacts the additionality of JI projects.[4]

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 of each project.

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that all JI projects currently registered shall 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 for the second commitment period.***

7. IMPROVE PUBLIC PARTICIPATION

Paragraph 45 of the draft revised joint implementation guidelines outlines that monitoring reports be made publicly available through the UNFCCC Secretariat. Yet the draft guidelines do not include any provisions for providing input on these monitoring reports. It makes little sense to publish monitoring reports if there is no possibility to submit comments.

→ ***Carbon Market Watch calls upon Parties to***

- ***Decide that all JI projects must go through a 30 day commenting period after the monitoring reports have been published. Relevant comments have to be addressed.***

[4] 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.