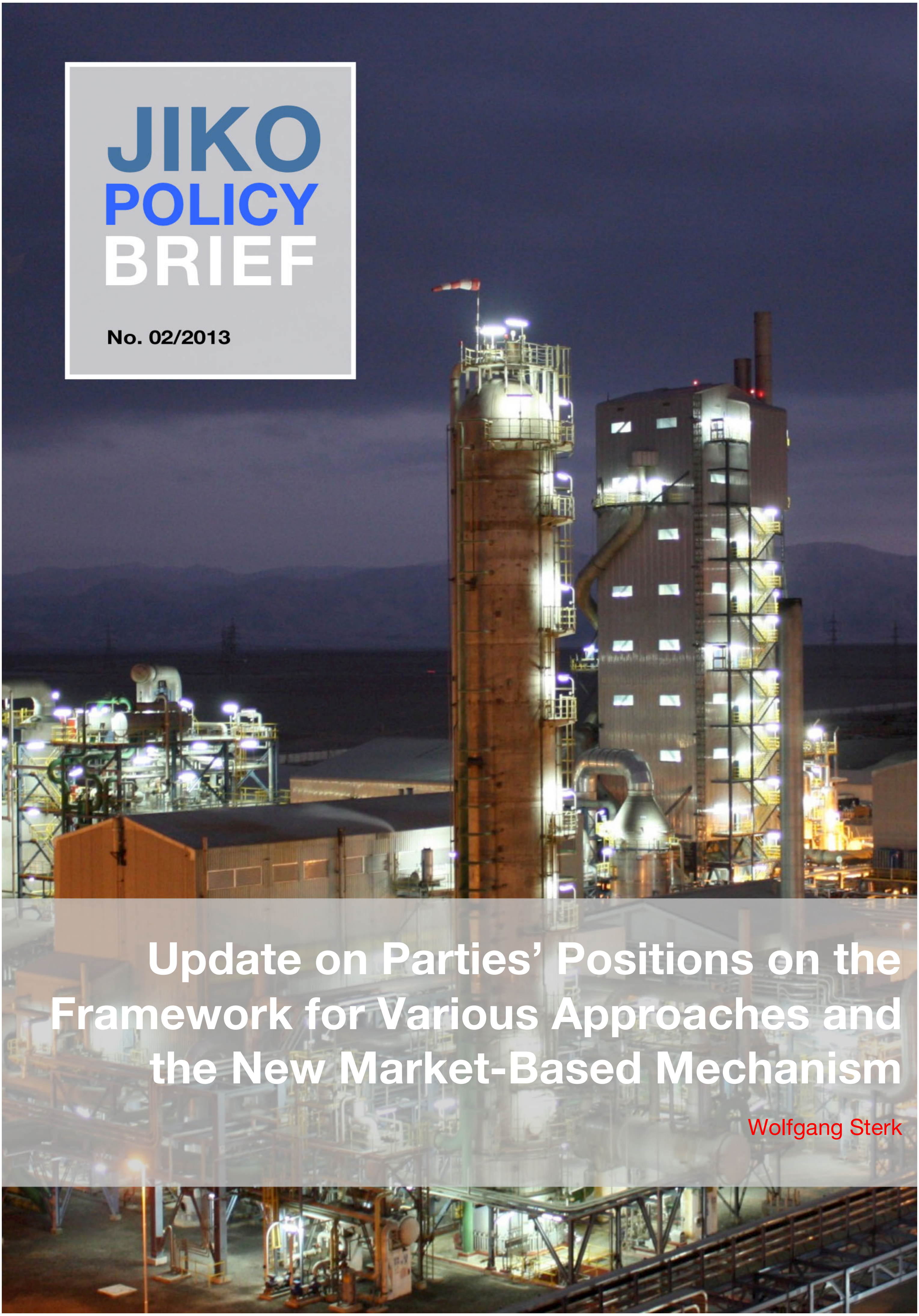

JIKO POLICY BRIEF

No. 02/2013

Update on Parties' Positions on the Framework for Various Approaches and the New Market-Based Mechanism

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May 2013

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Summary

Parties have been discussing to establish a centralised new market-based mechanism (NMM) and to consider establishing a "framework for various approaches" to govern decentralised market approaches. COP 18 in Doha decided to invite submissions of views by 25 March 2013. This policy brief is an update on JIKO policy paper 2/2012, *Current Proposals and Positions on New Market Mechanisms*, and therefore focuses on aspects that are new compared to last year's negotiations.

So far, there are ten submissions on each of the FVA and the NMM. Overall, the submissions reveal only marginal conceptual or political advancement compared to last year's discussions. Most submissions are very short and do not go into substantial technical detail. The main stumbling stones seem to be political differences rather than lack of conceptional clarity.

On the FVA, there is consensus that a common infrastructure of registries and possibly an ITL would be needed to ensure proper tracking of units and prevent double counting. However, there continues to be a fundamental controversy on whether the FVA should have the function to approve decentralised systems or only to facilitate their development and operation. European and many developing countries have been in favour of the former while Japan, New Zealand and the USA have argued for the latter. There seems to be no rapprochement of positions.

One item that seems to have been clarified is that the FVA would only address international implications of systems, not purely domestic approaches. One sensitive issue that now seems to have made it on the agenda is the potential for double counting by buyer and host countries. Japan proposes to add the emissions equivalent of the transferred credits to the host countries' reported emissions.

On the NMM opinions seem to continue to be divided on whether it should be sector- or project-based. Several developing country submissions posit that both should be allowed and that the definition of boundaries should be left to the discretion of host countries, while the EU urges the need for common definitions based on the UNFCCC guidelines for reporting and review.

Only the EU and Tunisia go into some technical details on the NMM, but these are mostly a repetition of past discussions. However, one may note positively that not only the EU but also a number of developing country submissions support a prompt start for the NMM with concrete pilots. Tunisia notes that it is already preparing a pilot NMM in its cement sector. Given the lack of demand in the carbon market, Tunisia suggests a possible way forward for the short to medium term by proposing that buying NMM credits should count towards the buyer countries' financial commitments rather than emission commitments.

One problem for progress on both the FVA and the NMM is Bolivia's continued opposition to any scale-up of market mechanisms. If Bolivia maintains its uncompromising position and is supported by other countries, it may be impossible to make any kind of progress in the negotiations and the development of new approaches may have for the time being have to take place outside the UNFCCC context.

1 Introduction

Countries have been discussing "various approaches, including opportunities for using markets, to enhance the cost-effectiveness of, and to promote, mitigation actions" for several years. At COP 17 Durban, Parties decided to establish a centralised new market-based mechanism (NMM) and to consider establishing a "framework for various approaches" to govern decentralised initiatives. COP 18 in Doha decided in decision 1/CP.18 to invite submissions of views by 25 March 2013.

The following summarises Parties' views on the issues raised in the COP decision.[1] This policy brief is an update on JIKO policy paper 2/2012, *Current Proposals and Positions on New Market Mechanisms*[2], and therefore focuses on elements that are new compared to last year's negotiations.

[1] Parties' submissions are available for download' at https://unfccc.int/documentation/submissions_from_parties/items/5901.php.

[2] Available for download at http://jiko-bmu.de/1152.

2 The Framework for Various Approaches

2.1 Issues to be Addressed

Parties have so far had fundamental differences on the basic purpose of the FVA. On one side, European and many developing countries have posited that it should have the function to approve systems and credits for international use. On the other side, in particular Japan, New Zealand and the USA have taken the position that the FVA should only have a facilitative function, leaving the development of standards and approval of activities and credits to the implementing Parties.

This controversy could not be resolved in Doha. Decision 1/CP.18 identified the following issues for further discussion:

- The purposes of the framework;
- The scope of approaches to be included under the framework;
- A set of criteria and procedures to ensure the environmental integrity of approaches in accordance with decision 2/CP.17, paragraph 79;
- Technical specifications to avoid double counting through the accurate and consistent recording and tracking of mitigation outcomes;
- The institutional arrangements for the framework.

So far, there are seven submissions from non-Annex I and three from Annex I Parties. Most submissions cover all or at least many of the issues raised in the COP 18 decision. The following is therefore structured according to this list.

2.2 Purpose and Scope of the FVA

While in 2012 some statements had seemed to imply that the FVA should also cover purely domestic approaches, there now seems to be an emerging consensus that the FVA should only concern itself with the international implications of systems. If a system is applied only domestically, without international transfers of units, all associated emissions and reductions will anyway be captured in the national emission inventory. The limitation to international aspects is endorsed in the submissions by the Coalition for Rainforest Nations, the EU, Japan, Norway, and South Africa.

On whether the FVA should have an approval function, **AOSIS** continues to take the most stringent position, stating that endorsing a decentralized approach would “fatally undermine the credibility of the UNFCCC regime”. AOSIS reiterates its view “that an internationally-agreed framework already exists for standards and approaches to deliver real, permanent, additional and verified mitigation outcomes for mitigation“, namely the Kyoto Protocol. The purpose of the FVA should therefore be to develop accounting rules for the coordination of mechanisms established under the Kyoto Protocol and under the Convention, and the coordination of market and non-market approaches developed under the Convention. The accounting rules established in the Marrakesh Accords should also apply to any approach under the FVA, including the limitation of access to mechanisms to those Annex I countries which have binding commitments.

South Africa also demands limitation of access to countries with binding obligations. The FVA should in their view cover market and non-market approaches and include common standards

The **Coalition for Rainforest Nations**[3] suggests that the FVA should cover domestic and international approaches and include units produced by developed and developing countries. The various approaches must in their view comply with common standards and compliance with these standards should be ensured through international institutions. **Indonesia and Morocco** also highlight the need for common standards.

In the same vein, the **European Union** posits that the purpose of the FVA should be to establish "common accounting standards and conformity checks". Units used internationally should either originate from the Kyoto mechanisms or the NMM, or be recognised as eligible through the FVA ex ante. As the Kyoto mechanisms and the NMM are governed by their respective modalities and procedures, the scope of the FVA would be the development of common accounting standards and conformity checks for other mechanisms to be recognised through the FVA.

Norway also emphasises that establishing a "robust international framework for the approval and tracking" of internationally traded units is needed.

By contrast, **Japan** continues to refer to facilitation and coordination of approaches, not approval. It suggests coverage of the Kyoto mechanisms, the NMM, domestic emission trading systems that link to other systems internationally as well as other approaches developed by Parties, such as the bilateral mechanism Japan is developing.

Bolivia continues to promote non-market approaches and proposes a system for the "Management of Environmental Functions" based on the rights of Mother Earth, historical responsibilities, and obligations and duties at different governmental and societal levels.

Saudi Arabia emphasises that market-based mechanisms should ensure voluntary participation and not introduce commitments for developing countries.

2.3 Criteria and Procedures to Ensure Environmental Integrity

As noted, **AOSIS** demands that the accounting rules of the Marrakesh Accords should also apply to all approaches under the FVA.

The **Coalition for Rainforest Nations** posits that the FVA should include common standards approved by the COP to address issues including additionality, accounting and monitoring, double counting, independent verification, leakage and reference levels.

The **European Union** suggests that common accounting rules should include common eligibility criteria, common approaches to determine broad segments of the economy and net emission reductions, common accounting systems and methodologies, common requirements for monitoring and independent verification, and a review process under an UNFCCC-established body.

Norway also calls for agreeing on common criteria to define and recognise units. These could involve "an environmental quality test based on for instance a standardised baseline

[3] Bangladesh, Costa Rica, Cote d' Ivoire, Democratic Republic of Congo, Dominica, Dominican Republic, Fiji, Gabon, Guyana, Honduras, Kenya, Liberia, Nigeria, Panama, Papua New Guinea, and Republic of Congo.

approach", use of common global warming potential values, principles for methodology development and monitoring standards.

Japan proposes "clear ex-ante eligibility criteria", such as positive lists. Emission reductions should be calculated conservatively at levels below BAU. Validation and verification should be conducted by independent third parties. Draft methodologies and projects should be made available for public input.

The **Coalition for Rainforest Nations** suggests discounting of emission reductions on the buyer side as a means to achieve net emission reductions. This approach would in their view be much more straightforward to implement than trying to maintain consistency in achieving net emission reductions on the emission source side while taking into account differing national circumstances.

2.4 Technical specifications to Avoid Double Counting

All countries that express views on this issue consider that units will need to be tracked through registries and an international transaction log (ITL). The **European Union** suggests that these should build on the existing infrastructure and experience.

Norway specifically proposes to expand the Kyoto Protocol's ITL to new mechanisms, including non-UNFCCC ones. In addition, Norway posits that the ITL should conduct both technical and policy-related checks. The latter would allow to check whether the units that are to be transacted originated from a system that fulfils the eligibility criteria agreed internationally.

Japan distinguishes "double registration" of projects in different schemes, "double issuance" of credits as result of double registration, "double usage" of one credit in various applications, and "double claiming" of emission reductions by the buyer and the host country. While the former three should be prevented through information sharing between schemes and linked registries, on the latter Japan proposes to add the emissions equivalent of the transferred credits to the host countries' reported emissions.

South Africa concurs that a unit can be claimed only once, either towards the achievement of a developed county Party's target, or towards the achievement of a developing country Party's mitigation action.

2.5 Institutional Arrangements

The **Coalition for Rainforest Nations** suggests that the FVA should have a regulatory body to oversee all various approaches and ensure that the common standards are applied.

The **European Union** suggests to consider the use of existing infrastructure.

Norway proposes that the UNFCCC could maintain its role of accrediting verification agencies. These would verify activities against both national standards and the common criteria or standards agreed by Parties.

3 The New Market-Based Mechanism

3.1 Issues to be Addressed

Decision 1/CP.18 identified the following issues for further discussion:

- Its operation under the guidance and authority of the Conference of the Parties;
- The voluntary participation of Parties in the mechanism;
- Standards that deliver real, permanent, additional, and verified mitigation outcomes, avoid double counting of effort and achieve a net decrease and/or avoidance of greenhouse gas emissions;
- Requirements for the accurate measurement, reporting and verification of emission reductions, emission removals and/or avoided emissions;
- Means to stimulate mitigation across broad segments of the economy, which are defined by the participating Parties and may be on a sectoral and/or project-specific basis;
- Criteria, including the application of conservative methods, for the establishment, approval and periodic adjustment of ambitious reference levels (crediting thresholds and/or trading caps) and for the periodic issuance of units based on mitigation below a crediting threshold or based on a trading cap;
- Criteria for the accurate and consistent recording and tracking of units;
- Supplementarity;
- A share of proceeds to cover administrative expenses and assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation;
- The promotion of sustainable development;
- The facilitation of the effective participation of private and public entities;
- The facilitation of the prompt start of the mechanism.

One of the key controversial issues in 2012 had been the question whether the NMM should be sector- or project-based. As listed above, decision 1/CP.18 did not resolve this issue but stipulated that broad segments of the economy could be defined by the participating Parties on a sectoral or project basis.

So far, there are eight submissions from non-Annex I and two from Annex I Parties. Most submissions take positions on only some of the issues listed in the COP 18 decision and only the EU and Tunisia go into some technical details. The following therefore summarises the main points submission by submission.

3.2 Party Submissions

The **European Union** calls for a "prompt start" for the NMM, including a pilot phase before 2020. The EU mostly repeats its 2012 submissions with its proposals for sectoral crediting and sectoral trading, based on an international review process with governance under an international Implementation Committee, acting under the authority and guidance of the

COP, and technical reviews of proposals by an International Review Team.

Baselines should be based on the most conservative baseline scenario, incorporate policies and measures that are adopted or at an advanced stage of development, and go beyond reductions expected from unilateral and supported NAMAs. Crediting thresholds should be set substantially below the baseline, taking into account available mitigation potential, the implementing Party's capability to implement emission reductions and finance received or expected.

The EU emphasises the importance of a common approach to defining broad segments of the economy, these should in the EU view mean one or more sector, category or subcategory as listed in Annex II to the UNFCCC reporting and review guidelines. Divergent definitions would be possible, but would need to be sufficiently justified.

Tunisia highlights the crucial importance of creating higher demand for credits. Similar to the EU, they suggest that the institutional framework of the NMM should consist of an international body to register NMM activities and issue credits and of Designated National Authorities to approve activities and confirm whether they contribute to sustainable development.

Contrary to the EU, Tunisia suggests that the definition of sectors should be at the discretion of the host country, while noting that existing definitions such as those of the IPCC may be applied. Tunisia posits the need for common criteria regarding the development of baselines, the crediting/trading thresholds, periods and targets, but with „sufficient flexibility" for the host country to take into account national circumstances. CDM projects should be reflected in the baseline to avoid double counting. It should in their view also be left to the host country whether to choose absolute or intensity targets.

Tunisia urges to encourage early pilot activities and allow industrialised countries to purchase credits and count those purchases towards their financial commitments. After the NMM has become fully operational, credits could be counted towards emission commitments, but the finance for those credits could not at the same also be counted towards financial commitments. Tunisia notes that is has been preparing to launch an NMM pilot in its cement industry.

The relationship between the NMM and NAMAs should in Tunisia's view be clarified, for example whether a supported NAMA could be used to achieve the net emission reduction which is demanded within the NMM. The EU submission does posit that "own contributions" could indeed be implemented as unilateral or supported NAMAs.

Bolivia continues to be "opposed to any kind of market mechanism" and demands to establish a moratorium on NMM development.

The **Coalition for Rainforest Nations** supports sectoral crediting and sectoral trading but mainly focuses on REDD+. They suggest that a REDD+ mechanism should be defined as part of the NMM. An NMM pilot phase should be started at COP 19. The NMM should be sectoral in nature. Units would be issued at the national level based on national accounting and MRV.

Morocco supports sectoral, sub-sectoral and project-based approaches. In its view the NMM should contribute to NAMA implementation by directly assigning NAMA emission credits for the implementation of a policy instrument. Morocco supports a prompt-start period with voluntary pilots.

Norway supports the EU proposals for sectoral crediting and sectoral trading but in its submission mainly defines questions that would need to be answered in the further work programme, such as on the appropriate form of governance, guidance or criteria for the definition of sectors, and methodologies for determining baselines and crediting thresholds. Norway suggests that the Secretariat should elaborate a technical paper on these issues and to organise a workshop well before the next COP.

Saudi Arabia raises the same points as on the NMM regarding voluntary participation and not introducing new commitments for developing countries. It supports both sectoral and project-based approaches, subject to the discretion of the host Party, with modalities similar to those of the Kyoto mechanisms. They suggest that, given the currently low demand for credits, a centralised NMM under UNFCCC oversight may be "premature". Bottom-up "organic growth" of domestic systems may in their view be more sensible.

South Africa urges that the NMM should avoid the CDM's problems of unequal geographical distribution. As in its submission on the FVA, it posits that access to the NMM should be limited to developed country Parties with binding emission obligations. In contrast to the sectoral perspective, which usually envisages to issue credits on the basis of the aggregate sectoral performance, South Africa opines that the NMM should cover reductions "resulting from a clearly identified action or policy (activity)".

4 Summary and Conclusions

The submissions on both the FVA and NMM once again reflect the existence of differences of opinion on fundamental issues, which would need to be overcome to be able to come to any substantive decision.

On the FVA, there is consensus that a common infrastructure of registries and possibly an ITL would be needed to ensure proper tracking of units and prevent double counting. However, there continues to be a fundamental controversy on whether the FVA should have the function to approve decentralised systems or only to facilitate their development and operation. European and many developing countries maintain the position that common standards, international approval and oversight through an international regulatory body are crucial for the use of credits towards pledges. Japan continues to refer to facilitation and coordination rather than approval and considers that units from its bilateral mechanism should be eligible for meeting its target. There hence seems to be no rapprochement of positions. New Zealand and the USA, which have also been strongly in favour of a purely facilitative role of the FVA, have not made new submissions.

One item that seems to have been clarified is the scope of the FVA. While in 2012 some statements had seemed to imply that the FVA should also cover purely domestic approaches, there now seems to be an emerging consensus that the FVA should only concern itself with the international implications of systems.

One sensitive issue that now seems to have made it on the agenda is the potential for double counting by buyer and host countries. According to the current rules, emission reductions could be counted by the credit buyers towards their targets but would also contribute to the achievement of the host countries' emission reduction pledges. Japan proposes to add the emissions equivalent of the transferred credits to the host countries' reported emissions.

On the NMM opinions seem to continue to be divided on whether it should be sector- or project-based. Several developing country submissions posit that both should be allowed and that the definition of boundaries should be left to the discretion of host countries, while the EU urges the need for common definitions based on the UNFCCC guidelines for reporting and review.

Other EU proposals may also give cause for controversy, such as the view that baselines should incorporate all policies and measures that are adopted or at an advanced stage of development. This is the opposite of the E+/E- rule that has been agreed in the CDM.

The dearth of detail in the submissions on the NMM is even more pronounced than in the submissions on the FVA. Only the EU and Tunisia go into technical details, but these are mostly a repetition of past discussions. However, one may note positively that not only the EU but also a number of developing countries support a prompt start for the NMM with voluntary pilots. Tunisia notes that it is already preparing a pilot NMM in its cement sector.

A question raised by Tunisia and Saudi Arabia is how the NMM is supposed to function without demand for credits. Tunisia suggests a possible way forward for the short to medium term by proposing that NMM pilots should generate credits and that the purchase of these credits should count towards the buyer countries' financial commitments rather than emission commitments.

Overall, the submissions reveal only marginal conceptual or political advancement compared to last year's discussions. Most submissions are very short and do not go into substantial technical detail. This underlines the hypothesis that the main stumbling stones are political differences rather than lack of conceptional clarity.

One problem for progress on both the FVA and the NMM is Bolivia's continued opposition to any scale-up of market mechanisms. If Bolivia maintains its uncompromising position and is supported by other countries, it may be impossible to make any kind of progress in the negotiations and the development of new approaches may have for the time being have to take place outside the UNFCCC context.

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