

# Cooperative approaches under Art. 6.2 of the Paris Agreement

*Status of negotiations – key areas of consensus and contention*

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## Executive Summary

The informal note that is the outcome of the negotiations the cooperative approaches under Art. 6.2 of the Paris Agreement at COP 23 shows the tension between two lines of positions. The first line wants to minimize international oversight, ideally limiting it to the accounting of ITMOs, whereas the second proposed to introduce international oversight comparable to that for Art. 6.4. The Umbrella Group and Like-Minded Developing Countries but also AILAC support the former, Brazil, AOSIS and the EIG the latter. The EU and Canada take the middle ground with the demand for requirement to report on sustainable development and human rights.

The note is structured into seven overarching topics. Generic umbrella issues such as a preamble, principles, scope and purpose are followed by a section on governance. The key building blocks of the transfer system under Art. 6.2 are lined out before additional issues that could be covered by international oversight are listed. Possible modalities and procedures on the international level are followed by the topic of the transfer process and participation of non-government stakeholders. Finally, safeguards against double counting of ITMOs are listed.

Unsurprisingly, there is more text underpinning the strong international oversight, as this requires more specific textual proposals. This concentrates on quality requirements for ITMOs and participation requirements for Parties depending on the nature of NDCs.

Room for compromise could be found regarding prevention of negative impacts on sustainable development and human rights, with mandatory reporting. Likewise, environmental integrity could be fostered by transparent reporting requirements.

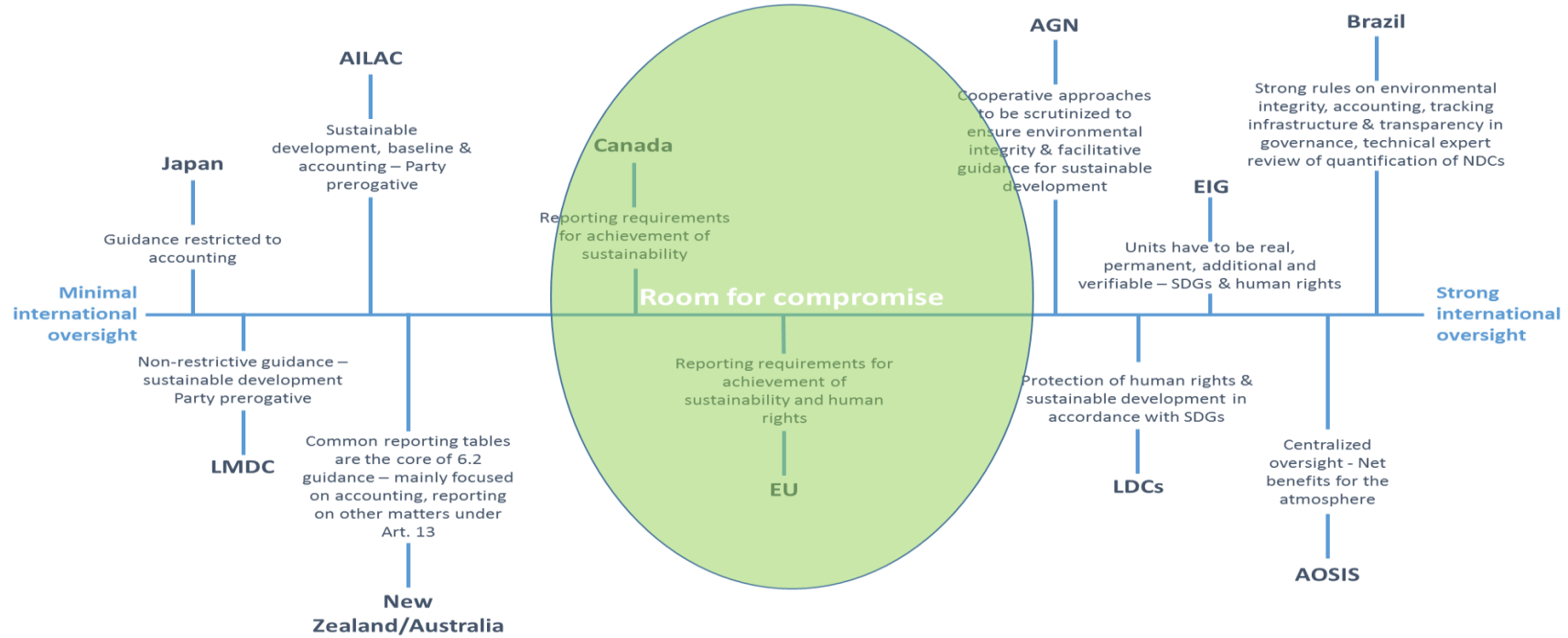


Figure: Spectrum of views on the scope and depth of the Article 6.2 guidance



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## 1. Introduction

The Paris Agreement (PA) has defined an ambitious long-term goal to keep the average global temperature increase to well below 2°C compared to pre-industrial levels and aspires to even limit it to 1.5°C. A crucial difference to the Kyoto Protocol is that every country can freely specify the level of mitigation, and there is no longer a bifurcation in countries with mitigation commitments and those without. The mitigation targets are enshrined in countries' Nationally Determined Contributions (NDCs). Countries can collaborate in order to meet their NDC targets in a flexible and cost-effective way through market mechanisms defined in Article 6 of the Paris Agreement.

Article 6.2 defines Cooperative Approaches (CAs) which can be used to transfer "internationally transferred mitigation outcomes" (ITMOs) from one country to another. The detailed rules and procedures for the Article 6 mechanisms are to be defined in the second half of 2018 at the latest through COP 24 in Katowice in December 2018. This process can be compared with the negotiation of the Marrakech Accords, which specified the rules for the Kyoto Mechanisms, in the years following the agreement on the Kyoto Protocol.

At COP 23 in Bonn in November 2017, negotiators collected the topics to feature in the negotiation paper for COP 24. This resulted in an "informal note" (UNFCCC 2017a) and a decision (UNFCCC 2017b) that the co-chairs of the Subsidiary Body for Scientific and Technological Advice (SBSTA) develop a new text for the 48<sup>th</sup> meeting of SBSTA in April-May 2018. The informal note is structured in the following way:

- 1) Preamble
- 2) Principles
- 3) Scope and purpose
- 4) Scope
- 5) Purpose
- 6) Definitions
- 7) Governance
- 8) Guidance for a party using / transferring in ITMOs
- 9) Guidance for a party creating / issuing/transferring out ITMOs
- 10) Infrastructure
- 11) Participation requirements
- 12) Accounting
- 13) Reporting
- 14) Review and assurance of consistency with guidance on the creation and use of ITMOs towards NDC
- 15) Application of share of proceeds for adaptation
- 16) Overall mitigation of global emissions in context of Art. 2
- 17) Environmental integrity



- 18) Social integrity
- 19) Sustainable development
- 20) Adaptation ambition
- 21) Addressing negative social and environmental impacts
- 22) Mitigation co-benefits resulting from parties' adaptation actions and/or economic diversification plans
- 23) Multilateral governance and rules-based system
- 24) Guidance for transfers
- 25) Guidance for participation of other actors
- 26) Guidance for avoiding use of ITMOs/emission reductions for more than one purpose
- 27) Avoiding use of emission reductions resulting from mitigation activities by more than one party
- 28) Emission reductions applied to purposes other than towards achievement of NDCs

Sections 1-6 cover generic umbrella issues. Section 7 looks at the overall governance. Sections 8-13 contain the key building blocks of the transfer system under Art. 6.2. Sections 14-21 cover additional issues that could be covered by international oversight. Section 23 addresses possible modalities and procedures on the international level; it is a bit strangely placed. Sections 24 and 25 address the transfer process and participation of non-government stakeholders. Sections 26-28 address safeguards against double counting of ITMOs in all possible forms.

The objective of this paper is to dissect the informal note and to elaborate where country positions converge and where there are areas of contention, including "red lines". It will do this for all key issues under negotiations. This will allow to understand where zones of convergence exist and can be enlarged, and where the resolution of "red line" items needs to wait until the final huddles in Katowice.

When referring to elements of the informal note, a referencing system according to the sequence in the note is used, e.g. 9,A,i refers to a country transferring ITMOs (section 9) facing the participation requirement (section 9,A) that it needs to be a Party to the Paris Agreement (section 9, A, i). The paper therefore is preferably read in with the informal note at hand.

## **2. Scope and depth of the guidance**

### **2.1. Spectrum of views**

One of the fundamental divergences in the negotiations on Article 6.2 guidance is whether it should mainly serve to ensure robust accounting in the transfer of ITMOs, or whether it should also cover aspects of environmental integrity, sustainable development and transparency in governance. Since these elements are introduced with "shall" in the Paris Agreement text, it is clear that simply ignoring them is not an option and that they will have to be addressed in some way or another. The differences in viewpoints therefore translate into how far-reaching, detailed and prescriptive the Article 6.2 guidance should be on these issues.



Parties that wish to see minimal international guidance on environmental integrity, sustainable development and transparency in governance have reservations regarding the UNFCCC process and believe that national governments are instead better equipped to design the rules of market mechanisms in a way that is environmentally sound and operationally practical. This view is held by most members of the Umbrella Group. It is argued that national governments firstly answer to national constituencies and therefore, when it comes to ensuring the soundness of cooperative approaches, they place their faith in national level checks rather than UN oversight. This is because in their view, governments exert the greatest care when it comes to the money of taxpayers or national business interests. According to these Parties, diversity and bottom-up design essentially lie at the heart of cooperative approaches and thus international interference should be reduced to a minimum. Only aspects that go beyond the competency of individual Parties and that need a harmonized approach, such as accounting, should be subject to international guidance.

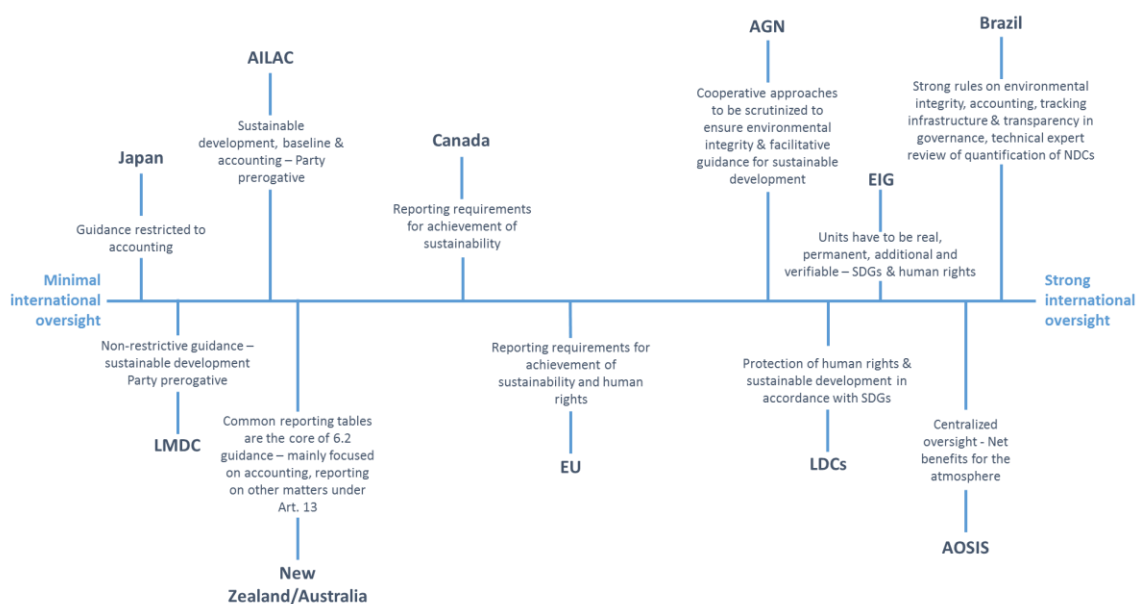
Similarly, members of the LMDC group stress the bottom-up nature of cooperative approaches and the prerogative of national governments to define sustainable development. They argue that NDCs take priority over cooperative approaches and therefore international guidance must not restrict the type of cooperation Parties wish to engage in. As cooperative approaches are simply a tool for achieving the NDCs, any cooperation that helps to achieve Party defined sustainable development goals should be allowed.

On the other end of the spectrum are Parties that are concerned with the national or global impacts of a laissez-faire approach to environmental integrity and sustainable development. They fear that with Article 6.2, the overall stringency of the NDCs could be undermined if hot air enters the system and Parties export mitigation outcomes that do not represent real reductions against business-as-usual. The EIG therefore seeks to ensure that any units traded represent real, additional, permanent and verifiable emission reductions. Members of AOSIS wish to additionally see net benefits for the atmosphere from cooperation. In addition, EIG, AOSIS and the LDCs also wish to see human rights protected and that sustainable development be defined in accordance with the SDGs. Brazil, sees the cooperative approaches resembling emission trading under the Kyoto Protocol and therefore sees a need for international oversight even on the quantification of NDCs. This leads to a different view of the scope of the Article 6.2 guidance and the need for international review procedures and oversight.





Figure 1: Spectrum of views on the scope and depth of the Article 6.2 guidance



## 2.2. Treatment of the issue in the informal note

The dichotomy between Parties wishing more, or less, international oversight is reflected throughout the informal note, as this issue translates into almost every aspect of the guidance.

Elements introduced into the informal note with the motivation to *reduce* international oversight on cooperative approaches are the following, ordered from generic to specific:

- Maintaining national prerogative through bottom-up approaches (2,v)
- Accommodation of all NDC types (2,ix). Participation requirements are a national prerogative (8,A,xxi) (11,A,xvii). No limits to use of ITMOs towards NDCs (8,C,f,b). Prioritize NDC implementation, while avoiding extraneous influences (2,vii). ITMOs are defined by Parties implementing a cooperative approach (6,g,b). The full spectrum of mitigation outcomes can be used - tonnes of CO<sub>2</sub> eq as well as other metrics (6,g,a,d).
- Environmental integrity covered through the accounting rules (6,f,iii)
- No specific Article 6.2 body (for oversight) (7,B,b) (14,a,b)
- No need for Sections A-E [no for guidance for Parties that are creating/issuing/transferring out ITMOs as proposed in sections 9A-E] (9,b)



- Demonstration of how the use of ITMOs towards the NDC promotes sustainable development is the Party's national prerogative (8,E,b,xvii), (9,E,a,xvii)
- No Share of Proceeds on Article 6.2 (15b)
- Overall Mitigation not applicable to Article 6.2 (16b)

The majority of the text of the informal note consists of elements introducing certain requirements on cooperative approaches however. These would give rise to international oversight if adopted and include, inter alia:

- Multilateral governance and rules-based system (2,xv) (23), Multilateral issuance of units (7,A,iii), (7,B,vii)
- *Requirements on the quality of units:* [Need for] Rules for ITMO generation if not from Article 6.4 (3,vii); [Environmental integrity defined through] Quality of units (6,f,ii) [ITMO] That is real, permanent, additional and verifiable (6,g,i) and evidence thereof (8,E,b,vi); Approving the methodologies and baseline approaches for crediting-type systems – no less rigorous than Article 6.4 (7,b,iii); Ensuring that standards and methodologies developed in all cooperative approaches follow the guidance of the CMA, as appropriate (7,b,iv); Third party technical review of the environmental integrity of ITMOs created/approval of ITMOs (7,b,v); (xix) ITMOs that do not result in environmental harm (8,A,xix), (9,A,xix) (11A,xvi), (17,i), ITMOs that do not adversely affect human rights (8,A,xx), (9,A,xx) (11A,xvi), (18i,)
- *Participation requirements* for Parties wishing to use or create/issue ITMOs: Confirmation of Party's preparedness to create/issue/transfer/acquire/use ITMOs (7,b,i); Have quantified its NDC and identified the relevant sectors and gases covered / annually (8,A,viii) (9,A,viii) (11,A,vi); (ix) Have quantified its NDC in absolute emissions (caps) (8,A,ix) (9,A,ix) (9,A,xxi) (11,A,vii); Have economy wide target, absolute emissions, multi-year (8,A,x) (9,A,x) (11,A,ix); Have economy wide long term low emissions strategy (8,A,xi) (9,A,xi), (11,A,x); Biennial inventories consistent with long term trajectories (8,A,xii) (9,A,xii) (11,A,xi); Have submitted an indicative emissions trajectory consistent with its long-term goals under its low emissions development strategy (8,A,xiii) (9,A,xiii) (11,A,viii); Have a system for identifying the origin of ITMOs/tracking the acquisition of ITMOs/tracking the international transfer and/or have access to a system for recording the use of ITMOs (8,A,xiv) (9,A,xiv), (11,A,xii); Have requirements to mitigate leakage risk (9,A,xxii); Have systems to ensure permanence, including systems to address reversal (9,A,xxiii); Checks that the Party has achieved the relevant requirements (9,A,xxiv) (11,A,xviii); System for determining sustainable development in accordance with national prerogative (9,A,xxv), [demonstration] how the use of ITMOs towards the NDC does not erode the environmental integrity of the using Party's NDC (8,E,b,ix); How the cooperative approach is consistent with the Party's long-term strategy (8,E,b,x), Evidence that the activity resulting in ITMOs fosters the transition of the using Party to a low carbon economy (8,E,b,xi); Have provided a quantification report that has been assessed by a reviewer (11,B,iv)



- Share of proceeds on Article 6.2 (15,a)
- Overall mitigation of global emissions applicable to Article 6.2 (6,h), (7,C,vi), (16,a)

### 2.3. Analysis of common ground, red lines and opportunities for compromise

It is clear that Parties will need to seek a compromise that falls in the middle of the spectrum. It will not be possible to limit the Article 6.2 guidance solely to accounting, nor will Parties agree to establish a multilateral system that approves cooperative approaches in a similar fashion as the Article 6.4 mechanism.

The following red lines can be identified:

#### Umbrella Group

- Having approval of cooperative approaches or eligibility criteria for approaches
- Prescriptive international guidance on the design of cooperative approaches
- An international Article 6.2 body similar to the 6.4 supervisory body

#### LMDCs

- Top down definition of sustainable development
- Restriction of cooperative approaches

#### EIG/AOSIS/LDCs

- No guidance on what constitutes environmental integrity
- No limits on the possibility for hot air entering the system
- No link to the SDGs
- No consideration of human rights

#### Brazil

- Engagement in cooperative approaches without a multi-year budget of absolute emissions

The question is how compromise can be reached between these opposing views. An opportunity for compromise may lie in the nature of the guidance. Considering that many Parties seek to have safeguards against hot air and human rights violations as well as, at the very least, a definition of sustainable development, these aspects will most likely need to be part of the guidance.

In order to at the same time meet the concerns of Parties seeking to preserve national ownership over the design of cooperative approaches and the definition of sustainable development as well as environmental integrity, it would be important for the guidance to stay at a principle level and enable Parties to operationalize these principles themselves. Parties wishing to limit UN interference in cooperative approaches might accept facilitative



guidance, based on transparency and reporting and expert review, but no provisions that would give authority to the multilateral system to approve cooperative approaches and make a final judgement of whether cooperative approaches meet environmental integrity, sustainable development and transparency in governance.

In that sense the design of the review and compliance process for the Article 6.2 guidance could be central to overcoming differences on the scope and depth of the guidance.

Brazil's requirement of a budget approach and international scrutiny on the quantification of NDCs if they wish to engage in cooperative approaches, however, will likely overstretch Parties' willingness for compromise and might only be solved in final trades with other agenda items.

### **3. Features of ITMOs**

#### **3.1. Spectrum of views**

Internationally transferred mitigation outcomes or "ITMOs" remain undefined in the Paris Agreement. Parties have therefore taken to interpreting the nature of ITMOs in different ways.

Some Parties (AOSIS, EIG) think of ITMOs in much the same way as units generated under carbon standards. They see ITMOs as "retrospective outcomes" that are issued following a third party (independent and competent) technical review. This is to ensure that ITMOs represent real, measurable, additional, verified and permanent emission reductions. Units generated by the Article 6.4 Mechanism qualify as ITMOs but ITMOs can also be created outside of Article 6.4 if Parties ensure that the above principles are met. Transfers would happen and be checked through a centralized system (an international transaction log). AILAC proposes the use of DOEs to ensure that ITMOs are real, measurable and verifiable.

Other Parties (AGN) make a clear distinction between the units issued under a carbon standard and ITMOs. They see ITMOs as accounting units that represent the net flows between Parties and are reported in Parties (biennial) communications demonstrating the implementation of their NDCs. With the focus on national reporting and accounting, these Parties prefer the term "creation" rather than "issuance" of ITMOs. Another important implication is that ITMOs do not represent a type of tradeable commodity but only have value in the context of the bilateral or plurilateral relationship of the cooperative approach. The creation of fully fungible units is the domain of the Article 6.4 mechanism or other carbon standards. ITMOs on the other hand, cannot be used for purposes other than for meeting or exceeding NDCs. This excludes the use of ITMOs by private entities, for instance under CORSIA.

The most hands-off approach to ITMOs comes from the LMDCs which advocate that the Article 6.2 guidance focuses on the transfer and not the creation of ITMOs. Consequently there is no need for a multilateral definition of ITMOs but this should be left to the cooperating Parties. LMDCs also stress that ITMOs cannot only represent



emission reductions but also avoidance of emissions, in cases where emissions are still growing due to the country's further development.

Yet another view of ITMOs is held by Brazil, which likens ITMOs to allowances (AAUs) under the Kyoto Protocol. Issuance of ITMOs by a country is contingent upon a quantification of the permitted emissions under its NDC. Similar to emissions trading under the Kyoto Protocol, ITMOs must be subtracted from the country's overall budget, if exported. Brazil also insists on using the full quotation of Article 6.2 which reads "the use of internationally transferred mitigation outcomes *towards nationally determined contributions*."

Australia and other Parties of the Umbrella group focus on the lifecycle stages of an ITMO, including its creation, holding and transfer and emphasize that these need different institutional and governance arrangements.

Another question is the denomination of ITMOs. While most Parties consider ITMOs to be denominated in metric tonnes CO<sub>2</sub>equivalent, some Parties (AGN) want to keep the metric open to potentially cater to different metrics used in the NDCs, such as energy efficiency or renewable energy-related units.

### 3.2. Treatment of the issue in the informal note

The features of ITMOs are discussed in various sections of the non-paper. The key question whether ITMOs are subject to international rules is repeatedly covered (3,vii; 6,g,a; 7,A,iii; 7,B,a ), e.g. regarding their "quality" (6,f,ii). Specific proposals limiting national prerogatives include:

ITMOs should not be freely tradable (6,g,iv). They should be real, permanent, additional and verifiable (6,g,i) and be identified by a unique serial number (6,g,ii). They should be only generated if the issuer has an NDC target specifying net absolute national reductions (6,g,viii). A somewhat weaker proposal is that ITMOs could only be created inside NDCs (24,C,I; issuer: 9,B,c,a; user: 8,B,a; accounting: 12,A,b,a), except for LDCs (issuer: 9,B,c,a,i; user: 8,B,a,i). In a similar vein, ITMOs could only accrue for gases covered by the NDC (issuer: 9,b,d,a; user: 8,B,b; accounting: 12,A,b,b). A less specific proposal requests consistency between issuer and users (6,g,xiii).

Further proposed features are that ITMOs should be denominated in CO<sub>2</sub>e (6,g,a,a) and that they should include CERs (6,g,x and xi) and ERUs (6,g,xi). It is also suggested that other approaches are subject to CMA approval (6,g,vi). In addition, there is a proposal of multilateral issuance of units (7,b,vii).

Those Parties who do not want any limitation ask for a specification that ITMOs should not be subject to international rules (6,g,b, 6,g,vii, 7,B,b) and that their definition should be open (6,g, a, c or d, 6,g, iii, 6,g,vii).



### 3.3. Analysis of common ground, red lines and opportunities for compromise

It might be possible to agree on certain characteristics of ITMOs such as their denomination in tonnes CO<sub>2</sub>e while not making their generation contingent on NDC characteristics. Any more explicit definition of what an ITMO is will be challenging, considering the different outlooks by Parties and the fact that some do not wish to see an upfront definition at all.

Parties seeking to ensure quality of units might be able to achieve their objectives by focusing on the quality criteria that cooperate approaches must meet and Parties have to report on, rather than by further specifying ITMOs themselves. Again, the demonstration that approaches meet the criteria would have to be under multilateral assessment and review but not subject to multilateral approval in order to achieve buy-in from those Parties that want to see less multilateral oversight.

Non-tradeability and limitation to absolute NDC targets will not be palatable to any relevant group of Parties.

## 4. Accounting

### 4.1. Spectrum of views

Accounting deals with the avoidance of double counting of ITMOs towards more than one Party's NDC, which many Parties consider to be the core of the Article 6.2 guidance. According to paragraph 37 of the COP 21 Decision, double counting shall be avoided on the basis of "corresponding adjustments by Parties for both anthropogenic emissions by sources and removals by sinks covered by their NDCs under the Agreement".

While all Parties recognize the need for robust accounting, they make different proposals for its technical implementation. Among the main issues discussed are the basis for accounting – i.e. whether accounting would start on the basis of national inventories, NDC pledges, or from a different basis - how correspondence of the adjustment can be ensured in light of different NDCs and when the corresponding adjustments should take place.

The EU advocates for Parties to establish an "accounting balance" with preferably actual emissions as starting point to which ITMOs are added to or subtracted from. The EU also advocates for a common accounting approach that should address different coverage areas of NDCs (with respect to sectors, gasses, and target years).

New Zealand and other members of the Umbrella Group propose the development of tabular formats for reporting of ITMO transactions under the Article 6.2 guidance, which is to be used in countries' biennial reporting.

Japan stresses the need for a common understanding of the types of double counting, including double registration, double issuance, double usage and double claiming and the development of guidance to address them.



Saudi-Arabia, on behalf of the LMDCs, proposes a “buffer approach” as basis for the accounting, which shields the NDCs from ITMO transactions. ITMOs sold or acquired would be recorded in a separate buffer registry that starts at zero.

EIG stresses the fact that ITMOs always have to be added to the exporting country’s reported emissions, independent of the final use of the ITMOs, which may be towards NDCs, for voluntary cancellation or towards CORSIA, at the time the ITMOs are exported.

Many Parties, including EU, EIG, AOSIS and the LDCs express the need for a centralized infrastructure including an international transaction log to keep track of ITMOs.

Parties do not agree whether accounting stretches beyond the recording and accounting of transfers. Some think that the way ITMOs are accounted for also has impacts on progression, ambition, environmental integrity and sustainable development. These issues therefore should be considered in the elaboration of the guidance (see chapters on environmental integrity and sustainable development).

Another contentious issue is whether ITMOs can be created from outside the NDCs and whether in such a case corresponding adjustments should be made.

#### 4.2. Treatment of the issue in the informal note

Draft elements for guidance on accounting are centralized in section 12 (accounting) of the informal note. They are largely repeated in section 8 (guidance for a Party using/transferring in ITMOs), and section 9 (guidance for a Party creating/issuing/transferring out ITMOs) with mostly identical requirements for Parties that are using or creating ITMOs. Some draft elements on accounting are also found in section 3 (scope and purpose), section 6 (definitions) section 10 (infrastructure), section 13 (reporting), section 14 (review), section 15 (SOP), section 16 (overall mitigation), section 23 (multilateral governance) and section 24 (guidance for transfers). Considering the centrality of the topic it is not surprising that aspects of accounting cut across many sections.

The informal note lists five options as starting point for accounting:

- Target/budget-based approach (quantifying NDCs into a budget of NDC-allowed emissions) (8,C,a,a), (9,C,a,a), (12,A,a,a)
- Emissions-based approach (“accounting balance”) (8,C,a,b), (9,C,a,b), (12,A,a,b)
- Buffer registry approach (using an account separated from NDCs and inventories starting from zero) (8,C,a,c), (9,C,a,c), (12,A,a,c)
- Emission reduction-based approach (quantity of emission reductions required for NDC achievement) (8,C,a,d) (9,C,a,d), (12,A,a,d)
- Party may choose its accounting approach and apply consistently (8,C,a,e) (9,C,a,e), (12,A,a,e)



The note also gives ample attention to the treatment of different types of NDCs, particularly those with single year targets. Several options are identified for dealing with single year targets:

- Use of ITMOs limited to those ITMOs having the same vintage as the target year (8,D,c,a) (9,D,c,a) (12,D,c,a)
- Use of cumulative ITMOs throughout the NDC implementation period towards the target year (8,D,c,b) (9,D,c,b) (12,D,c,b)
- ITMO use is distributed throughout the NDC implementation period based on an emissions trajectory consistent with NDC achievement (8,D,c,c) (9,D,c,c) (12,D,c,c)
- Use of average amount of ITMOs acquired/used over the NDC period in the target year (8,D,c,d) (9,D,c,d) (12,D,c,d)
- Use of average amount of ITMOs generated by the activity in the target year (8,D,c,e) (9,D,c,e) (12,D,c,e)
- Use of ITMOs in each period reflected in biennial reports (8,D,c,f) (9,D,c,f) (12,D,c,f)
- Representative transfer of ITMOs over the NDC period accounted in target year (8,D,c,g) (9,D,c,g) (12,D,c,g)
- No specific guidance for single year targets (8,D,c,h) (9,D,c,h) (12,D,c,h)
- Parties to have quantified its NDC in absolute emissions, multi-year (8,a,x), (9,a,x)

Furthermore, the note prominently identifies various options for the timing of corresponding adjustments, including:

- Upon creation/issuance (9,C,c,a) (12,F,a)
- Upon transfer (12,F,b)
- Upon acquisition (8,C,c,a) (12,F,c)
- Upon use towards NDC (8,C,c,b) (9,C,c,b) (12,F,d)
- Upon reporting under Article 13.7 (8,C,c,c) (9,C,c,c) (12,F,e)
- All/some of the above (8,C,c,d) (9,C,c,d) (12,F,f)

Finally, the note gives various alternatives for accounting of ITMOs outside the NDCs

- Source of ITMOs only from a sector inside the NDC (except for LDCs) (12,A,b,a[i])
- Source of ITMOs from any sector, inside or outside the NDC (12,A,b,b)
- Source of ITMOs only from a GHG gas inside the NDC (12,A,b,a-2)
- Source of ITMOs from any GHG gas, inside or outside the NDC (12,A,b,b-2)
- Application of corresponding adjustments for ITMOs issued/created from inside the NDC only (12,A,c,a)
- Application of corresponding adjustments for all ITMOs, created/issued inside or outside the NDC (12,A,c,b)





### 4.3. Analysis of common ground, red lines and opportunities for compromise

There seems to be common ground that corresponding adjustments are effected through additions or subtractions in the relevant basis of accounting and that this is reported in biennial communications following Article 13.7.

While many Parties express a preference for an accounting basis that starts with actual emissions taken from the inventories, some have clearly divergent views. Notably Brazil advocates for a budget approach that is based on NDC permitted emissions. A compromise line may be that countries can choose between a target- and an emission based approach, which are mathematically the same. A proposal that lies squarely out of the compromise zone for many Parties is the buffer approach from the LMDCs. It is not clear how double counting would be avoided in the sense that a country exports ITMOs while still benefiting from the emission reduction for achievement of its NDC.

Regarding the issue of single year targets, it is unlikely that Parties would agree to limiting participation in cooperative approaches to Parties with certain types of NDCs. This goes against the bottom-up character of the Paris Agreement and the call for inclusiveness by many Parties (e.g. AGN). It also goes against the higher standing of the NDCs vis-à-vis cooperative approaches emphasized by the LMDCs. The options for dealing with single year targets fall into two categories: those that try to mitigate the potential negative implications of cumulatively inflated emissions and those that do not include specific restrictions. A compromise may be to allow countries to choose among different options that seek to curb negative effects on environmental integrity (use of same vintages, average amounts of ITMOs over the period), and agree on the principle of what should be achieved

In terms of acceptance of ITMOs from outside a country's NDC, a possible compromise line has been proposed by Canada. ITMOs could be 'locked' until the time that the country would include the sector into its NDC.

## 5. Environmental integrity

The most far-reaching proposal is a multilateral, rules-based system (2,a,xv; 7,B,c; 24,D,ii; for users: 8,A,xxii). Under such a system, environmental integrity would be checked by a supervisory body (7,B,a). Some suggest a review by third parties (14,a,iv; 14,c,viii) when an ITMO is generated (7,B,a,v) and before it is transferred. Methodologies would in descending order of stringency be approved by a supervisory body (14,a,iii), approved by some institution (14,c,vii), be as strict as under Art. 6.4 (7,B,a,iii;) or just be guided by CMA (7,B,a,iv). Additionality would be covered under Art. 6.2 (6, g, i), with a report on additionality (13,A,vii), by the selling country (9,E,a,a, vi), or the buying country (8,E,b,vi). Issuers should have requirements for mitigating leakage risks (9,A,xxii). Discounting/cancellation of units (7,C,vi; 16,a,i-iv) should be done to ensure that no increase in global emissions takes place – through cancellation (issuer: 9,C,e,a; accounting: 12,E,a,a; user: 8,C,e,a; accounting:



12,E,b,a; accounting general: 12,D,d;) or discounting (issuer: 9,C,e,b; accounting: 12,E,a,b user: 8,C,e,b; accounting: 12,E,b,b).

In a middle ground with no dedicated international oversight, key issues regarding environmental integrity could be addressed as follows:

- The principle not to increase global emissions (2,a, ii; 6, h), with the user having to report on this (8,E,b,v)
- The need to report on environmental integrity of ITMOs used (13,A,vi; transferred by issuer: 9,E,a,a,iv; 9,E,a,a,vii; 13,C,ii; used by user: 8,E,b,viii; 13,D,iii), with an explanation how its NDC is impacted by ITMOs (issuer: 9,E,a,a,viii; user: 8,E,b,ix; 13,D,iv).
- Issuer to have a system for baseline setting (9,A,xiii; 11,B,ii) and ensuring permanence and redressing reversal (9,A,xxv)

Rules with environmental integrity relevance under accounting with regards to which type of NDC targets would be required for Art. 6.2 eligibility have been proposed as follows, ordered from the highest to the lowest level of stringency:

- Multi-year targets only (all: 11,A,ix; issuers: 9,A,x; 9,C,a,a; users: 8,A,x; 8,C,f,v), through budgets (issuers: 9,C,a,a; users: 8,C,a,a) or emission totals (issuers: 9,C,a,b; users: 8,C,a,b). Accounting (12,A,a,a)
- Single year target ITMO “conversion”: Same vintage as single target year only (issuer: 9,E,a,b,a; user: 8,E,c,a; accounting: 12,B,b,a;12,D,b,a), cumulative ITMOs (8,E,c,b; accounting 12,D,b,b), emissions trajectory against which ITMOs are accounted (issuer: 9,E,a,b,c; user: 8,E,c,c; accounting: 12,B,b,c; 12,D,b,c), average ITMO transfer (9,E,a,b,d; accounting: 12,B,b,d; 12,D,b,d) and use (user: 8,E,C,d;) during period as in target year, average ITMO transfer (9,E,a,b,e; accounting: 12,B,b,e; 12,D,b,e) and use (8,E,c,e) with regards to “activity”, “representative transfer” throughout period (issuer: 9,E,a,b,g; user: 8,E,c,g; accounting: 12,B,b,g;12,D,b,g), reflection in biennial reports (issuer: 9,E,a,b,f; user: 8,E,c,f; accounting: 12,B,b,f;12,D,b,f)
- User needs to have full coverage of emissions by NDC (8,A,x)
- Absolute emissions NDC (all: 11,A,vii; issuer: 9,A,xxi; user: 8,A,ix)
- Quantification in CO<sub>2</sub>e units (6,g,a,a)
- Comparative accounting Art. 6.2 and 6.4 (2, a, xii)
- All NDC types (2,a,ix; users: 8,A,xxi) and gases (users: 8,B,b,b).
- Unilateral measures (2,a,viii) are to be avoided

### 5.1. Contention and possible “red lines”

An international oversight on environmental integrity is not acceptable to the LMDCs as well as Japan. A complete absence of rules on environmental integrity is not acceptable to the EU and AOSIS.



## 5.2. Possibilities to resolve contentious issues and remaining inconsistencies

The middle ground requiring reporting of parties on how they ensure environmental integrity could be an area for convergence. Accounting rules should be made consistent between user and issuer and reporting show clearly the nature of the transferred unit. A way forward would be to ask the CMA to annually provide guidance with regard to environmental integrity.

## 6. Sustainable development

The strictest approach suggested is a supervisory body checking compliance with a set of international rules on sustainable development contributions of Art. 6.2, including human rights, listed in the principles (2,a,iii; 19; 21; 24,E). Internationally defined guiding principles would include

- No environmental harm (all: 11,A,xvi; 17,I; user: 8,A,xix; issuer: 9,A,xix)
- No adverse effect on human rights (18,I; all: 11,A,xvi; user: 8,A,xx; issuer: 9,A,xx)

A less stringent approach would be sustainable development contributions defined by countries, with reporting requirements (issuer: 9,E,a,a,xvi; 13,B,iii; user: 8,E,b,xvii; 13,D,iv), link to SDG processes

The least stringent approach would be full national sovereignty (2,a,v; user: 8,A,xxi).

### 6.1. Convergence

A middle ground could be a reporting requirement on how Art. 6.2 activities contribute to Sustainable Development.

### 6.2. Contention and possible “red lines”

Developing countries, especially the LMDCs do not want international rules on Sustainable Development contributions.

### 6.3. Possibilities to resolve contentious issues and remaining inconsistencies

There is limited room for maneuver on the Sustainable Development issue.



## 7. Limits

### 7.1. Spectrum of views

Parties are calling for several types of restrictions placed on either the participation in cooperative approaches or on the use or creation of ITMOs.

Brazil seeks to restrict participation in cooperative approaches to Parties with quantitative absolute emission targets, underpinned by a calculation report of NDC permitted emissions that is reviewed by technical experts. In a similar vein, the EU seeks to limit participation to Parties that have long term low emission development strategies in place.

AOSIS is calling for a number of limitations on the transfers of ITMOs to prevent “overselling”. This includes restrictions on certain types, sectors or vintages. Concerned with the effects of unused ITMOs on environmental integrity AOSIS also seeks to rule out carry-over of ITMOs from the pre-2020 period or between NDC periods.

For the buying countries, AOSIS and AGN wish to see limits on how many ITMOs a country may use towards achieving its NDC (supplementarity).

### 7.2. Treatment of the issue in the informal note

Limits on the issuance/creation/transfer or the use of ITMOs towards NDC are specifically addressed in section 12,H (Limits) of the informal note as well as in section 23 (multilateral governance). Restrictions concerning the participation in cooperative approaches are found throughout the document.

The main options for limits on issuance/creation/transfer include:

- Limit on the creation of tradable units based on a calculation: NDC target multiplied by the NDC period (e.g. 5 or 10 years), with downward adjustment based on the previous actual emissions trend (12,H,a,i)
- Limits on transfers/overselling (e.g. may only transfer ITMOs up to a limit, calculated as a percentage of annual emissions or percentage of quantified NDC) (12,H,a,ii)
- Restrictions on types of transfers (12,H,a,iii)
- Quantitative restrictions on carry-over (12,H,a,iv)
- Restrictions in sectors with high degree of uncertainty in emission estimates (12,H,a,v)
- No use of pre-2020 units post 2020 (12,H,a,vi)
- Compulsory limitation of tradeable units, within NDC timeframe reserve, permitted emission units to be exclusively used for retirement or cancellation purposes (23d).

And for the use of ITMOs towards NDCs options include:



- Use by a Party towards NDC must be supplemental to domestic action (12,H,b,i)
- Limits on banking/carrying-over (12,H,b,ii)
- Limits on use of vintages (12,H,b,iii)
- Limits on the percentage of NDC compliance that can be achieved through the use of ITMOs (12,H,b,iv)

Finally the informal note contains several restrictions with respect to countries' participation in cooperative approaches:

- Have economy wide target, absolute emissions, multi-year (12,H,b,v)
- Have economy wide long term low emissions strategy (12,H,b,v)
- Have consistent inventories (12,H,b,vii)
- [Have] National systems, registries, international transaction log, national accounts (23a)
- [Have] Quantification of NDC-permitted emissions, including common metrics, calculation report of permitted emissions, technical expert review of the calculation report (23b)
- [Have] Issuance of NDC permitted emission units (23c)

With respect to issuance/creation and use the informal note also specifically includes a "no limits" option (12,H,a,b), (12,H,b,b).

### **7.3. Analysis of common ground, red lines and opportunities for compromise**

It is rather inconceivable that relevant groups of Parties would agree to limiting participation in cooperative approaches based on the requirement to quantify emissions (see above). This is unlikely to be agreeable to LMDCs and AGN, among others. If Parties do not agree to the quantification of NDC emissions, it is also difficult to see how limiting the percentage of NDC emissions that may be sold as ITMOs could be acceptable.

Similarly, the exclusion of "types of transfers" or certain sectors is likely to be met with opposition on the basis of being insufficiently clear or encroaching on perceived prerogatives of Parties. Restrictions on banking and carry over, on the other hand, could convince many Parties, especially if ITMOs are not conceived as stand-alone tradeable units but tied to NDC implementation periods and reporting cycles. Some Parties may find it important though that ruling out banking/carry over of ITMOs would not by the same token prevent flexible use of units generated by the Article 6.4 mechanism or other carbon standards during various NDC periods.

## **8. Links to other rules of the Paris Agreement**

### **8.1. Spectrum of views**

Article 6.2 is not developed in isolation but has close links to the other sub-Articles of Article 6 (namely the 6.1 chapeau and the Article 6.4 mechanism) as well as to other provisions of the Paris Agreement.



The most direct link is to the accounting and transparency frameworks that are being established under Articles 4.13 (NDC accounting) and 13.7 (tracking progress towards NDCs) as well as to the compliance mechanism of Article 15. While it is generally undisputed that the reporting and accounting of ITMOs would integrate into these processes, different views exist as to whether Article 6.2 would need additional oversight arrangements, expert reviews or even dedicated bodies. Some Parties (AGN, South Africa, EIG, AOSIS) fear that processes established under the transparency framework alone would not sufficiently ensure environmental integrity of cooperative approaches and call for additional oversight arrangements. Members of the Umbrella Group, on the other hand, see the Article 6.2 guidance feed seamlessly into the reporting and review processes established elsewhere in the Paris rulebook.

In addition, many Parties make connections between Article 6.2 and the long-term goal of the Paris Agreement in Article 2. While there is no clear operational connection, it is seen as higher level objective guiding the elaboration of the Article 6.2 rules. In the same spirit the EU also highlights the relevance of Article 3 (progression over time).

The LMDCs emphasize the links between Article 6.2 with Article 4.7 (mitigation co-benefits from adaptation action) and Article 4.15 (response measures). With regards to Article 4.7, this translates into an emphasis on using the term ‘mitigation co-benefits from adaptation action’ in the Article 6.2 guidance. With regard to 4.15, a procedural link is pursued, meaning that progress in the negotiations of Article 6 and Article 4.15 should be symmetrical.

Most Parties maintain that emission reductions from the Article 6.4 mechanism should, when internationally transferred, be subject to the Article 6.2 guidance and to corresponding adjustments. The AGN and Arab Group distinguish the case where emission reductions from the Article 6.4 mechanism are not used towards NDCs but are retired or voluntarily cancelled. They argue that in such a case application of Article 6.2 guidance is not needed because no ITMOs are changing hands and consequentially no risk of double counting arises. Brazil states that the Article 6.2 guidance is not applicable to the country that is hosting activities under Article 6.4. Corresponding adjustments would not be required until the first transfer between national registries, hence they would only take place between the “SDM registry” and the acquiring Party’s national registry. Another angle that some Parties are taking is that any methodologies developed under 6.2 should not be any less rigorous than approaches under Article 6.4.

Some Parties (EIG) also highlight the link between Article 6.2 and non-UNFCCC processes, calling for any emission reductions that are exported (be it under CORSIA or for purposes of voluntary climate action or climate finance) to follow the Article 6.2 guidance.

Finally some Parties (Brazil, Ukraine) establish the link between the Article 6.2 guidance and the Kyoto Protocol mechanisms by considering CERs or ERUs to qualify as ITMOs.



## 8.2. Treatment of the issue in the informal note

The link to Article 2 is highlighted in the Preamble (1.i) and the scope and purpose section (3) of the informal note.

Article 4.7 and 4.15 are included in the section on principles in connection with addressing negative social and economic impacts (2.vi).

The note specifically mentions oversight arrangements for the cooperative approaches to be under other processes (e.g. Article 13, Article 4.13, Article 15) (14,c) (7,B,c,i) and specifically the reporting and review to be under Article 13.7 (7,B,c). In various places the note makes reference to the timing of ITMO reporting to be at the time of submitting information per Article 13,7 (8,C,c,c) (8,D,b,a) (9,C,c,c) (9,D,b,c) (12,F,e) (13,E,a). Furthermore, the use of ITMOs in each period should be reflected in the biennial reports under Article 13.7 (8,E,c,f) (9,E,b,f) (12,B,b,f) (12,D,b,f). To demonstrate the role of ITMOs in achieving NDCs, information should be forwarded to Article 4.13 (8,E,b) (9,E,b).

In a few places reference is made to the Article 6.4 mechanism, e.g. the need for comprehensive accounting between Article 6.2 and Article 6.4 (2,xii), the coverage of Article 6.4 under the scope and purpose of the guidance (3,iv) as well as the reference to CER under the SDM (6.g,x), (6,g,xi) or emission reductions and/or avoidance from the Article 6.4 mechanism (6,g,xii) in relation to ITMOs. Furthermore reference is made that Approving the methodologies and baseline approaches for crediting-type systems should be no less rigorous than Article 6.4 (7,B,a,iii) .

Article 6.1 is referenced only once under scope and purpose (3.ii)

Finally, section 28 deals with emissions reductions applied to other purposes than towards NDCs, identifying the following options:

- Towards other international mitigation action (28,i)
- Towards voluntary climate actions, climate finance(28,ii)
- May require accounting in accordance with Article 6.2 guidance if used for non-UNFCCC purposes if created/issued from within the scope of a host Party's NDC (28,iii).
- Require accounting in accordance with Article 6.2 guidance if used for non-UNFCCC purposes (28,iv)

## 8.3. Analysis of common ground, red lines and opportunities for compromise

As all Parties agree with the links to Articles 4.13 and 13.7, the issue is not finding common ground on these links but rather how to practically implement the linkage across agenda items. There are clear overlaps between the work on the Article 6.2 guidance under SBSTA and the elaboration of the modalities, procedures and guidelines



(MPG) for the transparency framework developed under the APA as well as with the APA agenda item on further guidance in relation to the mitigation section of decision 1/CP.21 that is dealing inter alia with NDC accounting. The link to Art. 4.7 can easily be implemented by allowing countries to create ITMOs for mitigation achieved as a co-benefit from an adaptation or economic diversification action. It may be more complicated to create a link to the response measures other; this probably requires exchange of a negotiation chip from another topic.

Not the linkages but the addition of oversight arrangements beyond those negotiated under the transparency framework are the difficult aspects of Article 6.2. In order to satisfy the environmental integrity concerns of many Parties it is clear that reporting on ITMOs will have to go beyond adding tabular formats to Parties reporting obligations under the transparency framework.

## References

UNFCCC (2017b): FCCC/SBSTA/2017/L.26, <http://unfccc.int/resource/docs/2017/sbsta/eng/l26.pdf> (accessed 17 December 2017)

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