

## **New Market Mechanism**

### SBSTA 41

The Environmental Integrity Group (EIG) welcomes the opportunity to submit its views on the work programme under SBSTA to elaborate the modalities and procedures for the new market-based mechanism (NMM), based on the suggestions contained in SBSTA 40 conclusions. SBSTA 40 invited Parties and admitted observer organizations to submit to the secretariat their views on the mechanism<sup>1</sup>, including on:

- 1) Its design and governance;
- 2) The elaboration of the possible elements of its modalities and procedures;
- 3) The meaning of “a net decrease and/or avoidance of global greenhouse gas emissions”;
- 4) Lessons learned from the mechanisms under the Kyoto Protocol that could be relevant to the further elaboration of the possible elements of the work programme;
- 5) Its relationship with the framework for various approaches and the mechanisms under the Kyoto Protocol;
- 6) Its relationship to enhanced mitigation ambition.

The EIG would like to reemphasize the important purpose of the NMM which is to promote the development of mitigation actions in a cost-effective way and therefore to contribute to address the urgent need for further global ambitious mitigation action, before and after 2020. In support of SBSTA 40 conclusions the EIG aims at a substantive decision on the NMM at COP 20.

### **The relationship of NMM to enhanced mitigation ambition (6)**

The EIG qualifies the NMM as a cost-efficient instrument to reduce emissions before and after 2020. The use of units (outcomes) from the mechanism for meeting pledges should be supplemental to domestic action. Furthermore, the NMM should go beyond pure offsetting and deliver net decrease and / or avoidance of global emissions. This means that the buyer country uses units in a supplemental way to its domestic action. In addition, to ensure net decrease, a certain share of the emission reductions is neither used by the buyer country nor by the host country.

---

<sup>1</sup> <http://unfccc.int/resource/docs/2014/sbsta/eng/l12.pdf>

The EIG would like to emphasize that the NMM should not substitute the CDM but complement it. CDM, JI, IET and new market mechanisms should be complementary mechanisms that all play a role in enhanced mitigation action.

**Lessons learned from the mechanisms under the Kyoto Protocol that could be relevant to the further elaboration of the possible elements of the work programme (4)**

In order to consider lessons learned from the mechanisms under the Kyoto Protocol regarding design and governance, the EIG is of the view that a specific timeline regarding the development and the use of market mechanisms is needed.

Market mechanisms used currently under the Kyoto Protocol are classified as allocation mechanism and offset mechanism; basic procedures of these mechanisms are summarized below:

**Allocation mechanism:** Setting target → Allocating units → GHG reduction and trading units → Submitting results → Checking compliance → Retiring units → Penalty, banking, etc.

**Offset mechanism:** Project design document → Registration of project → Monitoring and verification → Issuing offset units (credits) → Trading units (credits)

The characteristics of the existing classifications also apply to the elaboration of possible elements of the NMM modalities and procedures. In order to decide whether the NMM should cover both classifications or should be limited to only one, it should be identified when the mechanism has been created. Decision 1/CMP.8 enables a pre-2020 start of such mechanisms as it allows for the use of units from mechanisms established under the Convention by Parties with commitments in the second commitment period of Kyoto Protocol to assist them in achieving compliance.<sup>2</sup> In conjunction with Decision 2/CP.17 where the NMM was formally defined<sup>3</sup>, the EIG qualifies Decision 1/CMP.8 as the legal ground for the establishment of the NMM pre-2020. The EIG therefore considers both periods (pre- and post-2020) as being relevant to the NMM.

Therefore, a decision on the characteristics of the NMM to be used pre-2020 needs to consider the relationship with the mechanisms under the Kyoto Protocol. At the current stage the EIG sees the scope of the NMM until 2020 limited to the offset mechanism classification. The reason for that conclusion is that:

<sup>2</sup> see Annex 1 1/CMP.8 (J) <http://unfccc.int/resource/docs/2012/cmp8/eng/13a01.pdf>

<sup>3</sup> see Para. 83, <http://unfccc.int/resource/docs/2011/cop17/eng/09a01.pdf>

- first, an allocation mechanism already applies for all Annex B Parties to the Kyoto Protocol (so there would be no need for these Parties to have a second allocation mechanism), and
- second, all Parties currently discuss enhanced mitigation activities under workstream 2 of the ADP (and a duplication of work should be avoided given the tight timetables until COP 21 in Paris).

However, for the post-2020 period both classifications - offset and allocation mechanisms - should be further elaborated. Therefore, the work program should address both classifications within its pre-2020 scope, since the allocation mechanism has also an important mitigation potential

The EIG would like to again reemphasize its view that the NMM should not substitute the CDM but complement it.

With respect to the consideration of lessons learned regarding the two different market scope classifications the EIG is of the view that:

- an allocation-classified mechanism should draw, among others, on the experiences of the establishment of national registries, governance for compliance check, carry-over (banking), penalty; and
- an offset-classified mechanism should draw upon the experiences of the processes for developing and approving methodologies for baseline and monitoring, establishing offset registries, methods for preventing double counting of units, etc.

**Relationship of the NMM with the framework for various approaches and the mechanisms under the Kyoto Protocol (5)**

**Relationship to the FVA**

The EIG would like to refer to its submission on non-market-based approaches<sup>4</sup> where the relationship of the NMM to the framework for various approaches has been visualized as follows:

Framework for Various Approaches, FVA			Outside FVA
Market approaches		Non-Market-based Approaches, NMA	
New Market Mechanism, NMM	Other market mechanisms (incl. bilateral agreements)	Accountable NMA <sup>5</sup>	Non-accountable NMA <sup>6</sup>

The EIG considers that the NMM is to be operated under the FVA. To ensure coherence of rules and structures across mechanisms and to avoid that there are largely diverging quality standards between mechanisms, some core elements will apply both to mechanisms qualifying for the FVA and to the mechanisms developed according to NMM rules (see EIG submission on the FVA).

**Relationship to the mechanisms of the Kyoto Protocol**

As already stated, the NMM aims at complementing the existing Kyoto mechanisms rather than substituting them. However, the NMM shall build upon the valuable experiences of the Kyoto mechanisms. The CDM and JI have allowed the development of strong expertise by a wide range of stakeholders. In addition, many synergies between market mechanisms can be identified, including: the large corpus of methodologies, standards and tools, the regulatory bodies, the International Transaction Log (ITL) and the accreditation procedures.

In addition to the consideration of these synergies, the relation of the Kyoto mechanisms to the NMM is characterized by a broader scope and application of the latter one. The NMM scales up mitigation action in comparison to the CDM and JI by facilitating mitigation activities in large segments of economies, their sectors and subsectors or policies. Furthermore, the NMM shall be

<sup>4</sup> [http://unfccc.int/files/cooperation\\_support/market\\_and\\_non-market\\_mechanisms/application/pdf/nma\\_environmental\\_integrity\\_group\\_12092013.pdf](http://unfccc.int/files/cooperation_support/market_and_non-market_mechanisms/application/pdf/nma_environmental_integrity_group_12092013.pdf)  
<sup>5</sup> Accountable NMA means NMA accountable toward an emission reduction target of a contributor country.  
<sup>6</sup> Non-accountable NMA means NMA that cannot be accountable toward an emission reduction target of a contributor country; it is only accountable toward the emission reduction target of the host country.

guided by a stronger role of the designated national authority (or another national entity) of the host countries as well as by the principle of a net decrease and/or avoidance of global greenhouse gas emissions.

### **The meaning of “a net decrease and/or avoidance of global greenhouse gas emissions” (3)**

The EIG understands “a net decrease and/or avoidance of global greenhouse gas emissions” as safeguard within a market based mechanism which leads to more abatement than credited, i.e. that the ratio of actual abatement to credits issued is greater than 1.<sup>7</sup>

The EIG sees “net decrease and/or avoidance of global greenhouse gas emission” as involving emission reductions beyond pure offsetting, i.e. beyond the commitment of both the buyer and the host countries. This net atmospheric benefit can only be achieved if a certain share of the resulting emission reductions is neither used for compliance by a buyer country nor used by the host country for compliance with its commitment. Therefore, it goes beyond a situation where the emission reductions are distributed between the buyer and host countries, with a share of the emission reductions being credited and used by the buyer country to meet its commitment and the other share of the emission reductions not being credited but kept by the host country to meet its own commitment. There are mainly two ways for achieving this net atmospheric commitment. One way is if these reductions occur outside the existing reduction commitment of a host country. Another way would be a post-issuance discount or cancellation by the buyer or host country where the emission reductions take place in segments of the economy covered by the commitment.

### **The elaboration of the possible elements of its modalities and procedures (2)**

Considering the findings concluded under (2) the elaboration of the possible elements of the modalities and procedures of the NMM would take into account the time period when the NMM is used:

- pre-2020: only offset mechanism
- post-2020: offset and allocation mechanism<sup>8</sup>.

Elements should be developed based on the lessons learnt, practices and experiences within the scope of the Kyoto mechanisms (CDM, JI, and IET ). The elements could apply as shown in the table below – common elements apply to both classifications (offset and allocation) within “Principles”,

---

<sup>7</sup> SEI(2013), Potential for International Offsets to Provide a Net Decrease of GHG Emissions, Working Paper(2013-06), Stockholm Environment Institute

<sup>8</sup> depending on the continuation of EIT post 2020

“Governance” and “Management of units”. Different elements apply with regard to “Methodology” – depending on the mechanism classification. For more details on EIG’s views on these elements, please refer to the September 2013 submission.<sup>9</sup>

### The design and governance of the NMM (1)

1	2	3	
Principles	voluntary participation		
	scale-up of reduction		
	environmental integrity	sustainable development	
		avoid double counting	
		net reduction and/or avoidance	
	others		
supplemental use of unit			
Governance	international body	framework for body	
		role of international body	
	Party	criteria for participation	
		conformity check by int. body	
	third organization	validation/verification	
relation with Kyoto governance			
Management of units	tracking of units	registry, ITL	
	double counting		
	share of proceeds		
Methodology	scope of mitigation action	broad segment of economy	
	accounting rules	(allocation) emissions accounting	
		(offsets) reduction accounting	
	baseline, credit threshold	(only offsets)	
	crediting period	(only offsets)	
others			
Others			

<sup>9</sup> [http://unfccc.int/files/cooperation\\_support/market\\_and\\_non-market\\_mechanisms/application/pdf/nmm\\_environmental\\_integrity\\_group.pdf](http://unfccc.int/files/cooperation_support/market_and_non-market_mechanisms/application/pdf/nmm_environmental_integrity_group.pdf)