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**AD HOC WORKING GROUP ON FURTHER COMMITMENTS  
FOR ANNEX I PARTIES UNDER THE KYOTO PROTOCOL**

Seventh session

Bonn, 29 March to 8 April 2009

**Item 5 (a) of the provisional agenda**

**Other issues arising from the implementation of the work programme of the Ad Hoc Working Group on  
Further Commitments for Annex I Parties under the Kyoto Protocol**

**Emissions trading and the project-based mechanisms**

**Further elaboration of possible improvements to emissions trading and  
the project-based mechanisms under the Kyoto Protocol**

**Note by the Chair**

*Summary*

This note contains a further elaboration by the Chair of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP) of possible improvements to emissions trading and the project-based mechanisms, namely the clean development mechanism and joint implementation under the Kyoto Protocol.

The elaboration builds upon the elements contained in annexes I and II of the report of the AWG-KP at the first part of its sixth session, an earlier elaboration of these issues by the Chair and further input submitted by Parties.

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## **I. Introduction**

### **A. Mandate**

1. The Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP), at its resumed sixth session, agreed to continue, including through in-depth consultations at its seventh session, its deliberations on the possible improvements to emissions trading and the project-based mechanisms identified in annexes I and II to the report on the first part of its sixth session,<sup>1</sup> with the focus on those in annex I and avoiding duplication of work in its consideration of those in annex II.<sup>2</sup>

2. In order to facilitate these consultations, the AWG-KP invited Parties to submit to the secretariat, by 6 February 2009, further input on how the possible improvements to emissions trading and the project-based mechanisms would function<sup>3</sup> and requested its Chair to further elaborate the possible improvements to emissions trading and the project-based mechanisms on the basis of document FCCC/KP/AWG/2008/INF.3 and the further input submitted by Parties.<sup>4</sup>

### **B. Scope of the note**

3. In response to the above mandate, this note contains a further elaboration by the Chair of the AWG-KP of possible improvements to emissions trading and the project-based mechanisms, namely the clean development mechanism and joint implementation.

4. This note should be read together with the note by the Chair on possible elements of a text relating to issues outlined in document FCCC/KP/AWG/2008/8, paragraph 49, and the note by the Chair on the elaboration on how to address, where applicable, the definitions, modalities, rules and guidelines for the treatment of land use, land-use change and forestry.<sup>5</sup>

### **C. Possible action by the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol**

5. The AWG-KP may wish to consider the further elaboration of possible improvements to emissions trading and the project-based mechanisms contained in this note and advance its work in clarifying how these possible improvements would function, with a view to the need to develop text for adoption by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol at its fifth session.

## **II. Approach to the elaboration**

6. The further elaboration of possible improvements for the period after 2012 with potentially significant implications for the ability of Annex I Parties to achieve mitigation objectives is contained in annex I to this note. The further elaboration of other possible improvements is contained in annex II to this note.

7. The submissions referred to in paragraph 2 above focus on the possible improvements contained in annex I to this note. These submissions mostly contain views supporting, or not supporting, individual possible improvements and contain less input on how these improvements would function. Parties

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<sup>1</sup> FCCC/KP/AWG/2008/5.

<sup>2</sup> FCCC/KP/AWG/2008/8, paragraph 51 (a).

<sup>3</sup> These submissions are contained in document FCCC/KP/AWG/2009/MISC.3.

<sup>4</sup> FCCC/KP/AWG/2008/8, paragraph 51 (b) and (c).

<sup>5</sup> Contained in documents FCCC/KP/AWG/2009/4 and FCCC/KP/AWG/2009/INF.1, respectively.

provided limited views on the possible improvements contained in annex II to this note. Guidance is needed on how the elements in annex II should be addressed further in the work of the AWG-KP.

8. Both annexes maintain the structure developed at the first part of the sixth session, which was also used in the earlier elaboration of these issues by the Chair, as contained in document FCCC/KP/AWG/2008/INF.3. Additions to the earlier elaboration of these issues by the Chair have been underlined. Notes have been maintained, and in places expanded, to indicate further issues that may need to be taken into account when considering these possible improvements. The Chair has made every effort to advance all ideas and alternative options in a balanced manner, to the extent possible given the differing levels of inputs that could be drawn upon.

9. The annexes to this note continue the approach taken in the earlier elaboration of these issues by the Chair by keeping in mind the need to progress towards legal or decision text.

10. This note does not strive to fully develop all aspects and details of the possible improvements. Instead, a level of detail has been sought that can provide sufficient clarity on how the mechanisms can help Annex I Parties achieve their mitigation objectives after 2012, without overloading the process of reaching agreement with details that can be resolved after the AWG-KP has completed its work.

Annex I

**Possible improvements to emissions trading and the project-based mechanisms under the Kyoto Protocol for the period after 2012 with potentially significant implications for the ability of Annex I Parties to achieve mitigation objectives**

Note: For each element contained in this annex, there exists a 'status quo' option representing the maintenance of the current approaches and rules adopted by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP).

Note: Some Parties have expressed the view that the elements in sections I.E, I.F, I.G, I.J, II.A, III.A, III.B, III.C, IV.C and IV.D below would require an amendment to the Kyoto Protocol and would not be within the mandate of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP). Some other Parties have expressed the view that legal analysis is needed to determine which elements in this annex would require a decision of the CMP or an amendment to the Kyoto Protocol and that such amendments would be within the mandate of the AWG-KP.

## I. Clean development mechanism

### A. Include other land use, land-use change and forestry activities<sup>1</sup>

1. The eligibility of land use, land-use change and forestry (LULUCF) activities under the clean development mechanism (CDM) includes:

- (a) Option 1: Afforestation and reforestation [including wood produced from forests established under the CDM];
- (b) Option 2: Reducing emissions from deforestation and forest degradation;
- (c) Option 3: Restoration of wetlands;
- (d) Option 4: Sustainable forest management and other sustainable land management activities;
- (e) Option 5: Soil carbon management in agriculture;
- (f) Option 6: Revegetation, forest management [including wood produced from forests established under the CDM], cropland management and grazing land management, as defined in decision 16/CMP.1.

2. In relation to LULUCF activities under the CDM, the CMP shall adopt modalities and procedures for:

- (a) Option 1: Temporary certified emission reductions (tCERs) and long-term certified emission reductions (lCERs);
- (b) Option 2: Responsibility assumed on a voluntary basis by the host Party for the cancellation of permanent units in the event of a reversal of greenhouse gas (GHG) removals by sinks that had occurred through project activities;

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<sup>1</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

- (c) Option 3: Insurance issued for project activities to cover the cancellation of permanent units in the event of a reversal of GHG removals by sinks that had occurred through these project activities;
- (d) Option 4: Buffers to ensure that quantities of credits for carbon stored through project activities are reserved for cancellation in the event of a reversal of GHG removals by sinks that had occurred through these project activities;
- (e) Option 5: Credit reserves to ensure that quantities of units that are not retired at the end of a commitment period are reserved for cancellation in the event of a reversal of GHG removals by sinks that had occurred through project activities;
- (f) Option 6: Exemptions from modalities and procedures for addressing potential non-permanence in the case of low-risk LULUCF project activities.

*Note: Further issues that may need to be addressed include:*

- Whether combinations of the above options for eligible LULUCF activities should be included
- Whether project participants may choose from a menu of modalities and procedures for addressing potential non-permanence

#### **B. Introduce a cap for newly eligible land use, land-use change and forestry activities<sup>2</sup>**

3. A Party may use certified emission reductions (CERs)<sup>3</sup> issued for LULUCF project activities under the CDM for compliance with its emission commitment under Article 3, paragraph 1,<sup>4</sup> to a maximum of [x] per cent of its assigned amount pursuant to Article 3, paragraphs 7 and 8.

#### **C. Include carbon dioxide capture and storage<sup>5</sup>**

4. Option 1: Carbon dioxide capture and storage (CCS) activities are not eligible as CDM project activities.

Option 2: Annex I Parties are to refrain from using CERs generated from CCS activities to meet their commitments under Article 3, paragraph 1.

Option 3: CCS activities may be registered under the CDM and Annex I Parties may use CERs issued for such project activities, on the basis of emission reductions achieved during the second commitment period, to meet their emission commitments under Article 3, paragraph 1, for the second commitment period.

*Note: Further issues that may need to be addressed include:*

- *The short- and long-term liability (e.g. in relation to leakage and non-permanence)*
- *The provisions for monitoring, reporting and verification, taking account of data availability*
- *The possible environmental impacts*

<sup>2</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

<sup>3</sup> In this annex, "CERs" may also refer to temporary certified emissions reductions and long-term certified emission reductions.

<sup>4</sup> In this annex, "Article" refers to an article of the Kyoto Protocol.

<sup>5</sup> This issue is being considered by the Subsidiary Body for Scientific and Technological Advice under its work on carbon dioxide capture and storage in geological formations as CDM project activities. Furthermore, at its fourth session, the CMP requested the Executive Board of the CDM to assess the implications of the possible inclusion of carbon dioxide capture and storage in geological formations as CDM project activities and report back to the CMP at its fifth session (decision 2/CMP.4, paragraph 41).

- *The definition of project boundaries*
- *The potential for perverse outcomes*

#### **D. Include nuclear activities**

5. Option 1: Activities relating to nuclear facilities are not eligible as CDM project activities.

Option 2: Activities relating to new nuclear facilities may be registered under the CDM, and Annex I Parties may use CERs issued for such project activities, on the basis of emission reductions achieved during the second commitment period, to meet their emission commitments under Article 3, paragraph 1, for the second commitment period.

*Note: Further issues that may need to be addressed include:*

- *Specific criteria or requirements for eligible nuclear activities*
- *Costs relating to access to the technology*
- *The direct contribution to emission reductions*
- *Issues relating to non-proliferation*
- *Issues relating to permanent disposal of nuclear waste*
- *Safety, security and safeguards*

#### **E. Introduce sectoral clean development mechanism for emission reductions below a baseline defined at a sectoral level**

6. Sectoral CDM project activities, covering all emission sources within a defined sector, may be registered under the CDM and shall be subject to all modalities and procedures for the CDM adopted by the CMP and all procedures and decisions issued by the CDM Executive Board, except where specific modalities, procedures or decisions are defined by the CMP or the Executive Board for sectoral CDM project activities.

7. The supervision of the CDM by the Executive Board shall extend to sectoral CDM project activities. In this context, the Executive Board shall amend and establish its procedures as necessary for the effective functioning of sectoral CDM project activities.

8. Option 1: The baseline for a sectoral CDM project activity shall be the scenario that reasonably represents the anthropogenic emissions by sources of GHGs within the sector boundary, or the sum of the changes in carbon stocks in the carbon pools within the sector boundary, that would occur in the absence of the project activity.<sup>6</sup>

Option 2: The baseline shall be the carbon intensity [within the sector boundary during the calendar year 2012] [defined by an appropriate benchmark established on the basis of each sector in each host country].

9. The sector boundary for a sectoral CDM project activity shall encompass all anthropogenic emissions by sources and removals by sinks of GHGs that are reasonably attributable to the defined sector.

10. Individual CDM project activities, registered at the time a sectoral CDM project activity is registered and falling within the sector boundary, may continue until the end of their current crediting period. The quantity of CERs issued on the basis of such individual CDM project activities shall be deducted from the quantity of CERs to be issued on the basis of the sectoral CDM project activity.

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<sup>6</sup> This option reflects the current provisions for the CDM and is based upon decision 3/CMP.1, annex, paragraph 44.

Once a sectoral CDM project activity is registered for a sector, no further CDM project activities may be approved in relation to that sector.<sup>7</sup>

11. There shall be no double-counting of emission reductions or removals between sectoral CDM project activities.

12. In relation to sectoral CDM project activities, the CMP shall adopt modalities and procedures for:

- (a) The determination of a sector boundary;
- (b) The determination of additionality for sectoral CDM project activities;
- (c) The determination of sectoral baselines, in particular through the use of standardized baselines;
- (d) The monitoring, verification and certification of emissions, and of emission reductions and removals, within the sector boundary;
- (e) The treatment of potential leakage from within the sector boundary.

*Note: The following table is to clarify the terminology used in this section.*

<i>Mechanism under which the activity is undertaken</i>	<i>Clean development mechanism</i>
<i>What would be registered?</i>	<i>Sectoral CDM project activity</i>
<i>What would be the scope?</i>	<i>Defined sector</i>
<i>What would be the reference level?</i>	<i>Baseline</i>
<i>What would be issued?</i>	<i>Certified emission reductions</i>

*Note: Further issues that may need to be addressed include:*

- *The definition of a sector*
- *New measures relating to the governance and operation of sectoral CDM activities*
- *The potential for crediting cumulative emission reductions*

#### **F. Introduce sectoral crediting of emission reductions below a previously established no-lose target**

13. A sectoral crediting mechanism is established. A non-Annex I Party may propose to the CMP a crediting target for emissions or removals within a defined sector to be achieved through national actions. Reductions in emissions by sources in the sector below the crediting target, or enhancements in removals by sinks in the sector above the crediting target, shall result in the generation of credits which may be used by Annex I Parties to meet their emission commitments under Article 3, paragraph 1.

14. The sectoral crediting mechanism shall be supervised by [a dedicated body constituted by the CMP and operating under its authority] [the CDM Executive Board]. Before the supervisory body registers a sectoral crediting activity, the crediting target shall be recommended to the CMP by the supervisory body and shall be approved by the CMP.

15. A crediting target shall be [set below the level of projected anthropogenic emissions by sources of GHGs within the sector boundary or above the sum of the projected changes in carbon stocks in the

<sup>7</sup> The purpose of this provision would be to avoid the double-counting of emission reductions between a sectoral CDM project activity and other CDM project activities.



carbon pools within the sector boundary] [as a carbon intensity target below the level of the projected carbon intensity of emissions by sources of GHGs within the sector boundary].

16. The sector boundary for a sectoral crediting activity shall encompass all anthropogenic emissions by sources and removals by sinks of GHGs that are reasonably attributable to the defined sector.

17. CDM project activities, registered at the time a sectoral crediting activity is registered and falling within the sector boundary, may continue until the end of their current crediting periods. The quantity of CERs issued on the basis of such CDM project activities shall be deducted from the quantity of credits to be issued on the basis of the sectoral crediting activity. Once a sectoral crediting activity is registered for a sector, no further CDM project activities may be approved in relation to that sector.<sup>8</sup>

18. There shall be no double-counting of emission reductions or removals between sectoral crediting activities.

19. The following LULUCF activities shall be eligible under the sectoral crediting mechanism: [...]

20. The non-Annex I Party may receive financing and technology in advance of credits being generated for a crediting target.

21. No credits shall be generated for a sectoral crediting activity if a crediting target has not been met. There shall be no other consequences for a Party that does not meet a crediting target.

22. In relation to the sectoral crediting mechanism, the CMP shall adopt modalities and procedures for:

- (a) The governance and administration of the sectoral crediting mechanism;
- (b) The determination of a sector boundary;
- (c) The determination and approval of crediting targets [on a country-by-country basis];
- (d) The monitoring, reporting and verification of emissions, and of emission reductions and removals, within the sector boundary;
- (e) The treatment of potential leakage from within the sector boundary;
- (f) The issuance of credits.

*Note: The following table is to clarify the terminology used in this section.*

<i>Mechanism under which the activity is undertaken</i>	<i>Sectoral crediting mechanism</i>
<i>What would be registered?</i>	<i>Sectoral crediting activity</i>
<i>What would be the scope?</i>	<i>Defined sector</i>
<i>What would be the reference level?</i>	<i>Crediting target</i>
<i>What would be issued?</i>	<i>Credits</i>

*Note: Further issues that may need to be addressed include:*

- *The definition of a sector*
- *The degree to which a crediting target should be set below the projected level of emissions by sources, or above the projected level of removals by sinks within the sector boundary, taking into*

<sup>8</sup> The purpose of this provision would be to avoid the double-counting of emission reductions between a sectoral crediting activity and CDM project activities.

*account national circumstances, capabilities and factors such as the homogeneity of products/processes, and the potential for efficiency and innovation in the sector*

- *The definition of the credit to be issued*
- *The potential for crediting cumulative emission reductions*
- *The roles and functions of the supervisory body*

#### **G. Introduce crediting on the basis of nationally appropriate mitigation actions**

23. Nationally appropriate mitigation actions (NAMAs), as referred to in decision 1/CP.13 (Bali Action Plan), paragraph 1 (b) (ii), may be registered under the CDM and shall be subject to all modalities and procedures for the CDM adopted by the CMP and all procedures and decisions issued by the CDM Executive Board, except where specific modalities, procedures or decisions are defined by the CMP or the Executive Board for NAMAs registered as CDM project activities.

24. The baseline for a NAMA registered as a CDM project activity shall be the scenario that reasonably represents the anthropogenic emissions by sources of GHGs within the NAMA boundary, or the sum of the changes in carbon stocks in the carbon pools within the NAMA boundary, that would occur in the absence of the project activity.

25. The NAMA boundary shall encompass all anthropogenic emissions by sources and removals by sinks of GHGs that are reasonably attributable to a defined NAMA.

26. Individual CDM project activities, registered at the time a NAMA is registered as a CDM project activity and falling within the NAMA boundary, may continue until the end of their current crediting period. The quantity of CERs issued on the basis of such individual CDM project activities shall be deducted from the quantity of CERs to be issued on the basis of the NAMA registered as a CDM project activity. Once a NAMA is registered, no further CDM project activities may be approved in relation to activities within the NAMA boundary.<sup>9</sup>

27. There shall be no double-counting of emission reductions or removals between NAMAs registered as CDM project activities.

28. NAMAs meeting the following criteria shall be eligible under the CDM:

- (a) NAMAs not supported by financing and technology transfer by developed countries outside the context of the CDM;
- (b) NAMAs with high costs;
- (c) [...]

29. In relation to NAMAs registered as CDM project activities, the CMP shall adopt modalities and procedures for:

- (a) The scope of NAMAs qualifying for crediting under the CDM;
- (b) The determination of a NAMA boundary;
- (c) The determination of additionality for NAMAs registered as CDM project activities;
- (d) The determination of NAMA baselines;
- (e) The discounting of credits to be issued;

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<sup>9</sup> The purpose of this provision would be to avoid the double-counting of emission reductions between a NAMA registered as a CDM project activity and other CDM project activities.

- (f) The monitoring, verification and certification of emissions, and of emission reductions and removals, within the NAMA boundary;
- (g) The treatment of potential leakage from within the NAMA boundary.

*Note: The following table is to clarify the terminology used in this section.*

<i>Mechanism under which the activity is undertaken</i>	<i>Clean development mechanism</i>
<i>What would be registered?</i>	<i>NAMA as a CDM project activity</i>
<i>What would be the scope?</i>	<i>Defined NAMA</i>
<i>What would be the reference level?</i>	<i>Baseline</i>
<i>What would be issued?</i>	<i>Certified emission reductions</i>

*Note: Further issues that may need to be addressed include:*

- *The nature of participation of Parties*
- *The definition of NAMAs and the attribution to them of emission reductions and removals*
- *The consequences if an emission reduction or removal goal is not achieved*
- *The potential for perverse outcomes*
- *The potential for crediting cumulative emission reductions*

#### **H. Ensure environmental integrity and assess additionality through the development of standardized, multi-project baselines**

30. Option 1: The CDM Executive Board shall define standardized baselines for specific project activity types [and specific sectors or subsectors] under the CDM by establishing parameters, including benchmarks, and procedures and making them available for use by project participants and designated operational entities (DOEs) in the application or development of baseline methodologies. The Executive Board may define such standardized baselines for types of project activities meeting the following criteria: [...]

Option 2: The use of standardized baselines as the basis for the determination of additionality and emission baselines shall be mandatory for the registration of new CDM project activities of the following types: [...]

31. Option 1: Parameters and procedures shall be established by the Executive Board on the basis of similar project activities undertaken in the previous five years, in similar social, economic, environmental and technological circumstances, whose performance is among the top [10] [20] per cent of their category. Such parameters and procedures shall reflect national circumstances and shall be periodically adjusted.

Option 2: Parameters and procedures shall be established by the Executive Board on the basis of top performing installations or processes in the relevant sector, based on, inter alia, the performance of key technologies that are beyond common practice and technology penetration rates.

Option 3: Parameters and procedures shall be established by the Executive Board on the basis of the top [x] per cent of the current distribution of carbon intensity for specific types of project activities or within specific sectors. Such parameters and procedures shall reflect national circumstances and shall be periodically adjusted.

*Note: Further issues that may need to be addressed include:*

- *The types of project activities for which standardized baselines may be approved*
- *Further criteria for the definition of standardized baselines*

**I. Ensure environmental integrity and assess additionality through the development of positive or negative lists of project activity types**

32. Reductions in anthropogenic emissions by sources or enhancements of anthropogenic removals by sinks achieved by the following categories of project activities are deemed to be additional to any that would occur in the absence of the project activities:

- (a) [Criteria based on the primary technology employed in the project activity;]
- (b) [Criteria relating to the host Party of the project activity;]
- (c) [Criteria based on the scale of the project activity (small-scale or large-scale).]

*Note: Further issues that may need to be addressed include:*

- *The categories of project activities to be included on a positive list*
- *The process for periodic review of the positive list*
- *The consequences for project activities registered without an additionality test if the project circumstances or the list change such that the project activities are no longer covered by the positive list*

33. Reductions in anthropogenic emissions by sources or enhancements of anthropogenic removals by sinks achieved by the following categories of project activities are deemed not to be additional to any that would occur in the absence of the project activities and the project activities are not eligible as project activities under the CDM:

- (a) [Criteria based on the primary technology employed in the project activity;]
- (b) [Criteria relating to the host Party of the project activity;]
- (c) [Criteria based on the scale of the project activity (small-scale or large-scale).]

*Note: Further issues that may need to be addressed include:*

- *The categories of project activities to be included on a negative list*
- *The process for periodic review of the negative list*
- *The consequences for registered project activities if the project circumstances or the list change such that the project activities are now covered by the negative list*

**J. Differentiate the eligibility of Parties through the use of indicators**

34. Option 1: Non-Annex I Parties meeting the following criteria shall [not] be eligible to host [particular types of] project activities [in specific sectors in specific countries] under the CDM: [...]

Option 2: Non-Annex I Parties meeting the following criteria shall [not] be eligible to use specific types of methodologies for project activities under the CDM: [...]

35. Annex I Parties meeting the following criteria shall [not] be eligible to use CERs issued for [particular types of] project activities under the CDM for the purpose of compliance with commitments under Article 3, paragraph 1: [...]

*Note: Further issues that may need to be addressed include:*

- *Appropriate criteria and thresholds, taking account of differing national circumstances*
- *The project activity categories affected by the eligibility determination*
- *The types of methodologies affected by the eligibility determination*
- *Transition issues*

#### **K. Improve access to clean development mechanism project activities by specified host Parties**

36. Option 1: For [specified host Parties] [least developed countries and small island developing States] the following provisions shall apply:

- (a) The definition of a small-scale project activity is amended to [...];
- (b) Project activities that meet the requirements of small-scale project activities shall be [exempt from the requirement] [subject to simplified requirements] to demonstrate additionality;
- (c) The validation, verification and certification of project activities shall be funded through the [CDM management plan] [financial mechanism of the Convention].

Option 2: An Annex I Party may use CERs generated on the basis of project activities in a region for compliance with its emission commitment under Article 3, paragraph 1, up to a maximum of [x] CERs.

*Note: Further issues that may need to be addressed include:*

- *The determination of the host Parties for which provisions are applicable or definition of criteria for subsequently determining the host Parties for which provisions are applicable*
- *The definition of regions*
- *The identification of further measures to improve access*
- *Potential measures to improve the enabling environment for CDM project activities*

#### **L. Include co-benefits as criteria for the registration of project activities**

37. Option 1: Project activities that demonstrate specific co-benefits shall be promoted through the following means:

- (a) Exemption from payment of registration fees;
- (b) Exemption from the share of proceeds to cover the administrative expenses of the CDM and/or assist with the costs of adaptation;
- (c) Expedited time lines for the registration of project activities.

Option 2: Each project activity shall demonstrate specific co-benefits.

38. A DOE shall, as part of its validation of a project activity, confirm [that the designated national authority of the host Party has confirmed that its stipulated co-benefits are demonstrated by the project activity] [that the proposed project activity demonstrates [any of] [all] the following co-benefits:

- (a) Energy efficiency;
- (b) Technology transfer;

- (c) Environmental services such as conservation of biodiversity, management of hydrological resources and maintenance of air quality;
- (d) Poverty alleviation;
- (e) Economic growth;
- (f) Social benefits;
- (g) Strengthening human and institutional capacity.]

*Note: Further issues that may need to be addressed include:*

- *Provisions for the measurement of co-benefits, including indicators*
- *The definition of a sufficient level of co-benefits*
- *The relationship to project scale*
- *The contribution to minimization of negative spillover effects*
- *The potential for perverse outcomes*

**M. Introduce multiplication factors to increase or decrease the certified emission reductions issued for specific project activity types**

39. Option 1: A CDM project activity shall receive CERs equal to the emission reductions that are certified by the DOE multiplied by a factor decided by the CMP. Multiplication factors may be greater or less than one. The total quantity of CERs issued for a commitment period shall not exceed the aggregate quantity of emission reductions or removals achieved by CDM project activities during the commitment period.

Option 2: Specific CDM project activities shall receive CERs equal to the emission reductions that are certified by the DOE multiplied by a discount factor decided by the CMP.

40. The CMP shall adopt, and periodically review, the [multiplication factors] [discount factors] on the basis of the following criteria:

- (a) [Criteria based on environmental integrity;]
- (b) [Criteria based on the primary sectoral scope of the project activity;<sup>10</sup>]
- (c) [Criteria based on the primary technology employed in the project activity;]
- (d) [Criteria based on the global warming potential of the gases whose emissions are reduced through the project activity;]
- (e) [Criteria relating to the host Party of the project activity;]
- (f) [Criteria based on the scale of the project activity (small-scale or large-scale).]

*Note: Further issues that may need to be addressed include potential for perverse outcomes.*

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<sup>10</sup> The sectoral scope of the project activity refers to the classification used under the CDM for the sector in which the project activity is located.

## II. Joint implementation

### A. Introduce modalities for treatment of clean development mechanism project activities upon graduation of host Parties

41. Option 1: Where a Party becomes eligible to host joint implementation (JI) projects, any registered CDM project activities hosted by that Party shall continue to be subject to all rules and modalities governing CDM project activities until the end of the current crediting period of the activities and a quantity of assigned amount units (AAUs) equal to the CERs issued from the time of JI eligibility onwards shall be cancelled. The provisions relating to the treatment of CERs generated by afforestation and reforestation project activities, as contained in decision 5/CMP.1 and other related decisions, shall apply mutatis mutandis in the second commitment period.

*Note: Further issues that may need to be addressed include provisions for the cancellation of AAUs.*

Option 2: Where a Party becomes eligible to host JI projects, any registered CDM project activities hosted by that Party shall be converted to JI projects and shall be subject to provisions for JI.

*Note: Further issues that may need to be addressed include:*

- *Specific provisions for CDM afforestation and reforestation project activities*
- *The provisions relating to the crediting period*
- *Transition issues*
- *The ability to select the JI Track 1 procedure if the relevant eligibility requirements are met by the host Party*

### B. Include nuclear activities

42. Option 1: Activities relating to nuclear facilities are not eligible as JI projects.

Option 2: Activities relating to new nuclear facilities are eligible as JI projects and Annex I Parties may use emission reduction units issued for such projects, on the basis of emission reductions achieved during the second commitment period, to meet their emission commitments under Article 3, paragraph 1, for the second commitment period.

*Note: Further issues that may need to be addressed include:*

- *Specific criteria or requirements for eligible nuclear activities*
- *Costs relating to access to the technology*
- *The direct contribution to emission reductions*
- *Issues relating to non-proliferation*
- *Issues relating to permanent disposal of nuclear waste*
- *Safety, security and safeguards*

### C. Include projects that reduce greenhouse gas emissions from deforestation and forest degradation<sup>11</sup>

*Note: Projects that reduce GHG emissions from deforestation and forest degradation are not currently excluded from JI.*

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<sup>11</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

**D. Ensure environmental integrity and assess additionality through the development of positive or negative lists of project types**

43. Reductions in anthropogenic emissions by sources or enhancements of anthropogenic removals by sinks achieved by the following categories of projects are deemed to be additional to any that would occur in the absence of the projects:

- (a) [Criteria based on the primary technology employed in the project;]
- (b) [Criteria relating to the host Party of the project;]
- (c) [Criteria based on the scale of the project (small-scale or large-scale).]

*Note: Further issues that may need to be addressed include:*

- *The applicability to JI Track 1 projects*
- *The categories of projects to be included on a positive list*
- *The process for periodic review of the positive list*
- *The consequences for projects that have received a final positive determination without an additionality test if the project circumstances or the list change such that the projects are no longer covered by the positive list*

44. Reductions in anthropogenic emissions by sources or enhancements of anthropogenic removals by sinks achieved by the following categories of projects are deemed not to be additional to any that would occur in the absence of the projects, and the projects are not eligible as projects under JI:

- (a) [Criteria based on the primary technology employed in the project;]
- (b) [Criteria relating to the host Party of the project;]
- (c) [Criteria based on the scale of the project (small-scale or large-scale).]

*Note: Further issues that may need to be addressed include:*

- *The applicability to JI Track 1 projects*
- *The categories of project activities to be included on a negative list*
- *The process for periodic review of the negative list*
- *The consequences for projects that have received a final positive determination if the project circumstances or the list change such that the projects are now covered by the negative list*
- *The potential for perverse outcomes*

**E. Include co-benefits as criteria for the final determination for projects**

45. Option 1: Projects that demonstrate specific co-benefits shall be promoted through the following means: [...]

Option 2: Each project shall demonstrate specific co-benefits.

46. An accredited independent entity shall, as part of its determination regarding a project, determine [that the designated focal point of the host Party has confirmed that its stipulated co-benefits are demonstrated by the project] [that the proposed project demonstrates [any of] [all] the following co-benefits:

- (a) Technology transfer;
- (b) Environmental services such as conservation of biodiversity, management of hydrological resources and maintenance of air quality.]



*Note: Further issues that may need to be addressed include:*

- *The applicability to JI Track 1 projects*
- *The determination of the means of promoting projects*
- *The provisions for the measurement of co-benefits*
- *The definition of a sufficient level of co-benefits*
- *The potential for perverse outcomes*

### **III. Emissions trading**

#### **A. Introduce emissions trading based on sectoral targets<sup>12</sup>**

47. Sectoral emissions trading may occur in non-Annex I Parties on the basis of agreed emission targets established for sectors. The emission target for a sector shall be set below the level of projected anthropogenic emissions by sources of GHGs within the sector boundary and shall be based on the most recent available data. The sector boundary for a sectoral emissions trading scheme shall encompass all anthropogenic emissions of GHGs that are reasonably attributable to the sector in question.

48. A participating non-Annex I Party shall issue emission allowances corresponding to its sectoral target. Parties may devolve emission targets and allowances to legal entities and allow them to participate in sectoral emissions trading.

49. Once a participating Party has complied with modalities for monitoring, reporting and verification of sectoral emission levels, and accounting of emission allowances, the emission allowances may be transferred and acquired internationally and may be used by Annex I Parties to meet their emission commitments under Article 3, paragraph 1.

50. Registered CDM project activities in the sector in question may continue in parallel with the sectoral emissions trading scheme. A quantity of the emission allowances under the sectoral emissions trading scheme, issued for the host Party of the CDM project activity and equal to the CERs issued during the compliance period, shall be cancelled.

51. In relation to sectoral emissions trading, the CMP shall adopt modalities for:

- (a) The governance of sectoral emissions trading and the means of reaching agreement on sectoral targets;
- (b) The determination of a sector boundary;
- (c) The monitoring, reporting and verification of emissions within the sector boundary;
- (d) Accounting of emission allowances, including their issuance;
- (e) The treatment of potential leakage from within the sector boundary.

*Note: Further issues that may need to be addressed include:*

- *The definition of a sector*
- *The form of the emission targets*
- *The definition of the tradable unit and its use for compliance*

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<sup>12</sup> This element has been revised to reflect more accurately the proposal made by the proposing Party.

## **B. Introduce emissions trading on the basis of nationally appropriate mitigation actions**

52. CERs that are generated on the basis of a NAMA registered as a CDM project activity may be transferred and acquired under international emissions trading pursuant to Article 17.<sup>13</sup>

53. [Emission reduction units that are generated on the basis of a NAMA in an Annex I Party, under the JI Track 1 procedure, may be transferred and acquired pursuant to Article 6.]

## **C. Introduce the linking of emissions trading schemes in Annex I Parties to voluntary emissions trading schemes in non-Annex I Parties**

54. Where a national or regional emissions trading scheme implemented on a voluntary basis by a non-Annex I Party or non-Annex I Parties meets specific eligibility requirements, emission allowances [and other units] issued under the scheme may be transferred and acquired internationally, and may be used by Annex I Parties to meet their emission commitments under Article 3, paragraph 1.

55. The specific eligibility requirements shall be:

- (a) [Requirements relating to the basis for establishing emission targets;]
- (b) [Requirements relating to the monitoring, reporting and verification of emissions;]
- (c) [Requirements relating to the accounting of emission allowances;]
- (d) [Requirements relating to the avoidance of double-counting with emission reductions under the CDM.]

*Note: Further issues that may need to be addressed include the relationship to voluntary projects.*

## **IV. Cross-cutting issues**

### **A. Relax or eliminate carry-over (banking) restrictions on Kyoto units**

56. Option 1: There shall be no restrictions on the carry-over of Kyoto units to a subsequent commitment period.

Option 2: Limits on the carry-over of specific Kyoto units to a subsequent commitment period shall be as follows: [...]

*Note: Further issues that may need to be addressed include proposed limits on carry-over, by Kyoto unit type.*

### **B. Change the limit on the retirement of temporary certified emission reductions and long-term certified emission reductions<sup>14</sup>**

57. Option 1: There shall be no restrictions on the use of tCERs and ICERs by Annex I Parties to meet their emission commitments under Article 3, paragraph 1.

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<sup>13</sup> See section I.G. CERs issued on the basis of a NAMA registered as a CDM project activity would automatically be eligible for transfer and acquisition under emissions trading pursuant to Article 17.

<sup>14</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

Option 2: For the second commitment period, the total of additions to a Party's assigned amount resulting from eligible land use, land-use change and forestry project activities under Article 12 shall not exceed one per cent of base year emissions of that Party, times five.

Option 3: Limits on the use of tCERs and ICERs by Annex I Parties to meet their emission commitments under Article 3, paragraph 1, shall be as follows: [...]

*Note: Further issues that may need to be addressed include proposed limits on retirement for tCERs and ICERs.*

### **C. Introduce borrowing of assigned amount from future commitment periods**

58. An Annex I Party may borrow assigned amount from the subsequent commitment period and use it for the purpose of compliance with its emission commitment under Article 3, paragraph 1, in the current commitment period in accordance with the following provisions: [...]

*Note: Further issues that may need to be addressed include:*

- *The timing of the 'repayment' of the assigned amount*
- *Limits on borrowing*
- *The cost of borrowing, including through an 'interest rate'*
- *The consequences for non-compliance in the subsequent commitment period*
- *The implications for the environmental integrity of the Kyoto Protocol*

### **D. Extend the share of proceeds**

59. To assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation, [x] per cent of AAUs and removal units for each Annex I Party shall be set aside when such units are issued. The international transaction log shall ensure that this share is issued and transferred to the specified account of the Adaptation Fund before the remaining units may be issued. The Adaptation Fund Board shall offer these units for sale by auction by an appropriate institution authorized by the Board.

Annex II**Other possible improvements to emissions trading and the project-based mechanisms under the Kyoto Protocol**

Note: For each element contained in this annex, there exists a 'status quo' option representing the maintenance of the current approaches and rules adopted by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP).

Note: Some Parties have expressed the view that the elements in sections I.F, I.G, I.H, I.K, II.I, II.K, II.L and II.M below would require an amendment to the Kyoto Protocol and would not be within the mandate of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP). Some other Parties have expressed the view that legal analysis is needed to determine which elements in this annex would require a decision of the CMP or an amendment to the Kyoto Protocol and that such amendments would be within the mandate of the AWG-KP.

**I. Clean development mechanism**

- A. Introduce a different supervisory structure and institutional arrangement in case of modification of the scope of the clean development mechanism**
- B. Change the composition of the Executive Board membership to ensure equitable representation of Parties**
- C. Move the secretariat's function of supporting the Executive Board to another organization**
- D. Introduce alternative institutional arrangements for validation, verification and certification**
- E. Broaden the role of host Party governments**
- F. Differentiate the treatment of types of project activities by Party**
- G. Allocate proportions of demand to project activity types that contribute more to the sustainable development of host Parties**
- H. Allocate proportions of demand to specific groups of host Parties to enhance their sustainable development**
- I. Introduce alternative accounting rules for afforestation and reforestation project activities in order to increase demand<sup>1</sup>**
- J. Restrict the clean development mechanism to bilateral project activities**
- K. Use global temperature potentials instead of global warming potentials<sup>2</sup>**
- L. Include technology transfer as a criterion for the registration of project activities**
- M. Revise criteria for accreditation of designated operational entities, especially financial criteria, to enhance the accreditation of designated operational entities based in non-Annex I Parties**

<sup>1</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

<sup>2</sup> Global warming potentials are being considered by the AWG-KP under its work on greenhouse gases, sectors and source categories.

## **II. Joint implementation**

**A. Ensure that approaches for land use, land-use change and forestry projects under joint implementation are in line with the treatment of land use, land-use change and forestry under Article 3, paragraphs 3 and 4, of the Kyoto Protocol<sup>3</sup>**

**B. Introduce approaches for land use, land-use change and forestry projects under joint implementation that are parallel to the treatment of clean development mechanism afforestation and reforestation project activities<sup>4</sup>**

1. The procedures for the development of project design documents set out in appendix B of the annex to decision 5/CMP.1 shall apply mutatis mutandis to land use, land-use change and forestry project activities under joint implementation.

**C. Introduce crediting on the basis of nationally appropriate mitigation actions**

**D. Introduce a different supervisory structure and institutional arrangement in case of modification of the scope of joint implementation**

**E. Change the composition of the Joint Implementation Supervisory Committee membership to ensure equitable representation of Parties**

**F. Move the secretariat's function of supporting the Joint Implementation Supervisory Committee to another organization**

**G. Introduce alternative institutional arrangements for determination and verification**

**H. Broaden the role of host Party governments**

**I. Differentiate the eligibility of Parties through the use of indicators**

*Note: Issues that may need to be addressed include carbon accounting and related concepts, including additionality, project boundaries and land eligibility.*

**J. Improve access to joint implementation projects by certain host Parties**

**K. Differentiate the treatment of types of projects by Party**

**L. Allocate proportions of demand to project types that contribute more to the sustainable development of host Parties**

**M. Allocate proportions of demand to specific groups of host Parties to enhance their sustainable development**

**N. Restrict joint implementation to bilateral projects**

**O. Introduce multiplication factors to increase or decrease the emission reduction units issued for specific project types**

**P. Use global temperature potentials instead of global warming potentials<sup>5</sup>**

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<sup>3</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

<sup>4</sup> Discussion to be informed by outcomes from the consideration of non-permanence and other methodological issues.

<sup>5</sup> Global warming potentials are being considered by the AWG-KP under its work on greenhouse gases, sectors and source categories.

**Q. Include technology transfer as a criterion for the final determination for projects**

**III. Emissions trading**

**A. Eliminate restrictions on the trading and use of certain Kyoto unit types under national and regional emissions trading schemes**

**B. Enhance equivalence among Kyoto unit types**

**C. Reduce the commitment period reserve**

2. Each Annex I Party shall maintain, in its national registry, a commitment period reserve (CPR) which should not drop below the lower of either:

- (a) [x] per cent of the Party's assigned amount calculated pursuant to Article 3, paragraphs 7 and 8, of the Kyoto Protocol;
- (b) The sum of the reviewed inventories reported thus far in that commitment period plus the most recently reviewed inventory multiplied by the number of years remaining in that commitment period.

*Note: Further issues that may need to be addressed include the operation of the CPR during the transition between commitment periods.*

**D. Increase the commitment period reserve**

**E. Encourage disclosure of information on transactions of Kyoto units**

**F. Move the secretariat's function of maintaining and operating the international transaction log to another organization**

**IV. Cross-cutting issues**

**A. Reduce the number of unit types under the Kyoto Protocol**

**B. Introduce a mid-commitment-period assessment and review process**

3. The Parties to the Kyoto Protocol shall undertake an assessment and review of efforts made to meet quantified emission limitation and reduction commitments agreed for the second commitment period in order to assess progress and determine whether additional measures are needed, based on best available scientific assessment, to meet the ultimate objective of the Convention. This review shall be concluded no later than 31 December 2015 and shall enable a decision of the Parties specifying additional measures to be taken by Annex I Parties, which may include more stringent quantitative emission limitation and reduction commitments for adoption by the Parties.<sup>6</sup>

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<sup>6</sup> The Party proposing this provision stated that it would be relevant in the case of commitment periods longer than five years.