

## Submission on a *New Market-based Mechanism*

March 2012

### INTRODUCTION

Admitted UNFCCC observer organizations are invited to submit views, including experiences, positive and negative, on matters referred to in paragraphs 83 and 84 of the Durban decision of the AWG-LCA<sup>1</sup> which defines a *New Market-based Mechanism* (NMM), operating under the guidance and authority of the Conference of the Parties. The above mentioned NGOs welcome the opportunity to submit their views.

First we must put a potential NMM in context. The window of opportunity to prevent catastrophic climate change is rapidly closing. Several studies show that current pledges are not only woefully insufficient to keep warming below 2°C; loopholes, such as the surplus allowances (AAUs) from the first Kyoto commitment period (commonly referred to as ‘hot air’) could negate all current pledges and enable developed countries to meet mitigation targets while continuing with business-as-usual.<sup>2</sup> We are now on an emissions path that could lead to warming of 4°C or more.<sup>3</sup> In addition, impacts associated with 2°C have been revised upwards and are now considered ‘dangerous’ and ‘extremely dangerous’.<sup>4</sup> Maintaining a reasonable likelihood of limiting temperature increases to within 2°C will require commitments in the next few years to considerably higher levels of ambition by all nations.

Market-based mechanisms alone will not suffice to finance adequate emissions reduction activities. Public finance to seed mitigation activities by building capacity and governance infrastructures and by fostering mitigation policies is vital to enable sufficient private finance for global low-carbon development.

International market-based mechanisms must not compete with domestic action in developing countries. Developing countries must be able to utilize lowest cost mitigation actions towards meeting their own mitigation targets. Furthermore, the use of international credits must remain supplemental to domestic action in developed countries.

It is also important to point out that NMMs are no silver bullet and do not automatically resolve all environmental integrity issues. Although some problems, such as project-based additionality testing as

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<sup>1</sup> [http://unfccc.int/files/meetings/durban\\_nov\\_2011/decisions/application/pdf/cop17\\_lcaoutcome.pdf](http://unfccc.int/files/meetings/durban_nov_2011/decisions/application/pdf/cop17_lcaoutcome.pdf)

<sup>2</sup> UNEP (2011). Bridging the Emissions Gap. A UNEP Synthesis Report.

Kartha, S. and Erickson, P. (2011). Comparison of Annex 1 and non-Annex 1 pledges under the Cancun Agreements. *SEI Policy Brief*. Available at: <http://sei-us.org/publications/id/424>

Rogelj, Joeri, Julia Nabel, Claudine Chen, William Hare, Kathleen Markmann, Malte Meinshausen, Michiel Schaeffer, Kirsten Macey, and Niklas Höhne (2010). "Copenhagen Accord pledges are paltry." *Nature* 464, 1126-28.

Meinshausen, Malte, Nicolai Meinshausen, William Hare, Sarah C. B. Raper, Katja Frieler, Reto Knutti, David J. Frame, and Myles R. Allen (2009). "Greenhouse-gas emission targets for limiting global warming to 2°C." *Nature* 458, 1158-63. Available at: <http://dx.doi.org/10.1038/nature08017>.

<sup>3</sup> Betts R., Collins M., Hemming D., Jones C., Lowe J., Sanderson M., (2011). When could global warming reach 4°C? *Phil. Trans. R. Soc. A* 2011 vol. 369, 1934 p.67-84 doi: 10.1098/rsta.2010.0290

<sup>4</sup> Anderson K., Bows A. (2011). Beyond ‘dangerous’ climate change: emission scenarios for a new world. *Phil. Trans. R. Soc. A* 2011 vol. 369, 1934 p.20-44, doi: 10.1098/rsta.2010.0290

currently practices in the CDM would no longer apply, new mechanisms such as sectoral approaches can lead to just as many free-riders as project based mechanisms. The devil lies in the details and although the principles we elaborate on below are important, it is the decisions that are made when defining the implementation details that will determine if such a NMM will be successful in actually delivering emissions reduction on a meaningful scale.

The design of the NMM must draw upon the lessons learned and experiences from existing market based mechanisms, such as the CDM, JI and the EU-ETS.

## IMPLEMENTATION OF KEY PRINCIPLES

We believe that the following principles and the lessons that have been learned from existing market based mechanisms should guide the development of the NMM:

- Secures net atmospheric benefits
- Delivers real, measurable, verifiable and additional emissions reduction
- Avoids double-counting
- Upholds human rights
- Delivers sustainable development benefits
- Does not undermine the goals of other international environmental treaties
- Ensures complementarity

## SECURE NET ATMOSPHERIC BENEFITS

Given the mitigation imperative we are facing, a NMM must go beyond pure offsetting, as it is currently practiced in the CDM and JI. The CDM is a pure offsetting mechanism and therefore zero-sum and does not lead to emissions reduction beyond the cap. This means that non-additional credits lead to a de-facto increase in global emissions. Estimates for the number of CDM offsets that do not lead to an emissions reduction range between 0.7 to over 3 Gt by 2020.<sup>5</sup>

We welcome that the AWG-LCA text from Durban states “that various approaches .... must meet standards that achieve a net decrease and/or avoidance of greenhouse gas emissions.” Yet these goals must be further strengthened. The modalities and procedures for a NMM have to elaborate on the specifics of how such net benefits will be defined, monitored and verified (see section on MRV). Atmospheric benefits can be achieved, *inter alia* though:

- Setting crediting baselines at levels below business-as-usual
- Discounting (e.g. issuing systematically fewer credits from projects/activities with business-as-usual baselines)
- Excluding types of projects/action where net benefits are unlikely or difficult to establish
- Excluding types of projects/action that perpetuate high carbon fuel uses and high GHG emitting practices

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<sup>5</sup> See CDM Watch Policy Brief, 2011, available at <http://www.cdm-watch.org/?p=2969>

## DELIVER REAL, MEASURABLE, VERIFIABLE AS WELL AS ADDITIONAL EMISSIONS

### REDUCTION

Accounting rules must, *inter alia*, be guided by the following principles:

- **Accuracy:** GHG emissions must be measured and continuously monitored and verified to ensure they are as accurate as possible;
- **Completeness:** GHG emissions data must include all relevant sources;
- **Reliability:** Baselines must be set using verified data;
- **Conservativeness:** Baselines must be set to achieve net-atmospheric benefits. Uncertainty about the reliability, completeness or accuracy of data must be compensated with conservative baseline setting.

### AVOID DOUBLE COUNTING

In both the Cancun and Durban agreements, the necessity of avoiding double counting is mentioned but not clearly defined. In the upcoming discussion, the avoidance of double counting of both emissions reduction and financial assistance should be clearly defined.

Double-counting of international offsets could reduce the ambition of current pledges (developed and developing countries) by up to 1.6 billion tons CO<sub>2</sub>e in 2020, equivalent to roughly 10 percent of the total abatement required in 2020 to stay on a 2°C pathway.<sup>6</sup> To avoid double counting, the following is needed:

- Clear and specific rules regarding the complementary relationship between CDM, NMM and other regional trading mechanisms are needed to ensure that there is no double counting.
- A common international transaction tracking mechanism for all credits counted towards pledge attainment, with assignment of unique serial numbers to each ton transacted or registered. Such a registry should not be limited to CDM and mechanisms covered under the Framework but also include non-market based activities and NAMAs.
- Rules to ensure that offsets are only counted by the buyer and not by the seller.

Similarly, financial flows should only be counted once. Double counting of financing financial flows may reduce the total amount of financial support from developed countries to developing countries and thus reduce the emissions reduction that could occur otherwise. The financial flow related to the purchase of credits by one country cannot be counted as a financial assistance to the host country.

### UPHOLD HUMAN RIGHTS

The CDM has recently come under criticism because of human rights abuses connected with several CDM projects. There are no explicit safe-guards under the CDM to avoid credits that come from projects that violate international conventions such as the human rights declaration.

Human rights are mentioned in the chapeau of the Cancun Agreements.<sup>7</sup> A Framework must ensure that all internationally traded credits come from activities that uphold human rights.

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<sup>6</sup> See SEI Working Paper and SEI Policy Brief, 2011, available at <http://sei-us.org/publications/id/424>

<sup>7</sup> [http://unfccc.int/files/meetings/cop\\_16/application/pdf/cop16\\_lca.pdf](http://unfccc.int/files/meetings/cop_16/application/pdf/cop16_lca.pdf)

## **DELIVER SUSTAINABLE DEVELOPMENT BENEFITS**

Experience with the CDM shows that the sustainable development criteria set at the national level are usually too general and vague. For a meaningful contribution to sustainable development, international standards and guidance are needed to define sustainable development indicators and social and environmental safeguards for national authorities. In addition, associated reporting and verification standards to monitor and verify claims to ensure actual realization of the stated sustainability benefits need to be put in place.

## **DO NOT UNDERMINE THE GOALS OF OTHER INTERNATIONAL ENVIRONMENTAL TREATIES**

Under the CDM, HCFC-22 facilities can earn credits through the destruction of HFC-23, an unwanted byproduct in the production process. The exorbitant profits these CDM projects have made, has lead to gaming and perverse incentives. Such perverse incentives have delayed the fast and efficient phase out of ozone depleters under the Montreal Protocol (MP) and stifled a comprehensive solution for the destruction of HFC-23.

Explicit safeguards must be put in place under a new framework that ensures that the goals of other international environmental treaties are not undermined.

### **ADDRESSING HFC EMISSIONS**

We believe that a non-market based approach under the MP is best suited to address the increasing emissions of HFCs. HFC mitigation actions implemented under the UNFCCC should be complementary to the phase-down of HFCs under the MP.

## **ENSURE SUPPLEMENTARITY**

A NMM must not discourage developed parties from implementing domestic climate actions despite the fact that a NMM may generate a large supply of credits. The use of credits from a NMM must be supplemental to domestic mitigation actions and not dissuade parties from the significant increases in mitigation ambition that are required.

The supplementarity principle is mentioned in both Cancun and Durban agreements. However, the definition of supplementarity remains vague. We believe that a quantified limit for the use of international emissions reduction units would be the most effective way to protect the principle of supplementarity.

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