**Inputs to Structured public consultations on Draft Recommendation “Requirements for the development and assessment of mechanism methodologies”**

***{Question for additional inputs: Should the above paragraph (46/46bis) be split to improve clarity?}***

***Current version:***

46. Mechanism methodologies shall justify the appropriateness of the choice(s) made in the methodology for setting the baseline approach while taking into account guidance on the performance-based approach in the RMP and providing full flexibility to reflect local conditions and host Party circumstances (e.g. by referring to specificities of technologies/measures or sector(s) covered by the methodology such as homogeneity or variability of emission sources, data required for the parameters for a conservative and reliable estimation of the baseline, where applicable drawing from experience from typical mitigation activities that have been already implemented).

***Proposed revision (split up of the paragraph):***

46. Mechanism methodologies shall justify the appropriateness of the choice(s) made in the methodology for setting the baseline approach while taking into account guidance on the performance-based approach in the RMP and providing full flexibility to reflect local conditions and host Party circumstances.

47. The appropriateness of the choice(s) can be substantiated by referring to specificities of technologies/measures or sector(s) covered by the methodology such as homogeneity or variability of emission sources, data required for the parameters for a conservative and reliable estimation of the baseline, where applicable drawing from experience from typical mitigation activities that have been already implemented).

***Current version:***

*46 bis* Mechanism methodologies shall require justification of the appropriateness of the choice(s) made in the methodology for setting the baseline, and in particular the choice of approach, with reference to the requirements of paragraphs 33 and 35 of the RMP, as implemented in this and further guidance. Factors affecting the appropriateness of the choice shall include the homogeneity or variability of emission sources with respect to technologies and measures applied, or sectors covered by the methodology, availability of data required for the parameters for a conservative and reliable estimation of the baseline. When considering these elements methodologies shall, where applicable, draw from experience from typical mitigation activities that have been already implemented.

***Proposed revision (split up of the paragraph):***

*46 bis* Mechanism methodologies shall require justification of the appropriateness of the choice(s) made in the methodology for setting the baseline, and in particular the choice of approach, with reference to the requirements of paragraphs 33 and 35 of the RMP, as implemented in this and further guidance.

*47*  Factors affecting the appropriateness of the choice shall include the homogeneity or variability of emission sources with respect to technologies and measures applied, or sectors covered by the methodology, availability of data required for the parameters for a conservative and reliable estimation of the baseline. When considering these elements methodologies shall, where applicable, draw from experience from typical mitigation activities that have been already implemented.

***Justifications:*** The split up of the paragraph 46/ 46 bis will improve the readability and clarity of the requirements.

***{Question for additional inputs: should the downward adjustment be eligible/applicable for all the approaches to setting the baseline?}***

The most common application of a “performance-based” approach in carbon markets is a performance benchmark baseline approach, which allows the estimation of the GHG emission reductions of activity against peers by providing a reference emission level. In the case of RMP, the ambitious benchmark is set at least at the average emission level of the best performing comparable activities providing similar outputs and services in a defined scope in similar social, economic, environmental and technological circumstances. Considering that the “best performing “peer activities will be accounted for deriving the benchmark this already includes the aim of encouraging ambition over time and does not require additional [quantitative]/[qualitative] or [either quantitative or qualitative approaches] to be applied. If the reference level is set in the same and consistent way this will ensure a similar benchmark stringency level the conservativeness of the baseline will be applied across different countries and sectors.

Similarly, the “best available technologies” that represent an economically feasible and environmentally sound course of action will determine the range of technologies under consideration, and therefore the baseline level with have the required level of stringency. Taking into account that the possible interpretation is that the “best available” approach is essentially a variant of a “performance based” approach, considering the “best available technology” (BAT) or the best available process means that this approach also does not require any adjustment downwards as it already represents an approach for encouraging ambitions over time. The “Best available technology” approach also includes transformative measures for the sector to which it applies by crediting only the better performing technologies and thus will facilitate the transition of the specific sector in which it applies towards low GHG emitting technologies.

It is also very well established that the benchmark established based on the “best performing “peer activities, as well as performance reference level consistent with the “best available technologies” does not correspond to “Business as usual” scenario thus making these approaches consistent with the respective requirement of paragraph 33 of RMP.

Given the nature and specifics of the baseline setting approaches, under the RMP the only approach where the downward adjustment must be applied to encourage increased ambitions over time and consistency with a baseline which is below the “business-as-usual” scenario is the approach on existing actual or historic emissions that by default have to be adjusted downwards. Furthermore, paragraph 36 (iii) of the D3/CMA.3 clearly stipulates that only this particular approach requires downward adjustment in order to comply with the requirements of paragraph 33 of RMP.

***{Question for additional inputs: should it be specified that only activities triggered by policies can be credited? Will there be complexities in relation to additionality assessment in this regard?}***

Under CDM the consideration of domestic policies of the host country in additionality determination and baseline setting under the CDM was a very contradictory topic and called the environmental integrity of the mechanism into question.

The CDM EB adopted the so-called E+/E- rule on the consideration of policies in baseline setting for host countries: Policies that provide a comparative advantage to more emission intensive technologies (E+) were only taken into account if their adoption predated the adoption of the Kyoto Protocol in 1997. The rationale was to prevent countries from artificially inflating the baseline. Policies that provide a comparative advantage to less emission-intensive technologies (E-) were only taken into account if adopted prior to the adoption of the Marrakech Accords in 2001. The rationale behind this rule is to prevent a perverse incentive not to adopt mitigation policies.

However, when it comes to the concrete current question it could be argued that specifying that only activities triggered by policies can be credited may be unjustified because the mechanism shall incentivize all legitimate project activities that comply with the requirements of RMP even if they are outside of the scope of the formulated policies but lead to real, measurable and additional emission reductions. On the one hand, there may be instances where the eligible proposed project activities for crediting are not included in the sectors covered under the NDC of a country or the country in question has not formulated specific policies for all sectors included in the scope of its NDC and the requirement of crediting activities only triggered by policies will be penalizing such project activities. On the other hand in terms of additionality assessment the project activities may be negatively affected because along with the formulated policies countries can establish various instruments to incentivize and support the policy implementation which need to be accounted for when demonstrating additionality.

In addition to that it should be pointed out that in general setting baselines for policies is very complex as the determination of the mitigation outcomes requires comprehensive, robust, and reliable modelling. When the policy itself is to be credited, it is not required to be incorporated into the crediting baseline alongside other existing or planned policies but a model without the policy should be applied.

***{Question for additional inputs: would option 2 above fit under ‘adjustment downwards? And is it linked to additionality demonstration? How can ‘transformative’ be defined?}***

The definition of transformational change, in particular in the context of different circumstances of countries shall be elaborated by the DNA of the respective countries. As the Paris Agreement infrastructure is based on a bottom-up and Party-driven approach it should be left at every individual country’s discretion to specify what defines transformative change. Thus, the ultimate responsibility to decide whether an activity is eligible under a methodology and compliant with the transformative change requirement shall be of each individual host country. The host country should identify in its NDC implementation plan the project activities which are eligible for crediting and conformable with transformative change requirement making them eligible for carbon crediting. Typically, project activities that can transform a sector in a country are associated with large marginal abatement costs and require carbon market support, thus their additionality can be easily demonstrated. Furthermore, the “transformative” project activities/technologies/measures can be defined by the country in top-down developed positive lists which should be publicly available in order to give predictability to project developers and to make the mechanism attractive for market players.

The baseline approaches which are formulated as benchmark established on the basis of the “best performing “peer activities, as well as performance reference levels consistent with the “best available technologies” have the potential to safeguard the host countries’ NDC achievement while potentially contributing to ambition raising through incentivizing transformational activities beyond those planned under the host countries’ commitment. The level of stringency chosen for these approaches should achieve a balance of cost-effectiveness and long-term incentives for transformation.

***{Question for additional inputs: how does this issue link to policy crediting where policies deliberately intended to generate credits? What considerations are needed in this regard?}***

The Article 6 rulebook - in particular the rules, modalities, and procedures (RMP) of the Article 6.4 mechanism formulates new principles and requirements for the demonstration and assessment of additionality.

*Paragraph 38 of RMP requires additionality to be demonstrated using a* ***robust assessment*** *that shows the activity* ***would not have occurred in the absence of the incentives from the mechanism****, taking into account all* ***relevant national policies, including legislation****, and* ***representing mitigation that exceeds any mitigation that is required by law or regulation****, and taking a* ***conservative approach*** *that* ***avoids locking in levels of emissions, technologies or carbon-intensive practices*** *incompatible with* ***paragraph 33****.*

This necessitates having mandatory legal test for additionality along with taking into account the relevant national policies. Considering that most Parties[[1]](#footnote-1) (81 per cent) provided information on voluntary cooperation under Article 6 of the Paris Agreement. Almost all of them (76 per cent) stated that they plan to or will possibly use at least one type of voluntary cooperation, with the use of cooperative approaches most frequently communicated. At the same time, some Parties (30 per cent) have set qualitative limits on their use of voluntary cooperation for achieving their mitigation targets, such as using units that adhere to certain standards and guidelines to ensure, for example, additionality, permanence or avoidance of double counting of emission reductions, the policies that will represent policy crediting will be very much subject to discussion.

The policies that deliberately intend to generate credits need to be taken into consideration in a modified way mimicking the approach and complying with the rationale of E+/E- policies under the CDM e.g. policies that provide a comparative advantage to crediting were only taken into account if their adoption predated the adoption of the Paris agreement, whereas policies that are adopted to in order to achieve compliance with the Paris Agreement and under the NDC may be disregarded as they are align with the architecture of the Paris Agreement.

***{Question for additional inputs: should there be a statement about the general additionality test before specifying how it may be simplified in certain cases, or be subject of a positive list? Could be a more nuanced approach, i.e. all projects need to demonstrate additionality, some can be excluded or included based on one sort of assessment while others require more detailed assessment: (a) What are the general rules? (b) Where may they be simplified, or deemed to have been satisfied?}***

The additionality assessment shall take into account the risks to additionality relevant to the general activity type and to the specific project conditions. In general a stepwise approach to assess and demonstrate the additionality of projects and programs of activities in order to robustly determine additionality under Article 6 is required where the first step is the mandatory legal additionality test.

Automatic financial additionality through positive lists still has a role to play when it comes to specific country circumstances. Thus, for specific technologies national and international positive lists for financial additionality that are updated regularly are required to incentivize crediting mechanisms in the respective countries.

For project types where risks to additionality are high the detailed financial analysis and respective evidence-based approach have to be applied on case-by-case basis.

Positive lists need to be justified in relation to all or specific aspects e.g., financial additionality and regulatory additionality and must meet minimum predefined criteria. The process for developing global and national positive lists should include transparently presented and robustly justified argumentation.

In the development of positive lists for financial additionality, the following may be applied that needs to be regularly reviewed and updated:

**For global positive lists:** In case a project type/category can demonstrate that their net present value of costs exceeds revenues and savings without carbon finance more than certain established default threshold the same can be considered qualifying to be included in the global positive list.

**For regional/country-specific positive lists:** In case a project type/category can demonstrate in a national context that either their costs significantly exceed revenues and savings so that their IRR is negative under conservative assumptions regarding the discount rate, or their levelized costs of delivering a product or service are more than certain threshold which is higher than the industry average, or their marginal abatement cost exceeds a country specific benchmark they may be eligible to qualify for inclusion in the regional/country-specific positive list.

Also, well-established thresholds for technology penetration rate can be applied for deriving positive lists.

***{Question for additional inputs: are positive lists needed? If yes, is the above guidance on positive lists too specific and detailed, and may the guidance be shortened?}***

Positive lists are very much needed for incentivizing project crediting.

The provided guidance for developing positive lists shall be detailed and specific so that consistency and an equal playing level field is ensured across the board. The detailed elaboration of the requirements on the deriving positive list is very much needed in order to have transparency and trust in the process.

Please also kindly consider the response provided above with respect to positive lists.

***{Question for additional inputs: should pre-project activity emissions and upstream emissions be accounted as activity emissions or leakage emissions, or be identified by the Supervisory Body as being beyond the scope of activity accounting guidance? What further assessment is needed in this regard?}***

The way to address comprehensively all net changes of anthropogenic emissions by sources of GHGs that occur outside the project boundary but are measurable and attributable to the project activity directly corresponds to the ultimate goal of maintaining environmental integrity of the mechanism. However, having a full pledged life-cycle approach towards all associated upstream and downstream emissions may be difficult to justify in terms of their contribution to actual significant GHGs sources associated with the project activity. The “net” approach may be explored as the accounting for pre-project activity emissions may easily cancel out with upstream and downstream project emissions and furthermore many of these emissions sources may be insignificant. Thus, the efforts and the burden of data collection for negligible upstream and downstream emission sources may cause undue difficulties to project participants. Leakage must be estimated based on a comparison to the baseline scenario for the project activity causing the leakage and applied to the sources/sinks affected.

1. Source: https://unfccc.int/ndc-synthesis-report-2022#Targets [↑](#footnote-ref-1)