

**COMMENTS ON ARTICLE 6 OF THE PARIS AGREEMENT
FOR COP 23 BONN**

The American Carbon Registry (ACR) is pleased to offer input for development of Article 6 provisions of the Paris Agreement. As the first non-governmental greenhouse gas registry in the world, ACR has twenty years of experience in the development of rigorous, science-based carbon offset standards and methodologies, as well as operational experience in project registration, verification oversight, and credit issuance. ACR is a pioneer in harnessing the power of markets to realize emissions reductions without burdening the economy. ACR's parent organization, Winrock International, is named for philanthropist Winthrop Rockefeller and is a nonprofit organization that works around the world to empower the disadvantaged, increase economic opportunity, and sustain natural resources.

Article 6.2

Parties shall, where engaging on a voluntary basis in cooperative approaches that involve the use of internationally transferred mitigation outcomes towards nationally determined contributions, promote sustainable development and ensure environmental integrity and transparency, including in governance, and shall apply robust accounting to ensure, inter alia, the avoidance of double counting, consistent with guidance adopted by the Conference of the Parties serving as the meeting of the Parties to this Agreement.

- Operationalization, scope, and definition of “internationally transferred mitigation outcomes” (ITMOs)

ACR encourages adoption of a broad definition of ITMOs that allows Parties the flexibility to create innovative collaborations for GHG mitigation. Any definition that unduly constrains the ability to devise and implement new forms of cooperation presupposes that we already possess full knowledge of the most effective modalities. Furthermore, by allowing for differentiation, approaches can be optimized for local conditions.

Any definition of ITMOs must accommodate transferable units that represent greenhouse gas reductions. Maximizing climate benefit with limited financial resources demands efficient allocation of capital to lowest-cost GHG reduction opportunities. Transferable instruments, of the type created by carbon offset standards, exemplify how flexibility and adaptability empower economic efficiency for effective climate action.

With specific regard to the ITMOs that involve transferable units, operationalization should allow for at least the following three modalities:

- 1) Linkage of emissions trading systems. Subject to mutually agreed quality criteria for GHG reduction credits, Parties must be allowed the efficiency in GHG mitigation that combined markets can achieve. By encompassing a wider range of emissions reduction opportunities, while also creating a larger pool of financial resources, linked markets support greater ambition.

- 2) Use of voluntary carbon offset standards. Parties should have the flexibility to avail of the array of emissions reduction methodologies and the crediting infrastructure offered by voluntary standards. Subject to quality criteria for credits and security requirements for registries, Parties should not be restricted in their opportunities and ability to tackle GHG emissions. Voluntary standards accordingly support ambitious climate action.
- 3) Use of the Article 6.4 crediting mechanism. Bilateral or multilateral cooperation should be able to leverage the crediting infrastructure of Article 6.4. Although the spirit of Article 6.2 is that Parties should be free to address climate change in ways well outside of Article 6.4, the crediting mechanism of Article 6.4 may be incorporable in initiatives created under Article 6.2.

- Article 6.2 accounting and corresponding adjustments

To account for GHG reductions necessitates their quantification, and a common accounting system is facilitated by uniform units of measure. As such, all ITMOs should be denominated in tons of CO₂e.

Global carbon accounting of high integrity fosters the trust requisite for international cooperation, the ability to track progress, and our understanding of the climate challenge itself. Therefore, all ITMOs should be subject to a corresponding accounting adjustment by the host country to avoid double counting. Whether the adjustment should be an addition to the Party's emissions inventory (offsetting a subtraction due to the mitigation action) or a more aggressive NDC is a question to be resolved. It may depend on the quality of the inventory or the type of NDC. For example, for those Parties with a NDC based on a set of actions, rather than a numerical GHG target, the appropriate adjustment may be to commit to more ambitious actions, to an extent equivalent to the ITMO.

A weakness of NDCs that specify emissions levels to be achieved in a single year is that emissions levels in the target year may be aberrantly low. Emissions in years immediately before and after the target year could be much higher. Single-year NDCs need to be converted to multi-year NDCs, or accounting for ITMOs should address the shortcoming. For host and recipient countries with target-year NDCs, one approach would be to require accounting adjustments be amortized across the NDC periods. The adjustments could be to emissions inventories or NDCs, as discussed previously. With such amortization, a host country could not allocate emissions increases only to non-target years, and a recipient country could not allocate the reductions to a single target year.

Sub-national ETS linkages across national boundaries (e.g. California and Quebec) should be accounted for as ITMOs. Transfers of allowances and offsets should be adjusted in national inventories or NDCs. Note that, in principle, "hot air" allowances sold by a sub-national jurisdiction do not present a problem for national accounting. The national government of the sub-national jurisdiction selling excess allowances would simply face a greater challenge in meeting its NDC. In practicality, the scenario could present a significant challenge, particularly when one considers California's recently passed Assembly Bill 398. The legislation directs the creation of unlimited allowances at predetermined price caps. If Canadian jurisdictions are net buyers, Canada's NDC would be easier to achieve and the U.S.'s more difficult. Accounting rules could be established so that allowances issued in excess of emissions caps do not distort national inventories or NDCs, although this falls within the domain of national and subnational governments.

- Governance and oversight

A centralized accounting function should be established within the UN. This entity would ensure consistent application of the accounting rules. In addition, circumstances that present unique challenges of interpretation could be deliberated in the context of all ITMO accounting, with decisions then applied uniformly to similar situations that may arise thereafter.

The integrity of ITMOs and the credibility of voluntary standards must be ensured. Voluntary standards and their credits should be accepted only in accordance with quality criteria. Further, registries should be subject to security requirements to guard against fraud. Guidance on quality and security criteria would aid the establishment of ITMOs, while enhancing their consistency and comparability.

All ITMOs, credit-based or otherwise, should be strengthened with third-party verification. The integrity of emissions reduction claims should not be left in doubt. Existing verification systems may be applicable, such as those associated with the Article 6.4 mechanism, voluntary offset standards, and sustainability certifications. However, innovation under Article 6.2 may often result in ITMOs that do not fit neatly into existing structures. In these cases, verification programs will need to be tailored. Guidance should be established to facilitate the development and implementation of third-party verification systems.

Despite the mitigation potential of ITMOs, they present risks. Much like the “hot air” Assigned Amount Units transferred between countries under the Kyoto Protocol, ITMOs could be based on emissions reduction claims associated with macroeconomic changes or faulty baselines. Worse still, unlimited ITMOs could create perverse incentives that thwart the very climate progress ITMOs are meant to foster. For example, Parties may commit to less aggressive NDCs in order to realize revenue from the sale of emissions reductions under ITMOs. In this way, ITMOs could actually result in decreased ambition to address climate change. A possible solution for consideration is to limit emissions reductions, as a proportion of the host country’s emissions inventory, that can be exported under ITMOs. Other approaches may be necessary for Parties lacking robust emissions data.

Article 6.4

A mechanism to contribute to the mitigation of greenhouse gas emissions and support sustainable development is hereby established under the authority and guidance of the Conference of the Parties serving as the meeting of the Parties to this Agreement for use by Parties on a voluntary basis. It shall be supervised by a body designated by the Conference of the Parties serving as the meeting of the Parties to this Agreement, and shall aim:

- (a) To promote the mitigation of greenhouse gas emissions while fostering sustainable development;*
- (b) To incentivize and facilitate participation in the mitigation of greenhouse gas emissions by public and private entities authorized by a Party;*
- (c) To contribute to the reduction of emission levels in the host Party, which will benefit from mitigation activities resulting in emission reductions that can also be used by another Party to fulfil its nationally determined contribution; and*
- (d) To deliver an overall mitigation in global emissions.*

- Operationalization, scope, and definition for the mechanism under Article 6.4

An Emissions Mitigation Mechanism (EMM) should be built on the experience of CDM/JI, though designed for the very different Paris Agreement. The EMM will need to be adapted to a world in which all Parties are committing to GHG reductions, leaving no uncapped geographies. The fundamental success of CDM/JI – its demonstration of the power of markets to address climate change – should continue. The EMM should result in a system for trading emissions reductions in order to steer capital to least-cost GHG reductions.

One weakness of CDM/JI was the bottleneck that resulted from burdening the UN Executive Board with all methodology development, project review and credit issuance. The EMM should resolve this problem by adopting an open architecture approach such as ICAO's CORSIA, allowing voluntary offset standards a parallel role. Subject to quality criteria, the EMM should enable approval of voluntary standards and credits. Registries would be required to adhere to high security standards. Issuances of credits by voluntary programs would have to be reported to the EMM for purposes of accounting. Competition among voluntary standards would spur efficiency since project developers would have choices.

- Units, credits

Credits issued by voluntary standards should be held to the same stringent quality criteria as those issued directly by the EMM. Uniform quality criteria underpin the fungibility of credits and the comparability of NDCs.

- Activities

Article 6.4 explicitly links greenhouse gas mitigation with sustainable development. The widely varying circumstances of Parties necessitate that each Party independently determine its own sustainable development priorities. However, the Sustainable Development Goals (SDGs) should serve as a common framework. By following the SDGs, Parties can more efficiently identify priority actions, and developers of GHG reduction projects will have a level of clarity on the sustainability co-benefits that must occur. Third-party verification and certification are encouraged but may be subject to host country requirements.

- Accounting

As for ITMOs under Article 6.2, measures to avoid double claiming of emissions reductions are important for the EMM. All GHG reductions under the EMM must trigger reporting and an accounting adjustment by the host country. In correspondence to the EMM credits, the emissions inventory may be increased (offsetting a decrease in actual emissions) or the NDC made more ambitious. Which approach is preferable is open for consideration and may depend on whether the host country has a quantified and robust emissions inventory.

As was highlighted in comments on Article 6.2, NDCs that specify emissions levels in target years may not result in real climate progress in other years. Attributing EMM credits to target-year emissions levels could allow success in achieving the NDC that is inconsistent with a Party's general emissions trend. Conversion of single-year NDCs to multi-year NDCs or development of accounting rules for EMM credits should attempt to close this loophole. For host and recipient countries with single-year NDCs, accounting adjustments (to emissions inventories or NDCs) could be amortized across the NDC periods. This would preclude a host

country from allocating emissions increases only to non-target years, and a recipient country would not be able to allocate reductions only to target years.

- Participation by public and private entities, as authorized by Parties

Incorporating voluntary standards into the EMM further enfranchises public and private entities. A wider range of available project methodologies translates into more mitigation opportunities. The credit-issuance efficiency resulting from competition among voluntary standards should engender a marketplace that attracts capital and interests private and public actors.

Parties should be encouraged to unlock private sector demand for EMM credits by allowing entities covered by domestic schemes to use EMM credits for compliance. This would be akin to the EU-ETS allowing covered entities to use CDM/JI credits.

- Lessons learned from existing mechanisms, and the future of the existing mechanisms

The offsets market created by the Kyoto Protocol demonstrated that tradeable credits facilitate uniform carbon pricing. In so doing, market distortions are reduced. Similarly, an EMM can limit the degree to which carbon pricing impacts the economic competitiveness of Parties.

The bureaucratic nature of CDM/JI meant that issuance of credits took longer than expected and that project developers lacked sufficient clarity on the amount of time that would be required. Long lead times and uncertainty discouraged mobilization of capital. If EMM allows for voluntary offset standards, competition among the standards to attract projects should lead to greater efficiency.

Certain CDM/JI infrastructure can likely be adapted to a new EMM. For example, a need to ensure accurate recording of credit holdings will still exist. In this way, the International Transaction Log (ITL) should continue to be of value.

- Governance and oversight

The centralized accounting function recommended in reference to Article 6.2 should also be instituted with respect to Article 6.4. This entity would ensure consistent application of the accounting rules. A critical responsibility would be managing the adjustments to emissions inventories or NDCs necessitated by credit transfers as reported in an ITL.

The integrity of the EMM must be ensured, which includes, among other aspects, establishing a standard for project eligibility and quality criteria for credits. While voluntary standards should be accepted, for reasons stated herein, it is imperative they be held to the same benchmarks. In addition, security protocols are needed to protect registries from fraudulent activity.

With the opportunity to sell emissions reductions comes risks, as highlighted in comments on Article 6.2. The ability to generate revenue from EMM credits creates the perverse incentive for each party to commit to less ambitious NDCs; why not get paid for the emissions reductions, instead? Collectively, less ambitious NDCs would result in all Parties worse off insofar as we fail to limit the planet's warming. Therefore, a limit on EMM credits that can be exported, as a proportion of the host country's emissions inventory, should be considered. Other approaches may be necessary for Parties lacking robust emissions data. In such cases, an EMM export limit relative to a proxy for aggregate emissions, such as gross domestic product, could be considered.