BUILDING IN A TRANSITION

DAVID HONE AND JONATHAN GRANT OUTLINE IETA'S STRAW PROPOSAL FOR ARTICLE 6 OF THE PARIS AGREEMENT – AND SET OUT WHY A TRANSITIONAL PERIOD FROM CURRENT MARKET SYSTEMS TO THE NEW IS IMPORTANT

In the many months prior to COP21 in Paris, IETA and others campaigned for the inclusion of market provisions within the Paris Agreement. It was never imagined that the new agreement would establish a trading market in the way the Kyoto Protocol did. But some structure was essential to lay the foundation for market development by allowing links between national and regional systems and creating market mechanisms. This would bring a degree of homogeneity and price alignment between otherwise disparate and independently designed systems. The case for linkage was initially put forward through collaboration between IETA and the Harvard Kennedy School in Massachusetts[1].

The Article 6 outcome only happened thanks to many months of advocacy and legwork. IETA and its members were the ones who picked up on this issue, releasing a straw proposal for the Paris Agreement during the 2014 New York Climate Summit. IETA imagined a relatively short Paris Agreement that devoted just a few paragraphs to each key subject. In reality, this was very close to the mark. It was also clear that a focussed proposal on carbon pricing or international emissions trading would not make the cut, so a more tangential approach would be needed to include these key concepts in the final text. The proposal didn't mention carbon pricing or emissions trading; instead it offered a provision for transfer of obligation between respective Nationally Determined Contributions (NDCs), in combination with rigorous accounting to ensure the integrity of the transfer.

. . . may transfer portions of its defined national contribution to one or more other Parties …

In addition, the proposal suggested a broader mechanism for project activity and REDD+. Article 6 of the Paris Agreement now provides the opportunity for internationally transferred mitigation outcomes (ITMOs) and a mechanism to contribute to the mitigation of greenhouse gas (GHG) emissions and supporting sustainable development.

Of course, like every other part of the Paris Agreement, this is just the beginning of the task ahead. The story of the Clean Development Mechanism (CDM) was similar: it was defined in the 1997 Kyoto Protocol, but it was not until COP7 in Marrakech in 2001 that the high level rules for the mechanism were agreed. Even then, the CDM required further revisions over the ensuing years as detailed methods for baselines and additionality were developed. The division between countries with and without targets in the Protocol had significant implications for the design of the CDM. Complex rules are needed to ensure the integrity of the creation and transfer of new units from a country without targets to one with them. With the Paris Agreement, all countries have agreed to the global goal of net zero emissions in the second half of the century. In the long term, this should make the rules for the mechanism much simpler – and as all emissions will need to be covered by the system, there will be no need to worry about additionality or leakage.

The challenge is in making that transition from patchy action, like that seen under the Kyoto Protocol, to a system of high environmental ambition and integrity supporting gigaton-scale transfers. Negotiators are currently discussing the rules for Article 6 and appear more focused on the short to medium term implications for existing mechanisms rather than taking a longer-term view.

(1) Facilitating Linkage of Heterogeneous Regional, National, and Sub-National Climate Policies Through a Future International Agreement. Harvard Project on Climate Agreements, November 2014 (2) See www.ieta.org/Article-6-Submissions-Portal

The IETA team and the companies behind the organisation are justifiably proud of their contribution to the Paris Agreement, recognising of course the immense amount of effort put into delivering Article 6 by so many others, including the dedicated market negotiators who worked long hours throughout COP21.

Now we come to COP23 this year and COP24 in 2018, where the detail behind Article 6 needs to be delivered. Once again, IETA has entered this process by developing a new straw proposal. This continues the work that IETA has done for over a decade to support market development in the UN process. At the first UN climate meeting post Paris in May 2016, IETA was first out of the blocks on Article 6, presenting a thought piece on its long-term structure. The emphasis was on accounting, scalability and environmental effectiveness. IETA developed this further in the lead up to COP22 focusing on the critical issue of the role of accounting in ensuring integrity of transfers between countries. Robust treatment of transfers and the development of mechanisms that result in demand for its units requires increasing levels of quantification of NDCs.

Quantifying NDCs such that they are ready to release and/or receive carbon units brings a new challenge to Parties, but particularly those who have benefitted from the CDM. The buyers or users of CDM credits were part of systems that had full accounting and inventory procedures up and running. But the CDM projects themselves were typically stand alone, with GHG accounting related only to the project, rather than to the broader economy. As such, detailed additionality procedures had to be developed to give confidence to the buyers that the units being purchased represented real reductions within the broader originating economy.

Assessing additionality under the CDM was a largely subjective, evidence-based process, which in turn slowed the turnaround of projects and increased the cost of verification. That process was fine to kick-start emissions trading under the Kyoto Protocol, but it isn't suited to the Paris Agreement. Scale, speed of turnaround, and numerical clarity rather than subjective assessment are required to deliver the substantial emissions reduction required. In light of this, the IETA straw proposal on the rules for Article 6 has built in suitable accounting proposals.

The full Article 6 straw proposal was released in time for the May 2017 UN climate meeting in Bonn. That proposal can now be found on the recently created IETA Article 6 Portal[2]. It represents an end-point for the shape of Article 6, which is a major step from where the international carbon market stands today.

But there is further work to do.

At the opening of the 2017 IETA Carbon Forum North America in New York, the Fijian Climate Ambassador gave a major push forward for Article 6. She stated to the attentive audience that it was perhaps the most important part of the Paris Agreement. Her assertion rested on the argument that a functioning global carbon market can enhance ambition. Looking some decades down the road, trade in carbon units can give confidence to nations to set net-zero emission goals, given that they will feel assured that the balance that needs to be reached against remaining emissions in their economy can be achieved by purchasing suitable units from a recognised international market. Without such a market, net-zero emissions is unlikely to be realised.

While the full need for such a mature global market may be many years away, the negotiators faced with the task of developing suitable guidelines, rules and procedures for Article 6 must still consider that end-point now as well as the transition period to get there. Although it is always possible to return to the table and build on existing systems, the history of this within the climate negotiations is not good.

But most negotiators are focussed on the near term and the role that carbon markets might play over the next five to 10 years. Many have seen the CDM bring much needed energy investment into their countries and some are keen for such projects to continue, rather than wait for a new round of activity to get going under a new mechanism; that could take some years. But as the earlier IETA thought pieces noted, the Paris Agreement will also bring fundamental changes to the accounting around these projects, given the existence of NDCs. That could also take some time to fully develop.

All the above points to a transitional arrangement; an approach which allows the structure, project pipeline and methodologies of the CDM to continue, but which sees the CDM subsumed into the new Article 6.4 mechanism as it emerges. Retaining aspects of the CDM and encouraging smaller emissions mitigation projects in least-developed economies and sub-national regions should be part of the new mechanism, but equally this mustn't end up as the mechanism itself.

Article 6, including the transfer arrangements of 6.2, the mechanism of 6.4 and the non-market approaches of 6.8, must herald in trade and cooperative arrangements that operate on the gigaton scale, not kilotons and megatons as has been the case with the CDM. The mitigation challenge ahead is enormous and the potential trade even in a net-zero emissions world could be very large. Continued emissions from agricultural systems, chemical processes, smelters, aviation and shipping alone would require several gigatons of trade to offset with units representing removed carbon dioxide (ie, sinks).

This points to a relatively short transition period, perhaps one or two of the five-year cycles for Nationally Determined Contribution (NDC) implementation and review. After that, if the Paris Agreement goals are to be met, NDCs should have expanded to cover all parts of every economy, therefore introducing the full accounting rules on which Paris is based. While project activity such as under the CDM will doubtless continue, it will need to be transparently accounted for within the NDC process. This in turn will change the nature of the trading arrangements for the reduction units coming from the projects.

IETA plans to be there for this journey and help develop the map by bringing the experience of its members into the negotiations through its straw proposal, thought pieces and side events.

The task for the negotiators in Bonn will be to find a balance between the shorter term needs of several Parties and the project investment pipeline that is important to their energy development, along with the creation of a new emissions mitigation mechanism and accompanying transfer provisions that are scalable and robust for the decades ahead. Transitional arrangements could be an important part of the solution.

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