

# COMPLETING THE PARIS ‘RULEBOOK’: KEY ARTICLE 6 ISSUES



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The major piece of unfinished business in the Paris “rulebook” adopted at the U.N. Climate Change Conference in Katowice, Poland, was a set of detailed guidance for implementing Article 6 of the Paris Agreement. This includes guidance under Article 6.2 for Parties using internationally transferred mitigation outcomes (ITMOs), and rules, modalities and procedures governing the Article 6.4 mechanism.

This paper provides background on the Article 6 issues and discussions; presents a hypothetical transfer to help illustrate issues pertaining to double counting; and reviews four key outstanding issues and options for addressing them:

- Transferred emission reductions arising from outside the scope of a nationally determined contribution (NDC)
- Emission reductions used for non-NDC purposes
- The relationship of Article 6.4 to Article 6.2 accounting
- The dedication of a share of proceeds resulting from Article 6 transfers to support adaptation in developing countries

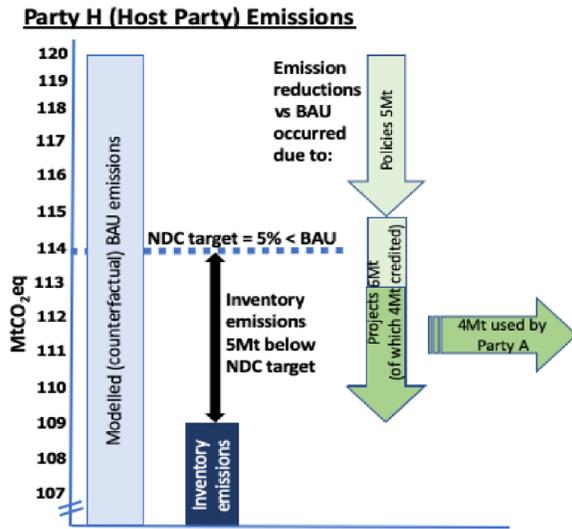
## BACKGROUND

Article 6 of the Paris Agreement recognizes that parties may cooperate voluntarily in implementation of their NDCs, to allow for higher ambition and to promote sustainable development and environmental integrity. Around half the NDCs make reference to use of cooperative approaches or international markets,<sup>1</sup> so Article 6 has the potential to be widely applied. Some parties intend to use international carbon markets to help achieve their NDC mitigation target, having communicated a target that reflects a sum of domestic and cooperative efforts. Other parties envision cooperative approaches as a means to generate mitigation and adaptation ambition beyond the level communicated in NDCs. There is a desire from a broad range of parties, with differing NDC types and national capacities, to be able to participate in Article 6 cooperation. At the same time, ensuring high environmental integrity and avoiding any loopholes in

the rules that undermine trust are also paramount to many parties.

Article 6 sets the framework for this action: Articles 6.2 and 6.3 set principles for voluntary use of ITMOs towards NDCs, Articles 6.4, 6.5 and 6.6 outline a new centrally-governed market mechanism, and Articles 6.8 and 6.9 provide for a framework for non-market approaches. The agreement and accompanying decisions stress the importance of avoiding double counting or double use in relation to accounting for NDCs (Article 4.13, 6.2, and 6.5 with reference to 6.4(c), and accompanying 1/CP.21 paragraphs 36, 92(f), and 107). The Paris decision called on the Subsidiary Body for Scientific and Technological Advice (SBSTA) to develop and recommend guidance for Article 6.2, rules, modalities and procedures for the Article 6.4 mechanism, and a work program for the Article 6.8 framework, all for adoption at the first session of the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement (CMA 1).

**FIGURE 1: Example of Double Counting**



Significant progress was made at COP 24/CMA 1 in Katowice, with negotiations moving from multiple conceptual options to comprehensive text with a small number of remaining brackets. Convergence was seen in many areas, including in relation to governance, recording of transfers, accounting approaches, and the work program for the Article 6.8 framework. Areas where more detailed technical work programs are needed were also identified, such as the mechanics of corresponding adjustment for non-CO<sub>2</sub> and single/multi-year targets, and the details of recording databases. However, a small number of key political and technical issues remained unresolved. As a result, no substantive decisions on Article 6 were adopted and SBSTA was requested to continue its work, taking into account draft SBSTA and Presidency decision texts,<sup>2</sup> with a view to reporting to CMA 2.

Other CMA decisions taken at CMA 1 are relevant to Article 6. First, the overall guidance for NDC accounting (4/CMA.1) was agreed: Parties will account for NDC implementation and achievement in their biennial transparency reports, will provide information on methodologies used, and where possible, will account in accordance with methodologies and common metrics assessed by the IPCC and in accordance with decision 18/CMA.1. The decision provides more clarity on

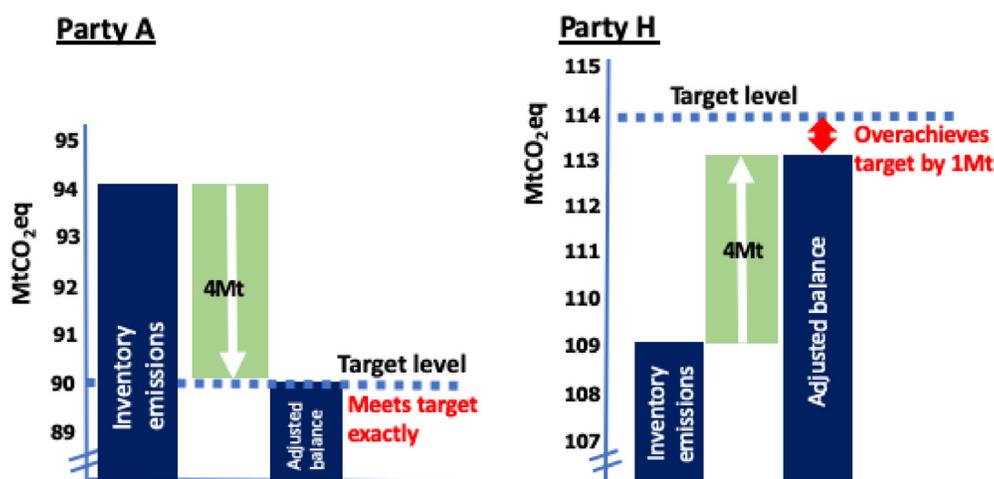
consistency of baselines, and reiterates Paris Agreement language that parties shall “promote environmental integrity, transparency, accuracy, completeness, comparability and consistency, and ensure the avoidance of double counting” in accounting for their NDCs.

A related decision on transparency (18/CMA.1 paragraph 77(d)) provides general guidance to parties participating in cooperative approaches that involve use of ITMOs toward an NDC<sup>3</sup>, or that authorize the use of mitigation outcomes for international mitigation purposes other than achievement of their NDC. This paragraph requires reporting of annual emissions covered by the NDC, an adjusted balance reflecting transfers of ITMOs, and information on how cooperative approaches promote sustainable development, ensure environmental integrity and transparency, and apply robust accounting including the avoidance of double counting.<sup>4</sup>

Major remaining issues not addressed in this paper include issues related to the transition of the Clean Development Mechanism (CDM) (e.g., whether CDM methodologies, projects and units should be transitioned from the Kyoto Protocol for use in the Article 6.4 mechanism); technical issues in Article 6.2 accounting (e.g., the “trigger” for applying a corresponding adjustment to avoid double counting, and the mechanics of corresponding adjustment for single and multi-year targets); and technical issues regarding accounting for any trade quantified in terms of metrics other than tons of carbon dioxide equivalent (tCO<sub>2</sub>-eq).

## DOUBLE COUNTING: AN ILLUSTRATIVE EXAMPLE

To inform the discussion of accounting-related elements of Article 6, **Figure 1** presents a simple example of accounting for transfers arising from a crediting system. In this example, Party H (the “host” party) has an NDC target for emissions to be 5 percent below business as usual (BAU). It implements national policies that result in emission reductions of 5 million tons (Mt) compared to BAU. It also hosts projects that reduce its inventory emissions by 6Mt (compared to counterfactual levels in the absence of the projects). A conservative baseline is used for crediting, so only 4Mt of this reduction is

**FIGURE 2: An Approach to Avoid Double Counting**

credited. The 4Mt of credits are used by another party, Party A (the “acquiring” Party), toward its NDC.

This example could represent projects in a bilateral crediting arrangement between Party H and Party A under Article 6.2, or projects hosted and authorized by Party H under the central Article 6.4 mechanism. The difference between these cases is that credits would most likely be issued directly by the host party in the first case, but would be issued by a central registry in the second.

In either case, Party H has lower inventory emissions than would be the case if the projects had not taken place. If Party H were to account for its NDC achievement only in terms of its inventory emissions (giving the result that its inventory emissions are 5Mt below the target level), it would be benefiting from the same 4Mt in emission reductions that Party A also counts toward its NDC, i.e. double counting or double use could arise.

**Figure 2** shows an approach to avoiding this double counting or double use, whereby a corresponding adjustment is made by Party A and Party H. After the corresponding adjustment for the 4Mt, Party H still overachieves its NDC target, but by 1Mt rather than 5Mt.

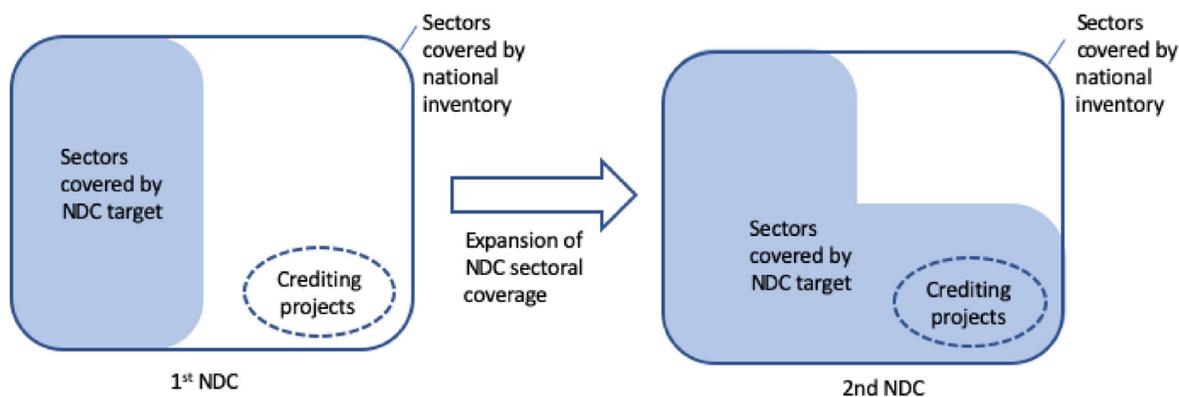
## TRANSFERS FROM OUTSIDE THE SCOPE OF AN NDC TARGET

NDCs reflect a major broadening of the sectoral coverage of mitigation goals compared to the pre-2020 period, with the majority of parties presenting economy-wide

absolute, BAU, intensity or peaking year greenhouse gas targets in their NDCs. Nonetheless, many NDC targets cover a smaller set of sectors and/or gases than the parties’ National Greenhouse Gas Inventories, in which case the NDC targets are not fully economy-wide.<sup>5</sup> The UNFCCC’s summary of NDCs finds that while nearly all NDCs address the energy sector, only around three quarters cover transport, waste, and LULUCF (land use, land use change, and forestry). Similarly, it finds that nearly all NDCs address carbon dioxide emissions, but a number do not encompass methane, nitrous oxide and the other gases.<sup>6</sup> In some cases, parties may have left sectors or gases out of their NDC where they have poor information, and they may wish to use the opportunity of hosting projects to build capacity in these sectors. It is therefore possible that transferred emission reductions could originate from sectors or gases not included in a host party’s NDC mitigation target but covered by its national inventory.<sup>7</sup>

From a technical standpoint, avoiding double counting or double use in the case of transferred emission reductions arising from outside the NDC target sectors or gases is simple, because the emission reduction is only contributing to achievement of the acquiring party’s NDC mitigation target and not the host’s NDC target. As such, one option for addressing such transfers is that no corresponding adjustment of the type shown in Figure 2 would be required for the host party.

However, this approach could create an incentive for the host to not expand the coverage of its NDC in

**FIGURE 3: Incentive for Host Party to Not Expand Coverage of its NDC in Future Periods**

future periods (**Figure 3**). As long as the project remains outside the NDC, the inventory emissions in that sector (outside the NDC) would be reduced. If the NDC coverage was expanded, the need to make an accounting adjustment might be perceived as a disadvantage by the host party, as the transferred reduction could not be counted toward its NDC. There could also be concerns about the environmental integrity of credits from sectors outside the NDC: As these do not “count” in terms of their NDC, the host party may have less incentive to ensure high quality. The “no adjustment” accounting option is therefore regarded by some as contrary to the overall thrust of the Paris Agreement’s mitigation provisions which emphasize progression and highest possible ambition (e.g. Article 4.3), and with Article 6.1 which recognizes cooperation “to allow for higher ambition.”

Accounting options which place more emphasis on incentives for progression of NDC coverage over time include: prohibiting transfers from emission

reductions outside the NDC target; placing quantity limits on transfers from outside the NDC; requiring a corresponding adjustment to the host Party’s NDC even for transfers arising outside the NDC; or requiring the host party to make corresponding adjustments only from a certain date such as 2031 or the Party’s next NDC period.

One detail that needs further technical consideration is the alignment between project crediting periods and NDC accounting: if crediting periods are longer than NDC periods, projects may transition from being “outside” to “inside” the NDC.<sup>8</sup>

An alternative concept of “outside” an NDC has arisen in the Article 6 negotiations, relating to going beyond the actions required to meet the NDC target, rather than referring to coverage of sectors or gases. In this viewpoint, an emissions-reduction activity that is not implemented by the host government for the purpose of achieving the NDC could be seen as “additional” to the NDC. This could for example apply to activities in sectors

### Box 1: Options for Transfers from Outside the Scope of an NDC Target

- No adjustment required by host party for transfers from outside its NDC target scope
- Time limit before host-party adjustment required (e.g. 2031)
- Quantity limits on use of transfers from outside NDC
- Transfers not allowed from outside NDC
- Host party must adjust NDC emissions balance for all transfers even those from outside NDC

## Box 2: Options for Use of Emission Reductions for Non-NDC purposes

### Article 6.2:

- Explicit host-party authorization for use of Article 6.2 ITMOs for non-NDC purposes
- Further transparency reporting of authorized non-NDC use
- Application of Article 6.2 guidance to authorized non-NDC use of ITMOs

### Article 6.4:

- Host party adjustment (or no host party adjustment) for non-NDC use of emission reductions

where the government has no NDC policies, Article 6.4 projects that are implemented and owned by project participants, or additional ambition beyond the NDC target. This has a linkage to the concept of additionality, i.e. ensuring that crediting projects make emission reductions beyond what would otherwise have occurred. Some parties have proposed that host parties should not have to make corresponding adjustments for reductions that go beyond the NDC, but other parties note that such projects can still reduce inventory emissions compared to what they would have otherwise been, and thereby contribute to the host Party's NDC (c.f. **Figure 1**), raising the possibility that the absence of an adjustment could lead to double use of emission reductions.

## EMISSION REDUCTIONS USED FOR NON-NDC PURPOSES

Emission reductions could potentially be used, or transferred and used, for purposes other than toward achievement of an NDC. Examples include voluntary cancellation of credits to enhance mitigation effort, and use towards mitigation obligations outside the UNFCCC, such as in the International Civil Aviation Organization (ICAO)'s Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) scheme that will require airlines to offset emissions growth from 2021 onwards. Avoiding double counting between NDCs and the CORSIA system is particularly pertinent due to CORSIA's very large potential demand of 1.6-3.7gigatons between 2021 and 2035.<sup>9</sup>

In March 2019, the ICAO Council approved Unit Eligibility Criteria for CORSIA and established a technical advisory board that will assess the eligibility of programs that are to provide offsets meeting those criteria.<sup>10</sup> The criteria require that credits be counted

only once toward a mitigation obligation, and that measures be in place to avoid double claiming between an airline and the host country of the emissions reduction. Avoiding double counting between NDCs and CORSIA also implies action on the UNFCCC side: as sketched in the example of **Figure 1**, emission reductions from a crediting project could contribute to a lower national inventory and hence toward NDC achievement.

Transparency decision 18/CMA.1 paragraph 77(d) references the possibility of non-NDC use of ITMOs. This decision requires that a party report information on transfers if it "authorizes the use of mitigation outcomes for international mitigation purposes other than achievement of its NDC." A related issue in the Article 6.2 discussions is whether the Article 6.2 accounting guidance should apply to such transfers.<sup>11</sup> Other issues include whether information reported via the transparency framework should include more detail such as quantities authorized for non-NDC use and the nature of their use. There is convergence in the negotiations that units from Article 6.4 activities could be used for non-NDC purposes, but there remains disagreement on whether an accounting adjustment similar to that shown in **Figure 2** should be made by the host Party to avoid double use of emission reductions.

## RELATIONSHIP OF ARTICLE 6.4 TO ARTICLE 6.2 ACCOUNTING

A conceptual question remaining in Article 6 discussions is the relationship of units generated by the Article 6.4 mechanism (A6.4ERs) to the ITMOs referenced in Article 6.2, and whether a single accounting process should address both.

The Paris Agreement requires that parties avoid

**Box 3: Options for the Relationship of Article 6.4 to Article 6.2 Accounting**

- Use Article 6.2 corresponding adjustment mechanisms to avoid double counting in relation to Article 6.4.
- Develop separate accounting for Article 6.4 that avoids use of emission reductions by more than one party, consistent with Article 6.5.

double counting in the use of ITMOs towards NDCs under Article 6.2, and avoid double use of Article 6.4 emission reductions for achievement of NDCs (Article 6.5).

One option under consideration is to treat A6.4ERs the same way as ITMOs and use the mechanisms of corresponding adjustment developed for Article 6.2 (similar to that shown in Figure 2) to avoid double counting and/or double use of all transfers using a single process.

As A6.4ERs would be issued from a central registry for the Article 6.4 mechanism, rather than by the host party itself, another proposed option would require no corresponding adjustment when credits are transferred from the registry (being “additional” to the NDC from this perspective), but would require an adjustment for any subsequent trades.

The example shown in Figure 1 suggests that to the extent that projects producing A6.4ERs deliver lower inventory emissions than otherwise would have been the case, they may contribute to the host Party achieving its NDC target (depending on the sector, gas, and time period in which the project is operating). This raises the prospect that in the absence of an adjustment, the host and another Party acquiring the A6.4ERs might both count the emission reductions.

**SHARE OF PROCEEDS FOR ADAPTATION**

A percentage of certified emission reductions (CERs) issued under the Kyoto Protocol’s Clean Development Mechanism are set aside to cover administrative costs of the mechanism, and to provide funding for the Adaptation Fund. As of June 30, 2018, monetization of the levied CERs has provided US\$199.4 million of the fund’s cumulative US\$753.3 million in receipts.<sup>12</sup>

Decision 1/CMP.8 extended the share of proceeds under the Kyoto Protocol to cover all its market mechanisms, including joint implementation (JI) activities between developed countries.<sup>13</sup> Under Article 6.6 of the Paris Agreement, a share of proceeds from activities under the Article 6.4 mechanism would similarly be used to cover expenses and help particularly vulnerable developing countries meet the costs of adaptation.

Although the Paris Agreement makes no mention of an equivalent levy on Article 6.2 transfers, some parties are proposing one, so that Article 6.2 crediting systems are not advantaged relative to the Article 6.4 mechanism, and as an additional revenue stream to the Adaptation Fund. The range of options proposed is summarized in the box below. Other parties oppose these proposals as unauthorized under the agreement and as a disincentive to transfers. They also note a potential legal impediment, in that an amendment to the Paris Agreement rather than a CMA decision might be required to implement a share of proceeds (c.f. the Doha Amendment implementing a share of proceeds for JI).

Some activities under Article 6.2 could be crediting systems similar to the Article 6.4 mechanism. However, Article 6.2 would also cover transfers resulting from international linkages between emissions trading systems. If two domestic emissions trading systems link, levying a share of proceeds only on international transfers would distort trading by imposing a cost on only some allowances within the system, creating a disincentive to link and affecting domestic policy.

In the absence of an explicit levy on Article 6.2 activities, participating parties could be asked to report on how mechanism revenue is used to support developing countries’ adaptation needs.

**Box 4: Options to Share Proceeds in Relation to Article 6.2****Subject 6.2 activities:**

- No share of proceeds for any Article 6.2 activities
- Share of proceeds only for crediting systems/systems similar to Article 6.4
- Share of proceeds for all Article 6.2 activities or all acquisition of ITMOs

**Structure and timing of levy:**

- Share of proceeds levied at issuance/first transfer
- Share of proceeds levied at every trade
- Share of proceeds levied at issuance or at use toward NDCs

**Alternatives to share of proceeds:**

- Reporting on use of mechanism revenues to support developing countries' adaptation needs

## ENDNOTES

- 1 [https://unfccc.int/sites/default/files/resource/94\\_IETA%20input%20to%20TD\\_final.pdf](https://unfccc.int/sites/default/files/resource/94_IETA%20input%20to%20TD_final.pdf)
- 2 The decision notes that sections III.A, III.B and III.C of the Presidency text do not reflect consensus and are without prejudice to the views of parties and consideration by the CMA.
- 3 Even in the absence of agreed guidance under Article 6.2 transfers can proceed, but participating parties would still need to meet the principles of Article 6.1, 6.2 and 6.3 in their use of ITMOs toward NDCs. Paragraph 77(d) provides a process for parties to report relevant information.
- 4 Decision 18/CMA.1 (in relation to Article 6) notes that the information referred to in paragraph 77(d) is without prejudice to the outcomes of discussions on Article 6 matters.
- 5 The transparency decision of -/CMA.1 requires all parties' national inventories to cover energy, industrial processes and product use, agriculture, LULUCF and waste, according to IPCC guidelines. Most parties will report on seven gases (carbon dioxide (CO<sub>2</sub>), methane (CH<sub>4</sub>), (nitrous oxide (N<sub>2</sub>O), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), sulphur hexafluoride (SF<sub>6</sub>) and nitrogen trifluoride (NF<sub>3</sub>)), but those developing countries that need flexibility in light of their capacities have flexibility to report on at least three gases (CO<sub>2</sub>, CH<sub>4</sub> and N<sub>2</sub>O) as well as any of the additional four that are included in the Party's NDC or are covered by an activity under Article 6. As such, any sectors or gases relevant to an Article 6 activity will be covered by the host Party's national inventory.
- 6 Synthesis report on the aggregate effect of the intended nationally determined contributions, Available at: [http://unfccc.int/focus/indc\\_portal/items/9240.php](http://unfccc.int/focus/indc_portal/items/9240.php).
- 7 For NDC targets expressed for a single year only, emission reductions can also be "outside" the NDC in terms of time. In the SBSTA negotiations, this is being addressed through a separate stream of work that relates to accounting for single- and multi-year targets.
- 8 For comparison, standard crediting periods in the Clean Development mechanism are up to 21 years (7 years, with two possible renewals) and can be even longer for afforestation projects.
- 9 [https://www.carbon-mechanisms.de/fileadmin/media/dokumente/sonstige\\_downloads/CTI\\_Workshop\\_2017/5\\_Healy\\_170623\\_CORZIA\\_CTI\\_Presentation.pdf](https://www.carbon-mechanisms.de/fileadmin/media/dokumente/sonstige_downloads/CTI_Workshop_2017/5_Healy_170623_CORZIA_CTI_Presentation.pdf)
- 10 <https://www.icao.int/Newsroom/Pages/CORSIA-implementation-on-course.aspx>
- 11 In this case the mitigation outcomes would not necessarily be transferred internationally, but an adjustment would still be needed to avoid double counting or double use.
- 12 Report of the Adaptation Fund Board, 3 October 2018, FCCC/KP/CMP/2018/4, [https://unfccc.int/sites/default/files/resource/4e\\_1.pdf](https://unfccc.int/sites/default/files/resource/4e_1.pdf)
- 13 This is yet to be implemented, as 1/CMP.8 the Doha Amendment to the Kyoto Protocol has not yet entered into force.



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