

Towards readiness

Supporting Article 6 integration in NDCs and NDC implementation plans

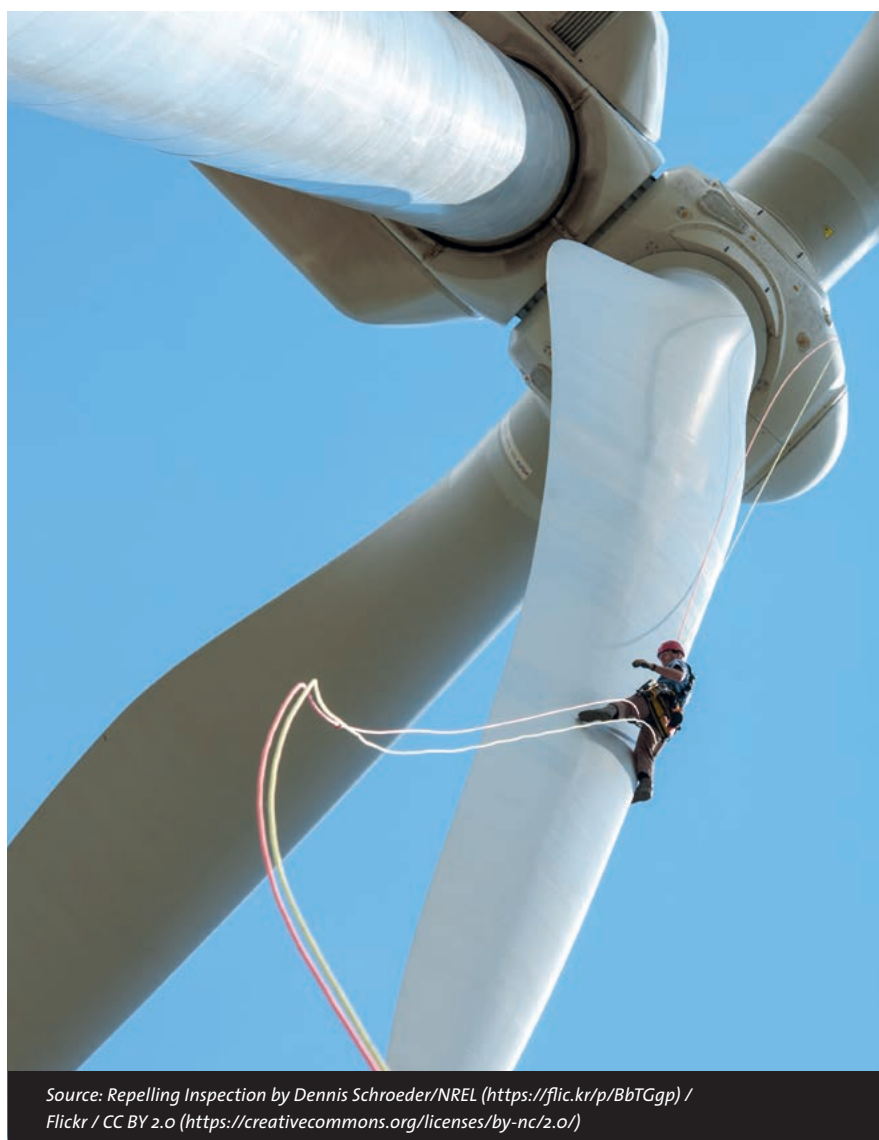
By Hanna-Mari Ahonen, Perspectives Climate Group; David Newell, Swedish Energy Agency; Aayushi Singh, Perspectives Climate Group

To achieve the long-term goals of the Paris Agreement (PA), the scale and pace of mitigation action must be urgently stepped up, and the private sector needs to be engaged. International market-based cooperation can enable ambition-raising by accelerating and scaling up mitigation action faster and cost-effectively. It can mobilise public and private actors to implement and enhance countries' Nationally Determined Contributions (NDCs), and contribute to ambition-raising beyond NDCs.

Following six years of negotiations, COP26 in Glasgow marked the adoption of rules for market-based cooperation under Article 6 of the PA ("Article 6 Rulebook"). Article 6 presents participating Parties with three forms of cooperation to allow for higher ambition in climate action and promote sustainable development. These are:

- i) Article 6.2 guidance for cooperative approaches;
- ii) Article 6.4 rules, modalities, and procedures for an internationally governed crediting mechanism and
- iii) a framework for Article 6.8 non-market approaches (NMAs).

This article focuses on market-based cooperation under Article 6.2 and 6.4.



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Article 6.2 guidance governs the use of internationally transferred mitigation outcomes (ITMOs) towards NDCs, international mitigation purposes (e.g., compliance under the CORSIA scheme for airlines) and/or other purposes (e.g., voluntary offsetting). Countries participating in such cooperation must ensure environmental integrity and apply robust accounting. They can apply their own criteria and procedures for ensuring the environmental integrity of mitigation outcomes and/or utilise the Article 6.4 Mechanism (A6.4M) or independent crediting standards. Public and private actors participating in Article 6 cooperation will need capacity to understand and meet the relevant requirements. Host countries have a key role in assessing whether proposed mitigation activities are consistent with their NDC and long-term low emission development strategies. Since ITMOs cannot be used towards the host country's NDC, a host country should authorise ITMOs only for mitigation beyond what is needed for NDC achievement.

Understanding the interlinkages between Article 6 cooperation and host country NDC implementation is crucial for ensuring that Article 6 cooperation contributes to – and does not undermine – the implementation of NDCs or the long-term goals of the PA. National Article 6 strategies and criteria should be developed in parallel with NDC implementation planning. This article aims to shed light on these issues, based on conceptual work and practical experience.

The role of Article 6 in NDCs and NDC implementation plans

NDCs and the NDC implementation plans reflect national circumstances and priorities of countries to combat climate change. NDCs are high-level documents that describe a country's targets. An NDC implementation plan elaborates the country's policies, priorities and plans to achieve its NDC targets, available resources and support needs, potentially including sector/activity-level information and plans for Article 6 cooperation (Michaelowa et al., 2021a). NDCs and NDC implementation plans set the framework conditions for Article 6 cooperation by that country. Consequently, Article 6 readiness requires a clear understanding of current and future NDC targets and plans. The clearer and more detailed the overall information and strategy for NDC implementation, the easier it is to define an Article 6 strategy that focuses on additional mitigation opportunities that are consistent with the short-, mid-, and long-term targets of the country.

International market-based cooperation under Article 6 can serve different objectives. A country may seek to engage in Article 6 cooperation to help to meet and enhance its NDC targets, attract investment into the country, facilitate technology transfer, or build capacities or finance "high-hanging" mitigation measures that it cannot implement without external financial support. Depending on the choice of goal(s), a country may pursue a pure 'buyer', 'seller' or even a 'mixed' strategy in its Article 6 engagement. It must be noted that cooperation under Article 6 cannot be the primary instrument of NDC implementation. It should be viewed as one of the many tools available to enhance a country's climate action by incentivising cost-effective mitigation and mobilising finance for low-carbon development (Michaelowa et al., 2021b). Also, non-state actors, such as companies, can engage

in Article 6 cooperation, as activity developers and sellers and/or as buyers. Companies may use ITMOs or Article 6.4 Emission Reductions (A6.4ERs) to finance mitigation beyond their value chains and make claims about offsetting specific emissions or contributing to NDC achievement.

To be “ready” for Article 6 cooperation, countries need to gain a good understanding of Article 6 participation requirements, develop policies, build institutional capacities, and establish necessary infrastructure. However, as countries differ in their formulation of NDCs as well as their Article 6 strategies, Article 6 readiness will not be based on one-size-fits-all actions. Rather, it is a dynamic process involving different steps performed by different entities (Michaelowa et al., 2021a).

Michaelowa et al. (2021a) propose three building blocks for Article 6 readiness: Article 6 strategy and guiding principles, Article 6 governance and institutional framework and Article 6 monitoring infrastructure. Figure 2 presents key considerations for each building block.

In an empirical analysis of Article 6 readiness in updated NDC submissions, Michaelowa et al. (2021b) found that 77% of the 68 countries who submitted updated or revised NDCs between July 2019 and July 2021 indicated their interest in market-based cooperation under Article 6. Of these, 7% of the countries communicated a ‘buyer’ strategy, while others preferred Article 6 engagement as sellers or through a mixed strategy. This may hint at a prolonged imbalance between buyers and sellers. The adoption of the Article 6 Rulebook provides countries with much needed clarity to develop their Article 6 strategies, institutions, and infrastructures.

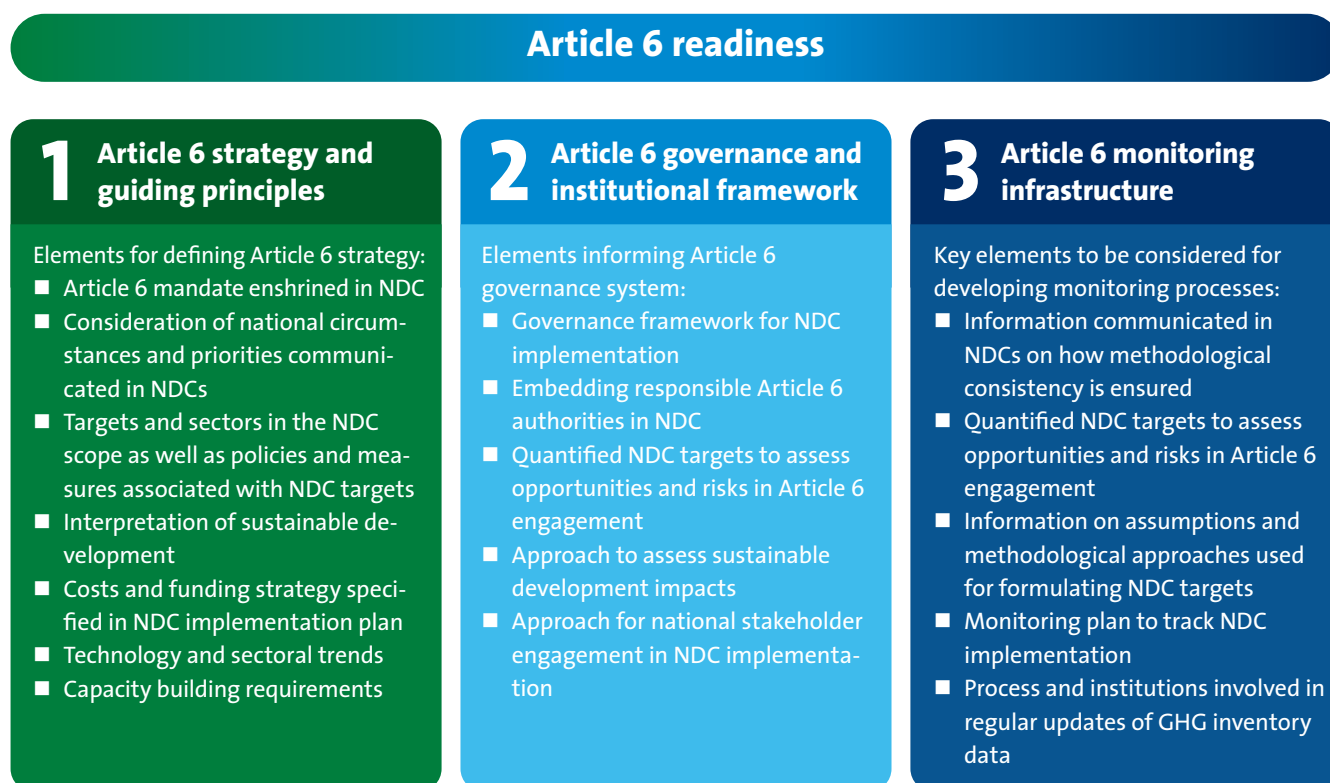


Figure 2: Article 6 readiness - Building blocks. Source: The authors

How to maximise synergies in getting ready for Article 6

Article 6 strategies and priorities should be developed in close collaboration with entities involved in NDC development and implementation, and ideally incorporated in NDC implementation plans.

The analytical framework to assess Article 6 readiness in NDCs and NDC implementation plans developed by Michaelowa et al. (2021a) is discussed below.

Assessing Article 6 readiness in NDCs

The NDC sets the context for the Article 6 strategy. Communication of the **intention to use Article 6** as well as the scope of intended Article 6 cooperation in the NDC is an important signal of the country's willingness to engage with the international carbon market community and can attract potential partner countries.

Information regarding the **scope and coverage of the NDC** as well as a clear description of **NDC targets** helps countries in effectively utilising Article 6 as a means to achieve their mitigation targets. For buyers, this means understanding



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the demand for ITMOs, for host countries it relates to information such as using revenues from the sale of ITMOs for NDC implementation, retaining mitigation from cooperative approaches domestically, agreeing on mitigation-sharing with ITMO buyers and/or using the A6.4M for results-based climate finance. The more disaggregated and granular the information, the better the countries will be prepared to identify the opportunities for international cooperation.

Several countries' NDCs include information on the legal and institutional framework for formulating, implementing and updating NDCs. This information is useful for identifying which responsible entities should be engaged also in national Article 6 processes.

With regards to **accounting and monitoring under Article 6**, information on the calculation of the NDC emission balance from all emission sources and sinks covered in the NDC, clarity on target years for NDC targets, as well as disclosure of applied accounting approach are important. A functional transparency framework is necessary to track a country's progress in achieving its NDC targets, thereby supporting the country's engagement in market-based cooperation.

Assessing Article 6 readiness in NDC implementation plans

NDC implementation plans report existing and planned **policies and measures**, prioritisation of said measures as well as on the country's interpretation of **sustainable development**. For a country participating in market-based cooperation, it is important to keep track of relevant policies as it is a requirement for determining

(regulatory) additionality and setting robust crediting baselines for Article 6 activities. However, there are some key challenges with NDC implementation plans in that they do not have a common format; require strong national ownership and coordination across sectors and actors; and are not required to be publicly available. Improving the transparency and clarity of NDC targets is crucial for ensuring that Article 6 activities go beyond current NDC targets and contribute to higher ambition.

Transparency on the estimation of **mitigation costs** is crucial for differentiating between mitigation measures that can be mobilised through international and domestic carbon markets, international climate finance, or domestic means. Estimation of mitigation costs also informs the development of a country's **funding strategy**. The disclosure of mitigation costs and funding strategies provides much needed clarity to buyer countries when engaging with a host country.

Article 6 cooperation can also be promoted by disclosing information on **technology** needs and availability as well as **sectoral strategies**. It attracts interested buyers to support the best available technologies and foster transformational changes within a sector. This information is also necessary for setting baselines and determining additionality.

During the development of an NDC implementation plan, it is recommended that guiding principles of Article 6, Article 6 institutional framework and a robust monitoring system are embedded in the plan.

Insights on the role of NDC implementation in Article 6 cooperation

The SEA views NDCs as an important statement of political will which indicates the level of ambition of the host country. This is also likely true for host countries, who evaluate the acquiring country's ambition on basis of the NDC. Thus, the NDC provides a foundation for the collaboration and assists in the evaluation of potential partners. Not surprisingly, the NDC is one of the primary criteria the SEA uses to evaluate a potential partner country, besides political will, capacity for the cooperation and general suitability for Swedish cooperation.

It is important to remember that NDCs will be updated and therefore are dynamic in their nature. Building an earnest interest for cooperation and establishing mutual trust between countries is the most important parameter for successful Article 6 cooperation. Designing the actual cooperation as a win-win situation with clear outcomes for all participating countries is paramount.

When evaluating NDCs, the SEA looks at the general ambition, historical and current emissions, any partition into conditional and unconditional targets as well as the approach to Article 6 and designation of sectors for Article 6-cooperation. SEA also examines the degree of integration of Agenda 2030 into the NDC, i.e., if specific SDGs are highlighted, prioritized, as well as the potential of integrating these into the design of the activities.

The comprehensiveness and granularity of the NDC is another important feature the SEA considers. If sufficient detail is provided in the NDC and the associated implementation plan, ambiguity is reduced and potential for constructive discussions on concrete action is increased. The

SEA's experience from analysing NDCs so far is that there is significant room for improvement here. A majority of countries are still struggling to make sense of how their own NDC will be operationalized and implemented to ensure fulfilment of targets.

Designing a "white list" that identifies the sectors or activities that the host country designates to be suitable for Article 6 cooperation facilitates additionality assessments as well as the discussions on activity selection with the host country. Up until the Glasgow decision, the market for Article 6 has been characterized by a shortage of both host countries and activity implementers, which also influences the discussion on activity selection. However, since then there has been a notable increase in interest from countries to participate in Article 6 cooperation.

At this early stage, the work is constantly evolving at the SEA, where internal processes are being developed and adapted on a continuous basis. Relying on our experience of over 20 years of bilateral and multilateral work under the CDM, analysing our internal processes from an Article 6 perspective has been a very fruitful journey. The role of sustainability in carbon markets, for example, is a prioritised area for Sweden and thus important to integrate into the design of our Article 6 purchasing programme.

After the decision in Glasgow, it became apparent that we all needed to align our national processes with the Article 6 Rulebook. For the SEA, this meant initiating a project to develop our national framework for Article 6 and we have dedicated resources for this internally. In anticipation of capacity building needs, we are working with our implementing partners to deliver capacity building, both on a theoretical and practicable level.



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The road ahead

To promote Article 6 readiness-building, we recommend the following:

- Actors participating in Article 6 cooperation need capacity building to enable strategic engagement, informed decision-making, and robust activities. Capacity building needs and efforts must be mapped to streamline and coordinate international support for Article 6 readiness and avoid the duplication of efforts. Capacity building relating to NDC planning and transparency contributes also to Article 6 readiness.
- Guidance can be developed for host countries to embed Article 6 into their “toolbox” for NDC implementation. Article 6 is an important means of implementation which can be utilised by countries for the achievement of their NDCs and increasing ambition in future NDC updates.
- Alignment of activities with host countries NDCs and long-term strategies can be ensured through approaches to determine whether an activity is additional to the NDC package and through setting crediting baselines that go beyond the NDC implementation pathways and are aligned with the long-term strategy. However, this requires revision and transformation of the methodologies used in carbon markets to date. The International Initiative for Development of Article 6 Methodology Tools (II-AMT, 2022) is developing an NDC guidance to allow host countries to assess how the proposed Article 6 activity

aligns with NDCs, NDC implementation plans and long-term strategies, while offering programme developers methodological guidance on how to ensure this (Michaelowa et al., 2022).

Regarding Sweden's Article 6 work, the coming year will be an exciting one. The SEA is in discussions with several partner countries on entering into legally binding bilateral agreements regarding Article 6 cooperation, some of which are at a very advanced stage, and which hopefully will be concluded during the year. These will provide proof-of-concept and serve as a signal to our political leaders that Article 6 cooperation is possible. At the same time, the SEA is developing the selection criteria and a process for identifying activities and has begun evaluating activities in parallel.

Domestically, the national framework for Article 6 is developed to deliver on the participation requirements for Article 6 in the Glasgow decision. Naturally, the anticipated decision in COP27 will inform this process, with guidance on how to approach corresponding adjustment and reporting tables.

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