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Issues and Options: Elements for Text Under Article 6

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This paper seeks to capture some of the issues that need to be addressed in the rulebook, and unpack the options for each issue, with the intention of catalyzing a discussion among Parties.

The views expressed in this paper are those of the authors, and they are not intended to represent a summary, consensus or elaboration from any specific meeting or discussion. It is intended as food-for-thought, to help Parties consider the issues, and define their own positions according to national interests.

This paper will be updated as the discussions progress and mature, and new ideas emerge, while others may clearly be discarded.

Introduction

Understanding of the elements needed to operationalize Article 6 of the Paris Agreement (PA) has evolved since COP 21 through formal and informal discussions, through workshops as part of the UNFCCC process, and through Party submissions to SBSTA.

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Parties have identified a number of issues, and put forward their views on how they could be addressed. As was the case in the negotiations for the PA at this stage, there are many views, and significant divergences, not only on substance, but also on what is legitimate to be included in a negotiating text. The constructive ambiguity that was needed in order to reach a deal in Paris at COP 21 needs to be resolved now.

The work programme put forward by the co-Facilitators would indicate that the outcome at SBSTA 47 ought to be, in some form, that of "elements" which could help in the elaboration of a negotiating text leading to SB 48. This would be coupled with a mandate, to be given to the Chairs/Facilitators, to elaborate such a text.

1. Principles

Given the divergence of views that will need to be bridged, both in terms of the legitimacy of issues to be included, as well as the choices between the different options put forward by Parties, it may useful to identify some basic principles to help in the review of these options.

a. **Bottom up**. The ethos of the whole PA is bottom up, and that should permeate our thinking in making decisions. That is true in the determination of NDCs, and true in the governance that we choose.

b. **Governance**. While the governance is certainly much more decentralized than in the Kyoto Protocol (KP) it is not a totally one-way street. However, the balance between centralization and decentralization is remarkably different from the KP.

c. **Transparency**. Transparency plays a critical role in the governance of the PA, and it is meant to create trust among Parties, as they aim to raise the level of ambition. Transparency is not meant to be a silver bullet, but it is seen as an important tool in the PA, to be used to solve problems.

d. **Article 6 is unitary**. Art 6 elements cannot be considered in isolation, they need to be considered together. One view is that Art 6.2 and Art 6.4 were put forward as options, with different governance, for Parties to cooperate internationally. Mitigation activities are not pegged into Art 6.2 or 6.4, it is more likely that Parties should have a choice between Art 6.2 and Art 6.4.

e. **Paris Agreement is unitary**. Art 6 must not be seen in isolation, but in the context of the whole PA. Sustainable development (SD), transparency, environmental integrity (EI) and accounting are not only present in Art 6, but throughout the PA. Art 6 will have to build on and

be connected with Articles 4, 13 and 15. At the same time, Art 6 will also inform the more general framework (Art 13.7 information "to track progress" will necessarily include information with respect to use of ITMOs pursuant to Art 6.2). Conversely, Art 6.2 (including arrangements for "corresponding adjustment") may inform the format and timing of that information under Art 13.7).

2. "Elements" of Article 6.2[1]

A number of elements can be identified under Art 6.2 that will need to be part of the "rulebook". Parties see different ways of treating these elements.

2.1 Elements defining an ITMO

The elements that define an ITMO, and its scope, will be an important issue, with many ramifications for the scope of Art 6.2, and how it meets the Principles enunciated in Section 1 above.

2.1.1. What is an ITMO?

ITMO is the abbreviation for Internationally Traded Mitigation Outcomes. It was developed during the process leading to COP 21, and became part of the jargon post-COP21, with some attributing it a status not dissimilar to that of a unit. However, nowhere in the PA is a new unit or special status created. Some Parties emphasize that the word "traded", and not "tradable", was used in the PA.

There are a number of ways that Parties look at ITMOs, including the following views:

a. Any domestic mitigation outcome, which is exported from the Party where it was created, to another Party, for eventual use towards meeting its Nationally Determined Contribution (NDC). This may include units such as EU ETS units (EUAs), Joint Crediting Mechanism (JCM) reductions, Korean ETS units, Indian renewable energy certificates, etc.
b. Only units issued from NDCs quantified in tCO2e, with units (e.g. Quantified Contribution Units issued, and equal in number to the NDC budget. These units are transferred between Parties, and only Parties can own them.
c. Mitigation outcomes from an NDC quantified in tCO2e, transferred between Parties, but without the attribute of unit, without a legal or

[1] For further details on this issue, see Marcu A., & González Holguera, S. (2017). *Aide Memoire on the Scope of Article 6.2*

regulatory persona. Also, there is no relationship between a number of ITMOs and NDC budgets.

2.1.2 Who issues ITMOs?

ITMOs, prior to their transfer from Party A (to Party B), must come into existence. Options could be that:

a. ITMOs are issued by a Party
b. ITMOs are issued by the CMA, or a designated body

2.1.3 Metric of an ITMO

Three options can be considered:

a. **Carbon metric**. In this option, only an ITMO denominated in tCO_2e could be transferred under Art 6.2. This option would commoditize ITMOs, and would make accounting significantly easier.
b. **Any choice of metric**. In keeping with the bottom-up ethos, this option would allow ITMOs to be denominated in any choice of metric that fits with the NDC of the Parties involved in the transfer. An ITMO could for instance take the form of an energy efficiency or renewable energy certificate.
c. **List of acceptable metrics.** Under this option, a positive list of acceptable metrics would be developed which will increase over time, as the need is identified.

2.1.4 Shelf life of an ITMO

a. **No shelf life limit**. A Party could bank an ITMO and use it towards its NDC, or transfer it, at any point in the future.
b. **Restricted shelf life.** ITMOs would:
    i. Not be bankable from one NDC period to another.
    ii. Would be cancelled if it remains unused after some time, within the timeframe of an NDC. If this option is chosen, the temporal limit will need to be determined.

2.1.5 ITMOs originating outside/inside the scope of NDCs.

The issue to be settled is whether an ITMOS coming from a sector outside the scope of a Party's NDC can be transferred, and become an ITMO.

a. **Do not allow transfers from outside the scope of an NDC.** Since the aim of Art 6.2 is to help Parties to achieve their NDC, one option would be that ITMOs originating outside the scope of the host Party's NDC could not be transferred under Art 6.2. To be transferable and become an ITMO, the Party would first have to expand the scope of its NDC to include that sector.

b. **Allow transfers from outside the scope of an NDC.** This position is justified by the fact that it may lead to an increase in ambition. Allowing transfers of ITMOs from outside the scope of a Party's NDC may encourage mitigation actions in these sectors, and promote, in future NDC rounds, the broadening of its scope, eventually towards an economy-wide NDC. However, there is difficulty regarding the corresponding adjustment. Discussions on how corresponding adjustments are made in this scenario are discussed under the Accounting section (2.2.5).

2.2 Accounting[2]

Art 6.2 introduces three "shall" provisions, and creates through paragraph 36 of 1/CP.21 a work programme to develop guidance for robust accounting, including the avoidance of double counting towards Party's NDCs.

Robust accounting includes the application of corresponding adjustments. For guidance on accounting and corresponding adjustments to be developed, a number issues must be settled.

2.2.1 What gets adjusted?

Three views can be identified:

a. **Inventory approach**. The inventory itself is not adjusted. Instead, a new number, which uses the inventory as a starting point is created, and then adjusted, based on in/out transfers. Some would call that an "accounting balance".
b. **Target approach.** In this option, what is being adjusted is not the NDC itself, but a number that uses the NDC as a starting point. It is then adjusted, based on in/out transfers, but this is different from the NDC itself. Some may refer to this with similar terminology as to that above, such as an "accounting balance".
c. **Interchange approach**. This approach relies on the creation of an Interchange account. Beginning from zero, the Interchange Account would count in/out transfers and produce a net total. This Interchange value, together with the inventory, and the NDC number, would give a picture of how the Party is performing vs. its NDC pledge.

Each of these options present plusses and minuses. The Interchange approach can be seen as an option in itself, or a step in the adjustment of the inventory, or the target.

[2] For further details on this issue, see Marcu, A., & Martin-Harvey, O. (2017). *Aide Memoire on Corresponding Adjustments in Article 6.2*

2.2.2 What is the basis for adjustment?

Two views can be identified:

a. **Adjustment at transfer.** The adjustment at the time of transfer ensures that the adjustment occurs separately from the decision by the receiving Party on how to use the ITMO.
b. **Adjustment at use**. If accounting at the time of usage were employed, then the transferring Party would be uncertain about achieving its NDC, because they must wait for another Party, and find out whether it will, or will not use, the imported ITMO. This presents transparency concerns.

2.2.3 Timing of corresponding adjustments

NDCs encompass long time periods and ITMOs can be accounted for in different ways, which will affect NDC compliance. Two options can be considered:

a. **Time of NDC compliance.** Make the adjustments at the time when the Party must show that it meets its NDC. This may not show an accurate picture of the real transfer activity and NDC compliance by the Party.
b. **Time of transfer.** If adjustments are made when transfers take place, this may represent a more accurate picture of transfer activity. However, it may affect the outcome of the Party's efforts to meet its NDC and force a certain pattern in transfers, unless they are somehow connected with the vintage of the ITMO.

2.2.4 Single year target NDC

Single-year target NDCs presents a challenge, especially as many Parties have single year targets. There are a number of ways to treat this type of NDC:

a. **Cumulative.** Credits/units generated during the NDC period could be used for the achievement of the point year target.
b. **Same vintage.** The vintage year of credit/units will be used for the achievement of the point year target.
c. **Average.** Credits/units generated during the NDC period could be averaged by the NDC period and the averaged amount of credits/units would be used for the achievement of the point year target.

2.2.5 Transfers from Inside/Outside the NDC

The issue of transferring ITMOs originating from inside or outside the scope of the NDC, also appears in relation to other Art 6 issues. In terms of accounting, this could be treated in a number of ways, which may include:

a. Transfers from outside NDCs are not permitted.
b. Only adjust for transfers from inside the NDC.
c. Adjust for transfers from both inside and outside NDC.

d. Report transfers originating from outside the scope of the NDC, but do not do a corresponding adjustment.

2.3 Ensuring Environmental Integrity[3]

Ensuring environmental integrity is one of the "shall" provisions included in Art 6.2, which states that "*Parties shall, where engaging on a voluntary basis in cooperative approaches [...] ensure environmental integrity [...] including in governance*."

An informal definition of EI could be formulated as needing to provide the assurance that transfers of ITMOs will not lead to an increase in atmospheric emissions. There is still considerable ambiguity concerning this provision, and it could be unbundled in a number of sub-issues.

2.3.1 What does EI in Art 6.2 apply to?

a. **Transfer only.** In this option, EI focuses on ensuring that the transfer itself does not lead to an increase in emissions.
b. **What is being transferred.** In this option, the quality of the ITMO is part of how we understand ensuring EI in the context of Art 6.2.
c. **Both:** Under this option both the transfer, and the quality of ITMOs, are within the scope of EI under Art 6.2.

2.3.2 Operationalization of EI under Art 6.2

a. Through (i) robust accounting (corresponding adjustments) and (ii) transparency provisions. The transparency provisions would be part of the Transparency Framework under Art 13.
b. Through (i) accounting provisions; (ii) provisions for EI, potentially in the form of "guidance" or criteria; and (iii) transparency provisions, including additional disclosure provisions on how the ITMOs meet this "guidance" on EI. Another provision that may also be added is in the form of a technical peer review process.
c. Through standards for ITMOs defined by the CMA and adherence to these standards checked by the CMA.

2.3.3 Governance of EI under Art 6.2

The governance of EI can be unbundled into a number of elements, which are very much related to the way the EI "shall" is operationalized. Governance is also, in many ways, a misunderstood term, interpreted in different ways by different stakeholders.

[3] For further details on this issue, see Marcu, A., & Vangenechten, D. (2017). *Aide Memoire on Environmental Integrity in Article 6.2*

For the purpose of this paper, governance will be understood to mean "the process by which authority is conferred, by which rules are made, and by whom those rules are enforced and modified". It could also be enunciated as "who makes the rules, the process for making rules, and the process of enforcing rules".

a. **Transparency provisions.** In the case of transparency/reporting, the options available are:
    i. By the Parties, if Art 6.2 is totally left to Parties, with no functions for the CMA.
    ii. By the CMA, or a designated body, as part of Art 13.
b. **Guidance for EI.** If there is guidance on EI characteristics of ITMOs it could emanate from:
    i. Parties involved in the transfer.
    ii. The CMA or a designated body.
c. **Review of compliance with EI guidance.** If there is guidance on EI characteristics then:
    i. The review can be undertaken through peer review convoked by the Parties involved.
    ii. Peer review arranged under the auspices of the CMA or a designated body.
d. **Approval of ITMOs.** If ITMOs need to be checked and approved for EI, that approval can emerge from:
    i. Parties involved in the process only.
    ii. The CMA, or a designated body.

2.4 Promoting Sustainable Development

Promoting Sustainable Development is also one of the "shall" provisions included in Art 6.2, which states that "*Parties shall, where engaging on a voluntary basis in cooperative approaches [...] promote Sustainable Development [...] including in governance*."

In principle, without rendering judgment whether or not SD is a matter of national prerogative, the scope, operationalization and governance of SD could be structured along similar lines as EI. However, SD is much more broadly accepted as being the prerogative of the Parties.

2.4.1 What does SD in Art 6.2 apply to?

a. **Transfer only.** This option focuses on ensuring that the transfer itself promotes SD.
b. **What is being transferred.** In this option, the quality of the ITMO is part of how we understand promoting SD in the context of Art 6.2.

c. **Both.** Under this option both the transfer and the quality of ITMOs are within the scope of SD under Art 6.2.

2.4.2 Operationalization of SD under Art 6.2

a. Through transparency provisions. The transparency provisions would be part of the Transparency Framework under Art 13.
b. Through (i) provisions for SD, potentially in the form of "guidance" or criteria; and (ii) transparency provisions, including additional disclosure provisions on how the ITMOs meet this "guidance" on SD. Another provision that may also be added is in the form of a technical peer review process.

2.4.3 Governance of SD under Art 6.2

Similar to the governance of EI, the governance of SD can be unbundled into a number of elements, and they are very much related to the way the SD "shall" is operationalized:

a. **Transparency provisions.** In the case of transparency/reporting, the options available are for these provisions to be developed:
    i. By the Parties, if Art 6.2 is totally left to Parties, with no function for the CMA.
    ii. By the CMA, or a designated body, part of Art 13.
b. **Guidance for promoting SD.** If there is guidance on SD characteristics of ITMOs it could emanate from:
    i. Parties involved in the transfer
    ii. The CMA or a designated body
c. **Review of SD guidance.** If there is guidance on SD characteristics then:
    i. The review can be undertaken through peer review convoked by the Parties involved.
    ii. Peer review arranged under the auspices of the CMA or a designated body.

2.5 Use of ITMOs

Restrictions on the use of ITMOs can take a number of forms.

2.5.1 Supplementarity

This was a central principle under the Kyoto Protocol, which stipulated that commitments were to be met primarily through domestic action, with flexibility mechanisms playing a supplementary role.

a. **No supplementarity.** Unlike the Kyoto Protocol, the Paris Agreement makes no mention of supplementarity.

b. **Apply supplementarity to the Paris Agreement.** A limit could be imposed on the quantity of ITMOs that a Party can use to meet its NDC. This would put the onus on those advocating such a limitation to identify in the text of the PA a reference that could be in some way interpreted as referring to supplementarity.

2.5.2 Transfer restrictions: quantity

If the transfer of ITMOs can help a Party meet its NDC, a country that oversells ITMOs may fail to meet its NDC. In the Kyoto Protocol, a "Commitment Period Reserve" was introduced to reduce the risk of overselling.

a. **No restrictions.** As the Paris Agreement does not mention such a provision in Art 6.2, one position is to put no restrictions on the quantity of ITMOs a Party can transfer out, and trust the Parties not to oversell.
b. **Imposition of transfer restrictions.** Parties could be prevented from selling more than a certain quantity, expressed as a percentage related to its NDC. As above, those advocating such an approach would have to justify why they feel that this issue has not been put to bed in Paris and why there is no ''hook" for such a restriction in the text.

2.5.3 Share of proceeds

Share of proceeds is only mentioned in Art 6.4 of the PA. Such a clause was included in the KP, and stated that a fixed percentage (2%) of Certified Emission Reductions issued for a Clean Development Mechanism (CDM) project, would be used to "cover administrative expenses as well as to assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation." The options for Art 6.2 are:

a. **No share of proceeds included**. One option is to defend that there is no such clause in the text of the PA.
b. **Introduction of a share of proceeds clause.** An alternative is to introduce such a clause. If this is what is opted for, it will have to be determined what is the basis in the PA for doing so. Should this clause be considered, additional decisions will have to be made including:
    i. Where to apply it?
        1. First transfer only
        2. Every subsequent transfer
    ii. In the case of 2) above do you apply it
        1. At a constant rate
        2. At a decreasing rate
        3. At a progressive rate

2.5.4 Authorization for participation by Parties

Art 6.3 states that the use of ITMOs towards NDCs shall be "voluntary and authorized by participating Parties". This translates into the need for authorization for any non-Party entity to take part in the cooperative approaches under Art 6.2. Therefore, subnational entities and private sector organizations need to be authorized by a Party to the PA to take part in such cooperation.

One issue that has been debated is whether this implies that the national government who needs to authorize a subnational entity must be a Party to the PA. Another set of options emerges from the choice of how this permission is granted. The only experience so far in this area is with CDM, which, as a project-by-project approach, required a Letter of Approval for each project. However, many types of cooperation may emerge under Art 6.2, which may lead to consideration of other options. Authorization may be granted:

a. On a transfer-by-transfer basis
b. As a general authorization to participate in Art 6.2

2.6 Eligibility of Parties for Art 6.2

There have been eligibility conditions under the KP for participation in Art 6, 12 and 17. Some potential eligibility requirements may be considered, based on the discussions so far.

2.6.1 Type of NDC.

According to some views, Parties may need to have NDC with certain characteristics, or would need to have their NDC expressed in a certain way, to be able to participate in Art 6.2. This would have implications for other issues discussed in this paper. Two options seem to be under consideration:

a. **NDCs expressed in carbon budgets.** If a CO_2e metric is used for ITMOs, it could be coherent to also require NDCs to be quantified in CO_2e budgets. Parties could then formulate their NDC in whichever way they wish, but could only participate in Art 6.2 transfers if they can quantify them in carbon budgets. How non-CO_2e expressed NDCs are then converted into CO_2e budgets, and how the factors are calculated, and by whom, are decisions which will have to be made.
b. **Any type of NDC.** Another option would be that Parties with any type of NDC can participate in Art 6.2. The transfer may take place in the metric the NDC is expressed in, or the ITMO may be expressed in Co2e.

2.6.2 Regulatory requirements.

Certain regulatory requirements may need to be met for Parties to be eligible for participating in Art 6.2.

a. **National institutional requirements**. To participate in Art 6.2 transfers, a Party may be required to have a Designated National Authority (DNA), accredited with the CMA. Parties are currently required to have a DNA for the CDM under the KP.
b. **No requirements.** Alternatively, there could be no requirements for any national institution to be accredited with CMA. Any requirements for national institutions may be left to the cooperating Parties to determine.

2.6.3 Registry Requirements

The availability of a National Registry may be another condition for eligibility for Art 6.2. A number of options can be considered in this respect. This could be more than a multiple choice, with a combination of the options below to be considered.

a. **System of National Registries.** A National Registry, as part of a system of national registries, which the Party operates, is a requirement.
b. **Central registry option**. Availability of a central registry, operated by the UN, for those Parties which may not wish to operate their own National Registry.
c. **National Registry only if a transfer-in takes place.** Under this scenario, a National Registry, or Accounts in a Multilateral Registry are only needed if there are transfers-in.
d. **Multilateral Registry/data base**. A Multilateral Registry, operated by the UN, where information related to transfers and quantified NDCs is recorded. Parties will have accounts in this Multilateral Registry. The Multilateral registry could be an option in itself, or in addition to the National Registry system.

2.7 Tracking transfers

In the Kyoto Protocol, many rules were drafted for the issuance and tracking of the transfers through an International Transaction Log. However, it is not yet clear how transfers will be tracked under the PA.

a. **International Transaction Log**. One possible approach would be to use a structure similar to that of the Kyoto architecture and track individual transfers through an International Transaction Log.
b. **Netting bilaterally.** Alternatively, Parties could report net bilateral transfers made, either under the transparency framework of Art 13 or with additional guidance under Art 6.2 to ensure there is a common standard. The Multilateral Registry mentioned above could be used for tracking.

3. "Elements" of Article 6.4

Art 6.4 states that *"a mechanism [...] 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."*

For the purpose of this paper we will call the new mechanism "A6.4M", and its output "credits". The CMA, or its designated body, could issue A6.4M credits:

a. **In a UN Holding Registry**. This Holding Registry would be similar to the CDM registry.
b. **In a National Registry.** In this case credits would be issued, without going through a UN Holding registry, in the
    i. Registry of the host country of the mitigation action under the A6.4M
    ii. Registry of another Party**,** as directed

3.1 Governance

3.1.1 Respective role of CMA and Parties

The governance of Art 6.4 clearly falls under the authority of the CMA. However, it is unclear what the extent of the role of the CMA is to be, and how this will relate to the envisioned enhanced role of the Parties under this mechanism, compared to the CDM under the KP.

In our view, this is an important consideration given the bottom-up, decentralized governance of the PA. In terms of the respective roles of the CMA (or its designated body) and the Parties, a few options emerge:

a. **CMA/designated body with a similar role as under the CDM.** The role of the CMA could be similar to the role it had under the CDM. This centralized option would limit the role of Parties to what is under their remit, similar to what is currently under the CDM.
b. **Enhanced role of Parties.** If the role of the CMA is to be different than under the CDM, then some of the responsibilities of the CMA will have to be devolved to Parties. This may include:
    i. Provide an initial approval and certification that it meets country SD priorities
    ii. Withdraw certifications
    iii. Accredit verifiers
c. **Regional bodies.** Some of the more technical functions currently under the remit of the UNFCCC Secretariat and technical panels of the CDM Executive Board could be devolved to regional centres. Regional Cooperation Centers have been established and currently exist under

the CDM, to increase the geographical distribution of CDM projects and promote CDM tools. Issues such as human rights and stakeholder consultation could be considered as areas where regional centers could play a useful and legitimate role in a more cost-effective manner.

3.1.2 Appeals process

The issue of an appeals process has been an ongoing discussion under the CDM and was never resolved. The discussion was less on the validity of the idea, and more on how to operationalize it. A number of options could be considered:

a. **Appeals process.** A number of options could be considered, based on the parameters of a) who can appeal; b) who do they appeal to; c) the basis of the appeal:
    i. National stakeholders and project proponents can appeal to national authorities/CMA designated regulatory body on issues related to the Art 6.4 process only.
    ii. International & national stakeholders and project proponents can appeal to national authorities/CMA designated regulatory body on issues related to the Art 6.4 process only.
b. **No appeals process.** The CDM practice may be continued, with no appeal mechanism under Art 6.4.

3.2 Functions & scope

The scope of the A6.4M was discussed in Paris, as well as in many post-Paris submissions and discussions. A number of issues and options can be identified, some of which are clear, and some more open for discussion.

a. **Hosting of Art 6.4 activities**. All Parties (meeting eligibility criteria?), can host Art 6.4 activities.
b. **Use of Art 6.4 outcomes towards NDCs**. All Parties (meeting eligibility criteria?), can use Art 6.4 outcomes towards NDCs.
c. **Type of activities**
    i. Limited to baseline and credit CDM-like activities**.** Paragraph 37 of 1/CP.21 refers to "additionality", which may imply that Art 6.4 is limited to baseline-and-credit activities.
    ii. Also includes additional activities such as:
        1. REDD+ activities
        2. Certify other non-UN standards (e.g. VCS, JCM)
        3. Provide unbundled services for result-based financing

3.3 Relationship between 6.2 and 6.4

Art 6 is not explicit on the relationship between Art 6.2 and 6.4. There are different and subtle option, but with very powerful ramifications. This will also

influence whether credits from A6.4M are subject to corresponding adjustments, and if so, when. The discussion is premised largely on a number of assumptions.

a. Like the CDM, the Art 6.4 mechanism will issue credits under the instructions of the body designated by the CMA Regulatory Body.
b. There will be a secondary market emerging in A6.4M credits, i.e. there will more than one transfer.

There are a number of options in terms of how Art 6.4 credits and ITMOs relate to each other:

a. **A6.4M credits are ITMOs all the time.** There is a unitary system, and set of rules, for secondary transfers of ITMOs and A6.4M credits. Both will always have to follow the same rules for international transfers, including for corresponding adjustments. A6.4M credits could then be seen as an example of ITMOs. When these credits are internationally transferred, this will be done under the same rules as ITMOs from Art 6.2.
b. **A6.4M credits are never ITMOs.** Another position, fed by the uncertainty over the quality of ITMOs, is that there is no fungibility. Art 6.4 creates a particular type of unit, whose integrity must be protected by keeping them separate from ITMOs. This implies the creation of a parallel set of rules for the transfer of A6.4M credits, distinct from those from ITMOs under Art 6.2. If this scenario is adopted, such a set of rules will have to be developed. There is no provision for such a work programme in the PA.
c. **A6.4M credits will become ITMOs – at some point.** Under this scenario, A6.4M credits will be treated as ITMOs at some point in the transfer chain.
    i. <u>If credits are issued into a UN Holding Registry</u> they are not ITMOs, as no international transfer has taken place at this point, and no corresponding adjustment is needed. If they are further transferred from the Holding Registry into another Party's account, views differ:
        1. This is an international transfer and credits become ITMOs, requiring an adjustment in the initial host country, and in the receiving country.
        2. Under this first international transfer the credit is still not an ITMO and no corresponding adjustment is needed.

    While there are different views about the first international transfer, everyone under this scenario seems to agree that the second transfer will make the credit an ITMO and requires a

corresponding adjustment between the first buyer and the second buyer.

ii. If credits are issued in a National Registry, the scenarios for how they are treated for transfer and corresponding adjustment purposes will be similar to a) above. However, not doing a corresponding adjustment at any transfer from the host country registry to a purchasing country will require further elaboration and explanation.

3.4 Overall mitigation

Art 6.4(d) states that the mechanism "*shall **aim** to deliver an overall mitigation in global emissions".* In some views "shall aim" expresses intent, not an obligation to deliver.

A number of issues need to be addressed, and options identified.

3.4.1 How do you achieve Overall Mitigation?

a. **Subjective.** One way of achieving overall mitigation is to use conservative baselines. However, this option, a subjective definition of "conservative", may add additional uncertainty to the uncertainty already present in a counter-factual event, and to the already inherently uncertain exercise of baseline and crediting.
b. **Objective.** An alternative is to clearly define a percentage as the level of actual reduction. This may be done at issuance, during the transfer or at usage towards NDCs (see 3.4.3)

3.4.2 Voluntary or binding?

a. **Voluntary.** The 'shall aim' can be understood as something voluntary. Overall mitigation is a goal, which is desirable for Parties to fulfill, but not a binding one.
b. **Binding/obligatory.** We focus on the "shall" and interpret it as setting an obligation for Parties to deliver overall mitigation when using Art 6.4.

3.4.3. When is Overall Mitigation delivered?

Overall mitigation, could be delivered at three different times:

a. **At issuance.** In that case, not all reductions will be issued as credit for the activity.
b. **During the transfer.** The full mitigation is credited, but the amount is adjusted at the first transfer.
c. **At usage.** In this case, the Party that uses the credit towards its NDC can only use part of what has been transferred into its account. That would

be true for Party compliance. National compliance regimes would be set up by the respective Party, but would have to take into account international arrangements, unless it chooses to make up the difference between what an entity with domestic obligation surrenders to it, and what the Party has to show for NDC compliance.

3.5 Share of proceeds

Contrary to Art 6.2 (see 2.5.3), a share of proceeds is explicitly introduced in the context of Art 6.4 (in Art 6.6). Thus, the debate in this case is not about whether it should be included or not, but how it should be operationalized. Two decisions have to be made:

a. The percentage used for the share of proceeds.
b. The use of the share of proceeds (e.g. Adaptation Fund).

3.6 Eligibility

There may be eligibility considerations, imposing restrictions to which Parties are allowed to participate in Art 6.4.

3.6.1 Registry requirements

a. **Registry required.** One position could be that a Party that wishes to participate in Art 6.4 requires a national registry.
b. **No registry required**. Another position could be that a Party does not require a registry to participate, if it does not intend to transfer-in A6.4M credits.

3.6.2 Inside – Outside NDC

An important issue is whether there can be A6.4M activities outside the scope of a Party's NDC. In this respect, the discussion should mirror the one under ITMOs (see 2.1.5).

3.7 Participation of the private sector

Art 6.4(a) is specific in that it aims to incentivize private sector participation. While the A6.4M is seen as very similar to the CDM, depending on the scope of the participation and the scope of the mechanism, Parties could authorize private sector entities to participate through:

a. **Activity-by-activity authorization.**
b. **Blanket authorization.** Blanket authorization can be used for participation in A6.4M, with individual activities getting approval depending on their nature.

3.8 A6.4M and KP mechanisms

The regulatory credibility of the UN system is seen as being at stake in the way that the new mechanism relates to CDM and JI. In this case, a number of options could be considered:

a. A6.4M is a totally new mechanism and has no relation to the KP mechanisms. In this case, the way CDM/JI are treated will be decided under a totally different agenda item.
b. Grandfather into A6.4M all existing CDM projects, and credits issued from them, until the end of the true up period of KP2.
c. Apply b) above, for projects registered after the entry into force of the PA/after the adoption of the rulebook.
d. All projects registered after the entry into force of the PA/after adoption of the rulebook will be accepted (and credits issued from them) after re-qualification under A6.4M rules.
e. Apply b), c) or d) for Africa, SIDS and LDCs only.

4. User guide

This paper represents the state of play, or as best as we can define it, at this stage. It may not have captured all options, or all subtleties in the options outlined so far. The thinking on these topics, as well as Party positions, will evolve. As such, this paper will change with the times.

We will correct, add, subtract and otherwise make changes to it as we detect new elements and views, or that you will bring to our attention. It is cliché, but we see this as a living document.

Please use this to discover what is out there in terms of ideas and options.