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Corresponding Adjustments: Interpretation of the "Buffer Account"

INFORMAL FORUM ON IMPLEMENTATION OF ARTICLE 6

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This paper is intended to address an issue that has been elaborated a number of times, but continues to re-emerge from some negotiators, namely the issue of "what gets adjusted" under what is generally referred to in the Art. 6 negotiations as the "buffer account approach" for corresponding adjustments.

- The name "buffer account" may be misleading as this name may not convey the true function that it is intended to deliver. A more appropriate name may be "netting account". The number in the netting account provides, at any time, the net ITMOs position (in terms of imports - exports of ITMOs) of that Party.
- In this paper the term "netting account" will therefore be used instead of "buffer account".
- For each Party that participates in Art. 6, a netting account will be set up, which has a starting balance of 0 (zero).
- Every time there is an ITMOs transfer, the netting account in the exporting and in the importing Party will be "correspondingly adjusted" (in or out (+/-)).
- The number in the "netting account" is **an intermediate number.**
- This **intermediate number in the "netting account"** will be used to compare the results obtained in the NDC covered sectors (at the end of the NDC period, or at any time), to the NDC pledge. This will provide information for reporting progress towards achieving the NDC.
- A formula may be of some help in clarifying this:

  NDC pledge = (what was accomplished) +/- (number in "netting account")

  Ex: NDC pledge (emission of 100,000 tons) = 110,000 tons (actual emissions at the end of the NDC) - 10,000 (net imported - exported ITMOs/number in "netting account")

Background

One of the main features of international cooperation that involves the use of International Transferred Mitigation Outcomes (ITMOs) under Article 6 of the Paris Agreement is ensuring environmental integrity.

One aspect of environmental integrity, which is specifically referred to in Art 6.2, but is also part of the ethos of the entirety of Article 6, is the avoidance of double counting. According to 1/CP.21, para. 36, one way to achieve this is through corresponding adjustments.

The operationalization of corresponding adjustments has been one of the hotly debated issues in the negotiations towards producing the rulebook for Article 6. In our view two questions need to be addressed:

- What needs to be adjusted?
- When does the adjustment take place?

These questions are not unrelated, but the focus of this short piece is on **what needs to be adjusted.**

The texts forwarded from Katowice in **Decision 8/CMA.1**[1] provide two options in ***The Katowice Texts, Proposal by the President*** **(KTP)**[2],

> 10. *For ITMOs measured in a metric determined by participating Parties, each participating Party shall consistently apply its corresponding adjustments by effecting an addition or subtraction from a starting point of a zero balance, with a resulting balance that reflects net transfers and acquisitions and is applied to the NDC in accordance with guidance under Article 4, paragraph 13, Article 6, paragraph 2, and Article 13, paragraph 13. The corresponding adjustment shall be effected through an addition for ITMOs transferred and a subtraction for ITMOs acquired.*

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[1] See FCCC/PA/CMA/2018/3/Add.1, Decision 8/CMA.1, p. 22, available at https://unfccc.int/sites/default/files/resource/cma2018_3_add1_advance.pdf#page=22

[2] See FCCC/CP/2018/L.24, Annex V. A., paras. 10-11, p. 34 available at https://unfccc.int/sites/default/files/resource/Katowice%20text%2C%2014%20Dec2018_1015AM.pdf

11. *For ITMOs measured in tonnes of CO2e, each participating Party shall consistently apply its corresponding adjustments by effecting an addition or subtraction to the emissions and removals covered by its NDC, as derived from its national inventory report, and reported pursuant to paragraph VII.B.26(a), resulting in an adjusted balance. The corresponding adjustment shall be effected through [either]:*

. *(a) [An addition of the quantity of ITMOs first transferred and a subtraction of the quantity of ITMOs used;]*

. *(b) [An addition of the quantity of ITMOs transferred and a subtraction of the quantity of ITMOs acquired].*

The approach referred in para 11 adjusts a number, which uses the inventory (of the NDC covered sectors) as a starting point. In this case, the ITMOs need to be denominated in CO2e.

The approach that is referred to in para 10 is generally known as the "buffer account" approach. Although clarified verbally before in multiple informal meetings and negotiations, this paper is an opportunity to provide a written explanation and critique of this approach.

<u>What is the "buffer account"?</u>

The buffer account may not be the best name to use for this approach. A more appropriate name may be that of "netting account". Essentially the netting account nets out the (ITMOs imports – ITMOs exports) every time there is a transfer.

<u>What gets adjusted?</u>

The number in the netting account that gets adjusted has a starting number of 0 (zero), and is denominated in the metric of the ITMOs that was transferred.

The netting account provides an "intermediate" number" which will show, at any time, the "net position" of that Party in terms of its imports and exports of ITMOs.

<u>To illustrate:</u>

If the NDC, and the ITMOs, are in MWH of wind power, then when 10 GWH of wind power are imported, the "netting account" will show +10.

If subsequently, that Party exports 7 GWH of wind power, the netting account will show (+10-7=+3).

<u>When does the netting take place - how is the "netting account" used?</u>

As mentioned above, the "netting account" will, at any time, show the net ITMO position of that Party. On its own however, that number does not show the progress towards accomplishment of the NDC and is an "intermediate number". The "netting account" towards corresponding adjustment is used in two steps:

(1) An adjustment is made at time of any transfer. There is a transfer of an ITMO to another party (shown as a "-" for the transferring party but as "+" for the receiving party). This way a "net position" is always available to the Party

(2) When progress towards the NDC is checked, at any time, including the end of the NDC period. At that time, in order to understand progress/accomplishment of the NDC pledge, the initial NDC pledge together with the number in the netting account is compared to what was accomplished in the NDC covered sectors.

To illustrate again, continuing the simplified equation above, let us assume that at the end of the NDC period the Party had produced 107 MWH of wind power. In its NDC, the Party had pledged a production of 110 MWH. In this case the equation will show:

Promise (110) MWH= Achieved (107) MWH + Netting account = 3.

This would indicate that the NDC pledge has been fulfilled.

Why do we need a "netting account"?

Among the choices of adjustment mechanisms for corresponding adjustments, the reason for supporting the use of the netting account is the fact that it is neutral to the question of what type of NDC the Party in question is using, including metric (CO2e, MWH of renewable, etc).

The ability to use multiple metrics for ITMOs may be seen as being inferred in the Paris Agreement, as NDCs are nationally determined. ITMOs in multiple metrics are also useful for recognizing the multiple ways in which international cooperation can be carried out. The same explanation for the use of a netting account is valid if there are multiple metrics for ITMOs/NDCs. In that case, there will be one "netting" account for each metric.

At time of use, it may be envisaged that any Party that wishes to use ITMOs from an account denominated in a metric other than its NDC, will need to use a conversion factor, reported in a very transparent way through the Art. 13 provisions.

For example, a Party with an NDC that is budget based would use the number in the netting account need to adjust its target upon the use of an ITMO towards its NDC; a Party with an NDC that is emissions based would need to makes a different adjustment when verifying progress towards its NDC by using the netting account to compare the inventory achievement at any time.

The appeal of the netting account must be that the same adjustment approach works in the context of both target-based and inventory-based NDCs.

This allows for the adoption of a common adjustment mechanism by all Parties, and does not suffer from the limitation of either one or the other adjustment depending on the type of NDC. It is therefore, simpler to adopt, follow and consequently translate into the Article 4 accounting process when the final net transfer information is used for such purposes.

A netting account is useful for some purposes and essential for others. A netting account will provide total transparency to the regulator, in real time, of the ITMOs transfer situation and progress towards NDCs. Given the essential role that transparency plays in the Paris Agreement, it is difficult to see validity in any arguments against additional transparency for the regulator.

A netting account is essential if we are to respect the national determined nature of NDCs and in order to allow for ITMOs to be in metrics other than CO2e.