Promoting transformational change through carbon markets

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Objectives of the presentation

- **Present pre-final results of the UBA research project "Strengthening the transformative effect of markets approaches under the Paris Convention"**

  - How can transformational change be promoted through Article 6?

  - Role of regulatory and monetary incentives in driving transformation

  - Identification of Article 6 specific transformation characteristics and their application in three different Article 6 case studies in Morocco's waste sector, Costa Rica's transport sector and Pakistan's energy sector

- **Literature analysis, case studies and consultations with international experts**

- **Preparation of the main publication of research project (Q1/2022)**

Definition of transformational change through carbon markets

"A fundamental, sustained change of a system that ends established high-carbon practices and contributes to a zero-carbon society, in line with the Paris Agreement goal to limit global warming to 1.5-2°C and the United Nations Sustainable Development Goals."

Characteristics of transformational change through Art.6, inspired by ICAT

➢ **Large scale**, **system-wide impacts**, including through multiple smaller changes
➢ **Sustained, long-term outcomes** that reinforce zero-carbon practices
➢ **Technology change** – R&D, early adoption and widespread scale-up of clean technologies
➢ **Agents of change** – cross-cutting coalitions & networks incubate transformational change
➢ **Incentives for change** – long-term, adaptive policies and practices, consistent over long periods
➢ **Norms and behavioural change** – influence awareness and behaviour to drive long-lasting change in societal norms and practices

Conceptual options for strengthening transformational impact

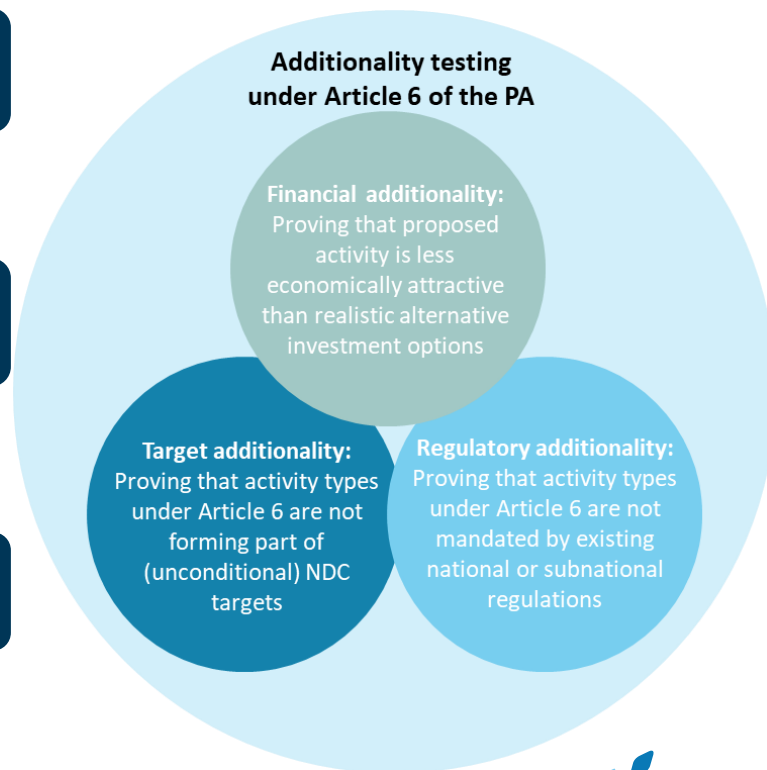**Mitigation outcomes at scale, sustained over time**

- **Redefine additionality for all activities** in light of NDC
- Promote **shift to upscaled activities** (incl. policies)

SDG outcomes at scale, sustained over time

- **Enhancing MRV systems for SD impacts** to achieve a market differentiation
- Developing a **revised SD Co-Benefits tool** for the A6.4M

Technology change and digitalisation

- **'High-hanging fruit'** be supported by carbon finance
- **Crediting periods adjusted to technologies** (shorter)
- **Digitalisation** as enabler of MRV frameworks, payments

Additionality testing under Article 6 of the PA

Financial additionality: Proving that proposed activity is less economically attractive than realistic alternative investment options

Target additionality: Proving that activity types under Article 6 are not forming part of (unconditional) NDC targets

Regulatory additionality: Proving that activity types under Article 6 are not mandated by existing national or subnational regulations

Strengthening transformational impacts through baselines

Normative change: Reflecting global mitigation aspirations in baselines

- **Performance-based benchmarks** for stringent baseline setting
- More **dynamic baseline setting**
  - Option 1: Issuance against ex-post calculations
  - Option 2: Baseline emissions intensity decreases through applying **ambition coefficient**

Practical implications of moving towards dynamic & stringent baselines

Incentives

Less carbon credits requires higher prices to remain attractive for project developers

Predictability

Project developers require certainty about expected revenues for taking investment decisions

Resources and capacity

Developing BAT benchmarks and SB is resource-intensive → Technical assistance and institutional capacity building

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Conceptual options for safeguarding transformational impact

Safeguards have not been widely applied in carbon market mechanisms, but are crucial to prevent compromising NDC ambition and integrity

- **Safeguards against negative impacts on sustainable development**
    - MRV infrastructure, minimum SD requirements, negative lists, impact assessments at different stages of development etc.

- **Safeguards against overselling, e.g. non-additional MOs or 'low-hanging fruit'**
    - Retaining a share of MOs by host country (considering overall costs if the marginal cost of a specific mitigation activity is lower than the marginal cost of meeting the NDC goal

- **Safeguards against perverse market incentives on NDC** formulation
    - Prevent generation of 'hot air' through **stringent additionality/baseline setting**

- **'Outside NDC' activities and perverse incentives not to expand NDC scope**
    - Inclusion in NDC updates, stringent additionality test/baseline setting on activity level

Article 6 pilot case studies

🇲🇦 **Morocco: Organic Waste to Energy activity**

🇨🇷 **Costa Rica: Modal shift to non-motorized transport (biking and walking)**

🇵🇰 **Pakistan: Competitive renewable energy auctions**

➢ **Art.6 piloting remains at design stage and thus does not yet allow conclusive assessment on TC impacts**

- All pilots build on SDG priorities, but do not yet consider safeguards
- Baseline approaches remain not clearly defined
- Procedures for GHG accounting not yet agreed

Conclusions

- **Carbon markets should serve to increase ambition: TC requires a practical incentive structure which also provides safeguards against negative impacts**

- **Carbon market rules & methodologies provide an important knowledge-base and toolkit, but need to be updated to achieve ambition and integrity required for TC**

  - Additionality needs to be reconsidered against NDC, positive lists established

  - Baseline setting needs to stringent and dynamic (e.g. ambition co-efficient)

  - Differentiation by host countries to ensure equitable access to carbon revenues

- **Both monetary and regulatory incentives needed to support "high-hanging fruit" activities through Art.6, and to cultivate political will to undertake cost-efficient mitigation options domestically**

- **Market participants need a transparent, predictable market environment that rewards SDG benefits**

Thank You!

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