
# Opportunities for mobilizing private climate finance through Article 6

**SB50 Side Event,** Bonn, 19 June 2019

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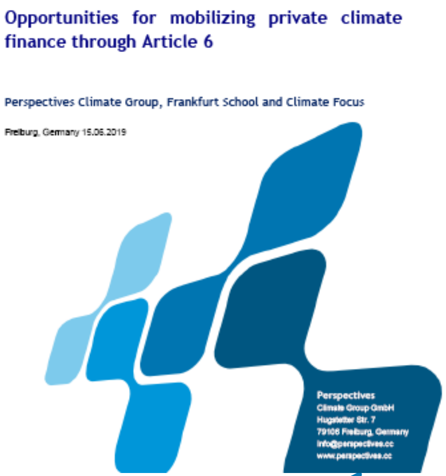
Based on recently released study: Michaelowa et al. (2019) Opportunities for mobilizing private climate finance through Article 6, Perspectives Climate Group, Frankfurt School and Climate Focus

# Agenda for this side event

## Session 1: Key lessons on mobilizing private finance through Article 6

- **Axel Michaelowa (Perspectives/University of Zurich):** Driving private sector credit demand- designing national level policy instruments
- **Ulf Moslener (Frankfurt School):** Scaling-up credit supply balancing between environmental integrity and low transaction costs
- **Lieke 't Gilde (Climate Focus):** Promoting rural electrification in Nigeria through Article 6: A Swedish Energy Agency Virtual Pilot


Opportunities for mobilizing private climate finance through Article 6

Perspectives Climate Group, Frankfurt School and Climate Focus

Freiburg, Germany 15.06.2019

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# Agenda for this side event

## Session 2: Designing Article 6 rules that allow for private sector mobilization

- **Axel Michaelowa:** Moderation of panel discussion with:
  - **Simon Henry**, IETA
  - **Sara Sundberg,** SEA

# Context and scope of the study

- **Article 6 as gap of the PA rulebook:** **to be finalized by COP25 in December 2019**
- **Mobilizing private finance at scale is key to meet the Paris Agreement objectives of Article 2.1a-c**
  - There are two key provisions in the PA related to mobilization of private finance: Article 2.1c and Article 9.
  - ➢ The former looks more generally into consistency of financing investments with the long-term ambition of the PA, the latter into climate finance flows from industrialized to developing countries, including private finance mobilized by public interventions.
- **This study applies a multi-level analysis to the question how Article 6 mechanisms can mobilize private finance and help achieve Art.2.1c, looking both at ITMO / credit demand and supply**

# The role of Article 6 in mobilizing private climate finance

- In order **to achieve low carbon investment levels** consistent with the long-term ambition of the PA and Article 2.1c, several trillion USD are required annually
- The **100 billion USD per year climate finance mobilization** commitment is a small fraction of this investment need and already includes mobilization of private finance. **Definition of what constitutes such finance is heavily contested**
- Governments need to introduce **domestic policy instruments** to generate a shift of private finance towards low carbon investments
- Article 6 mechanisms can play a decisive role in the mobilization of the private sector as proven by the **market mechanisms under the Kyoto Protocol**, particularly the CDM
- The **price of emissions credits** is a crucial determinant of private sector engagement in market mechanisms

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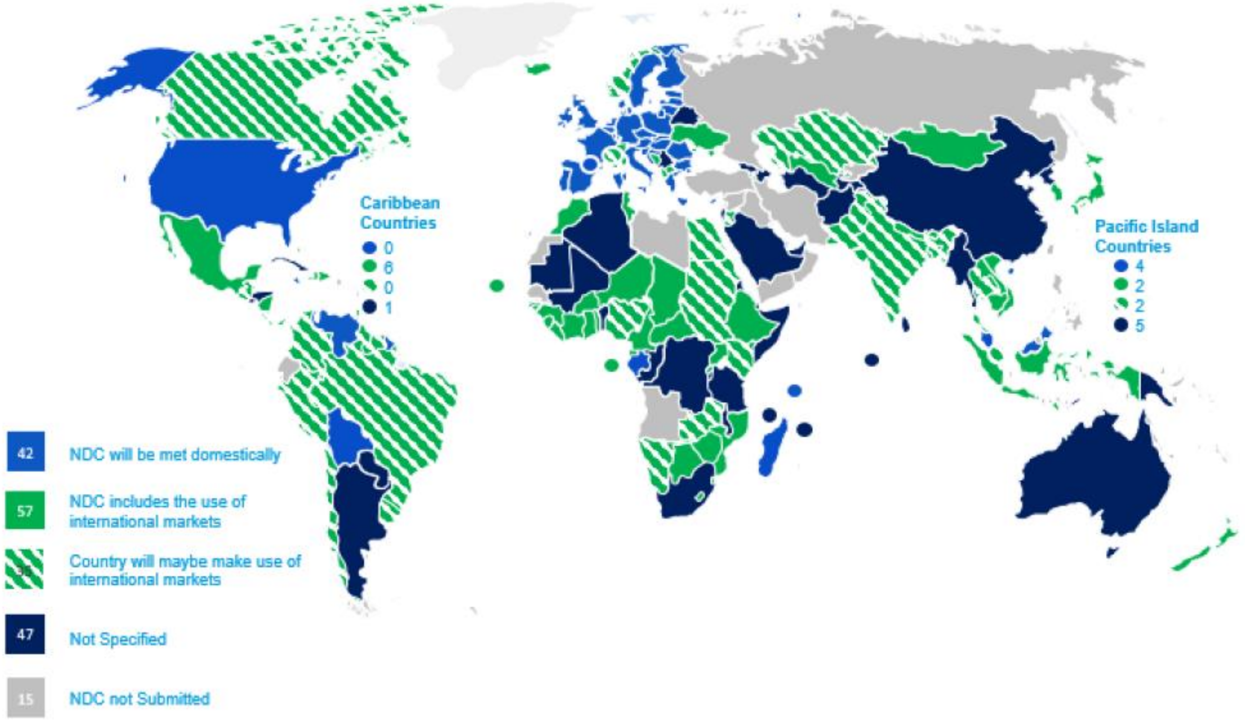
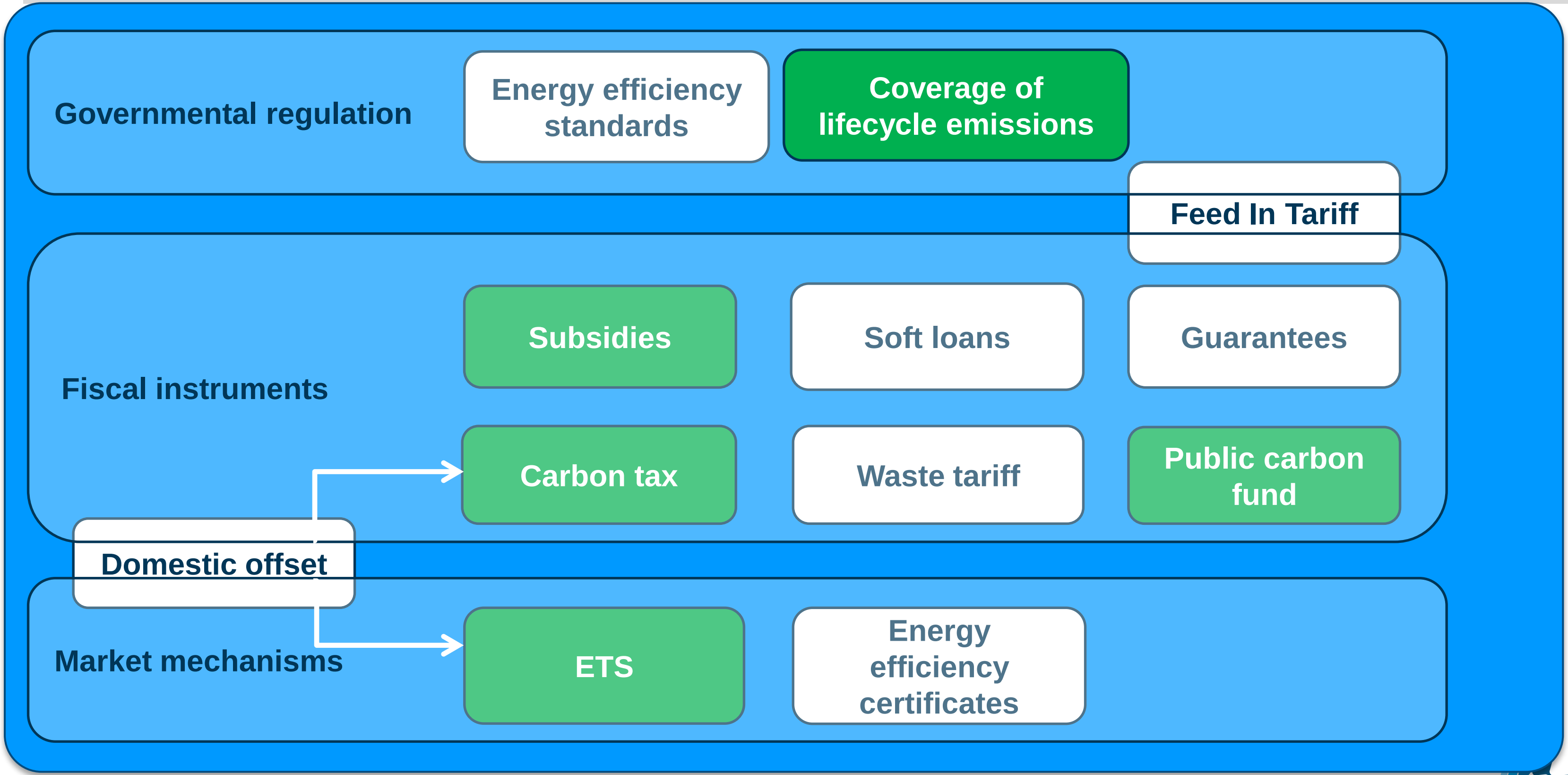
# Many NDCs foresee the use of international market mechanisms




Source: IETA (2018)

# Policy instruments that could mobilize Art. 6 demand



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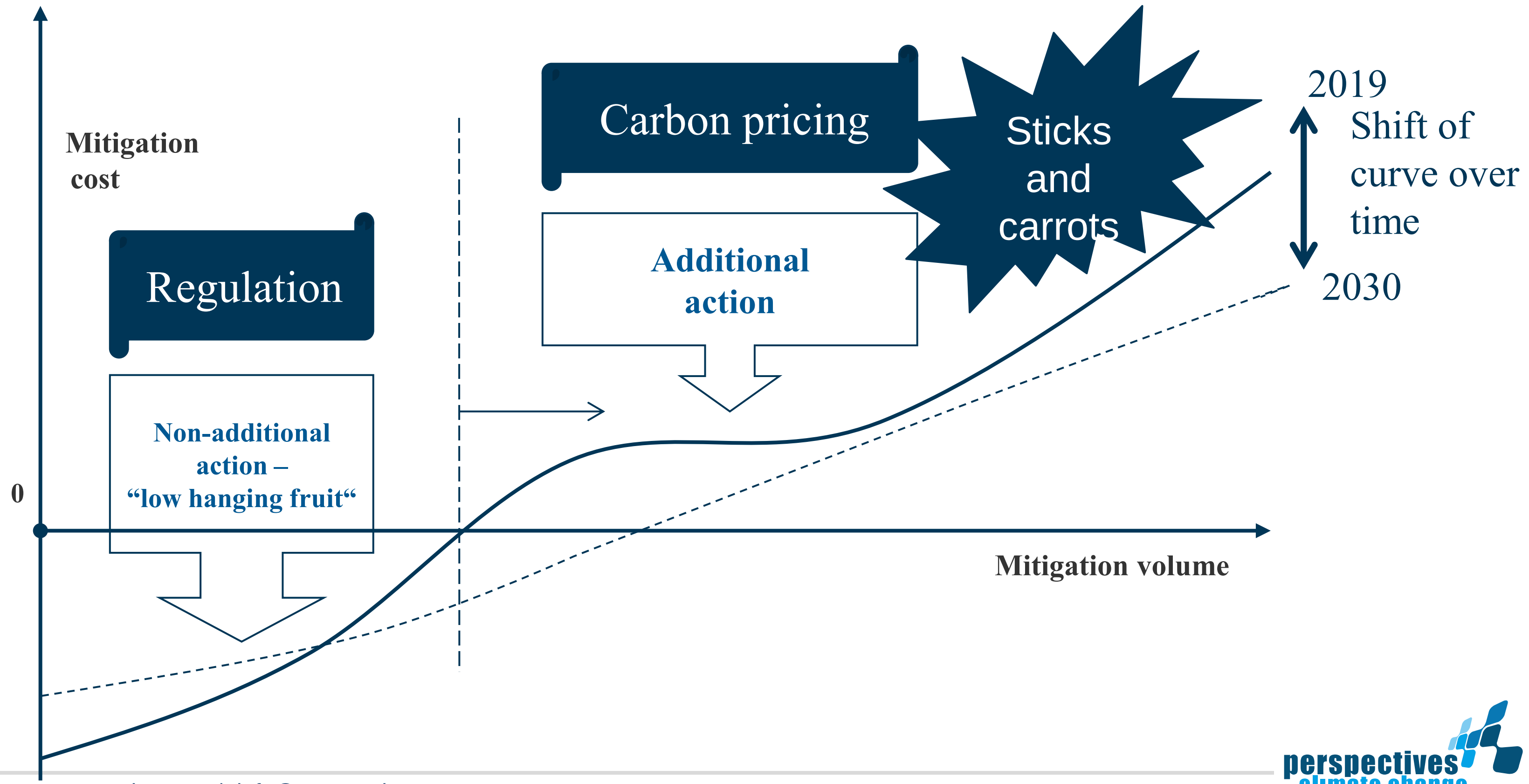

# The role of national level policy instruments for Article 6

- A range of countries, including several developing ones, already accepts units from international market mechanisms, but the total demand volume generated is still much less than demand from the EU for CDM credits prior to 2013
- National level policies accepting ITMOs/A6.4ERs are crucial incentives for private sector activities under Art. 6.
  - Key to mobilize the willingness of financial institutions to provide loans for such activities
- Accepting Art. 6 units will lower the revenues from national carbon pricing policies
  - Limiting eligibility to certain transferring countries or technologies, or to a certain percentage of the obligation has widely been used to protect revenues, but reduces the incentive for the private sector.

# National policy instruments driving demand for Art. 6 units

## Historical and *current* examples for use of international units

- **Regulation**
  - EU fuel quality directive – *acceptance of CERs*
- **Fiscal instruments (“sticks”)**
  - Carbon tax (Colombia, South Africa) – *surrender offsets instead of paying tax*
- **Fiscal instruments (“carrots”)**
  - Subsidy for offsets - *Australian Emission Reduction Fund*
- **Market mechanisms**
  - Emission trading scheme – EU acceptance of CERs

→ Such policies could also become main drivers of demand for Article 6 units

# National level policy instruments to generate supply for Article 6

- **National level policies** can be used to **mobilize** private sector mitigation that can then generate **ITMOs to be sold by the government**
- In the context of NDC achievement, host country strategies and policy design will become crucial for **environmentally sound** supply in the market
- **Government could retain the revenues** to cover **costs** of "**carrot**"-type policies
- **Government could pass on the revenues** to private sector entities mitigating emissions under a "**stick**" type policy like a carbon tax or regulation

# Thank you!

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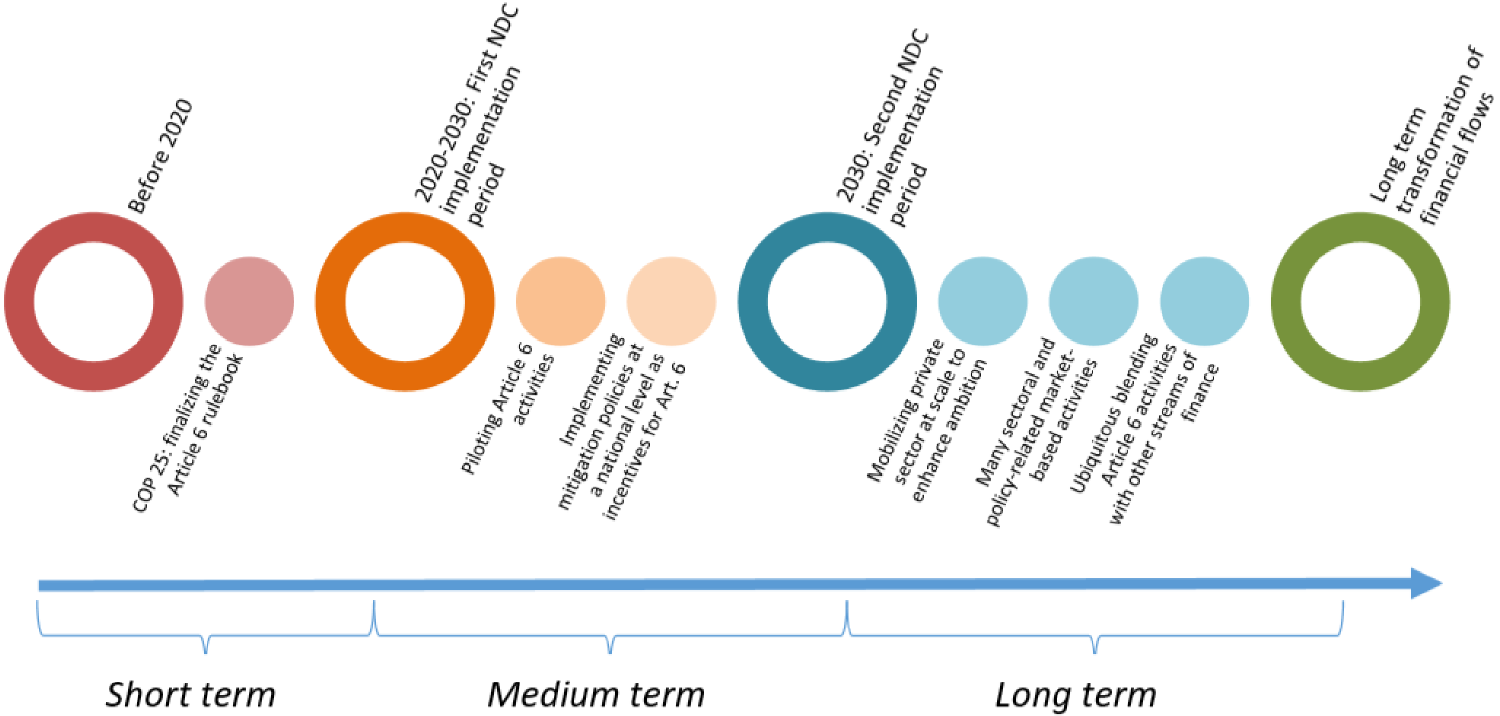
# Generic preconditions for private sector engagement

- **Importance of drawing on experiences with the Kyoto Protocol and its three international market mechanisms (CDM, JI and international emissions trading)**
- **Need to overcome tension between regulators and private sector players by blending public climate finance with revenues from ITMO generation**
  - Clear approach required to allocate mitigation results to the two strands of financing
- **Private sector investment requires a robust regulatory foundation and political willingness to act**

# Timing of interventions to mobilize private sector

- short term: Development of credible additionality tests that do not entail high transaction costs, combined with credible and effective audit procedures, as well as diffusion of domestic policy instruments that accept ITMOs/A6.4ERs as offsets.
- medium term: Blending of public climate finance with private Article 6 activities needs to be tested, and agreement on attribution of mitigation found.
- long term: Ways to align Article 6 with 1.5°C compatible emissions pathways and rising ITMO/A6.4ER price paths need to be explored.

# Private sector mobilization through Article 6 of the PA over time



# Combining Art. 6 with public climate finance

## Key messages:

- **Results-based climate finance can lead to demand for ITMOs that are subsequently cancelled.**
- **Blending of ITMO revenues with public climate finance is important to mobilize higher-cost private sector mitigation. However, in order to prevent double claiming, ITMOs should be issued for the share of the total financing of the activity provided by the ITMO sales revenue**

# Setting Article 6 rules to enable private finance mobilization

Key messages:

- **Private sector participation in market mechanisms will be the higher:**
  - **the lower transaction costs (including taxes)**
  - **the lower government interference**
  - **the broader the scope of eligible activities**
  - **The more lenient baselines and additionality determination**
  - ➢ There is a clear tradeoff with environmental integrity regarding the first and the last points regulators need to address. Negotiators need to see where to position themselves regarding this tradeoff.
- **Article 6 mechanisms are likely to have stronger government involvement than the CDM, which may reduce private sector engagement**
- **Some activity developers' trust in the long-term stability of Article 6 mechanisms will be reduced if registered CDM projects and credits cannot be transitioned into Article 6**

# Research questions on rules for Article 6 conducive for private sector participation

**1. Creating a framework conducive for private sector engagement**

- Defining the role of the private sector in the governance framework of both cooperative approaches and the centralized Art.6.4 mechanism
- Reducing private sector transaction costs without threatening environmental integrity

**2. Incentivizing up-scaled supply of mitigation outcomes while preserving environmental integrity**

- Preserving trust in market-based mechanisms through a transition of CDM and JI
- Defining the scope of activities eligible for crediting
- Setting robust baselines while striving for standardization
- Determining additionality of activities in the context of the NDCs
- The impact of taxes on market mechanisms - share of proceeds and overall mitigation

**3. Allowing for enhanced private sector demand beyond NDCs**

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