

## Governing Cooperative Approaches under Art. 6.2 of the Paris Agreement

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Katowice | 11 December 2018

# Flow of the Presentation

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2. Mandate for Guidance on Article 6.2
3. Negotiating Issues at Stake
4. Alternative Visions for Guidance on Article 6.2
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# Full Report and Summary

Harvard Project on Climate Agreements  
Discussion Paper ES 2018-8  
November 2018

Available at:

<https://bit.ly/2Qlut87>



# Role of Article 6.2 of the Paris Agreement (I)

- Article 6.2 allows Parties to cooperate in mitigation and use Internationally Transferred Mitigation Outcomes (ITMOs) to meet their Nationally Determined Contributions (NDCs)
- Although Article 6.2 avoids market terminology, it is widely seen as the “latest incarnation” of market approaches in international climate cooperation (together with Art. 6.4)
- Importantly, the aim of such voluntary cooperation is to help lower the cost of achieving mitigation pledges as well as collective temperature stabilization targets

# Role of Article 6.2 of the Paris Agreement (II)

Holding everything else constant, the ability to achieve mitigation at lower cost should facilitate an increase in overall ambition:

- *More mitigation per unit of investment:* market channels resources to the most cost-effective abatement options
- *More investment for mitigation:* unused resources can be invested towards additional abatement efforts
- *Lower political barriers:* reduced costs can lower political resistance against more ambitious future pledges

# Role of Article 6.2 of the Paris Agreement (II)

Holding countries to their commitments under the Paris Agreement requires mitigation at lower costs than otherwise, which is a challenge for developing countries:

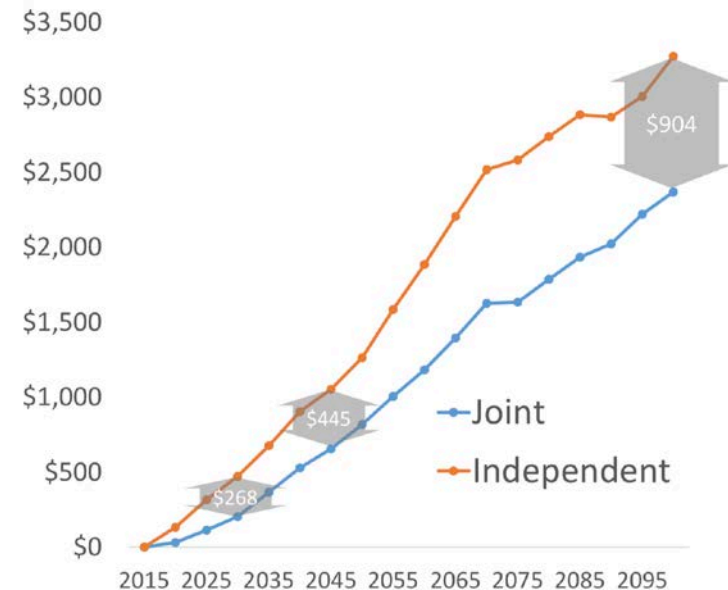
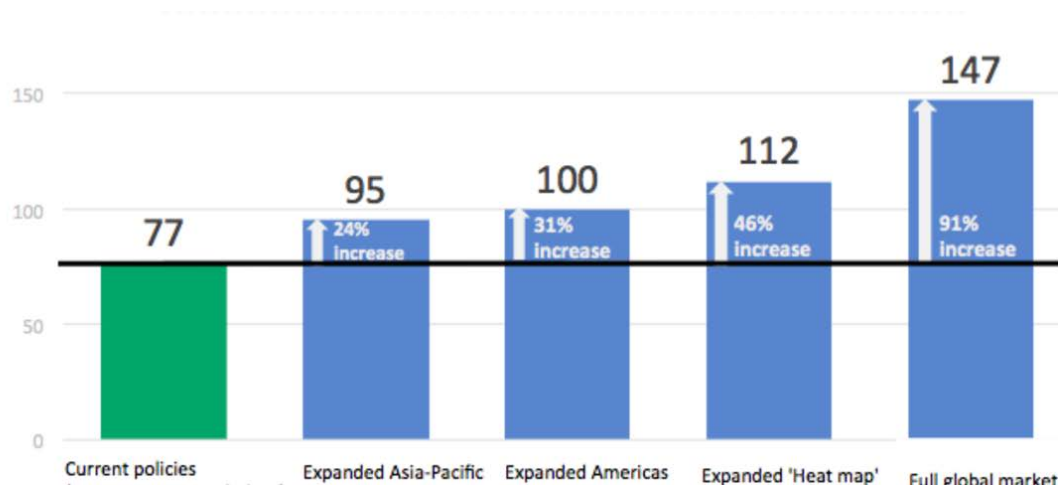
- Market-based mechanisms can help reduce costs, but they are not sufficient
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resistance against more ambitious future pledges

# Estimates of Cost Reduction & Ambition Potential

Estimates vary, but consistently suggest large potential benefits:

- Yu et al. (JGCRI), 2018: 35% cost reduction (\$445 billion) by 2050
- World Bank et al., 2016: 54% (\$3.9 trillion) by 2050
- EDF, 2018: 59-79% by 2035, allowing an ambition increase of 91% between 2020 and 2035



# Negotiating Guidance for Article 6.2 (I)

- Negotiators are engaged in elaborating the “Paris Rulebook” setting out operational details for the Paris Agreement
- One element of this Rulebook is “guidance” on implementation of Article 6.2, based on a mandate in Article 6.2 and Decision 1/CP.21 adopting the Paris Agreement
  - *Agenda item 11(a) of SBSTA 49*
- Adoption of the outcomes of this process – the Paris Agreement Work Program – is mandated for COP24, with some unresolved issues deferred to the 2<sup>nd</sup> Session of CMA



# Negotiating Guidance for Article 6.2 (II)

- Mandate for elaboration of guidance on Article 6.2 leaves considerable discretion to Parties

# Negotiating Guidance for Article 6.2 (II)

## Article 6.2 of the Paris Agreement:

*“Parties shall, where engaging on a voluntary basis in cooperative approaches that involve the use of internationally transferred mitigation outcomes towards nationally determined contributions, promote sustainable development and ensure environmental integrity and transparency, including in governance, and **shall apply robust accounting** to ensure, inter alia, the avoidance of double counting, **consistent with guidance adopted by the Conference of the Parties serving as the meeting of the Parties to this Agreement.**”*

# Negotiating Guidance for Article 6.2 (II)

- Mandate for elaboration of guidance on Article 6.2 leaves considerable discretion to Parties

# Negotiating Guidance for Article 6.2 (II)

## Paragraph 36 of Decision 1/CP.21:

*“Requests the Subsidiary Body for Scientific and Technological Advice to develop and recommend the guidance referred to under Article 6, paragraph 2, of the Agreement for consideration and adoption by the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement at its first session, **including guidance to ensure that double counting is avoided on the basis of a corresponding adjustment by Parties for both anthropogenic emissions by sources and removals by sinks covered by their nationally determined contributions under the Agreement.**”*

# Negotiating Guidance for Article 6.2 (II)

- Mandate for elaboration of guidance on Article 6.2 leaves considerable discretion to Parties
- Discretion also relates to the level of prescriptiveness in governance of Article 6.2, including in relation to flexibility and issues of environmental integrity and mitigation ambition

# Negotiating Guidance for Article 6.2 (II)

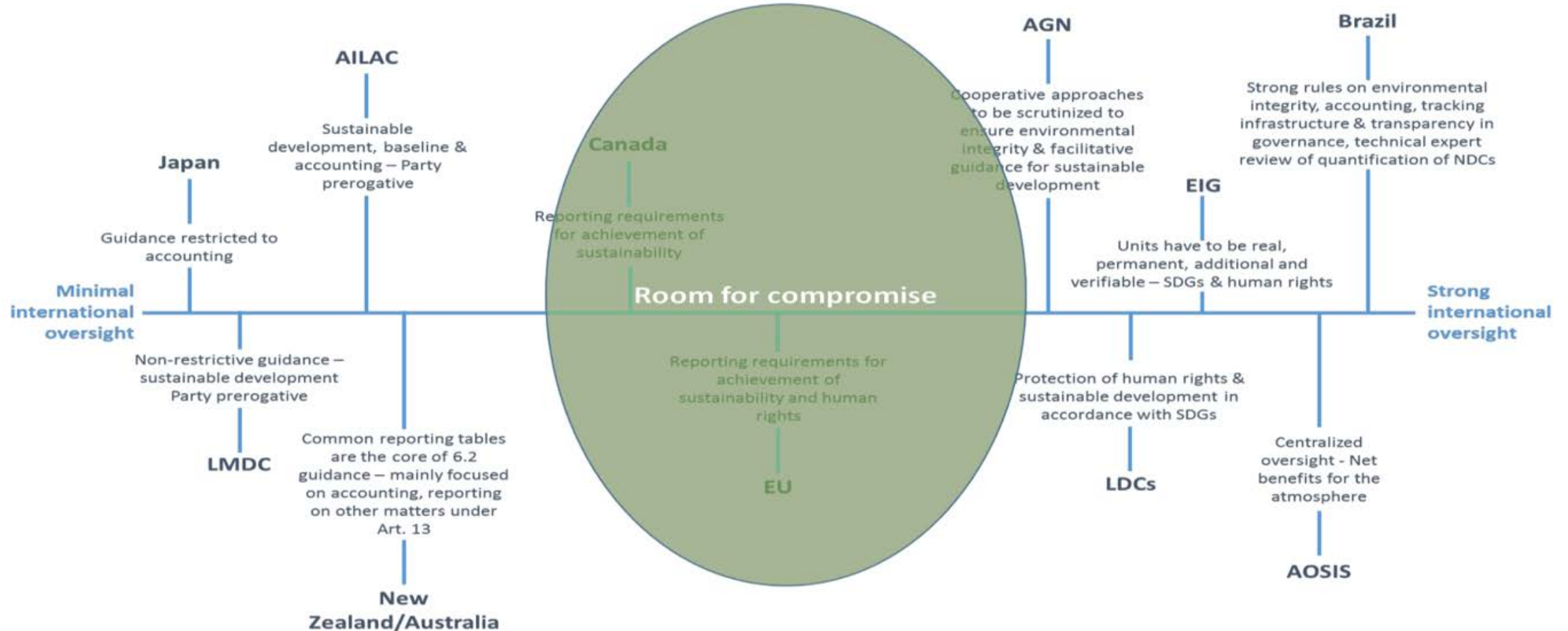
[Negotiating text](#), Version 2 of 8 December 2018, 10:00, Annex:

- Para. 1: Definitions
- **Paras. 3-9: (Institutional) governance**
- **Para. 10: Participation responsibilities**
- Para. 11, 44-51: Tracking, infrastructure
- Paras. 12-15: Corresponding adjustment
- Paras. 23-43: Reporting, review, recording
- **Para. 52: Safeguards and limits**
- **Para. 53: Overall mitigation in global emissions**
- Paras. 54-57: Share of proceeds for adaptation

# Negotiating Guidance for Article 6.2 (II)

- Mandate for elaboration of guidance on Article 6.2 leaves considerable discretion to Parties
- Discretion also relates to the level of prescriptiveness in governance of Article 6.2, including in relation to flexibility and issues of environmental integrity and mitigation ambition
- Party positions have fallen along a spectrum of preferences between prescriptiveness and flexibility, expressed in the degree of central oversight and role of ambition

# Negotiating Guidance for Article 6.2 (II)



Source: Greiner, Sandra, and Axel Michaelowa. 2018. [Cooperative Approaches under Art. 6.2 of the Paris Agreement: Status of Negotiations – Key Areas of Consensus and Contention.](#)



# Alternate Visions for Governance of Article 6.2 (I)

At opposite ends of the spectrum, Parties could exercise their discretion in negotiating Article 6.2 guidance to:

- Create a highly decentralized system, in which guidance is limited to accounting issues and leaves matters of environmental integrity and oversight to Parties (*“bottom up”*)
- Agree on more centralized governance, with material restrictions and institutional oversight (*“top down”*)
- International law is a permissive system: what is not governed multilaterally by express conferral of national sovereignty remains a prerogative of Parties (*S.S. Lotus*)

# Alternate Visions for Governance of Article 6.2 (II)

**Why does this matter?** Defensible arguments for each view:

- For “*Bottom-up*”: excessive regulation can limit uptake of cooperative approaches and thereby curtail benefits, e.g.:
  - Onerous conditions and procedural requirements increase transaction costs and investor risk
  - Some restrictions limit or preclude participation altogether
  - Wording of Article 6.2 does not set out a mandate for prescriptive governance

# Alternate Visions for Governance of Article 6.2 (III)

- For “*Top-down*”: insufficient regulation risks allowing cooperative approaches that increase overall emissions, e.g.:
  - Transferred ITMOs have questionable environmental integrity, for instance due to “hot air”, or are not properly accounted for
  - Because all countries now have pledged mitigation, they may be incentivized to weaken future NDCs (dynamic inefficiency)
  - Mandate for guidance has to be interpreted in light of the object and purpose of the Paris Agreement (Article 31 VCLT)
- What is the right balance of prescriptiveness and flexibility?

# Insights from Theory

## Market Failure and Government Failure

- Climate policy is justified by different market failures; market-based approaches are a particularly cost-effective option
- Robust enforcement of rights & obligations and transparency of emissions & transactions are critical for functioning markets
- Particularities of carbon markets render them susceptible to price volatility and strategic and fraudulent behavior
- That justifies regulation of carbon markets, but such regulation is itself subject to cognitive, administrative and political failures

# Case Study: Kyoto Protocol

- Limited market activity in international emissions trading (Art. 17) due to exclusion of private sector from participation
- Individual project approval under the CDM (Art. 12) contributed to high transaction costs, delays & regional/project type bias
- Various regulatory failures in the approval and verification process have damaged reputation and increased investor risk
- Complex and continuously evolving “additionality” test has still proven unable to prevent registration of non-additional projects
- Yet no evidence that CDM negatively influenced climate policy adoption in developing countries (no perverse incentive)

# Case Study: EU ETS

- Prolonged price weakness and periodic price volatility
    - Lack of emissions data in Phase 1 (information asymmetry)
    - External factors in Phases 2 and 3 (CER use, complementary policies, economic downturn)
  - Series of criminal activities 2009-2012:
    - Value-added tax fraud (“VAT caroussell”), account phishing and allowance theft, use of recycled CERs
- Multiple regulatory reforms with greater degree of centralized management, strengthened market oversight and ongoing allowance supply management

# General Takeaways (I)

- Carbon trading theory and experience affirm the need for robust governance in transparency of emissions, accurate accounting of transfers, as well as avoidance of market power and abuse
- Theory and case studies also highlight the need to avoid overly restrictive governance with high transaction costs, investor risk, and uncertain benefits, e.g. individual approval of ITMOs
- Quantity limits on transfers will proportionally curtail the economic benefits of trading, and thus impose commensurate limits on any potential cost savings and potential ambition

# General Takeaways (II)

- Essential governance aspects such as definitions, accounting, and corresponding adjustments should feature in guidance, with precise language and – where appropriate – mandatory terms
- Optional or aspirational terms are preferable for other items to safeguard the flexibility of Parties and an efficient res. allocation
- Safeguards & limits as well as overall mitigation requirements should be used with caution, as they suffer from their own cognitive, administrative and political failures



# General Takeaways (III)

- Some issues may defy a regulatory solution, e.g. additionality tests, yet contribute to transaction costs and project risk
- Some concerns may also be misplaced, such as fears of a dynamic incentive to weaken future mitigation pledges
- Private sector participation can greatly increase market activity, liquidity, and efficient price discovery
- Standardization of metrics and other parameters may help streamline cooperative approaches and increase fungibility of traded units, pot. accelerating emergence of a global market

# General Takeaways (IV)

- Ambition is not mentioned in Article 6.2, but the broader context of Article 6 as well as the object and purpose of the Paris Agreement allow for its consideration in guidance
- Still, lacking ambition of NDCs should not be compensated with greater restrictions on cooperative approaches, as this may impede their uptake even if NDCs are eventually strengthened
- Guidance that reflects the multiple balancing acts struck in the Paris Agreement will also find a solid basis in the negotiating mandate of Article 6.2, and offer resilience against challenges

# Takeaways Related to the Latest Negotiating Text

## Negotiating text, Version 2 of 8 December 2018, 10:00, Annex:

- Paras. 3-9: **(Institutional) governance**  
No mention of approval; [non-Party actor participation]
- Para. 10: **Participation responsibilities**  
Only Parties eligible; but potentially circumvented w. [para. 9?]
- Para. 52: **Safeguards and limits**  
[Transfer limits, minimum holding requirements, supplementarity, maximum limits on ITMO use, carry-over & other limits]
- Para. 53: **Overall mitigation in global emissions**  
Automatic cancellation/discounting: [shall/should]/none

# Thank you for your attention!

*Questions? Please ask, or contact me at:*

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