SUBMISSION BY US CLIMATE ACTION NETWORK
IN RESPONSE TO THE NOTE BY THE CHAIRMAN OF THE
CONTACT GROUP ON MECHANISMS

US Climate Action Network (USCAN) appreciates the opportunity to prepare an NGO submission that will be posted on the UNFCCC website. USCAN is a coalition of some thirty-five US environmental NGOs committed to limiting human-induced climate change to ecologically sustainable levels.

The flexibility mechanisms must be governed by strong rules that guarantee the environmental integrity of the Kyoto Protocol. USCAN is submitting these detailed comments and recommendations to help ensure that this happens. The mechanisms will only be a valid option if they benefit the environment, are institutionally independent, transparent and verifiable. In their decisions at COP6, it is essential that Parties not allow the mechanisms to become loopholes that permit the most developed countries to evade taking aggressive domestic action.

The following USCAN recommendations are aimed at producing strong rules that ensure global GHG reductions and meaningful progress towards the ultimate objective of the UN Framework Convention. The recommendations follow the structure and paragraph numbering of the *Note by the Chairman of the Contact Group on Mechanisms* distributed at COP5 on November 5, 1999.[1]

[1] These recommendations represent the views of the vast majority of USCAN members. Some members, however, do not support the use of market-based mechanisms to mitigate climate change.

PART II: ARTICLE 6 JOINT IMPLEMENTATION

I. NATURE AND SCOPE

A. Purpose

Comment: *The purpose of JI should be to supplement the domestic measures implemented by developed countries to reduce their domestic GHG reductions.*

C. Supplementarity

Para. 27 – Limits on acquisitions

Comment:

- *Rules defining the "supplemental" role of emissions trading and joint implementation must be quantified and verifiable. The vast majority of Climate Action Network members believe that placing a quantitative cap on the use of the flexibility mechanisms is crucial to ensuring the environmental integrity of the system.*
- *Rules governing JI among current and future Annex B parties must ensure that net global emissions are no higher than they would be in the absence of JI.*

Para. 28 – Limits on transfers

Comment: *USCAN supports Option 1.*

D. Participation

Para. 29 – Eligibility rules for participation in JI

Comment*: Our suggested text adapts the language proposed as Option 2. This is preferable to Option 1, which would restrict JI ERU transfers (not participation) only upon a formal finding of non-compliance. Subparagraph (c) is offered on the condition that an eligibility function for mechanisms participation is established under the compliance system. The national registry language of subparagraph (d) is taken from Option 1.*

Suggested text:

A Party included in Annex I may transfer or acquire ERUs from an Article 6 project only if the Party:

(a) Has ratified the Protocol;

(b) Is bound by a compliance system adopted by the COP/MOP;

(c) Is entitled to participate in Article 6 according to the procedures and mechanisms regarding eligibility established under the compliance system, which shall include, but are not limited to:

(i) compliance with Article 12 of the Convention,

(ii) compliance with Articles 5 and 7 of the Protocol; and

(d) Maintains a national registry in accordance with the provisions of this [annex] and any related rules or guidelines established by the COP/MOP.

Para. 30 – Whether Parties can develop their own rules or guidelines for their own participation and for the participation of their private entities

Comment*: Our suggested text fine tunes the language in the Chairman's Paper to assure that the rulemaking powers of individual Party participants are limited in scope.*

Suggested text:

Any Party included in Annex I participating in an Article 6 project may develop rules or guidelines governing its participation in the project, and/or the participation of its legal entities, provided that any such rules or guidelines do not conflict with the terms of this [annex], the Convention, the Protocol, or rules or guidelines established by the

COP/MOP. Participation of legal entities in Article 6 projects does not affect the responsibility of Parties included in Annex I to fulfill their commitments under the Protocol.

E. Share of Proceeds

Para. 33- Share of proceeds defined
Comment: *USCAN supports Para. 33. Levying a fee for adaptation and administrative costs on all Kyoto Mechanisms will help correct the current competitive disadvantage of the CDM, as well as the failure of markets to generate projects in the least developed countries.*

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Project Approval/Validation

Para. 34 – Types of projects that may be approved

Recommended additional text:
(c) be designed so as to minimize the risk of greenhouse gas emissions leakage, including the displacement of emissions to other sites within the country and outside the country. In some cases, leakage will be prevented through the adoption of a large project boundary.

Comment:
- *Large hydro, coal and nuclear projects should be categorically excluded from the JI project portfolio.*
- *USCAN recommends that the COP/MOP develop an approach that ensures that those technologies and activities that are most clearly additional receive priority treatment and expedited baseline review. For example, technologies that involve very low or zero GHG emissions, i.e., wind and solar technologies, would face a simpler registration process utilizing standardized baseline rules.*

Para. 35 – Terms of project validation
Comment: *USCAN supports Option 2.*

Recommended additional text:
Any Party, or public or private entity, may raise questions at any stage of the JI process regarding the implementation of a project. Such questions must be supported by corroborating data and should be submitted to, and considered by, the entities responsible for verification and auditing of the project.

Comment: *To ensure the long-term integrity of JI projects, stakeholders must be involved throughout the lifetime of the project.*

Para. 37 – Early commencement of JI
Comment: *If the Parties allow JI to commence at the same time as the CDM, any ERUs generated by JI projects before 2008 must be subtracted from the assigned amount of the host country, as required by Article 3.11.*

B. Project Monitoring

Para. 38bis – Monitoring data
Comment: USCAN supports Para. 38bis.

C. Project Verification

Comment: *USCAN urges that this section be maintained in some form.*

Recommended additional text:

Para. __: Verification procedures should incorporate the full range of stakeholders, including local NGOs, affected communities and indigenous peoples, and should build on experiences of the AIJ pilot phase. The methodologies for verification shall account for additionality and baselines.

D. Certification/Issuance of ERUs

Para. 41 – Rules for certifying/issuing ERUs

Comment: *We support the certification requirements of Option 3. USCAN believes that JI projects should be subject to the same criteria for certification, additionality and verification as CDM projects.*

Recommended additional text:

Para. __: ERUs may only be issued for emissions reductions or removals after they have occurred and been certified by an approved independent entity.

E. Issues Related to Compliance

Para. 44 – Restrictions on use of ERUs when compliance issues are raised; triggers

Comment: *Our suggested text is based upon Option 1, which is taken from the text of Protocol Article 6.4. However, we have made additions to incorporate the compliance system's eligibility function into the trigger, and to assure that "resolution" of a compliance issue will not result in bad ERUs being redeemable.*

Suggested text:

If a question of compliance by a Party included in Annex I with the requirements referred to in Article 6 or [these rules/this annex] is identified in accordance with the relevant provisions of Article 8 or the procedures and mechanisms regarding eligibility established under the compliance system, transfers and acquisitions of ERUs may continue to be made after the question has been identified, provided that any such units may not be used by a Party to meet its commitments under Article 3 until the issue of compliance is resolved. The resolution of an issue of compliance may include the voiding of ERUs derived from projects whose emissions reductions or removals were called into question by the issue of non-compliance.

Para. 44bis – Resolution of Article 6 question of implementation

Comment*: We believe that Article 6 questions of compliance (implementation) should generally be resolved through the compliance system. Assuming the compliance system's eligibility function governs JI, that function should be able to serve not only as a way of determining whether a Party is qualified to trade in ERUs, but whether such a Party should be eligible to participate in implementing a project. Article 6 implementation questions should be resolved through that part of the compliance system that determines eligibility for both JI and emissions trading.*

Suggested text:

All questions of an Annex I Party's implementation of, or compliance with, the requirements of Article 6 will be [expeditiously] resolved through the appropriate procedures and mechanisms of the compliance system.

Recommended additional text:

Para. ___: Disputes. In the event of a dispute between two or more Parties concerning the transfer or acquisition of ERUs between themselves, the Parties concerned shall settle the dispute pursuant to the terms of Article 19 of the Protocol. However, in no event may the provisions of this paragraph preclude the applicability of procedures or mechanisms established under the Protocol's compliance system, should any aspect of the dispute raise a question of compliance with the Protocol.

G. Reporting by Parties

Paras. 53-54

Comment: *USCAN supports full and transparent annual reporting by each Party that transfers or acquires ERUs. Reporting should include information about any legal entities involved in transactions. All reports should be in a uniform format, prepared under guidelines developed pursuant to Article 7.*

III. INSTITUTIONAL ISSUES

Para. 56 – Role of the COP/MOP

Suggested text:

The COP/MOP shall

(a) Serve as the supreme body of the global framework established under the Protocol;
(b) Define the roles of verification and auditing entities, including private sector entities;
(c) Issue guidelines for reporting by Parties under Article 6; and
(d) Issue guidelines for comparable methodologies for baseline determination.

Para. 57 – Review of JI guidelines by COP/MOP

Comment: *USCAN supports Para. 57 with a review no later than 2012.*

Para. 59 – Role of Parties

Comment: *USCAN supports subparagraphs (a)-(c) as they are. The reporting described in subparagraph (d) should be governed by Article 7.*

APPENDICES TO PART TWO: ARTICLE 6 PROJECTS

A. Baselines

Given that JI projects must provide a reduction in emissions by sources, or an enhancement of removals by sinks, that is additional to any that would otherwise occur, baselines must be designed so that all JI projects involve measurable activities that are verifiable and will sustain real emissions reductions over time.

Analyses of the AIJ pilot phase have demonstrated that project-specific baselines have not always clearly demonstrated additionality. Moreover, such baselines can be difficult to develop and verify, leading to concerns over transparency, consistency, administrative burden, and overall effectiveness. Project-level baselines can also create perverse incentives that lead to inflation of baseline emissions estimates for projects, or high emissions intensity in non-JI activities.

Instead, JI rules should allow for the use of performance benchmarks that demonstrate advanced environmental performance. Using such benchmarks will more likely ensure real emissions reductions, as well as increased transparency, reduced costs for demonstrating additionality, and increased certainty for project developers.

Performance benchmarks can apply to new projects or to retrofits. For "new" projects, performance benchmarks should be chosen to represent the high-performance end of the spectrum of current commercial practice. For example, renewable energy projects such as solar and wind energy will tend to meet criteria for both environmental and financial additionality. By contrast, nuclear technologies, large-scale hydropower, and "clean" coal will not meet the tests of advanced environmental performance.

For retrofit projects, the measurable baseline of energy consumption/ emissions prior to the project can be taken into account, assuming a depreciation schedule that recognizes a facility's finite lifetime and the fact that improvement in performance would take place, even in the absence of a JI project. Credits for retrofits would be calculated relative to a baseline derived from measured pre-project emissions using a "straight line depreciation schedule" based on a facility lifetime of no more than 25 years. Finally, post-project performance for all projects should meet minimum performance criteria.

C. Registries

Comment: *The New Zealand proposal (March 2, 1999 paper in FCCC/SB/misc.3) is primarily concerned with the registration of trading of AAUs. Additional information should be included regarding the registration of ERUs, including 1) a brief description of the project, 2) the date the project was established, 3) the date of ERU approval, 4) the name of the legal entity developing the project, 5) the name of entity performing the verification, and 6) the name of the entity approving the ERUs.*

PART III: CLEAN DEVELOPMENT MECHANISM

I. NATURE AND SCOPE

B. Principles

Comment:

- *CDM objectives and priorities should support the overall process of assisting Parties in achieving sustainable development. CDM-related activities must therefore take into account their social, cultural and biodiversity impacts.*
- *The CDM must not serve as a substitute for Annex I countries implementing the domestic actions needed to achieve deep reductions in their emissions. The vast majority of CAN members believe that a separate quantitative cap should be placed on each Annex I Party's use of CERs.*

C. Part of/Supplementarity

Comment: *Rules defining the "supplemental" role of the CDM must be quantified and verifiable. The vast majority of Climate Action Network members believe that placing a quantitative cap on the use of the flexibility mechanisms is crucial to ensuring the environmental integrity of the system.*

D. Participation

Para. 66 – Rules for when Annex I Party can use CERs to contribute to compliance
Comment: *Our suggested text is similar to our recommended participation rules for Art. 6 JI. We believe that satisfaction of these Annex I participation rules should also be a prerequisite for project registration and certification.*

Suggested text:

A Party included in Annex I may use CERs to contribute to compliance only if the Party:

(a) Has ratified the Protocol;
(b) Is bound by a compliance system adopted by the COP/MOP;
(c) Is in compliance with all CDM rules and guidelines and relevant provisions in the Protocol;
(d) Is entitled to participate in the CDM according to the procedures and mechanisms regarding eligibility established under the compliance system, which shall include, but are not limited to:
  (i) compliance with Article 12 of the Convention,
  (ii) compliance with Articles 5, 7, and 10 of the Protocol; and
(e) Maintains a national registry in accordance with the provisions of this [annex] and any related rules or guidelines established by the COP/MOP.

Para. 68 – Rules for non-Annex I Party participation

Comment: *Our suggested text allows project registration and CER certification only after a non-Annex I Party's eligibility is first confirmed.*

Suggested text:

Project Activities may be registered and CERs certified only if the participating Party not included in Annex I:

(a) Has ratified the Protocol;
(b) Is bound by a compliance system adopted by the COP/MOP;
(c) Is in compliance with all CDM rules and guidelines, and relevant provisions in the Protocol;
(d) Is entitled to participate in the CDM according to the procedures and mechanisms regarding eligibility established under the compliance system;
(e) Is in compliance with its commitments under Article 12 of the Convention; and
(f) Has conducted a dialogue with stakeholders whose access to resources may be affected or who may suffer the consequences of any adverse environmental or health impacts of a project.

USCAN also suggests that the COP/MOP explore the desirability of developing guidelines for the use of host countries in producing national CDM strategy plans. Under these plans, host countries could assess where CDM projects could be deployed most effectively, and would establish how their domestic policies could be mobilized to support successful project implementation.

Paras. 70-71 – Who can develop a project

Comment: *Because voluntary participation approved by each Party involved is a requirement for certification, we see no reason to restrict who can develop a project (provided the developer has the host's permission). The fewer restrictions at the international level, the greater the possibility that developing countries will actually see some meaningful investment from the CDM. However, regardless who can develop a project, CERs must not be issued nor redeemed unless the concerned Parties have satisfied the participation requirements.*

Para. 72 – Entity participation; effect on responsibility of Parties

Comment: *This is an essential prerequisite to the participation of any non-Party entities. All Parties must be fully responsible for fulfilling their treaty obligations, regardless of what their public or private entities may do or not do.*

E. Share of Proceeds

Para. 75 – Share of proceeds defined

Comment: *USCAN supports Option 1. The share of proceeds should be based on a percentage of the CERs generated. Additionally, we believe such a fee should be levied on all Kyoto*

Mechanisms to help correct the current competitive disadvantage of the CDM and the failure of markets to generate projects in the least developed countries.

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Project Validation/Registration

Comment:

- *USCAN prefers the term "project registration"—as opposed to "project validation"—to signify the initial acceptance by the executive board that will entitle a given project activity to be officially considered a CDM project.*
- *USCAN recommends that the COP/MOP develop an approach that ensures that those technologies and activities that are most clearly additional receive priority treatment in the registration process, including expedited baseline review. For example, technologies that involve very low or zero GHG emissions, i.e., wind and solar technologies, should face a simpler registration process that employs standardized baseline rules.*

Para. 79

Suggested revisions to subparagraphs (a) and (b):

Project activities under the CDM shall:

(a) Cover one or more of the gases listed in Annex A of the Protocol.

(b) Provide reductions in emissions in one or more of the sector/source categories listed in Annex A of the Protocol until the COP/MOP decides that other sector/source categories should be included.

Para. 79 (g) – Exclusion of nuclear power projects

Comment*: CDM rules must categorically exclude the possibility of any nuclear power projects being accepted under the CDM.*

Para. 80 – Inclusion of sinks projects

Comment: *Any decision to include sinks in the CDM should be deferred until the IPCC Special Report, scheduled to be released this year, is fully considered by the COP and relevant subsidiary bodies.*

Para. 81 – "Embedding" CDM projects in larger project activities

Comment: *USCAN supports this proposal.*

Para. 83 – Project registration: operational entities and executive board

Suggested text:

A designated operational entity shall prepare a registration report on the project activity in accordance with Appendix B, which it shall submit to the executive board. The executive board will have the option of rejecting the project, based upon information in the report and other relevant information. The executive board will also have the option of requesting resubmission of the registration report in the event it believes the information in the report was not completed in accordance with the requirements of Appendix B.

Para. 84 – Public access to decisions on registration

Suggested text:

Information pertaining to registered project activities shall be publicly accessible.

Para. 84bis – Stakeholder involvement

Suggested text:

Stakeholders shall have the right to submit information relevant to project registration to the operational entities and to the executive board.

Para. 86 – Sustainable development

Suggested text:

Projects must contribute to the sustainable development of the host country. The climate and other environmental and social impacts of projects must conform to sustainable development goals that are recognized internationally and agreed upon both locally and nationally. To help ensure that the CDM assists Parties not included in Annex I in achieving sustainable development, all CDM projects must:

(a) be consistent with all relevant international agreements relating to sustainable development, including RAMSAR and the conventions on desertification and biodiversity;
(b) take into account existing international guidelines, indicators, and/or standards for sustainable development that utilize the best available environmental methods and technologies; and
(c) contribute to the ultimate objective of the Convention.

Para. 87 – Emissions baselines

Suggested text:

The emissions baseline should be the basis for calculating the environmental additionality of the project and the emission reduction to be certified. Baselines should be credible, verifiable and, where possible, consistent and comparable.

Para. 88 – Emissions baselines

Suggested text:

Baselines shall be established in accordance with Appendix A. In some cases, in accordance with Appendix A, sectoral baselines and standard baselines for project categories for each host Party may be applied.

Para. 91 – Commencement date

Suggested text:

A project activity will be eligible for consideration as a CDM project activity if it meets the criteria contained in Appendices A and B. Following project registration, verification, and certification, CERs may be issued from the date of the host Party's ratification of the Protocol or from the year 2000, whichever is later, provided that the host and investing Party are in compliance with the Convention and Protocol.

Para. 92 – Project bundling

Suggested text:

Two or more small-scale projects of the same type may be bundled so that they are treated as a single transaction involving a single Party, provided that they retain their own project identity with respect to requirements for registration, verification and certification. Projects may be bundled by an investing Party acting on its own or on behalf of several small-scale investors.

B. Project Financing

Para. 95 – Sources of funding

Comment: *USCAN supports Option 3, and recommends that Para. 95bis be included as subparagraph (b). We believe that the fewer restrictions at the international level, the greater the possibility that developing countries will actually see some meaningful investment from the CDM. However, regardless who can finance and implement a project, CERs must not be issued nor redeemed unless all the rules for CDM projects have first been satisfied.*

Recommended additional text:

Public or private entities of a participating Party or Parties may finance and implement a CDM project unilaterally, bilaterally or with the participation of multilateral institutions. Projects may also, with the consent of host countries, be financed through a portfolio approach by means of a central market or a private placement, on the condition that such projects are subject to the same rigorous rules established for all CDM projects.

C. Project Monitoring

Para. 101 – Monitoring plan

Suggested text:

Participants shall develop a monitoring plan containing information on their procedures for accurate, systematic and periodic monitoring of the project in accordance with the criteria in Appendix C. The monitoring plan will be assessed and accepted or rejected by the operational entity as part of the registration process.

Para. 102 – Implementation of monitoring plan

Suggested text:

Participants shall ensure that the monitoring plan is properly implemented, that all relevant data are collected, recorded and stored in a standardized format and are reported to the relevant operational entity for verification and certification purposes. All information reported under the monitoring plan shall be entered into a publicly accessible electronic international CDM database.

Para. 103 – Adequacy of monitoring plan

Suggested text:

The continuing adequacy of the monitoring plan and its implementation shall be assessed by the designated operational entity in its verification reports to the executive board. Other Parties and bodies, including civil society, may submit commentary to the executive board on the adequacy of the monitoring plan or its implementation.

D. Project Verification

Para. 104 – Process

Suggested text:

Emission reductions achieved by the project in relation to the registered baseline shall be periodically verified from the monitored data and other pertinent information in accordance with the methodology and standardized format contained in Appendix C.

Para. 105 – Verification entity

Suggested text:

Project verification shall be performed independently by a designated entity selected by the executive board. The entity shall be selected on the basis of its technical competence and qualifications. The executive board will assign the qualified verification entity to a particular project according to a random or rotating selection from the list of qualified entities.

E. Certification/Issuance of CERs

Para. 108(b) – Certification allowed only if project has been validated and continues to meet validation requirements

Comment: *We support this requirement, and cross reference the CDM participation requirements we suggest in Paras. 66 and 68, which should be prerequisites for registration of all projects and all certification of emissions reductions.*

Para. 109 – Certifying and issuing entity

Option 1: designated operational entity
Option 2: executive board on basis of a verification report submitted by an operational entity
Option 3: host Party under its own procedure
Option 4: the Convention body
Option 5: the COP/MOP

Comment: *USCAN supports a combination of Options 1 and 2. We believe emissions reductions from registered projects should be certified by fully accredited operational entities. CERs for such certified reductions should then be issued under the direction of the executive board. We believe Option 3 is unacceptable, because it would provide a significant opportunity for gaming and conflict of interest. Options 4 and 5 are unworkable and would merely serve to accomplish a de facto shut down of the CDM.*

Para. 110 – Criteria for baselines, etc.

Comment: *We support the premise that there should be methodological compatibility between JI and CDM projects, and that both types of projects should be subject to the same rigorous rules.*

Para. 111 – Certifying entity promptly notifying participants of decision; publishing decisions

Comment: *We support the highest degree of transparency possible throughout the CDM process, including full public disclosure of certification results. In addition to the decision, the full report with data and analysis should be published.*

Para. 112 – Information contained on CERs

Comment*: CERs should bear sufficient information to allow them to be tracked through the national and international registry systems, just as joint implementation and emissions trading certificates should be tracked (see Paras. 170-175). This information should include, inter alia, a unique serial number, the host and home country, project name, year of issuance, and certifying entity.*

F. Issues Related to Compliance

Para. 114 – Applicability of the compliance system developed under Article 18 to cases of non-compliance with CDM rules

Comment*: Assuming the compliance system's eligibility function governs CDM participation for both Annex I and non-Annex I Parties, that function should be able to serve as a means for determining not only whether a Party is qualified to begin participating in the CDM, but also whether such a Party should be eligible to continue participating. Accordingly, Article 12-related questions should be resolved through that part of the compliance system that determines eligibility for CDM participation.*

Suggested text:

(a) All questions of a Party's compliance with the rules governing the CDM will be resolved through the appropriate procedures and mechanisms of the compliance system, provided that the Executive Board will have jurisdiction over those types of questions that the COP/MOP instructs it to resolve. The resolution of an issue of compliance may include the voiding of CERs derived from projects whose emissions reductions or removals were called into question by the issue of non-compliance.

(b) Notwithstanding the provisions of subparagraph (a) above, any Party, or public or private entity, may raise questions at any stage of the CDM process regarding the implementation of a specific project. Such questions must be supported by corroborating data and should be submitted to, and considered by, the operational entities responsible for registration, verification, and/or certification of the project.

(c) Should a question of implementation regarding a specific CDM project not be resolved through the process described above in subparagraph (b), then the Party or public or private entity that raised the question may submit the question and corroborating data to the executive board for its consideration of the matter.

Recommended additional text:

Para. ___. Disputes. In the event of a dispute between two or more Parties concerning their mutual participation in a CDM project or the transfer or acquisition of CERs between themselves, the Parties concerned shall settle the dispute pursuant to the terms of Article 19 of the Protocol. However, in no event may the provisions of this paragraph preclude the applicability of procedures or mechanisms established under the Protocol's compliance system or this [annex], should any aspect of the dispute raise a question of compliance with the Protocol.

III. INSTITUTIONAL ISSUES

A. COP/MOP

Para. 128 – Duties of COP/MOP

Comment*: USCAN supports paragraphs 128(d) and (e).*

Para. 129 – Disputes Between Parties

Comment: *This paragraph should be deleted or moved to an appropriate section.*

B. Executive Board

Para. 130 – Relation of executive board to COP/MOP

Comment: *The executive board should function as a separate standing body of the COP/MOP.*

Para. 131 – Duties of the executive board

Comment: *USCAN believes subparagraphs b, d, and f are particularly vital to the operation of the executive board. However, the decision-making powers described in subparagraphs (a) (project eligibility), (c) (criteria for establishing baselines), and (k) (percentage of proceeds) should be vested in the COP/MOP, not the executive board.*

Suggested text (following the lettering in the chairman's text):

In relation to methodological and operational issues, the executive board shall, *inter alia*:

(b) Supervise CDM project activities to ensure they are in conformity with the Convention, the Protocol and all relevant decisions by the COP/MOP;

(d) Ensure that information on baselines used for project evaluation, including standardized baselines, is publicly accessible;

(e) In so far as authorized by the COP/MOP, provide guidance for public and/or private entity participants;

(e)bis. In so far as authorized by the COP/MOP, provide guidelines, indicators, and/or standards for sustainable development;

(f) Review reports submitted by operational entities, provide synthesis reports to the COP/MOP, and make recommendations to the COP/MOP relating to the independent auditing and verification of project activities, as necessary;

(g) Issue CERs on the basis of verification reports submitted by designated operational entities;

(h) Publish, in a timely manner, information on transfers of CERs, including, *inter ali*a, dates, project type, project start date, participating Parties and organizations, and quantity and prices of CERs transferred;

(h)ter. Maintain databases of projects and emission reductions, including identification numbers, project description, baseline approaches, operational entities involved and relevant dates;

(l) Assist in arranging funding of CDM project activities as necessary, including by acting as a project clearing-house and publishing summary information on proposed CDM projects in need of funding;

(m) Assign, as necessary, functions to other institutions under Article 12 within the framework provided by the COP/MOP;

(o) Call on experts for technical advice if deemed necessary;

(p) Assure that all of its official meetings are open to all Parties and accredited observers; and

(q) Record the full text of its decisions, in all six official languages of the United Nations, and release such texts in a medium that is accessible by the public.

Para. 132 (a) – Relation to institutional issues

***Comment**: The executive board should accredit operational entities based on guidance from the COP/MOP, taking into account principles of equitable geographic distribution.*

Para. 134 – Composition of executive board

***Comment**: USCAN supports Option 2, with the following addition: The CDM executive board should include civil society representation from countries included in Annex I and countries not included in Annex I.*

Para. 136 – Decision-making

***Comment**: USCAN does not support this paragraph. Instead, we recommend that decisions be made by a supermajority of two-thirds or three-quarters of those present and voting.*

Para. 137 – Location of the executive board

***Comment**: USCAN supports locating the executive board of the CDM in the UNFCCC secretariat.*

C. Operational Entities

Para. 138

Suggested text:

Operational entities shall:

(a) Be accredited by the executive board based on selection criteria contained in Appendix F;

(b) Be supervised by the executive board and fully accountable to the COP/MOP, through the executive board;

(c) Be subject to modalities and procedures specified in applicable decisions of the COP/MOP;

(d) Have no proprietary or financial relations with CDM project activities, nor have been involved in the identification, development or financing of the project for which they are serving as an operational entity;

(e) Submit annual activity reports to the executive board [in accordance with the modalities and procedures for reporting] [in accordance with Appendix C];

(f) Register project activities under Article 12 in accordance with Appendix B, to ensure that they meet the standards agreed upon by the COP/MOP;

(g) Verify emission reductions achieved by projects, in accordance with Appendix C, and propose their certification by means of a verification report to the executive board;

(h) Verify that projects

(i) are consistent with all relevant international agreements;

(ii) are consistent with guidelines, indicators, and/or standards provided by the executive board; and
(iii) contribute to the ultimate objective of the Convention.

Para. 139 – Designation of operational entities
Comment: *USCAN supports Option 1, both subparagraphs (a) and (b), with the following minor changes in language to include verification, and exclude certification.*

Suggested text:

Entities may be designated as operational entities only if they:

(a) Demonstrate that they possess the necessary expertise and means to register project activities, verify emission reductions, and carry out sample checks if so mandated;

(b) Work in a credible, independent, non-discriminatory and transparent manner and ensure, where appropriate, that emission reductions verification is based on internationally agreed standards;

Para. 140 – Functions of operational entities
Comment*: This paragraph should be merged with Para. 138 (see above). USCAN does not support Option 2, including subparagraph (c), which proposes that certification and issuance of CERs be performed by the executive board, based upon verification reports of independent operational entities.*

E. Administrative Support

Para. 143 – Role of the secretariat
Comment*:* USCAN supports Option 1, with the following suggested text.

Suggested text:

The secretariat, on request of the executive board and under the guidance of the COP/MOP, shall provide administrative and secretariat assistance to the executive board. This assistance may include, *inter alia*, compiling, synthesizing and disseminating information related to CDM activities, including those related to Article 12, paragraph 6, and performing any other secretariat functions the executive board may deem appropriate.

F. Review

Para. 146
Comment*: USCAN supports this paragraph.*

APPENDICES TO PART THREE: CLEAN DEVELOPMENT MECHANISM

A. Baselines

Given that CDM projects must demonstrate emissions reductions that are additional to any that would have occurred in the absence of the project, baselines must be designed so that all CDM projects involve measurable activities that are verifiable and will sustain real emissions reductions over time.

Analyses of the AIJ pilot phase have demonstrated that project-specific baselines have not always clearly demonstrated additionality. Moreover such baselines can be difficult to develop and verify, leading to concerns over transparency, consistency, administrative burden, and overall effectiveness. Project-level baselines can also create perverse incentives that lead to inflation of baseline emissions estimates for projects, or high emissions intensity in non-CDM activities.

Where practical, such as in the case of electricity generation and building construction, CDM rules should allow for the use of performance benchmarks that demonstrate advanced environmental performance. Using such benchmarks will more likely ensure real emissions reductions, as well as increased transparency, reduced costs for demonstrating additionality, and increased certainty for project developers.

Performance benchmarks can apply to new projects or to retrofits. The performance benchmarks for "new" projects should be chosen to represent the high-performance end of the spectrum of current commercial practice. Nuclear technologies, large-scale hydropower, and "clean" coal do not meet the tests of advanced environmental performance.

Performance standards can be identified that provide easily quantifiable reductions in greenhouse gases. For example, a CDM project involving a new source of renewable energy (e.g., photovoltaics) could generate a predictable level of credits under the following approach:

> Example of performance standard or benchmark: photovoltaics
> Example of quantity of energy generated: 1,000 MWh in the year 2012
> Example of baseline against which to compare performance standard: new natural gas plant emitting 0.11 tonne carbon/MWh
>
> CER potential for photovoltaic project in 2012 = 110 tonnes of carbon

Considering the above example, the role of the operational entities responsible for verification of baselines and CERs would be relatively simple and inexpensive. In this case, the operational entity would need to confirm that the specified technology had been operational at the stated capacity for a given period of time. Project-specific calculation of greenhouse gas emissions, additionality, and leakage effects would not be necessary.

For retrofit projects, the measurable baseline of energy consumption/ emissions prior to the project can be taken into account, assuming a depreciation schedule that recognizes a facility's finite lifetime and the fact that improvement in performance would take place even in the absence of a CDM project. Credits for retrofits would be calculated relative to a baseline derived from measured pre-project emissions using a "straight line depreciation schedule" based on a facility lifetime of no more than 25 years. In addition, post-project performance should meet specified criteria such that measured greenhouse gas emissions factors reflect a level of low emissions intensity.

For both of the above approaches, the role of the operational entities and the executive board should be relatively straightforward. However, in the near-term it may be difficult to identify clear performance benchmarks in all sectors and sub-sectors that could otherwise be good candidates for CDM investments. A multi-tiered approach would be needed to develop additional baseline criteria and review procedures for sectors and activities where performance benchmarks cannot be identified. For sectors and activities where related greenhouse gas emissions are not well understood, additional steps would be needed.

In sectors and activities where strong performance benchmarks are not available, the following procedures for baseline determination and review would need to be implemented, at a minimum. Project developers will need to calculate greenhouse gas emissions for both project and without-project scenarios. The expected impact of emissions leakage should be used to calculate net emissions reduction units expected from the project. For projects that involve more than one sector or gas, or an emissions reduction activity that is not well understood, research on indirect as well as direct greenhouse gas emissions will need to be undertaken.

The adoption of performance benchmarks would require minimum involvement of the executive board, which would review development, monitoring and verification reports containing standardized information on project production and emissions before approving the issuance of CERs. In contrast, project and non-standardized baselines will demand considerable involvement of the executive board and/or operational entities in both the project development and certification phases.

D. Registries

Comment: *The New Zealand proposal (March 2, 1999 paper in FCCC/SB/misc.3) is primarily concerned with the registration of Article 17 trades. Additional information should be required for the registration of CERs , including (1) a brief description of the project, (2) the date the project was established, (3) the date of CER approval, (4) the name of the legal entity developing the project, (5) the name of the entity performing the verification, and (6) the name of the entity approving the CERs.*

PART IV: EMISSIONS TRADING

I. NATURE AND SCOPE

B. Principles

Para. 149 (e) – Rights to atmosphere
Comment: *USCAN supports this text. Tradable permits are not property rights.*

Para. 149 (i) – Fungibility
Comment: *USCAN supports Option 2, provided that a registry system information tracks the transfer of all units, the registry system is transparent and all information contained therein is publicly accessible, and that rules implementing the Kyoto Protocol are strict enough to ensure the environmental integrity of the mechanisms and the Protocol itself.*

C. Supplementarity

Para. 150 – Limits on acquisitions
Comment:

- *Rules defining the "supplemental" role of emissions trading and joint implementation must be quantified and verifiable. The vast majority of Climate Action Network members believe that placing a quantitative cap on the use of the flexibility mechanisms is crucial to ensuring the environmental integrity of the system.*
- *Rules governing trading among current and future Annex B parties must ensure that net global emissions are no higher than they would be in the absence of trading and JI.*

Para. 151 – Limits on transfers
Comment: *USCAN supports Option 2. USCAN believes that the quantitative limit on transfers can be an effective means of limiting hot air.*

The climate protection benefits anticipated in the Kyoto Protocol targets are threatened by a combination of low targets for some Parties—notably Russia and the Ukraine—and their potential participation in the Article 17 emissions trading regime. De-industrialization in both of these countries has drastically reduced their emissions since 1990, whereas the targets assigned to these Parties allow relatively constant emissions. As a result, even under business-as-usual scenarios there will be large unused portions of their assigned amounts, which will be available for sale to other Annex B Parties. These "hot air" transfers will undermine the environmental integrity of the Kyoto Protocol by allowing higher emissions from purchasing countries.

New projections of the amount of hot air add urgency to finding a way to eliminate it. According to the US Energy Information Administration, roughly two-fifths of the emissions reductions required of industrialized countries could be provided by hot air. The projected hot air available from Russia, Ukraine, and CEE, according to this report, is 374 million metric tonnes of carbon equivalent (MMTCE), dramatically larger than earlier projections.[2] *(The selection of alternative base years by some CEE countries accounts for 43 MMTCE of this amount.) Even calculations based on official UNFCCC documents project hot air of 140 MMTCE.*[3]

Hot air reduces the need for domestic action, and is likely to set up a cycle whereby Annex I Parties do not develop the technologies in the first commitment period that will be needed for deeper cuts in the second commitment period. Moreover, with some Non-Annex I Parties wishing to adopt targets and join the emissions trading regime, it is imperative that such Parties do not believe they will be entitled to their own form of hot air.

D. Participation

Para. 152 – Terms of Annex I Party eligibility to take part in emissions trading

Comment*: We believe it is essential that the default rule for participation be that an Annex I Party may not engage in emissions trading until it has been deemed eligible to do so under the eligibility function of the compliance system. In the absence of such a rule, Parties that are wholly incapable of ensuring the integrity of their traded tonnes could nonetheless sell assigned amount units. Hence, we offer the following text, based upon the EU submission, and similar to the text we suggest for participation in Art. 6 JI and Art. 12 CDM.*

Suggested text:

A Party included in Annex I may not participate, nor authorize any legal entity to participate, in emissions trading under Article 17 unless the Party:

(a) Has ratified the Protocol;

(b) Is bound by a compliance system adopted by the COP/MOP;

(c) Is entitled to participate in Article 17 emissions trading according to the procedures and mechanisms regarding eligibility established under the compliance system, which shall include, but are not limited to:

(i) compliance with Article 12 of the Convention,

(ii) compliance with Articles 5, 7, and 10 of the Protocol,

(iii) implementation of adequate national monitoring and verification systems,

(iv) implementation of an adequate domestic compliance system, and

(d) Maintains a national registry in accordance with the provisions of this [annex] and any related rules or guidelines established by the COP/MOP.

Para. 154 – Changes in eligibility

Comment: *This provision that a Party's eligibility can change during the commitment period is essential, and flows naturally out of the eligibility criteria above.*

Para. 155 – Legal entities participation

Suggested text:

Legal entities of a Party included in Annex I may participate in emissions trading only under the authorization of that Party.

[2] EIA, *International Energy Outlook* (1999).

[3] Greenpeace, *Undermining the Kyoto Protocol: An Update on Loopholes* (1999).

Para. 156 – Responsibility of Parties

Comment: *USCAN strongly supports the proposition that any Party authorizing legal entity participation must nevertheless always remain responsible for fulfilling its Protocol obligations, regardless of the acts or omissions of its legal entities.*

E. Share of Proceeds

Para. 157- Share of proceeds defined

Comment: *USCAN supports the present text. Levying such a fee on all Kyoto mechanisms would help correct the current competitive disadvantage of the CDM, as well as the failure of markets to generate projects in the least developed countries.*

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Modalities of Operation

Comment*: There should be maximum transparency and competition in emissions trading. To ensure this, information on purchasers, quantities bought and amounts paid should be included in a country's national communication. USCAN recommends the COP/MOP explore developing procedures and guidelines so that government sales of assigned amounts are publicly advertised for open tender with sealed bids from interested Parties conducted in line with current best practice. Independent auditing could then be used to ensure that assigned amounts were sold to the highest bidder.*

Para. 158 – Transfers and acquisitions of AAUs

Comment*: Bilateral and multilateral arrangements, as well as exchanges, may be acceptable options for Parties and legal entities to use in order to facilitate emissions trading under the Protocol. However, such arrangements must be contingent on the existence of: (1) a compliance system that can adequately evaluate a Party's eligibility to trade, consistent with Articles 5 and 7; (2) an expedited, reliable review and verification procedure for evaluating each Party's annual reports; and (3) an effective international registry system or network for tracking transferred assigned amount units.*

C. Issues Related to Compliance

Paras. 165, 169 – "Liability"

Comment: *We support a synthesis of the "traffic light" approach outlined in Para. 169 and the Swiss proposal described in Para. 165 as Option 5. Our suggested text sets a default rule of buyer liability ("yellow light") for emissions trading, but allows for trades to switch retroactively to seller liability ("green light") when the seller's reported annual emissions do not exceed its emissions allocation plan. Our proposal is premised on the existence of (1) a compliance institution that can adequately evaluate a Party's eligibility to trade, consistent with Articles 5 and 7; (2) an expedited, reliable review and verification procedure for evaluating each Party's annual reports; and (3) an effective international registry system or network for tracking transferred assigned amount units.*

Suggested text:

1. Emissions Allocation Plan. Each Party that intends to transfer parts of its assigned amount under Article 17 shall first prepare an emissions allocation plan. Under the plan, the Party will allocate its total assigned amount among the five years of the commitment period. The assigned amount allocation for any single year must not exceed plus or minus [ten][five] per cent of the total assigned amount divided by five. Emissions allocation plans shall be submitted to the [eligibility division of the compliance system].

2. Upon submitting a valid plan to the [eligibility division of the compliance system], a Party may transfer parts of its assigned amount during the commitment period, subject to the eligibility rules for emissions trading and the rules of this [annex].
3. Assignment of Risk or Liability. In addition to the obligations set forth in Article 3.1 and 3.11, the assignment of risk or liability between Parties who transfer or acquire assigned amount units under Article 17 emissions trading shall be determined by comparing the transferring Party's emissions estimates during the commitment period (as reported in the Party's annual inventories) with that Party's emissions allocation plan. The [eligibility division of the compliance system] shall be responsible for making the determination.
    a. "Green Light" for Confirmed Assigned Amount Units. If the [eligibility division of the compliance system] confirms that a Party's reported emissions for the previous year were equal to or less than the allocation for that year as contained in the Party's emissions allocation plan, all assigned amount units originally transferred by that Party during that year shall be available to an acquiring Party for purposes of achieving compliance with its commitments as specified in Article 3.10. Any such confirmed assigned amount units shall be valid for trade or compliance purposes without risk of revocation or discounting.
    b. "Yellow Light." Any assigned amount units transferred under Article 17 which have not been confirmed under the procedure described in subparagraph (a) above shall be available to an acquiring Party for purposes of achieving compliance with its commitments as specified in Article 3.10 *only* if the Party from whom the assigned amount units were originally transferred is in compliance with its obligations under Article 3 at the end of the commitment period; *provided that* any assigned amount units remaining after the [discounting] ["last in, first out"] procedure described below may nonetheless be used by an acquiring Party for compliance purposes.
        i. Option One: Discounting. If the Party from whom the assigned amount units were originally transferred is not in compliance with its Article 3 obligations at the end of the commitment period, then the tonne-value of any such assigned amount units shall be discounted by a factor equal to the total number of tonnes of the Party's overage divided by the number of assigned amount units transferred by the Party that have not been confirmed under the procedure described in subparagraph (a) above. Any tonne-value remaining in such discounted assigned amount units shall be available to an acquiring Party for purposes of achieving compliance with its commitments, as specified in Article 3.10.
        ii. Option Two: Last In, First Out. If the Party from whom the assigned amount units were originally transferred is not in compliance with its Article 3 obligations at the end of the commitment period, then the assigned amount units shall be voided in the reverse chronological order of their original transfer, until assigned amount units have been voided in an amount equivalent to the amount by which the Party's emissions exceed its assigned amount. Any assigned amount units not so voided shall be available to an acquiring Party for purposes of achieving compliance with its commitments, as specified in Article 3.10.
    c. "Red Light." If the [eligibility division of the compliance system] determines that a Party's emissions for the previous year exceeded the allocation for that year as contained in the Party's emissions allocation plan by [twenty] percent or more, then that Party shall be barred from transferring parts of its assigned amount until the next annual evaluation of its emissions inventory. Transfers by such a Party will be permitted to resume only upon a determination by the [eligibility division of the compliance system] that the Party's cumulative

emissions for the commitment period do not exceed [100][110] percent of the Party's cumulative allocation as contained in its emissions allocation plan.

4. Seller Liability.
   a. If any Party from whom assigned amount units were originally transferred is not in compliance with its Article 3 obligations at the end of the commitment period, and that Party's non-compliance causes the voiding or discounting of assigned amount units originating from it that have been acquired by other Parties, then the Party shall be barred from transferring parts of its assigned amount under Article 17 during the next commitment period.
   b. In no event may the procedure described in subparagraph (a) above indemnify a Party from any additional responses to non-compliance that may be available under the procedures and mechanisms of the compliance system.

Para. 165, Option 6 – Compliance reserve

Comment: *We favor the inclusion of a compliance reserve, but caution that such inclusion must not lead to relaxed emissions trading participation or liability rules.*

Para. 167 – End of commitment period; overage; true-up

Comment: *We agree that a Party with overage at the end of the commitment period should be able to purchase, but not transfer, AAUs. We also agree that there should be a short true-up at the end of the commitment period, during which time a Party may have an opportunity to cure overage. However, the rule establishing the true-up should be a general compliance rule applicable to all Parties, not simply traders. Consequently, the rule should be promulgated as part of the overall compliance system.*

Recommended additional text:

Para. ___. Disputes. In the event of a dispute between two or more Parties concerning the transfer or acquisition of AAUs between themselves, the Parties concerned shall settle the dispute pursuant to the terms of Article 19 of the Protocol. However, in no event may the provisions of this paragraph preclude the applicability of procedures or mechanisms established under the Protocol's compliance system, should any aspect of the dispute raise a question of compliance with the Protocol.

Recommended additional text:

Para. ___. All questions of an Annex I Party's compliance with the requirements of Article 17 and this [annex] will be resolved through the appropriate procedures and mechanisms of the compliance system.

D. Registries

Para. 170 – National and central registries

Comment*: USCAN supports the establishment of national registries and a central registry that compiles and consolidates all of the information available in the national registries. Registries should accurately record all holdings, transfers, acquisitions and retirements of AAUs by any Party that participates in emissions trading. Registries should include the trading activities of authorized legal entities. They should be based on real-time reporting, should be accessible to the public, and should be able to show at any given time during the compliance period how many AAUs are in any given Party's national account. National registries should be maintained in a format that is compatible with the central registry. The format should be developed by the secretariat with the assistance of outside experts as the secretariat deems necessary.*

Para. 173 – Retiring AAUs

Comment*: USCAN supports this paragraph.*

Para. 174 – National registries, public accessibility of information
***Comment**: USCAN supports this paragraph.*

E. Reporting by Parties

Para. 176 – Annual submissions
***Comment**: USCAN supports the proposition that complete information regarding a Party's Article 17 activities, including those of its authorized legal entities, should be included in its annual inventories. However, reporting of AAU transfers should also be performed in real time, through both the national and central registries.*

Para. 177 – Secretariat's synthesis report
***Comment:** We support this paragraph, provided that it does not diminish the requirement that Parties support their national registries and the central registry through real time reporting.*

III. INSTITUTIONS

A. Role of the COP and/or the COP/MOP

Comment:

- *Because the COP will not necessarily be comprised of the same Parties who make up the COP/MOP, it will not be legally competent to bind the COP/MOP with its decisions. Accordingly, the COP/MOP should be the ultimate decision-making body for all Article 17 issues.*
- *Some Parties that wish to engage in trading may not have experience regulating similar kinds of activities. We suggest that the COP/MOP provide assistance to such Parties by devising guidelines or recommendations for accrediting, managing, and regulating their private entities who may be engaged in providing trading-related financial services.*

B. The Role and Duties of Parties

Para. 181
***Comment:** These issues should be included in the Participation section of the text.*

C. Administrative Support

Paras. 182-83
***Comment:** As discussed in our comments on registries in Para. 170, USCAN believes that both national registries and a central registry will be necessary. The central registry should be administered by the secretariat. It should be open to the public and accessible via the secretariat's website. This will provide actors with current information on the status of Parties' assigned amounts.*

D. Review

Para. 184 – Timing and nature of reviews
***Comment:** We support this paragraph, and stress that the first review should be carried out no later than the year 2012.*