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SUBSIDIARY BODY FOR SCIENTIFIC AND TECHNOLOGICAL ADVICE

Eighth session

Bonn, 2-12 June 1998

Items 6 (b) and (c) and 8 (b) to (d) of the provisional agenda

SUBSIDIARY BODY FOR IMPLEMENTATION

Eighth session

Bonn, 2-12 June 1998

Item 8 (b) to (d) of the provisional agenda

PREPARATORY WORK NEEDED FOR THE FOURTH SESSION OF THE  
CONFERENCE OF THE PARTIES ON THE ITEMS LISTED IN  
DECISION 1/CP.3, PARAGRAPH 5

Submissions by Parties

1. By its decision 1/CP.3, the Conference of the Parties (COP) adopted the Kyoto Protocol to the United Nations Framework Convention on Climate Change. In that same decision, the COP requested the Chairmen of the Subsidiary Body for Scientific and Technological Advice (SBSTA) and the Subsidiary Body for Implementation (SBI) to give guidance to the secretariat on the preparatory work needed for consideration by COP 4 of the five items listed in paragraph 5 of that decision and to allocate work thereon to the respective subsidiary bodies, as appropriate (decision 1/CP.3, para. 5).
2. In order to promote substantive progress at the eighth sessions of the SBSTA and the SBI, the Chairmen of the subsidiary bodies requested the secretariat to invite Parties to submit their views on the preparatory work needed for COP 4 on each of the above-mentioned five items by 21 March 1998.
3. Nine such submissions\* have been received. In accordance with the procedure for miscellaneous documents, these submissions are attached and reproduced in the language in which they were received and without formal editing.

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PAPER NO. 1 CANADA

Following please find Canada's views on issues that should be addressed as Parties begin to consider the elaboration of frameworks for the cooperative implementation mechanisms identified in the Kyoto Protocol. As a general principle, Canada would prefer an approach in the multilateral discussions that would initially engage countries to participate in problem solving - identifying issues that will need to be addressed over this year and sharing information on what clearly are highly complex issues. Canada also believes that it is critical that the international design of such mechanisms be as simple as possible, allowing for maximum flexibility in the domestic design of such systems and working to minimize overall transaction costs. It is of course also critical that these mechanisms be environmentally credible - Canada is committed to making its contribution to the overall commitment of Annex 1 Parties to reduce their net greenhouse gas emissions by 5.2% from 1990 levels for the commitment period of 2008 - 2012 remains intact.

Article 17 - Emissions Trading

Decision L.7 of the Third Session of the Conference of the Parties specifies that the fourth session of the Conference of the Parties is to consider "the definition of relevant principles, modalities, rules and guidelines, in particular for verification, reporting and accountability of emissions trading". While Canada does view it important that some progress is made in defining an appropriate framework for emissions trading by CoP 4, it is also critical that Parties have realistic expectations about what can be accomplished in such a relatively short time frame. Agreement, by CoP 4, on a set of core principles to guide Parties in further design issues would, in our view, represent significant and constructive progress.

We would note the specific recommendations in Decision L.7 and in that respect would strongly support developing a credible international framework that would, in particular, focus on issues related to verification, reporting and accountability. In particular, Parties may wish to consider whether and what provisions on those three elements would be needed in addition to what is already contained in the Protocol, in particular, as found under Articles 5, 7 and 8. Simply put, are the current provisions relating to verification, reporting and accountability, as found in Articles 5, 7 and 8 (and any other related Articles) sufficient in establishing a credible emissions trading framework, and if not, what additional provisions should be considered?

Other issues that could be addressed include:

- \* Linkages with Joint Implementation (Article 6) - how would credits for reductions achieved through Article 6 be transferred to an emissions trading framework?
- \* Coverage - how to design an international framework that would include all six greenhouse gases, sources and sinks?

- \* Market Power - what assurances/principles would be required to ensure that Annex B Parties will have competitive access to emission trading opportunities?
- \* Linkage to compliance - in addition to the issue of what, if any, provisions related to compliance and Article 18 that could be dealt with by an emissions trading system, principles related to liability (buyer or seller?) will also need to be clarified.
- \* Nature of the mechanism - although this is not likely to be fully defined by CoP 4, an agreement on relevant principles that will help to frame the overall design of the mechanism will be useful.

Article 6 - Emission Reduction Units Resulting From Projects Aimed at Reducing Net Greenhouse Emissions Among Annex 1 Parties The Kyoto Protocol enables Annex 1 Parties to transfer to, or acquire from, any other Annex 1 Party emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy.

Key issues to be addressed include:

- \* Determination of credible criteria/principles for a comprehensive baseline that could be used for relevant projects, but not too onerous for private sector engagement.
- \* Details for independent verification and monitoring mechanisms for such projects, to ensure a credible regime is in place while still allowing for a cost-effective and comprehensive approach for Parties.
- \* Linkages with the other flexibility mechanisms.
- \* While not explicitly mentioned in Article 6, Canada is of the view that the precedent set for banking of credits in the CDM for the period of 2000-2007 is also applicable to Article 6. Hence any analysis of the implications of Article 12.10 should also be addressed in discussions on Article 6.
- \* What lessons have been learned from the AIJ Pilot Phase, particularly for those pilot projects between Annex 1 Parties?

Article 12 - The Clean Development Mechanism:

According to Article 12 of the Protocol, the purpose of the Clean Development Mechanism shall be to assist Parties not included in Annex 1 in achieving sustainable development and contributing to the ultimate objective of the Convention, and to assist Parties included in Annex 1 in achieving compliance with emission limitation/reduction commitments under Article 3.

It is Canada's view that the elaboration of the Kyoto provisions covering the Clean Development Mechanism should be a priority consideration at CoP 4. This is especially so, since Article 12.10 allows countries to count emission reductions from CDM projects starting in 2000 towards fulfilment of the commitment period beginning in 2008. It will be critical to determine corresponding institutional arrangements and the process for putting these in place. In that respect, while we note that decision L7 (e) only makes mention that Parties are to participate in an analysis of the implications of Article 12.10, it is Canada's view that the work for the CDM should be broader in scope, covering the design of an appropriate framework for the CDM.

Key issues to be addressed should include:

- \* The elaboration of the modalities and procedures for determining project eligibility, including how "real long-term benefits" and "additionality" can be so devised that it does not serve as a disincentive for private sector investments.
- \* Definition of the nature and structure of the operating entities, covering the membership, role and functions of the Executive Board, clarification of its role in relation to the COP, and terms of reference, including verification, certification and monitoring.
- \* The Protocol also talks about using a share of the proceeds from certified project activities to cover administrative cost and to assist LDCs in meeting adaptation costs. There is a need to have a clear cut interpretation and criteria for determining this share.
- \* Guidelines for the banking of credits. Given that reductions can accrue after the year 2000, while the first commitment period does not start until 2008, there is a need to define guidelines to ensure that banking is both effective and credible.

PAPER NO. 2 CHINA

Views of China on Questions listed in Subparagraphs (a) to (e) in Paragraph 5 of Decision 1/CP.3 as adopted by COP 3 to UN FCCC

China is of the opinion that the prerequisite to resolving the questions listed in Paragraph 5 of Decision 1/CP.3 is to carefully study and then ascertain the appropriate and required methodologies. Procedurally, these questions should first be discussed adequately and thoroughly at the SBSTA of the Convention. And only after completion of such thorough discussions and study by the SBSTA will these questions be referred to SBI of the Convention for consideration.

As regards the questions listed in Subparagraphs (a) to (c) of Paragraph 5 of Decision 1/CP.3, the general views of China are as follows.

Regarding (a). This matter is very complicated, involving GHG “sinks”, etc. The matter involves “how and which additional human-induced activities related to changes in GHG emission and removals ...shall be added to, or subtracted from, the assigned amount...”. In this connection, what are to be taken into account are questions relating to (1) uncertainties, (2) transparency in reporting, (3) verifiability, and (4) the relevant methodologies, etc. as stated in Paragraph 4 of Article 3 of the Kyoto Protocol. All these questions need firstly to be analyzed and studied thoroughly by SBSTA. China’s further comments on this matter will be communicated to the Secretariat of the Convention later on.

Regarding (b). The matter of “emissions trading” is fraught with unusual complexities, involving a number of political, economic, legal, institutional, organizational and methodological issues, which call for serious study and solution, and which cannot be treated with simplism nor be aimed at establishing a certain sort of arbitrary international system or regime.

For the present, the primary tasks of SBSTA on this matter are, inter alia, to conduct a thorough study of, and to exchange views extensively on, the following relevant questions which have to be addressed and resolved properly:

- (i) Whether “emissions trading” can lead to genuine reduction and limitation of GHG emissions conducive to meeting the objective of the Convention?
- (ii) What are to be traded?
- (iii) Taking into account the objective and other relevant provisions of the Convention, bearing in mind the historical and current cumulative emissions ever since the Industrial Revolution, and abiding by the principle of equity, how to correctly identify “emissions rights”, and how are “emissions rights” to be equitably allocated?

- (iv) How is “emissions trading” to be effectively verified?
- (v) What are the environmental impacts of “emissions trading”? Can such “emission trading” really contribute to protecting the atmosphere? What are the negative effects and implications of “emissions trading”?
- (vi) How to ensure that “Any such trading shall be supplemental to domestic actions” for the purpose of meeting the commitments under Art.3 (Art.17 of the Kyoto Protocol). In this context, how to formulate and define the relevant principles, modalities, rules and guidelines, in particular for verification, reporting and accountability for emissions trading, so as to ensure that such trading leads to verifiable emission-reduction at the project level, and to prevent “hot air” trading etc. which have no projects, and which are lacking in transparency and verification and are, in fact, deviating from the objective of the Convention.

Regarding (c). On the “guidelines” referred to in paragraph 2 of Article 6 of the Kyoto Protocol, from the theoretical, practical and methodological point of view, it is premature to start defining the guidelines for implementing Article 6 of the Kyoto Protocol. However, it is necessary to begin study the matter, so as to make the necessary preparations for considering and defining such “guidelines”. Hence, China hereby proposes to begin with SBSTA conducting relevant discussions and study on this matter, inviting interested Parties and competent bodies to provide relevant information or scientific data, and then SBSTA will make recommendations on the relevant principles and elements concerning the formulating and defining of the guidelines, to be submitted to the Conference of the Parties serving as the meeting of Parties to the Protocol at its first session, or as soon as practicable thereafter, for consideration of, and taking decisions on, the “guidelines”.

Regarding (d). Comments will be communicated later, as necessary.

Regarding (e). Implementation of Paragraph 10 of Article 12 of the Kyoto Protocol might have negative impacts on the implementation of the provisions contained in Article 3 of the Protocol. The “certified emission reductions” obtained (obtained by certain Party under Article 12 of the Protocol) during the period 2000 to 2008, if used wholly in its “first commitment period”, will mean that Party’s exploitation of an additional 8 years’ time to meet the commitments under Art.3 of the Protocol in the first commitment period, which obligations, however, should normally be met in the 5 years of the “commitment period”. Therefore, viewed from the protecting of the atmosphere, the implications of implementing Paragraph 10 of Article 12 of the Protocol might be, in effect, something not conducive to the genuine reduction or limitation of GHG emissions. China hereby proposes that SBSTA thoroughly study and analyze such negative implications and make recommendations on measures to reduce or eliminate such negative implications in accordance with the objective and other relevant provisions of the Convention.

### PAPER NO. 3 ICELAND

#### Input from Iceland concerning the work of the subsidiary bodies of the UNFCCC arising from the adoption of the Kyoto Protocol

With respect to subparagraph 5(d) of decision 1/CP.3, which states that COP 4 should consider, and as appropriate, take action on suitable methodologies to address the situation of Parties listed in Annex B of the Protocol for whom single projects would have a significant proportional impact on emissions in the commitment period, Iceland would like to make the following observations:

During the negotiations of the Kyoto Protocol, Iceland elaborated on the difficulties Parties might face in circumstances where the implementation of single projects has very significant impact on total greenhouse gas (GHG) emissions. This could even be the case where such projects have global benefits with respect to the objective of the Climate Change Convention. To illustrate this point, Iceland referred to an aluminium smelter with an annual production capacity of 180,000 tonnes, that is under construction in Iceland, and will add some 13 per cent to Iceland's total emissions. The smelter will use renewable energy and best available techniques (BAT), but process emissions alone would have such impact due to the size of the economy and relatively low per capita emissions.

In such cases, limitations and decreases in GHG emissions in other sectors will not be sufficient to compensate for increases caused by new production units. This implies that the approach taken in the Kyoto Protocol does not take into account one important factor, namely the size of the economy. In a small economy, single projects can add to a Party's total GHG emissions to the extent that it would become impossible for that Party to hold total emissions within the quantified emission limitation or reduction commitments set in Annex B. This can be the case even under the most favourable conditions where renewable energy is used.

It would be useful if the Secretariat prepared a paper on this issue to be presented for discussion at the meetings of the subsidiary bodies in June. The paper should i.a.:

- Suggest operational interpretation of the terms used in subparagraph 5(d).
- Through the use of examples illustrate the circumstances described in 5(d).
- Discuss what legal instruments or modalities need to be developed and adopted, to enable Parties that find themselves in a situation where single projects would have a significant proportional impact on emissions, to comply with the Protocol.

For Iceland, the outcome of this process is of utmost importance. This can be illustrated by the fact that one project in the energy intensive industry sector has been realised in Iceland since 1990; two are under construction and a few more are in the planning stage. It is clear that these projects will cause a very significant increase in Iceland's total GHG



emissions. All the projects are based on BAT and will use renewable energy sources. Consequently, in a global context they will contribute towards the goal of reducing greenhouse gas emissions.

Iceland believes that this issue can be satisfactorily addressed without weakening the Protocol or undermining the objective of the Convention to reduce global GHG emissions. In fact, satisfactory solution to this matter should enhance efforts to limit global greenhouse gas emissions.

Iceland would like to see an outcome in the June session that can be taken to COP 4 for making a decision on item d in paragraph 5 in decision 1/CP.3. Iceland will make every effort to facilitate a process that can bring about an agreement on action on suitable methodologies and modalities to solve this important issue.

With respect to subparagraph 5(a) of decision 1/CP.3, Iceland's view is as follows:

The list of human-induced activities to enhance carbon dioxide uptake by sinks, which can be included in quantified emission limitation or reduction commitments set in Article 3(3), will limit the options open to some Parties to exploit the full potential for carbon sequestration.

At COP 3, Iceland suggested the inclusion of revegetation of degraded land in the list. Iceland also suggested that this should be defined as direct action to increase carbon stocks in soil with low organic matter content. This suggested addition was supported by some other delegations. This was the only non-forest sink enhancement activity suggested.

Iceland pointed out that revegetation of degraded land is important in the context of the Convention to Combat Desertification. It would therefore be mutually supportive for the objectives of the two conventions to include this activity in the list of human-induced activities to enhance carbon uptake by sinks.

COP 3 deferred the decision on additional activities to COP 4 in decision 1/CP.3. This is an important issue which should be given high priority by SBSTA and COP 4. For some Parties the successful outcome of this process may enhance their possibility to sign and ratify the Kyoto Protocol.

The modalities, rules and guidelines as to how and which additional human-induced activities can be included in quantified emission limitation or reduction commitments, should be based on the principle that activities to sequester carbon, can be documented in a transparent manner and verified.

Parties wishing to add to the list of activities at COP 4 should be invited to notify the secretariat prior to the eighth session of SBSTA. Proposals for additions should include a clear definition of the activity and information on how the resulting sequestration will be quantified. If further elaboration of the reporting guidelines will be needed for the additional

activity, this should be indicated by the Party. The Parties would also be asked to provide the rationale for the inclusion of the activity within the context of the Climate Change Convention.

The secretariat would summarise the proposals and present them to the eighth session of SBSTA, which would evaluate the proposals and develop recommendations to COP 4. The approach applied when adding activities, should be to accept those receiving general support at COP 4 and to defer decision on the more controversial activities for subsequent sessions.

The following criteria should apply when adding activities to the list:

- Can the activity be documented in a verifiable manner ?
- Would the inclusion of the activity provide an incentive for Parties to take additional action to sequester carbon ?
- Would the inclusion of the activity contribute towards meeting the goals of other environmental agreements ?

PAPER NO. 4 INDIA

View on sub-paragraphs (a) to (e) of paragraph 5 in Decision 1/CP.3

India is of the view that the items in sub-paragraphs (a) to (e) in paragraph 5 of decision 1/CP.3 require detailed examination in the Subsidiary Body for Scientific and Technological Advice (SBSTA) at the outset. Some comments on the five items referred to above are outlined below. Further comments will be sent subsequently.

Reference 5(a), the questions are intricate and beset with uncertainties, particularly the issues relating to “sinks” and methodologies. The SBSTA should first examine the concerned issues before the matter is taken up by the Subsidiary Body on Implementation.

Reference 5 (b), a fundamental step in developing emissions trading is the determination and creation of equitable emission entitlements of the parties. For this, principles and modalities have to be discussed and agreed upon. The per capita criterion is central to the determination of emission entitlements; this will also provide a direct measure of human welfare. At the foundation of equitable emission entitlements is the right to develop equitably. The entitlements cannot derive from historical emissions which are inequitable. Any precept having the potential of depriving the world’s poor from their right to development must not be allowed. There are many other issues of a legal, institutional, methodological and organizational nature, which need to be discussed and settled equitably.

Reference 5(c), because of complex methodological issues, the starting point of the discussions relating to the elaboration of guidelines, reference Article 6 of the Protocol, should be the SBSTA.

Reference 5(d), comments will be communicated subsequently, as found necessary.

Reference 5(e), paragraph 10 Article 12 of the Protocol should not detract from the implementation of greenhouse gas reduction commitments of Annex I parties for meeting the objective of the Convention. The SBSTA should keep this in perspective while studying the issue.

PAPER NO. 5 NEW ZEALAND

New zealand views: Input to FCCC secretariat due 21 March 1998

Proposal on Work Priorities; paragraph 5 of Decision 1/CP.3

New Zealand proposes that:

- greatest priority should be given to item (b) - definition of relevant principles, modalities, rules and guidelines, in particular for verification, reporting, and accountability of emissions trading, pursuant to Article 17 of the Protocol.
- on item 5(a) of Decision 1/CP.3 (sinks):
  - ◇ work clarifying aspects of Article 3.3 should be given highest priority (in particular the definitions of “afforestation”, “reforestation”, and “deforestation”). Article 3.3 should be the focus of work at the June subsidiary bodies meetings, and addressed at COP4.
  - ◇ work on matters raised in Article 3.4, which relate to decisions applying to the second and subsequent commitment periods are less urgent, and in any case cannot be resolved by the COP until substantive progress has been made on outstanding technical/methodological issues.
- lower priority should be given to items (c) and (d) and no substantive work is necessary associated with item (e). (In our view paragraph 10 of Article 12 is clear in its meaning and intent.)

These proposals are discussed below in detail, together with suggestions on the division of labour , taking into account other tasks arising from the Kyoto Protocol.

Specific comments regarding Decision 1/CP.3, paragraph 5(a) - (sinks)

In New Zealand’s view the immediate focus of work on sinks relating to the Kyoto Protocol should be the resolution of any technical matters associated with Article 3.3, including any interpretative matters:

- the phrase “...net changes in”;
- definitions of “afforestation”, “reforestation” and “deforestation” (We note the glossary in the Revised 1996 IPCC Guidelines included the first two but not the third. The principle underlying the first two is a land use change; this is equally applicable to the third.);
- the practical application of the phrase “...shall be used to meet commitments” (We note the different wording in Article 3.4 for the same intent - i.e. adding removals and subtracting emissions from Parties’ assigned amounts - and suggest that this is an appropriate method.)

The June 1998 subsidiary body meetings should seek to have these matters clarified in appropriate COP4 decisions.

However, in New Zealand's view it is premature to address the matter of sinks resulting from the second sentence in Article 3.4 of the Kyoto Protocol until substantial progress has been made in resolving inter alia the following issues:

- concerns about the definition of anthropogenic activities in the land use change and forestry (LUCF) sector;
- concerns about the adequacy of the draft IPCC guidelines for accurately reporting inventories of emissions and removals from LUCF in the context of legally binding commitments under the Kyoto Protocol;
- concerns about the 'unfinished business' in the draft IPCC guidelines, e.g. treatment of harvested wood products, biomass burning and forest fires;
- concerns about the lack of comparability and transparency of data in Annex I Parties' inventory reports to-date for the LUCF sector; and
- concerns about the absence of inventory reports for the LUCF sector by Annex I Parties.

We question the practicality of the last point in the proposed COP3 decision, namely aiming for a SBSTA report on what constitutes "anthropogenic" activities in the LUCF sector to be presented at COP4 for deliberation and subsequent decision.

SBSTA needs to address the question of whether the work of the IPCC to date, and other scientific work, is sufficient for a SBSTA report to be prepared by COP4, or whether this needs to await the outcome of the ongoing 1-2 years work of the IPCC. New Zealand is not ready to provide a view on this particular question at this time, but we believe it is a question that SBSTA needs to consider immediately.

At COP3, New Zealand facilitated the multi-Party development of a proposed COP decision (appended below). This was provided to the Secretariat on 10 December 1997 with the intent that it be included in a 'prompt start' decision that we understood was being prepared for presentation to the Parties at the final plenary. The intent of this proposed decision was to address the issues raised above and establish and support work efforts to aid in their resolution.

The aim of the subsidiary body work should be to develop a comprehensive accounting approach for all anthropogenic emissions by sources and removals by sinks for the land use change and forestry sector, consistent with the work of the IPCC inventory programme.

As previously expressed, New Zealand's view remains that all anthropogenic emissions by sources and removals by sinks from the land use change and forestry sector should eventually be brought under legally binding commitments. This should be the underlying objective of the ongoing work on sinks by the subsidiary bodies.

We support the establishing of an appropriate process in the June meetings to eventually achieve this objective. The needs of Article 3.4 would be best served in this way.

Division of labour; paragraph 5 of decision 1/CP.3

In terms of the agreed division of labour between the SBI and the SBSTA (FCCC/SBI/1997/16, Annex II), it is not totally clear how the tasks outlined in paragraph 5 of decision 1/CP.3 might be divided up. It may be that some of the issues are better handled in joint meetings of the SBI and SBSTA. That said, the following is a suggested allocation:

5(a) Determination of modalities, rules and guidelines as to how and which additional human-induced activities related to changes in greenhouse gas emissions and removals in the agricultural soil and land-use change and forestry categories shall be added to, or subtracted from, the assigned amount for Parties included in Annex I (Article 3.4).

The determination of modalities and rules probably belongs with SBI, and following this determination, development of guidelines could be done within SBSTA.

5(b) Definition of relevant principles, modalities, rules and guidelines, in particular for verification, reporting and accountability of emissions trading (Article 17).

The definition of relevant principles, modalities, and rules probably belongs with SBI, and following this definition, development of guidelines could be done within SBSTA.

5(c) Elaboration of guidelines for any Party included in Annex I to transfer to, or acquire from, any other such Party any emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy (Article 6).

Elaboration of guidelines is clearly within the mandate of SBSTA.

5(d) Consideration of and, as appropriate, action on suitable methodologies to address the situation of Parties listed in Annex B of the Protocol for whom single projects would have a significant impact on emissions in the commitment period.

The wording would suggest the development of such methodologies would take place outside of the subsidiary bodies, with SBSTA/SBI giving approval (in advance of COP) to agreed methodologies. (Similar to greenhouse gas inventory methodologies being developed by the IPCC/OECD and then being approved for use under the FCCC). There are several ways of approaching this task:

- (i) ask an appropriate international/intergovernmental organisation to develop a methodology which would be considered by Parties;
- (ii) the secretariat could request Parties to make submissions containing suggested methodologies which could be considered directly by Parties;

- (iii) as with (ii) above, but using a roster of experts to perform the analysis before consideration by Parties.

We would note that the above described approach may be useful for some of the other tasks arising from the Kyoto Protocol listed below.

5(e) Analysis of the implications of Article 12, paragraph 10, of the Protocol.

The terms of Article 12.10 are clear.

Other tasks arising from the Kyoto Protocol

In addition to the tasks listed in paragraph 5 of Decision 1/CP.3 there is a substantial amount of work to be completed in advance of the first meeting of the Parties to the Protocol, including:

- (i) guidelines for national systems for the estimation of emissions by sources and removals by sinks (Article 5.1);
- (ii) methodologies for adjusting inventories when IPCC methodologies have not been applied (Article 5.2);
- (iii) guidelines for the preparation of information under Article 7 i.e. national communications and inventories (Article 7.4);
- (iv) guidelines for the review of information (Article 8.1);
- (v) guidance on the composition of expert review teams (Article 8.2);
- (vi) guidelines for the review of implementation of the Protocol (Article 8.4);
- (vii) with respect to the clean development mechanism, elaboration of modalities and procedures [for its operation] with the objective of ensuring transparency, efficiency and accountability through independent auditing and verification of project activities (Article 12.7); and,
- (viii) development of appropriate and effective procedures and mechanisms to determine and to address cases of non-compliance (Article 18).

As noted in paragraph 6 of Decision 1/CP.3 it will be necessary for the FCCC subsidiary bodies to initiate the process for the broad work plan necessary to accomplish these tasks over the 1998-2001 time period.

Given Article 12.10, (vii) above should be considered a 'prompt start' issue and be on the agenda of the June subsidiary body meetings and COP4.

### Existing FCCC subsidiary bodies' work

The subsidiary bodies already have a substantial amount of work underway on national communications, development and transfer of technology, consultations with NGOs, AIJ, research and systematic observation, and matters pertaining to education, training and public awareness. Where there are overlaps between work already underway and requirements for the Protocol, these should be used to advantage.



## Appendix

Methodological issues related to uncertainty and inventory reporting concerns, improving inventory guidelines in the context of their use for legally binding commitments and other outstanding issues, in particular related to land-use change and forestry.

The Conference of the Parties,

Recognising the importance of transparent, accurate and verifiable inventories of anthropogenic emissions by sources and removals by sinks, and the important role that the IPCC Inventory Guidelines will play, in ascertaining compliance by Parties with legally binding commitments,

Recognising that, while Parties agree that to achieve the objective in Article 2 of the FCCC it is important to account for emissions and removals of all anthropogenic sources of greenhouse gases not covered by the Montreal Protocol, concerns have been expressed by Parties relating to the uncertainty and lack of completeness and comparability of the data reported to date by Parties for some inventory categories,

Recognising that, for some inventory categories, it is necessary for the COP to take decisions at a future meeting on what constitutes anthropogenic activities resulting in emissions by sources and removals by sinks,

1. Decides to request that the IPCC, in collaboration with the UNFCCC Secretariat, continue its work programme on greenhouse gas inventories for inventory sectors with higher uncertainty, in particular non-CO<sub>2</sub> greenhouse gases and CO<sub>2</sub> emissions and removals from the land-use, land-use change and forestry sectors, relevant to inventory methodologies, uncertainties of national greenhouse gas emission and removal estimates and guidance for good practice for reducing uncertainties and inventory verification;
2. Decides to request that the IPCC continue its long-term programme of expert meetings and reports, and review and update the IPCC Inventory Guidelines, recognising their use to ascertain compliance by Parties with legally binding commitments;
3. Decides to request that the IPCC continues to give high priority to its on-going development of inventory guidelines and to the completion of work in the land-use change and forestry sector, including the treatment of harvested wood products and emissions from biomass burning and forest fires;
4. Requests the SBSTA, informed by all relevant science and taking into account the progress of the work of the IPCC, to provide a report to the COP at its fourth meeting on what constitutes anthropogenic activities resulting in emissions by sources and removals by sinks in the land-use, land-use change and forestry sectors, and any other sector where this definition is not clear, in order to enable the COP to take decisions on this subject as soon as possible thereafter.

PAPER NO. 6 SAMOA  
(On behalf of the Alliance of Small Island States (AOSIS))

Initial Views of the Alliance of Small Island States (AOSIS) on the  
Preparatory Work for the fourth session of the Conference of the Parties (COP-4)

Ensuring Accountability in the Protocol's 'Flexibility Mechanisms'

I. Introduction

The Alliance of Small Island States (AOSIS) welcomes this opportunity to present its initial views on preparatory work needed for the fourth session of the Conference of the Parties to the UN Framework Convention on Climate Change (COP-4). From the outset of these negotiations, AOSIS has promoted the design of a Convention and a Protocol with legally binding commitments, that followed the basic design principles of certainty, effectiveness and equity. These commitments, and the mechanisms employed to implement them, must be stated clearly, in manner understandable to regulators and those they regulate, comprehensible to the media and the public, and capable of sending strong signals to the market place.

Among other things, this submission, seeks to highlight the many scientific and regulatory uncertainties which the Kyoto Protocol has left unresolved. By scientific uncertainty, we mean, for example, methodologies for calculating and comparing emissions and uptake by sinks of various GHGs from a variety of sources and sectors. These methodologies, even if applied with best possible information will always involve some range of uncertainty.

Regulatory uncertainty, on the other hand, refers to weaknesses in the rules and institutions put in place to monitor, verify and to enforce compliance with commitments. For example, assuming that the IPCC and other bodies are able to reduce scientific uncertainties with regard to methodologies for calculating net emissions, it remains uncertain whether the Protocol's institutions will be capable of confirming that these methodologies have been properly applied. The task is further complicated by the Protocol's flexibility mechanisms, which will allow Parties to meet their commitments, through emissions trading or joint implementation, and that will require the Protocol's institutions to track rights and obligations as they are exchanged between Parties and, potentially, with the private sector. The extremely innovative and untested character of these mechanisms raises uncertainties as to whether they will increase or undermine the Protocol's effectiveness. It also remains to be decided whether it is the buyer or the seller who must beware in the operation of these new flexibility mechanisms.

A. Techniques for reducing or accounting for uncertainty

We are supportive of the use of a range of techniques available to the Parties for reducing or accounting for scientific and regulatory uncertainty, through the use of caution, experimentation, and discounting. More specifically, the Convention and the Protocol processes should allow opportunities for Parties to:

- increase the use and reliance upon objective and science-based processes and institutions, such as the IPCC and ad hoc technical advisory panels;
- restrict the scope of the Protocol's activities to only those with a higher degree of certainty;
- postpone or condition the authorisation of activities until uncertainties are resolved or reduced;
- require the use of discounting to take risks associated with uncertainty into account, to create disincentives for the use of less certain activities and to promote further the reduction of uncertainties;
- strengthen processes and institutions related to monitoring, verification and compliance in order to promote transparency and to expose those taking advantage of uncertainties;
- ensure that, where there is an inconsistency of approach within the Protocol with regard to reducing scientific and regulatory uncertainty, that the highest possible standard is applied in each circumstance; and
- encourage 'learning by doing' by piloting flexibility mechanisms.

#### B. Internalising the costs of flexibility

Our approach to flexibility mechanisms can be characterised as having the dual objective of ensuring that emissions reduced through these mechanisms are achieved in manner that is both cost effective and environmentally effective. Efforts to ensure environmental effectiveness, by reducing scientific and regulatory uncertainty may be criticised as raising the transaction costs of mechanisms that were designed to be cost-effective, thus defeating their purpose.

While it is true that high transaction cost and an over-burdensome bureaucracy must be avoided, it is also true that some portion of the cost differential between emissions reduction activities in investor states and in those in host states results from lower regulatory capacity in host states. Furthermore, the complex nature of these flexibility mechanisms may require additional oversight at the international level that necessarily entails additional transaction costs. In these circumstances, raising transaction costs to ensure environmental effectiveness is entirely appropriate.

#### II. Comments on specific issues

The Secretariat has specifically requested comments on preparatory work needed for COP-4 on the 5 items indicated in 1/CP.3.

##### A. Methodological work on sinks

1/CP.3, para 5(a): Determination of modalities, rules and guidelines as to how and which additional human-induced activities related to changes in greenhouse gas

emissions and removals in the agricultural soil and land-use change and forestry categories shall be added to, or subtracted from, the assigned amount for Parties included in Annex I, as provided for under Article 3, paragraph 4, of the Protocol.

Our concern with the request by some parties for the blanket inclusion of agriculture, land use change and forestry sectors and sources ("sinks") in the Kyoto Protocol are well known and need not be restated here. It is worth recalling, however, that our concern with sinks had to do with the fact that their use would increase regulatory options, introduce uncertainties, and distract the Protocol from focusing on its main policy task of shifting the global economy away from its excessive dependence on fossil fuels.

We continue to believe that there are a number of unresolved scientific uncertainties and methodological inadequacies associated with both Article 3.3 and Article 3.4 of the Protocol. In this regard, we wish to again underline the view that methodological weaknesses and scientific uncertainties associated with sinks has lead to gaps in data, and a lack of comparability between information already reported by Annex I Parties. These shortcomings will make the credible assessment of compliance with Article 3 commitments extremely difficult. This challenge will only be compounded by the introduction of flexibility mechanisms that will depend heavily upon common and verifiable methodologies to ensure the comparability of data and the demonstration of compliance.

Recognising that Article 3.3 and 3.4 allow for a staged approach for the treatment of emissions from sources and removals by sinks in the agriculture, land use change and forestry sectors, we feel that it is even more critical that the Parties adopt a 2-track approach to resolving and accounting for uncertainties in these areas by:

- 1) accelerating efforts to improve and harmonise methodologies for calculating emissions and removals from these sectors; and
- 2) capping or discounting the use of removals from those sectors where significant uncertainties remain.

We recognise that some Parties attach great importance to the early completion of the decision making process on the issue of sinks. These Parties must also recognise that other Parties like the AOSIS members are extremely concerned with the need to avoid unnecessary loopholes and the creation of perverse incentives. Therefore, to facilitate the adoption by the COP and the COP/MOP of methodologies for the accounting of sinks, we suggest that SBSTA-8 should request that the IPCC prepare, as a matter of urgency, a special report on the scientific and technical issues surrounding sinks. The IPCC should address the issues that are unresolved from a scientific and technical perspective as well as those that cannot be resolved by the IPCC without further guidance from the COP/MOP.

Based on this request, the IPCC could examine various methodological tools and approaches for the treatment of sinks with a view to providing an analysis of short and long term consequences that could be expected from each approach, in particular the impact on emissions. The IPCC should also be requested, in particular to study methodologies for "discounting" credits from sinks associated with higher levels of uncertainty that would specify a discount for each sink category that would be applied to any credits generated by

that category towards a Parties assigned amount. The discount values, and modalities for gaining credits in excess of the default values would then be agreed by Parties.

The development of these methodologies may progress in the interim period from now until the entry into force of the Protocol through the work of the COP, under Article 12 of the Convention; and after the entry into force of the Protocol, by the COP/MOP through work on inventory methodologies under Articles 5 and 7 of the Protocol.

## B. Systems of accountability for the Protocol's flexibility mechanism

Decision 1/CP.3 identifies 2 overlapping issues specifically directed at 2 of the Protocol's flexibility mechanisms (Article 17 and Article 6). These are dealt with here together, and the discussions extend to the Protocol's other 2 closely-related flexibility mechanisms in Articles 4 and 12.

- (b) Definition of relevant principles, modalities, rules and guidelines, in particular for verification, reporting and accountability of emissions trading, pursuant to Article 17 of the Protocol;
- (c) Elaboration of guidelines for any Party included in Annex I to transfer to, or acquire from, any other such Party any emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy, as provided for under Article 6 of the Protocol;

The most innovative and untested aspects of the Kyoto Protocol can be grouped together as the Protocol's 4 "flexibility mechanisms". Although they have important, distinguishing features, each is based on the principle that the Protocol will operate most efficiently if Parties and/or private entities are allowed to invest in emissions reduction opportunities where they are cheapest to achieve. In effect this will allow Annex I Parties and, in some cases, private entities, to purchase, or invest in the creation of "emissions reduction units" outside their territories, which can then be used to offset their obligations under the Protocol.

### 1 . Accountability and compliance

The acceptance of this "extraterritorial" achievement of sovereign obligations is based on the assumption that emissions reduction efforts are equally valuable contributions to the achievement of Article 3, regardless of where they take place. For this assumption to be confirmed with confidence, "principles, modalities, rules and guidelines" must be designed that deliver a level of regulatory and scientific confidence equivalent to the highest common denominator of national circumstances among the Protocol's parties. In other words, before an emissions reduction unit generated in Party A can be offset against any part of an amount assigned to Party B, the rules adopted under Articles 4, 6, 12 or 17 for verification, reporting and accountability must be able to demonstrate that the regulatory mechanisms in place in Party A are as effective as those in Party B.

This requires either a harmonisation of rules for verification, reporting and accountability between participating Parties at the domestic level or the intervention of regional or international rules with equivalent "bite". Furthermore, because there will be a shared, global

interest of all Parties to ensure that arrangements between two or more Parties are jointly achieving the relevant part of an assigned amount, the Protocol must provide multilateral oversight to ensure verification, reporting and accountability.

The proponents of the Protocol's flexibility mechanisms have consistently emphasised the great need for strong compliance mechanisms at both the domestic and international level for joint implementation and emissions trading operate in a way that both sovereign and private investors find credible. For these reasons, AOSIS would support requiring Parties wishing to participate in these mechanisms to demonstrate that, through domestic, regional or international arrangements, the selling Party has put in place systems of verification, reporting and accountability that are of at least as high a standard as those in place for the "buying" Party.

Furthermore, at the international level, AOSIS strongly supports the establishment, under Article 18, of "appropriate and effective procedures and mechanisms to determine and to address cases of non-compliance with the provisions of this Protocol, including through the development of an indicative list of consequences, taking into account the cause, type, degree and frequency of non-compliance." It would, furthermore, wish to see, prior to the operation of any emissions trading regime adopted under Article 17, the adoption, by means of an amendment to the Protocol, a list of binding consequences that could be associated with non-compliance. Any Party wishing to participate in an Article 17 trading regime would be required first to have accepted such an amendment under Article 20 of the Protocol.

## 2. Coverage of sinks

Given its concerns, outlined above, about the inclusion of sinks in the Protocol as a whole, AOSIS appreciates the restraint exercised by the negotiators in making no reference to "removals by sinks" in Articles 4, 12, 17. AOSIS believes this provides Parties with an opportunity to reduce, resolve or account for the inclusion of sinks within each of these mechanisms, in light of the particular regulatory challenges that each mechanism may present. For example, emissions reduction units generated by sinks projects may only be properly offset against parts of an assigned amount emitted from a source of an equivalent life-span.

## 3. Environmental and financial additionality

Relevant primarily to project-based transfers in Articles 6 and 12, additionality requires project proponents to establish that the investment is yielding genuine net reductions in emissions that are additional to what would otherwise have occurred. The concept of additionality can be broken down into the closely related concepts of environmental and financial additionality.

Environmental additionality requires the project proponent to establish that the net result of the investment will be a reduction in global emissions as compared to a baseline of emissions that assumes the investment had not been made. Common methodologies for establishing baselines will be required of projects in both Annex I and non-Annex I Parties. Furthermore, the issue of the life-span of the emission reduction units must be taken into account for the purpose of estimating environmental additionality.

Financial additionality requires an assessment of whether the investment would have taken place in the absence of the regulatory incentive provided by the Convention or the Protocol. Financial additionality is important to regulators because it can provide important evidence for environmental additionality -- i.e., the fact that additional financial resources are flowing towards climate friendly projects may provide important evidence that the emissions reductions produced by that investment might not otherwise have occurred.

Proof of financial additionality is important to developing countries in particular, because it helps reassure them that GEF resources, "regular" flows of Official Development Assistance, or Foreign Direct Investment, are not being redirected to CDM-related investments from investments that would otherwise have received a higher national priority. There are explicit references to financial additionality in the AIJ guidelines and AOSIS believes that financial additionality, and in particular, the results of the GEF replenishment should form part of the context of the further development of Article 12. However, should the "financial additionality" of the GEF replenishment be brought to bear on the evolution of Article 12, then Parties will need to examine what role, if any, the GEF will play in the implementation of the provisions of this Article.

#### 4. Certification provisions

Each of the Protocol's flexibility mechanisms requires some form of "government approval" either at the point of transfer, or under Article 3, at the point that the part of the assigned amount or emissions reduction unit is added to or deducted from the Annex I Parties' assigned amount. However, only Article 12 provides for a process of auditing and certification that would provide for an objective assessment of whether the transfer was likely to result in net emissions reduction.

The additional guidelines and rules that will be developed for Article 6, 17 and, should seek to take the precedent set by Article 12 into account by requiring that certification procedures be established for emissions reduction units generated and traded through these mechanisms, as well.

#### 5. Compliance conditionality

The rush of the Kyoto negotiations led to an inconsistency in the Protocol's approach to flexibility is its strong rules on compliance conditionality under Article 6 transfers while it is silent for other mechanisms. Under Article 6.1(d), an Annex I Party is prohibited from acquiring emissions reduction units unless it is in compliance with its inventory and reporting obligations under Articles 5 and 7. Furthermore, should a question arise through the Protocol's In Depth Review procedures with regard to a Party's compliance with Article 6, its may not apply its emission reduction units until the question is resolved.

Regulatory risk associated with project-based flexibility mechanisms could be further reduced by allowing emissions reductions units to be certified and transferred only after the activity has been completed. The text of Article 6 and 12, which refer to emissions reductions "resulting from" project activities provides the basis for this "ex post" approach .

AOSIS believes that there are strong arguments for extending compliance conditionality to emissions reduction units under Article 12, and under Article 17, and for providing for "ex post" certification for emissions reduced through activities under Articles 6 and 12.

## 6. Liability provisions

As an instrument of public international law, negotiated, signed and ratified by states, the Kyoto Protocol will represent an exchange of sovereign obligations, and be subject to classical international rules of state responsibility. However, the flexibility mechanisms outlined above anticipate that the static obligations reflected in the allocation of commitments in Annex B, will be made fluid, allowing for a potentially infinite series of transactions through which emissions reduction units representing the Annex B commitments are bought, sold and reallocated.

Article 4.5 contains the only clear liability provision related to the Protocol's flexibility mechanisms. It operates on the principle that the seller or the transferor of the emissions credit bears the full risk of the bargain.

However, transition and developing countries wishing to participate in Article 6, or in CDM projects should be aware Article 4.5 could provide a precedent for any liability rules that emerge under that mechanism, that may seek to hold host countries liable should the projects they are hosting fail to generate the promised emissions reductions. In these transactions, a potentially far wider range of actors may be responsible for the success or failure of the project, including in the design, funding and in the certification of the project. This complicates considerably the legal relationships and the chain of liability associated with an "emissions reduction unit". Disputes could arise between and among states, private entities, and intergovernmental organisations, each of which may share an interest in and a responsibility for the success or failure of a project.

AOSIS believes that liability rules developed for the Protocol's flexibility mechanisms, particularly those involving developing countries and the private sector need to be designed to ensure that, responsibility is spread equitably with regard to which participants are enjoying the "benefit of the bargain."

## 7. Maintaining the bargained-for allocations

Finally, the bargain struck in Kyoto, however imperfect, represents allocation of obligations based, to some extent on an appropriate allocation of burdens among Annex I countries and between Annex I and developing countries. Each of the Protocol's flexibility mechanisms provides an opportunity for market and other disciplines to redistribute these burdens through a principles of cost-effectiveness. In order to generally maintain a sense of equity, and more specifically, to ensure that Annex I countries take action domestically, Articles 6 and 17 require that JI and emissions trading are supplemental to domestic action. Article 12 requires that the CDM can "contribute to compliance with a part of" Article 3 commitments, as determined by the COP/MOP.

AOSIS believes that, in preparation for COP-4 Parties should explore how each of these provisions should appropriately limit the use of flexibility mechanisms to preserve aspects of the allocation reflected in Annex B.



## 8. Administration and adaptation fees

At present only the CDM under Article 12 makes express provision for the assessment of administrative fees for the application of an adaptation surcharge. There are strong policy reasons for both of these fiscal instruments, to ensure the mechanism is self-supporting and to establish a reliable source of funds for a long neglected aspect of the climate change regime. The exclusive application of these fees to Article 12, raises questions as to how Article 6 and Article 17 mechanisms will pay their way, and may provide disincentive for investments in the CDM vis a vis the Protocol's other flexibility mechanisms.

AOSIS therefore proposes that administrative and adaptation surcharges should be applied equally to all transactions certified under the Protocol's other flexibility mechanisms.

### C. Single project impact assessment

- (d) Consideration of and, as appropriate, action on suitable methodologies to address the situation of Parties listed in Annex B of the Protocol for whom single projects would have a significant proportional impact on emissions in the commitment period.

AOSIS is concerned generally that, unless very narrowly defined, single project exceptions could provide substantial loopholes in Article 3 commitments, and reserves its comments until presented with specific proposals from the proponents of such methodologies.

### D. Pre-commitment period banking

- (e) Analysis of the implications of Article 12, paragraph 10, of the Protocol.

Prior to the first commitment period it is not possible for a Party to formally "bank" emissions reductions efforts to offset its assigned amount in the first commitment period. With one significant exception. It appears that emissions reductions units generated through the CDM may under Article 12.10, from the year 2000, be banked and used to offset some, as yet undefined, "part of" a Parties' assigned amount.

The potential size of this loophole will depend largely on how quickly the Protocol enters into force and the COP/MOP is able to design the operation of the CDM. Conflicts may arise if, as seems likely, the CDM is not ready for operation prior to 2000. AOSIS will seek to ensure that any procedures put in place by the COP to operate an "interim CDM" are of as least as high a standard as those required by the Protocol. Prior to the certification of any 12.10 offsets, the COP must also adopt the requisite rules anticipated under other Articles of the Protocol, on reporting, monitoring, verification, In Depth Review and non-compliance.

### E. "Evolutionary" process

The question of "commitments" on the part of developing country Parties to the Protocol was a divisive one during the negotiations leading up to and including Kyoto. There is every reason to believe that this "debate" will resurface at COP 4 with potentially tragic consequences that almost torpedoed the negotiating atmosphere in Kyoto. Against this backdrop, Parties may wish to consider the establishment of an ad hoc process at

SBI/SBSTA-8 to handle discussions on issues related to the original Article 10, which it may be recalled was included in the AOSIS Protocol proposals. Questions that will have to be addressed by this ad hoc process should include what actions or efforts it is reasonable to expect from developing countries. This must be discussed in the context of the priorities of poverty eradication and sustainable development, while cognisant of the threats posed by climate change to the developing countries. At the same time it is imperative that efforts by the Annex I Parties to assist such efforts by developing countries be given high prominence in the discussions.

PAPER NO. 7 SOUTH AFRICA

View on preparatory work needed for COP-4

1. BACKGROUND

During the third session of the Conference of the Parties held in Kyoto in December 1997, the Chairman of the Subsidiary Body for Scientific and Technological Advice and the Chairman of the Subsidiary Body for Implementation were requested to give guidance to the Secretariat on preparatory work needed for the consideration by the fourth session of the Conference of the Parties of a number of matters (1/CP.3), which are listed below.

1.1 5 (a) Determination of modalities, rules and guidelines as to how and which additional human-induced activities related to changes in greenhouse gas emissions and removals in the agricultural soil and land-use change and forestry category shall be added to, or subtracted from the assigned amount for Parties included in Annex I, as provided for under Article 3, paragraph 4, of the Protocol;

Article 3 (4) is quoted below for convenience.

Article 3

4. Prior to the first session of the Conference of the Parties serving as the meeting of the Parties to this Protocol, each Party included in Annex I shall provide for consideration by the Subsidiary Body for Scientific and Technological Advice data to establish its level of carbon stocks in 1990 and to enable an estimate to be made of its changes in carbon stocks in subsequent years. The Conference of the Parties serving as the meeting of the Parties to this Protocol shall, at its first session or as soon as practicable thereafter, decide upon modalities, rules and guidelines as to how and which additional human-induced activities related to changes in greenhouse gas emissions and removals in the agricultural soil and land use change and forestry categories, shall be added to, or subtracted from, the assigned amount for Parties included in Annex I, taking into account uncertainties, transparency in reporting, verifiability, the methodological work of the Intergovernmental Panel on Climate Change, the advice provided by the Subsidiary Body for Scientific and Technological Advice in accordance with Article 5 and the decisions of the Conference of the Parties. Such a decision shall apply in the second and subsequent commitment periods. A Party may choose to apply such a decision on these additional human-induced activities for its first commitment period, provided that these activities have taken place since 1990.

1.2 5 (b) Definition of relevant principles, modalities, rules and guidelines, in particular for verification, reporting and accountability of emissions trading, pursuant to Article 17 of the Protocol;

Article 17 is quoted below for convenience.

#### Article 17

The Conference of the Parties serving as the meeting of the Parties to this Protocol shall, at its first session, approve appropriate and effective procedures and mechanisms to determine and to address cases of non-compliance with the provisions of this Protocol, including through the development of an indicative list of consequences, taking into account the cause, type, degree and frequency of non-compliance. Any procedures and mechanisms under this Article entailing binding consequences shall be adopted by means of an amendment to this Protocol

1.3 5 (c) Elaboration of guidelines for any Party included in Annex I to transfer to, or acquire from, any other such Party any emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy, as provided for under Article 6 of the Protocol;

Article 6 is quoted below for convenience.

#### Article 6

1. For the purpose of meeting its commitments under Article 3, any Party included in Annex I may transfer to, or acquire from, any other such Party emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy, provided that:

- (a) Any such project has the approval of the Parties involved;
- (b) Any such project provides a reduction in emissions by sources, or an enhancement of removals by sinks, that is additional to any that would otherwise occur;
- (c) It does not acquire any emission reduction units if it is not in compliance with its obligations under Articles 5 and 7; and
- (d) The acquisition of emission reduction units shall be supplemental to domestic actions for the purposes of meeting commitments under Article 3.

2. The Conference of the Parties serving as the meeting of the Parties to this Protocol may, at its first session or as soon as practicable thereafter, further elaborate guidelines for the implementation of this Article, including for verification and reporting.

3. A Party included in Annex I may authorize legal entities to participate, under its responsibility, in actions leading to the generation, transfer or acquisition under this Article of emission reduction units.

4. If a question of implementation by a Party included in Annex I of the requirements referred to in this paragraph is identified in accordance with the relevant provisions of Article 8, transfers and acquisitions of emission reduction units 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 any issue of compliance is resolved.

5(e) Analysis of the implications of Article 12, paragraph 10, of the protocol.

Article 12(10) is quoted below for convenience.

#### 1.4 Article 12

10. Certified emission reductions obtained during the period from the year 2000 up to the beginning of the first commitment period (2008 - 2012) can be used to assist in achieving compliance in the first commitment period.

In terms of Article 3(2) progress in achieving commitments has to be shown by 2005.

#### COMMENTS

It is assumed that the implications to be analyzed are what impacts the transfer of reductions achieved earlier to the first commitment period defined in terms of Article 3(7), will have on overall reduction.

Any mechanism that encourages countries to pursue reductions as soon as possible should be encouraged. In essence what is being said here is that any reduction in emissions achieved prior to the actual commitment period should be credited in terms of commitment. This approach should be supported providing a certification system has been agreed.

#### 2. ISSUES TO BE CONSIDERED

##### 2.1 5.(a) Agriculture and Land Use

Determination of modalities, rules and guidelines as to how and which additional human-induced activities related to changes in greenhouse gas emissions and removals in the agricultural soil and land-use change and forestry categories shall be added to, or subtracted from, the assigned amount for Parties included in Annex 1, as provided for under Article 3, paragraph 4 of the Protocol:

Distinctions between natural and anthropogenic sinks

- \* How to distinguish between managed part of "natural" sink and rest. Particularly as more forests become managed.

Carbon stocks within wood products:  
Are these to be included and how?

Creation of sinks should not have negative impacts on other components of environment, including social or economic issues.

Need to ensure that promotion of sinks takes into account other national and international imperatives. What regulatory functions are needed to ensure that the carbon sequestration function is not maximised over other functions? E.g.

- \* question of promotion of biodiversity
- \* prevention of soil erosion
- \* displacement of local people to plant forests

Uncertainty of sequestration of carbon

Who will be held responsible if carbon re-sequestered is later released into atmosphere?

Methodologies for preparing inventories for anthropogenic sources/sinks

- \* what degree of uncertainties can be allowed?
- \* how will differences in forest and other sinks be dealt with?

Should there be a limit to the extent which certain sinks can be added

- \* discounting according to uncertainty levels of different types of sinks.

Reporting and Verification

- \* establishment of 1990 sink levels - what data exists?
- \* adequate measurement and assessment methodology.
- \* sinks other than CO<sub>2</sub> (what methodologies need to be developed?)
- \* adequate reporting.
- \* system of verification.

## 2.2 Principles, Modalities, Rules & Guidelines For Emissions Trading

Verification of emissions

The verification process must conform to certain principles like:

- Independence
- Transparency and openness
- Recognition by all Parties
- Credibility
- Mutual acceptability'

In order to give practical effect to the principles the following issues need to be considered:

- \* Competency of the certifiers or auditors?
- \* Accreditation of auditors
- \* Role of national accreditation systems
- \* Recognition of national accreditation systems

- \* Guidelines for recognition
- \* Mutual recognition of emission certificates

## 2.3 QUALIFICATION AND ACCOUNTABILITY

Consideration needs to be given to the following:

- \* Criteria for emission reduction quantification
- \* How to define the period/permanence of reductions - including criteria for recognition for reductions from 2000
- \* Base year for reductions to qualify for trading
- \* Nations qualifying for emissions trading (including of entry of newcomers)
- \* Percent of trading permitted
- \* Mechanisms to address the potential negative impacts of emissions trading on developing nations especially knock on economic impacts and means to measure this
- \* Criteria for banking and borrowing
- \* Penalties for non-compliance
- \* Definitions
- \* Time frames and methodologies for developing nations to participate in trading
- \* Policies and measures eligible for trading
- \* Mechanisms/rules for changes to the system
- \* Rules for participants -Governments, private sector, NGO's
- \* Dispute settlement

## 2.4 TRADE IN EMISSION REDUCTION UNITS

Consideration needs to be given to the following:

- \* Long term implications of crediting mechanisms
- \* Initial starting point based upon the principle of global equity.
- \* Start Annex 1 nations with a CO2 debt?
- \* Allocate theoretical but non-tradable credits to developing nations
- \* Consider a time restriction on credits - after a certain period they expire - e.g. After a particular target period set under the protocol such as 2012 for Kyoto.
- \* Mechanisms to ensure new entrants are able to start trading on an equitable basis to historical traders
- \* Definition of limits to percentage of total reduction target which may be achieved using emission reduction units
- \* Units to use for emission reduction units
- \* Links to AIJ and JI
- \* Monitoring, verification and audit mechanisms, including establishment of central banking and monitoring mechanisms
- \* Market mechanisms

PAPER NO. 8 SWITZERLAND

Issues related to the implementation of the Kyoto Protocol to be considered by COP 4

In response to the call at the third session of the Conference of the Parties for comments concerning the various matters related to the implementation of the Kyoto Protocol, Switzerland presents the following views.

Sinks

1. Further methodological work by the IPCC is required on guidelines for inventories for direct human-induced land-use change and forestry (LUCF) and agricultural soil related activities, as well as decisions from SBSTA. The issue of uncertainties should be addressed with the aim of reducing them from the scientific and technical point of view (better emission factors, activity data and coverage). Furthermore, more precise definition is needed for "anthropogenic activities", "sink", "managed/non managed forest". Decisions are also needed on how to treat harvested wood throughout its full life cycle as well as forest fires from the point of view of emissions. In order to assure uniform reporting, presently adopted IPCC Guidelines for LUCF and agricultural soil related emissions and removals should be revised as soon as possible in the light of (1) these improvements and (2) an assessment of Parties experiences with their application to date.

2. Parties which are interested in including new categories under Art. 3.4 of the Kyoto Protocol shall be invited to make presentations of practical applications (project types, methodological approaches, and related verification procedures) in the categories they envisage. Open questions linked to such proposals shall be subject to discussion among all interested Parties. For this purpose, the Secretariat is invited to organise hearings (with the participation of experts, i.a. from IPCC) in the course of a future SBSTA meeting. On the basis of these hearings, eligibility for inclusion of new categories/project types shall be assessed by SBSTA, which then may formulate a recommendation to the COP.

3. Concerning Joint Implementation to sequester carbon, Switzerland proposes the following additional eligibility criteria : (i) the projects shall result in net carbon sequestration at the national level (ii) they shall contribute to local benefits generation (taking into account the interests of indigenous and local populations) (iii) they shall contribute to sustainable management of natural resources (e.g. conservation of eco-systems, biodiversity, forests and soils; substitution of fossil fuels). Furthermore, Switzerland considers necessary to solve issues on baselines for carbon sequestration and on benefits sharing.

4. Sink enhancement projects shall have a long-term duration and be sustainable. They shall be subject to project related long-term monitoring. An adequate monitoring scheme as well as the appropriate reporting requirements need to be defined by the competent Convention bodies.

Article 6: Annex I transfers of Emission Reduction Units (ERU)

According to Art. 6, it is the COP serving as the MOP to the Protocol that may further elaborate guidelines for ERU transfers, so no decision is necessary at COP4. Still, we



believe that the SBSTA should consider how it can synthesize the work being done by experts in other fora and use the experience that is being gained by the Secretariat through its methodological work in the framework of the AIJ Pilot Phase to develop standard methodologies and/or guidelines for:

- baseline determination,
- project monitoring and verification,
- reporting on and accounting for JI transfers (including provisions for banking of ERUs transferred prior to the first budget period) and
- implementing paragraph 6.4 of the Protocol.

The SBSTA should also consider what additional rules or guidance might be required for transfers conducted by legal entities.

Article 12: implications of transferring non-Annex I Certified Emission Reductions (CER) beginning in 2000

Although decision 1/CP.3 only refers to the issue of banking of CERs prior to the first commitment period in the context of the Clean Development Mechanism (CDM), SBSTA and/or SBI should address several other issues as well. It will be important, for example, to decide on the continuation/ conclusion of the AIJ pilot phase and the implications of this for the establishment of rules & guidelines for the CDM.

There is also a need to assign responsibility for addressing the other design issues surrounding the CDM. In our view, the Secretariat should be mandated to promote and coordinate a series of regional consultations with a broad constituency (government, private sector, NGOs, IGOs) to scope out possible options for institutional arrangements & the management structure of the mechanism (mandates of the various bodies, entities appointed to conduct the various tasks) as well as for its mode of operation with respect to the following functions:

- designation by the COP/MOP of operational entities to certify emissions reductions (Art. 12.5),
- certification of emissions reductions resulting from each project activity (Art. 12.5),
- assisting in arranging funding of certified project activities (Art. 12.6) and
- assisting developing countries in meeting the costs of adaptation (Art. 12.8).

If consultations are undertaken prior to COP4, the Secretariat could be asked to prepare a synthesis of views expressed on the various institutional and operational options and to identify issues for further consideration by the SBSTA and the SBI at future sessions.

Methodological issues could be addressed in parallel to the institutional questions, drawing from the work on baselines, monitoring, verification, reporting, accounting, etc. to be undertaken in the context of Art. 6 and the AIJ pilot phase.

## Emissions Trading

In the view of Switzerland, key principles for emissions trading are: (i) environmental effectiveness/credibility; (ii) economic efficiency/practicability; (iii) equity; and (iv) supplemental nature to domestic actions.

At its June session, the SBSTA should strive to develop a work plan and a time table for reaching consensus on a set of minimum rules and the international and domestic institutions needed to establish a credible and efficient trading system.

Important issues for Switzerland, which SBSTA should deal with are:

- \* issues such as: who trades (question of legal entities); what is traded (the unit of transfer); when trading can begin
- \* definition of "supplemental"
- \* requirements for reliable inventories of the assigned amounts on the best available and comparable methodologies
- \* requirements for international and national systems for tracking, accounting, recording and reporting of transfers
- \* mechanism(s) for dealing with cases of non-compliance
- \* the need of the establishment of suitable institutions and mechanisms to ensure the above
- \* the inter-relationship between emission trading and other transfer mechanisms (Art. 6 and 12 of the Kyoto Protocol).

The SBSTA (via the Secretariat) should seek inputs from Parties, private sector experts in the field of financial markets and relevant organisations. Informal consultations and small expert workshops prior to Buenos Aires might help to clarify key issues.

## Single projects

As a matter of principle, cases of non-compliance with emission targets should be dealt with in the context of Art. 18 of the Kyoto Protocol and the multilateral consultative process referred to in Art. 13 of the Convention and in Art. 16 of the Kyoto Protocol.

Switzerland can not accept a separate process of assessment for "unforeseeable events" as this weakens the value of the agreement reached in Kyoto and would be a threat to its effectiveness and credibility. The Kyoto Protocol grants great flexibility to Parties, inter alia by differentiating emission targets and by offering a broad choice of instruments at home and abroad for meeting commitments.

The establishment of a practicable allocation regime for emissions linked to the international trade of goods has been addressed earlier within SBSTA, where the resolution of related "methodological issues" is still pending.

PAPER NO. 9 UNITED KINGDOM OF GREAT BRITAIN  
AND NORTHERN IRELAND

(On behalf of the European Community and its member States)

VIEWS OF THE EUROPEAN COMMUNITY AND ITS MEMBER STATES  
ON PREPARATORY WORK NEEDED FOR COP4

Agenda for COP4

The EU considers it is essential that “analysis of the implications of Article 12.10 of the Protocol” (para 5(e) of decision 1/CP.3) is interpreted widely to allow for full discussion of the clean development mechanism at the June sessions and at COP4. In view of the fact that the Protocol allows for Parties to use certified emission reductions from cdm projects from 2000 onwards, it is imperative that work begins as soon as possible to begin to elaborate the necessary modalities and procedures for this mechanism.

The EU also considers that an opportunity will need to be provided at the June sessions for Parties to raise other Protocol issues (such as compliance, monitoring, reporting) which they consider need to be taken forward at an early date in order for decisions to be taken at the first COP/MOP. Whilst we would not envisage a substantive discussion in June or indeed at COP4, these meetings should decide upon how such issues will be dealt with at future meetings and the timetable for this work.

In addition, the EU recalls the statement it made on evolution / review under Article 7.2 of the Convention during the COP3 plenary. The EU believes that the idea of a review of the commitments of all Parties should feature again at COP4 and that there will be a need for preparatory discussion at the June sessions.

Allocation of work

In deciding how to allocate tasks between SBI and SBSTA, our main priorities would be efficiency and the avoidance of delay and duplication. We would therefore envisage a short joint SBI/SBSTA opening session to agree the allocation of work and which would also provide an opportunity for any initial, general statements. Work should then proceed in each subsidiary body as appropriate.

Given the tremendous workload for the June sessions, we believe that where possible consideration of issues by both bodies should be avoided. This would also be consistent with the COP3 decision on Division of Labour, which states that in general one of the bodies will take the overall responsibility in considering an issue (if necessary requesting specific inputs from the other body).

Our suggested split of work would be:

SBI - emissions trading and the clean development mechanism (institutional and financial arrangements) [but see also comments below]

SBSTA - sinks, joint implementation, methodologies for Parties where single projects have disproportional impact on emissions, clean development mechanism (calculation of certified emission reductions).

If it is felt that splitting consideration of the clean development mechanism in this way would cause confusion and delay as one body waits for the other to resolve a particular issue, an alternative would be to deal with the issue in a joint SBI/SBSTA session. This is consistent with the approach set out in the COP3 decision on Division of Labour.

Similarly, if other Parties wish SBSTA also to address emissions trading, the EU would be equally happy for this issue to be dealt with in a joint SBI/SBSTA session. This would again be consistent with the approach set out in the COP3 decision on Division of Labour and would be preferable to SBI and SBSTA both dealing with the issue separately at the June sessions.

#### Role for the Secretariat

Clearly the Secretariat already has a substantial organisational role and provides valuable analytical advice on many issues. There are two new areas in particular where the EU believes that the Secretariat could also usefully provide inputs for the June sessions:

- an analysis of the procedures (such as the Uniform Reporting Format) and methodologies being used under the AIJ pilot phase, to inform the considerations by Parties of how Articles 6 and 12 should operate;
- suggestions as to suitable methodologies to address the situation of Annex B Parties for whom single projects would have a significant proportional impact on emissions in the commitment period.

The Secretariat may also be able to advise on some of the institutional issues arising from the new clean development mechanism, and to draw on the experience and views of existing institutions such as the GEF and UNEP.

The EU would be grateful for early clarification of the Secretariat's work programme. In this context, the EU would also like to underline the importance to Parties of receiving papers or other inputs from the Secretariat at as early a stage of the negotiations as possible.

#### Links with work being undertaken by other bodies

Given the short amount of time before COP4 and the fact that there is only one formal UN negotiating session before then, the EU would underline the importance of making the best possible use of work being undertaken by other organisations. In particular, in relation to emissions trading, we believe that consideration should be given as to how to take account of the extensive work done to date by both UNCTAD and the OECD/IEA Annex I Experts Group. We should certainly avoid trying to reinvent the wheel!