

effectively used by means of establishing adaptation fund managed by an existing institution determined by COP/moP.

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Project validation/registration

➤ Modified (based on 79)

Project activities under the CDM shall:

- (a) Cover at least one of the gases listed in Annex A of the Protocol.
- (b) Result in emission reductions of greenhouse gases listed in Annex A of the Protocol.
- (c) Provide emission reductions that are additional to any that would occur in the absence of the project activity.
- (d) Assist developing country Parties “in achieving sustainable development”, which shall be only determined by the developing country Parties themselves.

B. Project financing

Modified (based on 95)

(merge option 1 and option 2)

Option 1: Funding for CDM project activities shall be provided by the participating Party included in Annex I to the participating Party not included in Annex I on the basis of the CERs acquired from the project activity as returns for the participating Party included in Annex I for meeting part of its quantified emission limitation and reduction commitments under article 3 Of the Protocol. Annex I country Parties may involve private and/or public entities in such funding.

New (insert at the end of 96)

Option 4: CDM projects shall be financed by Annex I participants through bilateral agreement between Annex I participants and Non-Annex I participants.

New (insert at the end of 99)

Option 3: Executive Board shall help provide information on eligible CDM projects and their financing to both Annex I Parties and non-Annex I Parties. If necessary, EB may assist arranging funding of CDM project activities.

C. Project monitoring

➤ Modified (based on 102)

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 certification purpose. The monitoring results shall be entered into an electronic national CDM database. The participants of Annex I Parties should provide the necessary financing and technical support to the participants of non-Annex I Parties for project monitoring.

D. Project verification

➤ **New (insert before 104)**

Independent operational entities designated by the COP/moP shall perform independent auditing of CDM projects in accordance with the methodology and standardized format contained in Appendix C.

E. Certification and acquisition of CERs

Please note that the title of E. is suggested to change as above.

F. Issues related to compliance

New (insert at the end of 114)

Non-compliance issues arising from operation of CDM projects shall be resolved within the framework of the CDM as much as possible. Only when the non-compliance is beyond the framework of the CDM, the issues shall be addressed in accordance with the non-compliance procedure under Article 18 of the Protocol.

G. Adaptation assistance

H. Registration

Please note that the title of H. is suggested to change as above.

Modified(based on 123)

Registration of CERs shall be in accordance with Appendix D.

I. Reporting by Parties

III. INSTITUTIONAL ISSUES

A. Role of the COP/moP

➤ **New(based on 127)**

127 (c) bis Decide to accept or invalidate the CERs acquired; **(insert it between 127(c) and 127(d))**

B. Executive board

➤ **New(based on 131)**

131. (q) bis option 2

Propose to the COP/moP the amount of charges that should be applied to the CERs acquired by Annex I Parties participating in CDM projects in order to meet the administrative costs of the executive board.

Register the projects as CDM projects on the basis of validation reports submitted by the operational entities.

C. Operational entities

D. Parties

➤ **Modified(based on 141, replace 141)**

Each Party participating in the CDM projects shall

- (a) bear overall responsibilities for approval and reporting of CDM projects,
- (b) be responsible for the public and/or private entities that may be involved in the CDM projects in accordance with Article 12 of the Protocol.

E. Administrative

F. Review

➤ **Modified(based on 146)**

The COP/moP shall:

- **modified(replace 146(d))**
 - (d) Review the allocation of the share of proceeds for adaptation projects five years after the adoption of these modalities and procedures;
- **new(insert at the end of 146(d))**
 - (146 (d) bis) Periodically review the needs of developing country Parties particularly vulnerable to the adverse effects of climate change for adaptation assistance under Article 12, paragraph 8;

APPENDICES TO PART THREE: CLEAN DEVELOPMENT MECHANISM

A. Baselines

Modified:

1. Baseline definition

The baseline of a CDM Project should be defined on the basis of the GHG emission level of a given case and its related tech-economic characteristics that would be most likely to occur in the absence of such a CDM project, taking into account the domestic circumstances in the participating developing country Party.

2. Baseline approach

In order to determine the baseline of a CDM project, the specific details in technical processing, energy efficiency, GHG emission and financial performance need to be identified based on the technical specification, standards, local fuel availability, and/or existing operational records of the facilities relating to GHG emission, through an on-site survey if necessary, and on the basis of the future trend perspectives of a given activity that would be most likely to occur in the absence of the CDM project.

3. Dynamic baseline

A dynamic change in baseline over time will often be driven by many factors, including economy, technology and policy development. Such a change is “most likely to occur” in the absence of CDM project activities, as a result, the baseline needs to be adjusted accordingly.

In particular, in case the dynamic baseline level falls down to the CDM project emission level, the CERs of the CDM project should no longer accrue.

B. Validation/registration

Modified:

1. Participating entities shall submit a CDM project proposal to their governments for approval. The governments of the participating Parties should approve the proposal in accordance with the modalities and procedures adopted by COP/moP. An approved project should be registered with EB.

2. Criteria of project eligibility

2.1 The CDM project shall be implemented only between Annex I and non-Annex I country Parties on a voluntary basis and should be approved by the Governments of the participating Parties in accordance with Article 12 of the Protocol.

2.2 CDM is a project - based mechanism, and the CDM activities shall be carried out on a project-by-project basis.

2.3 The CDM project shall bring about real, measurable and long term environmental benefits related to the climate change mitigation, and shall bring about reductions in emissions that are additional to any that would occur in absence of such CDM project.

2.4 Emission baseline that is determined for the CDM project shall meet the criteria adopted by the COP/moP.

2.5 The CDM project shall promote the transfer of advanced environmentally-sound technologies needed in the project by the participating developing country Party.

2.6 Developed country Parties or their public/private entities should fund in developing country Parties the CDM projects which should assist sustainable development and should be compatible with national priorities and needs by the developing country Parties.

2.7 The public funds involved in the CDM project shall be additional to ODA, GEF and other financial commitments of the developed country Parties.

C. Monitoring, reporting, verification and certification/acquisition of CERs

Please note that the title of B. is suggested to change as above.

➤ New (insert before 47 of the Appendix C.)

- (1) The two participants in a CDM project shall develop a detailed monitoring plan containing information on their procedures for accurate, systematic and periodic monitoring of the project;
- (2) The developed country participant should help the developing country participant in providing related monitoring technology, monitoring cost, and necessary training.

D. Registration of CERs

Please note that the title of C. is suggested to change as above.

➤ **New (insert before 50 of the Appendix D.)**

- (1) The EB shall keep the record of the amount of CERs accrued to each participating developed Party from each CDM project.

E. Procedures for the operation of the executive board

F. Guidelines for operational entities

New (insert it into Appendix F)

- (1) The operation entity should function independently under the guidance of COP/moP and under the supervision of the executive board. Their designation should take into account regional balance.
- (2) Operational entities shall apply the standard methodologies or matured process to certify the CERs under the guidance of the COP/moP. If the information submitted by the project participants is insufficient, operational entities can use information from other sources but it should be coordinated with the Parties involved and agreed by the involved Parties at first.
- (3) Operational entities shall have no operational or financial links with CDM project activities and shall not be entitled to participate in the identification, development or financing of CDM projects.

G Disbursement of the share of proceeds

New (insert it into Appendix G)

- (1) Surcharge shall be levied on the basis of the amount of the CERs acquired by the Annex I Party participating in the CDM project. The rate of the surcharge shall be decided by COP/moP.
- (2) The share of proceeds to cover administrative expenses of EB should be kept to the minimum to ensure that a large amount of the share of proceeds is used to cover adaptation costs.
- (3) The share of proceeds for adaptation costs shall be reasonably distributed and effectively used by means of establishing adaptation fund managed by an existing institution determined by the COP/moP.

H. Adaptation

New (insert it into Appendix H)

- (1) A CDM adaptation fund shall be established to administer the share of proceeds used for adaptation costs. The funding for adaptation through this share of proceeds must be additional to the current and future financing by Parties included in Annex II of adaptation activities under other provisions of the Convention and the Protocol.
- (2) The developing country Parties particularly vulnerable to the adverse effects of the climate change should identify adaptation projects for funding, and should follow

a process of adaptation options identification. Consideration in this respect should be consistent with ongoing work on adaptation under the Convention. Such a developing country Party should be assisted with capacity building at all levels in order to be able to carry out adaptation activities.

Amendments and Additions Proposed by China on “Emissions Trading” under Article 17 of the Protocol

I. NATURE AND SCOPE

A. Purpose

147. The Parties included in Annex B may participate in emissions trading for the purpose of fulfilling their commitments under Article 3. Any such trading shall be supplemental to domestic actions for the purpose of meeting quantified emission limitation and reduction commitments under that Article. Any such trading is only an instrument for “transfer and acquisition”, between Annex B Parties, of part of the assigned amount under Article 3 of the KP.

Amendment (add at the end of paragraph 147)

148. Such “transfer and acquisition” shall be transparent and in compliance with the relevant provisions of the KP.

(Add as the paragraph 148 bis)

B. Principles

149. In designing “emissions trading” under Article 17 of the KP, nature and scope, principles and related basic elements of emissions trading under Article 17 of the KP shall be addressed firstly.

Addition (add before paragraph 149 as a separate paragraph)

C. Supplimentarity

150 . The design and implementation of emissions trading under Article 17 must not in any way compromise the modification of longer-term trends in GHG anthropogenic emissions and concentrations. Commensurate non-compliance processes must be put in place.

- (a) Annex B Parties access to Article 17 should be contingent on satisfaction of prescribed domestic effort in fulfillment of commitments under Article 3.
- (b) Domestic actions must be the main means of achieving the quantified emission limitation and reduction commitments.
- (c) Therefore, a concrete ceiling for the total assigned amount of acquired from the emission trading under the Article 17 of the Protocol should be defined in quantitative and qualitative terms based on equitable criteria.

(Add as paragraph 150 bis)

D. Participation

152. "Emissions trading" under Article 17 shall be conducted only between or among the Parties included in Annex B to the Protocol. The Parties included in Annex B shall be eligible to "transfer" or "acquire" part of the assigned amount, if they:

Addition (as option 1 bis of paragraph 152)

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Modalities of operation

158. Transfers and acquisitions of any part of the assigned amount could be effected through bilateral or multilateral arrangements between or among Parties included in Annex B, without creating a new international business transaction system or regime.

Amendment (replace the options 1 of the paragraph 158)

C. Issues related to compliance

165. If an Annex B Party is in non-compliance with its commitments, that part of the assigned amount that has been "transferred" shall be invalidated."

Addition (as the option 1 bis of paragraph 165)

D. Registration

Addition (replace Registries by Registration)

E. Reporting by Parties

176. Any Annex B Parties participating in the transfers and acquisitions of parts of assigned amounts under Article 17 of the Protocol shall include in their national inventory, to be communicated to the Secretariat under Article 7.1 of the Protocol, information on any part of an assigned amount added to or removed from "transfers" and "acquisitions" under Article 3.10 and 3.11 of the KP in the relevant year.

Addition (as the option for the chapeau of the paragraph 176)

III. INSTITUTIONAL ISSUES

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

178. The COP shall define the relevant principles, modalities, rules and guideline, in particular for verification, reporting and accountability for emissions trading.

Addition (as paragraph 178 bis)

C. Administrative support

183. The secretariat shall make information on the Parties that are eligible to participate in the **transfers and acquisitions** of parts of assigned amounts under Article 17 of the Protocol publicly available.

Addition (as the option 1 bis of the paragraph 183)

D. Review

184. The COP shall review the principles, modalities, rules and guidelines governing the operation of the **emissions trading** under Article 17 of the Protocol.

Addition (as paragraph 184 bis)

REPUBLIC OF COSTA RICA¹
PARTIAL PROPOSAL

CLEAN DEVELOPMENT MECHANISM

I. NATURE AND SCOPE

A. Purpose

The CDM is a project-based mechanism conceived and introduced in the Protocol to:

- (a) Assist Parties not included in Annex I in achieving sustainable development and in contributing to the ultimate objective of the Convention;
- (b) Assist Parties included in Annex I in achieving compliance with their quantified emission limitation and reduction commitments under Article 3; and
- (c) Assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation by ensuring that a share of the proceeds of each project is assessed for this purpose.

B. Principles

In their actions to achieve the purpose of the CDM, the Parties shall be guided by Article 3 of the Convention and, inter alia, by the following considerations:

- (a) Nature and scope:
 - (i) Unlike the other mechanisms provided in the Kyoto Protocol, the CDM is the only mechanism which involves the participation of both developed and developing country Parties.
 - (ii) The Protocol has made provision for "Certified Emission Reductions" (CERs) from a CDM project. Accordingly, CERs will enable the participating developed country Party to contribute to compliance with part of its quantified emission limitation and reduction commitments under Article 3 to the extent permissible under the principle of "supplementary" to be decided;
 - (iii) Developed country Parties may fund CDM projects activities in developing country Parties, through project equity financing or by acquiring CERs;

¹ Preliminary version submitted to the UNFCCC Secretariat on 31 January 2000; Spanish original will, along with unofficial translation, be submitted in time for SB12.

- (iv) Developed country Parties may involve private and/or public entities for such funding. In return, the developed country Party, funding the project, will be enabled to meet part of its emission reduction commitment. "Any CERs which a Party acquires from another Party in accordance with the provisions of Article 12 shall be added to the assigned amount for the acquiring Party";
- (v) It must be ensured that "a share of the proceeds from certified project activities": is used to meet costs of adaptation. For these purposes, a CDM adaptation fund should be established;
- (b) Equity: The principle of equity in the Convention must apply to all aspects of the CDM based on equitable developmental rights and to the extent as possible, balanced regional activity. The COP/MOP shall take appropriate action to promote the principle of equity.
- (c) Climate Change Effectiveness: Climate change effectiveness shall be in terms of real, measurable and long-term benefits related to the mitigation of climate change at project level. This should be addressed by taking into account the additional emissions reductions at project level as against a baseline. The benefits related to a project activity would be recognized as real if the actual greenhouse gas (GHG) emissions can be shown to be less than the baseline. The benefits would be recognized as measurable if the actual level of GHG emissions of the project case and the level of GHG emissions in the baseline can be established with a reasonable degree of certainty. The benefits of a project activity would be recognized as long-term if the emission reduction persists over an appropriate period of time taking into account the life span of project activities, and bearing in mind Article 2 of the convention.
- (d) Sustainable Development: Sustainable development priorities must be set by national designated authorities to the UNFCCC according its specific sustainable development objectives and priorities.
- (e) Transparency: The principle of transparency must be observed in all CDM activities, including project approval, implementation, certification, monitoring and verification, establishment of baselines, operation of the Executive Board, as well as regarding costs, risks and liabilities to be incurred by the Parties.
- (f) Non-discrimination: All developing country Parties can participate in CDM project activities on a voluntary basis.
- (g) Capacity Building: Least developed country Parties need assistance to build up capacity in monitoring, reporting and verification, as well as regarding risks and liabilities to be incurred by developing country Party.
- (h) Transfer of Technology. The special needs of a developing country Parties have to be addressed for identifying technology needs and helping enhance capacities for assimilation of technology.
- (I) Adaptation: As provided for in Article 4.8 of the Convention and Article 12.8 of the Protocol, developing country Parties that are particularly vulnerable will be assisted

to meet the costs of adaptation. The COP/MOP of the Protocol shall ensure that a share of the proceeds from certified project activities is used to cover these costs. Adaptation project for funding should be consistent with the developing country Parties national communications.

(j) Compliance: Appropriate and effective procedures and mechanisms to determine and to address cases of non-compliance with the provisions of Article 2 should be established. The procedures and mechanisms should be consisted with the principles of the Convention.

(k) Eligibility Criteria: Eligible project activities, apart from meeting national sustainable development priorities, should ensure access to environmentally-sound technology needed by the developing country Party participating in the project activity.

C. "Part of"/supplementary

"Parties included in Annex I may use CERs accruing project activities to contribute to compliance with 25% of their quantified emission limitation and reduction commitments under Article 3, as define in Annex B to this Protocol".

D. Participation

Participation in a CDM project activity is voluntary and a Party included in Annex I shall only use CERs to contribute to compliance if the involved Party:

- (a) Has ratified the Protocol;
- (b) Is in compliance with all CDM rules, guidelines, compliance regimen and relevant provisions in the Protocol and to be adopted by the COP/MOP.

Private and/or public entities can participate in CDM project activities with the approval of the Parties involved subject to:

- (a) Guidance provided by the CDM Executive Board;
- (b) Compliance with CDM rules and guidelines;
- (c) Compliance with relevant provisions in the Protocol.

The Party or Parties participating in the CDM project activities must be responsible at all stages and in all aspects for the project activity in which they are participating. In cases where no Party included in Annex I or entity resident in such a Party is involved, the host country assumes total responsibility for the project.

E. Share of proceeds

Public and private entities from non-Annex I Parties may finance CDM project activities through CERs acquisitions and or implement projects, according to the national policies of the host countries.

A share of the proceeds from trading in the CDM shall be used to:

- (a) Cover administrative expenses of the CDM and costs pertaining to the activity of the Executive Board. The share of proceeds to cover administrative expenses is set to three per cent of the market value of the CERs;
- (b) Assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation. This responsibility is to be shared among all the Parties, provided that Parties included in Annex I bear a larger share. The share of proceeds for adaptation shall be managed by the entity operating as the UNFCCC financial mechanism. Therefore, the administration of those resources will not be part of the CDM operational aspects.

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Project validation/registration

Project activities under the CDM shall:

- (a) Cover one or more of the GHG listed in Annex A of the Protocol;
- (b) Provide reductions in emissions by sources in one or more of the sector categories listed in Annex A of the Protocol or enhance removals by sinks, as noted in Article 3, paragraphs (3) and (4);
- (c) Assist the host country Party "in achieving sustainable development".

Providing the proper decisions to be adopted by the COP/MOP, based on the recommendation of the IPCC Special Report on Land Use, Land Use Change and Forestry, the modalities for CDM projects on land use change and forestry should be those provided in Article 2, 3 and 6, without discrimination treatment in respect of project activities carried out in developing country Parties.

Registration of a project activity is a prerequisite for the certification and issuance of CERs. A designated national entity shall present the project proposal to the CDM Executive Board. The Executive Board shall accept or reject the project, and decisions on registration by the Executive Board shall be published in a suitable public manner.

A project activity shall be registered by the Executive Board only if:

- (a) It meets the national eligibility criteria for CDM projects established by host Parties, as indicated by a letter of endorsement, and contributes to the sustainable

development country priorities of the Party not included in Annex I. The determination of whether a proposed project activity contributes to sustainable development priorities of the involved Party shall be made solely by the developing country Party;

- (b) It provides emissions baseline that meets the rules and procedures specified in Appendix A. Baselines shall be determined on a project basis. In some cases, in accordance with Appendix A, sectoral baselines and standard baselines for project categories may be applied;
- (c) It is expected to yield real, measurable and long-term benefits related to the mitigation of climate change;
- (d) It is expected to lower emissions from the level that would have occurred in the absence of the project activity;
- (e) Funding in exchange of CERs is additional to commercial investment and additional to funding provided through Official Development Assistance (ODA), the Global Environment Facility (GEF) and other financial commitments of the Parties included in Annex I;
- (f) It provides a monitoring plan, which meets the approved criteria specified in Appendix D, for the collection of data to track the performance of the project as well as the adequacy of the proposed monitoring plan by assessing its method, frequency and accuracy of measurement.

A host country Party may develop its own criteria for project approval based on its domestic circumstances. These criteria shall be made publicly accessible. A Party may also define priority sectors for CDM projects.

A project activity initiated before the COP/MOP, as well as any project activity under the AIJ pilot phase, with the agreement of the participating Parties, shall be eligible for consideration as a CDM project if it meets modalities, criteria and rules applicable to CDM to be defined by the COP/MOP. Following AIJ project validation and registration as CDM project, resultant reductions in emissions by sources and/or enhancements of removals by sinks from 1 January 2000 onwards will be eligible for retrospective certification.

B. Project financing

Funding for CDM project activities shall be provided by the participating Party included in Annex I to the participating Party not included in Annex I in exchange of CERs acquired from the project activity for meeting part of its quantified emissions limitation and reduction commitments. Public and private entities may finance and/or implement projects under the guidelines of Article 12 of this Protocol with specific reference to Decision 1/CP.3, article 5-subparagraph (e). Project financing may be provided by other sources, including multilateral financial entities.

CERs shall be traded through a portfolio approach, under a sole supplier arrangement and by means of a centralized market. This market may operate through regional clearinghouses accredited by the Executive Board. The clearinghouse should be the coordinating office and could serve to facilitate, *inter alia*, the selection and screening of projects and resource mobilization. CERs price shall be set using criteria of joint supply by sectors of the economy, regardless of the origin of the project.

Initiatives to ensure that CDM investments take place in Parties that are often marginalized by purely market-based instruments should be promoted by the Executive Board.

Parties not included in Annex I may propose CDM projects individually or jointly with other Party.

C. Project monitoring

Participants shall develop a monitoring plan containing information on their procedures for systematic and periodic monitoring of the project activities in accordance with the criteria in Appendix D.

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 certifying entity for certification purposes.

The continuing adequacy of the monitoring plan and its implementation shall be assessed by the designated operational entity in its reports to the Executive Board.

D. Project verification

Emission reductions achieved by the certified project activity shall be periodically verified from the monitored data and other pertinent information, in accordance with the methodology and standardized format contained in Appendix D. Verification shall be performed independently by a designated operational entity accredited by the Executive Board and selected by the proponents of the project. It should be of recognized technical capacity to assume the responsibility involved. The verifying entity shall report the results to project participants, the national designated offices from the Party or (ies) involved and the Executive Board.

E. Certification/Issuance of CERs

Certification of emission reductions shall be conducted on a yearly basis, in accordance with Appendix C. The procedure shall be as follows:

Emission reductions from a project activity shall be certified, after they have occurred, only if:

- (a) A participant in the project applies for the certification of the emission reductions resulting from the project during a specific period of time;

- (b) The project activity has been registered by the Executive Board and continues to meet requirements;
- (c) All Parties involved are entitled to participate in the CDM and in compliance with the Protocol, in particular with Articles 2,3,5,7 and 10.

The certification of emission reductions and/or enhancement of removals by sinks shall be performed by an accredited certifying entity, in light of the requirements of Article 12 paragraph (5), upon request of a project participant. The operational entity shall inform the applicant of its decision in writing immediately upon completion of the certification process.

Issuance of CERs shall be performed by the Executive Board on the basis of a report, submitted by the national designated authority which states whether the project meets the necessary requirements and the amount of emissions reductions achieved by the project in the period since the last certification was performed, as reported by the accredited certifying entity. CERs shall be trackable through a registry system.

F. Compliance

Steps to address cases of non-compliance with the provisions of the CDM should be based on guidelines to be laid down by the COP/MOP in accordance with procedures defined under Article 18. Issues arising shall be expeditiously resolved through a general procedure applicable to the Protocol.

In the case of a Party's non-compliance with its obligations resulting from the Protocol, and from its Article 3 in particular, CERs acquired under the CDM should be invalidated, either in full or in part, and can not be counted as the fulfillment of assumed obligations to reduce greenhouse gas emissions.

G. Adaptation

An adaptation fund shall be established to administer the share of proceeds used to assist with adaptation costs. The generation of funding for adaptation through this share of proceeds must be additional to the current and future financing by Parties included in Annex I for adaptation activities under other provisions of the Convention and the Protocol.

The special vulnerabilities and character of small island developing states shall be taken into account and provided for adaptation and capacity-building processes.

Adaptation project activities and measures to be implemented under Article 12, paragraph 8, shall be guided by information from national communications, as set out in decision 11/CP.1

Parties not included in Annex I that are particularly vulnerable to the adverse effects of climate change and wish to receive proceeds from the CDM for adaptation purposes shall prepare a national adaptation programme, taking into account the distribution of actions over time and including estimates of the full cost, with its breakdown into sectors.

Project activities and measures that help particularly vulnerable Parties not included in Annex I to adapt to the adverse effects of climate change shall be financially assisted by the adaptation fund only if they meet the following requirements:

- (a) They shall be country-driven and in conformity with the national strategies and priorities for sustainable development of the Parties concerned;
- (b) They shall be implemented cost-effective manner.

H. Reporting

Parties participating in CDM project activities shall report to the Executive Board on the progress and results of their project activities on a project-by-project basis, using a uniform reporting format to be adopted by the COP/MOP.

Parties included in Annex I participating in CDM projects shall report on their CDM activities to the Executive Board annually within the framework of their reporting commitments under Article 7, paragraph 1, specifying, in a standard format, *inter alia* new CERs issued to the Party as a result of CDM project activities during that year on a project-by-project basis and any CERs that have been retired that year.

Parties not included in Annex I participating in CDM projects shall report annually on their CDM activities to the Executive Board. This report shall include how Parties included in Annex I have been assisted in achieving compliance with their commitments under Article 3.

III INSTITUCIONAL ISSUES

A. COP/MOP Role

“The CDM shall be subject to the authority and guidance of the COP/MOP”

In relation to methodological and operational issues, the COP/MOP shall, *inter alia*:

- (a) Determine the “part of the quantified emission limitation and reduction commitments under Article 3” which Parties included in Annex I can meet through CERs;
- (b) Elaborate, review and approve methodologies for determining baseline, monitoring, verification, certification, reporting formats and technical guidelines for operational application;
- (c) “Ensure that a share of the proceeds from certified project activities is used to cover administrative expenses as well as to assist developing country Parties that are particularly vulnerable to the adverse effects of climate change to meet the costs of adaptation and determine that share;

- (d) Determine eligibility criteria for adaptation under Article 12 paragraph (8) and designate the entity entrusted with the operation of the financial mechanism of the Convention.

In relation to institutional issues, the COP/MOP shall, *inter alia*:

- (a) Determine the modalities and procedures governing the operation of the CDM;
- (b) Define the terms of reference for and establish the Executive Board;
- (c) Designate regional operational offices (clearinghouses) or establish guidelines as a basis for delegating this function and decide which functions they will carry out;
- (d) Disqualify, upon recommendation of the Executive Board, operational entities from certifying emission reductions if the Executive Board concludes that the requirements for the certification of the emission reductions have not been fulfilled;
- (e) Determine the basis for private and public sector participation in CDM projects;
- (f) Establish sanctions and penalties for non-compliance in the framework of the Protocol and the CDM.

In instances of a dispute arising between Parties, transfers and acquisitions of CERs may continue to be made after the issue has arisen, provided that any such CERs may not be used by a Party to meet its commitments under Article 3 until the issue is resolved. Arbitration for disputes between Parties shall be undertaken in accordance with Article 14 of the Convention.

B. Executive Board

The Executive Board shall supervise and be responsible for the daily management of the CDM as a separate standing body of the COP/MOP. The Executive Board shall be fully accountable to the COP/MOP and shall carry out all instructions and all other functions assigned to it by the COP/MOP.

In relation to methodological and operational issues, the Executive Board shall, *inter alia*:

- (a) Supervise that CDM project activities to ensure that these are in conformity with the Convention, the Protocol and all relevant decisions by the COP/MOP;
- (b) Determine criteria and operational guidelines for baselines based on principles, modalities, rules and guidelines adopted by the COP/MOP;
- (c) Ensure that information used for project evaluation, including standardized baselines, is publicly accessible;

- (d) Provide guidance for public and/or private entity participants following decisions recommended by the COP/MOP;
- (e) Receive CDM project proposal from national designated entities of Parties, validate projects on the basis of certification/verification reports submitted by entities and announce the validation of projects;
- (f) Issue CERs on the basis of certification/verification report prepared by an accredited entity and submitted by a national designated entity from Parties;
- (g) Publish, in a timely manner, information on transfers of CERs, including, *inter alia*, dates, project type, project start date, participating Parties and organizations, and quantity and prices of CERs transferred;
- (h) Maintain databases of projects and of emission reductions, achieved under the CDM including identification numbers, project description, baseline approaches, organizations and Parties involved relevant dates, etc;
- (i) On the basis of a centralized trading operation play a fiduciary role which will:
 - (i) Guarantee a favorable commercial position to negotiate a fair price for the Parties involved;
 - (ii) Ensure the transparency and credibility of the trading process;
 - (iii) Reduce transaction costs;
 - (iv) Lower the environmental risk by means of a portfolio approach guaranteeing the effectiveness and credibility of the mechanism.
- (j) Determine the procedure to be followed for the transfer of CERs;
- (k) Ensure the percentage of CERs that will be part of the adaptation fund and the manner in which the CERs will be transformed into financial resources;
- (l) Define the roles of the multilateral agencies with experience in climate change, especially as regards development of the institutional capability required to promote broad participation by all Parties not included in Annex I;
- (m) Call on experts for technical advice if deemed necessary;
- (n) Propose to the COP/MOP and receive the share of proceeds that should be applied to CERs transactions in order to meet the administrative costs of the Executive Board.

In relation to institutional issues, the Executive Board shall, *inter alia*:

- (a) Accredite certifying/verification operational entities based on guidance from the COP/MOP, coordinate with the designated national entities which will be in charge of the operation of CDM in each Party;
- (b) Review and audit operational entities, through carrying out sample checks and revoke, in accordance with a process to be determined by the COP/MOP, the accreditation of those entities which fail to comply with and procedures determined by the COP/MOP;
- (c) Maintain a publicly available list of operational certifying/verifying entities;
- (d) Report on its operations to each session of the COP/MOP.

The Executive Board shall consist of 9 members elected by the COP/MOP and shall comprise two representatives from Asia, two representatives from the Americas, two representatives from Europe, two representatives from Africa and one representative from the Island States, making up a total of nine members. The Parties shall propose members.

Members of the Executive Board should be appointed for a period of up to two years. Members most possess appropriate technical expertise. The COP/MOP shall select a Chairman and Vice-Chairman of the Executive Board from among its members, with one of those officers being from a Party not included in Annex I.

The Executive Board should be located in the Secretariat of the Convention.

C. Operational entities

Operational certifying/verifying entities shall:

- (a) Be accredited by the COP/MOP;
- (b) Be supervised by the Executive Board and fully accountable to the COP/MOP, through the Executive Board based on criteria contained in Appendix E;
- (c) Be subject to modalities and procedures specified in applicable decisions of the COP/MOP;
- (d) Have no operational or financial links with CDM project activities and shall not have been involved in the identification, development or financing of CDM projects;
- (e) Prepare technical reports, upon which projects will be validated and CERs will be issued and accredited;

Entities shall be accredited as operational entities only if they demonstrate the necessary expertise.

The functions of an operational certifying/verifying entity shall be to:

- (a) Certify and verify project activities and emissions reductions under Article 12, II accordance with Appendix C and D, on request of a project participant, to ensure that it meets the standards adopted by the COP/MOP;
- (b) Certify and verify emission reductions by sources and/or enhancements of removals by sinks which have resulted from CDM project activities;
- (c) Report to the Executive Board their decisions on the certification/verification of project activities and related CERs to be issued in accordance with Appendix C and D.

D. Parties

Each Party interested should develop its own legal and institutional framework related to the implementation of Article 12 of the Protocol in order to promote, evaluate, approve, verify, register at national level and report to the Executive Board about projects to be included in the CDM.

A designated national CDM authority shall:

- (a) Determine independent criteria for project eligibility on the basis of national priorities/strategies for sustainable development;
- (b) Evaluate projects using national criteria and international standards;
- (c) Approve project proposals and submit to the Executive Board;
- (d) Inform the Executive Board of the anticipated ending of a project and state the reason for the project's ending and the consequences for any CERs;
- (e) Bear overall responsibilities for reporting;
- (f) Promote broad participation of public, private and non-governmental organizations;
- (g) Coordinate international fora, including operational activities in verification and certification, with the Executive Board and the accredited operational entities;
- (h) Register individuals and organizations involved in trading of CERs;
- (i) Register and account for national emission reductions reported to the Executive Board and accredited by the Executive Board;
- (j) Reconcile the national account and report it annually to the Executive board;
- (k) Ensure fair distribution of CERs economic benefits among project participants.

E. Administrative support

The Secretariat under the guidance of the COP/MOP shall provide administrative and secretariat assistance to the Executive Board. This assistance could include compiling, synthesizing and disseminating information related to CDM project activities, including in relation to Article 12 paragraph (6), and performing other secretariat functions as requested by the Executive Board.

The Secretariat shall keep a record of Executive Board decisions and communicate the full text of all decisions to each Party.

The share of proceeds according to Article 12, paragraph (8), shall be used to cover all administrative expenses of the CDM, including the administration of the Executive Board and administration of the share of proceeds for adaptation.

F. Review

The COP/MOP shall:

- (a) Periodically review the performance of the Executive Board, the national designated entities and accredited operational certifying/verifying entities;
- (b) Review Article 12 modalities, procedures and technical guidelines five years after their adoption and periodically thereafter. Any revision of these modalities and procedures will not have an impact on emission reductions already certified;
- (c) Periodically review the implementation of CDM project activities and their geographical spread, and take appropriate action to promote the principle of equity;
- (d) Periodically review the needs of developing country Parties particularly vulnerable to the adverse effects of climate change for adaptation assistance under Article 12, paragraph (8);
- (e) Review the allocation of the share of proceeds for adaptation projects five years after the adoption of these rules and procedures;

**III APPENDICES TO PART THREE:
CLEAN DEVELOPMENT MECHANISM**

A. Baselines

According with the provisions of Article 12 paragraph 5 (b) and (c), CDM projects must produce “real, measurable and long-term benefits” and emission reductions can be certified only if they are “additional to any that would occur in the absence of the project activities”.

In virtue of the above projects to be registered under the CDM shall to establish baselines on a project base to quantify “what would have happened” in the absence of those project activities.

Baseline should be: environmentally credible to ensure long-term benefits greater than what would happen other wise; transparent and verifiable by a third party, be simple and provide a reasonable level of crediting certainty for investors.

Any baseline approach shall involve tradeoffs among the criteria above and be strictly the best available, although in some cases it will be necessary to use projections from a specific sector of the economy. This type of baselines includes those variously referred in the literature as “benchmarkes”, “activity standards”, technology matrix” and “sectoral”.

The difference between the baseline and the project emission or removal scenario shall determine the net environmental benefit of the project in terms of emission reductions to be expressed in carbon dioxide equivalent units.

Baselines, once certified, should remain static for the life span of the project. However, baselines may be revised periodically for subsequent application to new projects.

The least cost option and among them, the minimum emissions alternative, shall be considered to be used for baselines in CDM projects with low level of financial return, even if as a result of economic circumstances of the Party, the least cost option would not necessarily been bankable. This is so, contingent that the emissions of CDM project scenario should be less than those from the least cost option considered as baseline. Additionally, CDM project, before CERs economic valuation, shall be financially less attractive or less likely to occur than the baseline option.

Reaffirming the above, baseline shall not have only a time dimension, but development dimension too. When evaluating CDM project baselines from least developing country Parties, it has to be allowed the “development-benefit-of-the-doubt” and consider the least cost option as baseline, even if not bankable, to be compared with the CDM project scenario to create CERs to be valued and make the DCM project bankable.

On the basis of the foregoing, the orientation of the CDM is assured towards promotion of sustainable development without discriminating arbitrariness the least cost development option which has much to offer to developing country Parties.

B. Additionality

According with the provisions of Article 12, paragraph 5 (c), additionality is one of the basic eligibility criteria for CDM projects.

The concept of additionality is vital in order to guarantee the environmental and financial soundness of the CDM. Accordingly, the concepts of environmental additionality and financial additionality should be considered as viable eligibility criteria for CDM projects.

Environmental additionality should be quantified in a project basis in terms of emission reductions or enhancement of removals by sinks during the life span of the project.

How environmental additionality is assessed will depend on which methodology a project developer uses. Under a project-by-project approach, developers shall establish a baseline against which the project's emissions scenario will be compared. If the project's emissions are below the baseline, then it would be considered additional. Standardized baselines for a type of project, for example benchmarking, could be developed to distinguish between those activities that generate GHG reductions in excess of the baseline and those that do not. Activities that perform better than the benchmark would automatically be considered additional.

Financial additionality is derived from the concept of environmental additionality and relates to whether the project activity would have existed in the absence of the economic valuation of CERs accrued to project activities and the internalization in its financial structure.

Financial additionality should be quantified in terms of the impact of the economic valuation of the emission reductions on the project finances. It will be necessary to compare financial indicators (internal rate of return, net present value and equivalent annual value), drawn up in the light of the flows of funds with and without economic valuation of CERs accrued project activities during its life span.

The necessary conditions for financial additionality shall be:

- (a) The baseline should be the least cost option and among those, the minimum emissions alternative;
- (b) The CDM project, before the economic valuation of CERs, should be financially less attractive or less likely to occur than the baseline case;
- (c) The emissions scenario of the CDM project should be less than those from baseline case;
- (d) The valuation of CERs from the CDM project, alternative at some reasonable price, shall significantly impact the financial performance of the project. It suffice to assure that CERs valuation significantly improves the CDM project bankability or likelihood to occur.

Condition (a) asserts developing countries Party the right to persue economic development and allows developing counties Party with low emissions profile to benefit from CDM. Condition (b) provides environmental effectiveness. If the CDM Project case, before CERs economic

valuation, is not less financially attractive than the baseline case, then. The baseline wouldn't be the least cost or "most bankable" option. Condition (c) is part of CDM definition and (d) the additionality condition.

The purpose of the Kyoto Protocol is not only to set the world in a cleaner development path, where a convergence of emissions-per-capita would happen by promoting cleaner projects in least development country Parties, but also a convergence of income-per-capita by promoting the implementation of clean development projects in sectors where not even the "dirty" option would have happened. The last is the "sustainable development" goal of the CDM.

C. Certification

Recognizing that only emissions reductions which have been duly certified may be traded and accounted for under the CDM, minimum standards shall be adopted for CERs to guarantee homogeneity and environmental effectiveness regardless the nature and origin of the project.

The certification process shall comprises a qualitative assessment of the project design and a quantitative assessment of the project anticipated emission reductions. The qualitative analysis shall comprises two distinct assessments, the suitability assessment of the project and the scientific methodology assessment.

The former shall address the following eligibility criteria:

- (a) Acceptability: the project must be acceptable by the national designated entity;
- (b) Additionality: the offsets claimed must be genuinely generated by the project and not result from changes in practices and policies of programmes that would have occurred in the absence of the project;
- (c) Externalities: the project must not result in negative social, developmental or environmental impacts and the emission reductions claimed shall not be negated by increased emissions as a result of project activities;
- (d) Capacity: the project must have the management, financial and technological capacity to implement the activities and the results must be clearly demonstrable.

The assessment of the scientific methodology to estimate the anticipated project output shall address data availability and quality, methodologies used for offsets determination, project boundaries, etc.

On the other hand, the quantitative analysis shall comprises two distinct assessments, the quantification of carbon offsets and the risk and uncertainty assessment.

The former shall verify emission reductions that will be achieved by the project during its lifetime. The later shall determine which proportion of the offsets must be retained in a buffer to cover for the risk and uncertainty. This shall be seen as a means of self-insurance of the project.

The quantification of emission reductions and the quantitative risk and uncertainty assessment together determine the CERs that can be expected over the project lifetime as described in the certified project design. This schedule of CERs shall be updated on an annual basis.

The process of certification must be independent and only emission reductions accrued from duly implemented project activities should be eligible for certification.

The certification service should be provided by independent certifying organizations accredited by the COP/MOP.

D. Monitoring and verification

According to the provision of Article 12 paragraph (7), "the COP/MOP... shall ... elaborate modalities and procedures with the objective of ensuring transparency, efficiency and accountability through monitoring and independent verification of project activities".

On the basis of the effectiveness of the monitoring process, both in environmental and accounting terms, certain minimum requirements shall be adopted such as: the application of scientifically approved methodological procedures in accordance with the type of project, standard reports, consistent records, allocation of responsibilities and provisions for non-compliance.

The monitoring shall be complemented by a verification process, which ensures compliance of emission reductions on a project basis.

Verification should be an independent auditing service that backs up the monitoring results and ensures the effective implementation of the project in keeping with the provisions stemming from the prior certification process.

Monitoring, certification, verification and the interaction between them are, in the context of follow-up and surveillance, the basic elements in guaranteeing environmental effectiveness, consistency and transparency at project level, and in ensuring the integrity and credibility of the CDM.

E. Registry

Once a Party has met the eligibility criteria for international trading, it can be accredited its assigned amount as CERs. Once accredited by the Executive Board, CERs will be registered in the system of national registries of involved Parties.

To keep track of CERs holdings, the Executive Board registry would be required to:

- a) record CERs issued to Parties;
- b) record in 'real time' (or near 'real time') changes of CERs holdings as a result of trades;

- c) maintain a record of CERs retired (i.e. cancelled) by the Annex I Party for the purpose of meeting its Article 3 commitments.

Given the large volume of data to be handled and the wide availability and low cost of modern computer technology, national registries would be kept in the form of computer databases. The design of national registries should be compatible so that transactions can be processed at low cost and almost instantaneously. Each Party should identify an agency (government or private) that is responsible for maintaining the Party's national registry and performing the necessary functions. This will facilitate the effective operation of the international trading system since the Executive Board and traders will be clear about the point of contact for each national registry. The use of computer databases would remove the need for Parties to issue a paper certificate for each tradeable unit. Computer databases can give both Parties and entities greater security and confidence in the recording system and lower transaction costs.

Once a buyer have agreed to make a trade, the Executive Board would request that the supplier national registry removes CERs from its account and the buyer national registry credits the buyer's account with those CERs. Contractual information beyond the appropriate account details and quantity of CERs to be transferred would not need to be provided to national registries by the Executive Board.

For all trades recorded by a national registry, a record of the transaction must be kept. Transaction records would also enable a check to be made at any time to ensure that correct double-entry bookkeeping has taken place within national registries.

Buyers and sellers could potentially make a variety of private contractual arrangements for future trades (also known as 'contract trades' –e.g. forward contracts and futures). However, for the purposes of the national registry, these transactions would only be recognized when the contract is executed and the national registry of the seller is officially notified of the transfer by the Executive Board.

To promote transparency and the efficient operation of the market, the trading rules should ensure that account information is publicly accessible. Transparency of information on holdings would help generate confidence in the market and ultimately encourage compliance by Parties at the end of the commitment period.

India

**SUBMISSION ON ARTICLE 12 OF THE KYOTO PROTOCOL
THE CLEAN DEVELOPMENT MECHANISM**

I. NATURE AND SCOPE

A. Purpose

1. The purpose of the clean development mechanism (CDM) is defined in Article 12 of the Kyoto Protocol to the U.N. Framework Convention on Climate Change. The CDM has a two-fold purpose: (a) to assist developing country Parties in achieving sustainable development, thereby contributing to the ultimate objective of the Convention, and (b) to assist developed country Parties in achieving compliance with part of their quantified emission limitation and reduction commitments under Article 3. Each CDM project activity should meet the above two-fold purpose.

B. Principles

2. The principles related to the nature and scope of the CDM must guide and direct the methodological and operational issues pertaining to project activity and the institutional issues. The principles, including the nature and scope of the CDM, must be decided first so that the issues relating to the methodological, operational and institutional matters can be guided and directed accordingly. Parties should have further opportunity to make proposals and submissions about the methodological, operational and institutional issues after the principles, including the nature and scope of the CDM, have been decided. Such an approach is required to ensure conformity of the methodological, operational and institutional issues with the principles and the nature and scope of the CDM.

3. Any decision by the COP/moP on the CDM must be a separate decision. There should be three separate decisions, each on Article 6, 12 and 17, related to the three mechanisms.

4. The principles and the nature and scope of CDM project activity are defined below.

(a) Nature and Scope of CDM

(1) The CDM is a project-based mechanism conceived and introduced in the Protocol with a two-fold purpose: (a) to assist developing country Parties in achieving sustainable development, thereby contributing to the ultimate objective of the Convention, and (b) to assist developed country Parties in achieving compliance with part of their quantified emission limitation and reduction commitments under Article 3 of the Protocol.

(2) The nature and scope of the CDM is different from the other mechanisms. The CDM is a distinctive and stand-alone mechanism.

(3) Each CDM project activity must involve the participation both of developed and developing country Parties. Developed country Parties will fund projects in developing countries, which will assist sustainable development.

(4) The CDM is unlike the other mechanisms. The CDM differs from the other mechanisms in respect of basis, purpose and participation. Any decision by the COP/moP on the CDM must be a separate decision.

(5) Unlike the other mechanisms, the CDM is the only mechanism which involves the participation of developing country Parties in project activities. Project activity will be based in developing countries. Unlike the other mechanisms, the CDM stipulates sustainable development in developing countries as a basic purpose. The basis of CDM activity is prospective, whereas "emissions trading" in Article 17 for the commitment period of 2008-2012 is derived from the retrospective. Article 12, providing for CDM activity, is based on projects to be set up in developing countries seeking prevention of emissions in the future, in contrast to "emissions trading" in Article 17 which is based on greenhouse gas inventories derived from past emissions in developed countries. The emission reductions resulting from CDM project activity in developing countries are not transferrable, though the emission reductions resulting from Article 6 projects and part of assigned amount on fulfilment of necessary conditions consequent to "emissions trading" under Article 17 are transferable among developed country Parties.

(6) The Protocol provides for emission reductions resulting from Article 6 projects to be transferred between developed country Parties as emission reduction units, but the Protocol does not provide for transfers of emission reductions resulting from CDM project activity. The Protocol treats project based activity in Article 6, which is between developed country Parties, differently from Article 12 projects which are between developed and developing country Parties.

(7) Developed country Parties may involve private and/or public entities for funding project activity in developing countries in accordance with the terms of agreement between the participating developed and developing country Parties.

(8) The emission reductions resulting from each CDM project activity shall be certified. The Protocol has made provision for certifying the emissions reduced from a CDM project. The emission reductions so certified shall be used by developed country Parties to contribute to compliance with part of their quantified emission limitation and reduction commitments under Article 3 to the extent permissible under the principle of "supplementarity". The emissions certified to be reduced in CDM project activity will be used by developed country Parties to meet part of their quantified emission limitation and reduction commitments in return for funding a CDM project in accordance with the terms of agreement between the participating developed and developing countries.

(9) The certification for emissions reduced in Article 12 relates to projects which have been funded by developed countries in developing countries as CDM project activity. CDM envisages the funding by developed country Parties of project activity in developing countries for contributing to compliance with part of its quantified emission limitation and reduction commitments under Article 3 because of the project being a lower cost option for reducing emissions compared to the alternative of implementing policies and measures in the developed country funding the project for limiting and reducing an equivalent amount of emissions.

(10) The emissions certified to be reduced in CDM project activity must be additional to what would have occurred in the absence of such activity. It is the additional reduction, which is the certified emission reduction. The additional emission reduction will be certified on the basis of agreed baselines.

(11) CDM project activity and emissions certified to be reduced in such activity do not have any link with the other mechanisms. In the other mechanisms, only developed countries participate. The CDM, in which both developed and developing countries participate, is a distinctive mechanism.

(12) The commitment of developed country Parties in Article 3 is to achieve their quantified emission limitation and reduction commitments by ensuring that their emissions do not exceed their assigned amounts. The assigned amount is the emission commitment of developed country Parties. The assigned amount for each Party included in Annex I of the Convention shall be equal to the percentage inscribed for it in Annex B of the Protocol of its aggregate carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol, multiplied by five.

(13) The emissions certified to be reduced by CDM project activity may be used by developed country Parties to contribute to compliance with their quantified emission limitation and reduction commitments under Article 3 if that developed country Party falls short of complying with its assigned amount of emissions. The emissions certified to be reduced in CDM project activity funded by the developed country Party, and acquired by that Party in accordance with the terms of agreement with the developing country Party participating in the project, can be used to make up shortfalls in achieving emission commitments, subject to the principles of supplementarity. The emissions reduced in CDM project activity, as certified, can be used by the developed country Party only for

making up the shortfall in compliance with emission commitments. If the developed country Party emits less than its assigned amount, any certified emissions reduced which such developed country Party may have acquired may be used by that acquiring Party in the next commitment period.

(14) There is no fungibility between the emissions certified to be reduced in CDM project activity and any part of the assigned amount. The certified emissions reduced (CER) and the assigned amount are unlike concepts. The assigned amount for the commitment period is the emission commitment. On the other hand, the CER is a certification of the emissions reduced from a certified CDM project activity assisting sustainable development in a developing country which a developed country has funded. Such project activity, while achieving the two-fold purpose of the CDM, has been funded because of the project activity being a lower cost option for reducing emissions compared to the alternative of implementing policies and measures in the developed country funding the project for limiting and reducing an equivalent amount of emissions. The assigned amount, calculated pursuant to the quantified emission limitation and reduction commitments inscribed in Annex B of the Protocol, cannot be altered.

(15) Acquisition of certified emission reductions does not alter the assigned amount for the commitment period or any part of the assigned amount transferable under Article 17. In respect of Article 17 transfers, if a developed country Party is able to limit and reduce its GHG emissions to an extent so that its emissions become less than its assigned amount, then, such difference, i.e., such excess limitation and reduction is a transferable under Article 17, subject to the satisfaction of related principles and rules. Only such excess limitation and reduction, relative to the assigned amount for each Party inscribed in Annex B, and nothing else, can be transferred and acquired under Article 17. The assigned amount represents the quantified emission limitation and reduction commitment of the Annex B Parties for the commitment period. In the event of an Annex B Party having limited and reduced its emissions below its assigned amount of emissions, the opportunity arises for another Annex B Party which having exceeded its assigned amount of emissions may seek to offset its excess emissions. In this connection, any transfers and acquisitions of part of assigned amount will only add to or subtract from the quantified emission limitation and reduction commitment of the Annex B Parties. The assigned amount for the commitment period cannot be altered through acquisition of CERs.

(16) Limitation and reduction of emissions through CDM project activity cannot lead to the creation or bestowal of any title, holding, entitlement, goods, commodity or proprietary facility of any nature.

(17) CDM project activity must be based on environmental integrity and maintenance of transparency between the developed and developing country Parties participating in CDM project activity through close interface between the Parties for generating information relevant and specific to the particular project taking into account the need to reduce transactional delays and costs while enhancing bilateral confidence between the funding and recipient Parties.

(b) Equity

It must be ensured that the CDM does not have dormant any possibility or potential of freezing or perpetuating past and present inequities between developed and developing countries. The right to development of developing countries must not be affected adversely in any way. The first and overriding priority of developing countries is economic and social development and poverty eradication.

Equity relates to equitable emission entitlements. The matter should be viewed in the light of contraction and convergence of emissions, wherein developed countries must contract greenhouse gas emissions to reduced levels with per capita emission levels in developed and developing countries coming on a converging path. Equal per capita emission levels is an equitable norm. The per capita criterion is central to the determination of emission entitlements. Per capita emission levels provide a direct measure of human welfare for economic and social development and poverty eradication.

(c) Climate Change Effectiveness

The effectiveness of CDM project activity must be assessed in terms of real, measurable and long-term benefits related to the mitigation of climate change at the project level. The reduction of emissions and their certification must be credible. The system should not be afflicted with scientific uncertainties.

(d) Sustainable Development Priorities

The developing country Party where the CDM project activity is proposed to be set up shall be the sole judge for deciding whether that project activity meets its national sustainable development objectives and priorities. CDM projects should give priority to the renewables sector or highly energy efficient projects that are at the top end of efficiency practice anywhere. The CDM should also be oriented towards improving the quality of life of the very poor from the environmental standpoint.

(e) Funding Additionality

Funding for CDM project activity shall be additional to ODA, GEF and other financial commitments of the developed country Parties. The CDM, a mechanism introduced in the Protocol, will entail transfer of technology and funds, but it cannot be a substitute for developed country commitments in the Convention relating to financial resources and transfer of technology contained in Article 4.3, 4.5 and 4.7 of the Convention.

Article 4.7 of the Convention states that the extent to which developing country Parties will effectively implement their commitments under the Convention will depend on the effective implementation by developed country Parties of their commitments under the Convention related to financial resources and transfer of technology and will

take fully into account that economic and social development and poverty eradication are the first and overriding priorities of the developing country Parties.

(f) Transparency

Transparency must be observed in the design and application of CDM project activity.

(g) Needs of Least Developed Countries

The needs of least developed countries have to be addressed from the point of view of building up endogenous expertise for identifying technology needs and enhancing capacities for assimilation of technology.

(h) Capacity Building

Capacity-building should be incorporated in all CDM project activities. Developing country Parties will also need to develop capacity in the design, implementation and evaluation of CDM project activities, and the monitoring, reporting and verification of emissions.

(i) Adaptation

The COP/moP of the Protocol shall ensure that a share of the proceeds from certified project activities is used to cover the costs of adaptation to assist developing countries that are particularly vulnerable to the adverse effects of climate change. The proceeds from certified project activities must fund adaptation measures for facilitating vulnerable systems to cope with actual or likely pressures resulting from climate change. The poorest populations are the most vulnerable. Agricultural sustainability, food and nutrition vulnerability is of critical importance, requiring adaptation on priority basis. Impact assessment and adaptation must be very closely coordinated. Impact assessment is a pre-requisite for adaptation activity.

The “share of proceeds from certified project activities” shall be a stipulated percentage of the differentials of the costs incurred by the developed country Party in reducing greenhouse gases through a project activity in a developing country and of the projected costs that would have been incurred had the greenhouse gas reduction activity taken place in the developed country funding the project.

(j) Compliance

Appropriate and effective procedures and mechanisms to determine and address cases of non-compliance with the provisions of this Protocol should be established. The procedures and mechanisms should be in accordance with the principles of the Convention.

The objective of the procedures and mechanisms in Article 18 of the Protocol is to ensure the attainment of the targets and time-tables set for developed country Parties for achieving the quantified emission limitation and reduction commitments in accordance with the relevant principles, rules, modalities and guidelines, and the fulfilment of the commitments of developed countries in Article 4.3, 4.5 and 4.7 of the Convention and Article 10 of the Protocol for transfer of financial resources and technology taking fully into account that economic and social development and poverty eradication are the first and overriding priorities of the developing country Parties.

(k) Criteria for Project Eligibility

Eligible project activities, apart from meeting national sustainable development priorities, must ensure access to the technology needed by the developing country Parties participating in the CDM project activity. Climate change mitigation through CDM project activity should be consistent with national sustainable development policies.

(l) Transparency, non-discrimination, prevention of distortion of competition

No unilateral measures for CDM participation should preclude a developing country Party from participating in any CDM project activity.

(m) Institutional Framework

The institutions as provided for in Article 12 of the Kyoto Protocol must be in accordance with the nature and scope of the CDM.

C. "Part of"/supplementarity

5. The design and implementation of the CDM must not in any way compromise the modification of longer-term trends in greenhouse gas anthropogenic emissions and concentrations. All the mechanisms, including the CDM, must be supplemental to domestic action in developed countries for GHG limitation and reduction. Developed country Parties' participation in CDM project activities should be contingent on satisfaction of prescribed domestic effort in fulfilment of commitments under Article 3. A quantified ceiling on the emissions limited and reduced through the mechanisms is required. Commensurate non-compliance processes must be prescribed.

D. Participation

6. Unlike the other mechanisms provided for in the Kyoto Protocol, the CDM is the only mechanism which involves the participation by both developed and developing country Parties in each project activity. Developed country Parties will fund projects in developing country Parties, which will assist sustainable development. Parties are responsible for the involvement of their private and/or public entities in CDM project

activities. Any costs, risks or liabilities that have not been expressly accepted by the developing country Party shall be assumed to be the responsibility of the participating developed country Party.

7. A developed country Party shall use CDM project activity, subject to relevant principles, rules, modalities and guidelines, to contribute to compliance with its quantified emission limitation and reduction commitments only if the Party is bound by a compliance system adopted by the COP/moP, and has not been excluded from participation in the CDM according to its procedures and mechanisms and has also satisfied the prescribed domestic effort for limiting and reducing emissions in accordance with the principle of complementarity in fulfilment of commitments under the relevant provisions.

E. Share of Proceeds

8. The "share of proceeds from certified project activities" shall be a stipulated percentage of the differentials of the costs incurred by the developed country Party in reducing greenhouse gases through a project activity in a developing country and of the projected costs that would have been incurred had the greenhouse gas reduction activity taken place in the developed country funding the project. The "share of the proceeds from certified project activities" must not be of an order which adversely affects the competitiveness of the CDM compared to the other mechanisms.

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Project Validation/ Registration

9. The CDM is a project-based mechanism conceived and introduced in the Protocol with a two-fold purpose. Eligible project activities, apart from meeting national sustainable development priorities, must ensure access to the technology needed by the developing country Party participating in the CDM project activity. The Protocol has made provision for certifying the emissions reduced from each CDM project activity. The emission reductions so certified shall be used by developed country Parties to contribute to compliance with part of their quantified emission limitation and reduction commitments under Article 3 to the extent permissible under the principle of "supplementarity" and other relevant principles, rules, modalities and guidelines.

10. The emissions certified to be reduced in CDM project activity funded by the developed country Party, and acquired by that Party, in accordance with the terms of agreement with the developing country Party participating in the project, can be used to make up this shortfall in achieving its emission commitments, subject to the principles of complementarity. The emissions reduced in CDM project activity, as certified, can be used by the developed country Party only for making up the shortfall in emission commitments. If the developed country Party emits less than its assigned amount, any

certified emissions reduced which such developed country Party may have acquired, may be used by that acquiring Party in the next commitment period.

11. The establishment of baselines for the determination of emission reduction should be on a project-by-project basis. The determination of baseline will depend on the sector and the complexity involved. There could be technology additionality or energy saving additionality. The establishment of the baseline will quantify the level of emissions that most likely would have occurred in the absence of certified CDM project activity. Baseline determination, from the global environment perspective, must be such, which does not lead to an inflation of the emission reductions claimed by the project.

12. Independent auditing of project activities may be done by public or private sector entities not involved in the identification, development or management of the project. There is need to develop uniform auditing practices. Verification has to be carried out by independent entities that have had no operational or financial links with the project, and that are fully accountable to COP/moP which shall exercise authority and guidance over all aspects of the CDM. The composition of any team should be approved by the developing country Party participating in the CDM project activity.

13. The developing country Party, where the CDM project activity is proposed to be set up, shall be the sole judge for deciding whether that project activity meets its national sustainable development objectives and priorities. Project activities shall promote transfer of state-of-the-art, environmentally sound technology in addition to that required under the other provisions of the Convention and the Protocol. The project activity should lead to reduction in emissions in addition to any that would occur in the absence of the project activity. The project activity should yield real, measurable and long-term benefits related to the mitigation of climate change.

B. Project Financing

14. Developed country Parties will fund projects in developing country Parties which will assist sustainable development. Developed country Parties may involve private and/or public entities for such funding. In return, the developed country Party, funding the project, will be enabled to meet part of its emission reduction commitment. The Protocol has made provision for certifying the emissions reduced from CDM project activity. The emission reductions so certified shall be used by developed country Parties to contribute to compliance with part of their quantified emission limitation and reduction commitments under Article 3 to the extent permissible under the principle of "supplementarity". The emissions certified to be reduced in CDM project activity will be used by developed country Parties to meet part of its quantified emission limitation and reduction commitment in return for funding a CDM project in accordance with the terms of agreement between the participating developed and developing countries. Funding for the CDM project shall be additional to ODA, GEF and other financial commitments of the developed country Parties.

C. Project Monitoring

15. Auditing of CDM project activities may be done by entities which are not involved in the identification, development or management of the project. Uniform auditing practices must be developed.

D. Project Verification

16. Verification should be carried out by entities that have had no operational or financial links with the project. The composition of any verification team should be approved by the developing country Party participating in the CDM project activity. Emission reductions achieved by the project in relation to the baseline shall be verified from the monitored data and other pertinent information, in accordance with the methodologies accepted by the Parties participating in the project activity.

E. Certification/issuance of CERs

17. The Protocol has made provision for certification of the emissions reduced from CDM project activity. The certified emission reductions (CERs) from CDM project activity funded by a developed country will be acquired by that developed country Party from the developing country Party where the project is funded, in accordance with the agreement between the two Parties. The emissions reduced in CDM project activity, according to the CERs, may be used by the developed country Party, subject to the principle of "supplementarity", for making up any shortfall in complying with its quantified emission limitation and reduction commitment which is the assigned amount of emissions for that developed country Party.

18. The assigned amount of an Annex B Party is the quantified greenhouse gas emission limitation and reduction commitment for the commitment period from 2008 to 2012. The assigned amount of emissions which shall be equal to the percentage inscribed for that Annex B Party of its aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases (GHGs) listed in Annex A of the Protocol in the base year or period determined in accordance with the Protocol, multiplied by five. Though, the assigned amount cannot alter because of acquisition of CERs, but, for the purpose of meeting shortfall in complying with the emission commitments of an Annex B Party, subject to the principle of supplementarity, the "additional" emissions reduced in CDM project activity, as certified, get "added" to the assigned amount of emissions of the developed country Party to the extent of the shortfall in its emission limitation and reduction commitment, in lieu of the "additional" emissions reduced in that project activity. If the developed country Party emits less than its assigned amount, any CERs which such developed country Party may have acquired from CDM project activity funded by it may be used by that acquiring Party in the next commitment period.

19. The CERs are not fungible with the assigned amount. The certification from CDM project activity and the assigned amount are unlike concepts. The certification and the assigned amount cannot mix or assimilate with each other. The CER is a certification of the emissions reduced from a certified CDM project activity assisting sustainable development in a developing country which a developed country has funded. Such project activity, while achieving the two-fold purpose of the CDM, would be funded by the developed country Party because of the project activity being a lower cost option for reducing emissions compared to the alternative of implementing policies and measures in the developed country funding the project for limiting and reducing an equivalent amount of emissions. The assigned amount, on the other hand, is the quantified emission limitation and reduction commitment of a developed country Party for a commitment period, which has been derived from past GHG emissions relating to a base year.

F. Issues Related to Compliance

20. Appropriate and effective procedures and mechanisms to determine and address cases of non-compliance with the provisions of this Protocol should be established, in conformity with the principles of the Convention.

G. Adaptation Assistance

21. The COP/moP of the Protocol shall ensure that a share of the proceeds from certified project activities is used to cover the costs of adaptation to assist developing countries that are particularly vulnerable to the adverse effects of climate change. The proceeds from certified project activities must fund adaptation measures for facilitating vulnerable systems to cope with actual or likely pressures resulting from climate change. The poorest populations are the most vulnerable. Agricultural sustainability, food and nutrition vulnerability is of critical importance, requiring adaptation on priority basis. Impact assessment and adaptation must be very closely coordinated. Impact assessment is a pre-requisite for adaptation activity. Activities to adapt to the adverse effects of climate change shall be country-driven and in conformity with the national strategies and priorities for the sustainable development of the developing country Party concerned.

22. The "share of proceeds from certified project activities" shall be a stipulated percentage of the differentials of the costs incurred by the developed country Party in reducing greenhouse gases through a project activity in a developing country and of the projected costs that would have been incurred had the greenhouse gas reduction activity taken place in the developed country funding the project.

H. Registries

23. National registry systems shall be established for keeping account of the emissions reduced from certified CDM project activities in developing countries and the acquisition of certified emission reductions by developed country Parties from developing country Parties, accruing from related activity, funded by such developed

country Parties for meeting the quantified emission limitation and reduction commitments.

I. Reporting by Parties

24. The format for reporting by developed country Parties participating in CDM project activity, must be standardized to cover CDM project activity. The reporting format must facilitate the accounting required for assessing the contribution of CDM project activity to the fulfilment of quantified emission limitation and reduction objectives under Article 3 of the Protocol.

III. INSTITUTIONAL ISSUES

A. Role of the COP/moP

25. As stated in Article 7 of the Convention, the COP is the supreme body of the Convention which shall keep under regular review the implementation of the Convention and related legal instruments that the COP may adopt, such as the Kyoto Protocol. The CDM, supervised by an executive board, shall be subject to the authority and guidance of the COP/moP. There shall be full accountability of the CDM executive board to the COP/moP. The COP/moP shall review periodically the implementation of CDM project activity. The COP/moP shall review and approve the methodologies for determining baselines, monitoring, verification, certification and reporting. The COP/moP shall issue technical guidelines, and determine the eligibility criteria for adaptation under Article 12.8.

B. Executive Board

26. The executive board shall be a standing body, fully accountable to the COP/moP. Under the authority and guidance of the COP/moP the executive board shall supervise the CDM, and provide guidance for the involvement of private and/or public entities in CDM project activities. The executive board shall be fully accountable to the COP/moP and carry out all instructions and other functions assigned to it by the COP/moP. The executive board shall manage CDM project activity to ensure conformity with the Convention, the Protocol and relevant decisions by the COP/moP. The composition of the CDM executive board must be based on equitable geographical representation.

C. Operational entities

27. Operational entities to certify emission reductions resulting from each CDM project activity shall be designated by the COP/moP. These entities shall be accountable to the COP/moP, through the executive board. The operational entities shall be subject to the modalities and procedures specified in applicable decisions of the COP/moP. The entities will have no operational or financial links with the CDM project activity of which

the emissions are to be certified. The entities, also should not have been involved in the identification, development and financing of the project.

D. Parties

28. The Parties participating in CDM project activity must be responsible at all stages and in all aspects for the project activity in which they are participating . Any costs, risks or liabilities that have not been expressly accepted by the developing country Party before approval of CDM project activity shall be assumed to be the responsibility of the participating developed country Party. Each Party participating in the CDM project shall establish a national system for monitoring, verification and reporting under the CDM. The Party shall determine criteria for project eligibility on the basis of national priorities/strategies for sustainable development in conformity with decisions taken by the COP/moP.

E. Administrative Support

29. The COP/moP shall ensure that a share of the proceeds from certified CDM project activities is used to cover the administrative expenses.

F. Review

30. As stated in Article 7 of the Convention, the COP is the supreme body of the Convention which shall keep under review the implementation of the Convention and related legal instrument.

ARTICLE 6 PROJECTS

I. NATURE AND SCOPE

A. Purpose

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;
 - (d) The acquisition of emission reduction units shall be supplemental to domestic actions for the purposes of meeting commitments under Article 3.

B. Principles

2. The principles related to the nature and scope of Article 6 projects must guide and direct the methodological and operational issues pertaining to project activity and the institutional issues. The principles, including the nature and scope of Article 6 projects must be decided first so that the issues relating to the methodological, operational and institutional matters can be guided and directed accordingly. Parties should have further opportunity to make proposals and submissions about the methodological, operational and institutional issues after the principles, including the nature and scope of Article 6 projects have been decided. Such an approach is required to ensure conformity of the methodological, operational and institutional issues with the principles and the nature and scope of Article 6 projects.
3. Any decision by the COP/moP on Article 6 projects must be a separate decision. There should be three separate decisions, each on Article 6, 12 and 17, related to the three mechanisms.
4. The principles must conform to the purpose of Article 6 projects. The purpose of Article 6 projects is to enable developed country parties to jointly develop emission reduction projects which are effective in terms of real, measurable and long-term benefits

related to the mitigation of climate change. 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;
- (d) The acquisition of emission reduction units shall be supplemental to domestic actions for the purposes of meeting commitments under Article 3.

5. The nature and scope of Article 6 projects is different from the other mechanisms. Unlike the other mechanisms, Article 6 provides the only mechanism for project based activity between developed country Parties. The Protocol provides for emission reductions resulting from Article 6 projects to be transferred between developed country Parties as emission reduction units, but the Protocol does not provide for transfers of emission reductions resulting from CDM project activity. The ERUs and the assigned amount are unlike concepts. There is no fungibility between ERUs and the assigned amount. The assigned amount of an Annex B Party is the quantified greenhouse gas emission limitation and reduction commitment for the commitment period from 2008 to 2012. On the other hand, the ERU represents the emissions reduced from a certified Article 6 project.

6. Limitation and reduction of emissions through Article 6 projects cannot lead to the creation or bestowal of any title, holding, entitlement, goods, commodity or proprietary facility of any nature.

7. It must be ensured that Article 6 projects do not have dormant any possibility or potential of freezing or perpetuating past and present inequities between developed and developing countries. The right to development of developing countries must not be affected adversely in any way. Equity relates to equitable emission entitlements. The matter should be viewed in the light of contraction and convergence of emissions, wherein developed countries must contract greenhouse gas emissions to reduced levels with per capita emission levels in developed and developing countries coming on a converging path. Equal per capita emission levels is an equitable norm. The per capita criterion is central to the determination of emission entitlements. Per capita emission levels provide a direct measure of human welfare for economic and social development and poverty eradication in developing countries.

8. The effectiveness of CDM project activity must be assessed in terms of real, measurable and long-term benefits related to the mitigation of climate change at the project level. The reduction of emissions and their certification must be credible. The system should not be afflicted with scientific uncertainties. It must be ensured that climate change effectiveness must not be compromised at all in Article 6 projects. All the rigours and conditions of CDM project activity for ensuring real, measurable and long-term benefits related to the mitigation of climate change at the project level must apply to Article 6 projects.

C. "Part of"/supplementarity

9. The design and implementation of Article 6 projects must not in any way compromise the modification of longer-term trends in greenhouse gas anthropogenic emissions and concentrations. All the mechanisms, including Article 6 projects must be supplemental to domestic action in developed countries for GHG limitation and reduction. Developed country Parties' participation in Article 6 projects activities should be contingent on satisfaction of prescribed domestic effort in fulfilment of commitments under Article 3. A quantified ceiling on the emissions limited and reduced through the mechanisms is required. Commensurate non-compliance processes must be prescribed.

D. Participation

10. Parties included in Annex I shall only transfer or acquire ERUs from a project under Article 6, if they: (a) have ratified the Protocol; (b) are bound by a compliance regime adopted by the COP/moP; (c) have not been excluded from participation in Article 6 according to the procedures and mechanisms under the compliance regime; (d) are in compliance with their commitments under Article 12 of the Convention.

SUBMISSION ON ARTICLE 17 OF THE KYOTO PROTOCOL

I. NATURE AND SCOPE

A. Purpose

1. "Emissions trading" under Article 17 of the Protocol will assist Parties included in Annex B of the Protocol in achieving part of their quantified emission limitation and reduction commitments under Article 3. Only Parties included in Annex B may participate in "emissions trading" under Article 17 for fulfilling their commitments under Article 3. The purpose of "emissions trading" under Article 17 of the Kyoto Protocol is to enable a Party included in Annex B to transfer a part of its assigned amount of emissions to another Annex B Party for implementing commitments in Article 3, according to which Parties included in Annex B shall, individually or jointly, ensure that their aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol do not exceed their assigned amounts, calculated pursuant to their quantified emission limitation and reduction commitments inscribed in Annex B of the Protocol, with a view to reducing their overall emissions of such gases by at least 5 per cent below 1990 levels in the quantified emission limitation and reduction commitment period from 2008 to 2012.
2. The assigned amount of emissions is the quantified greenhouse gas emission commitment of Annex B Parties for the commitment period from 2008 to 2012, which shall be equal to the percentage inscribed for it in Annex B of its aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol in 1990, or the base year or period determined in accordance with the provisions in the Protocol, multiplied by five.
3. An Annex B Party may transfer a part of its assigned amount to another Annex B Party under Article 17, if the transferring Party, in the achievement of its quantified emission limitation and reduction commitment under Article 3, has been able to limit or reduce its greenhouse gas emissions through domestic policies and measures to an extent which exceeds its emission limitation and reduction commitment thereby resulting in a part of the assigned amount of emissions not being used. This part of the assigned amount, which has not been used because of emissions having been limited and reduced below the assigned amount of emissions, represents the difference between the assigned amount of the Party and its domestic emissions.
4. Such part of the assigned amount, not used by the transferring Annex B Party, may be transferred to another Annex B Party seeking to acquire a part of an assigned amount for offsetting domestic emissions exceeding its assigned amount of emissions. Any transfer and acquisition is of that part of an assigned amount which has not been used by the transferring Annex B Party due to limitation and reduction of domestic emissions below the assigned amount of emissions, to enable Annex B Parties to ensure

jointly that their emissions do not exceed their assigned amounts, thereby contributing to the achievement of quantified emission limitation and reduction commitments under Article 3. According to Article 3, Annex B Parties, individually or jointly, have to ensure that their emissions do not exceed their assigned amounts.

5. Transfers and acquisitions under “emissions trading” in Article 17 pertain only to a part of the assigned amount which has remained unused on account of the emissions having been limited and reduced below the assigned amount of emissions. Nothing else can be transferred and acquired under Article 17.

6. “Emissions trading” under Article 17 will be subject to the principle of complementarity and any other relevant principles, rules, modalities and guidelines.

B. Principles

7. The principles for “emissions trading” and related other basic elements must be decided first and formulated accordingly. These principles and basic elements must be in conformity with Article 3 of the Convention. The methodological and operational issues must be guided accordingly.

8. Parties should have further opportunity to make proposals and submissions about the methodological, operational and institutional issues pertaining to “emissions trading” under Article 17 after the principles, including the nature and scope of the CDM, have been decided. This approach is required to ensure that the methodological and operational issues pertaining to “emissions trading” under Article 17 and the institutional issues are guided and directed in accordance with the principles and nature and scope of Article 17.

9. The principles for “emissions trading” under Article 17 between Parties included in Annex B must be in conformity with the purpose of the mechanism. The principles for the mechanism must be in accordance with the principles of the Convention.

10. The purpose of “emissions trading” under Article 17 between the Parties included in Annex B, individually or jointly, is to ensure that their aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol do not exceed their assigned amounts, calculated pursuant to their quantified emission limitation and reduction commitments inscribed in Annex B of the Protocol, with a view to reducing their overall emissions of such gases by at least 5 per cent below 1990 levels in the quantified emission limitation and reduction commitment period, from 2008 to 2012.

11. The assigned amount of emissions is the quantified greenhouse gas emission commitment of Annex B Parties for the commitment period from 2008 to 2012, which shall be equal to the percentage inscribed for it in Annex B of its aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol in 1990, or the base year or period determined in accordance with the provisions

of the Protocol, multiplied by five. The assigned amount represents the quantified emission limitation and reduction commitment of each Annex B Party.

12. An Annex B Party may transfer a part of its assigned amount to another Annex B Party under Article 17 if that Party, in the achievement of its quantified emission limitation and reduction commitment under Article 3, has been able to limit or reduce its greenhouse gas emissions through domestic policies and measures to an extent which exceeds its emission limitation and reduction commitment thereby resulting in a part of the assigned amount of emissions not being used. This part of the assigned amount, which has not been used because of emissions having been limited and reduced below the assigned amount of emissions, represents the difference between the assigned amount of the Party and its domestic emissions.

13. Such part of the assigned amount, not used by the transferring Annex B Party, may be transferred to another Annex B Party seeking to acquire a part of an assigned amount for offsetting domestic emissions exceeding its assigned amount of emissions. Such transfer and acquisitions of unused parts of assigned amounts, because of emissions having been limited or reduced below the assigned amount of emissions, will enable the Annex B Parties to jointly ensure that their emissions do not exceed their assigned amounts, thereby contributing to the achievement of quantified emission limitation and reduction commitments under Article 3. According to Article 3, Annex B Parties, individually or jointly, have to ensure that their emissions do not exceed their assigned amounts.

14. Transfers and acquisitions under "emissions trading" in Article 17 pertain only to a part of the assigned amount which has remained unused on account of the emissions having been limited and reduced below the assigned amount of emissions. Only the excess limitation and reduction of emissions by an Annex B Party, resulting in the prevention of a part of its assigned amount of emissions, and nothing else, can be transferred and acquired under Article 17. Nothing else can be transferred and acquired under Article 17.

15. "Emissions trading" under Article 17 between Annex B Parties is unlike the other mechanisms. It is the only mechanism which is not project based. Unlike the other mechanisms, which are based on transnational projects to be set up for abatement of greenhouse gases, "emissions trading" in Article 17 for the commitment period of 2008-2012 is based on greenhouse gas inventories derived from past emissions. It must be ensured that such "emissions trading" does not have dormant any possibility or potential of freezing or perpetuating past and present inequities between developed and developing country Parties. The right to development of developing countries must not be affected adversely in any way.

16. "Emissions trading" under Article 17 between Annex B Parties can not create or bestow any right, title, holding, entitlement, goods, commodity or proprietary facility of any nature to the participating Parties. "Emissions trading" under Article 17 is only for

accounting of transfers and acquisitions of parts of assigned amounts between Annex B Parties for fulfilling their commitments under Article 3.

17. The principles, rules, modalities and guidelines will ensure that "emissions trading" under Article 17 between Annex B Parties does not create or bestow any right, title, holding, entitlement, goods, commodity or proprietary facility of any nature to the participating countries.

18. Only the Parties included in Annex B may participate in "emissions trading" under Article 17 for the purpose of fulfilling their commitments under Article 3.

19. There is no fungibility between the assigned amount, the ERUs and the CERs. The assigned amount, the ERUs, and the CERs are unlike concepts. The CER is a certification of the emissions reduced from a certified CDM project activity assisting sustainable development in a developing country which a developed country has funded. Such project activity, while achieving the two-fold purpose of the CDM, is being funded by developed countries because of the project activity being a lower cost option for reducing emissions compared to the alternative of implementing policies and measures in the developed country funding the project for limiting and reducing an equivalent amount of emissions. The ERU is a certification of the emissions reduced from joint implementation of projects between developed country Parties under Article 6 because of such project activity being a lower cost option for reducing emissions compared to domestic policies and measures for limiting and reducing an equivalent amount of emissions. The assigned amount of emissions is the emission commitment for the commitment period.

20. Of fundamental importance is the environmental integrity of the system to be brought in place under Article 17 and its credibility. The rules to be formulated must conform to the principles.

21. Any system established under Article 17 of the Protocol shall contribute to bringing about real, measurable and long-term benefits related to mitigation of climate change. Transfers and acquisition of part of assigned amount under "emissions trading" in Article 17 should result in contraction of emissions among developed country Parties leading to per capita equity in distribution of emissions between developed and developing countries. Equal per capita emission levels is an equitable norm. The per capita criterion is central to the determination of emission entitlements. Per capita emission levels provide a direct measure of human welfare for economic and social development and poverty eradication.

22. "Emissions trading" under Article 17 between Annex B Parties shall be supplemental to domestic actions for the purpose of meeting quantified emission and limitation reduction commitments under Article 3 of the Protocol.

23. There must be no compromise on climate change effectiveness. Any system established under Article 17 of the Protocol shall contribute to and bring about real, measurable and long-term benefits related to mitigation of climate change.

24. The rules must conform to the principle of climate change effectiveness, and stipulate the conditions to be fulfilled before the transfer or acquisition of a part of the assigned amount.

C. Supplementarity

25. Article 17 states: "Any such trading shall be supplemental to domestic actions for the purpose of meeting quantified emission limitation and reduction commitments under that Article".

26. The design and implementation of any system under Article 17 must not in any way compromise the modification of longer-term trends in greenhouse gas anthropogenic emissions and concentrations. Commensurate non-compliance processes must be put in place. Annex B Parties access to Article 17 should be contingent on satisfaction of prescribed domestic effort in fulfilment of commitments under Article 3. The rules will lay down the conditions which must be fulfilled before any such transfers and acquisitions can occur.

27. Domestic policies and measures must be the principal means for achieving the quantified emission limitation and reduction commitments under Article 3 of the Protocol. A quantified ceiling on the emissions limited and reduced through the mechanisms is required.

D. Participation

28. Article 17 states: "the Parties included in Annex B may participate in emissions trading for the purpose of fulfilling their commitments under Article 3." Annex B Parties have quantified greenhouse gas emission limitation and reduction commitments. Annex B Parties, individually or jointly, have to ensure that their aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A of the Protocol do not exceed their assigned amounts, which is the emission limitation and reduction commitment of Annex B Parties for the commitment period from 2008 to 2012.

29. Parties included in Annex B shall be eligible to transfer or acquire part of the assigned amount, if they:
- (a) are in compliance with Articles 3, 5 and 7 of the Protocol and are responsible for meeting their commitments under the Protocol;
 - (b) are not in violation of the compliance procedures as referred to in Article 18 of the Protocol;
 - (c) have a transparent national system for registration and verification of transfers and acquisitions.

II. METHODOLOGICAL AND OPERATIONAL ISSUES

A. Modalities of operation

30. Any Annex B Party participating in the system to be established under Article 17 shall establish and maintain transparent national registration system of transfers and acquisitions. Such information shall be communicated regularly to the Convention Secretariat. Annex B Parties participating in the transfers and acquisitions of parts of assigned amounts under Article 17 of the Protocol, shall include in their national inventory, information on any part of an assigned amount added to or removed from its national registration, which should be communicated to the Secretariat. Parties included in Annex B shall be eligible to transfer or acquire part of the assigned amount, if they are in compliance with Articles 3, 5 and 7 of the Protocol. The Parties should not be in violation of the compliance procedures in Article 18 of the Protocol. The Parties should have a transparent national system for registration and verification of such transfers and acquisitions.

B. Verification

31. Each Annex I Party participating in "emissions trading" under Article 17 must establish a national system for the monitoring and verification of "emissions trading" in accordance with the provisions of the Protocol and the principles, rules, modalities and guidelines to be established. There must be certification of the transfers and acquisitions by a COP/moP designated independent entity, according to the rules, modalities and guidelines decided by the COP/moP.

C. Issues related to Compliance

32. Effective procedures and mechanisms to determine and address cases of non-compliance with the provisions of the Protocol and the relevant principles, rules, modalities and guidelines should be established by the COP/moP.

D. Registries

33. Registration of transfers and acquisitions of parts of assigned amount must be in accordance with the relevant principles, rules, modalities and guidelines. The transfer and acquisition of a part of assigned amount can be only of that part of the assigned amount which has not been used by the transferring Annex B Party due to limitation and reduction of domestic emissions below the assigned amount of emissions. Such transfers and acquisitions will be contingent on the fulfilment of the principle of supplementarity.

34. Transfers and acquisitions of parts of assigned amount due to "emissions trading" under Article 17 cannot increase or decrease the assigned amount of Annex B Parties which has been calculated pursuant to the quantified emission limitation and reduction commitments inscribed in Annex B. The assigned amount for each Annex B Party shall be equal to the percentage inscribed for it in Annex B of its aggregate anthropogenic carbon dioxide equivalent emissions of the greenhouse gases listed in Annex A multiplied by five.

35. The registration system must keep in view the purpose of "emissions trading" under Article 17, which is to enable Annex B Parties to ensure jointly that their emissions do not exceed their assigned amounts. The registration system should take into account, that the assigned amount represents the quantified emission limitation and reduction commitment of the Annex B Parties for the commitment period. In the event of an Annex B Party having limited and reduced its emissions below its assigned amount of emissions, the opportunity arises for another Annex B Party which having exceeded its assigned amount of emissions may seek to offset its excess emissions. In this connection, any transfers and acquisitions of part of assigned amount will only add to or subtract from the quantified emission limitation and reduction commitment of the Annex B Parties.

E. Reporting by Parties

36. Annex B Parties participating in "emissions trading" under Article 17, shall incorporate in their annual inventories, to be submitted to the Secretariat under Article 7 of the Protocol, specific information on the acquisitions and transfers of the assigned amount. As part of the annual compilation and accounting of emission inventories under Articles 7 and 8 of the Protocol, the secretariat shall annually present a synthesis of the reports by Annex B Parties about the acquisitions and transfers of part of assigned amounts.