Scaled-up crediting: possible role, basic framework and design issues

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Today’s main focus

To explore opportunities and challenges of scaled-up crediting
Topics to be covered today

- Rationale and expectations for scaled-up crediting
- Role of a new generation of crediting:
  - Place in the international climate policy architecture
  - Non-regrets readiness for countries
- Building blocks & methodologies
- Design & Implementation beyond project-by-project:
  - Options for implementation & set-up
  - New design issues
- Examples & relevance for Vietnam
• Rationale and expectations for scaled-up crediting
• Role of a new generation of crediting
• Building blocks & methodologies
• Design & Implementation beyond project-by-project
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Some basic concepts of crediting

<table>
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<tr>
<th>Crediting</th>
<th>Offseting</th>
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<td>recognising an emission reduction “below baseline” (CDM, VCS, ACR all issuing “credits”)</td>
<td>using allowances or credits to comply with a mandate (voluntary target, cap under an ETS)</td>
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- Crediting for offsetting was extensively used under the Kyoto Protocol (CDM, JI) and with voluntary offsetting mechanisms
- Crediting mechanism can also deliver towards other types of commitments:
  - Compensation or neutralisation goals
  - Used in results-based finance as metric of GHG performance

*Based on presentation by P. Barata at WB Technical workshop on scaled-up crediting approaches, Bonn, June 2015*
Why scaling-up crediting?

• Reach larger emission reduction opportunities
• Cover more sectors using market mechanisms
  • Addressing mitigation options with more complex causality/impact demonstration
• Address leakage in existing systems
  • Achieving more widespread exposure to a price of carbon
• Facilitate transformational change
  • More strategic, targeted incentives at the level of key sectors and technologies

But...

• Lack of demand for offsetting for carbon markets
• Allocation of resources is rather driven by (mostly public) financing flows than by (mostly private) carbon market forces

Based on presentation by P. Barata at WB Technical workshop on scaled-up crediting approaches, Bonn, June 2015
Place of scaled-up crediting in the international climate change architecture

- Outcomes in Paris COP is uncertain:
  - NMM or non-UNFCCC approaches (FVA) or both?
  - Continuation of CDM/JI beyond KP2?
  - No agreement/work program on markets at all?

New Market Mechanism
Pilot programs follow principles underlying NMM
Net mitigation, broad segments of the economy

Non-UNFCCC Approaches
Bilateral options
Design largely left to national/regional authorities (e.g., NAMA with crediting component)

Reformed CDM/JI
Increased interest in a reformed post 2020 CDM/JI
Existing methodologies with discounting

Lack of any UNFCCC framework
Pure VER approach
Possibly use of a national standard
Example of a “vision” for a new generation of market-mechanism under UNFCCC

- Stimulating mitigation across broad segments of the economy
- Safeguarding environmental integrity
- Ensuring a net decrease and/or avoidance of global emissions
- Crediting track:
  - “Emissions of a broad segment of an economy will be checked against an ex-ante agreed crediting threshold for this segment. If emissions are below this threshold, emission credits will be issued ex post, which can be sold to recover, at least partly, the cost of mitigation activities. If emissions are not below the threshold, no penalty will be applied (no-lose target).”

  Source: EU NMM UNFCCC Submission 2012

  - Crediting should discount for effects of national policies
Adequate demand for carbon credits both in volume and price is critical for the success of crediting instruments.

Factors determining the future of crediting:

- Levels of ambition in climate agreements
  - Type of targets (e.g., in INDCs)
  - Number of countries setting them
  - Stringency of targets in relation to cost-effective GHG mitigation potential
  - Timeline for achieving targets

- Role of crediting in future targets and policies choices to meet targets
  - Use of credits as mean for compliance
  - Quantitative & qualitative restrictions on the use of credits
  - Choice of main mitigation instruments (ETS, carbon tax, EE policies)

- Ability of implement policies
  - Implementation of policies that allow use of credits as mean of compliance
  - Political preferences for the sources of credits
  - Macro-economic conditions
  - Ability of participants (supply side) to meet buyers’ requirements
• Rationale and expectations for scaled-up crediting
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Why new generation of crediting matters?

- Facilitate contribution to national mitigation action
  - Mobilize larger mitigation potential in targeted sectors
  - Trigger available policy options in different sectors
  - Contribute to mitigate national abatement costs in a longer term

- Serve broader policy objectives and bring multiples benefits
  - Create readiness to access other types of climate finance
  - Pave way for using more comprehensive market-based instruments

- Offer opportunity to design and pilot future mechanisms
  - Build on experience learned from implementation
  - Overcome limitations of current approaches
Climate policy frameworks under which crediting readiness could catalyze scaled-up mitigation

- Various policy frameworks may include potential market and non-market mechanisms that countries may pursue to “scale up” mitigation action

**Market-based mechanisms**
- Domestic ETS
- Carbon tax
- Crediting instruments
  - Internationally-recognized crediting (e.g. via NMM or FVA)
  - Domestic voluntary crediting program
  - Domestic crediting program for domestic ETS/tax compliance

**Non-market mechanisms & finance options**
- Direct GHG regulation (e.g. performance standard)
- A boarder policy, legislative and institutional framework for low-carbon investment
- Finance options or vehicles
  - Results-based finance as a tool to channel international climate finance
  - NAMA (i.e., with crediting component)
  - Other traditional finance options
Role of crediting instruments under multiple climate policy instruments (1/2)

- Crediting readiness can contribute to a wider climate policy development and fostering mitigation under multiple policies

- This role can be achieved by building readiness in an “adaptable” way to support:

  **Broader applicability to other policy instruments and funding approaches (“minimizing regrets”)**
  - Data management
  - Quantification of mitigation potential
  - Baseline determination

  **Building political momentum and a broad stakeholders’ engagement (“maximizing benefits”)**
  - Advancing regulatory frameworks
  - Developing domestic sources of demand
  - Setting up financing vehicles
Role of crediting instruments:
Support to the evolution of domestic climate policy (2/2)

- Illustrative domestic policy pathway:

- NAMA
  - Emission reductions (ERs)
  - Climate finance (RBF or other)

- Sectoral crediting
  - ERs as carbon credits for international (compliance) markets
  - Purchase of credits

- Emissions trading
  - Emission reductions (from binding cap)
  - Demand for allowances, credits, own reductions
• Rationale and expectations for scaled-up crediting
• Role of a new generation of crediting
• **Building blocks & methodologies**
• Design & Implementation beyond project-by-project
• Examples & relevance for Vietnam
Building blocks of crediting programs: using current broad framework of principles

• Program building blocks envisaged:
  • Scale and target of the crediting program
  • Coverage
  • Baseline setting
  • Performance indicators and emission reduction quantification
  • Financing and incentive structure
  • Monitoring, reporting and verification (MRV) approach
  • Net mitigation
  • Issuance, transfer and accounting of creditable emission reductions

• Key principles to ensure high quality of credits:
  • Environmental integrity
  • Transparency
  • Simplicity and low transaction costs
Building blocks of crediting programs: ensuring environmental integrity and transparency

- Environmental integrity is critical and could be achieved via the approach to baseline setting:
  - In relation to the overall policy context and the relationship of the crediting program with the objectives and instruments outlined in the INDCs
  - Under NMM, it could be further strengthened by the principle of “net mitigation”

- Monitoring, reporting and verification (MRV) approaches for the crediting programs should ensure that:
  - Impacts of the implemented measures and policy actions can be accounted for with transparency
  - Sufficient levels of accuracy of MRV is achieved

- Institutional and policy infrastructure to ensure efficient and transparent functioning of the crediting programs
Examples of crediting-related activities supported by PMR in 8 Implementing Countries

- **Analysis of policy options**
- **Instrument design**
- **Mitigation potential assessment**

- **Data collection**
- **Data management**
- **MRV**

- **Regulatory and Institutional frameworks and coordination**

- **Quantification approaches (including baseline setting)**
- **Crediting methodologies or protocols**
- **Approaches to achieve net emission reductions**

- **Registries for crediting projects and units**

- **Creation or strengthening of domestic demand**
- **Finance vehicles**

- **Capacity building, engagement, and stakeholder participation**
- **Piloting activities**

- **Implementation activities**
Net mitigation

• Net mitigation in a context when there is a shift to a common but differentiated approach whereby all countries define INDCs:
  • An intention to go “beyond offsetting” with the objective of leveraging domestic actions in the implementing country
  • A willingness not to account for a share of ERs “beyond offsetting” against any target in view of increasing international ambition (“net atmospheric mitigation”)

• Different ways to put into practice:
  • Discounting of generated ERs
  • Use of ambitious baselines
  • Apply conservative crediting line
Synergies with national mitigation efforts & avoidance of double counting

• Crediting programs in the context of INDCs/other voluntary efforts:
  • Programs are likely to be part of larger climate strategies and actions at the national or sectoral level (e.g., such as outlined in the INDCs)
  • Multiple sources/types of support from a variety of funders
• Crediting framework should ensure that the double counting is avoided, for example by:
  • Considering the overall policy context when setting consistent, ambitious baselines and crediting thresholds,
  • Quantifying the net mitigation
  • Agreeing with implementing countries on the principle of avoiding “double counting” in the absence of an international registry
Building blocks of crediting programs: using the experience of KP mechanisms (3/3)

• Build from CDM/JI experience and methods whenever relevant
  • Methodologies
  • Independent international/national auditing capacities
  • Stakeholder consultation process
  • MRV-related systems and processes
  • Extensive database generated by CDM on mitigation options/costs, benchmarks
• Rationale and expectations for scaled-up crediting
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Several possible tracks of scaled-up crediting

- Sectoral with sectoral targets
- Policy-driven crediting approach:
  - Based on national/sectoral MRV protocols (related to GHG inventories)
  - Applying standards across an entire sector/section of economy
- Integrated crediting approach:
  - Sub-national jurisdictions (cities, nested crediting programs) that may cover several sectors
  - Coverage may depend on the jurisdictional mandate and overall climate policy context
Examples of scaled-up crediting programs envisaged (1/2)

- Integrated approach – complementing host country policies
  - Energy rehabilitation of buildings + mandatory energy efficiency standards
  - Soft loans for renewables + feed-in tariff system
  - Grants for fuel efficient vehicles + fuel efficiency standards

- Policy-based – increasing and enabling policy ambition
  - Energy efficiency standards
  - Feed-in tariff systems
  - Increasing ambition in domestic carbon pricing: acceleration of fossil fuel subsidy removal, carbon tax enhancement, ETS enhancement

- Sector target-based – catalyzing ambitious target setting (country to chose implementation measures)
  - Power sector
  - Industrial sectors, e.g., steel, cement
  - Waste sector
Examples of scaled-up crediting programs envisaged (2/2)

- Market mechanism principles suggested by European countries are compatible with broad range of sector programs.
- Emerging INDC landscape requires flexibility in designing and implementing crediting/trading instruments.
- Lack of real world experience and uncertainty of UNFCCC process allow broad design options under the suggested principles of scaled-up crediting.
- Blueprinting exercise indicates that large number of possible variations are possible in each main program type.
- A priori no program type dominates the others.
Quick zoom into sectoral crediting: Two possible tracks (1/2)

- Installation-based approach:
  - Based on MRV protocols such as CDM, applied at a sufficiently high level of aggregation at sector
  - Building on programmatic CDM, introducing “net mitigation/own contribution”

- Sector-based approach:
  - Based on national/sectoral MRV protocols (related to GHG inventories)
  - Applying standards across an entire sector/section of economy
Sectoral crediting: Technical issues (2/2)

- Signal pass-through
  - Crediting of individual performance or group performance
- Defining “broad segment of economy”: coverage issues
  - Product-based or process-based definition of sectors
- Baseline construction and interaction with policies / policy crediting
- Defining “meaningful contribution” / “net mitigation”
  - Political requirement of the new climate framework
  - Different ways to put into practice (e.g., discounting, use of ambitious baselines)
  - How to relate the “own contribution” to the INDCs?
Key methodological needs beyond project-by-project

• Aggregate GHG accounting and monitoring
  • Simpler, less costly methods for MRV and data collection techniques
  • Aggregate performance indicators to capture impacts of complementary polices

• Quantification & attribution of aggregate impacts in presence of other policies
  • Baseline setting in consideration of other national /sectoral policies and instruments
  • Demonstration of net emission reductions / own contribution at (sub-)sectoral level
  • Attribution of impacts in presence of other policies (horizontal & vertical interactions)

• Approaches to avoid double counting and leakages
  • Design MRV and registry systems compatible with national GHG accounting
  • Definition of accounting rules for crediting in a capped environment with a mix of climate policies (e.g., use of crediting reserves)
• Rationale and expectations for scaled-up crediting
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Status of crediting-related activities in the PMR countries (1/3)

- Examples & relevance for Vietnam -

• 8 out of 17 PMR Implementing Countries include crediting as the principal market-based instrument in their MRPs
Status of crediting-related activities in the MRPs (2/3)

- Crediting-related activities in the MRPs primarily include:
  - Strengthening policy and legislative environment;
  - Enhancing technical capacity and build “institutional infrastructure”;
  - Support of specific initiatives and programs (in some Implementing Countries).

- Objectives put forward for crediting-related activities vary:
  - Using crediting instrument to complement existing climate policies and instruments (NAMAs, voluntary markets, standards in transport);
  - Using crediting instrument as a way to build technical capacity as possible foundation to emissions trading.
Status of crediting-related activities in the MRPs (3/3): Different considerations of the evolving context

- Implementing Countries have different (evolving) considerations about the international and domestic demand for credits
- Most of the MRPs incorporate (re-)assessments of evolving context, including for sources of demand
- A number of crediting-related activities have a broader applicability for a range of climate policy instruments:
  - Data management, MRV, capacity building.
- Design options can be chosen to stimulate this broader applicability (adaptability)
Some commonalities and divergences of implementing countries’ approaches to scaled-up crediting

- Choice of instrument:
  - No common blueprint for the choice and design

- Choice of sectors:
  - Reflects national priorities

- Role of crediting instruments:
  - Support for domestic climate actions, policies, and/or markets

- Sources of demand:
  - Various approaches to mitigate risks of uncertain int. demand

- Roadmaps to implementation:
  - Many common elements, tailored to each country context
Crediting-related activities in Vietnam’s MRP

**Steel sector**
- NAMA Piloting
- Pilot crediting NAMA Implementation
- Sectoral Cap-And-Trade

**Waste management sector**
- Data management & reporting
- Identify appropriate MBIs
- Development of credited NAMA
- Nationwide application of MBIs

*Capacity building to facilitate NAMA implementation and data management*
Thank you!

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