Introduction
Negotiations to define rules for the implementation of Article 6 remain far from the goal of achieving consensus – or even a common understanding – on the basic framework that will underpin mitigation cooperation that leads to transfers of mitigation outcomes from one Party to another or to mitigation outcomes that are cooperatively achieved by and apportioned to more than one Party.

Greater common understanding on what could occur should no rules be agreed can help elucidate the benefits of agreed rules under UNFCCC auspices. But are any rules better than no rules? Are “bad” rules better than none?

This paper seeks to elucidate this question, and related ones such as:

- Would a lack of Article 6 rules prohibit cooperative mitigation under the Paris Agreement?
- Would a no rules scenario imply no decision under Article 6.2 that enables such cooperation? What about under Article 6.4? Article 6.8?
- Would an absence of rules allow cooperation without a mitigation transfer?
- What alternatives are there for cooperative approaches in the absence of rules (e.g. continuation of CDM)?
- In the absence of “good” UNFCCC rules, is the world stuck with either “bad” rules or “no rules”? Are other forms of cooperation possible that improve environmental integrity?

In order to pursue this analysis, we first seek to define in basic terms the different potential types of mitigation transfers or cooperation that are possible under the Paris Agreement, and to consider whether they are possible in a no rules situation.

We then will seek to clarify what a “no”, “bad” and “good” rules could imply – defining stylized scenarios that illustrate each case, recognizing that how these are defined itself is a normative exercise. Based on this, we will be able to highlight risks in each scenario and alternatives that could be considered by Parties who wish to go further to define rules bilaterally or plurilaterally.

Consideration

Three (and a half) flavors
To help understand the impact of rules or no rules, it is useful to consider different “types” or “flavors” of potential mitigation transfers or cooperation that are enabled under the Paris Agreement – or could be should the rules allow for it.
First, there are bilateral transfers – Internationally Transferred Mitigation Outcomes (ITMOs), which come in three flavors:

- Pure bilateral transfers: when two Parties enter into an agreement to transfer MOs from the host or source Party A to the user Party B, without seeking to register the generated units in an international transaction log to enable their participation in a Paris Agreement-compliant carbon market.
  - Party B would therefore not be able to further transfer the acquired MOs to a third Party C without Party C having first certified Parties A and B for compliance of their systems with national Party C regulatory requirements.
  - Party A would also not be able to sell or transact the MOs on the open market to entities looking to acquire the units for compliance purposes, other than in Party B.

- Bilateral transfers of fungible units: when two Parties enter into an agreement to transfer MOs from the host Party A to the user Party B, registering the generated units in an international transaction log to enable participation in a Paris Agreement-compliant carbon market.
  - Party B would therefore be able to further transfer the acquired MOs to a third Party C without Party C having first certified Parties A and B.
  - Party A would also be able to sell or transact the MOs on the open market to entities looking to acquire the units for compliance purposes.

- Bilateral transfers through Article 6.4 mechanism: Party B acquires units generated and approved through the mechanism, and sourced from Party A. By going through the mechanism, the units are fully fungible.

In addition to bilateral transfers, mitigation cooperation under Article 6.8 can also be seen as “type” or “flavor”:

- For example, one can envisage a run-of-the-river hydro project on a transboundary river between Party A and Party B. Both Parties contribute to the investment, and both use the power. One can also envisage parties deciding to create a “bubble” over a shared sector, or even to cover their entire economies.
  - While no transfer of MOs occurs from one party to another, cooperatively achieved mitigation outcomes will have to be transparently attributed to participants.
  - No fungible units are created, but there is a need to establish that no cooperatively achieved MO has been counted twice towards NDC achievement in Party A and B.
What types of transfers will go ahead without rules

The figure below summarizes the types or flavors of mitigation cooperation provided for under Article 6, how they relate to the articles, and whether those articles enable in and of themselves, without further specification of rules, cooperation of that type to go ahead.

**Article 6 cooperative mitigation options: which require rules in order to occur?**

**Article 6.1:** voluntary cooperation by Parties in the implementation of their NDCs to allow for higher ambition and promote sustainable development and environmental integrity

**Article 6.2:** international transfers of mitigation outcomes

- **Pure Bilateral Transfers:** Parties transfer ITMOs that are recognized by their respective national systems; onward transfer to 3rd Parties for NDC compliance not possible w/out further bi- or plurilateral agreements.
- **Fungible Bilateral Transfers:** Parties transfer ITMOs with unique, UNFCCC-recognized identifiers; onward transfer to 3rd Parties through carbon market is facilitated.

**Article 6.4:** transfers through mechanism

- Parties transfer ITMOs through central institution under UNFCCC auspices; onward transfer to 3rd Parties through carbon market is facilitated.

**Article 6.8:** non-market cooperation

- Parties share mitigation outcomes of joint projects: no “transfer” from one Party to another, however, claiming of mitigation outcomes risks double counting.

It is important to highlight that until rules are agreed, some forms of cooperation will be able to go ahead and others won’t, namely those that depend on UNFCCC institutions to underpin them. Cooperation that only requires the approval of the Parties involved will be able to go ahead as there is no express prohibition on these activities in the absence of rules. In the absence of Article 6.2 guidance, parties would need to meet the Article 6 requirements as interpreted by those involved in the transfer, particularly the acquiring Parties.

- Large user Parties of ITMOs will essentially set the rules in this situation as it is their national authorities that will evaluate source countries for compliance with Paris Agreement obligations.

- Gaps may exist in the way different large Parties assess potential ITMOs, which could lead to inefficiencies and higher transaction costs for issuers.

- The lack of a shared international registry will lead to greater difficulty in assessing double counting and potential sales of the same MO to multiple acquirers.

- Smaller, lower capacity Parties will face difficulty in meeting different national standards, and will either be excluded from this system or will need to focus on one or two main acquiring Parties. This could result in lower prices than if a mechanism such as that provided for in Article 6.4 ensured that smaller Parties could access all potential buyers.
Table 1: “No rules”, “bad rules” and “good rules”

<table>
<thead>
<tr>
<th></th>
<th>Good rules</th>
<th>Bad rules</th>
<th>No rules</th>
<th>Alternatives</th>
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</thead>
<tbody>
<tr>
<td><strong>General</strong></td>
<td>• Rules provide clear guidance to Parties on how to implement the provisions and principles of PA and its Art. 6</td>
<td>• Rules are vague, ambiguous, lead to misunderstandings/conflict</td>
<td>• Only some types of cooperation can go ahead</td>
<td>Clubs of hosts and users set ”good rules” plurilaterally</td>
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<td></td>
<td>• Article 6.4 mechanism helps small/low-capacity Parties benefit from ITMO opportunities</td>
<td>• Least stringent Party sets standard for whole system</td>
<td>• Large users of MOs determine/enforce standards</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>• Least stringent Party sets standard for whole system</td>
<td>• Complex spaghetti bowl of bilateral arrangements</td>
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<tr>
<td></td>
<td></td>
<td>• Only some types of cooperation can go ahead</td>
<td>• Small/low-capacity Parties excluded or at a disadvantage</td>
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<td><strong>Pure bilateral transfers</strong></td>
<td>• Parties avoid double counting (DC) transfers</td>
<td>• Rules allow some DC</td>
<td>• Lack of common approach makes accountability and comparability very complex</td>
<td>Clubs can allow generation of fungible units to be traded by partners who mutually recognize standards and link registries</td>
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<tr>
<td></td>
<td>• Parties account transparently</td>
<td>• Rules don’t promote enough transparency and/or require Parties to show how transfers support ambition</td>
<td>• Linked emissions trading systems</td>
<td></td>
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<td></td>
<td>• Parties report on how transfers support ambition</td>
<td>• Rules allow some DC</td>
<td>• Without transaction log, there is no global carbon market under UNFCCC auspice</td>
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<td>• Transaction log tracks each ITMO unit from generation to retirement or cancellation</td>
<td>• Rules don’t promote enough transparency and/or require Parties to show how transfers support ambition</td>
<td>• Such transfers are not enabled by UNFCCC</td>
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<td><strong>Transfers through Article 6.4 mechanism</strong></td>
<td>• Supervisory body approves transfers that avoid DC</td>
<td>• Rules allow some DC</td>
<td>• Without supervisory body, such transfers are not possible</td>
<td>CDM could continue</td>
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<td>• Parties account transparently</td>
<td>• Rules don’t promote enough transparency and/or require Parties to show how transfers support ambition</td>
<td>• Without supervisory body, such transfers are not possible</td>
<td>Would be left to Parties to show DC is avoided (e.g. in when CDM unit is sourced within NDC scope)</td>
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<td><strong>Non-market mitigation cooperation</strong></td>
<td>• Parties account transparently, similarly as for 6.2 and 6.4</td>
<td>• Coop. mitigation outcomes could be double-claimed</td>
<td>• Lack of common approach makes accountability and comparability very complex</td>
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Conclusions

Whether “bad” rules are worse than “no rules” depends on a number of normative considerations, but it is clear that a “no rules” scenario would allow certain types of transfers to occur and would prevent others from taking place.

“No rules” could lead to a more complex system that would be hard for low-capacity countries to navigate. Large users would set the standards.

Without rules, smaller, lower capacity Parties would be dependent on national authorities in user countries, rather than being able to turn to the Article 6.4 mechanism to help them access acquiring Parties efficiently.

While it is true that large Parties will likely have an outsize say in any rules to be agreed, agreed rules would at least provide for common reporting frameworks and obligations, lower risk of gaps and a system that would be easier to navigate for stakeholders looking to understand the actions of Parties with a view to ensuring political accountability.

“Bad” rules would not necessarily be “better” than “no rules”, in the sense that bad rules could also result in gaps, mis-reporting, etc. but at least would allow for certain mitigation actions to occur that might not under a “no rules” scenario, for example, actions that would occur in Parties that are likely to depend on Article 6.4.

CCAP welcomes any questions, comments and suggestions about this working paper.

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