New Zealand

A Submission to the Ad-Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP)

Possible Improvements to Emissions Trading and the Project-Based Mechanisms

24 April 2009

Purpose

1. At its seventh session, the AWG-KP:

   a. Continued its deliberations on the possible improvements to emissions trading and the project-based mechanisms identified in annexes I and II to the report on the first part of its sixth session (FCCC/KP/AWG/2008/5).[1]
   b. Agreed to continue these deliberations at its eighth session (June 2009) in the context of its deliberations on the Chair's text referred to in paragraph 4(b) of the draft conclusions contained in FCCC/KP/AWG/2009/L.5.[2]
   c. Invited Parties to submit to the secretariat views on annexes I and II for compilation into a miscellaneous document for consideration at its eighth session.[3]
   d. Invited Parties to submit to the secretariat further views and proposals on matters relating to the request referred to in paragraph 4(b) of the draft conclusions contained in FCCC/KP/AWG/2009/L.5 for compilation into a miscellaneous document.[4]

2. This submission from New Zealand is in response to the invitations for submissions referenced in both points (c) and (d) above.

Introduction

3. New Zealand considers that agreement on effective rules for the operation of emissions trading and the project-based mechanisms (the "flexibility mechanisms") after the first commitment period will be essential in order for Parties to meet their quantified emission limitation and reduction commitments (QELRCs) in a way that ensures environmental integrity, supports sustainable development and technology transfer for developing countries, and enables the maximum amount of global emission reductions to be achieved for a given level of investment.

4. In order to provide Annex I Parties with the level of understanding of the environmental and cost implications of QELRCs necessary for them to accept binding QELRCs, certainty on the key rules for the flexibility mechanisms is

[1] FCCC/KP/AWG/2009/L.2.
[2] FCCC/KP/AWG/2009/L.5, paragraph 4(b) records that the AWG-KP requested its Chair to prepare a text on other issues outlined in the report on its resumed sixth session (FCCC/KP/2008, paragraph 49).
[3] FCCC/KP/AWG/2009/L.2.
[4] FCCC/KP/AWG/2009/L.5.

required. More detailed rules for implementation of the flexibility mechanisms can then be decided in subsequent negotiations prior to the start of the second commitment period.

5. Improvements to the flexibility mechanisms that are part of a comprehensive agreement at the fifth meeting of the CMP in Copenhagen may require amendments to the Kyoto Protocol in some instances and CMP decisions in others. New Zealand considers that the AWG-KP has the mandate to consider both types of proposals, and has therefore proposed a mixture of legal formulations for the recommendations in this submission on improvements to the flexibility mechanisms.

6. In evaluating the proposals for possible improvements to the flexibility mechanisms, New Zealand re-iterates the importance of considering the proposals' cost effectiveness, administrative complexity, and potential for perverse outcomes.

Views on Improvements to Emissions Trading and the Project-Based Mechanisms

Annex I

I. Clean Development Mechanism (CDM)

I.A. Include other land use, land-use change and forestry activities

7. Refer to New Zealand's submission on land use, land-use change and forestry prepared in response to FCCC/KP/AWG/2009/L.3.

I.B. Include carbon dioxide capture and storage

Description

8. New Zealand supports Option C (paragraph 7) to include carbon dioxide (CO_2) capture and storage in geological formations[5] (CCS) as CDM project activities starting in the second commitment period provided that the further issues relating to CCS identified in annex I are sufficiently addressed in the CDM modalities and procedures.[6] If CCS is included in the CDM, its eligibility beyond the second commitment period should be assured to help provide certainty to project developers.

Rationale

9. New Zealand considers that CCS is an important option in the portfolio of mitigation measures available to reduce CO_2 emissions to the atmosphere. According to the Intergovernmental Panel on Climate Change (IPCC), the

[5] For the avoidance of doubt, the term "geological formations" is assumed to include saline aquifers and does not include ocean sequestration.
[6] These issues include: the short- and long-term liability (e.g. in relation to leakage and non-permanence); the provisions for monitoring, reporting and verification, taking account of data availability; the possible environmental impacts; the definition of project boundaries; and the potential for perverse outcomes.

widespread application of CCS will depend, *inter alia*, on technical maturity, uptake capacity, costs and regulatory frameworks. New Zealand considers CCS technology transfer highly important in improving these key aspects of CCS, and that the CDM will facilitate CCS technology transfer and the further development of CCS. However, a number of important methodological issues need to be addressed to ensure the long-term environmental integrity of CERs from CCS projects under the CDM.

10. Because CCS projects could be expected to involve long-term investment decisions, it will be important to ensure that they remain eligible for crediting beyond the second commitment period. However, the rules for the determination of additionality and the definition of crediting periods provided in decision 3/CMP.1 should continue to apply to CCS projects.

11. We note that the CDM Executive Board has been requested to assess the implications of the possible inclusion of CCS in geological formations as a CDM project activity, taking into account technical, methodological and legal issues, and report back to the Conference of the Parties serving as the Meeting of the Parties to the Kyoto Protocol (CMP) at its fifth session.[7] This request has been made in the context of the first commitment period, but the findings will be relevant to consideration of the eligibility of CCS project activities under the CDM after the first commitment period.

12. The general process and legal text that we are proposing for the development of definitions and modalities for CCS in the CDM is informed by the approach applied in the annex to Decision 5/CMP.1 on afforestation and reforestation project activities under the CDM.

Proposed legal text: CMP Decision: CCS in the CDM

Affirms that carbon dioxide capture and storage in geological formations[8] shall be eligible as a clean development mechanism project activity in the second and subsequent commitment periods;

Requests that the Subsidiary Body for Scientific and Technological Advice develop definitions and modalities for including carbon dioxide capture and storage in geological formations under the clean development mechanism in the second and subsequent commitment periods, taking into account the issues of leakage, non-permanence, monitoring, reporting, verification, environmental impacts, the definition of project boundaries, issues of international law, and the potential for perverse outcomes, with the aim of the Conference of the Parties serving as the Meeting of the Parties to the Kyoto Protocol adopting a decision on these definitions and modalities at its [Xth] session;

Invites Parties and the Executive Board of the clean development mechanism to submit their views on the work to be conducted under the paragraph above;

Decides that the decision by the Conference of the Parties serving as the Meeting of the Parties to the Kyoto Protocol on definitions and modalities for inclusion of carbon dioxide capture and storage in geological formations under the clean development

[7] FCCC/KP/CMP/2008/L.6.
[8] For the avoidance of doubt, the term “geological formations” is assumed to include saline aquifers and does not include ocean sequestration.

mechanism for the second and subsequent commitment periods shall be in the form of an annex on modalities and procedures for carbon dioxide capture and storage in geological formations reflecting, *mutatis mutandis*, the annex to decision 3/CMP.1 on modalities and procedures for the clean development mechanism;

I.C. Include nuclear activities

Description

13. New Zealand supports Option B (paragraph 9) which provides that activities relating to nuclear facilities are not eligible as CDM project activities.

Rationale

14. Noting that the purpose of the CDM is to assist non-Annex I Parties in achieving sustainable development, New Zealand does not consider that nuclear activities are appropriate under the CDM. We do not consider that nuclear power is a sustainable energy source. We have long-standing concerns about safety, security, non-proliferation and waste management.

15. New Zealand's view is that Option B provides greater clarity than the status quo in decision 17/CP.7, as confirmed by decision 3/CMP.1.

Proposed legal text: CMP Decision: Nuclear Facilities in the CDM

Decides that activities relating to nuclear facilities shall not be eligible as clean development mechanism project activities in the second and subsequent commitment periods;

I.D. Introduce sectoral crediting of emission reductions below a previously established [no-lose] target

Description

16. New Zealand supports further consideration of the concept contained in Option B (paragraphs 12-21) to establish a mechanism for sectoral crediting of emission reductions below a previously established no-lose target.

17. New Zealand considers that this concept should be advanced primarily in the context of market approaches for the implementation of nationally appropriate mitigation actions (NAMAs) under AWG-LCA, with consequential amendments to the Kyoto Protocol advanced under the AWG-KP. New Zealand proposes new market mechanism for NAMAs in developing countries (with a separate market mechanism for REDD), established under the Copenhagen agreement. The potential complexities involved in linking the two agreements under this approach highlight the possible advantages of having a single agreement as the outcome of negotiations under the AWG-KP and AWG-LCA.

18. An amendment to the Kyoto Protocol would be required to enable emission reductions from such a new "NAMA trading" mechanism to be applied by Parties

with commitments under Article 3.1. Amendment text is proposed below. New Zealand will elaborate further on the structure of a new NAMA trading mechanism, and how it fits within the broader framework of emissions trading and other climate change actions, in a supplementary submission to be provided shortly.

19. New Zealand will similarly elaborate in a separate submission on the structure for a new REDD mechanism under the AWG-LCA. Note that a similar amendment to the Kyoto Protocol, or the same amendment, could also be applied in the case of a new REDD mechanism.

Proposed legal text: Amendment to the Kyoto Protocol: New NAMA trading mechanism [and REDD mechanism]

Article 3, new paragraph 12bis

12bis. Any emission reductions or removals which a Party acquires from another Party in accordance with the provisions of [Articles X[9] [and Y][10] to the Copenhagen agreement] shall be added to the assigned amount for the acquiring Party.

I.E. Introduce crediting on the basis of nationally appropriate mitigation actions

Description

20. New Zealand considers that this proposal can be subsumed within the scope of a new NAMA trading mechanism, as discussed under section I.D above. New Zealand is preparing a separate submission on this issue.

I.F. Encourage the development of standardized, multi-project baselines

Description

21. New Zealand supports the development and use of standardized, multi-project (SMP) baselines in the CDM on a voluntary basis. Methodological guidance for SMP baselines, and potentially actual SMP baselines themselves, could be developed by one or more dedicated bodies established by the CDM Executive Board and operating under its authority. However, project developers (and other interested parties) should remain able to submit methodologies for SMP baselines, and to submit baselines using SMP methodologies approved by the CDM executive board. The CMP should not define further quantified performance standards (i.e. top [X] percentile of performance) to apply to SMP baselines across all project types because of differences in sectoral technologies and national circumstances.

Rationale

[9] Article X of the Copenhagen agreement would define the new NAMA trading mechanism as described in New Zealand's forthcoming submission on this topic.
[10] Article Y of the Copenhagen agreement would define the new REDD mechanism as described in New Zealand's forthcoming submission on this topic.

22. SMP baselines are already enabled under the CDM. They offer the potential to improve consistency and transparency in the assessment and crediting of CDM projects, and to lower project transaction costs. The provision of top-down methodological guidance for SMP baselines, and the development of actual SMP baselines, by bodies under the CDM Executive Board could help to facilitate the use of SMP baselines.

23. New Zealand has strong concerns that some of the options being considered would have perverse outcomes. For example:

    a. If the development of SMP baselines becomes a mandatory prerequisite for project validation and registration, then this could significantly slow the project pipeline. Countries potentially would have to wait in line for SMP baselines to be developed for their national circumstances, and this could take a long time.

    b. The development of SMP baselines would be very complex exercises involving extensive data collection and analysis on a country-by-country basis. It may not be realistic, or a good use of resources, to require all SMP baselines to be developed by, or under the auspices of, the CDM Executive Board.

    c. While SMP baselines should be used wherever possible, flexibility should be maintained to accommodate CDM projects that do not fit within the model used to develop SMP baselines so that CDM activities are not unnecessarily restricted.

    d. It is not practical to have the Parties agree on quantified performance standards (e.g. top [X] percentile) for SMP baselines that would apply across all project types, technologies and national circumstances. For example, projects in the LULUCF sector would require different considerations relative to projects in the industrial or energy sectors. The availability of data and the ability to apply valid statistical distribution tests for project performance could vary significantly between and within countries and sectors, and be particularly problematic for small countries.

Proposed legal text: CMP Decision: Standardized, Multi-Project Baselines

Requests that the Executive Board of the clean development mechanism, including any bodies operating under its authority, provide guidance on methodologies for standardized, multi-project baselines and, where appropriate, develop standardized, multi-project baselines for application in clean development mechanism projects;

Encourages clean development mechanism project participants to apply the Executive Board's guidelines for standardized, multi-project baselines where appropriate in developing new baseline methodologies to be approved by the Executive Board;

Encourages clean development mechanism project participants to apply standardized, multi-project baselines, including those developed by the Executive Board, where appropriate;

I.G. Ensure environmental integrity and assess additionality through the development of positive or negative lists of project activity types

Description

24. New Zealand supports Option A (paragraph 37), the status quo. In our view, it is not practical or politically feasible for the Parties to agree on either a positive or negative list of project activity types that could be applied successfully across all Parties, given the variation in national circumstances.

I.H. Differentiate the eligibility of Parties through the use of indicators

Description

25. New Zealand considers that the CDM should become a mechanism of diminishing significance for major emitting economies as they transition towards nationally appropriate mitigation actions. New Zealand is open to considering Option B (paragraph 40) to introduce indicators for non-Annex I Parties, but does not yet have a fully developed position on this issue.

I.I. Improve access to clean development mechanism project activities by specified host Parties

26. New Zealand is open to considering Option B (paragraph 43) to provide new definitions and modalities for small-scale projects and financial assistance for project validation, verification and certification, but does not have a fully developed position on this issue. The specific options need to be more clearly defined so their implications can be assessed.

I.J. Promote co-benefits for clean development mechanism projects by facilitative means

Description

27. New Zealand supports Option A (paragraph 44), the status quo, which is to not require validation and verification of co-benefits for CDM projects.

Rationale

28. Decision 3/CMP.1 already requires designated operational entities to receive and review documentation of the environmental impacts of a CDM project activity, a summary of comments by local stakeholders, and confirmation by the host Party that the project activity assists it in achieving sustainable development.

29. Every CDM project can be expected to deliver co-benefits, and host and buyer Parties can express their own preferences in the marketplace for how to report, value and prioritise those co-benefits. Requiring validation and verification of CDM project co-benefits by designated operational entities would require the challenging negotiation of standardised criteria for evaluating and weighting co-benefits, and would significantly increase project transaction costs without any further benefit to the atmosphere.

30. New Zealand strongly opposes the proposal to exempt CDM projects from additionality criteria on the basis of their co-benefits. This could threaten the environmental integrity of the Kyoto Protocol.

I.K. Introduce multiplication factors to increase or decrease the certified emission reductions issued for specific project activity types

Description

31. New Zealand supports Option A (paragraph 47), the status quo, which does not provide for multiplication factors.

Rationale

32. It is our strong view that units issued for CDM projects should represent real, measurable, verifiable reductions of emissions and enhancements of removals. It is not appropriate to apply multiplication factors or discount factors that would distort the technical accounting of emissions and removals from CDM projects.

33. New Zealand strongly opposes Option 1 of Option B (paragraph 48) which would enable the application of a multiplication factor of greater than one to CERs. This implies crediting some projects with more units than actually accrue to the atmosphere in return for crediting other project with fewer such units. This is not feasible to administer and threatens the environmental integrity of the Kyoto Protocol.

34. It is not technically appropriate or politically feasible for the CMP to decide on multiplication factors or discount factors to apply to CDM projects.

II. Joint Implementation

II.A. Introduce modalities for treatment of clean development mechanism project activities upon graduation of host Parties

Description

35. New Zealand supports the introduction of modalities for the treatment of CDM projects in the event the non-Annex I host Party assumes a quantified target or commitment for one or more sectors covered by the project that is not compatible with continuing to host CDM projects.

36. It is our view that in this circumstance, CDM projects should continue to operate through the end of their current crediting period, and the host Party should adjust its accounting of progress against its target or commitment, particularly where target or commitment-based emissions trading is involved, to avoid double-counting. At the end of the current crediting period, the host Party can then decide whether to discontinue the projects or, if appropriate and subject to the agreement of the project participants, devolve inventory-based units to the projects or initiate the projects as new projects under a more appropriate mechanism following the standard modalities and procedures.

Rationale

37. The Kyoto Protocol does not provide for the circumstance where a non-Annex I Party hosting one or more CDM projects assumes a quantified target or commitment for one or more sectors that is not compatible with continuing to host CDM projects in those sectors. Since the modalities and procedures for CDM projects were designed in the context of non-Annex I host Parties without such targets or commitments, it is not appropriate for the CDM modalities and procedures to continue to apply indefinitely if the host Party changes its status.

38. However, project developers and investors have entered into contracts for CDM projects with the assurance that they are eligible to receive certified emission reductions throughout the crediting period applied to the projects. An appropriate balance needs to be struck between fair treatment of CDM project developers and investors, and appropriate accounting for emissions and removals in the context of a new quantified target or commitment.

39. We recommend that CDM projects should remain eligible to receive CERs, tCERs or lCERs throughout the crediting period that is current at the time of host Party's change in status. At the end of the current crediting period, the host Party can then decide how to proceed with the projects (i.e. discontinuing the projects or, as appropriate and subject to the agreement of the project participants, devolving inventory-based units to the projects or registering the projects under a more appropriate mechanism). This is preferable to automatically transitioning CDM projects into the JI mechanism, which could be a very complex transaction that is not desired by all host Parties or by project participants, and may not be appropriate for some Parties.

40. To preserve environmental integrity, it will be critical to avoid double-counting of emission reductions and removals credited under CDM projects and under the quantified target or commitment of the host Party. The appropriate modalities for CDM projects in this circumstance will need to vary according to whether the

projects involve afforestation and reforestation activities, or emission reduction activities in other sectors.

41. In the case of CDM projects outside of the LULUCF sector, it would be appropriate to cancel a number of units equal to the CERs issued from the time of the host Party's quantified target or commitment until the end of the current crediting period. The Parties would need to decide which types of units would be eligible for this purpose.

42. In the case of removal activities from afforestation and reforestation CDM projects, the appropriate treatment would depend on whether the project involved the issuance of tCERs or lCERs, or whether the host Party had underwritten the units generated by the project to resolve concerns regarding non-permanence and the project involved the issuance of CERs (as proposed by New Zealand in its February 2009 and April 2009 submissions on LULUCF under the AWG-KP).

    a. If the project involved the issuance of tCERs and lCERs, those units would be replaced automatically through the cancellation of other units by the Annex I Party retiring those units as provided in the annex to decision 5/CMP.1. Therefore, it would not be necessary for the host Party to cancel a corresponding number of units (such as RMUs, if applicable) in order to avoid double-counting with removals reported under the inventory; the cancelled tCERs and lCERs would already be replaced with other units by the Annex I Party retiring those units [11]

    b. If the project involved the issuance of CERs because the host Party has assumed liability for non-permanence, then it would be appropriate for the host Party to cancel a number of units (such as RMUs, if applicable) equal to the CERs issued from the time of the host Party's quantified target or commitment until the end of the current crediting period. The Parties would need to decide which types of units would be eligible for this purpose.

[11] Note that it may be necessary to apply a solution to ensure that a Party is not liable under its quantified target or commitment for the reversal of previous removals for which tCERs and lCERs have been cancelled. An example of how to solve this is New Zealand's amended afforestation/reforestation debit-credit rule for Article 3.3 activities (refer to New Zealand's submissions of February and April 2009).

Proposed legal text: CMP Decision: Modalities for CDM Projects under Quantified Targets or Commitments by the Host Party

Decides that where a non-Annex I Party hosting one or more registered clean development mechanism projects assumes a quantified target or commitment for one or more sectors in which those projects are undertaken,

a. Each project shall continue to be subject to the rules and modalities governing the clean development mechanism until the end of that project's current crediting period, at which point that project's activities will no longer be eligible as a clean development mechanism project;

b. In the case of a clean development mechanism project involving the issuance of certified emission reductions for reductions in emissions by sources, the project's host Party shall transfer to its cancellation account a quantity of [units][12] equal to the certified emission reductions issued from the time of the host Party's quantified target or commitment until the end of that project's current crediting period;

c. In the case of a clean development mechanism project involving the issuance of certified emission reductions (but not temporary certified emission reductions or long-term certified emission reductions) for enhancements of removals by sinks, the host Party shall transfer to its cancellation account a quantity of [units][13] equal to the certified emission reductions issued from the time of the host Party's quantified target or commitment until the end of that project's current crediting period;[14]

II.B. Include nuclear activities

Description

43. New Zealand supports Option B (paragraph 54) which provides that activities relating to nuclear facilities are not eligible as JI project activities.

Rationale

44. New Zealand does not consider that nuclear activities are appropriate under JI. We do not consider that nuclear power is a sustainable energy source. We have long-standing concerns about safety, security, non-proliferation and waste management. New Zealand's view is that Option B provides greater clarity than the status quo in decision 16/CP.7, as confirmed by decision 9/CMP.1.

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[12] The Parties would need to decide which units would be eligible for this purpose.
[13] The Parties would need to decide which units would be eligible for this purpose.
[14] Reflecting the discussion above, this presumes a change to the non-permanence modalities for afforestation and reforestation projects under the CDM as proposed by New Zealand in its submission to the AWG-KP on LULUCF.

Proposed legal text: CMP Decision: Nuclear Facilities in JI

Decides that activities relating to nuclear facilities shall not be eligible as joint implementation project activities in the second and subsequent commitment periods;

II.C. Promote co-benefits for joint implementation projects under track 2 by facilitative means

Description

45. New Zealand supports Option A (paragraph 56), the status quo, which is to not require further determination of co-benefits for JI projects under track 2.

Rationale

46. Every JI project can be expected to deliver co-benefits, and host and buyer Parties can express their own preferences in the marketplace for how to report, value and prioritise those co-benefits. Requiring accredited independent entities to determine project co-benefits would require the challenging negotiation of standardised criteria for evaluating and weighting co-benefits, and would significantly increase project transaction costs without any further benefit to the atmosphere.

III. Emissions trading

III.A. Introduce emissions trading based on sectoral targets

Description

47. Refer to New Zealand's response to section I.D above, and New Zealand's separate submission with its proposal for a new market mechanism in relation to NAMAs implemented by non-Annex I Parties.

III.B. Introduce emissions trading on the basis of nationally appropriate mitigation actions.

Description

48. Refer to New Zealand's response to section I.D above, and New Zealand's separate submission with its proposal for a new market mechanism in relation to NAMAs implemented by non-Annex I Parties.

49. New Zealand does not support the option in paragraph 67 implying new modalities for the issuance of emission reduction units (ERUs) for NAMAs in an Annex I Party. The existing JI and international emissions trading mechanisms already provide sufficient means for Annex I Parties to channel carbon market support for the implementation of domestic NAMAs.

III.C. Introduce modalities and procedures for the recognition of units from voluntary emissions trading systems in non-Annex I parties for trading and compliance purposes under the Kyoto Protocol.

Description

50. Refer to New Zealand's response to proposal I.D above, and New Zealand's separate submission with its proposal for a new market mechanism in relation to NAMAs implemented by non-Annex I Parties.

51. New Zealand strongly believes that any emission units (or emission allowances) accepted for compliance with commitments under Article 3.1 of the Kyoto Protocol should be issued in accordance with the definitions, modalities and procedures agreed by the Parties to the Protocol for that purpose.

IV. Cross-Cutting Issues

IV.A. Relax or eliminate carry-over (banking) restrictions on Kyoto units

Description

52. New Zealand supports Option B (paragraph 72) to place no restrictions on the carry-over of Kyoto units to a subsequent commitment period.

Rationale

53. New Zealand supports consistent carry-over rules for AAUs, CERs, ERUs and RMUs from one commitment period to the next. This would improve the fungibility between unit types and improve the functioning and efficiency of the carbon market.

Proposed legal text: CMP Decision: Carry-Over of Kyoto Units

Modified paragraph 15 and 16 and new paragraph 16bis of the annex to decision 13/CMP.1

15. <u>For the first commitment period,</u> after expiration of the additional period for fulfilling commitments and where the final compilation and accounting report referred to in paragraph [62] below indicates that the quantity of ERUs, CERs, AAU and/or RMUs retired by the Party in accordance with paragraph [13] above is at least equivalent to its anthropogenic carbon dioxide equivalent emissions of the greenhouse gases, and from the sources, listed in Annex A to the Kyoto Protocol for that commitment period, the Party may carry over to the subsequent commitment period:

(a) Any ERUs held in its national registry, which have not been converted from RMUs and have not been retired for that commitment period or cancelled, up to a maximum of 2.5 per cent of the assigned amount pursuant to Article 3, paragraphs 7 and 8, of that Party

(b) Any CERs held in its national registry, which have not been retired for that commitment period or cancelled, to a maximum of 2.5 per cent of the assigned amount pursuant to Article 3, paragraphs 7 and 8, of that Party

(c) Any AAUs held in its national registry, which have not been retired for that commitment period or cancelled.

16. For the first commitment period, RMUs may not be carried over to the ~~subsequent~~ second commitment period.

16bis. For the second and subsequent commitment periods, after expiration of the additional period for fulfilling commitments and where the final compilation and accounting report referred to in paragraph [62] below indicates that the quantity of ERUs, CERs, AAU and/or RMUs retired by the Party in accordance with paragraph [13] above is at least equivalent to its anthropogenic carbon dioxide equivalent emissions of the greenhouse gases, and from the sources, listed in Annex A to the Kyoto Protocol for that commitment period, the Party may carry over to the subsequent commitment period:

(a) Any ERUs held in its national registry, which have not been converted from RMUs and have not been retired for that commitment period or cancelled~~, up to a maximum of 2.5 per cent of the assigned amount pursuant to Article 3, paragraphs 7 and 8, of that Party~~

(b) Any CERs held in its national registry, which have not been retired for that commitment period or cancelled~~, to a maximum of 2.5 per cent of the assigned amount pursuant to Article 3, paragraphs 7 and 8, of that Party~~

(c) Any AAUs or RMUs held in its national registry, which have not been retired for that commitment period or cancelled.

IV.B. Introduce borrowing of assigned amount from future commitment periods

Description

54. New Zealand does not support unlimited borrowing of assigned amount from future commitment periods because of concerns about the associated environmental and carbon market impacts.

IV.C. Extend the share of proceeds

Description

55. New Zealand considers that financing for adaptation, as a cross-cutting issue, is best dealt with in the AWG-LCA.

Rationale

56. New Zealand supports the scaling up of adaptation funding for the most vulnerable countries based on identified needs. This will require identification of adaptation needs, funding assistance required, and the most effective models for distribution. Parties should first focus discussion on what needs to be accomplished through adaptation funding, rather than beginning with mechanisms for collecting funds. (We acknowledge that some Parties have made good progress in this regard through the development of National Adaptation Plans of Action.) Parties should consider the need, identified in the Bali Action Plan, for financing to be adequate, predictable and sustainable, and for it not to have perverse outcomes for markets. It is important to analyse all options together in order to decide on which option or mix of options will be most effective and efficient in meeting adaptation needs.

57. With this in mind, New Zealand considers that financing for adaptation, as a cross-cutting issue, is best dealt with in the AWG-LCA. This will help to ensure that the Bali Road Map delivers efficient and effective outcomes in a consistent and coherent manner, and that issues of equity and fairness between all Parties are appropriately considered.

58. New Zealand notes that the CDM adaptation levy was introduced to help provide a more equitable solution for CDM-eligible countries with low CDM uptake. The proposal to raise funds for adaptation by applying a levy to AAUs and RMUs is of a different nature and context. New Zealand questions whether responsibility for adaptation funding should be distributed according to target burden sharing criteria for a commitment period. A country's responsibility for adaptation may not be readily assessed by reference to its mitigation potential and other effort-sharing criteria.

59. Scaling up financing for adaptation should avoid generating perverse environmental outcomes.

Annex II

III. Emissions trading

III.C. Reduce the commitment period reserve

Description

60. New Zealand supports reconsidering the design of the commitment period reserve (CPR) for the second commitment period in the context of the Copenhagen agreement. If the CPR remains relevant, then New Zealand recommends reducing the CPR to lower its impact on market liquidity while still maintaining environmental integrity. New Zealand also recommends correcting a flaw in the CPR design that could perversely impact on Parties whose emissions are below their QELRC.

Rationale

61. The CPR was intended to prevent Annex B Parties from "overselling" units, which could increase the risk of non-compliance with their Article 3 commitments and potentially compromise the environmental integrity of the Kyoto Protocol. The current form of the CPR was designed in the context of negotiations for the first commitment period. While the CPR serves an important function, the current design of the CPR has two shortcomings:[15]

    a. First, the current design of the CPR has the potential to constrain the efficient operation of carbon markets in the case where an Annex B Party chooses to devolve Article 17 emissions trading activities to legal entities. In the current design of the CPR, there is no practical way to distinguish between Parties that deliberately "oversell" units with a loss of environmental integrity, and Parties that temporarily trigger the CPR because of the relative timing of unit inflows and outflows under a fluid emissions trading regime.

    b. Second, the current design of the CPR could perversely require an Annex B Party calculating its CPR on the basis of its most recently reviewed inventory to maintain a reserve greater than its likely emissions. This could occur if this Party's emissions increased during the course of a commitment period.

62. As the Parties move toward an agreement for the second commitment period, then Parties should re-consider the need for, and if appropriate the effective design of, the commitment period reserve. If the current rationale for the CPR remains valid after the first commitment period, then New Zealand proposes to reduce the CPR and to correct the design flaw identified above.

63. We also note that if non-Annex I Parties enter into emissions trading on the basis of NAMAs, then it may be appropriate to consider whether a CPR should apply.

[15] For a more detailed explanation, refer to New Zealand's previous submission on this issue contained in FCCC/KP/AWG/2009/MISC.3.

Proposed legal text: CMP Decision: Commitment Period Reserve

Modified paragraph 6 of the annex to decision 11/CMP.1, and new paragraph 6bis

6. In the first commitment period, each Party included in Annex I shall maintain, in its national registry, a commitment period reserve which should not drop below 90 per cent of the Party's assigned amount calculated pursuant to Article 3, paragraphs 7 and 8, of the Kyoto Protocol, or 100 percent of five times its most recently reviewed inventory, whichever is lowest.

6bis. In the second and subsequent commitment periods, each Party included in Annex I shall maintain, in its national registry, a commitment period reserve which should not drop below the lower of either:

a. [X] per cent of the Party's assigned amount calculated pursuant to Article 3, paragraphs 7 and 8, of the Kyoto Protocol [where X is a value less than 90 per cent to be agreed by the Parties in the context of quantified emission reduction or limitation commitments, operation of emissions trading and the project-based mechanisms, and compliance procedures and mechanisms after the first commitment period], or

b. The sum of the reviewed inventories reported thus far in that commitment period, plus the most recently reviewed inventory multiplied by the number of years remaining in that commitment period.