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Draft Recommendation

Requirements for the development and assessment of mechanism methodologies

Version 01.0



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1. Procedural background

1. Decision 3/CMA.3, paragraph 6 (d),¹ requests the Supervisory Body to elaborate and further develop recommendations, for consideration and adoption by the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement (CMA) at its fourth session (November 2022), on the application of the requirements referred to in chapter V.B of the Rules, modalities and procedures for the mechanism established by Article 6, paragraph 4, of the Paris Agreement (RMP) to that decision (titled 'Methodologies'). The relevant paragraphs are as follows:

33. Mechanism methodologies shall encourage ambition over time; encourage broad participation; be real, transparent, conservative, credible, below 'business as usual'; avoid leakage, where applicable; recognize suppressed demand; align to the long-term temperature goal of the Paris Agreement, contribute to the equitable sharing of mitigation benefits between the participating Parties; and, in respect of each participating Party, contribute to reducing emission levels in the host Party, and align with its NDC, if applicable, its long-term low GHG emission development strategy if it has submitted one and the long-term goals of the Paris Agreement.

34. Mechanism methodologies shall include relevant assumptions, parameters, data sources and key factors and take into account uncertainty, leakage, policies and measures, and relevant circumstances, including national, regional or local, social, economic, environmental and technological circumstances, and address reversals, where applicable.

35. Mechanism methodologies may be developed by activity participants, host Parties, stakeholders or the Supervisory Body. Mechanism methodologies shall be approved by the Supervisory Body where they meet the requirements of these rules, modalities and procedures and the requirements established by the Supervisory Body.

36. Each mechanism methodology shall require the application of one of the approach(es) below to setting the baseline, while taking into account any guidance by the Supervisory Body, and with justification for the appropriateness of the choices, including information on how the proposed baseline approach is consistent with paragraphs 33 and 35 above and recognizing that a host Party may determine a more ambitious level at its discretion:

(a) A performance-based approach, taking into account:

(i) Best available technologies that represent an economically feasible and environmentally sound course of action, where appropriate;

(ii) An ambitious benchmark approach where the baseline is set at least at the average emission level of the best performing comparable activities providing similar outputs and services in a defined scope in similar social, economic, environmental and technological circumstances;

¹ See decision 3/CMA.3 contained in document FCCC/PA/CMA/2021/10/Add.1 available at: <https://unfccc.int/documents/460950>. The annex to the decision begins on page 29 (English language version).

(iii) An approach based on existing actual or historical emissions, adjusted downwards to ensure alignment with paragraph 33 above.

37. Standardized baselines may be developed by the Supervisory Body at the request of the host Party or may be developed by the host Party and approved by the Supervisory Body. Standardized baselines shall be established at the highest possible level of aggregation in the relevant sector of the host Party and be consistent with paragraph 33 above.

38. Each mechanism methodology shall specify the approach to demonstrating the additionality of the activity. Additionality shall be demonstrated using a robust assessment that shows the activity would not have occurred in the absence of the incentives from the mechanism, taking into account all relevant national policies, including legislation, and representing mitigation that exceeds any mitigation that is required by law or regulation, and taking a conservative approach that avoids locking in levels of emissions, technologies or carbon-intensive practices incompatible with paragraph 33 above.

39. The Supervisory Body may apply simplified approaches for demonstration of additionality for any least developed country or small island developing State at the request of that Party, in accordance with requirements developed by the Supervisory Body.

2. The Supervisory Body, at its first meeting, considered the concept note “Guidelines for the implementation of methodological principles, approaches and methods for the establishment of baseline and additionality”, and discussed how the principles included in chapter V.B of the RMP can be further elaborated as guidance for the development of methodologies for the mechanism.
3. The Supervisory Body agreed that an informal working group on methodologies comprising its members and alternate members as well as secretariat staff would work prior to the second meeting of the Supervisory Body to prepare draft recommendations to the CMA, taking into account the inputs provided at this meeting for consideration by the Supervisory Body at its second meeting, with a view to forwarding the recommendations to CMA 4. The Supervisory Body noted that there are capacity-building needs for host Parties to participate in the mechanism, including those relating to methodologies, to deliver higher ambition of the Parties.
4. The draft requirements below under section 3 are work in progress.

2. Definitions

5. For the purposes of defining the requirements in this document, the following definitions apply:
 - (a) **Baseline contraction factor (BCF_S):** value between 1 and 0 decreasing with time used to cap baselines for activities undertaken in a sector *S* to ensure ambition over time;
 - (b) **Baseline contraction factor curve:** the variation of the baseline contraction factor with time for a sector;

- (c) **Baseline emissions benchmark at year 1, in a sector S (BE_{1s}):** baseline emission or emission intensity determined through benchmark for a sector S at year 1 of its baseline contraction factor curve;
- (d) **Leakage:** net change of anthropogenic emissions by sources of GHGs which occurs outside the project boundary, and which is measurable and attributable to the Article 6.4 project activity. It includes activity-shifting leakage and market leakage;
- (e) **Suppressed demand:** a scenario where future anthropogenic emissions by sources of GHGs are projected to rise above current levels, due to the specific circumstances of the host Party.

3. Elaboration of the requirements in paragraphs 33 to 39 of the RMP

3.1. Encouraging ambition over time

3.1.1. Option 1: Setting a cap on baseline emissions

- 6. Mechanism methodologies shall encourage ambition over time through requirements related to baseline setting that enable GHG emission reductions only from activities that contribute to the achievement of the long-term temperature goals of the Paris Agreement.
- 7. For that purpose, the baseline of an activity in a sector S during year Y shall be capped with the product $BCF_s \times BE_{1s}$.

3.1.1.1. Options on the determination of BCF_s

- 8. Option A1: Host Parties shall, before the authorization of a 6.4 activity in a sector, **notify** the Supervisory Body of the baseline contraction factor curve it has developed for that sector. Host Parties shall provide justifications on how this baseline contraction factor curve is aligned with their NDC and LT LEDS and the long-term temperature goals of the Paris Agreement.
- 9. Option A2: Host Parties shall, before the authorization of a 6.4 activity in a sector, submit to the Supervisory Body for its **assessment**, the baseline contraction factor curve it has developed for that sector. Host Parties shall provide justifications on how this baseline contraction factor curve is aligned with their NDC and LT LEDS and the long-term temperature goals of the Paris Agreement.
- 10. Option A3: New **Methodologies shall include an approach** for the determination of the baseline contraction factor. The Supervisory Body shall revise the CDM methodologies, to include an approach for the determination of baseline contraction factor and to add a requirement to cap the baseline with $BCF_s \times BE_{1s}$.
- 11. Option A4: The **Supervisory Body shall develop an approach** for the determination of the baseline contraction factor to be used in conjunction with all mechanism methodologies. Host Parties shall, before the authorization of a 6.4 activity in a sector, use the approach to determine the baseline contraction factor curve for that sector.

- (f) Option A4a: Host Parties shall, before the authorization of a 6.4 activity in a sector, **notify** the Supervisory Body of the baseline contraction factor curve it has developed for that sector;
- (g) Option A4b: Host Parties shall, before the authorization of a 6.4 activity in a sector, **submit** to the Supervisory Body for its assessment, the baseline contraction factor curve it has developed for that sector.

3.1.1.2. Options on the determination of BE1_s

- 12. Option B1: Host Parties shall, before the authorization of a 6.4 activity in a sector S, **notify** the Supervisory Body of the BE1_s it has developed in that sector. Host Parties shall provide justifications on how BE1_s is aligned with their NDC and LT LEDS and the long-term temperature goals of the Paris Agreement.
- 13. Option B2: Host Parties shall, before the authorization of a 6.4 activity in a sector, **submit** to the Supervisory Body for its assessment the BE1_s it has developed in that sector. Host Parties shall provide justifications on how this baseline contraction factor curve is aligned with their NDC and LT LEDS and the long-term temperature goals of the Paris Agreement.
- 14. Option B3: **New Methodologies shall include an approach** for the determination of BE1_s. The Supervisory Body shall revise the CDM methodologies, to include an approach for the determination of BE1_s and to add a requirement to cap the baseline with BCF_s x BE1_s.
- 15. Option B4: The **Supervisory Body shall develop an approach** for the determination of BE1_s to be used in conjunction with all mechanism methodologies. Host Parties shall, before the authorization of a 6.4 activity in a sector, use the approach to determine BE1_s for that sector.
 - (a) Option B4a: Host Parties shall, before the authorization of a 6.4 activity in a sector S, **notify** the Supervisory Body of BE1_s it has developed in that sector;
 - (b) Option B4b: Host Parties shall, before the authorization of a 6.4 activity in a sector, **submit** to the Supervisory Body for its assessment the BE1_s it has developed in that sector.
- 16. Where the host Party develop the baseline contraction factor curve and BE1_s, the Supervisory Body shall revise the CDM methodology to add a requirement to cap the baseline with BCF_s x BE1_s.

3.1.2. Option 2: Facilitating transformative mitigation activities

- 17. Mechanism methodologies shall facilitate transformative mitigation activities by promoting:
 - (a) Deep decarbonization of the economic system, going beyond the low-hanging fruit pathways;
 - (b) Future thinking that address the long-term needs;
 - (c) Expanded space for mitigation actions beyond incremental improvements of industrial processes;

- (d) Enhanced sustainability through encouraging the host country to authorize coherent mitigation actions aligned with its NDC and LT-LEDS;
- (e) Scale through activities that can be scaled up and replicated.

3.1.3. Option 3: Use the following elements in mechanism methodologies:

18. Mechanism methodologies shall consider the following options for applicability conditions, baseline setting, additionality demonstration and monitoring:
- (a) When using a programmatic approach, progressively including more efficient and less greenhouse gas-intensive project technologies/measures in the distribution plan taking into account experience gained in host countries;
 - (b) Installation of more equipment/measures using the same technology over a period (i.e. wider geographic coverage or greater penetration among the potential end users) demonstrated using empirical data;
 - (c) Additional coverage of sectors over a period demonstrated using empirical data;
 - (d) Increasing the stringency of baselines during each renewal of the crediting period considering experience under the CDM and other mechanisms (e.g. requiring a more conservative grid emission factor over time);
 - (e) By incentivizing new low-emission technologies with very low penetration rates (e.g. <10% penetration rate) by designating them as 'first-of-its-kind' or 'automatically additional' and excluding technologies with high penetration rates (e.g. >50% penetration rate) by designating them as 'common practice' or 'business-as-usual';
 - (f) By making additional investments in adopting digital technologies, particularly for monitoring (e.g. Internet of Things technologies, blockchain technologies), thereby increasing the reliability of the estimates and reducing uncertainties.

3.2. Encouraging broad participation

19. Mechanism methodologies shall encourage broad participation by:
- (a) Being applicable in combinations for broad sectoral and technology coverage, while being able to address specific circumstances;
 - (b) Ensuring that all its requirements are relevant, address environmental integrity issues or enhance the transparency of any claimed GHG mitigation impact and cannot be replaced by alternative requirements that achieve the same purpose at lower cost;
 - (c) Ensuring that there are wider benefits from the activity;
 - (d) Simplifying for its users the requirements for baseline setting, additionality demonstration and monitoring;
 - (e) By requiring mitigation activities developers to conduct inclusive stakeholder consultations addressing how the mitigation activities respect, promote and consider human rights, the right to health, the rights of indigenous peoples, local

communities, migrants, children, persons with disabilities and people in vulnerable situations and the right to development as well as gender equality, empowerment of women and intergenerational equity. This consultation should also aim at enhancing the understanding of the mitigation activity's benefits and risk for these stakeholders as well as encouraging their participation in the mechanism.

3.3. Shall be real, transparent, conservative, credible and below business-as-usual (BAU)

20. The application of mechanism methodologies shall result in real outcomes with the entire emission reductions arising from the technology/measure employed or implemented, and not from any other co-factor such as the reduction of level of activity.
21. Mechanism methodologies shall require describing transparently the source of the data used, the assumptions made, the references used and the underlying steps of emission reduction estimates, where necessary including equations.
22. The application of mechanism methodologies shall result in conservative outcomes with the measures applied or the options chosen (e.g. due to the paucity of data, assumptions applied or multiple alternatives available) not overestimating the emission reductions and the error being on the conservative side. The mechanism methodologies shall require the description of the uncertainty associated with data parameters of interest and provide methods to quantify, manage and account for the impact of uncertainty.
23. The application of mechanism methodologies shall result in credible outcomes. The methodology shall require the GHG mitigation activity to have a robust monitoring and data capture system as well as a reporting system. Where secondary data is used, the mechanism methodology shall require that the activity developer demonstrate that it is from an authoritative source.
24. The application of mechanism methodologies shall result in below business-as-usual outcomes for the GHG mitigation activity. For that purpose, the mechanism methodology shall require the identification of the business as usual scenario and provide an approach for the calculation and require the calculation of the business-as-usual emissions, where necessary referring to the host Party inventory reports and any other transparency reports under the Paris Agreement.

3.4. Avoid leakage where applicable

25. Mechanism methodologies shall require:
 - (a) The identification of the sources of leakage including, but not limited to, used equipment transferred outside the project boundary, land-use by the project leading to the displacement of agriculture activities and deforestation, diversion of the biomass residues from other possible applications as mitigation activities outside of the project boundary;
 - (b) Where leakage is identified, the demonstration of how it is addressed, referring where available to the guidance from the designated national authorities;
 - (c) Positive leakage (decreasing emissions) shall not be accounted.
26. Mechanism methodologies shall provide approach to monitor any leakage at the country.

3.5. Recognizing suppressed demand

27. Mechanism methodologies shall address suppressed demand when a minimum service level to meet basic human needs, such as lighting, cooking, shelter and waste water treatment, is unavailable to the end user of the service prior to the implementation of the activity.
28. Host Parties that intends to authorize mitigation activities using mechanism methodologies addressing suppressed demand are encouraged to share a list of basic human needs that require a minimum service level.
29. Suppressed demand is addressed by considering that the baseline scenario is not the historical condition, but an alternative that provide the same level of service as the mitigation activity, where it is realistic or a minimum level of service where the baseline equipment cannot realistically provide the level of service of the mitigation activity.
30. The baseline is the most efficient technology/measure that meets the minimum service level and which is not facing any of the barriers below:
 - (a) Income barrier, i.e. inability to meet the capital cost;
 - (b) Lack of infrastructure (e.g. non-existence of supply/service infrastructure);
 - (c) Lack of skills to operate the alternative;
 - (d) Technological barrier, e.g. technologies with low market share with market penetration rates below a threshold.
31. The minimum service level should be realistic and reasonable. For establishing a minimum service level, the following approaches may be used:
 - (a) National/international peer-reviewed research or relevant studies (e.g. the World Health Organization recommendations on per capita safe drinking water);
 - (b) Benchmarks that take into account that emissions will rise to achieve the international/national development goals.

3.6. Contributing to the equitable share of mitigation benefits between participating Parties

32. Mechanism methodologies shall protect host Party to its ability to meet its NDC, and to reserve space to take on progressively greater ambition in further NDCs in line with any LT-LEDS.
33. All mechanism methodology shall provide an approach for the ex-ante calculation of GHG emission reductions to enable up-front payment of carbon credits and access to loan or low-cost finance.

3.7. Aligning with long-term temperature goals of the Paris Agreement and, with respect of each participating Party, contributing to reducing the emission levels in the host Party and aligning with its NDC (if applicable), its LT-LEDS (if it has submitted one) and the long-term goals of the Paris Agreement.

34. The host Party shall specify to the Supervisory Body:
- (a) A list of the types [(e.g. sectors [, including sub-sectors])] of mechanism activities, it would consider approving [from the list of sectoral scopes at appendix I];
 - (b) The approach it has used to establish that the activities will contribute to the achievement of its NDC, if applicable, to its long-term low greenhouse gas (GHG) emissions development strategy, if it has submitted one, [and to the long-term goals of the Paris Agreement];
 - (c) The list referred to in paragraph 34(a) above can be regularly updated by the host Party if the host Party intends to submit a mechanism activity in a sectoral scope not in the list in paragraph 34(a) by means of notifying to the Supervisory Body a revised list.
35. Mechanism methodologies shall require that the activity developer confirms that the activity they intend to implement belongs to the list referred to above.
36. Mechanism methodologies shall require that:
- (a) **Option 1:** The host Party, before the authorization of a 6.4 activity in a sector, **notify the Supervisory Body**, of the emission trajectory for that sector, with justifications on how that emission trajectory is aligned with the long-term temperature goals of the Paris Agreement, and how it will be used to assess the alignment of the baselines;
 - (b) **Option 2:** The host Party, before the authorization of a 6.4 activity in a sector, **submits to the Supervisory Body for its assessment**, an emission trajectory for that sector, with justifications on how that emission trajectory is aligned with the long-term temperature goals of the Paris Agreement, and how it will be used to assess the alignment of the baselines;
 - (c) **Option 3:** The baselines are aligned with a sector- and Party-specific emissions trajectory compatible with the long-term temperature goals of the Paris Agreement, **set by the Supervisory Body**;
 - (d) **Option 4:** The **SB provides an approach** applicable to all methodologies for the determination of the emission trajectories:
 - (i) **Option 4(a):** The host Party, before the authorization of a 6.4 activity in a sector, develops the emission trajectory for that sector and **notifies the Supervisory Body**, with justifications on how that emission trajectory is aligned with the approach provided by the Supervisory Body. In case a new methodology not addressed by the approach is developed by an activity participant, it shall submit to the Supervisory Body a revision to the approach;
 - (ii) **Option 4(b):** The host Party, before the authorization of a 6.4 activity in a sector, can either use the approach provided by the Supervisory Body to

develop the emission trajectory for that sector or follow an alternative approach and **submit it to the Supervisory Body for assessment.**

3.8. Mechanism methodologies shall include relevant assumptions, parameters, data sources and key factors and take into account uncertainty, leakage, policies and measures, and relevant circumstances, including national, regional or local, social, economic, environmental and technological circumstances, and address reversals, where applicable

37. Mechanism methodologies shall include relevant assumptions, parameters, data sources and key factors and take into account uncertainty, for the calculation of a conservative GHG emission reduction.
38. Mechanism methodologies shall address leakage emissions, and take into account policies and measures, and relevant circumstances, including national, regional or local, social, economic, environmental and technological circumstances in accordance with the requirements from section 3.4.
39. Mechanism methodologies addressing mitigation activities not involving removal shall address reversals, following the requirements in the tool to address reversal in the context of storage in geological formation².

3.9. Requirements on baselines

40. Each mechanism methodology shall require the application of one of the approach(es) below to setting the baseline, and with justification for the appropriateness of the choices, including information on how the proposed baseline approach is consistent with the requirements discussed under sections 3.1 to 3.8 above and recognizing that a host Party may determine a more ambitious level at its discretion:
- (a) A performance-based approach, taking into account:
 - (i) Best available technologies that represent an economically feasible and environmentally sound course of action, where appropriate;
 - (ii) An ambitious benchmark approach where the baseline is set at least at the average emission level of the best performing comparable activities providing similar outputs and services in a defined scope in similar social, economic, environmental and technological circumstances;
 - (iii) An approach based on existing actual or historical emissions, adjusted downwards to ensure alignment with the long-term temperature goals of the Paris Agreement.

² Reversal for mechanism methodologies involving removals that do not use storage in geological formation are addressed in the “Requirements for the development and assessment of methodologies involving removals”.

41. In case the activity **does not generate output**³, the approach based on existing actual or historical emissions cannot be used if the incentive of the mechanism is not the key driver for action e.g. there are other drivers such as new regulation that could have led to the mitigation activities.
42. For **activities generating outputs**, the above approaches for baselines are applicable to the output of the activity. The three approaches for baseline setting do not apply necessarily to the whole outputs of an activity generated during its entire lifetime. Each of them can be applied to identify the baseline for part of the output generated by an activity.
43. An approach based on existing actual or historical emissions cannot be used to determine the baseline for the generation of an amount of output, except under the conditions below:
- (a) The activity developers can substantiate that the scenario “not investing” is the baseline scenario, which means that they would not invest to generate that amount of output in the absence of incentive of the mechanism because the incentive is a key driver for the decision to invest or not; and
 - (b) They know precisely the conditions of generation of the outputs displaced as well as the related GHG emissions.
44. Addressing 43(a) requires that:
- (a) The most attractive course of action is “to not invest”; and
 - (b) Not investing is a realistic scenario because the financial incentive accounts for at least X% of the project revenues (economical attractiveness drives the investment and the incentive is enough high compared to the investment);
 - (c) If the implementers of the mitigation activity do not invest, a third party will not be able to invest, e.g. the project is not displacing more CO₂ intensive outputs in a market the scenario not investing provide the same level of output as the scenario of the mitigation activity (the project does not generate additional output as compared to the pre-project scenario: e.g. fuel switch or energy efficiency improvement without increase of output or methane destruction without energy generation) or produce less output or of lower quality but the incentive is the driver of the project activity (e.g. distribution of cook stoves).
45. Addressing the requirement under 43(b) includes:
- (a) In case the technology of existing equipment is displaced, the remaining lifetime of the equipment is known;
 - (b) Historical/actual data are available.
46. The downward adjustment of historical emissions is addressed in the context of the requirements in section 3.1.

³ Output is defined as a good or service, e.g. electricity generated, or cement produced. Example of activities that do not produce output include only flaring the methane from a landfill.

3.10. Additionality

47. Additionality shall be demonstrated using a robust assessment that shows the activity would not have occurred in the absence of the incentives from the mechanism, taking into account all relevant national policies, including legislation, and representing mitigation that exceeds any mitigation that is required by law or regulation, and taking a conservative approach that avoids locking in levels of emissions, technologies or carbon-intensive practices incompatible with the requirements discussed under sections 3.1 to 3.8 above.
48. This can be done by establishing that:
 - (a) Without the incentive from the mechanism, the activity would not be economically viable; and
 - (b) There is no national policy including legislation that prohibits the implementation of the more economically attractive alternatives to the activity; and
 - (c) The activity represents mitigation that exceeds any mitigation that is required by law or regulation; and
 - (d) The activity's carbon intensity and lifetime are aligned with an emission trajectory that contributes in achieving the climate goals, avoiding the activity to lead to locking in levels of emissions, technologies or carbon-intensive practices.
49. This can also be done by establishing that the activity is part of a global positive list of activities established by the supervisory body. The criteria for a positive list are:
 - (a) Activities should be zero emissions, or net negative emissions (or removals);
 - (b) Are not legally required;
 - (c) Are not financially attractive in any circumstances;
 - (d) It is possible to predetermine and specify these necessary conditions with a high degree of certainty.
50. Where it is established that the baseline emissions are equal or below the emissions of any activity that would have occurred in the absence of the incentives from the mechanism, taking into account all elements referred to under paragraph 48 above, an activity with emissions below the baseline is additional.

3.11. Standardised baselines

51. Standardized baselines may be developed by the Supervisory Body at the request of the host Party or may be developed by the host Party and approved by the Supervisory Body.
52. Standardized baselines shall be updated at frequent interval.
53. The Supervisory Body shall develop requirements for the coverage period and currentness of the data used to develop, revise and update standardized baselines and the requirements for the validity of approved standardized baselines and thus the frequency of update of standardized baselines.

54. Standardized baselines shall be established at the highest possible level of aggregation in the relevant sector of the host Party and be consistent with the requirements discussed under sections 3.1 to 3.8 above and the requirement in paragraph 55 below.
55. The level of aggregation shall be determined and proposed by the Host Party, taking into account the following:
 - (a) A default level of aggregation shall comprise the facilities producing the same type of output within the geographical boundaries of one Party. The level of aggregation could be expanded to a group of Parties with similar circumstances relating to the output;
 - (b) A default group of facilities should be disaggregated when significant dissimilarities exist in the performance of facilities or groups of facilities in the country/region. In this case, the disaggregation shall be carried out according to relevant criteria, such as production scale, installed capacity or age of the facilities, and standardized baselines should be developed for each group of similar facilities or for one prioritized group;
 - (c) The selection of the final level of aggregation may be an iterative process;
 - (d) Disaggregation should not result in standardized baselines with overlapping applicability (e.g. overlap would occur in the case of a standardized baseline for energy efficiency in commercial buildings, and another standardized baseline for energy efficient lighting in commercial and residential buildings).

Appendix. List of sectoral scopes

1. Energy industries (renewable - / non-renewable sources)
2. Energy distribution
3. Energy demand
4. Manufacturing industries
5. Chemical industry
6. Construction
7. Transport
8. Mining/Mineral production
9. Metal production
10. Fugitive emissions from fuels (solid, oil and gas)
11. Fugitive emissions from production and consumption of halocarbons and sulphur hexafluoride
12. Solvents use
13. Waste handling and disposal
14. [Afforestation and reforestation]
15. Agriculture
16. XXX
17. XXX
18. XXX

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