The Kyoto Protocol:
Verification Tops the Agenda

Key issues for the Seventh Session of the Conference of the Parties to the Climate Change Convention, Marrakech, November 2001

VERTIC Briefing Paper 01/05

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November 2001

Executive Summary

- At the sixth Conference of the Parties (COP6) to the 1992 Convention on Climate Change, signatories achieved a political deal on the rules for the 1997 Kyoto Protocol. Negotiators at COP7 in Marrakech, Morocco, must finalise the package to facilitate the Protocol's early entry into force.

- Important decisions relating to the verification of the Kyoto Protocol need to be taken, including:
  - the composition of expert review teams
  - reporting and review of information relating to Article 3.14
  - fungibility
  - the accounting of assigned amounts and guidelines for national registries
  - reporting on land use, land use change and forestry activities, and
  - compliance.

- These issues are cross-cutting in nature (see Table 1). Negotiators in the working groups on Articles 5, 7, and 8 compliance, mechanisms and LULUCF activities must work together to resolve the remaining issues.

- Strong leadership of the conference is key to finalising a workable deal. Only a clear overview of the whole package can lead to the consistent and workable rules necessary for the effective implementation of the Kyoto Protocol.

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INTRODUCTION

The sixth Conference of the Parties (COP) to the 1992 Convention on Climate Change resumed in Bonn, Germany from 16 – 27 July 2001, after failing to reach agreement in November 2000 in The Hague. In Bonn environment ministers finally secured a political deal on the operational rules for the 1997 Kyoto Protocol. Unfortunately, the United States rejected the terms of the deal and has withdrawn from the process. Nevertheless the agreement represents an important achievement for the remaining signatories, taking them closer to ratification and hastening the Protocol's entry into force. Parties should use the momentum provided by the political decisions in the Bonn agreement to finalise the details of the Protocol's implementation at COP7, to be held in Marrakech, Morocco, from 29 October – 9 November 2001.

One of the key areas still to be negotiated is the verification system under Articles 5, 7 and 8 of the Protocol. No real progress has been made on these texts since the working group's discussions at COP6 part I in The Hague. It is important therefore that the decisions taken in Bonn are now consolidated in the methodologies and guidelines for reporting and review. To successfully achieve this, attention will need to be paid to cross-cutting issues relating to the mechanisms, compliance and land use, land use change and forestry (LULUCF) activities.

VERIFICATION AND THE KYOTO PROTOCOL

A strong system for monitoring, reporting and review will provide the backbone for the effective implementation of the Kyoto Protocol. It should serve to detect and deter non-compliance and reassure parties that the treaty is being implemented fairly and effectively. Specifically, the Protocol aims to reduce global greenhouse gas emissions (GHG) by 5.2% of 1990 levels during the first commitment period from 2008-2012. The verification system must therefore demonstrate that the reductions claimed by each Annex 1 (developed) party are authentic and that they satisfy the individual targets they committed themselves to under Article 3.1. Any suspicion that parties are 'cheating the atmosphere' with fictitious or exaggerated emission reductions would undermine the integrity of the agreement and effect a party's confidence that the burden of implementation is being spread fairly.

KEY ISSUES FOR COP7

The guidelines under Article 5.1 of the Protocol, outlining how Annex 1 parties should implement national systems to estimate GHG emissions and removals, were agreed at the 12th meeting of the SBSTA (SB12). Since then, draft texts have been produced for reporting and reviewing under Articles 7 and 8. These still contain a number of square brackets, used to indicate areas of disagreement. Some of these brackets represent areas of complexity or those that are dependent on unresolved issues in other working groups (see Table 1). Others represent issues on which parties have taken entrenched positions. Therefore the problems to be faced at COP7 cannot be resolved in isolation from each other.

Composition of review teams

Article 8 of the Protocol makes provision for reviewing the data provided by each party under Article 7. Under a proposal from the Chairman of the working group, each party would be assigned a different team, selected on an ad hoc basis both from a roster of available experts and a standing group of review experts. The team will be expected to analyse the data from each party, apply any adjustments that have to be made and write a report highlighting any areas of potential non-compliance. Currently, the text states that, 'without compromising other selection criteria, the formation of an expert review team (ERT) should ensure [geographical balance] among its members…' However, parties are in disagreement about the nature of this geographical balance.

In the Bonn agreement, decisions were taken about the future composition of the compliance committee, an official panel with responsibility for judging possible cases of non-compliance forwarded to it by the ERTs. It was decided that the compliance committee, like the executive board for the clean development mechanism and the expert group on technology transfer, would consist of members from each of the 5 regional groups. The G77 and China now propose that the composition of the ERTs should follow a similar model. However, these requirements could seriously effect the standing group's ability to carry out its work. While a geographical balance between Annex 1 and non-Annex 1 countries is desirable, it is important that the review teams are assembled primarily on the basis of technical expertise. Developing countries, unable to provide skilled personnel and therefore worried about a lack of representation, should be reassured by the fact that the teams will not take compliance decisions, but will merely present information to the compliance committee, whose composition has now been formalised to their satisfaction.

Reporting and review of article 3.14

Article 3.14 of the Kyoto Protocol relates to minimising the social, environmental and economic impacts of its implementation on developing countries. Decisions at COP6 part II in Bonn included a recommendation that Annex 1 countries provide

Remaining issues	Linkages
Article 5.1 Guidelines for national systems	None (complete)
Article 5.2 Methodologies for adjustments	➢ International Panel on Climate Change good practice guidelines (IPCC GP) ➢ Expert workshops
Article 7.1 Annual reporting	
LULUCF activities under Article 3.3/3.4	➢ GP guidelines ➢ Eligibility ➢ Accounting ➢ Compliance
Additions to and subtractions from assigned amount	➢ Eligibility ➢ Accounting ➢ Commitment period reserve
Art. 3.14, funding and supplementarity	➢ Compliance
Article 7.2 National communications	
Reporting on bunker fuels	➢ Art. 4 bubbles
Article 7.4 Accounting assigned amounts	
Elaboration of assigned amount	➢ Fungibility ➢ LULUCF ➢ Mechanisms ➢ Eligibility
Operation of national registries	➢ Fungibility ➢ LULUCF ➢ Mechanisms ➢ Eligibility
Article 8 Review	
Composition of ERT	None
Review of Art. 3.14 information	➢ Compliance
Review of national registries	➢ Compliance

Table 1 Linkages between unresolved issues in the Articles 5, 7 and 8 working group and those on compliance, the mechanisms and land use, land use change and forestry (LULUCF) activities.

supplementary information as part of their annual inventory reports, in order to demonstrate how they are implementing their commitments under this article. Further, it explicitly states that the facilitative branch of the compliance committee should consider this information.

Saudi Arabia, which has concerns about compensation payments for economies dependent on fossil fuels and has persistently raised issues relating to Article 3.14 during negotiations, wants to incorporate a separate set of review guidelines under Article 8. It maintains that the ERTs should review the supplementary information on Article 3.14 prior to the first commitment period and should be used to establish eligibility for the financial mechanisms. Thereafter, reviews would consist of both annual desk reviews and periodic in-country visits, scheduled to coincide with those undertaken as part of the review of national communications. It also believes that a failure to provide the supplementary information on Article 3.14 should constitute a reporting problem and thus should be forwarded to the enforcement branch of the compliance committee.

Annex 1 countries are strongly resisting the inclusion of such a stringent review and enforcement procedure. Their position is based on the fact they are only asked to 'strive' to meet the provisions of Article 3.14 and therefore want to avoid a link between reporting and review and compliance. They are also likely to block any similar moves to introduce separate reviews for information submitted on funding (Articles 10 and 11) and supplementarity. China believes these issues to be at the core of the Protocol and although it did not propose new text on these issues, it indicated that it would like to see changes made. It is important that the negotiation of the procedures for the reporting and review of supplementary information is carried out constructively at COP7. Parties may wish to consider a compromise, agreeing that a failure to report information pertaining to these articles would be forwarded instead to the facilitative branch of the compliance committee for its consideration.

Assigned amounts and fungibility

Another key issue, which surfaced in the Articles 5, 7 and 8 working group in The Hague and has yet to be resolved, is the nature of the assigned amount. This in turn is related to the issue of fungibility and the operation of the national registries. Members of the Umbrella Group (Australia, Canada, New Zealand, Japan and the United States) indicated that they would be unable to ratify the Protocol without finalising these issues at COP7.

Annex 1 countries will each have an assigned amount that is calculated prior to the start of the commitment period, based on their base year emissions and the targets set out in Annex B to the Protocol. At the end of the commitment period the assigned amount held by each party will be compared to its total emissions, calculated from the annual inventories, to assess compliance with Article 3.1. Annex 1 countries expect that this initial assigned amount can be added to or subtracted from, using credits from the flexible mechanisms and land use, land use change and forestry (LULUCF) activities. This equivalence between credits under different articles of the Protocol is called fungibility and for many parties this would result in an increase in their assigned amounts during the first commitment period and increased flexibility within the flexible mechanisms.

However, the G77 plus China interpret the text differently. They maintain that the assigned amount is fixed at the start of the commitment period and cannot be altered using the different types of credits. In this way, acquired or traded Emissions Reduction Units (ERUs), CDM emissions reductions (CERs), Parts of the Assigned Amount (PAUs or AAUs) or sink credits obtained under Articles 3.3 and 3.4 would be accounted for separately from the assigned amount. India is proposing a new name for sink units and Brazil suggested the use of 'units of forestry' (UFOs) to describe units generated by activities under Article 3.3 and 3.4. India also prefers the use of the term 'allowable emissions', equal to AAUs ± 3.3/3.4 sink units + CERs ± ERUs ± PAA. This amount, differentiated from the assigned amount, would be used in the final compliance assessment.

The Bonn agreement clarified the fungibility position slightly in that it explicitly allows Annex 1 countries to use each type of unit to meet commitments under Article 3.1. However, non-Annex 1 countries continue to want to restrict the fungibility of these assets. Negotiators at COP7 need to decide:

- which credits can be traded and transferred between national registries and how
- which credits must be held as part of the commitment reserve
- how to prevent Annex 1 countries banking cheap CDM credits to offset against their assigned amount in future commitment periods, and
- whether parties can bank and carry over credits generated within and above the caps set for sinks activities for use in future commitment periods.

It is unclear whether these discussions will take place in the Articles 5, 7 and 8 or mechanisms negotiating groups. Either way, these decisions need to be taken in order to develop the guidelines for national registries under Article 7.4 and the review of these procedures under Article 8.

National Registries

In order to comply with Article 7.4 of the Kyoto Protocol, each Annex 1 country will need to demonstrate the implementation of a national registry prior to the start of the first commitment period. This will also provide one aspect of the eligibility criteria for taking part in the trading mechanisms. The registries will act like a bank, recording the issuance, transfer and cancellation of credits under Articles 3, 4, 6, 12 and 17. It will also provide information for the accounting procedure. For this reason, the system needs to be as foolproof as possible, to be transparent and to have clear procedures to correct mistakes and deal with parties flouting the operational rules.

Currently these issues have not been discussed in any detail within the working group on Articles 5, 7 and 8, pending decisions from the group working on the operational rules of the mechanisms. However, it is important that negotiators at COP7 agree on some key elements with a view to creating a workable and transparent system including:

- registry requirements for national and international transactions
- a secure method of tracking the transfer of units between registries and methods for resolving discrepancies where they occur
- the nature of the transaction log and what information is stored regarding the additions and subtractions to the accounting database
- the operation of eligibility checks, the commitment period reserve and the caps on sink activities
- a comprehensive review procedure, and
- enforcement and procedures for dealing with non-compliance.

LULUCF activities

Reporting and review

The Bonn agreement resolved many of the issues relating to the use of LULUCF activities in meeting targets. However, there are still conflicts over the reporting of information pertaining to sinks under Articles 3.3 and 3.4. Article 7.1 requires parties to provide the necessary supplementary information to demonstrate compliance with Article 3. However, the exact nature of this information is still under discussion and much of the text is contained in brackets.

Australia proposes that information on Article 3.3 and 3.4 activities only be reported once in the first commitment period and not annually as most other parties expect. It is important that these activities are treated in the same way as other sources and removals listed in Annex A of the Protocol and reported in the annual inventory. Not only will this minimise the difficulties in verifying the integrity of these activities, it will mean that Article 3.3 and 3.4 reporting becomes an eligibility requirement for the financial mechanisms and therefore a compliance issue.

Parties also disagree over the type of information that should be reported and what level of detail should be prescribed by the Articles 5, 7 and 8 text what should be left to the Intergovernmental Panel on Climate Change (IPCC) as it works on the LULUCF good practice guidelines. For example, discussion continues as to whether geographic location references and base year information for net-net accounting should be included. Finally, there is disagreement over the EU proposal that parties demonstrate whether GHG removals are due to 'direct human-induced' activities.

Accounting

Accounting is the process of adding up all of a party's efforts towards meeting its commitment under Article 3. Part of this calculation involves the units generated by activities under Article 3.3 and 3.4. The rules for how and when units should be issued and cancelled and the guidelines for reporting these actions need to be agreed.

New Zealand is proposing new text that states that the issuance and cancellation of credits should take place contemporaneously, but that parties should have the choice of doing this annually or at the end of the commitment period. The European Union agrees with this net approach, but has not stated how frequently this should occur. Australia's position is that the issuance and cancellation of credits need not occur at the same time and can happen at any point during the commitment period and at a party's discretion. These positions present the danger that credits issued in one year for a sink with a net removal cannot be retrieved if the same sink later becomes a net source. Therefore, a procedure which accounts for the issuance and cancellation of credits at the same time and at the end of the commitment period is most likely to be able to protect against these problems. Additions and subtractions to the assigned amount should be submitted annually under Article 7.1.

Canada has also proposed changes to the procedure for administering adjustments to information on Article 3.3 and 3.4 activities. Under this proposal, only information reported for the purpose of accounting the assigned amount would be subject to adjustments. Apart from not providing an incentive for the submission of good quality data, this would make the adjustment procedure for LULUCF activities different to that for the emissions inventories, creating a more complicated system and undermining the clear link between reporting and the issuance of units.

Eligibility

Only parties that comply with the key reporting guidelines under Articles 5 and 7 are eligible to take part in trading under the flexible mechanisms. However the eligibility criteria for parties wishing to use activities under Articles 3.3 and 3.4 are still being negotiated. It is important that the issuance of assigned amount units is contingent on the activities complying with the IPCC good practice guidelines. In addition, eligibility to trade these units should be strongly linked to reporting requirements. There are indications that the Umbrella Group would like to restrict the eligibility criteria to the annual reporting of sources and removals listed in Annex A of the Protocol, which does not contain the activities permitted under Articles 3.3 and 3.4. These countries stand to benefit greatly from these activities and thus want to avoid any extra eligibility restrictions based on their reporting of them. It is important that this loophole is closed—linking eligibility to compliance with the reporting requirements provides parties with the incentive to provide complete and accurate data on LULUCF activities.

Compliance

The last hurdle in securing the Bonn agreement was the issue of compliance. The agreement sets out the consequences of non-compliance, which are designed to bring the non-compliant party back into compliance and protect the environmental integrity of the emissions targets. However, the Bonn agreement did not decide whether these consequences should be 'legally binding'. Article 18 of the Protocol states that a compliance regime with 'binding consequences' can only be adopted through an amendment to the Protocol by the Conference of the Parties, serving as the Meeting of the Parties to the Protocol (COP/MOP).

Unfortunately, different interpretations still exist on what the Bonn agreement means. The Umbrella Group has taken the position that the consequences agreed in Bonn are not binding and consequently wants to see 'shall' in the compliance text replaced by 'should', in order to weaken a party's obligation to comply with the penalties imposed in the case of non-compliance. They also dislike the recommendation in the Bonn agreement that the COP/MOP amend the Protocol to make the consequences binding. Providing the current wording of the compliance text is preserved, the discussion of whether the consequences are binding in the sense of Article 18 should be left until the first COP/MOP rather than complicating the discussions in Marrakech.

Also relating to compliance, Canada is proposing changes to the Article 5, 7 and 8 text, which would change the way the ERTs deal with issues of potential non-compliance. Currently, the ERTs are expected to forward all cases of potential non-compliance to the compliance committee. This body decides whether the issue relates to a mandatory or non-mandatory aspect of the Protocol and sends it accordingly to the facilitative branch or the enforcement branch of the compliance committee for consideration. The Canadian proposal, however, would give the ERTs the power to decide themselves on the mandatory/non mandatory nature of the problem, sending only mandatory issues to the compliance committee.

This proposal is potentially damaging for the compliance regime. First, it would prevent non-mandatory issues, such as those relating to Article 3.14, funding, policies and measures and supplementarity, from being considered by the facilitative branch of the

compliance committee. This would essentially allow Annex 1 countries to avoid an assessment of their efforts to meet the commitments under these articles. Second, the proposal would undermine the 'technical' nature of the ERT, introducing political considerations to the decisions they are expected to make.

CONCLUSIONS

The negotiation of the Articles 5, 7 and 8 texts has traditionally been technical in nature. However, many issues that have proved difficult to resolve in other areas of the negotiations have been termed 'technical' and swept into the Articles 5, 7 and 8 working group to facilitate agreement on the more political aspects of the Protocol. This essentially political approach led to a favourable outcome at COP6 part II in Bonn. However, the items swept under the carpet now have to be faced at COP7 in the Articles 5, 7 and 8 negotiations. Where these negotiations were traditionally technical they are now likely to become highly politicised, making progress more difficult. The entrenched positions of parties will be reflected in negotiations on all the key issues outlined in this paper. Add to this the complexity and the cross-cutting nature of these issues and there is the potential for the final text to lack consistency and to contain loopholes.

To guard against this, negotiators must work across the negotiating groups, paying attention to the linkages between the operational rules for the mechanisms, LULUCF activities and compliance. Strong leadership of the conference is key to finalising a workable deal. Only a clear overview of the whole package can lead to consistent and workable rules necessary for the effective implementation of the Kyoto Protocol.

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