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# Harvard Project on Climate Agreements

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## Governing Cooperative Approaches under the Paris Agreement

*A summary of a discussion paper supported by the Enel Foundation*

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**November 2018**

Article 6 of the Paris Agreement allows Parties to engage in voluntary cooperation as they implement their nationally determined contributions (NDCs). One channel of cooperation – set out in Article 6.2 – involves the use of internationally transferred mitigation outcomes (ITMOs) towards achievement of NDCs. Although the provision omits explicit mention of markets, it harbors the promise of market-based approaches to lower the cost of achieving environmental policy objectives. Such cost reductions, in turn, offer an opportunity for greater climate ambition with given resources. By helping to achieve initial NDCs at lower cost, they can soften political resistance against more ambitious future pledges, and unlock resources that can be diverted towards additional abatement efforts.

Lower costs do not automatically translate into greater ambition, however. A growing body of research has examined the potential of cooperative approaches to weaken aggregate efforts if Parties transfer ITMOs with questionable integrity or are discouraged from progressively strengthening their NDCs over time. Unlike the Kyoto Protocol, the Paris Agreement requires all Parties to the Agreement to participate in mitigation, altering the incentive structure for countries as they consider their future climate pledges. As Parties negotiate guidance for the implementation of cooperative approaches under Article 6.2 of the Paris Agreement, they are therefore considering governance options to secure environmental integrity and address concerns about aggregate ambition.

How to address such concerns has consistently proven to be one of the most contentious items in the negotiations on Article 6.2. Parties and other stakeholders have voiced widely divergent views on the need to include ambition and environmental integrity in governance of ITMO transfers, and successive textual proposals have featured long lists of options for potential inclusion in Article 6.2 guidance. Relevant options proposed by Parties and other actors fall along a continuum ranging from very prescriptive, with more centralized oversight, to very flexible, with considerable delegation to Parties engaged in an ITMO transfer.

We map stakeholder views and evaluate relevant options contained in the latest proposals for how guidance can balance necessary safeguards for climate ambition with flexibility to contain transaction costs and facilitate greater participation. In doing so, we draw on an analytical framework that incorporates economic theory, deliberative jurisprudence, practical case studies, and treaty interpretation. Based on this analysis, we conclude that neither over- nor under-regulation will lead to efficient outcomes, nor indeed be conducive to greater ambition.

Because the mandate to develop operational guidance is enshrined in the Paris Agreement, we apply customary principles of treaty interpretation to a textual analysis of Article 6.2. Understood in light of the Paris Agreement's negotiating history – and its object and purpose – the wording of Article 6.2 allows Parties to consider ambition in operational guidance, but does not dictate a specific mitigation threshold or other material outcome. Parties thus retain significant discretion in how they choose to balance prescriptiveness and flexibility in guidance on Article 6.2.

A survey of the literature and case studies on market-based instruments lends support to specific recommendations for operational guidance on Article 6.2. Both theory and experience highlight the importance of a governance framework that ensures transparency in cooperative approaches, and guarantees accurate accounting for ITMO transfers. Failure to include these essential features would threaten to repeat painful episodes in the history of carbon markets, during which these markets have incurred considerable reputational damage. Not all policy interventions are created equal, however, and distinguishing such requisite elements from those that are needlessly restrictive is one of the central challenges facing policy makers in the operationalization of Article 6.2.

For that reason, the governance framework should avoid restrictions, such as a requirement for centralized approval of individual ITMOs, that incur high transaction costs, investor risk, and uncertain benefits. Experience with the Clean Development Mechanism (CDM), in particular, has shown how a lengthy and prescriptive approval process involving complex additionality tests can add transaction costs without guaranteeing desired environmental outcomes. This track record cautions against imposing quality criteria to regulate environmental integrity risks under Article 6.2; such criteria tend to suffer from their own regulatory failures, such as information asymmetries, capacity constraints, and regulatory capture.

Experience has also shown that mature and liquid markets rely on diversity of participation, arguing against an outright exclusion of non-Party stakeholder engagement in cooperative approaches. Other restrictions, such as quantity limits on transfers, can be effective in addressing environmental risks, but also curtail the economic benefits of cooperative approaches, and should therefore be used prudently, if at all.

Empirical data suggest that some concerns may be misplaced, such as fears of a supposed perverse incentive under Article 6.2 to weaken future mitigation pledges. Research on the CDM has shown that the ability to engage in carbon trading has not meaningfully affected domestic climate policy choices, which are instead driven by other political priorities and institutional power structures. Conversely, uniform metrics for ITMOs can facilitate linkage by increasing fungibility, and should be considered.

Invariably, these options will require political choices among competing priorities, inviting tradeoffs and compromises that accommodate contingent preferences. Process may therefore acquire as much weight as substantive considerations in the elaboration of Article 6.2 guidance. Deliberations preceding such a compromise should be fair, inclusive, and transparent, and take place in appropriate forums. As such, technical guidance on Article 6.2 should not seek to supplant or correct political decisions on ambition and flexibility reached under the Paris Agreement more generally.

Any viable compromise will likely reflect the delicate equilibrium struck in the Paris Agreement between pursuit of progressively greater climate ambition and a decentralized architecture that favors national determination by sovereign Parties. Whatever its final shape, the governance framework for Article 6.2 should avoid being too weak or too restrictive, as either outcome would diminish the very benefits that prompted introduction of compliance flexibility in the first place.

**Full paper available at:** [www.belfercenter.org/publication/governing-cooperative-approaches-under-paris-agreement](http://www.belfercenter.org/publication/governing-cooperative-approaches-under-paris-agreement)

## ACKNOWLEDGEMENT

The Harvard Project on Climate Agreements is grateful to the Enel Foundation and the Enel Endowment for Environmental Economics at Harvard University for generous support of a series of annual discussion papers on climate-change policy and related topics in energy policy, of which this paper is the eighth.