World Bank Carbon Finance Unit
Carbon Partnership Facility
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New Market Mechanism – Design Considerations and Piloting

Design features of the new market mechanism

- Global net emission reductions (instead of pure offsetting);
- Broad segments of the economy (instead of project-by-project);
- MRV and avoidance of double counting (also relating to domestic ambition targets);

NMM Design Considerations

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Demand-side requirements

- Convergence with evolving UNFCCC criteria
- Confidence in environmental integrity/ robustness
- Host countries to set ambitious crediting baseline below BAU and beyond project-by-project
- Possibility to use as a compliance tool for domestic targets and emission trading regimes

New market mechanism

Supply-side requirements

- Compatible with domestic policy setting for low carbon development
- Recognizing national circumstances and priorities
- Need to set up institutional & regulatory framework (transparent and predictable regulations & implementation, sound MRV, low transaction
- Prospects of off-take (demand)

How could the NMM work ?

- Host country decides on mitigation strategy for a particular sector/segment of the economy and related instruments;
- Host country defines crediting baseline below BAU for a particular sector/segment of the economy taking into account potential leakage effects;
- Host country sets up a MRV and registry infrastructure;
- UNFCCC endorsement (MPs to be defined);
- Host country sets up an implementation framework;
- Host country MRV system verifies achieved ERs below crediting baseline;
- Host country or UNFCCC body issues carbon credits.

Role of project entities – differences to CDM

- Initiative is with host country governments on national regulatory <u>and</u> implementation framework;
- Carbon assets can only be earned in aggregate and not based on the performance of individual projects;
- Strong incentives for financial transformation of carbon revenues and blending with other sources of funding within host countries;
- If implemented successfully investors can benefit from carbon revenues at lower transaction costs.

Piloting the new market mechanism - challenges

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- Starting before host countries made their strategic choices and before new infrastructure/regulation is in place;
- Building on private sector and sub-national initiative while following the logic of moving away from project-by-project;
- Setting sufficient incentives while following the logic of partial crediting in a low price-high risk environment;
- Remaining representative for “broad segments of the economy” while piloting on a much smaller scale with the potential for scaling up;
- Developing the required methodological framework for accounting emissions reductions beyond project-by-project.

A basic concept of piloting

- Identify a representative aggregate – e.g. sub-sector, region/city;
- Determine BAU reference line through a simplified approach – e.g. historical trend, least cost scenario;
- Determine a crediting line below BAU: sufficiently conservative to assure consistency with emerging national ambition targets;
- Define the crediting schedule along milestones of target achievement in aggregate;
- Structure the program in line with the crediting modalities;
- Build the required MRV capacity for the program.

Generic pilot model for a new market mechanism

Define the boundary and the scale

Selected intervention should be representative of sector, technology, city, etc.

Define eligibility criteria & methodology

Enable development of new aggregate methodology approaches	Address perverse incentives

Establish the crediting baseline

Determine BAU reference line (relevant aggregation level & methodology)	Define crediting baseline below reference line (compatible & beyond national targets)

Define operational structures of the program

Crediting period & schedule	Institutional & financing structure	MRV at aggregated level

Operational requirements for piloting

- Incentive schemes that do not already require host country policy making, potentially sub-national policy programs;
- Capacity needs to be in line with scale of operations;
- Reasonable prospects for achieving a concrete transaction;
- Sound economics where carbon revenues might need to be blended with international support including ODA;
- Clear perspective for scaling-up beyond pilot level.