



Wilton Park



# **COP26 PRESIDENCY UK 2022**

**DELIVERING THE  
GLASGOW CLIMATE PACT**

Report

**COP26 Catalyst for Climate Action Assembly at the  
UN Regional Climate Week for Latin America and  
Caribbean**

**Carbon markets participation**

Friday 14 May 2021

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### Introduction

In its role as the incoming COP26 Presidency, the UK is committed to better understanding the capacity building challenges faced by developing countries and climate finance recipients, particularly those most vulnerable to climate impacts, and to providing opportunities to share positive experiences and lessons learned across the Latin America and Caribbean region.

With an aim to better understand capacity needs to support use of carbon markets to meet NDC targets, this Catalyst for Climate Action Assembly brought together participants at the forefront of designing and implementing carbon markets in Latin America and the Caribbean. The participants highlighted what has worked and what has not in terms of capacity building. They discussed and shared experiences related to barriers, enabling environments, institutional environments, regulatory frameworks, stakeholder engagement and private sector participation.

The session, facilitated by Wilton Park, was attended by over 45 participants from different countries such as Mexico, Peru, Chile, Costa Rica, Trinidad and Tobago, Switzerland, UK, and participating organizations such as: World Bank, Perspectives, CCAP, South Pole, GIZ, and Vivid Economics, among others; the participants engaged in a rich and fruitful conversation in regards to capacity building in carbon markets, specifically in the LAC Region.

This report is a summary of the key points raised at the meeting.

### Key themes

**As possible, carbon pricing instruments should be anchored in law and the NDC.** A strong legal mandate provides certainty on the direction, even under government transitions. At the same time, there should also be room for trial and error. For example, a pilot phase of an ETS provides an opportunity to ensure systems are working and to make course corrections. Other types of programs may also benefit from flexibility.

**Market-based programs rely on data.** Depending on the program, emission inventories, emissions reporting and/or modelling may be needed to support design and implementation. For example, data collection is crucial to making informed decisions such as establishing a cap that is relevant for the country. Countries have focused extensively on building this capacity.

**Learning by doing offers a strong means to get started.** Governments can study and explore carbon pricing instruments in the abstract but the different design elements and options can be best understood in practice. For example, by engaging in pilot phases (ETS) and pilot projects (Article 6) that bring together the relevant government ministries and stakeholders, it is possible to explore how market-based instruments could benefit the country (and where they might not) while building the capacity for implementation. In the case of Article 6, it should be recognized that cooperation may look different from one country to another, and even small islands can engage and find opportunities to benefit. It can be possible to start small, with no regrets activities.

**Coordination among ministries and stakeholders is critical.** Participants stressed the value of inter-ministerial coordination and stakeholder engagement (e.g., private sector, indigenous communities, civil society, academia) to ensure the different actors have a common understanding of the instrument and an opportunity to input to key decisions that will affect how it will be implemented in support of national climate, development and other objectives. In particular, there is recognition of the importance of engaging the private sector to spur investments and ensure they are well-positioned to participate.

**It is possible to build from earlier mitigation programs.** There is much that can be learned from earlier experiences. For example, it may be possible to use or build on CDM standards and methodologies and insights gained from prior work on nationally appropriate mitigation actions (e.g., barriers to private sector investment). Cost curves and modelling can inform selection and design of Article 6 projects. That being said, the need to meet the NDC and undertake a corresponding adjustment for international transfers mean the host government needs to be more involved in the design and implementation of Article 6 projects to ensure they will be in the national interest.

**Clear communications on carbon pricing instruments can facilitate decisions.** Governments should not let the complexities of the design process obscure the big picture opportunities presented by market-based approaches.

**Further dialogue can build confidence in use of market approaches.** Country representatives pinpointed that further LAC regional dialogue and interaction, as well as broader south-south dialogue, is very much needed to advance capacity building. Learning by doing is key, but learning by knowing what other country experiences are, why they chose a particular mechanism or decision, and how the countries are making progress on carbon pricing can be even more encouraging. Talking more can help countries learn from each other, especially with respect to country experiences on how to win acceptance of market-based instruments.

**Capacity-building can be helpful at different stages of the process.** Even though countries are making good progress in evaluating and implementing different market-based instruments, the truth is that capacity building may be needed at all stages of implementation, from choosing an instrument, embedding the instrument in domestic laws and commitments, to program design and implementation. Since carbon markets adoption in the LAC Region is still emerging, there is a huge opportunity for innovation and improvement in making use of market-based tools to realize national climate goals.

## What can be learnt from Latin America and Caribbean country experience of carbon markets so far?

Participants shared experiences from a range of countries and contexts. Here are some examples.

### Mexico

Support over many years has helped the Mexican government consider a number of design issues and develop the required infrastructure and capacity to the point that they are now implementing the pilot phase of the ETS. One issue highlighted was the importance of a legal basis. In Mexico's case, this was the General Law on Climate Change (2018) and subsequent Guidelines (2019). Another key factor was learning from the lessons and experiences from other ETS programs in Europe and North America. A key issue as the country moves beyond the pilot phase is the decision on how the cap should decline over time.

### Peru

Peru raised questions to assess what is feasible in the national and subnational context, including: Whom to involve and how to involve all relevant actors? What policy framework should be put in place to ensure the legal security of the process? How to build a carbon market policy based on evidence and relevant data? What can be learned from experiences with CDM and REDD+? How to engage the private sector? How to link a carbon market policy with a Climate Change National Strategy or the NDC goals? And overall, how do carbon markets promote innovation in countries? In Peru, some key steps include clarifying institutional mandates and the approach to authorize transactions; establishing an agreement with Switzerland to explore Article 6 cooperative approaches in a stepwise manner; and strengthening systems for MRV.

### Chile

Chile highlighted some of the first steps a national government should take before adopting any carbon pricing mechanism: The government should have good knowledge and understanding about the carbon pricing instrument it would like to promote; second, the government should have in place a robust climate change MRV system, such as GHG inventory or an emissions database; and third, the government should be clear on the role of the instrument in meeting the NDC.

As far as specific measures, Chile started with a carbon tax first, in part because it was seen to be relatively simple. However, the choice of a downstream tax meant that MRV was needed from the regulated sources. This helped build capacity in both public and private sectors. Updates to the green tax included changes to the tax threshold and establishment of an offsetting system. Chile is still working to understand the role of Article 6 in meeting its NDC and how to apply the corresponding adjustment. They want to participate in Article 6 but don't want to jeopardize achievement of the NDC. There are a lot of issues to work through. It isn't necessary to start from scratch; it is possible to build on standards that already exist. Inter-agency coordination is highly important. Next steps are to further strengthen capacity and take a decision.

### Costa Rica

It is important to understand a country's situation – "know thyself." Sometimes the data aren't available. One thing that has been helpful in Costa Rica has been developing local modelling capacity (as opposed to modelling by international consultants). Such local capabilities can be institutionalized and sustained over time. It is also important to clarify principles for ambition and how you intend to reach them. In Costa Rica's case, such principles include being socially inclusive, a just transition, and engaging indigenous people, especially with respect to land use and land tenure issues.

"technical accompaniment received through international cooperation by an array of different international organization has been a key factor for the ETS technical reasoning and modelling".

## **Trinidad and Tobago**

Offering a Caribbean perspective, Trinidad and Tobago, highlighted their main challenges: capacity building, technology transfer, and capital investment. Another important issue raised was the lack of economies of scale to meaningfully participate in international carbon markets. There is concern that carbon markets may not accommodate smaller economies with fewer overall emissions and emissions reductions.

T&T are building many of the capabilities that would be required to participate in market-based mechanisms. For example, they have functional MRV and knowledge management systems, and are now crafting legislation to make reporting mandatory to track emissions. A key next step is to model business-as-usual emissions to evaluate carbon market options (consistent with the BAU-based NDC baseline). This could inform decisions on whether or not to utilize carbon markets.

## **Stacey Davis and Adriana Bazán Fuster**

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## **Annex**

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