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LOOKING AHEAD TO COP29: WHAT CAN WE EXPECT?

— THOUGHT LEADERSHIP

NOVEMBER 2024

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COP29 – the 29th annual United Nations climate meeting – takes place in Baku, Azerbaijan from 11 November, but what can be achieved, realistically, against a backdrop of geopolitical complexity? In this extract from a recent webinar moderated by Roger Leese, a member of the firm's ESG Board and co-head of Clifford Chance's Global Business and Human Rights practice, we look at the major issues that COP29 will cover, including carbon markets and climate finance.

Azerbaijan's Presidency

Oil and gas clearly play a significant role in Azerbaijan's economy – 90% of its export revenues relate to oil and gas products. But it is also clear that global warming is having a real impact on Azerbaijan. In the last five years, the country has suffered extreme heatwaves, water scarcity and declining sea levels in the Caspian Sea. "Climate-driven sea level reductions by the end of this century have been predicted to result in the desiccation of the Caspian Sea's Northern Basin," says Leese.

"As hosts of COP29, there will naturally be a huge focus on what Azerbaijan has been doing to counter this," says Clifford Chance Partner Sandy Hall, head of the firm's International Construction Practice who has been working on deals in the region for over 15 years. "There has been a big drive in the last decade or so to modernise Azerbaijan's infrastructure, including the oil and gas industry. For example, we have been advising SOCAR on the upgrade of the Heydar Aliyev oil refinery just outside Baku, which is now producing lower sulphur /cleaner gasoline and diesel which meet European emissions standards," he says. The President of Azerbaijan, Ilham Aliyev, talks about Azerbaijan being "in the active phase of its green transition."

"In the official COP statements released so far, it seems that Azerbaijan sees this as an opportunity to raise its profile further on the world stage as a key 'actor' in the fight against climate change," Hall says.

Azerbaijan's Nationally Determined Contributions (NDCs) have committed to reducing GHG emissions by 40% by 2050 (against 2010 levels) and increasing renewable power capacity to 30% by 2030. Renewable power generation currently stands at about 5% of total energy mix (mainly hydro, but with solar and wind coming through).

"It's the growth in the renewable power sector where, at Clifford Chance, we've seen the most recent activity. Over the course of the past five years, we've worked on the first utility-scale solar PV project (230MW) in the Garadagh region in the east; the largest wind farm in the country (the 240MW Khizi wind farm); and we're now working on 'Project Mega' – a 1GW renewable energy project comprising three separate wind and solar farms," says Hall.

All of these projects are being funded by Development Finance Institutions such as EBRD, IFC and ADB, and are often sponsored by Middle East developers, such as Masdar and ACWA, which have their own ambitious renewable energy production targets to meet.

"Officially, this year's COP has identified two key themes, or pillars – the need to enhance ambition in the fight against climate change and to enable action, predominantly via the power of finance, to tackle the crisis and accelerate change. However, I think the underlying theme which will run through the event will be how well Azerbaijan is able to avoid controversy or negative PR. It seems inevitable that there will be some backlash, or "oil shaming", at this year's event, as there was in Dubai for COP28. Azerbaijan has been promoting an alternative narrative that the existence of the fossil fuel industry cannot be denied and is a major source of income for many countries; the real test is how fossil fuel nations and their SOEs rise to the challenge of the climate crisis in a just, orderly and responsible manner," he says.

Carbon credits and trading – where are we now?

COP27 (the "implementation COP"), which took place in 2022, was expected to deliver the key decisions to enable operationalisation of the Paris mechanisms set out in Article 6.2 and Article 6.4 of the Paris Agreement on the role of carbon credits and trading. Decisions on Article 6.2 and Article 6.4 were published setting out agreements on reporting obligations and the "centralised accounting and reporting platform" (CARP), but they failed to tackle some of the biggest areas of contention holding the Paris mechanism back.

"Many hoped that COP28 would finally deliver the decisions needed to operationalize the Paris mechanisms and, in particular, to enable the Article 6.4 mechanism (now referred to as the Paris Agreement Crediting Mechanism (PACM)) to start," says Clifford Chance Partner Nigel Howorth, who is based in London. "However, after long and sometimes emotional negotiations, consensus could again not be reached. The Parties were unable to agree because they were split into two camps – the US (supported to some extent by countries such as India and China) wanted little detailed governance and process because that would slow down finance, while the EU, African and rainforest nations wanted detailed processes to be followed before trades can be undertaken, with integrity being key."

The President of COP 29 has expressed a commitment to finalise the operationalisation of Article 6, which he describes as "a long overdue priority." There are a number of high-level issues:

- Discussion focusing on the sequence of reporting, assessment and recording in the greenhouse gas inventory, verifying a country's actual emissions against its Nationally Determined Contributions (NDCs – climate action plans submitted by each country under the Paris Agreement) before Internationally Transferable Mitigation Outcomes (ITMOs – the credits that can be used to meet NDC commitments) are issued and can be traded.
- ITMOs use authorisations. These are a fundamental part of the process as they are the three authorisations necessary for emission reductions or removals to become ITMOs: process and timing, format and the ability to change or revoke them – which is a source of concern for many, particularly investors.

There are also more practical and detailed matters that need to be addressed:

- The detail of the Article 6.2 international registry, which records authorisations, transfers and usage. The US sees it as accounting for annual balances by each party, whereas the EU and Africa see it as a full transactional registry.
- Whether secondary trading in ITMOs should be permitted.
- Detail on definitions, process and clarification.

There are signs that some of the necessary groundwork to achieve a result at COP29 has been undertaken. At the pre-COP meeting in Bonn in June 2024 (known as SB60), Article 6 was agreed as a focus area for discussion; in particular, ITMOs use authorisations, the design of registries to be used under the Article 6.2 mechanism, and emissions avoidance. Then, at a more recent meeting in Baku in October 2024, the Article 6.4 Subsidiary Body took the highly unusual move of approving standards for carbon dioxide removal and methodology requirements. "The move to adopt standards, rather than making full recommendations, is an attempt to avoid the typical log-jam that recommendations incur. The conference is simply asked to "note" these standards (thereby endorsing them)," says Howorth. In addition, the United Nations Framework Convention on Climate Change (UNFCCC) has established an interim platform for the submission of reports and publication of non-confidential information. This interim platform is a step towards the development of a centralised accounting and reporting platform (CARP).

What can we expect?

"With regard to Article 6.2, it is expected that the key parties will make sufficient compromises to agree something on the sequencing. The US and the EU have had pre-COP discussions to try and find the common ground. The key is going to be finding that integrity aspect. As long as the high-level debate goes smoothly, we can expect that the more practical details will be largely agreed," says Howorth. "As for Article 6.4, I have been assured there will be fireworks. The country representatives are apparently very unimpressed with the Supervisory Board's attempt to circumvent the authority of the COP and the CMA – which oversees the implementation of the Paris Agreement. At COP28, they were expressly asked to go away and come back with recommendations, not attempt to ignore the process and adopt standards."

Implementation

The Subsidiary Body has also made significant progress in transitioning Clean Development Mechanism activities to the PACM, receiving almost 1,500 transition requests by the deadline of 31 December 2023, and adopting numerous procedures, standards and forms throughout 2023 and 2024 to enable transition. This means that a pipeline of activities for the PACM is already in place, and the first issuances under the mechanism may come as soon as early 2025.

Where have we got to on emissions avoidance?

An issue that is unlikely to be discussed at COP29 is emissions avoidance (where emissions are avoided by retaining carbon sinks such as forests). At the 2024 Bonn Climate Change Conference, following considerable debate, the Subsidiary Body for Scientific and Technological Advice (SBSTA) to the COP decided to exclude emissions avoidance as an eligible activity type under the Article 6.2 and Article 6.4 mechanisms, citing the absence of consensus on the issue and a general lack of alignment on what the definition of "emissions avoidance" is. It did, however, agree to revisit the matter in 2028.

While these issues would appear to have been settled, and no further discussion on them is expected at COP29, there remains a degree of uncertainty around emissions avoidance and the implications for avoided deforestation activities in Article 6.

This comes down to definitions. There is a lack of distinction between those activities where proactive measures are taken; for example, actions taken to avoid cutting down a forest (such as revoking a logging permit) or not permitting the extraction of oil reserves, and those characterised by lack of action, i.e. simply claiming that an existing forest or other carbon sink should be rewarded with credits.

The former being eligible for Paris mechanisms as emissions reductions or removal activities.

These persisting uncertainties would ideally be resolved at COP29 – and that would need the CMA to adopt a clear, agreed definition of "emissions avoidance." Without this, we expect that the divide between Parties that are pro-REDD+ type projects and those that are opposed to REDD+ type projects will remain.

Methane

Last year, the Global Stocktake called upon Parties to accelerate and substantially reduce non-CO2 emissions globally – particularly methane emissions – by 2030. Methane has more than eighty times the warming power of CO2 and rapid action can moderate future temperature rises. At COP28, the Parties signed up to a Global Methane Pledge to contribute to the global target of reducing methane emissions by at least 30% below 2020 levels by 2030, in line with the Intergovernmental Panel on Climate Change's (PCC's) 1.5°C pathway.

Azerbaijan was a signatory to this pledge and the COP29 Presidency will launch the COP29 Declaration on Reducing Methane from Organic Waste to supplement the Global Methane Pledge. Endorsers will declare their commitment to set sectoral targets to reduce methane from organic waste within future NDCs. They will also work towards developing and implementing subnational policies, roadmaps and action plans, and mobilising financial resources from both public and private sources, improving transparency and data-driven policy-making, and developing innovative partnerships for collaborative action. "We are already seeing such projects becoming a key new type of project in the VCM," says Howorth.

Biodiversity

COP16 – the United Nations Biodiversity Conference – which aims to address biodiversity loss, took place in Colombia in October, but no agreement was reached. Talks were overshadowed by a lack of progress on implementing the Kunming-Montreal Global Biodiversity Framework, the landmark "Paris Agreement for nature" deal made at COP15 in Montreal in 2022. The vast majority of countries missed a deadline to set out new plans for how they would meet the targets of the framework ahead of COP16. By the summit's end on 1 November 2024, just 44 out of 196 parties – 22% – had produced new biodiversity plans. "Countries did manage to find consensus on a new benefit-sharing mechanism for genetic resources – known as the "Cali fund" – and a new permanent body for indigenous peoples, giving them an official voice at biodiversity COPs. But they did not agree on setting up a new fund under the COP or a new framework for monitoring countries' progress on tackling biodiversity loss. While COP15 was regarded as a big step forward, COP16 was a step back," says Howorth.

The final day of COP29 will address biodiversity, indigenous peoples, gender equality, oceans and coastal zones but biodiversity does not appear in declarations, pledges or action plans.

Climate finance

Finance is high on the agenda for Baku, and the Presidency has said that the primary expectation for COP29 is an agreement on a fair and ambitious New Collective Quantified Goal (NCQG) on climate finance. "COP29 has been billed as the 'finance COP' as it is recognised that now is the time for countries to set a new ambitious global climate finance goal. This is a top negotiating priority due to the need to significantly increase the mobilisation of climate finance in developing countries," says Angela McEwan, a Clifford Chance Partner based in Amsterdam.

The idea is that the NCQG would replace the current USD 100 billion annual target which was originally set back in 2009 (and which developed countries were late to meet for most of that period). "This is quite a significant development as it is the first time in approximately 15 years that the countries will re-evaluate the amount and the type of climate finance which developing countries will receive. There are a lot of technical details that sit behind these negotiations, but the biggest issues are likely to come down to the level of overall investments which will be expected, which countries will provide finance and what will be included in the NCQG." Other considerations may include whether certain types of financial instruments will be favoured (such as concessional loans or grants, for example).

There is a currently an expectation that the NCQG is likely to have multiple targets reflecting different types of finance, for example, public finance and private finance, but would also include more qualitative policy actions which can support implementation of climate finance and deal with current barriers to scaling up the level of climate finance.

"The actual dollar figure for the NCQG will be one of the key decisions. Different climate finance targets have been suggested by different countries and organisations, which range from billions to trillions, and there are many questions still on the table such as the size and structure of the NCQG," McEwan says.

"The leaders at COP29 will have the task of reaching a final agreement on all of these topics and we can expect that they will be debating how to provide funding most effectively to developing countries to help them mitigate and adapt to climate change and transition to low-emissions economies."

The role of private finance

COP29 presents a great opportunity to engage the private sector in order to mobilise the levels of climate finance which will be needed to tackle the climate crisis. The NCQG has the potential not only to increase the quantity of public finance provided by developed countries, but also to unlock crucial private finance by calling for reforms by all relevant participants in the climate finance arena. "In order for this to be effective, I think it will be key to acknowledge the very crucial role that can be played by the many different types of investors in climate finance, including private investors, banks, institutional lenders and multilateral development banks," says McEwan.

COP29 comes at a very relevant time in relation to Nationally Determined Contributions (NDCs) as countries are expected to update their NDCs early next year and in advance of COP30. These pledges will form the foundation of the world's collective efforts to tackle climate change under the Paris Agreement and the COP29 Presidency has encouraged countries to come forward with their own 1.5°C-aligned NDCs at the earliest opportunity and well ahead of the 10 February 2025 deadline. The United Arab Emirates, Azerbaijan, Brazil and the UK are expected to lead the way and update their NDCs at COP29. "By putting forward ambitious pledges, these countries have the potential to set a high bar as other countries update their NDCs," she says.

These pledges and benchmarks are extremely important as unless emissions can be dramatically reduced by 2030, it may be difficult to hold warming to 1.5°C. NDCs provide an opportunity for countries to present climate plans which are comprehensive and investable in order to encourage long-term private investments and secure additional finance to meet climate goals. "In that respect, the NCQG and the NDCs are very much interlinked, with both presenting an opportunity to make private finance part of these discussions," she says.

In addition, climate change requires significant changes across all sectors of the economy in order to reach emissions targets and build resilience. By having sector-specific targets in relation to, for example, agriculture, transportation and energy, NDCs could have the benefit of giving a clear indication of how a particular sector is expected to develop and help promote the raising of more finance.

Funds for loss and damage

At COP28, the Fund for Responding to Loss and Damage (FRLD) was created to provide resources to developing countries which were struggling with loss and damage due to, for example, extreme floods and wildfires. Approximately USD 700 million has been pledged at, or since, COP28. However, it is expected that developing countries may have climate-related loss and damages of approximately USD 580 billion by 2030. At COP29, it is expected that developed countries may announce new pledges to support loss and damage in developing countries. There will also be the question as to whether the NCQG will itself include loss and damage and/or have a dedicated sub-goal for it.

Adaptation finance

Adaptation will also be an area of discussion at COP29 and is likely to include:

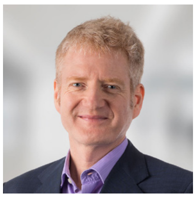
- Closing the adaptation financing gap, which is currently around USD 194-366 billion dollars per year. As part of the Glasgow Climate Pact, countries had agreed to double adaptation finance by 2025. At COP29, a report is expected to be shared to show progress towards this goal.
- The strengthening of the Global Goal on Adaptation. At COP29, it is expected that negotiators will work on agreeing a manageable set of indicators for tracking progress and finance flows at both the national and local levels.

The Climate Finance Action Fund (CFAF) will be launched at COP29, which is expected to be capitalised with voluntary contributions from fossil fuel-producing countries and companies across oil, gas and coal, with Azerbaijan as a founding contributor. The idea is that this Fund will be a public-private partnership, mobilising the private sector and de-risking investment. "The Fund is expected to provide off-take agreement guarantees for small and medium-sized renewable energy producers and first-loss capital for green industrial projects. It is expected to become operational after the initial fundraising round, which seeks to capitalise the fund with USD 1 billion and when 10 contributing countries are committed as shareholders.

CONTACTS

Sandy Hall
Partner
London
T: +44 207006 6806
E: sandy.hall@
cliffordchance.com

Nigel Howorth
Practice Area Leader
Real Estate
London
T: +44 207006 4076
E: nigel.howorth@
cliffordchance.com



Roger Leese
Partner
London
T: +44 207006 8710
E: roger.leese@
cliffordchance.com

Angela McEwan
Partner
Amsterdam
T: +31 20 711 9142
E: angela.mcewan@
cliffordchance.com

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