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REDUCTION OF GHG EMISSIONS FROM SHIPS

Principles for market-based measures

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SUMMARY

<i>Executive summary:</i>	This document summarizes the key principles that any market-based measure (MBM) agreed at IMO level needs to follow in order for it to be a fair and effective tool for contributing to the decarbonization of international shipping
<i>Strategic direction, if applicable:</i>	3
<i>Output:</i>	3.2
<i>Action to be taken:</i>	Paragraph 23
<i>Related documents:</i>	MEPC 77/7/4, MEPC 77/7/3; MEPC 76/7/12, MEPC 76/INF.21, MEPC 76/INF.22; ISWG-GHG 8/3/3; ISWG-GHG 10/5/3; MEPC 76/7/15; ISWG-GHG 10/5/3 and ISWG-GHG 10/5/2

Introduction

1 Discussions and negotiations on carbon pricing for the international maritime sector are picking up again. This is an important opportunity to increase the effectiveness of the international community's response to ship climate pollution and deliver significant enhanced emission reductions. A fair and effective carbon price could complement other instruments, such as the recently agreed short-term measures and that proposed in document ISWG-GHG 10/5/3 (Austria et al.) and help decarbonize the sector in line with the 1.5°C temperature goal of the Paris Agreement. Every country and sector should contribute to slowing down and averting the worst impacts of the climate crisis.

2 However, there is a significant risk that the negotiations turn into a prolonged political process, while we have very little time left to act. Ships are already responsible for approximately 3%¹ of global climate pollution, and in the absence of any meaningful climate action at the global, national and local levels this is projected to grow, rising in tandem with

¹ Fourth IMO GHG Study 2020.

increased international trade. At the global level there is a clear imperative for urgent action, and the mid-term measures process is an opportunity for the Organization and its Member States to show ambition and move forward swiftly with effective climate measures.

3 To ensure that any IMO market-based measure that involves carbon pricing (such as an emission trading scheme or a carbon levy) is effective and fair, CSC encourages delegations and stakeholders to acknowledge, respect and operationalize the following principles. The measure must be designed so that it:

A Decreases pollution from ships as soon as possible before 2030, and bridges the price gap between fossil and zero-carbon sustainable fuels

4 If shipping is to contribute to reaching the Paris Agreement's temperature goals, mid-term measures need to have an impact as soon as possible in this decade. This was highlighted in the Intergovernmental Panel on Climate Change (IPCC) Special Report on 1.5°C, which made it clear that climate action across all sectors has to be drastically scaled up pre-2030. The *Fourth IMO GHG Study 2020* shows that even a modest carbon price of \$100/tonne of CO₂e could reduce emissions by 13% by 2030 as ships reduce their speed and/or invest in wind power or other energy saving technologies. Bridging the fleet-wide price gap between fossil and zero-carbon fuels would need prices of above \$416/tonne² by 2050.

5 An IMO carbon price should be set at a level high enough to generate an effective, measurable and direct result, as the shipping sector responds to the price signal, that is commensurate with the scale of the climate emergency. Prices reaching \$400/tonne and more in this decade should be firmly on the table. In addition to a carbon price signal, other complementary policies (such as stringent energy efficiency targets, zero-GHG-fuel standards, targeted revenue recycling) can help to support rapid deployment of technologies to ensure the sector decarbonizes on time.

B Brings the shipping sector in line with the Paris Agreement's 1.5°C target

6 The shipping sector needs to have a transparent and environmentally ambitious carbon budget in line with the 1.5°C target. To this end and in line with the proposal in document MEPC 77/7/3 (Kiribati et al.) ship GHG emissions should reach zero well before 2050 and ideally by 2040.³ A carbon budget related to a carbon levy would be more complicated to implement than an Emissions Trading Scheme cap. The height of a carbon levy does not automatically translate into a total amount of carbon emissions reduced annually (as an ETS cap does), but this problem can be solved by:

- .1 setting a clear long-term decarbonization target with frequent intermediate milestones expressed in absolute emission reduction objectives;
- .2 regular independent scientific review and revision of the size of the levy to ensure it is delivering emission reductions in line with the intermediate and long-term targets; and

² Ibid.

³ According to the International Council on Clean Transportation (ICCT), to have a high likelihood (67% chance) of remaining below 1.5°C, shipping's carbon budget must not exceed 10 GT, and must fully decarbonize by 2040 at the latest. See most recently: Comer, B. (2021). *Zero-emission shipping and the Paris Agreement: Why the IMO needs to pick a zero date and set interim targets in its revised GHG strategy*. International Council on Clean Transportation. Available at: <https://theicct.org/blog/staff/marine-shipping-imo-ghg-targets-global-sept21>

- .3 by having other measures such as a fuel standard and/or medium- to long-term CII targets operating alongside the carbon price.

C Uses revenues wisely to i) support countries most at risk from climate change impacts, and countries and workers most affected by the transition, and ii) invest in decarbonizing the sector by supporting research and infrastructure development and roll-out

7 Carbon pricing not only puts a sorely needed price on climate pollution, it can also raise revenues, and these must be spent wisely.

8 Revenues should be used to address equity and fairness concerns. The Paris Agreement implies that all countries and sectors must decarbonize. However, least developed countries (LDCs) must be shielded from undue burden. Delegations should focus on countries that have low incomes and/or are at greater risk of significant climate change induced harm, especially if these countries bear no historical responsibility for the climate crisis.

9 Instead of exempting such countries from the carbon pricing scheme, they should be supported through earmarking revenues (also known as rebates). These rebates could help finance their climate transition and increase their climate resilience. Rebates should be targeted at those most in need, e.g. low-income small island developing States (SIDS) whose very existence is immediately endangered by climate change and who have no economic means to adapt to its consequences.

10 Carbon pricing revenues could also be used to alleviate socio-economic impacts related to the climate transition, e.g. by funding re-skilling schemes for affected workers.

11 A second priority for using revenues is financing in-sector climate action, including research, innovation and zero-carbon infrastructure, including designing and deploying zero-emission ships. Other examples include supporting the use of renewable energy, developing supply chains for sustainable and scalable marine fuels, and investing in energy savings technologies. The list of potential climate areas to invest in includes:

- .1 proving new technologies on the water in commercial operation with whole ship demonstrations;
- .2 retrofitting existing ships;
- .3 shoreside electrification; and
- .4 investing in R&D, production and supply of sustainable and scalable marine fuels and infrastructure.

12 Estimates of the amount of funding necessary to decarbonize the sector vary widely. Maritime consultancy UMAS estimated⁴ the total capital expenditure investment necessary for decarbonizing the shipping industry by 2050 at \$70 billion to \$95 billion annually between 2030 and 2050. An International Monetary Fund (IMF) working paper⁵ estimates however that a global carbon price of just \$75/tonne in 2030 (increasing to \$150/tonne by 2040) would be able to raise significant revenues, increasing from \$75 billion in 2040 to \$150 billion in 2050. When considering these, it is important to remember that investments in infrastructure will in many

⁴ UMAS (2020), [The scale of investment needed to decarbonize international shipping](#)

⁵ IMF (2018), [Carbon taxation for International Maritime Fuels: Assessing the Options](#)

cases be needed early on to ensure new technologies and fuels are feasible for large-scale deployment. For this reason and given the objectives expressed in principles A, B and C, the carbon price would need to be high from the beginning, instead of starting at a low level and increasing over time.

D Is negotiated and implemented fast without pilot phases to avoid further delays in global action

13 The world needs urgent climate action this decade. IMO needs to move faster. There is no time for protracted negotiations, pilot phases or phase-in periods. The clock is ticking. The mid-term measures, including carbon pricing, should be fully operational as soon as possible, and designed to deliver substantial emission reductions before 2030.

E Does not include offsets, free allocations or generous exemptions that would let polluters off the hook.

14 To have a climate impact, shipping companies must understand and trust that they will pay a real and effective price for their pollution. There should be no free allocation of permits or access to cheap project-based offsetting credits, as these will seriously undermine the system's effectiveness and slow the decarbonization of the sector. The lesson from existing carbon pricing schemes, and especially the EU Emissions Trading System (EU ETS), is clear: cheap offsets and free allocation of emission permits lead to windfall profits and climate loopholes.

15 Allowing offsets to be used for compliance must be avoided at all costs for the following reasons:

- .1 The environmental integrity and additionality of offsetting projects are problematic at best. Öko-Institut⁶ for example, estimates that only 2% of projects under the UN offsetting scheme the Clean Development Mechanism (CDM) were highly likely to be additional. Every project that was not additional, increased emissions globally, as countries and companies relied on these credits to compensate for their own lack of emission reductions.
- .2 An MBM for shipping should reduce emissions in the maritime sector itself, setting it on a path to full decarbonization, and contribute to the world, as a whole, reaching the goals of the Paris Agreement. Offsets and the zero-sum-game logic behind them can only postpone climate action in the sector itself, and siphon funds from the sector.
- .3 They would limit revenues. For the carbon pricing scheme to raise significant revenues, companies must pay an actual price for their pollution instead of buying cheap offsetting credits to "compensate" for their emissions. It would be in the interest of the shipping industry to support carbon pricing that recycles revenues back into the maritime sector, funding the climate solutions that they will use. An offsetting mechanism that might be cheaper in the short term would not help decarbonize shipping in the long run.

16 Exempting States or routes will have significant perverse impacts, as actors game the system to minimize their exposure to the carbon price. This could cause two potential types of regulatory avoidance: re-flagging and re-routing. Both of these will undermine the carbon pricing scheme's environmental effectiveness and could shift air pollution and related health

⁶ Öko-Institut (2016), [How additional is the Clean Development Mechanism?](#)

impacts towards exempted countries and/or routes. Exempting routes or States is therefore not the way forward. The rebates approach mentioned earlier is a more effective way to protect countries and workers that are at risk of adverse impacts.

F Does not undermine other more climate-ambitious regulations internationally, or in countries or regions

17 Some countries and regions, frustrated with slow progress at IMO, are considering their own climate actions for the shipping sector. The most relevant is the EU's plan to include incoming and outgoing ships into the EU ETS. The European Commission has proposed this as part of the *Fit For 55 climate and energy package*. Already in 2020, the European Parliament, which represents 500 million concerned citizens, backed including international shipping to and from EU ports in the EU ETS.⁷

18 What happens if the Organization also adopts a carbon pricing scheme? The difference in climate ambition between the two schemes should be the key issue when addressing this interaction. More environmentally ambitious measures must not be watered down or discarded just because a global measure exists. Countries and regions should retain the right to go above and beyond any international measure. This possibility is explicitly mandated by the port State jurisdiction provision of UNCLOS (Article 211(3)), especially if a state deems IMO action insufficiently effective and not in line with the 1.5°C target. The *Fourth IMO GHG Study 2020* highlights why: emissions from shipping continue to increase, and time is running out.

19 In addition, countries and regions will need to undertake significant climate action on land to enable the decarbonization of the maritime sector. These actions, including infrastructure investment and developing supply chains for sustainable and scalable marine fuels, can only be implemented through national or regional policies. Synergies between direct maritime and maritime-related land regulations can best be achieved through national/regional action and global negotiations should not undermine these complementary efforts.

20 It is also important that prolonged MBM discussion in the Organization do not divert attention away from other effective greenhouse gas reducing measures such as reducing ship speeds, wind propulsion and zero-carbon fuel standards. Carbon pricing alone will not solve the shipping industry's climate problem. For example, some technologies and practices that would save money and emissions are still not widely adopted. Split incentives play a role here and need to be addressed (see document ISWG-GHG 8/3/3 (IMarEST) for a more detailed discussion on this). A carbon price alone will not magically remove all hurdles to implementing these financially beneficial climate solutions; other international, regional and national command-and-control measures will also be needed.

Summary

21 There are various elements that need to be considered when designing a global carbon pricing scheme for shipping. First and foremost, it must deliver emission reductions. A clear, zero-emissions pathway in line with the 1.5°C target is essential, pushing behavioural change, and research and investment towards a zero-carbon maritime transportation sector without delay. The maritime sector should be well on the way to decarbonization by the end of this decade. Offsetting and exempting countries from the scheme would undermine this. Governments within the Organization should not lose sight of the countries and peoples likely

⁷ For more details, see the Carbon Market Watch press release here: <https://carbonmarketwatch.org/2020/09/15/eu-lawmakers-support-the-expansion-of-europes-carbon-market-to-shipping-as-global-talks-are-adrift/>

to be affected most by the measures' economic impacts and by climate change itself. Rebates should focus on ensuring countries, communities and people are not left behind during the transition. There continues to be a strong need for complementary policies to work hand-in-hand with carbon pricing to ensure at scale, fast and sustained uptake of mitigation measures. Carbon pricing will not deliver full decarbonization alone but can provide substantial support for other actions. Therefore, the design of a carbon pricing mechanism must accompany other measures and even support them. Finally, international measures cannot under any circumstances be allowed to undermine more effective climate action at national or regional level.

22 While discussions within the Organization on a market-based measure are only now starting up again and there are few new proposals on the table, CSC is pleased to see that one proposal at least (MEPC 76/7/12 (Marshall Islands and Solomon Islands)) includes a measure that is broadly in line with the principles set out in this submission.

Action requested of the Committee

23 The Committee is invited to consider the above proposals in the context of its deliberations on market-based measures and, in particular, to ensure that any agreed IMO market-based measure:

- .1 decreases climate pollution from ships as soon as possible in this decade, and bridges the price gap between fossil and zero-carbon sustainable fuels;
 - .2 brings the shipping sector in line with the Paris Agreement's 1.5°C target;
 - .3 uses revenues wisely to i) support countries most at risk from climate change impacts, and countries and workers most dependent on shipping, and ii) invest in decarbonizing the sector by supporting research and infrastructure development;
 - .4 is negotiated and implemented quickly without pilot phases to avoid further delays in global action;
 - .5 does not include offsets, free allocations or generous exemptions that would let polluters off the hook; and
 - .6 does not undermine other more climate ambitious regulations internationally, or in countries or regions.
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