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COLLABORATIVE LEADERSHIP ON MARKETS

Last year in December, few people reckoned with the Paris Agreement entering into force within 12 months. But it has been pushed through by a wave of political expression that has seen countries all over the globe mobilising to give their formal consent.

This is unprecedented for an international treaty of this nature. Entry into force for the Kyoto Protocol – the last fortification of the mothership UNFCCC in 1997 – took over seven years to gather the required international backing.

The International Civil Aviation Organisation was reaching agreement on its global emissions market at the same time as the threshold for entry into force of the Paris Agreement was reached, extending an international framework of climate action to one of the last two gaps in its global coverage. The first phase of ICAO's new market-based measure is voluntary but the proportion of emissions growth beyond 2020 to be neutralised is expected to be around 80%¹.

JOINING THE DOTS

These are exceptionally positive headlines for climate action and signal a serious political commitment to lead. Can this now be turned into collaboration on an international carbon market?

Increasingly, the question of national implementation of carbon pricing is becoming “what” or “when”, rather than “whether”. Around 60 countries and other jurisdictions have implemented or have scheduled carbon pricing policies, covering around 13%

of global emissions. Beneath these numbers, however, prices range from less than US\$1/tCO₂e to US\$137/tCO₂e and result from a patchwork of carbon taxes and mostly unconnected trading systems².

With over 90 countries signalling in their intended nationally determined contributions (INDCs) last year that they wish to make use of markets in some way, how much of a drive towards a common vision for markets will we see?

A number of initiatives have been set up in recent years to promote carbon markets. The International Carbon Action Partnership (ICAP) was established in 2007 by governments seeking to share best practices in emissions trading and discuss linking that could lead to a global trading market. It now includes 31 developed countries, regions and cities.

Another relative veteran is the Partnership for Market Readiness (PMR) supported by the World Bank. Eighteen primarily developing countries from all over the globe are working with the support of 13 contributing countries. The PMR is strongly focused on enabling countries to implement carbon pricing policies, and puts serious money and technical support behind these efforts.

SETTING A POLITICAL VISION

These initiatives have filled a primarily technical space in the international collaboration on markets. They have greatly enhanced the understanding of how effective policies can be implemented and how they can link.

The shift toward political emphasis began in the lead-up to the Paris COP as several new initiatives formed as an articulation of cross-country political leadership in the markets space. When the G7 met in Germany on June 2015, it established what is now called the Carbon Market Platform as a home for political and strategic dialogue that can understand differences, close political and institutional gaps, and help facilitate the emergence of new cooperative approaches.

The idea is to keep the platform quite small, though it has been inviting in members beyond the original seven in a bid to include major emitters and developing countries with a clear interest in carbon markets.

Several factors make this platform unique. Being only open to governments, it concentrates on their perspectives. It also targets participation at the director-general level, that is, the highest official in a country's relevant ministry. These people are close to the political debate and understand the constraints in their countries, while also forming a bridge to the expert level.

If all goes to plan, this balance will allow the platform to generate a political vision

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for how an international carbon market can emerge while also helping to create the political will to follow it.

COMMITTING TO INTEGRITY

Another initiative, led by New Zealand, saw 18 countries sign up to the Ministerial Declaration on Carbon Markets immediately after the Paris Agreement was adopted.

Originally prepared as a fallback if markets had not been part of the agreement, the Declaration instead found itself riding the Article 6 wave, and committing these countries to “environmental integrity, transparency and the avoidance of double-counting when market mechanisms are used”.

The Declaration countries have already set to work in mapping out the nature of standards and guidelines that could apply across their market activities and perhaps also the international carbon market. The idea is not to substitute for rules to be agreed via the UNFCCC, but to complement them. The group is embracing the decentralised approach to future markets but wishes to tap into a collective interest in higher levels of integrity and market confidence.

GOING FOR SCALE

Also launched in Paris was the World Bank’s Carbon Pricing Leadership Coalition (CPLC). This brings together 24 countries and more than 90 global companies and other partners. It aims to expand carbon pricing around the world by convening leadership dialogues and mobilising support from business and civil society.

The Carbon Pricing Panel, convened by the World Bank and the International Monetary Fund, is also weighing in. This group, made up primarily of heads of state, is calling for the emissions covered by carbon pricing policies to double to 25% by 2020 and double again to 50% within the decade beyond that.

PRIORITY NEEDS

These new leadership initiatives will have been very complementary if they can deliver both political vision and practical means to ensure the bar is left high for integrity.

There are a number of key facets to this political involvement that should be prioritised. Firstly, in a world where the benefits of carbon pricing are already widely accepted in climate policy circles, the need is now for an ambitious pathway and political rationale for the individual systems of countries to hook up in a truly international carbon market. Ultimately there may only be one global marketplace or there may be several major market hubs. But what the world needs to quickly get away from is the default option of each country doing its own thing with only sporadic linkages that we then welcome as an extra bonus.

Linking trading systems and setting up comparability across crediting programmes is hard work. But beyond the harmonisation of technicalities and balancing of interests, linking is a mindset that requires political readiness to make policy compromises for the sake of a collective benefit. The early work of the US Western Climate Initiative provides interesting lessons in the value of planning for such linking at the outset.

Secondly, there needs to be a clear understanding of how integrity underpins the long-term political and economic value of the market. It is in the interest of all countries to have confidence that what they buy really are genuine reductions in emissions that have not caused harm in a local community somewhere. This needs to find concrete expression in common principles, standards and guidelines that are meaningful when operationalised, and that enable countries to hold each other to account.

Thirdly, there is a need to define more tangibly how markets can strengthen mitigation ambition. We understand that more cost-effective reductions can enable greater

action, but in practice stronger targets may not eventuate or the causality may not be clear. Political commitments on the use of markets can however be directly linked to announcements of increased mitigation.

Crediting mechanisms can also be used to reduce emissions beyond what countries have already said they will do under the Paris Agreement. However, crediting requires some portion of reductions to not be used as offsets, or it risks being little more than moving emissions around. How crediting should contribute to “overall mitigation” is controversial, but it is in urgent need of resolution. One way of helping could be to integrate results-based climate finance, which results in reductions that should not be used for offsetting, into the funding mix to leverage private capital.

Giving certainty to a long-term rise in ambition for mitigation is perhaps the greatest contribution to effective carbon markets that governments can make. It gives a solid basis for expectations to form regarding long-term carbon prices and emission paths, allowing serious investments and climate action to be unlocked.

Dealing with issues like these, focused political groupings of countries have the potential to achieve what is difficult to reach in the much broader and more diverse forum of the UNFCCC. They can build upon the minimum standards that the UNFCCC lays down by seeing where countries have a common incentive to raise the bar higher and quicken the progress to a well-functioning and well-connected international carbon market.

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(1) International Air Transport Association (2) World Bank, Carbon Pricing Watch 2016