Carbon Pricing in Paris

Empowering change with the power of markets

- **The Paris 2015 Climate Summit can prompt a sustained wave of business action and investment through carbon markets.** In the past year, hundreds of governments and businesses have sounded a call for carbon pricing to stimulate transformative investments in climate action. The Paris Agreement should secure a sound foundation for carbon pricing, implemented via technical decisions on market elements.

- **The Agreement should support countries interested in using international market linkages to achieve more ambitious emissions reductions.** Networked carbon markets perform better, environmentally and economically, enabling nations and businesses to better manage the transition to a cleaner economy. The Agreement should contain a provision enabling Parties to transfer units between pricing systems under a transparent accounting framework.

- **The Paris Conference of the Parties (COP) should adopt Decisions to establish a unified project crediting mechanism and market tools to assist countries in achieving their Intended Nationally Determined Contributions (INDCs).** Developing countries can move to low-carbon pathways faster with the right set of market mechanisms and tools. Governments present at the Paris negotiations need to adopt a decisions to unify the array of crediting mechanisms under negotiation, including the CDM, JI, the New Market Mechanism and REDD+, into a coherent new crediting system. Parties should commit to adopt rules and modalities to make this new system operational by 2017.

- **Paris must deliver continued support for the healthy growth of the Green Climate Fund (GCF).** The Fund can become a valuable source of finance for developing countries to achieve their mitigation and adaptation goals. Working alongside market mechanisms, the GCF can multiply the effectiveness of private sector capital in financing low-carbon projects and programmes. It can "de-risk" investments in developing countries and accelerate clean development.

- **IETA's Straw Proposal offers an example of how market provisions could be featured in the Paris package.** Markets could grow from a simple provision in the Agreement, with detailed implementation rules specified in COP Decisions. A revitalised crediting mechanism could unleash greater action in developing countries – and a set of market-development tools could

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strengthen the capabilities in developing countries in launching their own market systems.

Background

Emissions trading is a policy tool designed to deliver an environmental objective at lower cost than traditional regulation. It allows covered entities flexibility to achieve reductions where they are most cost effective. Worldwide, governments are implementing greenhouse gas (GHG) emissions limits using trading flexibilities. Currently, 40% of global GDP is covered by emissions trading systems.[1] Still others use carbon taxes with use of carbon credits for cost containment.

For Parties to achieve the goal of limiting global warming to 2°C, they need the advantages of flexible market-based policies. If the Paris Summit produces no clear guidance and architecture on international carbon markets, it could result in fragmented actions and weak signals on carbon pricing.

There is broad authority for cooperative action under the UN Framework Convention on Climate Change (UNFCCC). But it offers no specific compliance structure or detail on how Parties should develop, account for and report on cooperative actions. That is why the Kyoto Protocol defined a clear market structure for the 2008–20 period.

For the post-2020 period, negotiators are pursuing a governance model that attracts action by every nation through a "pledge and review" system. Each nation **pledges** action in an INDC. Its performance is reported regularly and subjected to **review** of its effectiveness towards the global objective. In this system, it will be essential to account for units transferred across borders to avoid double-counting. More importantly, the ambition of a nation's pledge often depends on whether it can access international markets and the financial flows attached to these.

As more jurisdictions introduce policies that strengthen GHG emission limits over time, an international framework to support market linkages becomes more important. Linked markets would lower costs, avoid economic disruptions and encourage the harmonisation of policies to reduce risks to competitiveness. **The Paris Agreement must include language that encourages countries to cooperate in meeting their mitigation commitments through market linkages.**

Pricing Priorities for the 2015 Agreement

The Agreement should establish a unified international transfer system. Interested Parties would use the system to transfer units from their INDCs to other Parties. The system would assure transparency through accurate accounting rules for imports and exports of units. The operational elements of the transfer system would be elaborated in later Decisions, including rules and

[1] ICAP Status Report 2015

modalities on accounting, transfers and operation of a centralised crediting mechanism.

IETA's Straw Proposal outlines how such a system could fit into the Paris Agreement. This language would encourage countries to cooperate through a transfer system to meet the mitigation commitments in their INDCs. For many countries, the system would provide market access that could enable a greater level of contribution – ie, emissions reductions – than acting alone.

Pricing Priorities for COP21 Decisions

In addition to the Paris Agreement, future Decisions need to provide clarity on various aspects of the implementation of the Agreement, including clarity on the role and function of international market infrastructure.

Decisions are necessary in several areas to support robust contributions from Parties using market instruments. These elements are elaborated further in IETA's Straw Proposal.

- **A work-plan should establish rules and modalities for the unified international transfer system.** This plan would provide the details on how to define, register, track and account for valid units in the transfer system.

- **The transfer system should be grounded in transparent accounting.** Total transfers and receipts should be recorded in national reports to the UNFCCC. Standardised GHG emissions' accounting and reporting provisions should be elaborated to establish systemic integrity, including to safeguard against "double-counts" or "counterfeit" credits entering the system.

- **The transfer system should include a unified project crediting mechanism, drawing together the CDM, JI, New Market Mechanism and REDD+.** This mechanism should make high-quality project-based reductions broadly available for Parties to use for their national contributions. The Agreement should accelerate work on firm deadlines to produce detailed guidelines, modalities and procedures for this facility to assist in enabling early action.

- **The transfer system should include a centralised UN registry for use by interested Parties as well as a function to connect independent national or international registries.** It should be made available for potential use by both national and subnational institutions that may devolve mitigation responsibilities to private sector entities. It may also be useful to buttress this system with other market tools, such as standardised baselines and reporting protocols. It may also contain the existing international transaction log or a comparable tracking system, expanded to cover a wider range of unit types.

- **Land-use mitigation is essential to avoiding dangerous climate change.** Existing agreements on LULUCF and REDD+ should be recognised and integrated into the centralised crediting and transfer system.

- **Linking climate finance to results is essential to stimulate greater funding.** Similar technical measures for reporting and accounting for emissions reductions should be employed in climate finance arena, making it simple for private entities to join in public-private climate finance partnerships.

Looking Ahead

It is clear that our work does not end in Paris. COP21 marks the beginning of the next chapter of global climate policy, setting the stage for the next generation of global markets. We must ensure the right foundations and investment signals are laid in Paris so that work on implementing the Agreement can efficiently progress.

If realised in the Paris Agreement and Decisions, the elements outlined above will help set us on the right path to meet ambitious climate goals at least-cost to business, communities and the global economy far into the future.

For more information and resources about the design and benefits of a global emissions trading market, please see ***www.ieta.org***

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IETA is a non-profit business organisation *created in 1999 to establish a functional international framework for trading in greenhouse gas emission reductions. Our membership includes leading international companies from across the carbon trading cycle. We seek to develop an emissions trading system that results in real and verifiable greenhouse gas emission reductions, while balancing economic efficiency with environmental integrity and social equity.*