



WORKING PAPER

**HIGH-LEVEL MEETING ON A GLOBAL MARKET-BASED
MEASURE SCHEME**

Montréal, 11 to 13 May 2016

Agenda Item 1: Review of draft Assembly Resolution text on a global MBM scheme for international aviation

**KEY MESSAGES FROM IETA ON GLOBAL MARKET-BASED
MEASURE DESIGN**

(Presented by the International Emissions Trading Association¹)

EXECUTIVE SUMMARY

This paper presents key messages from IETA on a Global Market-based Measure design.

1. INTRODUCTION

1.1 The International Emissions Trading Association (IETA) welcomes this opportunity to submit a Working Paper for consideration at ICAO's High-Level Meeting (HLM) on a Global Market-Based Measure (MBM) on 11-13 May 2016. IETA's reflections and action-oriented recommendations are intended to inform HLM discussions and assist ICAO's broader MBM design efforts.

1.2 IETA views the global MBM as an important contribution to address climate change. At the 39th Session of the ICAO Assembly, IETA encourages the adoption of a global MBM resolution so it can enter into force by 2020. It is important to avoid "reinventing the wheel" in design of the global MBM. Instead, ICAO is well poised to use existing carbon market mechanisms and lessons learned from earlier carbon markets in designing the global MBM. We hope to send a clear message to ICAO that existing carbon markets are ready to support the aviation sector in cost-effectively reaching its carbon neutral growth target.

¹ ABOUT IETA. IETA is dedicated to the establishment of market-based trading systems for greenhouse gas emissions that are demonstrably fair, open, efficient, accountable, and consistent across national boundaries. IETA has been the leading voice of the business community on the subject of emissions trading since 1999. Our 130 member companies include some the world's largest industrial and financial corporations—including global leaders in oil & gas, mining, power, cement, aluminum, chemical, pulp & paper, and investment banking. IETA also represents a broad range of global leaders from the industries of data verification and certification; brokering and trading; offset project development; legal and advisory services. For more information about IETA, visit www.ieta.org.

2. STRONG KEY ELEMENTS IN GLOBAL MBM DRAFT RESOLUTION

2.1 IETA believes the draft ICAO resolution dated 11 March meets many of the criteria that we consider important in designing environmental markets. We share the objective that the system should achieve the desired environmental goals while minimising compliance costs.

2.2 Specifically, there are various features of the draft that we believe will enhance administrative simplicity and cost-effectiveness for aircraft operators:

- a) The draft resolution establishes a single market for the aviation sector. This approach will enhance efficiency and minimize an inefficient and costly patchwork of different compliance systems around the world. As such, the draft resolution would establish a price on carbon for the aviation sector to help drive investment in greenhouse gas (GHG) mitigation.
- b) The mechanism established by the draft resolution would assure adequate supply by leveraging existing infrastructure and capacity. It would enable broad participation of GHG standards and programs that meet the Emissions Unit Criteria (EUC) set out by ICAO. It would also recognize a suite of existing high-quality GHG offset standards, which cover a wide range of project types and use standardized baselines with approved measurement and verification protocols. We do not believe that simply adopting a single offset scheme is necessarily appropriate, because competition amongst schemes will deliver supplies, drive efficiency, lower overall costs and spur innovation.

3. ELEMENTS REQUIRING REVISION IN GLOBAL MBM DRAFT RESOLUTION

3.1 At the same time, we believe that the draft resolution could benefit from several changes that are important to building a robust and effective global MBM. IETA's proposed changes, outlined below, would help to ensure environmental integrity and efficient functionality from program outset. We also note explicit support for the inclusion of forestry credits to bolster supply from an important asset class.

- a) To improve environmental integrity of the future program, the language in paragraph 18 should require GHG programs to meet the EUC to gain recognition in the global MBM, as opposed to simply promoting its use. If the program accepts offset credits that do not meet the EUC, it could undermine the environmental integrity of the initiative. In addition, the proposed text makes only a passing reference to double-counting and also describes preferences that ICAO may want to encourage and promote. IETA recommends that there be a single paragraph addressing environmental integrity, specifically requiring that participating GHG programs meet the EUC and clearly indicating that all offset units used by the aviation sector must be accounted for in the host country's national accounts. It should also specify that it will not allow double-counting of GHG reductions that have been used by Parties to meet Intended Nationally Determined Contributions (INDCs) under the UN Paris Agreement.

Fundamentally, the integrity of the global MBM requires that offsets are real, permanent, quantifiable, verifiable, and additional. We support the proposed recommendations for offset programs, although more consideration may be needed to clearly define the criteria for “safeguarding systems to address environmental and social risks” and for “sustainable development criteria” for offset programs. We support CAEP’s recommendations for the offset credit criteria, but would suggest a careful approach in defining the meaning of “no net harm”. A definition that is ambiguous and overly broad could ultimately hinder the creation of credible offsets that provide robust co-benefits.

- b) Draft resolution language should be tightened to enhance policy certainty and confidence in the global MBM. For example, terms such as the global MBM being used as a “gap filler” in paragraph 3 could create uncertainty amongst market participants. The wording in paragraph 15 related to cost safeguards lacks specificity in terms of what might be considered an “excessive pricing of emissions units” and what type of intervention might be expected. In addition, the draft resolution refers to a 3-year periodic review of the global MBM. Market participants will need to understand what these terms would mean in practice.
- c) The proposed text has no clear language that would encourage early action. There is a reference to “early movers” in paragraph 9, which presumably refers to those airlines that would purchase and retire offsets before the first compliance period. However, there is no explicit early banking provision. IETA recommends including language in the resolution that would explicitly allow airlines to begin accumulating (or “banking”) offsets from accepted programs prior to the first compliance period. We suggest eliminating the language in paragraph 9 which denies adjustments for operators that do so. Allowing for early action would help resolve early challenges related to the global MBM, including:
 - 1) Providing an important signal to investors and project developers, enabling them to make the necessary investments in project activities.
 - 2) Enabling the airline industry to engage with the carbon market and learn how best to operate within a compliance system based on environmental markets.
 - 3) Enabling governments to put in place systems for accounting for emission reductions being used by the aviation sector, particularly given that all countries participating in the Paris Agreement will have INDCs, many of which are denominated in tonnes of carbon dioxide equivalent (CO₂e).
- d) Forests play an important role in regulating emissions in the atmosphere. Forest-related activities can be an important source of high-quality reductions. As such, we recommend that the resolution include language enabling “Reduced Emissions from Deforestation and Degradation” (REDD+) as an option for aviation to meet the goals of a global MBM.

Concerns over the inclusion of REDD+ credits relating to non-permanence, leakage, and double-counting have been addressed in existing carbon markets, such as California’s forest offset protocols and the “Jurisdictional” or “Nested REDD” programs of the Verified Carbon Standard (VCS) and American Carbon Registry (ACR). These systems provide appropriate rules and guidance to assure delivery of

high-quality units. For example, questions over non-permanence can be addressed using the JNR Non-Permanence Risk Tool, which defines how to establish a buffer account and address leakage concerns. Double-counting can be managed by establishing a national registry for emissions reductions. As with other asset classes, when REDD+ credits are sold into the global MBM market, the emissions reductions should be recorded in the host country's national registry and retired to avoid double-counted towards the country's national climate commitments.

- e) We also believe that forest recovery should not merely be “complementary”, as suggested in the draft resolution, but a crucial part of the transition to a low-carbon economy. Forest recovery offers valuable benefits as a mitigation pathway in terms of scale, speed, and cost. These actions also require relatively low start-up and management costs (important considerations in the draft resolution under paragraph 15).

4. ISSUES FOR FURTHER CONSIDERATION IN GLOBAL MBM DESIGN

4.1 Two items for further consideration and clarification by ICAO to support global MBM design:

- a) Multiple sources of credits. IETA supports an inclusive approach for identifying possible sources of eligible offset credits. We believe that multiple sources of credits from a broad pool of regions and sectors can help control costs and limit price volatility. As many offset systems are currently in use or under development, the global MBM should not discourage such efforts for sources of credits that meet the EUC. However, if positive or negative lists were to be established, the standards and project types must be defined as soon as possible, and the process clarified to approve new standards and project types or suspending formerly approved ones. Similar considerations exist about whether or not to allow offsets from States that are exempt from the global MBM. If geographic restrictions are established, careful consideration must be paid to the compliance cost impacts of using such restrictions.
- b) Harmonized reporting process and centralized registry. A harmonized and transparent process for submission of verified emissions by airlines to States, and from States to ICAO, should be developed promptly. A procedure is also needed to clarify ICAO's empowerment to request clarifications in the event of incomplete or inconsistent submissions. IETA recommends use of a centralized registry, instead of one per State. The centralized registry would track ownership of units, enable trading between account-holders, safeguard against double-counting or theft, facilitate compliance and provide regular public reports.

5. GUIDING PRINCIPLES TO DESIGN AN EFFECTIVE GLOBAL MBM

5.1 To help guide ICAO's global MBM design efforts and discussions, including those at the HLM in May 2016, we offer the following basic principles to creating an effective carbon market:

- a) Long-term, science- and environmentally-based goals should be set.

- This assumes a clear and stable regulatory regime that drives a stable market.
 - Supply and demand should create a dynamic market that drives the price.
 - Clear rules will provide confidence to participants and investors.
- b) An open and broad market will perform the best.
- The design should promote broad participation to enhance liquidity.
 - An open market will allow entities to hedge their exposure and minimize costs.
 - Use of existing offset standards and asset classes will help assure adequate supply.
- c) Sound market infrastructure should undergird the system.
- Solid measurement, reporting and verification techniques build confidence amongst market participants, regulators and other stakeholders.
 - Market information should be made available in a fair and transparent manner.
 - The registry must operate efficiently and securely.

6. CONCLUSION

6.1 We appreciate ICAO taking into consideration this input by carbon market experts and practitioners. IETA looks forward to participating as an Observer at the upcoming High-Level Meeting in Montreal, and we stand ready to work with ICAO to support the development of a robust and effective global MBM for the international aviation sector. If you have any questions, or require further information related to IETA's input, please contact sullivan@ieta.org or deblock@ieta.org.

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