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'I' ITEM NOTE

From: General Secretariat of the Council
To: Permanent Representatives Committee (Part 1)

No. Cion doc.: 11377/21
No. prev. doc.: 11620/21

Subject: Draft submission by Member States and the Commission to the 77th session of the Marine Environment Protection Committee of the International Maritime Organization proposing guiding principles for the further development of Market-Based Measures
– *Endorsement*

I. INTRODUCTION

1. On 7 September 2021, the Commission transmitted to the Council a Staff Working Document containing a draft submission to the 77th session of the Marine Environment Protection Committee (MEPC 77) of the International Maritime Organization (IMO) proposing guiding principles for the further development of market-based measures (MBMs). The deadline for transmitting the draft submission to the IMO Secretariat is 17 September 2021.
2. The purpose of the submission is to invite MEPC 77 to agree on the use of a set of basic guiding principles for the further development of any MBMs. The proposal builds on the list of criteria identified in IMO document MEPC 76/7/15. This document focused on the importance of starting work on mid-term GHG reduction measures that incentivise the use of sustainable low-carbon and zero-carbon fuels in international shipping. The present draft submission develops them further to address specific issues related to market-based measures.

The aim is to use the proposed criteria to guide and enhance future discussions on carbon pricing measures, namely a GHG levy and a cap-and-trade scheme.

II. WORK WITHIN THE COUNCIL

3. The draft submission was orally presented by the Commission at Shipping Working Party on 1 September 2021, before an advance copy reached the delegations on 3 September 2021¹ and the Commission Staff Working Document was officially transmitted. The draft submission was examined at two meetings of the members of the working party on 8 and 13 September 2021. Further to that last meeting, an informal silence procedure was launched on a Presidency compromise proposal², in view of reaching consensus. No delegation broke the silence procedure and consensus was reached on the substance of the draft submission that also allows the Presidency to indicate at the time of transmission that the document may be released to the public by the IMO secretariat prior to MEPC 77.
4. However, there is no agreement on who should submit the draft submission. The Commission maintains the view that the draft submission should be made by "the European Commission on behalf of the European Union", while the Member States consider that it should be made by the Member States and the European Commission.
5. Given the importance of the matter, it was agreed at working party level to propose to transmit the submission in the name of the Member States and the European Commission, while taking good note of the position of the Commission.

III. CONCLUSION

6. In the light of the above, the Permanent Representatives Committee is invited to endorse the text of the draft submission in the annex, with a view to its transmission by the Presidency to the International Maritime Organization by 17 September 2021.

¹ WK 10344/2021.

² ST 11620/1/21 REV 1.

MARINE ENVIRONMENT PROTECTION
77th session
Agenda item 7

MEPC 77/7/X
17 August 2021
Original: ENGLISH

Pre-session public release:

REDUCTION OF GHG EMISSIONS FROM SHIPS

Proposal on guiding principles for the further development of Market-Based Measures

Submitted by Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the European Commission

SUMMARY

Executive summary: This document suggests a number of criteria for assessment and comparison of carbon pricing measures. It builds on the list of criteria identified in MEPC 76/7/15, developing them further to address specific issues related to market-based measures. The aim is to use the suggested criteria to guide and enhance future discussions on carbon pricing measures, namely a GHG levy and a cap-and-trade scheme.

Strategic direction, if applicable: 3

Output: 3.2

Action to be taken: Paragraph 22

Related documents: MEPC 76/7/15, MEPC 76/7/42, MEPC 76/7/12, MEPC 76/7/2, MEPC 62/5/1, MEPC 61/24

Introduction

1 In order to have a chance to meet the minimum levels of ambition of the IMO Initial Strategy on Reduction of GHG Emissions from Ships, a transition from fossil fuels to renewable and low carbon fuels needs to start well before 2030. To accomplish this, measures to incentivise the use of these fuels and make them available in the market should apply as soon as possible and by the middle of this decade.

2 In order to progress effectively with the next package of such measures, MEPC 76 adopted a work plan for the development of mid- and long-term measures, which as its first phase will collate and consider proposals for measures.

3 The first phase of the work plan should be concluded in spring 2022, and should table various proposals for mid- and long-term measures in order to be able to understand and compare their main features and implications and identify the key issues to consider in relation to each proposed measure.

4 Several candidate measures listed in the Initial IMO Strategy address alternative fuels both as short-, mid- and long-term actions. A central candidate measure listed as mid-term action is new/innovative emission reduction mechanism(s), which possibly includes market-based measures (MBMs).

5 The need for mid-term measures to incentivise the uptake of renewable and low carbon fuels in international shipping was highlighted in several documents, including MEPC 76/7/15. The submission described two types of measures, market-based and standard-based measures respectively, which on their own or in combination could ensure that shipping decarbonises and that zero-emission vessels enter the fleet by the middle of the decade. The current document follows up on the market-based measures with carbon pricing as their main purpose, such as a GHG levy (as also proposed in MEPC 76/7/12) and a cap-and-trade scheme for maritime GHG emissions (as also proposed in MEPC 76/7/2). Standard-based measures are further elaborated in other documents, such as the Low GHG Fuel Standard, as proposed in ISWG-GHG 10/5/3, and a Carbon intensity standard, as identified in MEPC 76/7/2, which would build upon the recently approved CII and its rating scheme.

6 The need to consider carbon pricing measures and/or fuel standards was also supported in MEPC 76/7/42. This document stated that the most important market failure related to zero-carbon shipping is lack of commercial viability compared to conventional shipping. This is caused by the fact that negative side-effects, i.e. the externalities of conventional fuels, such as its GHG emissions and air pollution, are not included in the price of the latter. A pre-requisite for the assessment of the GHG impact of shipping should be a Lifecycle Assessment (LCA) covering the full Well-to-Wake GHG emissions from shipping, as further elaborated in document ISWG-GHG 9/2.

7 It is clear that the Committee has now entered a phase in which discussion on innovative reduction measures is becoming increasingly multi-dimensional and the proposals will entail several new key issues for IMO Member States and observer organizations to consider.

8 This is especially the case for the development of carbon pricing measures, which are complex in nature and may imply complex legal considerations and discussions, as was the case in the previous experience at IMO (e.g. MEPC 62/5/1).

9 Therefore, in order to pave the way for an effective decision-making process, and to facilitate an effective decision-making process in a technically and legally complex domain, the co-sponsors consider that it is of utmost importance to first consider a set of criteria against which market-based measures can be assessed and compared. This will ensure that the IMO focuses on measures, which are not only feasible and equitable but also effective and efficient in living up to the agreed level of ambition of the Organization.

10 MEPC 76/7/15 already listed six main criteria to assess any future mid-term measures, be it MBMs, standard-based measures or a combination thereof. Given the complexity of carbon pricing measures, the European Union developed a set of additional and more specific criteria for MBMs detailed in the next paragraph. These are important to keep in mind and have been also inspired by MEPC 61/24.

11 In light of the aforementioned considerations, the co-sponsors are of the view that any proposal for a carbon pricing measure should be evaluated based on the extended and more detailed list of criteria:

- .1 MBMs should create significantly effective, clear and measurable response to the climate strategy in form of reduced GHG emissions.

.2 MBMs should place a price on GHG emissions following the polluter pays principle and provide an economic incentive for the maritime industry to reduce their GHG emissions.

.3 MBMs should send a clear signal to the market on the future regulation and timetable of decarbonisation. This would provide clear long-term price trajectory aiming at initiating the use of renewable and low carbon fuels in international shipping by the middle of the decade and then steadily increasing their use in international shipping.

.4 MBMs should be goal-based with the aim to encouraging fuels and technologies that provide for effective emissions reduction.

.5 The administration of MBMs should be transparent, effective, easy to implement and enforceable to prevent fraud.

.6 MBMs should be designed to be flag-neutral and they should equal treatment of all operators.

.7 MBMs should be cost-effective.

.8 MBMs should not be duplicative. In case of any national or regional action by member States to further accelerate GHG emissions reduction from shipping, double counting of CO2 emissions should be avoided.

.9 For revenues generated from MBMs, significant funds should be used to support maritime climate mitigation and adaptation activities, in particular in developing countries, in order to ensure a globally effective and fair transition.

12 Criteria 1, 2 and 3 would require that the MBM imply a clear incentive for the reduction of GHG emissions, while also implying a clear timetable for GHG reduction. This would provide certainty for investments in ships, fuels and infrastructure.

13 Criterion 4 should ensure that any future MBM focuses on the goal of effectively reducing GHG emissions from ships without favouring or excluding the use of any specific renewable and low carbon fuels or technologies.

14 Criterion 5 should ensure that future MBMs would be designed to work in a transparent way both for industry and for IMO Member States as regulators keeping administrative cost for both industry and regulators at a minimum level. Furthermore, it should also be as easy to administer as possible for all actors and it should be designed in a way that makes the MBM enforceable in a practical and fraud free manner.

15 Criterion 6 should ensure that any MBM adhere to the principle of flag neutrality and No More Favorable Treatment (NMFT) and that market actors are treated equally on the same route.

16 Criterion 7 addresses the issue of cost-effectiveness so that the measures should aim at creating reduction in GHG in an effective way, minimising the cost for the society per ton of GHG emission reduced.

17 Criterion 8 addresses the need for any MBM to take into account national or regional MBMs by IMO member States to further reduce GHG emissions reduction from shipping, such as the proposed extension of the EU Emission Trading System to maritime transport. This would allow that some States increase the level of ambition at a higher speed. In the case of co-existence of schemes, double counting of emissions should be avoided.

18 The last criteria addresses the issue of revenues generated by an MBM. It should be

ensured that significant funds are used to support shipping decarbonisation in particular in developing countries. The revenues could be used to, e.g.:

.1 Reduce cost of GHG reduction for the maritime sector, in particular in developing countries. This could primarily include actions, which would lower the cost of climate change for the industry e.g. R&D, fuel infrastructure, fuel production etc. This would also address the lack of commercial viability as the most important market failure related to zero-carbon shipping.

.2 Assist and support, as appropriate, vulnerable developing countries, especially SIDS and LDCs. This could be done in the form of technical assistance, infrastructure investments, fuel production, targeted subsidies etc. This should also be seen in the context of the work on impact assessment and disproportionately negative impacts.

3. Mitigation of environmental impacts from maritime emissions e.g. support for maritime environmental and/or climate projects.

Proposal

19 As a central candidate mid-term measure, MBMs would need to be in force as soon as possible around the middle of this decade in order to ensure that the first zero-GHG fuelled ships enter the fleet well before 2030.

20 This will only be feasible by following the steps agreed in the work plan for mid-term measures adopted by MEPC 76. Furthermore, it should also be ensured that the MBMs taken forward are feasible, effective and efficient in implementing the agreed level of ambition of the Organization.

Action requested of the Committee

21 The Committee is invited to agree on the use of the set of basic guiding principles listed in paragraphs 11.1 to 11.9 of this document for the further development of any MBMs.
