

WORKSHOP REPORT

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Multijurisdictional Approaches to Carbon Pricing: Integrating Design Elements for a Low Carbon Club

On December 4, 2015, the Stanley Foundation and Climate Strategies co-hosted a workshop in Paris where experts from academia, industry, government, and international organizations convened to foster a greater understanding of multijurisdictional approaches to carbon pricing within the context of a low carbon club. This summary reflects the organizers' understanding of ideas presented by workshop participants and is intended to capture only key elements of the daylong discussion. Therefore, this summary does not reflect all discussion points put forward during the workshop, nor does it imply consensus among participants.

The aim of this workshop was to build on discussions started at the second Global Climate Policy Conference, organized by the Stanley Foundation and Climate Strategies and held in spring 2015 in New Delhi, India, and continued in two subsequent workshops. The first resulting workshop was hosted by the Stanley Foundation, Climate Strategies, the International Centre for Trade and Sustainable Development, and the Institute for Sustainable Development and International Relations in July and focused on the definition and role of, and interest in developing, low carbon clubs. The second discussion was held at the Stanley Foundation's 56th Strategy for Peace Conference in October and focused on designing elements for a robust carbon pricing club.¹

The December workshop was strategically held parallel to the two-week 21st Conference of the Parties to the United Nations Framework Convention on Climate Change (UNFCCC). On Saturday, December 13, close to 200 nations came to a consensus on the world's first international climate deal in close to two decades. Formally titled the Paris Agreement, this landmark success embodies the participation, through the submission of nationally determined contributions (NDCs)—or statements of intended climate action starting from 2020 through a nationally determined period of time—of more than 185 countries. At the start of this round of negotiations, the submitted NDCs included over 90 government proposals for some form of a price or pricing mechanism on carbon.²

Signals for Clubs and Markets

The NDCs in the Paris Agreement cultivate a bottom-up approach to climate governance that encourages national and subnational action in order to accelerate ambition and achieve the long-term goal set forth in Article 2 of the agreement. In addition to provisions detailing action for mitigation, adaptation, technology transfer, and finance, among others, the Paris Agreement set forth innovative approaches to multijurisdiction cooperation and the use of market mechanisms to achieve national climate targets.³

For example, the Paris Agreement references the ability of countries to use "cooperative approaches" to achieve national targets, language warmly welcomed by many experts involved in the carbon clubs discussion. By including this language on cooperative approaches, the Paris Agreement establishes a road map within the

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The rapporteurs and organizers prepared this report following the conference. It contains their interpretation of the proceedings and is not merely a descriptive, chronological account. Participants neither reviewed nor approved the report. Therefore, it should not be assumed that every participant subscribes to all recommendations, observations, and conclusions.

UNFCCC multilateral framework for countries with markets to cooperate bilaterally, plurilaterally, or multilaterally.⁴ In addition, the accompanying COP Decision to the Paris Agreement includes several provisions encouraging and welcoming the participation of nonparty stakeholders, including cities and subnational governments, in facilitating the implementation of climate policies. This opens the door for countries and nonparty actors to form and participate in a low carbon club, also referred to in this context as a multijurisdictional cooperative approach (MCA), and is an attempt to put to rest the concern that MCAs are in conflict with the UNFCCC process. This reflects the notion agreed on by workshop participants that the UNFCCC and MCAs are to be seen as complementary to one another in order to be successful.

Club Goals: Carbon Pricing, Ambition, and Technology

There was a consensus among participants in the workshop that the central goal of an MCA must be to increase the ambition of national and subnational governments' emissions reductions over time. The current NDCs are predicted to put global temperatures on a trajectory of 2.7 degrees Celsius of warming.⁵ While the Paris Agreement does include a scaling up of targets every five years, the agreement does not go into effect until 2020, thus leaving room for further and faster mitigation action from coalitions of the willing.

Several participants agreed that ambition could be increased through technological innovation in key sectors, including gas, electricity, oil, and mining. Discussion revolved around two central challenges that prevent innovation in these sectors: funding and limited market pull. An MCA with a carbon pricing element could create a market that overcomes these two challenges. Carbon markets are intended to generate revenue that could be shared among club members to increase funding for research and development in these sectors, which would spur innovation. A credible and strategically growing carbon market would accelerate technological uptake. This would help climate-friendly technologies overcome the so-called technology valley of death: the vast chasm that divides applied research and commercialization of a product. The subsequent economic gains of these innovations could theoretically be shared among producers, the public sector, the private sector, and consumers. Participants showed interest in this type of club with a carbon pricing focus that invests generated revenue in technological innovation and that would therefore be perceived by producers and consumers as a tax that provides an additional benefit rather than solely being a cost. A clear benefit to this approach for club members would be increased technology transfer; however, questions were raised regarding the feasibility to implement, the role of intellectual property rights law, and the equitable distribution of raised revenue. Some participants also voiced concern that requiring carbon pricing as a prerequisite to a low carbon club could limit country participation.

Global Carbon Market?

Growing support for carbon markets around the world could influence the discussion on whether carbon pricing should be required of a national or subnational government to join an MCA. According to a recent World Bank Report, 40 nations and 23 states, regions, or cities have implemented or have plans to implement either a carbon tax or emissions trading, a doubling of such schemes since 2012.⁶ Workshop participants discussed the inherent differences in these markets around the globe. For instance, these market approaches vary significantly with regard to carbon price, sectors included, and use of international offsets. Some countries, like New Zealand, remain dedicated to the Kyoto-era carbon market rules established by the UNFCCC while others, like Japan, have created their own unique mechanisms. Many experts see the large mitigation potential and efficiency gains that could be achieved by linking these markets; however, the current patchwork of regulations makes trade among schemes extremely challenging.

Participants contemplated a presentation about how MCAs could begin to shape a globally connected carbon market through a program currently spearheaded by the World Bank called the Networked Carbon Markets (NCM). The NCM explores and is aiming to develop the services and institutions needed to create an international carbon market that can accommodate and smooth linkages between unique emissions reductions systems. The goal of the initiative is not to create a global carbon price but to put a price on carbon that reflects countries' differing national circumstances.⁷

Participants discussed how such systems and services could provide a platform for knowledge sharing and ease the creation and implementation of carbon markets within a club framework. Several members mentioned how the NCM recommendations could incentivize countries on the fence about an MCA to institute a system that encourages linking and trading among members. However, participants voiced concerns that there is a lack of evidence to support whether countries would join the club based solely on the benefits of the trading system. To illustrate this point, an example of an existing club, the International Civil Aviation Organization (ICAO), was presented to the group. ICAO began with the broad club objective to reduce the carbon footprint of the aviation industry and later progressed toward solutions leveraging markets and trading. Club members are currently developing the criteria for a global, market-based mechanism that will be introduced and voted on in the 2016 ICAO general assembly. This example supports some participants' views that a club should first be made available to a wide number of participants with a broad vision, and then specifics on markets and trading can be created once there is an initial buy in.

Participants also discussed the role of corporations and subnational actors, including states, cities, and universities, in forming MCAs, setting carbon prices, and linking markets. Several challenges were mentioned, including integrating proper design elements into the carbon pricing mechanism and issues regarding compliance and accountability. There

was consensus among members that there must be a common set of rules among jurisdictions in an MCA on how to treat carbon as a trading commodity, in addition to forming other goals and objectives. Participants also agreed that the level of ambition among participating jurisdictions must be uniform in order for countries to enter into an MCA and prevent free riding by participants. The Non-State Actor Zone for Climate Action platform through the Lima-Paris Action Agenda was mentioned as a potential short-term home for MCAs to showcase their ambitions. It would, however, be necessary to clarify what criteria would be required for a club to be included in this platform.

While many questions remain to be answered, many experts are optimistic that this new international market framework will support carbon market linkages within MCAs. In addition, many seasoned observers hope the governing bodies of a centralized market mechanism will not repeat the mistakes of the past but learn from previous missteps such as those taken by actors on Joint Implementation and Clean Development Mechanisms of the Kyoto Protocol.

MCA Approaches for Developing Countries

In past workshops, participants noted that the discussion on MCAs focused more on developed countries, therefore, dialogue in this workshop revolved around the possible incentives or benefits that could also encourage emerging economies and developing nations to participate in an MCA. As mentioned earlier, centering clubs on carbon pricing mechanisms (for example, linking emissions trading schemes) could discourage the participation of some countries. In particular, doing so could alienate many developing and less-developed countries because these more-vulnerable nations are focused on the costs of climate impacts in addition to abatement measures. In order to expand interest in MCAs among all countries, participants discussed the clear need to complement carbon pricing with other incentives. These other benefits will differ depending on national contexts and how a country perceives and prioritizes possible benefits. Some of these additional benefits are rapid economic development, new infrastructure and economic transformation, increased competitiveness, enhanced international reputation, and country leaders' political gain. For instance, larger emerging economies such as the BASIC coalition of nations—Brazil, South Africa, India, and China—may be more inclined to join an MCA if it is framed as a climate change mitigation strategy that includes the benefits of economic growth, technology transfer, and capacity building.

Although many developing countries have ambitious climate targets within their NDCs, their investment pipelines are insufficient to transform their economies at the speed and scale necessary for ambitious climate action. Increased financing is needed for technological innovation, particularly in the upstream of the innovation cycle, which would work to achieve the benefits of increased research-and-development

financing mentioned earlier. Developing countries also need enhanced resources and capacity to deploy and integrate these new technologies. Clubs should therefore target the development of technology throughout the entire innovation cycle, even though investing in the upstream would reap the longest term benefits.

Technological improvement can often only be achieved with enhanced financial flows, so participants also discussed the possibility of sharing portions of carbon pricing revenues to help finance research and development or implementation of climate-friendly technologies and practices for members in an MCA, which could encourage more participation from emerging and developing economies. It was noted by participants, however, that parties must be wary of creating a carbon club that addresses all the issues outlined above, including carbon pricing, capacity building, finance, and technology transfer, because the club would essentially reflect a mini-UNFCCC and get bogged down in too many details slowing down the implementation of MCA objectives. On the contrary, the benefit of such complexity could be increased trust between club members since the club could more effectively address national priorities. It was agreed that MCAs are supposed to work alongside the UNFCCC process and maximize benefits while minimizing complexity. Clubs should not intend to duplicate the institutions and initiatives that are already in place.

Despite these cautions, the inclusion of financial benefits as a part of an MCA was voiced as being of the utmost importance for the Alliance of Small Island States negotiating bloc. In addition to financial benefits, the countries in the alliance may be more likely to join a club if it boosts their international reputation and reduces emissions. Moreover, Pacific nations are facing and attempting to battle the adverse impacts of climate change, including more intense storm surges and increased sea-level rise. These countries must strengthen their defenses against these climate change effects and are looking for new financing pathways for such adaptation measures. A club structure could be used to build bridges between countries and create opportunities for South-South investment rather than traditional North-South investment. The Commonwealth of Nations was presented as an example of an existing club formed of small island states and larger economies, like the United Kingdom and India. This could, therefore, be one place to start testing the idea of developed and developing country coalitions. More research could also be conducted into carbon pricing for the oceans and best accounting practices for emissions and offsets from forests.

Conclusion

Overall, the discussion raised a number of key issues and questions that will require clarification in the months ahead as actors in the international climate sphere begin to implement the Paris Agreement. While it may seem that the discussion resulted in more questions than answers, there was a clear signal from participants that the linking of climate action efforts

across jurisdictions is a critical way for parties to achieve their international climate objectives in a cost-effective and efficient manner, and the newly minted Paris Agreement encourages these cooperative approaches.

Participants were in consensus that MCAs must increase ambition, and therefore their formation must begin with an agreed-on level of ambition, in addition to establishing clear purposes and goals. Some participants believed it best to start an MCA with a smaller number of participants to ease initial rule formation, or to use an existing club whose rules could be expanded on. Also, giving countries a sense of community by simply providing a common name and ambition was seen by some participants as enough of an incentive for countries to join. This formation of rules in clubs for countries with different national targets and priorities (e.g., China versus the small island states) was viewed as a critical aspect of the discussion and must be further investigated. In addition, more dialogue should focus on how countries could raise their club's level of ambition with limited and controlled economic consequences.

The benefits of carbon clubs and how or whether to measure them also remains a critical topic for further discussion. For some participants, it is fundamental for a club to include an economic driver to allow countries to perceive its benefits, as well as a measurable outcome to demonstrate the club's efficiency and progress toward achieving tangible emission reductions. If emissions reductions are removed as a quantifiable benefit, then the MCA framework loses its ability to accurately measure and compare progress across jurisdictions.

Questions for further investigation include:

- How will the benefits of an MCA be differentiated depending on a country's national circumstances?
- How can a club's mission be inclusionary to the needs of developing countries without creating a club with too many objectives?
- How can technology transfer be included as a benefit in an MCA in order to spur innovation in green technologies?
- Should the benefits of the MCA be measurable or not?
- How do we communicate the benefits of the club to nonparticipating jurisdictions and the public if these are not measurable?

Climate Strategies

Climate Strategies is an international organisation that convenes networks of leading academic experts around specific climate change policy challenges. From this it offers rigorous, independent research to governments and the full range of stakeholders, in Europe and beyond. We provide a bridge between research and international policy challenges. Our aim is to help government decisionmakers manage the complexities both of assessing the options and of securing stakeholder and public consensus around them. Our reports and publications have a record of major impact with policy-makers and business. Online at www.climatestrategies.org.

Endnotes

- ¹ For more information or to find publications related to these events, please see "Global Research Policy Interface Climate 2015," Climate Strategies, <http://climatestrategies.org/projects/global-research-policy-interface-climate-2015-strengthening-the-research-policy-interface-in-the-international-climate-negotiations/>; and "Climate Change," the Stanley Foundation, <http://www.stanleyfoundation.org/programs.cfm?id=30>.
- ² World Resources Institute, Open Climate Network, CAIT Climate Data Explorer: Paris Contributions Map, <http://cait.wri.org/indc/>; World Bank, "Carbon Pricing: It's on the Move," November 30, 2015, <http://www.worldbank.org/en/news/feature/2015/11/30/carbon-pricing-its-on-the-move>.
- ³ For an in-depth analysis of the Paris Agreement, see International Centre for Trade and Sustainable Development, "'The End of a Journey, the Start of Another' as Paris Agreement Adopted," December 13, 2015, <http://www.ictsd.org/bridges-news/biores/news/biores-paris-update-3-%E2%80%9Cthe-end-of-a-journey-the-start-of-another%E2%80%9D-as-paris>.
- ⁴ Mike Szabo, "After Paris, UN's New 'Light Touch' Role on Markets to Help Spawn Carbon Clubs," Carbon Pulse, December 16, 2015, <http://carbon-pulse.com/13415/>.
- ⁵ Johannes Gütschow, Bill Hare, Louis Jeffery, Ryan Alexander, Michiel Schaeffer, Marcia Rocha, Niklas Hone, Hanna Fekete, Pieter Van Breevoort, and Kornelis Blok, "INDCs Lower Projected Warming to 2.70C: Significant Progress but Still Above 20C," Climate Action Tracker Update, Climate Analytics, Potsdam Institute for Climate Impact Research, Ecofys, NewClimate Institute, October 1, 2015, http://climateactiontracker.org/assets/publications/CAT_global_temperature_update_October_2015.pdf.
- ⁶ Alexandre Kossoy, Grzegorz Peszko, Klaus Oppermann, Nicolai Prytz, Noemie Klein, Kornelis Blok, Long Lam, Lindee Wong, and Bram Borkent, "Climate Change," the Stanley Foundation,, World Bank Group, September 20, 2015, <http://documents.worldbank.org/curated/en/2015/09/25053834/state-trends-carbon-pricing-2015>.
- ⁷ World Bank Group, Networked Carbon Markets, <http://www.worldbank.org/content/dam/Worldbank/document/Climate/Overview%20of%20Networked%20Carbon%20Markets.pdf>.

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