

### International Shipping Green House Gas Levy

Submission 76/7/12 and related .inf papers sponsored by the Marshall Islands and Solomon Islands.

#### **RMI/SOL GHG levy proposal – key features**

- **The primary objective to reduce GHG emissions** by creating a market for zero emission propulsion.
- **A universal mandatory levy applied to all GHG emissions from international ships from 2025.** Exemptions are strongly discouraged. A level-playing field for all emitting ships without discrimination.
- **Starting price of \$100/ton CO<sub>2</sub>-equivalent starting 2025 with five-yearly review and upward ratchets.** Clear and predictable signal to industry that the cost of oil to shipping will increase until there is market parity with non-carbon equivalent technologies and fuels.
- **Promoted under the Principle of Polluter Pays.** Shipping is a major source of GHG emissions fueling the climate emergency and yet pays no cost for the impact on the climate most vulnerable. The polluter should bear the burden of making adequate reparation to those most affected.
- **Majority of the significant revenue generated to compensate the climate most vulnerable.** Under a GCF-type mechanism, 154 countries would be eligible apply for access to this compensation.
- **Minority used to subsidize research, development and deployment (RD&D)** of GHG-free technologies for the sector. Significant R&D investment is already being committed by the industry and subsidized by leading states. What is particularly absent is the funds to deploy new technologies equitably to all.

#### **Context – why does shipping need a GHG levy now?**

- Shipping is a major and growing international GHG emitting sector that currently does not pay for the negative externality that its emission create and that is currently paid by community and not the Polluter.
- In 2015, high ambition Pacific states called on the International Maritime Organisation (IMO) for emission reduction targets commensurate with 1.5 degrees. In 2017 IMO agreed to prepare an Emissions Reduction Roadmap and in 2018 IMO agreed an Initial Strategy with a target of decarbonisation within this century and at least 50% overall emissions reduction by 2050.
- The Initial Strategy determined to develop short-term (2018-2023), mid-term (2023-2030) and long-term (2030-2050) measures to achieve these targets and to set them out in a Revised Strategy in 2023.
- Progress has been very slow. A short-term measure has been agreed that is of limited effectiveness. While it is widely held that Market-based measures (MBMs) are required to drive transition from fossil fuels at speed and scale, the Initial Strategy only allows them to be introduced as mid-term measures.
- MEPC 76, in June 2021, was the first time members were able to debate MBMs. The GHG levy is the only hard proposal for a specific MBM so far tabled, although other submissions called for a workplan to develop MBMs. It was agreed that both the RMI/SOL proposal in its own right and the now agreed MBM workplan will be debated at an Intercessional Working Group (IWSG10) in October, with the results being reported to MEPC 77 in November.
- MEPC 76 saw heavily polarized debate over MBMs. While a clear majority of participating members agreed with taking the matter forward, a significant number of states spoke in opposition, claiming they may be disproportionately negatively impacted and therefore should be considered exempt. The last attempt by the IMO to negotiate MBMs failed in 2010 due to inability to agree which states should be eligible. A similar divide is now re-forming.

## FAQ

### **Why are we asking the IMO to implement this levy?**

IMO is the only avenue for a universally applied global solution. Regional MBM's will not be universally applied or equitable nor ensure that none are left behind.

The International Maritime Organisation is a specialist UN agency, responsible for global regulation of international shipping. As the Paris Agreement only covers the emission responsibilities of nation states, IMO is assumed to have responsibility for regulating shipping GHG emissions in line with international agreements. 173 countries are member states of IMO. Much of the work of IMO is done by its various committees, with GHG emissions being negotiated at the Maritime Environment Projection Committee (MEPC).

### **Why is this proposal being brought forward now?**

Time is not our friend and ambition at IMO is inadequate to meet a 1.5-degree agenda.

All evidence is that we need to agree an ambitious universal and mandatory global levy now and have it operational by 2025. Further delay is not an option for this international sector.

IMO has committed to an evidence-based approach to decarbonisation. All science confirms the levels of ambition in the Initial Strategy are too low and need to be urgently revised upwards. The measures so far enacted by IMO are demonstrably insufficient. All expert global opinion, from the UN Secretary-General down, is that setting a price on shipping emissions is an essential next step. As MEPC76 was the first opportunity offered at IMO to bring a serious proposal to the table, Marshall and Solomon Islands have worked hard to understand the science and to prepare the best possible MBM to achieve the IMO targets in the most efficient and equitable manner and to present it for debate at the earliest possible opportunity.

### **What is the primary purpose of the GHG levy?**

To send an unequivocal market signal that full decarbonisation is inevitable, that emissions must peak now and reduce rapidly. This requires valuing fossil fuels adequately to reduce the price differential between fuel oils and the cost of alternatives. Given the long asset life of ships, the industry needs to make investment decisions in new technologies in the immediate term and the GHG levy provides certainty to the market of the speed and scale of change required.

### **Will this measure be sufficient for shipping to reduce its emissions in line with the IMO targets?**

Unlikely. It has always been argued that a basket of measures is needed to meet even the current low ambition target in the Initial Strategy and MBMs are only one essential tool. In the event that an MBM does not result in the desired market shift, then command and control measures will be required, such as a regulated and enforced global cap on sector emissions, enforceable fuel standards or mandatory slow steaming. But such measures alone are not able to create a market that offers the fuels that are necessary.

### **Why a universal mandatory levy and not some other form of MBM?**

Which MBM is best has been considered closely by international expertise since 2008. We have attempted to understand and consult with all such expertise in design of this measure. We have also considered carefully the legal research of Columbia Law School in regards the international principles at law that need to be met We have listened to the increasing voice of the progressive industry interests in shipping (owners, operators, charterers, insurers and financiers) on the need for a carbon price. The overwhelming evidence is that a global levy of sufficient ambition to demonstrate a clear market shift is the best option available.

There are three basic types of MBM – a levy/tax;

an emissions trading scheme (ETS) or some form of off-setting scheme where the costs of shipping emissions is traded to other sectors. IMO has agreed that this sector takes direct responsibility for its emissions, so this rules out off-setting. A global ETS would be extremely difficult/costly to administer. A mixture of regionally based ETS is the most likely result of IMO failing to agree an international regime and has already been clearly signaled by EU. Such a regional program would not be equitable and see the highest emitting regions receiving the vast majority of revenue from their own pollution. The climate most vulnerable would be even more disadvantaged

**Is \$100 ton/CO2 equivalent starting price sufficient? What is the real figure?**

No, \$100/ton is insufficient to bridge the price differential between carbon and non-carbon fuels which is currently several hundred dollars a ton. However, \$100 is a floor not a ceiling and hence the need for review and upward ratchets towards a price of \$250-400 ton by 2035. Most expert opinion is we have this starting price right, with Maersk recently saying it needs to be least \$150/ton.

**Will the levy increase transport cost? If so, will it increase it evenly to all states?**

Yes. As bunker is one of the main operational costs for a ship, if the cost of the fuel goes up, then it is anticipated that the increased cost will be passed on to the customer. For the levy to be effective in driving emissions reduction, then the rate set must be sufficient to impact the market.. The more fuel used by a ship, then the more levy that has to be paid. The States which are on longer routes or served by older, less efficient ships are likely to be more severely impacted.

If shipping does not decarbonize in line with a 1.5°C pathway, then the impacts of climate change are existential to some of these States. Also, the impact of not decarbonizing would certainly increase costs as global temperatures and sea-levels rise, disrupting all current global trade patterns. If shipping decarbonizes in any other way this will also increase costs.

Revenue raised by the tax/levy can be used to compensate for disproportionate negative impacts caused by the levy, by prioritising funding allocations by, for example, GCF, to projects which support the Climate Most Vulnerable and/or those States disproportionately impacted by the levy. It is likely that there could be an initial increase on overall transport costs. In the vast majority of cases, this is likely to be highly marginal according to most expert evidence. For those countries who already paying unduly high shipping costs, such as Pacific SIDS and other climate vulnerable, the cost may be more significant and will need to be offset or compensated for – see revenue disbursement below.

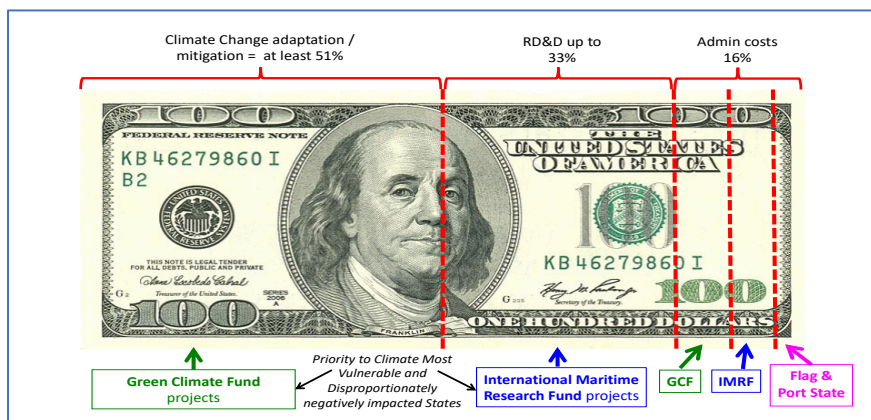
The cost of the levy is still less than the regular fluctuations in oil prices from existing market forces which vary by several \$100/ton from year to year and are already absorbed or passed to consumers.

**If the burden of the measure is not uniform, shouldn't some states, those most affected, be exempt?**

Exemptions only weaken the measure and create an artificial solution that simply puts off the problem and results in those routes maintaining ever more outmoded and expensive to operate shipping assets. Surely a much better solution is to use the considerable revenue of the levy to finance next generation deployment of new technologies to those most disadvantaged so that all can benefit equitably?

**A levy will generate significant revenue. What will happen to this?**

It is calculated that shipping generated about 900million tons/CO2-e in 2018. If all of this was captured by the levy it would have generated \$90billion p.a. at commencement. Using refinements such as 'feebates' and allowing for some leakage would reduce this initial revenue somewhat. However, it would still generate a significant revenue stream. The RMI/SOL proposal argues that the revenue should be allocated in three ways:



- **Adaptation/Mitigation – at least 51%.** In 2009 IMO reported to UNFCCC that the majority of proceeds from MBM revenues should be used to assist the needs of developing states, in particular SIDS/LDCs.

In the subsequent 12 years, as the climate emergency deepens and the global collective fails to achieve a 1.5-degree agenda, the costs of adaptation, disaster response and loss and damage compensation are increasing exponentially.

- **Research, development and deployment** – up to 33%. The second portion goes to subsidizing RD&D (with a strong emphasis on deployment) of new technologies equitably, recognizing that a global solution is required that leaves none behind.
- **Administration** - The third portion is to cover the transaction costs of administration of both collection and disbursement. In this model we have used the existing GCF overhead rate of 16% as a proxy for all related administration costs

**What ships would pay the 1.5°C levy?** All ships covered by MARPOL Annex VI sailing internationally (not the domestic fleet operating within a country). This would include all ship types, including bulkers, tankers, cruise liners, drilling rigs etc.

Introducing a similar tax/levy on domestic shipping would be the choice of each State under their NDC processes.

**Who would collect the 1.5°C levy?** The ship owner then pays the levy directly to the IMO body (to be established) who forwards all or part to the Green Climate Fund or other agreed instrument. Each ship would have a specific account (using the ship's IMO number) with the IMO fund to deposit the 1.5°C levy into.

**Who would check that the 1.5°C levy has been paid?** Flag States would issue compliant ships with a 1.5°C levy Compliance Certificate, based on the bunker delivery notes and confirmation from the IMO fund of payment received. Port States would check visiting ship's documentation for validity of 1.5°C levy Compliance Certificate.

**Who will decide the 1.5°C tax/levy rate and how the revenue will be spent?**

The IMO Member States participating in MEPC meetings that consider this matter will decide on whether to adopt a tax/levy, how much that tax/levy rate will be, and how it should be allocated. For example, if MEPC decides to allocate 51% of revenue generated to GCF and leave 33% to an IMO fund, then the respective Fund Board Members will decide exactly what projects would be funded through their respective fund.