



Naturskyddsforeningen



Bunker finance

A Breakthrough Option for the Copenhagen Climate Deal

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Channelling revenue from aviation and shipping measures to developing countries would pay a double dividend: 1. it is the key to agreeing global mitigation policies for these sectors, 2. it could significantly boost the scale of climate finance available and broker a high-ambition Copenhagen outcome.

Designing multilateral global policies that tackle emissions and generate climate finance would give all parties a stake in the outcome. This option is preferable to the adoption of unilateral measures by developed countries which would be unlikely to generate new climate finance.

Summary

Emissions from shipping and aviation are growing fast and are best tackled through a global mitigation framework. The finance raised from international bunker fuels, in the order of \$25-37 billion annually in 2020, could be critical in delivering a high-ambition Copenhagen outcome.

- International bunker fuel emissions could be regulated through a levy or an emissions trading scheme, initially focussed on CO₂ only. In the absence of a global framework, some developed countries plan to tackle these emissions through unilateral action.
- A number of developing countries have expressed concerns that adopting a global framework would contradict the principle of common but differentiated responsibilities. But these concerns can be addressed through the use of finance from international bunker fuels, as well as exemptions for the most vulnerable countries.
- To solve the impasse, revenues raised from regulating international bunker fuel emissions should be transferred to developing countries, to

support their mitigation and adaptation efforts and to meet any incremental costs they incur.

- Bunker revenues would represent a new and reliable source of public funds, not as a substitute for, but as a complement to, significant contributions by Annex I countries.
- A growing number of developed and developing countries support this option. Transferring finance to developing countries will make agreement at International Civil Aviation Organisation (ICAO) and International Maritime Organisation (IMO) on bunker regulation more likely by giving all countries a stake in the negotiations.¹
- If global regulation cannot be agreed, it is likely that unilateral regional measures will be adopted by some developed countries – like the EU’s inclusion of aviation within its domestic emission trading scheme – which would still cover developing country operators when they visited those markets, but would not generate international climate finance. This outcome would be sub-optimal both for mitigation and for provision of climate finance.
- Even though international regulations are likely to be agreed in ICAO and IMO, the funds should be channelled through the financial mechanism agreed through the COP. Priority should be given to funding adaptation, REDD projects and technology actions.
- To accelerate on-going efficiency improvements and cost reduction in the aviation and maritime industries, a small percentage of the funds could be directed into dedicated global fund for research, development and demonstration of low carbon technologies in these sectors.

¹ The Kyoto Protocol charged Annex I Parties with regulating greenhouse gas emissions from these sectors, working through the International Civil Aviation Organisation (ICAO) and International Maritime Organisation (IMO). However, there has been little progress to date in delivering this commitment.

1. Emissions from shipping and aviation are growing fast and need to be tackled through global mitigation framework. This need not contravene the CBDR principle.

International bunker emissions were over 1 GtCO₂ in 2007 and are expected to rise to around 1.7 GtCO₂ in 2020, with additional non-CO₂ warming impacts from aviation. Nearly all Annex I Parties have stated their aim of reducing these emissions through global sectoral policies. Because there are difficulties in attributing emissions from airplanes and ships to specific Parties, a feasible and effective mitigation strategy needs to incorporate all countries with substantial international transport activity to reduce the risk of carbon leakage.

Policies should initially focus on CO₂ emissions, but incorporate the non-CO₂ impacts of aviation as soon as possible.²

Developing countries are concerned that a global mitigation effort will affect Annex I and non-Annex I countries equally, and thereby undermine the principle of Common but Differentiated Responsibilities (CBDR). But:

- Parties are now agreed that these emissions cannot be attributed to any particular Party. Since the emissions do not belong to Parties, measures to tackle them do not establish emission reduction obligations on Parties, but rather on the sectors themselves;
- there is provision for global sectoral approaches in the UN Framework Convention on Climate Change (Art 4.1c), on condition that developing countries do not incur incremental costs.
- Revenue would not substitute but be additional to significant Annex 1 contributions

A global bunkers strategy can therefore be acceptable to developing countries, but only if revenues raised from the international regulation of bunkers are used to defray incremental costs, and to fund adaptation and mitigation efforts in the developing world.

2. Finance raised from international bunker fuels could be critical in delivering a high-ambition Copenhagen outcome.

An ambitious deal can still be achieved at Copenhagen if developed countries deliver a substantial commitment on new public finance. The EU has put forward a suggestion for Annex I public finance of \$33-75 billion by 2020³ to cover mitigation and adaptation. In a working paper, it estimates that regulation of international bunker fuel emissions, through emissions trading

² Aviation creates significant non-CO₂ impacts that approximately double its overall warming effect. Any comprehensive global GHG budget must account for these effects. The application of an emissions multiplier based on aviation's Global Warming Potential is supported by the latest science, and if applied in an ETS, would increase the available funding.

³ EU Council Conclusions, 30th Oct (given as €22-50 billion).

with auctioning of permits (or for shipping an equivalent levy on maritime fuel) could generate revenues of \$25-37 billion per annum by 2020⁴.

Thus international bunker fuel finance could supplement by a further 50% the public finance that the EU says is needed from industrialised countries.

The EU's offer is a starting point but needs to be significantly increased if a breakthrough is to be achieved in Copenhagen. NGOs believe that more than \$195 bn is required per year by 2020 of public finance for both mitigation and adaptation that is truly new and additional to the EU's existing commitments to provide ODA. An innovative bunkers mechanism would increase the level of ambition possible by providing a genuinely new and additional reliable and sustainable source of finance for developing countries without drawing further on the national budgets of developed countries.

3. There is growing support for bunker mitigation and finance in both developed and developing countries. Unilateral regional regulation will develop if global measures cannot be agreed.

The EU Council Conclusions of 30th October give clearer direction on bunker finance than in earlier policy statements (although the wording could still be improved considerably). As a result, the EU was able to respond well in Barcelona to requests from Botswana and Gambia to specify aviation and shipping as a source of climate finance.

Nigeria and Liberia have tabled a proposal for a global maritime levy, which is gaining support in the wider Africa group.

Norway has voiced its support for bunker finance. Canada tabled text in Barcelona identifying potential bunker revenues as a source of finance. Singapore supports a similar option.

The Least Developed Country group have proposed an air passenger adaptation levy, although this proposal is designed to raise finance rather than to reduce emissions.

At IMO, France, Germany, Norway and Denmark have detailed proposals for global shipping schemes (either an ETS or a levy) that would raise revenue. The Danish Prime Minister supported bunker finance in his speech to the November G20 meeting of finance ministers.

Note that both the EU and the US (in the Waxman-Markey House Bill and draft Senate Bill) have committed to regulate greenhouse gas emissions from international aviation and maritime. Both will implement unilateral domestic regulation on these sectors if international rules are not forthcoming, and most of the revenue raised is likely to be used domestically.

⁴ Staff Working Paper accompanying Communication 'Stepping Up Climate Finance'. See http://ec.europa.eu/environment/climat/pdf/future_action/sec_2009_1172.pdf, last page.

Under this scenario, developing countries would have lost the opportunity to participate in the design of an approach that could have generated international climate finance, but their operators would still be covered where they travelled to the EU or US.

4. The CBDR issue can be solved through the right financing mechanisms – and a system of exceptions for the poorest countries

All countries are agreed in principle that regulation of bunker fuels should be implemented through ICAO and IMO⁵, based on guidance given under the UNFCCC process. The Kyoto Protocol asked Annex I Parties to work through ICAO and IMO to reduce emissions, but little progress has been made to date on agreeing an effective system, in part because of the apparent conflict with the policies of non-discrimination and flag neutrality that apply in ICAO and IMO, whereby operators of all nationalities are treated equally.

A global policy would respect the principles of ICAO and IMO, but a number of developing countries currently object to this idea. Objections stem both from direct fears of the impacts of bunker fuel regulation on costs and exports, and concern that this will undermine the principle of “common but differentiated responsibilities” (CBDR) established in the UNFCCC.

Some non-Annex I countries have expressed concern over the impacts of bunkers regulation on (especially agricultural) exports. Preliminary analysis suggests that even if a price of \$30 is applied to every tonne of emissions from shipping, cost increases are likely to be a small fraction of one percent. Impacts on overall volumes of trade would be even lower, since the price elasticity of most shipped goods is low.⁶

From an economic perspective, the CBDR issue is less severe than often feared as the majority of the cost of a global bunker fuel policy is likely to fall on consumers in developed countries in the form of higher prices for imported goods. Around two-thirds of maritime trade goes into developed countries and the great majority of air travel is by developed country citizens.

To protect the least developed countries, a set of *de minimis* exceptions could be applied. These should be set in such way as to exempt traffic to and/or from the Least Developed Countries and Small Island States, without causing significant carbon leakage or trade distortion.

The principle issue of CBDR was discussed in section 1 above. Correctly designed, global regulation of international aviation and shipping would not contravene the Convention or the principle of CBDR.

⁵ The exception is Australia, which proposes two bunker protocols, to be negotiated at UNFCCC.

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5. A deal on bunker finance will make regulation at IMO and ICAO more likely by giving all Parties a stake in the outcome

Tying bunker fuel regulation to finance for developing countries will help unlock the IMO and ICAO processes by giving developing countries a stake in the outcome:

- Small Island and poor remote states which face disproportionately high transport costs could be exempted from any impacts, and would benefit if a high proportion of bunker finance was directed into climate adaptation funding. The group of Least Developed Countries has already proposed an adaptation levy on passenger flights, and so would be likely to support mitigation policies that raised a similar sum for adaptation.⁷
- Some African countries have proposed a maritime levy that will pay into a fund and for which developing country governments receive an automatic rebate (before money is distributed for climate purposes) in proportion to their share of imports. The remainder (around two-thirds, representing Annex I costs) remains in the fund and is used as climate finance⁸. Although it reduces the funds for climate finance, the principle of a direct rebate could address concerns about incremental costs.
- Major emerging economies dependent on bulk maritime exports and maintaining the principle of “common but differentiated responsibilities” for financing would see direct benefits from public finance for forest and technology actions.
- Ultimately, the decisions on the use of new resources generated by bunker mechanisms should be taken by the new financing mechanism agreed for the post-2012 regime.

By giving direct benefits to affected developing countries, bunker fuel finance is likely to make delivering effective regulation at IMO and ICAO far easier. A global approach will avoid the complexity and expense of parallel – but uncoordinated – unilateral systems in the EU, US and most likely other developed countries.

The precise allocation of funds to different activities under the Copenhagen agreement will depend on the structure and governance of the financial mechanisms established. Whatever the final arrangements, political support for bunker fuel regulation will require a fair split of funding between the areas described above.

In addition, the sectors are likely to be net buyers of allowances under any ETS in the medium term as their emissions are forecast to continue rising.

⁷ These countries have proposed an Adaptation Levy (IAPAL) for aviation in the form of a flat ticket tax, raising around \$10 billion annually.

⁸ http://unfccc.int/files/meetings/ad_hoc_working_groups/lca/application/pdf/awglcafina_nigeria051109.pdf

Including two significant buyers in schemes linked to the global carbon market will help to ensure robust demand and a buoyant carbon price, driving further mitigation, likely for the most part to be in emerging economies.

6. Precedents exist for similar international financing mechanisms

Objections have been raised that adoption of this proposal would breach long held positions in many countries over the legality of “international taxation”. However, precedents already exist – including in the maritime sector – for co-ordinated levies which flow to international funds managed under an international agreement.

The International Oil Pollution Compensation Fund (IOPC) has been established to provide a shared fund from which compensation for oil spill damage can be paid in the situation where the ship owner cannot provide sufficient compensation⁹. IOPC is established as an independent international organisation through a treaty under the IMO framework. The Assembly of Parties sets an annual total contribution needed for the fund each year, and IOPC collects contributions directly from operators based on the amount of oil they have received; *de minimis* limits apply.

Though not an exact analogy, the example of IOPC shows that where a significant international public good issue exists, countries are willing to develop innovative financing mechanisms to support joint action.

It is sometimes claimed that the United States would oppose any use of revenues from the bunker sectors as climate finance, as this would represent international taxation. However, this would not apply to revenues generated by auctioning permits under an ETS. Furthermore, there are moves in the US to amend legislation to allow for global bunker finance.

The US Waxman-Markey Bill and draft Senate Bill cover all aviation and shipping fuels sold in the US, whether for domestic or international use, with funds flowing to the US Treasury. This approach would prevent revenues from flowing directly to a global fund. However, a previous proposed bill in 2008 (Liebermann-Warner) had an exemption for fuel associated with activity was covered by laws in another country. By analogy, the final US climate bill could be amended to ensure compatibility with an international bunker fuel finance scheme, and there is growing support for this option amongst US legislators.

7. A portion of bunker finance could support low carbon RD&D

There is already strong support from the relevant industries for a non-distorting agreement that has global coverage and thus minimises potential leakage and avoidance possibilities.

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<http://www.iopcfund.org/npdf/genE.pdf>

The UK, Belgian, Swedish, Norwegian and Australian Shipping Associations have published a detailed design for an emissions trading system, which includes the principle of 100% auctioning and use of the money as climate finance¹⁰. The Danish, French, German and Hong Kong shipping associations support a global levy. The Aviation Global Deal group of some 10 airlines have published a clear, detailed proposal for a global ETS¹¹. The international airline body IATA supports a global sectoral approach in principle, although its preference is for revenues to be recycled to the industry.

In order to maximise industry support and meet future emission targets, a small proportion of the finance collected could be directed to a global RD&D fund for low carbon aviation and shipping. If the scheme is administered through ICAO and IMO then this percentage could be “top-sliced” directly before funds were transferred into the climate change mechanisms.

¹⁰ http://www.british-shipping.org/uploaded_files/cap-and-trade.pdf

¹¹ See <http://www.agdgroup.org/> for the group members and the 'discussion note'.