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PREVENTION OF AIR POLLUTION FROM SHIPS

Market-Based Instruments: a penalty on trade and development

Submitted by the Bahamas

SUMMARY

<i>Executive summary:</i>	This document discusses market-based instruments for international shipping and argues that, as a penalty on trade, they are contrary to the best interests of the developing States. Further, proportionality must be the key to any measures proposed for international shipping, especially if such measures have a financial component.
<i>Strategic direction:</i>	7.3 and 13.3
<i>High-level action:</i>	7.3.1
<i>Planned output:</i>	n/a
<i>Action to be taken:</i>	Paragraph 23
<i>Related documents:</i>	MEPC/60/4 and MEPC 60/4/9

Introduction

1 The Bahamas, as a low-lying, coral-fringed archipelago, is very susceptible to the effects of climate change and, recognizing this, the Government is already taking national measures to reduce its already low CO₂ emissions. However, the Bahamas is also concerned that shipping must not be disadvantaged by the imposition of excessive non-proportional penalties. To that end, this document addresses the problems that proposed measures for shipping pose to the industry and to world trade. Shipping, it should be remembered, is the most environmentally friendly mode of transportation and one which is a servant of world trade and development. Carrying over 90% of world trade, and only emitting 2.7% of global anthropogenic CO₂, is the mark of a remarkably efficient industry. Furthermore, through the implementation of operational and design measures, considerable reductions in GHG emissions will be achieved without the need for financial penalties.

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2 As laid out in the United Nations Framework Convention on Climate Change (UNFCCC), Article 3.5, “measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade”.

3 The United Nations Climate Change Conference in Copenhagen (COP 15)/CMP 5, failed to produce an agreed text on emissions from ships, but what was agreed by all UNFCCC parties throughout the negotiations was that IMO should continue to be responsible for the determination of appropriate measures for shipping and this is in accordance with the Kyoto Protocol, Article 2. It was also held that one United Nations body could not dictate to another but could only invite, request or encourage certain courses of action. The main areas of contention regarding emissions from ships were the setting of fixed targets, the necessity of market-based instruments and the extent that the actions taken in IMO should be compliant with the provisions of the UNFCCC and its Kyoto Protocol, in particular, the application of “Common But Differentiated Responsibilities” (CBDR).

4 This document will not attempt to address CBDR or fixed targets, but will concentrate on Market-Based Instruments.

Market-Based Instruments

5 There are two principal options currently being proposed, one based on emissions trading, the other on a levy (or contribution) on bunker fuel. This document will deal with each option separately.

Emissions Trading Schemes

6 Various schemes have been proposed which would require carbon credits to be drawn or purchased equal to the quantity of bunkers used by a ship. The value or size of the credits to be drawn or purchased varies from scheme to scheme. In general, there would be an allocation of credits to cover a certain amount of fuel. If more were to be required, they would have to be purchased, if less were required, they could be sold. Once the initial allocation of credits has been exhausted, credits will have to be purchased on the open market. Based on the experience of such schemes to date, brokers will buy and sell credits as any other commodity. These brokers are likely to operate in developed countries where financial resources are more readily available, meaning that the profits to be made in the process will be retained within developed countries.

7 The intention of such schemes is to encourage the more efficient use of fuel, but for them to be successful and equitable, certain criteria are essential. The countries involved must be at a similar level of economic development to avoid distortions in the ability of States to participate due to inequality of available funding. They must have some degree of political cohesion to ensure that any disadvantages for one country compared to another can be dealt with. There must be a common central body that can ensure proper coordination of the measures. This means that in areas such as the European Union or in countries such as the United States such schemes can operate successfully. If such a scheme is to be implemented on a global scale none of the three criteria mentioned will be satisfied. The result will be a skewing of the system in favour of developed countries and result in severe disadvantages for all developing States especially the most needy. The effectiveness of a trading scheme in a global context is untried and unproven. It is unlikely to reduce emissions in the short term and is likely to disadvantage the trade of the poorest countries.

8 Ships have an average life of 25 to 30 years. Efficiency gains are more difficult to achieve on older ships, emission trading schemes therefore tend to favour owners with new ships, which in turn means that owners able to afford newer ships can gain a competitive advantage from the scheme. Owners which are engaged in trades in which older ships operate are disadvantaged as these tend to be in those trades carrying low value cargoes. Again, these are mainly from developing States.

9 It is useful to look at an example. Therefore, imagine two companies operating an international ferry route. One is based in Northern Europe, the other in sub-Saharan Africa. The underlying belief is that an ETS will operate in an environment of perfect competition. All parties will be able to access the carbon market equally, purchase at the optimum time and sell in order to make a profit. In this manner, carbon trading is a financial zero sum game in which one party needs to purchase the excess carbon credits from another. However, in this example, it can be expected that the older vessel on the African trade will use more fuel and so the company would need to gain more credits in order for it to continue trade. Conversely, the European one would sell its excess to the market. The net effect will be that a company in a developing State will need to find money from the operating and safety budget of the vessel to purchase the credits from a company in a developed State. All transactions would be undertaken in a financial centre based in a developed country, so further increasing the capital transfer from developing to developed country.

Levy or Contribution

10 It has been proposed that an additional charge should be placed on ship's bunkers to provide funds to alleviate the effects of climate change. It has been called a levy or a contribution but, in effect, it is a tax on international trade. It would set a precedent as the first internationally imposed tax and this alone should give serious pause for thought. It can be readily imagined that once the precedent is set then other, perhaps even more swingeing, taxes could follow.

11 A number of serious questions must be asked about the proposals, such as:

- .1 Who would collect the funds and how would the integrity of the system be maintained?
- .2 A shipowner pays for bunkers and would also have to pay the additional levy. The money for the bunkers would be paid to the supplier, but who would collect the levy? Would it be paid to the supplier who would then pass it on, less an administrative fee? Or should it be paid to the flag State which would have to establish a bureaucracy to handle it and would have to charge an administrative fee for handling it? Or should it be paid directly to a central fund which would also require a bureaucracy. Because of the very large sums of money being proposed, the potential for fraud is inevitably very high. So any system will require an extensive monitoring and investigative system to ensure its integrity. The problems will be compounded by the considerable number of contributions coming from a large geographical spread of sources.
- .3 How would the funds be concentrated and distributed?

- .4 If the collection of funds has problems, the concentration of those funds and their equitable distribution have far more. A choice would have to be made about whether the funds should be handled by a new body or by an existing one. A new body would be better able to ensure that the money is used in a way which would ensure a reduction of emissions from ships. On the other hand, an existing fund would have established mechanisms which would only have to be enlarged.
- .5 Another major question would be how to determine the distribution of funds. The primary aim must be to reduce emissions from ships; this would require research and investment in new technology. Because the majority of research establishments capable of carrying out this work are in developed countries, most of the research money would be spent in developed countries. Any new technological innovations resulting from this research will be fitted mainly to new ships which will be built in very few countries for owners able to afford the more expensive ships. None of this will benefit the most needy countries.

IMO's Role

12 The aim of any measures taken at IMO to combat climate change should be to reduce emissions from ships. If this cannot be achieved, a proposed measure will not be of any direct benefit to the environment. It must not be the purpose of actions taken relating to shipping to provide funds which will benefit another industry. Any funds derived from shipping will result in an increase in the cost of trade and therefore be contrary to UNFCCC Article 3.5. In effect, it would be an international tax on trade.

13 Shipping facilitates world trade by carrying over 90% of internationally traded goods. It is by far the most efficient and environmentally friendly mode of transport for carrying goods. But shipping is an easy target when looking for a convenient source of revenue because it is open to scrutiny and action whenever it is in a foreign port. Caution must be exercised when taking action on shipping to avoid using this vulnerability to inspection as an excuse to take stronger action on shipping than is justified by its contribution to global emissions.

14 International shipping is responsible for 2.7% of global anthropogenic CO₂. If it is decided that a financial penalty is to be placed on shipping, it should be proportional to the global contribution to limiting CO₂ emissions. For example, if the global amount of money to be provided is \$10 billion, then shipping should not be expected to provide more than \$270 million. Proportionality must be the key to any measures proposed for shipping, especially if such measures have a financial component.

15 For many types of goods, in particular those at the high value end of the market, the cost of freight per unit of goods is small. For instance, if a ship is carrying 10,000 containers of manufactured goods, the cost per container will be small and the cost per unit of goods inside the container will be insignificant. But even in the container trades, much of the trade is one way and a ship has to carry many empty containers for sections of its voyage.

16 At the low value cargo end of the market, the cost of freight per unit of goods is much greater and the effect of any penalty much larger. Most of the goods exported from developing countries are low value; therefore, any penalty on freight will have a greater effect on developing countries than it will have on developed countries. Developing countries can only continue to develop by increasing the volume and value of their trade.

17 Any measure that creates an adverse effect on trade will not be to the advantage of developing States. Funds that are required to combat climate change should be obtained from sources that do not create an adverse impact on world trade, especially the trade of developing States.

Conclusions

18 Care must be taken to avoid restricting world trade. Any penalties on trade will be to the disadvantage of developing countries which need expanded trade to continue to develop in order to raise the living conditions of their people.

19 Operational and technical measures will provide shipping with the means to achieve significant reductions of emissions and high oil prices will provide the incentive to use them.

20 Both emission trading and levy schemes are disadvantageous for developing countries. They will simply provide a means to allow developed countries to penalize developing countries and collect money to finance research to be carried out in the research centres of those developed countries.

21 International shipping should not be used to collect money which would be difficult to obtain from numerous national sources simply because it is easy to do so.

22 If a financial penalty is applied to international shipping, it should be proportional to the emissions from shipping as part of global emissions: that is 2.7%.

Action requested of the Committee

23 The Committee is invited to take note of the information presented and take the arguments into account when considering actions to be taken to control greenhouse gas emissions from international shipping.
