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COMMISSION STAFF WORKING DOCUMENT

Union submission to the International Maritime Organization's 77th session of the Marine Environment Protection Committee proposing guiding principles for the further development of Market-Based Measures

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PURPOSE

This Staff Working Document contains a draft Union submission to the International Maritime Organization's (IMO) 77th session of the Marine Environment Protection Committee. The IMO has scheduled MEPC 77 from 22 to 26 November 2021.

The draft submission suggests criteria to assess and compare carbon pricing measures. The proposal builds on the list of criteria identified in 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.

EU COMPETENCE

Regulation (EU) 2015/757¹ (EU MRV Regulation) establishes the legal framework for an EU system to monitor, report and verify (MRV) CO₂ emissions and energy efficiency from shipping. The regulation aims to deliver robust and verifiable CO₂ emissions data, inform policy makers and stimulate the market uptake of energy efficient technologies and behaviours. It does so by addressing market barriers such as the lack of information. It entered into force on 1 July 2015.

Any IMO measure on GHG matters, which will unequivocally require the monitoring, verification and reporting of GHG emissions from shipping, would affect the EU MRV Regulation. Therefore, the EU has exclusive competence for GHG emissions in shipping.

In addition, on 14 July 2021, the Commission adopted the *Fit for 55* package of proposals to reduce GHG emissions. *Fit for 55* includes a number of Commission's proposals that specifically target the shipping sector, such as the revision of the EU Emission Trading System (ETS) to include the maritime transport sector (and the corresponding amendments to the EU MRV Regulation)² but also the FuelEU maritime proposal³, which focuses on the use of renewable and low-carbon fuels in the maritime sector and mandates the uptake thereof by the ships calling EU ports. Under the case-law⁴, the risk of affectation concerns not only the rules as they stand, but also their foreseeable future development. These legislative initiatives further lead to the exclusive competence of the EU for GHG emission in shipping.⁵

In light of all of the above, the present draft Union submission falls under EU exclusive competence.⁶

¹ Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport, and amending Directive 2009/16/EC, OJ L 123, 19.5.2015, p. 55–76

² COM(2021) 551 - Proposal for a directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation (EU) 2015/757

³ COM(2021) 562 - Proposal for a regulation of the European Parliament and of the Council on the use of renewable and low-carbon fuels in maritime transport and amending Directive 2009/16/EC.

⁴ Opinion 1/03 of the Court of Justice of 7 February 2006, Lugano Convention, point 126.

⁵ See in particular Commission proposal COM(2021) 551 referred to in footnote 2. It introduces a reporting and review provision (Article 3 ge) into Directive 2003/87 regarding possible amendments in relation to the adoption by the International Maritime Organisation of a global market-based measure to reduce greenhouse gas emissions from maritime transport. The existence of such a review provision confirms the existence of a risk of affectation of the existing and foreseeable EU acquis.

⁶ An EU position under Article 218(9) TFEU is to be established in due time should the IMO Maritime Safety Committee

Therefore, only the Union may act in the IMO to propose measures on GHG emissions. This Staff Working Document is presented to establish an EU position on the matter and to transmit the document to the IMO prior to the required deadline of 17 September 2021.⁷

eventually be called upon to adopt an act having legal effects as regards the subject matter of the said draft Union submission. The concept of '*acts having legal effects*' includes acts that have legal effects by virtue of the rules of international law governing the body in question. It also includes instruments that do not have a binding effect under international law, but that are '*capable of decisively influencing the content of the legislation adopted by the EU legislature*' (Case C-399/12 Germany v Council (OIV), ECLI:EU:C:2014:2258, paragraphs 61-64). The present submission, however, does not produce legal effects and thus the procedure for Article 218(9) TFEU is not applied.

⁷ The submission of proposals or information papers to the IMO, on issues falling under external exclusive EU competence, are acts of external representation. Such submissions are to be made by an EU actor who can represent the Union externally under the Treaty, which for non-CFSP (Common Foreign and Security Policy) issues is the Commission or the EU Delegation in accordance with Article 17(1) TEU and Article 221 TFEU. IMO internal rules make such an arrangement absolutely possible as regards existing agenda and work programme items. This way of proceeding is in line with the General Arrangements for EU statements in multilateral organisations endorsed by COREPER on 24 October 2011.

REDUCTION OF GHG EMISSIONS FROM SHIPS

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

Submitted by the European Commission on behalf of the European Union

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, which could ensure, on their own or in combination, that shipping decarbonises and that zero-emission vessels enter the fleet by the middle of the decade. The current document follows up on the first type of the introduced mid-term measures, namely 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 (also in MEPC 76/7/2). The second type of measures concerns standard-based measures such as a Low GHG Fuel Standard, which is further elaborated in document [ISWG 10/X], or a Carbon intensity standard as identified in MEPC 76/7/2.

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. The pre-requisite for the assessment of the GHG impact of shipping is 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 European Union considers 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 European Union is 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 be set at a significantly stringency level in order to create an 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 have genuine capability for deep emissions reduction.

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

.6 MBMs should be designed to be flag-neutral and they should ensure an equal treatment of all actors on the same route.

.7 MBMs should be cost-effective.

.8 MBMs should not be duplicative and should allow bottom-up action by member states to further accelerate GHG emissions reduction from shipping.

.9 For revenues generated from MBMs, most funds should be used to support maritime climate mitigation and adaptation activities, including in developing countries.

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 allow bottom-up action by IMO member States to further reduce GHG emissions reduction from shipping, such as the European Green Deal. 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 addressed and to the extent possible be avoided.

18 The last criteria addresses the issue of revenues generated by an MBM. It should be ensured that most funds are secured to address maritime climate issues. The revenues could be used to, e.g.:

.1 Reduce cost of GHG reduction for the maritime sector. 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 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.

21 As such, the European Union suggests that the Committee agrees to a set of basic guiding principles for the development of any MBMs. These principles are listed in para 11.1-11.9.

Action requested by the Committee

22 The Committee is invited to consider this document, and in particular paragraphs 11-18, and take action, as appropriate.
