Government-to-government Carbon Market Trading

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International Climate Change Policy after Paris

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Basic Idea

- Many countries or jurisdictions will implement carbon markets.
- Prices will vary.
- At some point, one government will likely find its price "too high" while another finds its price "too low"
  - *Alternatively: Jurisdictions worry about high prices.*
- Those jurisdictions could engage in a spontaneous government-to-government trade of allowances.

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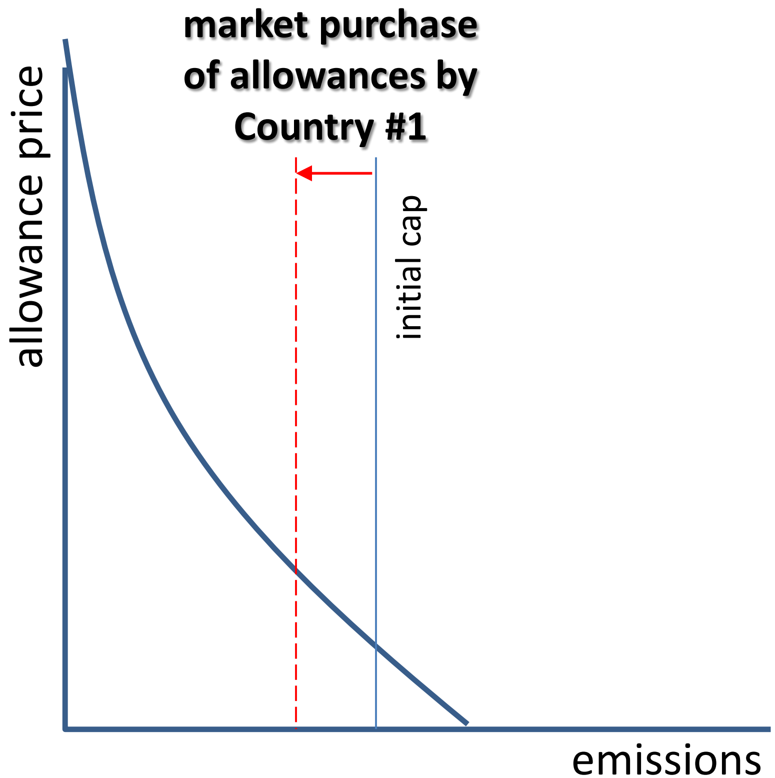
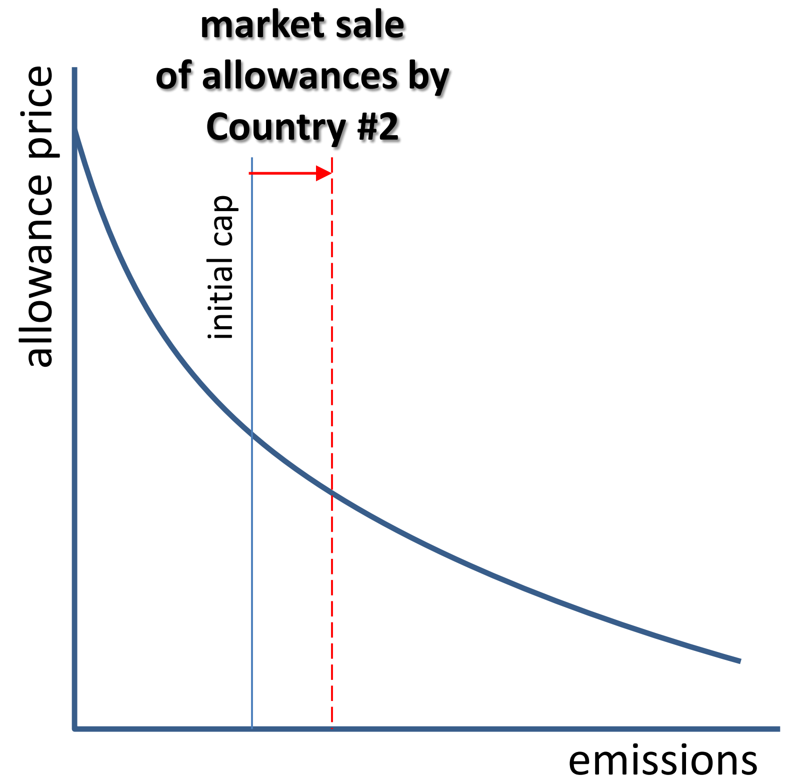
Basic idea



Country #1 (low price)



Country #2 (high price)

Government-to-government transaction:

allowances →

← cash

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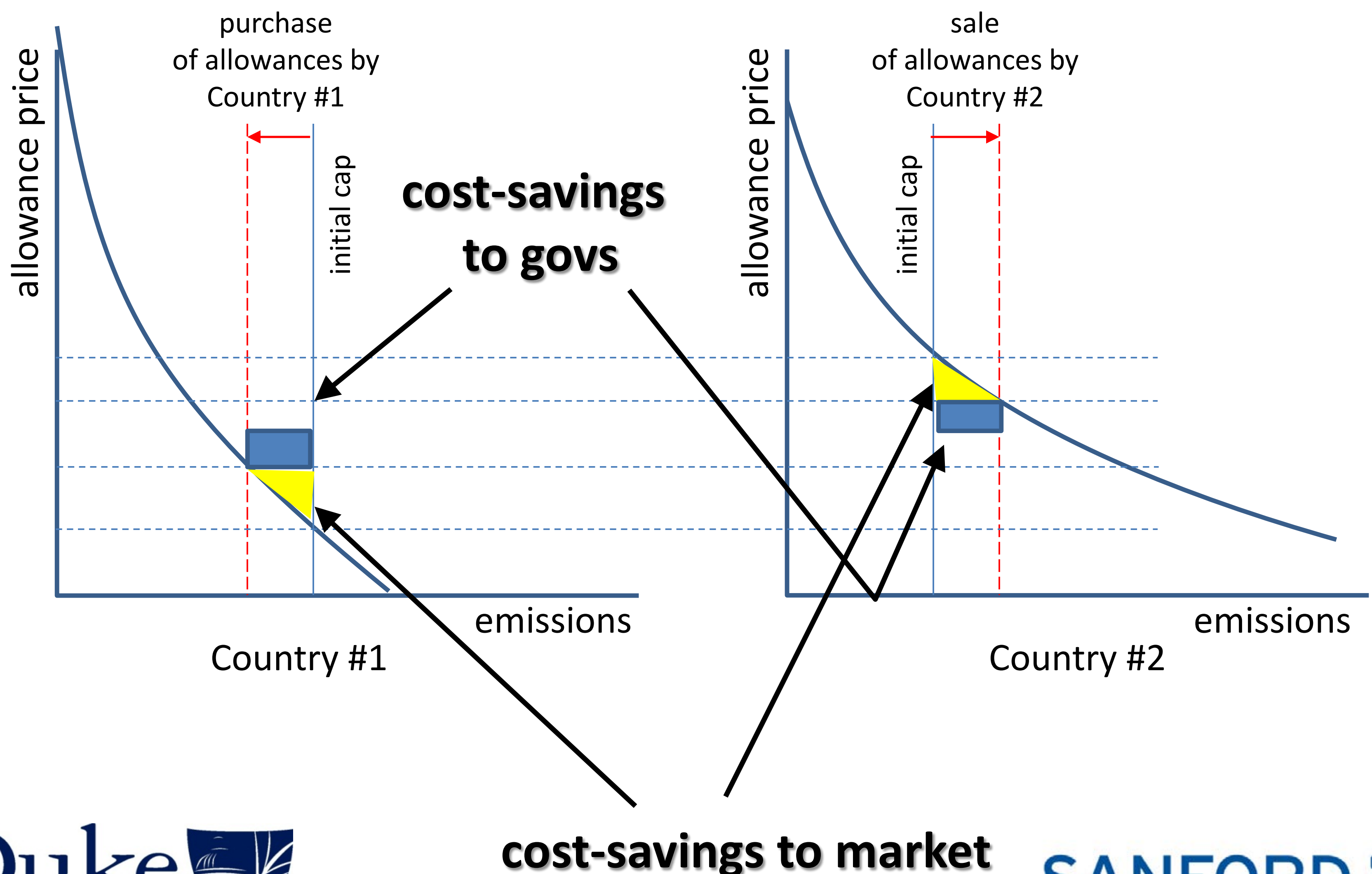
Points

- Improves cost effectiveness without overhead of linking markets; could also be a step to linking.
- Allowed under Article 6.
- Could occur between a jurisdiction with a tax and a jurisdiction with a cap.
- Potential next steps: Develop infrastructure.

Improves cost effectiveness without the overhead of linking markets

- Shifting any allowances from a low price market to a high price market reduces global compliance costs.
  - Some cost savings / profit accrues to market participants.
  - Some are shared by the governments who "buy low and sell high".
- Full bilateral market linking requires significant harmonization (Jaffe, Ranson, Stavins 2010; Burtraw et al 2013; Ranson and Stavins 2015).
  - Monitoring, oversight, tracking
  - Cost management
  - Ambition and domestic incentives
- *Parties should worry less about harmonization for a single, mutually beneficial transaction.*
- *Could build interest / trust for a more extensive link.*

Basic idea



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Paris Agreement

stocks in developing countries; and alternative policy approaches, such as joint mitigation and adaptation approaches for the integral and sustainable management of forests, while reaffirming the importance of incentivizing, as appropriate, non-carbon benefits associated with such approaches.

Article 6

1. Parties recognize that some Parties choose to pursue voluntary cooperation in the implementation of their nationally determined contributions to allow for higher ambition in their mitigation and adaptation actions and to promote sustainable development and environmental integrity.

2. Parties shall, where engaging on a voluntary basis in cooperative approaches that involve the use of internationally transferred mitigation outcomes towards nationally determined contributions, promote sustainable development and ensure environmental integrity and transparency, including in governance, and shall apply robust accounting to ensure, inter alia, the avoidance of double counting, consistent with guidance adopted by the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement.

3. The use of internationally transferred mitigation outcomes to achieve nationally determined contributions under this Agreement shall be voluntary and authorized by participating Parties.

4. A mechanism to contribute to the mitigation of greenhouse gas emissions and support sustainable development is hereby established under the authority and guidance of the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement for use by Parties on a voluntary basis. It shall be supervised by a body designated by the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement, and shall aim:

   (a) To promote the mitigation of greenhouse gas emissions while fostering sustainable development;

   (b) To incentivize and facilitate participation in the mitigation of greenhouse gas emissions by public and private entities authorized by a Party;

   (c) To contribute to the reduction of emission levels in the host Party, which will benefit from mitigation activities resulting in emission reductions that can also be used by another Party to fulfil its nationally determined contribution; and

Environmental Integrity under a Tax

- Suppose a jurisdiction with a carbon tax in place failed to meet its domestic or international emission objective.
- Higher emissions under a tax means higher revenue.
- Excess revenue could be used to purchase and retire allowances in another jurisdiction.

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Potential next steps

- Create a forum for jurisdictions to discuss the idea.
- Development a template for potential transactions.
  - Process to initiate a decisions and necessary items for agreement.
  - Transaction steps.
- Pilot transactions.

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Conclusions / Implications

- Achieves cost savings.
- Builds interest and trust in broader links.
  - Does not require harmonization.
  - True even if the mechanism is not used.
- Facilitates ambition by providing another degree of flexibility and cost savings.
- Provides an opportunity to address environmental integrity concerns under a carbon tax.