
Brazil Draft Market Readiness Proposal (MRP) Expert Group Feedback

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Outline

1. Expert group
2. Country context and the draft MRP
3. Expert group feedback
4. Challenges going forward (and their implications for carbon pricing instrument choice and design)

PMR Expert Group for Brazil

- Jan H. van Heerden (Pretoria University)
 - *Roberton C. Williams III* (University of Maryland)
 - Felix Chr. Matthes (Öko-Institut) (desk review only)
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- Desk review of draft MRP: early April 2014
 - Country visit: April 15-16

Country Context

- Brazil has been successful in substantially reducing overall GHG emissions, particularly from land use change (LULUCF)
- However, energy-related emissions are rising, and projected to continue rising, and further reductions in LULUCF emissions will be increasingly difficult
- CDM and other programs have given Brazil significant experience with market mechanisms
- Carbon pricing (ETS or carbon tax) will be necessary to limit future GHG emissions in a cost-effective way

Country Context and the Draft MRP

- With elections this year, political window for carbon pricing is not yet open.
- Need to have analysis ready in order to enable an informed decision when that window opens
- Draft MRP covers full set of building blocks, focuses mainly on analytical work

Expert Group Feedback

- Expert group feedback also covered all building blocks, focused mainly on analytical work
- Key topics discussed during country visit:
 - Role of computable general equilibrium modeling (CGE) vs. partial equilibrium modeling for studying effects of carbon pricing
 - CGE model development: expand existing model or build a new model
 - Economic vs. engineering approaches for estimating marginal abatement cost curves
- Brazil's revised draft MRP responds well to issues discussed with the expert group

Challenges: Cost-effective emissions reduction

- Cost-effective programs are essential for achieving necessary future emissions reductions
- Key here is some form of carbon pricing: either ETS or carbon tax
- ETS and tax are more similar than they are different
 - Both price carbon, providing incentive for cost-effective emissions reductions and flexibility in how to achieve those reductions
 - Both can provide predictable price path, compensate affected industries and households, etc.
 - Design of ETS or tax may be more important than choice between ETS and tax

Challenges: Predictable price path

- Stable, predictable future price path necessary for cost-effectiveness and to encourage technology and other investments in mitigation
- Carbon tax naturally provides stable price
- ETS prices are naturally volatile, but price ceiling and price floor provide price stability
- Under either instrument, clear guidance on future price changes needed for predictability

Challenges: Revenue

- Brazil, like many countries, faces pressure both to cut taxes and to expand government programs
- Carbon pricing can provide revenue to address this
- Carbon pricing revenue has many potential uses
 - Investments for the future (education, infrastructure, etc.)
 - Fiscal consolidation/deficit reduction
 - Revenue-neutral tax reform: cut inefficient taxes
- Carbon tax naturally provides revenue
- Auctioning ETS permits provides revenue

Challenges: Compensating industry/households

- Need to limit burden on industries and households that are vulnerable (or politically powerful)
- ETS: allowance allocation (grandfathering or benchmarking)
- Carbon tax: tax credits
 - Key is credit based on historical emissions (like grandfathering) or output (like benchmarking), rather than based on emissions
 - Tax exemptions hurt cost-effectiveness
- Either system needs to address effect on vulnerable households (use of revenue can help here)

Challenges: Enforcement/MRV

- All carbon pricing faces the challenge of measuring emissions and enforcing pricing
- Upstream carbon tax (tax on carbon content of fuels, as in British Columbia carbon tax) makes this much simpler
 - No need for facility-level MRV (except perhaps substantial process emissions, such as cement industry)
- Upstream ETS would have same advantage
- Advantage of carbon tax: already have institutional structure and capability to enforce taxes
 - Brazil could adapt existing fuel taxes into an upstream carbon tax

Thank you for your attention