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# Carbon Pricing

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## What is Carbon Pricing?

Carbon pricing is the mechanism by which the external costs of carbon emissions can be priced into business operations and financial decision-making.

Setting a price on emissions, directly or indirectly across a business' value chain helps to encourage greenhouse gas (GHG) emission reductions, driving investment towards low-carbon alternatives.

Emerging as a key policy mechanism to curb and mitigate the impacts of climate change, the same principle can be applied within an organisation to enable the true cost of carbon emissions to be factored into its growth development plans, creating budgets that can be directed towards supporting low-carbon transition planning.

> *Direct carbon pricing instruments, key policy to decarbonisation, now cover almost a quarter of global greenhouse gas emissions, according to a new World Bank report.*

Source: World Bank Press Release May 2023.

## Who uses Carbon Pricing?

Financial institutions are increasingly using carbon pricing as a tool to evaluate their investments, for example including the cost of carbon in economic analyses of new projects. Reasons include better understanding and measuring of carbon emissions and to integrate the negative externality of $CO_2$ emissions into project appraisal as part of commitments to support low-carbon solutions through their lending portfolio.

For many organisations, the most significant consequences of climate-related risks will emerge over time and their magnitude is uncertain.

As shifting regulatory and market dynamics influence the present and future cost of carbon, investors are demanding more consistent and transparent disclosures around a company's approach to embedding this potential risk within their business decisions.

Leadership is being shown by Carbon Disclosure Project (CDP), which has a module in its disclosure survey, coupled with the Carbon Pricing Leadership Coalition (CPLC), a voluntary initiative that brings together leaders from various sectors to share best practice.

### Approaches

Carbon pricing can take multiple shapes and forms – no one-size-fits-all. There are two potential approaches within organisations:

- a shadow price where a theoretical cost of carbon is included to inform decisions or,
- a carbon tax where a real fee is charged to business units to build a climate change fund for investment in decarbonisation measures.

At a country level, the two main policy levers are emissions trading systems (ETS) and carbon taxes.

## Points to consider when implementing carbon pricing:

- There's no definitive answer to what a carbon price should be – implementation is unique to each business.

- Identify the most appropriate "best fit" method by considering your climate or decarbonisation strategy and any specific constraints.

- The most important starting point is to understand the business driver for setting a carbon price.

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# Key benefits of carbon pricing

## Reduction in emissions

Carbon pricing provides a financial incentive for companies to reduce their carbon footprint. By putting a cost on emissions, organisations are motivated to invest in emission reduction projects and initiatives, as well as energy efficiency measures, including the adoption of cleaner technologies, leading to a decrease in overall GHG emissions.

## Efficiency and cost savings

By internalising the price of carbon, organisations become more aware of the financial implications of their emissions and related sources. This encourages the optimisation of resources focusing on reducing waste, exploring renewable energy, resulting in potential cost savings and increased operational efficiency.

## Stakeholder engagement and alignment

Internal carbon pricing (ICP) adoption sends out a clear message about a company's commitment towards climate change, helping to drive transparency and accountability, while fostering trust across different stakeholders – investors (aid to address portfolios that may be at risk), clients, staff, and governing regulators.

Additionally, internal carbon pricing aligns with both the climate-related reporting framework Task Force on Climate-related Financial Disclosures (TCFD) - carbon pricing is one key metric for scenario analysis and Science Based Targets (SBTs) – integrating ICP into target setting, companies can achieve greater emissions reduction.

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## Global climate commitments

Pricing carbon enables emissions reduction pathways compatible with keeping global temperature rise to well below 2°C, in line with the Paris Agreement – contributing to the global effort to mitigate climate change.

## Risk management

Setting a carbon price enables climate-related risks to be quantified when conducting scenario planning as part of risk evaluation, both physical and transitional, but also helps to ensure long term sustainability and future-proof in a carbon constrained world.

## Promotes carbon innovation and efficiency

Pricing carbon bolsters innovation and supports the development of carbon efficient technologies, as well as disincentivising emissions-intensive business practices.

## Regulatory preparedness

Organisations that implement a carbon price are better prepared for future regulations where carbon is taxed.

## Sourcing landscape – global and national context

Organisations that source or operate nationally can better understand international carbon pricing policies.

## How we can help

If you would like to learn more about how Acclaro Advisory can support you in integrating Carbon Pricing as part of your net-zero transition, please get in touch.

We help organisations maximise their performance by improving their environmental and social impacts, supporting them to achieve net zero and positive social outcomes.

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