

Reforming the EU ETS: Striking the right balance between the EU objectives of decarbonisation and competitiveness

Lessons learnt form the previous EU ETS periods

8 September 2015



IETA
CLIMATE CHALLENGES,
MARKET SOLUTIONS

What is IETA?



Cross-sectoral business association ...

Member companies from oil, electricity, banking, industry, traders, brokers, law, consulting, project developers, exchanges, verifiers, etc.

... providing a global business voice on carbon pricing & market mechanisms

Principles:

- GHG trading systems provide the most efficient means of achieving environmental objectives
- LT policy certainty is necessary to achieve cost-effective reductions
- Use of offsets/linkages to a global carbon market are effective ways to contain costs



Scene Setter

- ETS remains the centrepiece of EU's climate policy
- Current pricing reflects fundamentals
 - Sluggish economy, low manufacturing output & sagging energy demand
 - Environmental targets in line w/ low end of long term range
- Political challenges are significant:
 - Pricing signal faint for long-term investment
 - Industrial competitiveness concerns
 - Paris COP in December / EU's role as global leader
- Reform of the EU ETS has been difficult – towards a new beginning?



10 years

of
Emissions Trading
in Europe:
towards a
new beginning?

May 2015



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Looking back at the EU ETS

It has achieved emission reductions at low cost

- given its flexibility & links to the Kyoto mechanisms
- enabled decoupling of economic growth & emission reductions
- raised awareness in corporate boardrooms of the cost of carbon emissions & value of low-carbon investments

4 principles for well-functioning ETS:

- Scarcity of emission allowances
- LT clarity & predictability
- Adequate compliance periods
- Cost-containment provisions



The EU ETS has adapted to emerging challenges

Phase 3: 2013-2020: significant changes were introduced

- Auctioning: main tool for distributing allowances
- EU-wide benchmarks for calculating free allowances
- EU oversight on the amount of free allowances distributed by MS
- Creation of an innovation fund to fund low-carbon technologies

Despite these changes, a new challenge emerged: surplus of EUAs

- **Short-term measure:** Backloading of allowances started early 2014 (900 million allowances in total will be auctioned later on to avoid adding more allowances to current market)
- **Longer-term solution:** MSR changes the design of the system



Going forward - where do things stand ?

Challenges

- **Difficult reform of the EU ETS** → focus now is on shaping the EU 2030 package
 - Proposal aligns EU ETS w/ 2030 objectives & extends some elements in the Directive post-2020
- **Difficult international context** → what will the climate agreement include?

Opportunities

- **Political commitment** to maintaining the EU ETS as the main policy instrument to meet the EU's 2030 ambitions
- **Business support** for market-based-approaches to tackling climate change continues to grow



Topics of importance for the upcoming discussions

- Carbon Leakage provisions post-2020
- Overlapping Policies
- The role of international credits



Carbon Leakage Discussion

Crucial topic for market participants - central part of the ETS revision

- How to combine effective protection against the risk of CL, without putting into question the functioning of EU ETS?
- To what extent can the rules be transitional to meet the LT emission reductions, but linked to a level-playing field for industrial competitiveness?
- How can indirect costs be addressed?
- What is meant by ‘avoiding undue carbon costs’?



Parameters to assess the new carbon leakage rules

- Technical feasibility
- Political feasibility
- Effectiveness in preserving incentives
- Effectiveness in avoiding carbon leakage



Overlapping Policies Discussion

IETA's recommendation: EU ETS should remain the central pillar for reducing GHG emissions cost-effectively

If other policies are maintained, a minimum requirement should be to ensure greater transparency and comparability with the EU ETS.

Regular reviews prior to implementation & thereafter should assess the extent to which other policies achieve GHG reductions & at what cost.

Some Q to be asked if other policies are introduced:

- Is the policy a market instrument?
- Are the costs of the policy transparent?
- Are the emission reductions from the policy transparent?
- Is the most cost-effective abatement option being developed?



Role of International Credits

- Encourage carbon market solutions around the world
- Meet LT goals cost-effectively
- Important compliance options available to participants, & important contribution to sustainable development in LDCs that the private sector makes via this mechanism.

Classic “win-win” strategy: encourages global participation and lowers compliance costs for European companies.



Why is flexibility important?

- **Cost-effectiveness**

- Wider range of mitigation opportunities helps keep compliance costs down & reduces the risk of CL onto jurisdictions without a robust carbon price
- As emissions reduction targets grow more stringent, access to intl markets to decarbonise cost-effectively & maintain competitiveness will become important.

- **Global Climate Agreement in 2015 in Paris:** Imperative for global cooperation.

- **Carbon market is the key enabler for global change** as we see linkages develop amongst cap & trade systems, & more systems emerging



IETA's proposal

- Use intl credits if target increased beyond 40%
- Used by governments for reaching non-ETS target
- MS could purchase high-quality offsets from auction revenues
- Offsets can become a valuable means of cost containment at times of scarcity. Importance of strict quality standards and ensuring double-counting does not occur.
- Offsets should be available for use by airline operators as part of the future ICAO market-based-mechanism



Conclusion

- After a difficult process to reform EU ETS, we now focus on shaping the rules towards 2030
- Very different context:
 - Reform of the EU ETS has been agreed
 - Unanimous political support to ensure ETS maintains a central role towards 2030
 - Carbon markets & pricing initiatives developing globally



Thank you

Contact details:

Sarah Deblock, EU Policy Director, IETA
deblock@ieta.org

www.ieta.org



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