The EU ETS – an introduction

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The Climate and Renewable Energy (CARE) Package – WHY?

- January 2007: Communication on limiting Global climate change to 2°C:

  In international negotiations GHG reduction target of **30%** by 2020 for developed countries (vs. 1990)

  A firm, independent commitment to achieve at least **20%** GHG reduction by 2020 for EU-27 (vs. 1990)

- endorsed by the European Council (DE Presidency) in March 2007

CARE package – the elements

- <u>**The package consisted of four proposals:**</u>
- *A **review of the EU Emissions Trading Directive***
- a proposal for ***effort sharing*** by each EU Member State to meet the Community's greenhouse gas reduction commitment in sectors not covered by the EU ETS (e.g. agriculture, transport, buildings, services, smaller industrial installations and waste)
- a proposal for a Directive to create a legal framework for ***geological carbon capture and storage (CCS)***
- a proposal for a *Renewable Energy Directive*

+ *CO2 and Cars*

+ *Fuel Quality Directive*

Implementation of GHG and RES targets (20 = magic number)

<u>20-20-20: A challenge for the EU based on:</u>

- Coherent and mutually supportive approaches
- Cost-effectiveness
- Internal market
- Cohesion & solidarity
- Competitiveness

EU ETS - legislation

- **The Original:** EU ETS Directive 2003/87/EC: established a scheme for greenhouse gas emission allowance trading within the Community
- **Linking:** Directive 2004/101/EC of 27 October 2004 amended the EU ETS to include the Kyoto Protocol's project mechanisms
- **Aviation:** Directive 2008/101/EC of 19 November 2008 amended Directive 2003/87/EC so as to include aviation activities in the scheme

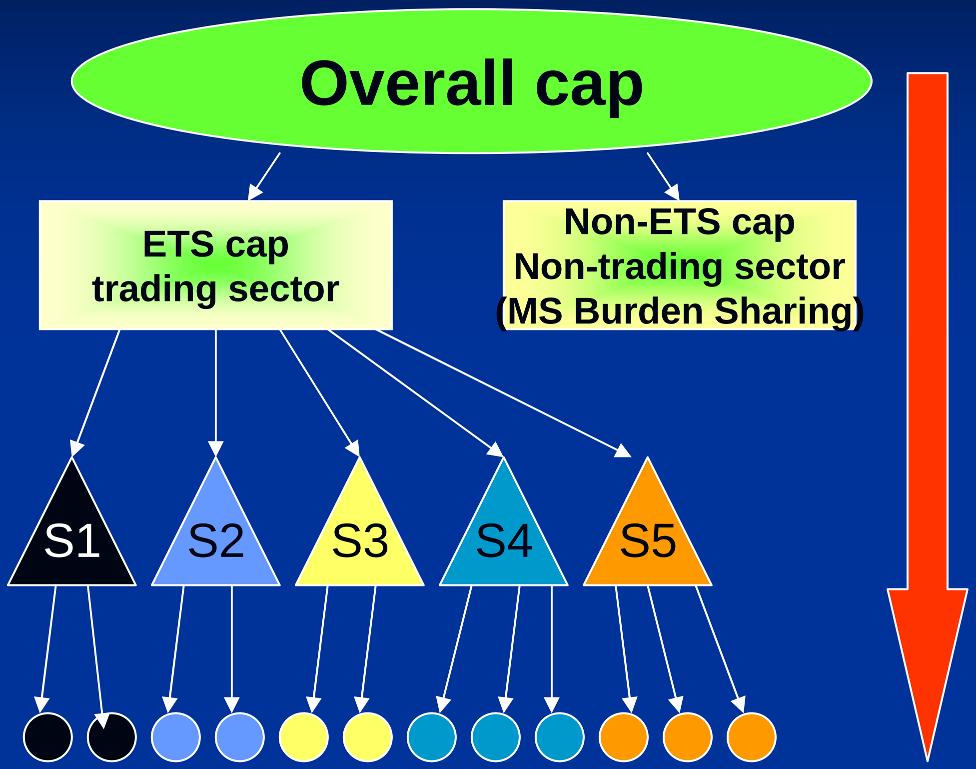
- **The Review:** Directive 2009/29/EC of 23 April 2009: amended Directive 2003/87/EC so as to improve and extend the greenhouse gas emission allowance trading scheme of the Community

- **Available at:** http://ec.europa.eu/environment/climat/emission/implementation_en.htm

The EU ETS – Why? How?

- Market-based instruments:
  - Taxes
  - Fees
  - Trading of certificates, such as the EU Emissions Trading Scheme (EU ETS)
- What is the EU ETS?
  - Coverage (sectors)
  - Gases – just CO2?
- How does it work?
  - Cap
  - National allocation plans (1st & 2nd phase)
  - Microeconomic efficiency
  - Macroeconomic efficiency?

Post 2012: EU-wide cap



- 1st step: defining ETS and non-ETS sector
- 2nd step: break down to sectors and installations
  - Free allocation (via Benchmarks) vs Auctioning of allowances

What are cap-setting and allocation about?

- Defines the scarcity at EU level
- Sets an overall limit on emissions
- Thereby ensuring the environmental integrity of an Emissions Trading System
- Applies to <u>all</u> economic sectors
- No matter what they are allocated for free, the Cap determines the amount that can be traded
- This drives the market and determines the <u>**Carbon Price**</u>

The EU ETS – leading the way

- Applicable since 1 January 2005, for 25 EU Member states (now 27 + 3 EEA countries)
- Mandatory cap on absolute emissions across more than 10,000 large energy-intensive installations across the Europe
- Covers around 2 billion tonnes of CO_2 emissions, half of our total emissions
- Simple and cost-effective approach to reducing emissions, with single market for trading allowances
- Credits from emission-reducing projects in more than 150 countries useable by companies for meeting the reduction target

Development of EU ETS (1)

- 2005-7: Start-up period - 1st Phase
- 2008 -12: 2nd Phase (1st phase under Kyoto)
- 23 January 2008: Commission unveils its Climate Package
- March 2008: Avril Doyle MEP announced as Rapporteur
- 7 October 2008: EP Environment Committee votes on the EU ETS proposal
- 17 December 2008: Parliament approves, by overwhelming majority, the revised EU ETS for the third trading period 2013-2020 as part of the EU's climate and energy package

Development of EU ETS (2)

- 28 January 2009: EU Commission sets out guidelines for a global climate change deal in its 'Road to Copenhagen' Communication
- March 2009: European Summit – Financing Global Climate Change on the Agenda
- 31 December 2009: Deadline for the publication of the Commission's list of sectors deemed to be exposed to a significant risk to carbon leakage
- March 2010: Commission Regulation on Auctioning due
- By 30 June 2010: Commission will publish the absolute Community-wide quantity of allowances for 2013
- By December 2010: Commission will publish an estimated amount of allowances to be auctioned
- 2013: Revised scheme due to enter into force.

Why did we need a review?

- Improve the functioning of the scheme based on practical implementation and experience
- Relevant for periods from 2013 onwards, as markets need regulatory stability
- Expand coverage – further sectors, gases and technologies
  - N20, CH4, carbon capture and storage, shipping (aviation previously decided on)
- Streamline design of the EU ETS
  - More harmonised approach to cap-setting and allocation
  - More predictability and certainty
  - More harmonised approach to new entrants and closures
  - Harmonisation of accreditation and verification

The main points (1)

- Harmonised cap-setting: 21% EU-wide cap for ETS sectors
- Automatic ‘trigger’: 20%-30% reduction target in case of International agreement
- Harmonised allocation: increased use of auctioning, benchmarking in many sectors, however move towards full auctioning
- Full auctioning for power sector
- Industrial sectors at significant risk of carbon leakage based on criteria agreed by EU leaders will be eligible to receive up to 100% of allowances free subject to an international climate agreement being concluded
- Harmonised new entrants: establishment of an EU-wide reserve

The main points (2)

- New fund for CCS technology development – 300million allowances!!!
- Half of all auctioning revenues should be used to finance climate mitigation and adaptation measures in Europe and the developing world.
- Half of reduction effort from 2008-20 may be covered by international carbon credits. No binding quality criteria for clean development mechanism (CDM) credits BUT buyers must report on their quality.
- In the event of a 30 % emission cut (1990 levels), half of the extra effort required may be covered by international credits
- SMEs: More excluded than originally foreseen
- The commission must propose including shipping in the scheme from 2013 if there is no international agreement by the end of 2011

The EU ETS – the International context

- ‘Linking Directive’ (2004/101/EC) amended the EU ETS Directive to allow for the use of CERs and ERUs (Kyoto Mechanisms
- Most important host countries for CDM: China, India, Brazil, Mexico
- More than half of all CDM projects relate to renewable energy (geothermal, tidal, wind, hydro, biomass or solar). Expected market for JI and CDM of up to 1.3 billion tonnes in the 2nd trading period
- Linked to EEA countries - ‘Linking’ – key aspect in drafting the Review
- Served as example for other ETS around the world: RGGI, California, New Zealand, Australia, Japan
- Waxman-Markey (Kerry-Boxer)

Final comments

- The introduction of the EU ETS in 2005 was a major achievement and signified a paradigm shift in Europe's climate policy
- The EU ETS is followed closely across the world and a successful scheme is therefore of strategic importance for the post-2012 climate architecture
- It is (currently) the only act in town and whilst it may have its shortcomings, it is still the MAIN act in town
- It is important to keep in mind that the first period of the EU ETS was established as a 'learning by doing period' for regulators and companies alike. The 2nd trading period has seen improvements in many areas.
- The review of the EU ETS further improves and extends the scheme.
- Move towards a Global Carbon Market

Thank you and Good luck!

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