

get to grips with  
**climate  
change**



# Review of the European emissions trading scheme

Brussels, 14th December 2006  
EU-Japan Centre for Industrial  
Cooperation

Damien Meadows, Deputy Head  
Market-based instruments incl EU ETS Unit  
Environment DG, European Commission





# Long term EU climate change policy objectives

- **Limiting the global temperature change to 2° Celsius above pre-industrial levels (EU Council, March 2005)**
- **Global GHG emissions to peak within 2 decades, followed by substantial reductions by 2050**
- **Emerging economies with low emission levels per capita?**
- **Order of magnitude of reductions by industrialised world:**
  - **15-30% by 2020**
  - **60-80% by 2050**



# The Carbon Market: EU ETS

- Applicable across EU since 1 January 2005
- Mandatory caps on emissions from over 10,000 large energy-intensive installations across the EU
- Covers around half of total EU CO<sub>2</sub> emissions
- Cost-effective approach to reducing emissions
- Single market for trading allowances
- JI and CDM credits can be used by companies for compliance against objective



# Why is the EU ETS so important?

- The cornerstone of Europe's strategy to reduce greenhouse gas emissions cost-effectively
- Better regulation and the Lisbon strategy – a market-based instrument for cost-effective environmental policy
- Main driver for the global carbon market
- A key structural element for climate strategy beyond 2012 that will limit global temperature increase to 2° C



# State of play

- First phase ongoing – 2005 to 2007
  - First compliance cycle successfully closed
  - Infrastructure for registries and monitoring established
  - Common data sets generated
  - Learning for both authorities and companies
- Second phase under preparation – 2008 to 2012
  - NAP submission deadline 30 June 2006
  - Commission Decisions on first 10 NAPs taken on 29 November 2006, with Communication setting out line taken on each issue
  - Equal treatment for all Member States
- Forthcoming proposal for including aviation in EU ETS



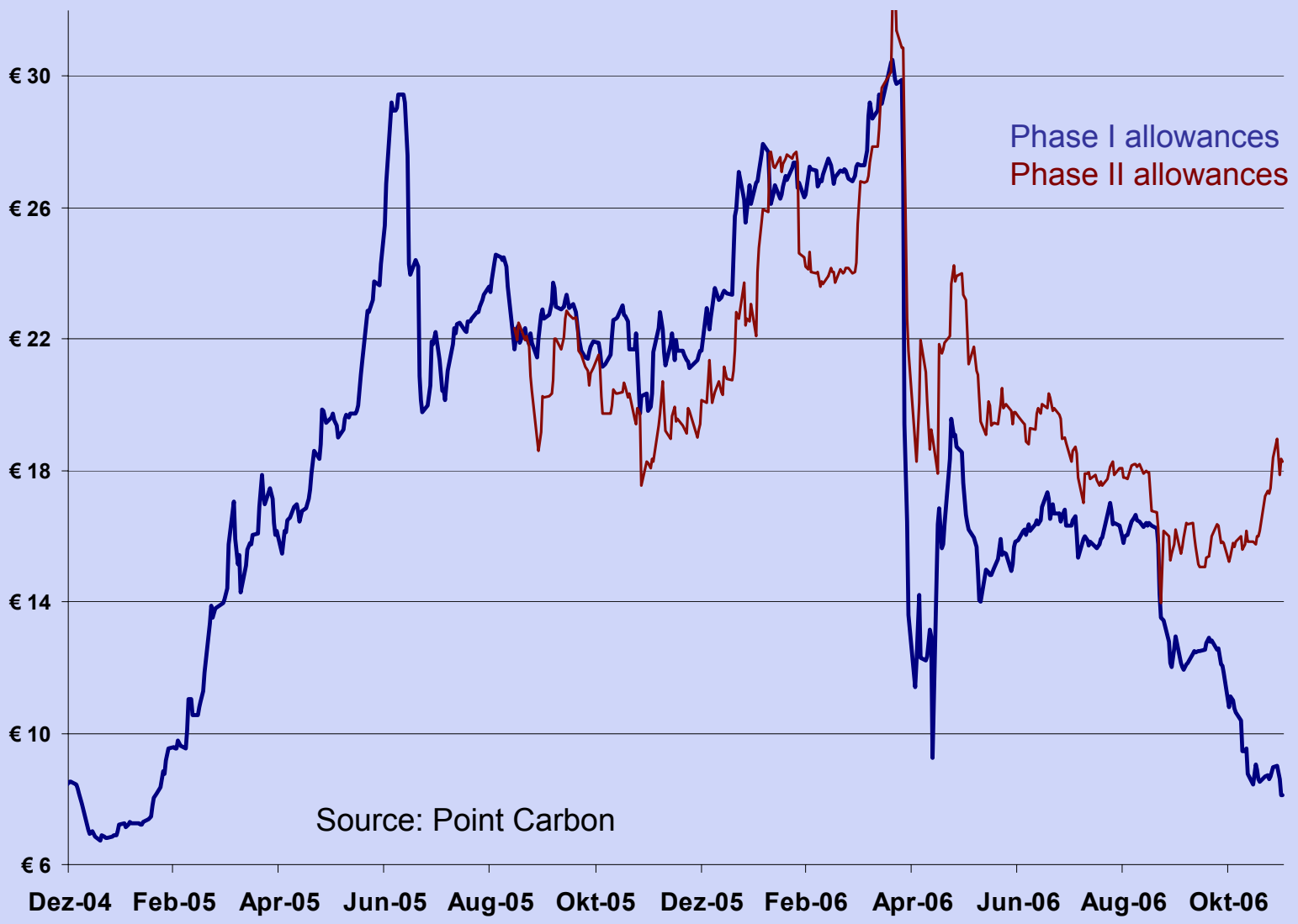
# EU ETS – the first year

- Allocation in 2005 to 2007 close to 2.2 billion allowances p.a.
  - of which some 75 million are put aside (i.e. not yet in circulation) and will be used for new entrants and auctioning
- Emissions recorded in 2005 somewhat over 2 billion tonnes

[http://ec.europa.eu/environment/climat/emission/  
pdf/citl\\_pr.pdf](http://ec.europa.eu/environment/climat/emission/pdf/citl_pr.pdf)



# EU ETS Price Development





Details about first assessments and draft  
NAPs are available at  
[http://europa.eu.int/comm/environment/climate/2nd\\_phase\\_ep.htm](http://europa.eu.int/comm/environment/climate/2nd_phase_ep.htm)

# Review process and the EU ETS beyond 2012



# Points of departure and timeline

- EU ETS remains the central instrument to tackle climate change
- Changes should take effect in 2013
  - Allocation plans are decided this year
  - Directive cannot be amended before the start of the 2nd period
  - Regulatory stability: appropriate lead-time for design changes
  - Need for more experience and stakeholder consultation
- Review report „*Building a global carbon market*“ released in November 2006
- Stakeholder consultation in a dedicated group under the ECCP umbrella – report in June 2007
- Commission puts forward a proposal to amend the ETS Directive – second half 2007



## Recommendations by the High Level Group on Competitiveness, Energy and Environment Policies

- Climate change is likely to have major negative global implications
- Global temperature increase should not exceed 2° C
- Preference for a well functioning EU ETS as a central instrument for GHG reductions
- Increase levels of certainty for investors
- Take into account the need for regulatory stability
- More harmonisation of allocation across the EU
- Advance the international policy framework post-2012
- Make significant contribution to further development of a global carbon market, consider linking of EU ETS with compatible systems emerging in other countries



# Focus areas for the review

- Improve the functioning of the scheme based on practical implementation experience
- Relevant for periods beyond 2012, as markets need regulatory stability
- Streamline current design
  - 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
  - Consider benefits and costs of smallest installations
- Expand coverage – further sectors and climate change impacts, beyond aviation, and to other emissions trading systems



# Scope of the EU ETS

- Streamline application of current scope => combustion installations
- Small installations and alternative approaches
- Expand to other sectors and gases
  - e.g.  $N_2O$  in ammonia production
  - $CH_4$  from coal mines
  - ...
- Recognition of carbon capture and storage

*ETS as part of a comprehensive and coherent policy mix.*



# More harmonised cap setting

- National allocation plan approach with assessment by the Commission brings differences with it
  - Burden sharing also stands in the way to more harmonisation
- Allocation process has two elements
  - Setting the cap
  - Distributing allowances between installations (incl. reserve)
- Various options to harmonise as regards cap-setting
  - Single EU-wide cap
  - Separate national caps: Up-front in Directive or via NAPs
  - Length of the cap setting period
  - Permanent elements in cap setting with periodic allocation decisions at installation level



# More harmonised allocation

- Auctioning
  - Full or partial auctioning
  - What (minimum) share?
  - Nationally coordinated or EU-wide auctions
  - Auction schedules and design, Market impacts
- Benchmarking
  - Suitable for which sectors
  - National or EU-wide benchmarks, How many factors per sector
  - Based on inputs (fuel use) or outputs (cement production)
  - Availability and transparency of needed data
- Caps and allocation
  - Simplicity and predictability of the allocation methodology
  - Level playing field in the internal market



# New entrants and closures

- Directive left it up to Member States to decide how to deal with new entrants and closures
  - reserve or not
  - design of the reserve
  - withholding future allocation upon closure or not
- All MS chose a reserve in first phase, but size, access and allocation criteria differed across MS
- Most MS chose to interrupt allocation following closure
- Some MS put in place nationally limited transfer rule

*The merits of keeping things simple and lean.*



# New entrants and closures

- New entrant options:
  - No reserve
    - For some or all sectors
  - If a reserve is kept, allocation should be harmonised
    - Common rules
    - EU-wide single reserve
- Closure options:
  - No closure rule
  - EU-wide rules on cross-border transfer

Longer allocation certainty

Simplicity

Low administrative burden

Appropriate incentive effects



# Robust compliance

- Robust compliance and enforcement is at the heart of a successful trading scheme
- Monitoring and reporting
  - Need for regulation on monitoring and reporting rules
  - Automation and advanced IT use
- Verification
  - Review stringency and MS oversight for verification and accreditation process
  - EU-wide accreditation process for verifiers
  - Mutual recognition of verifiers
  - Need for regulation on verification and accreditation rules
- Need for reinforced compliance provisions
  - Enforcement of verification rules (incl. site visits)
  - Provisions for no or late emission reports
  - Data inaccuracies



# Links to third countries

- Consider design of operating and planned third country schemes capping emissions at national or regional level
- Explore means and arrangements for links to such schemes
- Strengthen participation in CDM project activities
- EU-wide arrangements for authorisation of projects
- Further harmonise types of projects accepted
- Consider need for harmonised limit for JI/CDM use



# Concluding thoughts

- Europe leads the way in turning the concept of market-based climate policy into reality and a continent-wide carbon price signal has emerged.
- The review process is the opportunity to decide on the future strategic direction for the EU ETS.
- Review process faces a trade-off between quality and quantity and needs to build on experience.
- Simplicity should be a guiding principle in the review process.



**YOU CONTROL  
CLIMATE CHANGE.**



**TURN DOWN. SWITCH OFF. RECYCLE. WALK. CHANGE**

More information on EU climate policy:

[http://europa.eu.int/comm/environment/climat/home\\_en.htm](http://europa.eu.int/comm/environment/climat/home_en.htm)