

Response to the European Commission consultation on Review of the auction time profile for the EU Emissions Trading System

15 October 2012

Key messages

The Commission has invited comments on a proposed amendment of Commission Regulation (EU) No 1031/2010 (Auctioning Regulation). This provides for an auction time profile “back-loading” in the EU Emissions Trading Scheme (ETS).

Energy UK considers that the ETS today is at risk of being undermined and replaced by other policy instruments. We want the ETS to be the key policy driver for carbon reduction to 2030 and to remain integral to business operations and investment decisions in ETS Phase 3, through to 2020.

We would have preferred the Commission to propose options for permanent structural measures to strengthen the ETS, rather than back-loading. Nonetheless, we could support a Phase 3 back-loading, conditional on it being clearly linked to decisions on a 2030 carbon reduction target and beyond. The back-loading can give a signal to the carbon market – and also to international observers – that the EU is committed long-term to a strong ETS. Energy UK considers that the size of the back-loading should be meaningful, but its members do not collectively support a specific number. Any return of the back-loading should take place late in Phase 3.

Energy UK also sees the back-loading proposal as linked to wider issues. Our sector is committed to carbon-neutrality at EU level by 2050. To achieve this cost-effectively, the power sector needs a stable, long-term EU policy framework based on four key principles:

- The early adoption of an ambitious, firm, long-term, economy-wide greenhouse gas reduction target for 2030 up to 2050, in line with the European Council goal;
- The ETS to be the main policy instrument for driving investment choice in carbon reduction;
- Stronger coordination of Member State policy-making, to avoid distortion in the internal energy market;
- A resolution to the current problem of costly overlaps between the various climate-related policies.

None of these requirements is yet in place.

About Energy UK

Energy UK represents a wide spectrum of interests across the sector. This includes small, medium and large companies working in electricity generation, energy networks and gas and electricity supply, as well as a number of businesses that provide equipment and services to the industry.

Coherent policies and coherent decision-making

Energy UK is deeply concerned about the functioning of the 2008 Climate and Energy Package, and about current decision processes which will shape a future 2030 package. Policy overlaps between the instruments in the 2008 Package have resulted in a conflict between the carbon prices implicit in both renewable energy support schemes and energy efficiency measures, and the explicit EU Allowance (EUA) price. This undermines the ETS as a market tool and has the potential ultimately to destroy the competitive electricity market, at the expense of customers or taxpayers. Any solution must ensure that the ETS remains the key driver. Energy UK recognises that specific support policies for renewables and energy efficiency are likely to continue at least to 2020, but there needs to be greater coherence between climate-related policy instruments to ensure the delivery of objectives at least cost.

Further, the Package has been in constant evolution due to the national implementation of the renewables targets from 2009, subsequent revisions of these national renewables policies, the adoption of the 2012 Energy Efficiency Directive, and the carbon market “architectural and regulatory changes” which will affect the ETS as of 2013 (see the 25 July Staff Working Document). The result is extreme uncertainty for investments.

Looking ahead, the electricity sector faces additional uncertainties from on-going EU policy processes on roadmaps and climate targets, the implementation of the Energy Efficiency Directive, the report on the Renewables Directive, and the debate on ETS back-loading and structural measures. These processes are located in different parts of the EU institutions, working to different and non-aligned timetables. We therefore call for a single, coherent and finite process of EU decisions, which links together agreement on a 2030 carbon reduction target, the ETS Phases 3 and 4, the future of renewables and energy efficiency beyond 2020, and the internal energy market. This process needs to be substantially completed during the current Commission Mandate ending in 2014.

ETS structural measures and auctioning back-load

Energy UK would have preferred that the back-loading proposal had not been published separately from the Commission’s expected report on the functioning of the European carbon market, which promises to launch a thorough debate on what structural measures might be needed to address the challenges in the ETS. On its own, the back-loading proposal is not convincing, and there is no way of knowing whether the change would be temporary or permanent.

Instead, we need a clear link between the back-loading and a longer-term target. Energy UK therefore seeks a package of decisions with the following elements:

- The adoption of ambitious, firm, long-term, economy-wide, greenhouse gas reduction targets for 2030 and beyond to 2050, in line with the European Council goal;
- The Commission to propose an ETS cap aligned to the 2030 target, together with proportionate measures to revise the linear reduction factor. Some members consider this factor should have effect in Phase 3, as far as feasible, or support a Phase 3 set-aside. Others prefer a Phase 4 linear factor, taking into account impact on demand in Phase 3;
- Measures to broaden the scope of ETS by bringing in new sectors.

Energy UK looks forward to engaging with the Commission to discuss these and other possible measures to strengthen the resilience of ETS in response to external distortions. We recognise that some of the possible structural measures may require an extended legislative process. On that basis, as part of the package, we support back-loading in Phase 3 in order to give a signal to the carbon market – and also to international observers – that the EU is committed to a long-term strategy of driving carbon emission reduction through a strong ETS. By relieving the pressure of the ETS surplus,

the back-loading would also enable the EU institutions to undertake a full and thorough examination of the options to strengthen the cap permanently.

Energy UK considers that the back-loaded quantity should be meaningful and commensurate with present/future imbalances in supply and demand, but our members do not collectively support a specific number. Any return of the back-loading should take place late in Phase 3, but not during one single year.

Further to the documents published on 25 July 2012, Energy UK seeks more guidance clarifying the conditions under which the Commission will use the option to change the auction time profile:

- Definition of “exceptional circumstances [of] artificial and largely temporary imbalances between supply and demand”;
- Definition of “as appropriate”;
- Definition of the “orderly functioning of the market”, and the objectives of “a smooth transition” between trading periods and “a steadier price signal”.

In particular, does the Commission envisage that exceptional circumstances could arise other than during the transition between ETS phases? Is price volatility an indication of disorderly functioning, and what criteria are to be used to judge whether the various proposed volumes of EUAs to be back-loaded will best achieve an orderly functioning of the market?

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