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DIRECTORATE-GENERAL
ENVIRONMENT
Directorate C - Climate Change & Air
ENV.C.2 - Market based instruments including Greenhouse gas emissions trading

Brussels, 6/01/10

C.2/

ECCP STAKEHOLDER MEETING ON AUCTIONING

Venue:

Breydel building, Auditorium
45, Av. d'Auderghem-1049 Bruxelles
28 October 2009

FINAL MINUTES

WELCOME, AGENDA AND INTRODUCTORY REMARKS

The Commissions welcomed the participants and set out the agenda, which consisted in the Commission presenting a draft outline for the Auctioning Regulation on auctioning with discussion following the presentation of each individual issue. No final decisions have been made yet and the presentation reflected the DG Environment's assessment, taking into account the response to the stakeholder consultation and having had preliminary discussions with other Commission services. The Commission services should come to agreement on a proposal by the end of the year, so as to enable a vote in the Climate Change Committee (CCC) early 2010 as foreseen. This time schedule is very ambitious and whether the deadline of 30 June 2010 for adopting the Regulation will be met also depends on the vote in the Climate Committee and then the European Parliament scrutiny.

AUCTION PLATFORM, CLEARING HOUSE OR SETTLEMENT SYSTEM AND AUCTIONING MONITOR

The Commission sketched the overall architecture and entities involved in the auctioning system. The auction platform and clearing house or settlement system are to be selected through a single competitive dialogue tendering process with close involvement of Member States. The Commission also presented the time schedule foreseen for this procedure.

The European Association of Clearing Houses (EACH) highlighted that there is no harmonised regulation for central counterparties (CCPs) in Europe so far. This point was taken for future consideration by the Commission.

The Netherlands raised that, in order to maintain competition, appointing a platform for the duration of five years could be a concern.

AUCTIONING SPOT OR SPOT-FUTURES

The Commission explained its choice for auctioning spot or spot futures, but not futures.

The UK Emission Trading Group (ETG) emphasised the importance of auctioning both spot and futures.

WWF asked whether the Commission had modelled the effect of auctioning spot/futures? The Commission answered that in either case the clearing price should be very close to the prevailing secondary market price.

Eurelectric expressed its concerns on the Commission's proposal not to auction futures, as the market would not provide forwards and futures to cover the sector's hedging needs which will be very substantial. The increase of auctioning in the third trading phase implies a big change for the secondary market. Later in the meeting, Eurometaux supported Eurelectric in its views on hedging and the European Federation of Energy Traders (EFET) mentioned the results of New Energy Finance's report on the hedging needs (August 2009). The Commission pointed out that the market is already in place, and with sufficient and timely auctions of spot allowances, the market should be able to supply forwards and futures in line with the hedging needs of the energy sector, knowing that these will grow substantially. The Commission added to that that the price for futures should be established by the secondary market, the clearing price in case of auctioning futures would be very close to the secondary market price of futures. Therefore, auctioning futures or not has no financial consequences for the energy sector.

The Netherlands agreed and saw no need to auction futures.

AUCTION CALENDAR

The Commission set out how it would ensure predictability and optimal frequency by determining the auction calendar.

The International Federation of Industrial Energy Consumers (IFIIEC) asked for an explanation of what would happen in case of a low price as a result of the auction. The Commission answered that if the auction price is much below the market price, then it should not be cleared. This approach should, however, not be confused with a price-management system; there would not be a reserve price in the sense of a floor price but the force-majeure clause would make sure the revenues reflect the market price, which is in the interest of the Member States.

Eurelectric stressed the importance of enabling in a timely manner the single registry to deliver third phase allowances. The Commission replied that the timeline for the registry is tight and that a precautionous working assumption is for the single community registry to be ready in 2012. Secondly, Eurelectric stressed that a significant volume of allowances would need to be auctioned as early as 2011 and 2012 (position paper was distributed later in the meeting). In the discussion, it was clear that the key variables are: 1) the hedging needs of the energy sector, 2) the number of EUAs and CERs that will be available from Phase II and which is expected to be banked into Phase III. The Commission urged Eurelectric to provide stronger underpinning and analysis of the hedging needs. In addition, it pointed at the 300 million EUAs that will be available for CCS and Renewable energy demonstration projects,

and the EIB is expected to bring to the market a significant share of this in the form of futures already in 2011. Further analysis needed: a) how many spot allowances would be required to ensure an adequate supply of forwards and futures, b) to what extent will EUAs and CERs to be banked be brought to the market? The Commission stressed that the discussion on the 2011 and 2012 volume does not constitute a proposal for continuous discussion on annual volumes throughout the trading period. In contrast, a predictable system is required; the 2011 and 2012 volume is only a temporary start-up issue.

Following concerns expressed by WWF, the Commission replied that any scope for "games" by Member States must be avoided.

As regards the impact on electricity prices, the International Association of Oil and Gas Producers (OGP) pointed out that the cost of allowances is passed onto the customers. Netherlands confirmed that this is the case and that it is normal economic behaviour. Eurelectric replied that in the absence of liquidity, the higher risk would be passed on to the customers. The Commission replied that by having competitive markets, one would not expect absence of liquidity and the secondary market will continue to function, charging no more than a normal profit and companies will be able to hedge their risk.

AUCTION DESIGN

The Commission presented its outline for auction design: single round, sealed bid, uniform price. Tied bids would be resolved randomly. There would be a force majeure clause.

Europaia expressed concern about resolving tied bids randomly, fearing it would expose compliance buyers to risk not to get allowances. Europaia also questioned the transparency of the random selection. The Commission replied that protecting against risk of market abuse is important: random selection helps to mitigate risk of collusive bidding. The disadvantages are limited and do not outweigh the advantages. It must be kept in mind that the other potential tool to mitigate risk of market abuse, a maximum bid size, will not be applied from the outset, but will only be in the Regulation as an option for the future.

Following a question, the Commission explained that it had not decided the number of decimal points for the clearing price. Candidates for becoming the central auctioneer may make appropriate proposals.

With respect to know-your-customer checks (KYC), the Commission clarified that these checks must be as stringent and robust as those applicable in the secondary market.

PARTICIPANTS – SELLER ON BEHALF OF THE MEMBER STATES

The Commission explained that Member States must appoint (an) entit(y)(ies) to act as a seller on their behalf. Exchanges cannot themselves take positions on their own market, somebody has to step in and take the contractual responsibility. In terms of entities that can act as sellers it could be a public bank or a Debt Management Office (DMO), it can also be one entity, not necessarily 27.

AUCTION PARTICIPANTS

The Commission explained its preferred approach towards auction participation, which is based on ETS-operators and regulated entities established in the EU. This reflects the fact that auctioning is an allocation activity, where the public authorities are responsible for the primary issuance of allowances. In addition, it is easier for exchanges to do KYC as they are already dealing with licence entities, and therefore this approach is more cost efficient.

Following a question from WWF, the Commission confirmed that entities with only a personal holding account would not have direct access to the auctions. In answer to the question by Europaia, the Commission specified that those entities established both in the EU and EEA can participate. [Note: the Regulation would make an exception for ETS aviation operators which are not necessarily established in the EU or the EEA.]

PARTICIPATION REQUIREMENTS

The Commission set out its intention to potentially impose minimum participation requirements, but rely in the first place on the competitive dialogue tender process. EACH asked about any specific requirement to identify clients. The Commission answered that these would not be greater than those required in commodity market, non-authorised entities would not be allowed.

COLLATERAL

The Commission set out its intention as regards collateral.

The Commission explained that it may include a provision to ensure the possibilities for auction participants to use of EUAs as collateral despite the fact that these do not constitute a financial instrument under MiFID. This is current practice with Inter Continental Exchange (ICE). Such provisions would only apply to auctions, not for the secondary market at large. It would be up to bidders at the competitive dialogue to propose optimal collateral conditions.

As regards the seller, the Commission explained that EUAs would have to be pre-delivered in a separate blocked account before the auction.

When asked whether collateral for auctions that take place weekly is necessary the Commission responded that it is not to be decided at the moment, but in the competitive dialogue selection procedure. Member States may also decide not to take collateral for auctions, if they wish so, as it concerns in the first place their revenues. Collateral, however, also discourages participants to bid up the price, without taking delivery. Requiring collateral means that such behaviour has a cost in terms of cash flow.

The Carbon Markets and Investors Association (CMIA) asked whether there is any obligation on the exchanges to accept certain form of collateral. The Commission answered that this would not be the case: exchanges would remain free to decide what collateral to accept or not, as long as it respects minimum criteria such as being covered by the Financial Collateral Directive.

CONSEQUENCES OF DEFAULT

The Commission set out the provisions to apply to default. Notably, there would be no penalties for failure to deliver. In such cases, the auction platform would be required to offer the bidder the choice between delivery at minimum delay or return of the payment with interest.

Europaia asked what would happen if a potential clearing house involved became insolvent. The Commission assured that the contractual arrangements would provide for such hypothetical situations. It would be very unlikely and one would have to think of very, very extreme scenarios for this to happen.

Germany asked for the number of tender processes and stressed the need to find the right balance between the various criteria. The Commission confirmed a single procedure for selecting both the platform and clearing house/settlement system and agreed that the formulation of criteria is an important issue to get right. Therefore the competitive dialogue selection procedure is appropriate: broad ideas and expressions of interest will be exchanged before drafting the precise terms of reference for the selection.

In the light of managing financial and legal risks, EACH asked the option of SMEs directly becoming member of clearing houses, which the Commission had explained as one avenue for ensuring full, fair and adequate access to SMEs. The Commission referred to existing practice with at least one clearing house and clarified that, as regards insolvency, national law applies. Legislation will be conservative when it comes to payment, delivery and collateral.

Netherlands expressed concerns as regards legal complexity and asked which law would apply to the auction platform. The Commission responded that the Regulation would be directly applicable throughout the EU. Only for issues not regulated in the Regulation, national law would apply.

AUCTION MONITOR

The Commission set out its approach as regards the appointment and tasks for the auction monitor. In the discussion, the Commission further clarified that the frequency of reporting could be monthly, as the Directive requires reporting 'within one month of the auction'. Various participants stressed the importance of monitoring of absence of market abuse. The Commission agreed, but noted as well that the monitor should not reveal too much information too soon as it could actually facilitate collusion. In case collusive behaviour would be detected, the platform's market protection rules would be triggered. The Regulation should avoid duplication of protection currently present on the regulated market. At the same time, as spot EUAs do not constitute a financial instrument, spot auctions would not fall under applicable financial legislation and within the scope of enforcement authorities, so in that case (additional) rules to be negotiated in the competitive dialogue procedure would be particularly important.

FEES

The Commission explained that there would be fees only for the participating bidders, not for the Member States. Only the cost of the auction monitor would be financed directly by the revenues, rather than the fees charged to bidders. In the discussion, it was emphasised that variable fees can be expected to directly lower the bids to be submitted and thereby the clearing price and, more precisely, the difference between the clearing price and the secondary market price. Therefore, as regards overall cost for bidders, it does not make a difference whether the fees are charged to the bidders or to the authorities. The more efficient the process, the lower the fees.

OGP agreed that any cost of fees would be discounted in bidding. However since Member States had the possibility of both influencing the final fee structure and overseeing its operation along with the Commission via Climate Change Committee, it made sense for any fee costs to be paid from auction revenues as Member States & the Commission could exercise administrative control on the fee structure whereas auction buyers could not. Ireland emphasised that high fees reduce participation. Efficiency benefits all and transparency is important. For SMEs, simplicity and transparency are the best solutions. WWF mentioned that bidders paying the fees complies with the 'polluter pays principle'.

Eurometaux asked whether the fees would include infrastructure costs, to which the Commission replied that the fees would have to cover all cost of the auction platform and may include a normal business profit. The cost of infrastructure may not be very high, as existing infrastructure could be used. Moreover, a number of risks that are present in the secondary market would not be present, or would be much smaller, in auctions, notably the risk of seller's default. So the fees an exchange would offer for auctioning can be expected to be substantially lower than the fees that an exchange charges on its trading platform for the secondary market.

The Netherlands asked whether payments to 'primary participants' for indirect bidders would still be allowed. The Commission replied that this would not be appropriate, as the proposed model is not the 'primary participants' model based on DMOs, but the exchange-based model.

Eurometaux asked whether stakeholders would be given the possibility to see the terms of reference in sufficient time to give their comment. The Commission answered that this would not be possible neither appropriate. The terms of reference would be published at the same time as the Regulation.

CONFLICT OF INTEREST AND ENFORCEMENT

The Commission explained the intended provisions as regards potential conflict of interest for the auction platform, auction monitor, sellers and participants.

The Commission explained which enforcement provisions would apply. The detail level of force majeure clause, which could also apply in case of detected market abuse, is under consideration. WWF suggested financial penalties. OGP added to that that cancelling an auction is a serious issue, and it would be more appropriate to deal with it by means of a penalty.

AUCTION APPROACH

The Commission explained that for reasons of cost-efficiency, ensuring non-discrimination, harmonization, transparency, simplicity, predictability, competitiveness, optimal access for SMEs and small emitters and mitigating risk of market abuse, the centralized approach is preferred.

Eurelectric, BusinessEurope, the Netherlands, Europia, Eurometaux, OGP, EFET, the European Industrial Gases Association (EIGA), the International Air Transport Association (IATA), the UK Emission Trading Group (ETG) and WWF strongly favour the centralised approach. In the meeting, also FR, IT, MT, NL, SE strongly supported this approach (the only Member States explicitly disagreeing were DE, ES, PL and UK). Arguments raised to support the centralised approach proposed by the Commission include that the coordinated approach creates interpretation problems, higher cost and hence lower revenues, complexity, lack of transparency and additional costs would be passed on in electricity prices. In addition, the centralised approach ensures regulatory certainty.

As regards the hybrid approach, Eurelectric said its members had different views for the second best option. BlueNext raised that connecting the IT systems would be a challenge, but reusing existing infrastructure is beneficial. Nasdaq said that so far they have not opted for any of the alternatives, their slight preference is towards the centralised approach.

Business Europe stressed the urgency of the choice and in this respect IETA wondered whether, considering the timeline, there is actually a choice to consider anything else than centralised approach. BusinessEurope stressed, furthermore, that choosing a centralised approach gives the strongest message internationally. A sub-optimal process, starting decentralised and only later deciding on harmonisation, as was the case with the registries, should be avoided. Nasdaq also raised the argument that the centralised approach would facilitate discussions with third countries on linking to other emissions trading schemes.

DE, ES, PL and the UK strongly supported the coordinated approach.

The UK stressed the need of ‘fiscal sovereignty’, arguing that a common platform implies a single EU-level ‘coffer’ for the revenues and this would make it easier to divert the revenues to the Community budget later on. It raised a Commission document on the future Community budget that would raise this option. The Commission clarified that this ‘document’ is a draft from DG BUDG, which apparently has been leaked, but which has not been submitted to consultation to other services and if DG ENV would have known, it would already have given a very clear negative response, indicating that this is a ‘no-go’, not acceptable to Member States and completely incompatible with the provisions in the revised ETS Directive as negotiated with the Council and the European Parliament in December.

Germany argued that the co-ordinated approach with a limited number of harmonised platforms would have a number of positive impacts, such as allowing for competition and making use of innovation of services, institutions and products in the secondary market. Furthermore, a coordinated approach is in line with the directive, whereas there are serious legal doubts concerning a mandatory centralised approach. A centralised approach would seriously distort competition by creating a quasi-monopolist on the market with yearly 1 billion allowances for five years. As regards the latter argument, Nasdaq pointed out that the

primary market in EUAs is not the place for innovation, innovation concerns rather derivatives in the secondary market.

Poland defended its position by pointing at cultural and psychological specificities.

Spain mentioned their support for a national platform under the coordinated approach was in order to ensure access to SMEs and small emitters, which according to Spain were not well represented in the meeting. The Commission responded that the argument for SMEs is not convincing, as the centralised approach provides optimal access for all SMEs covered by the ETS and small emitters to all auctions throughout the EU, unlike the coordinated approach. Given the imperative rule of non-discrimination and openness, any special provision with a view to certain SMEs/small emitters would have to be accessible to all SMEs/small emitters throughout the EU on non-discriminatory terms. Therefore no specific benefit for Spanish SMEs/small emitters can be expected. In the end, SMEs and small emitters loose due to the lack of simplicity and harmonisation. BusinessEurope raised that, indeed, it also represented many SMEs and sectors like ceramics and paper were intensively involved in the discussions. Within an SME, there is often only one single person responsible for purchasing raw materials including emission allowances and therefore time and language are big issues for SMEs. This supports a centralised platform with translations into all European languages by Member States as foreseen by the Commission. CerameUnie confirmed the involvement, though admitted that the sector had not been able to agree on a common position.

CLOSING REMARKS

As the agenda was exhausted in one day, there was no need to continue the meeting in the morning of 29 October as originally foreseen. The Commission closed the meeting, thanking all participants for their contributions.

Stakeholder Meeting on Auctioning
28/10/2009
LIST OF PARTICIPANTS

<i>Commission</i>	
	DG ENV
	DG TREN
	DG MARKT
	DG ECFIN
<i>National experts</i>	
<i>Belgium</i>	
	Federal Ministry of Agriculture, Forestry, Env and Water Management
	Flemish Ministry of the Environment
<i>Denmark</i>	
	Danish Ministry of Finance
	Danish Ministry of Transport and Energy
<i>Finland</i>	
	Energy Market Authority
	Ministry of Employment and the Economy
<i>France</i>	
	Ministry for Ecology, Energy, Sustainable development and spatial planning
<i>Germany</i>	
	Federal Ministry of the Environment
	Federal Ministry of Economy and Technology
<i>Ireland</i>	
	Environmental Protection Agency
<i>Italy</i>	
	Ministry of Economic Development
<i>Latvia</i>	
	Ministry of the Environment

<i>Lithuania</i>	
	Permanent Mission of Lithuania to the EU
<i>Malta</i>	
	Ministry of Finance, the Economy and Investment
<i>Poland</i>	
	KASHUE
	Ministry of the Environment
<i>Portugal</i>	
	Ministry of Finance
<i>Slovakia</i>	
	Ministry of Finance
<i>Spain</i>	
	Ministry of the Environment
<i>Sweden</i>	
	Swedish Energy Agency
<i>The Netherlands</i>	
	Ministry of Environment
	Ministry of Economic Affairs
<i>United Kingdom</i>	
	DECC
<i>Industry</i>	
	IATA
	Eurometaux
	BusinessEurope
	Eurelectric
	IETA
	EIGA
	ETG
	Eurelectric

	Cembureau
	Eurelectric
	IFIEC
	Eurelectric
	OGP
	CEFIC
	Europia
<i>NGOs and other Institutions</i>	
	Polish Power Exchange
	ECSDA
	LCH Clearnet
	Friends of the Earth
	WWF
	Eurexchange
	Bluenext/ECS