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WWF Response to the European Commission public consultation on a measure to introduce further quality restrictions on the use of credits from industrial gas projects

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WWF welcomes the opportunity to contribute to the discussions on quality restrictions on the use of credits from industrial gas projects in the EU ETS. This is the first implementation of Article 11a paragraph 9 of the new EU ETS Directive which establishes option for quality criteria to be introduced from 2013. We hope that this first initiative from the Commission will be followed by other types of restrictions, especially on CDM credits from supercritical coal and non-additional large hydro, so as to increase the credibility and environmental integrity of the European carbon market.

In order to secure a strong post-2012 climate regime, we need deep carbon emission cuts by developed countries in line with the recommendations of the IPCC (domestic reduction by 25-40% below 1990 levels in 2020 for the developed countries as a group). Simultaneously, we also need significant deviations from BAU in developing countries. In the long term, emissions must be reduced by 80% below 1990 levels by 2050.

Offsetting does not reduce GHG emissions. Offsetting provides an alternative to reducing emissions in industrialised countries, i.e. it is at best a zero sum game for the climate. For every tonne of CO_2-equivalent reduced by the CDM, a country or a company buys the right to emit a tonne of CO_2 at home. As such, the ability to offset through purchased emissions reduction credits reduces the need to structurally adjust the emitter's carbon profile to a less carbon intensive one, country and company alike.

Furthermore, offsetting has lock-in effects for industrialised countries. Weak targets by developed countries in combination with an over-reliance on offsets is slowing down their efforts to modernise and transform their economies for the low-carbon future. They carry on polluting and locking themselves into high carbon infrastructure, such as new coal-fired power stations. Within international negotiations, it has become clear that even if regions go to the higher end of their emissions 2020 reductions pledges and close the numerous loopholes such as accounting for LULUCF, hot air, double counting, and offsets, we are faced with a multi-gigatonne gap.

Considering the poor quality of offsets, it is probable that offsetting actually increases emissions globally. WWF is concerned about the lack of quality of certain types of credits entering the EU ETS, such as HFC-23 and N_2O (from adipic acid) credits, with the following negative consequences:

- Since the introduction of these credits on the European market does not represent real emissions reductions, their use for compliance by European companies results in an increase in global emissions;
- This puts at risk the overall credibility of the EU ETS as a relevant instrument to fight against climate change;
- The CDM appears to have caused significant carbon leakage during the economic downturn in 2008 and 2009, as indicated by plant utilization and international trade patterns.
- The use of bad quality credits in the EU ETS is often used by opponents to the system as an argument against cap & trade in general and discredits this market-based instrument globally, making it harder to "sell" it in other regions of the world. In that regard, it is interesting to note that discussions over the introduction of a cap & trade system in the US had excluded the use of HFC-23 credits from the beginning.

HFC-23 – Strict ban needed

The lack of quality HFC-23 projects in the CDM has become the focus of media attention over their lack of environmental integrity. New evidence by CDM Watch and other NGOs[1] shows that the current CDM methodology creates perverse incentives for plant operators to artificially increase HCFC-22 production, from which HFC-23 is an unwanted by-product. This means that some of the carbon credits generated by these projects do not represent real emission reductions, introducing hot air in the system. This has the potential to seriously undermine global emission reductions, harm the objective of the CDM and threaten the achievement of HCFC phase-out objectives pursued under the Montreal Protocol, to which the EU is a signatory. The Montreal Protocol would provide a more appropriate forum for HFC-23 abatement than the CDM.

In the EU, over-allocation and generous quotas for external credits in the 2008-2012 period combined with the weak 20% GHG reduction target up to 2020 will result in a business-as-usual CO_2 development pathway scenario up to 2020. To limit global warming to less than 2° compared to pre-industrial times, industrial regions like the EU must reduce their greenhouse gases by 95% by the year 2050. CDM HFC-23 projects which produce artificial credits to offset emissions in industrial countries appear particularly counter-productive to achieve this objective.

For these reasons, WWF is resolutely opposed to the use of credits from HFC-23 abatement projects for compliance under the EU ETS. We call on the Commission to implement a strict ban on the use of credits from HFC-23 abatement projects in the EU ETS as soon as possible, i.e. at the very latest as of 1 January 2013. To be effective, this ban shall apply to all emission reductions that were generated after a certain cut-off date that is no later than 1 January 2013 and must strictly prohibit holders of HFC-23 CERs from "banking" these credits for use in Phase III of the EU ETS. WWF sees this restriction as an essential means of addressing the enormous number of HFC-23 credits that have not yet been surrendered. In addition to undermining the environmental integrity of the EU ETS during Phase II, unsurrendered credits also pose a serious risk to the success of Phase III of the

[1] http://www.cdm-watch.org/wordpress/wp-content/uploads/2010/07/HFC-23_Policy-Briefing1.pdf

EU ETS if banking is allowed. This ban would also provide the scarcity and carbon price needed to shift investment to good quality projects and contribute to a low carbon economy within the EU.

N_2O from adipic acid – imminent need for quality standards

This case is very similar to the destruction of HFC-23: the revenues from CERs can exceed the costs of adipic acid production. As a result of these incentives, all registered CDM projects run at high production levels, while production is going down in plants *with abatement but no CER production* in Singapore, the USA and other Annex I countries. During the economic downturn, the production in non-CDM plants dropped significantly, whereas the CDM plants produced more adipic acid than the plant operators themselves had assumed prior to the registration of the CDM. This ongoing carbon leakage already results in the issuance of millions of CERs without any real emission reductions. There are currently four projects registered that are expected to deliver more than 161 million CERs by 2012. A recent study commissioned by CDM Watch[2] sets out serious concerns that about 20% of the CERs issued for CDM adipic acid plants for 2008 and 2009 – totalling to about 13.5 Mt CO_2e – are a result of carbon leakage and do not represent real emission reductions.

An immediate revision of the crediting methodology that takes into account the voluntary benchmark of 90% applied by many non-CDM adipic acid plants could potentially be a step in the right direction in terms of putting an end to the carbon leakage created by the CDM. Since the CDM Executive Board has so far failed to take appropriate action, WWF is opposed to the use of credits from N_2O from adipic acid abatement projects in the EU ETS. We call on the Commission to implement a strict ban on the use of credits from N_2O from adipic acid abatement projects in the EU ETS as soon as possible and at the latest by 1 January 2013. To be effective, this ban shall apply to all emission reductions that were generated after a certain cut-off date that is no later than 1 January 2013 and must strictly prohibit holders of adipic acid N_2O credits from "banking" these credits for use in Phase III of the EU ETS. This restriction is ultimately necessary to provide the scarcity and carbon price needed to shift investment to good quality projects.

WWF believes that the EU must entirely prohibit the use of these credits from the EU ETS unless the CDM Executive Board adopts an ambitious benchmark that fully takes account of the high levels of abatement that can be achieved at non-CDM adipic acid plants. A discount factor at EU level is not recommended. If applied before the CDM Executive Board has revised the crediting methodology to include an ambitious benchmark, a discounting factor at EU level could even have the indirect effect of enabling the CDM EB to postpone indefinitely the application of such a factor.

Additional concerns over the lack of sustainable development benefits

WWF has always expressed concerns over the lack of sustainability benefits of industrial gas projects in host countries, which goes against the Kyoto Protocol's twofold objective of

[2] Industrial N2O Projects Under the CDM: Adipic Acid - A Case of Carbon Leakage?, Lambert Schneider, Michael Lazarus, Anja Kollmuss, Stockholm Environment Institute, October 9, 2010

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simultaneously delivering GHG emission reduction and contributing to sustainable development. This is an additional argument to ban the use of those credits in the EU ETS: since the CDM Executive Board has been inactive on fixing this shortfall over the years, we think it is the role of the EU, as the largest CDM user and buyer, to intervene to protect the integrity of its own system.

Need for equivalent quality restrictions in non-ETS sectors

Although we are aware that new quality restrictions on the use of credits only apply to credits entering the EU ETS and that the EU Commission does not have a formal authority on the use of credits used by Member States to comply with their obligations in non-ETS sectors, we think that Member States must be encouraged to apply equivalent unilateral quality restrictions that ban the use of credits from HFC-23 projects and N_2O destruction from adipic acid plants. These unilateral quality restrictions shall also include the prohibition of banking for sectors covered by the Effort Sharing Decision. Decisions by Member States in that direction would send a strong signal to the CDM Executive Board to increase scrutiny over bad quality CERs and to enhance the environmental integrity of the CDM.