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EUROPIA Response to the public Consultation on structural options to strengthen the EU Emissions Trading System

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EUROPIA supports the EU ETS as the EU's 'flagship instrument' within its energy and climate policy framework. At the same time, EUROPIA is opposed to any regulatory intervention in the ETS with the overt intention to alter the EU ETS price.

Any structural adjustment of the ETS should address the longer term picture (i.e. post 2020) taking a broader view of climate, energy and industrial factors and in particular looking at global action. Therefore we regret that most of the proposed structural measures in the Commission's report on '*The state of the European carbon market in 2012*' dated 14 November 2012 focus on short-term supply-demand adjustments and do not provide longer-term solutions. We fear that implementing these options would only result in piecemeal intervention, with potentially negative impacts on the effectiveness of the EU ETS. The "do nothing" option, for Phase 3 should also be examined so that any proposed intervention must be fully justified in terms of impact having first considered the option and consequences of no action.

For these reasons, as part of the debate on the post-2020 framework, EUROPIA would welcome further proposals from the Commission that:

- are capable of being implemented after 2020;
- address both ETS and non-ETS sectors; and resolve the double regulation effects of Renewables and Energy Efficiency measures, in particular, on the existing sectors covered by the EU ETS;
- are accompanied by a careful assessment of the impact on current ETS sectors;
- take into account the level of advancement in negotiations at international level and possible carbon leakage effects (as per Article 28 of the ETS Directive[i]).
- allows the current mechanism of free allocation as compensation to continue to provide an effective means to protect industry from carbon leakage and should therefore continue after 2020;

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Regarding the options that have been put on the table by the Commission

Option a: Increasing the EU reduction target to 30% in 2020
The EU has committed not to increase its target unilaterally until other developed countries commit themselves to comparable emission reductions, and economically more advanced developing countries contribute adequately according to their responsibilities and respective capabilities. Unilaterally increasing the EU's CO2 reduction target will impact the competitive position of the EU economy without having any noticeable impact in terms of global CO2 mitigation.

Option b: Retiring a number of allowances in phase 3
EUROPIA is against such intervention, because the EU ETS is currently responding to the economic conditions in Europe and therefore working as designed. In addition, EUROPIA has concerns as to the regulatory precedent that such an intervention would set. Moreover, the set-aside approach as a one off intervention would not address any concerns on aligning supply and demand over the longer term.

Option c: Early revision of the annual linear reduction factor
This option would also represent a unilateral increase in Europe's commitment pre 2020 and would change the overall trajectory of the system without corresponding international action. In addition, if the linear factor continued post 2020, its impact on carbon leakage would have to be carefully examined.

Option d: Extension of the scope of the EU ETS to other sectors
In its Carbon Markets Report, the Commission has referenced extending coverage to energy related CO2 emissions in sectors currently outside the EU ETS. There is already existing provision for such inclusion under EU ETS '*Article 24 Procedures for unilateral inclusion of additional activities and gases.*

However any sector or gas for inclusion should be considered on its own merits rather than as an option for tightening the scheme by underestimating the future emissions of a sector or gas as part of an enlarged EU ETS cap.

The Commission's report mentions the potential inclusion of CO2 emissions in fuel consumption in other sectors. Relevant to EUROPIA would be the surface transport sector. But any inclusion would need to be carefully assessed to ensure that such inclusion would be more effective than other alternative and/or existing measures.

The current EU ETS had been designed for direct emissions from large emitters: the EU electricity generation and energy intensive industry sectors. In order to cover direct emissions from millions of small sources in an extended EU ETS, a large revision of the system would be required in the definition of the obligated parties - currently almost all sources would be excluded under EU ETS provisions for small emitters. For example, an indirect or "upstream" scheme obliged for surface transport (e.g. obligation on the duty point, or point of import) would introduce significant complexity and entail significant revision of the monitoring, reporting and verification rules.

To include the transport sector in EU ETS, existing policy measures to tackle transport efficiency and emissions would need careful review and amendment to prevent double regulation or additional cost which could damage the economy;

Option e: Limit access to international credits
EUROPIA supports the use of international offsets in EU ETS which are subject to robust reporting monitoring and verification, and are additional in terms of emissions reductions compared to what would have otherwise occurred. International credits also facilitate international participation in GHG emissions

reduction thus paving the way towards an international agreement and or bilateral agreements with other nations. Finally, since this option has already been partially exercised by the Commission via restrictions in industrial gases, the potential restrictions placed on non-LDC credits post 2012 in Phase 3, and more recently ERU project credits, this option would have little effect.

Option f: Discretionary price management mechanisms

Discretionary price management is particularly controversial because the carbon price mechanism could become more a product of administrative and political decisions, than a result of the interplay of market supply and demand. Setting a price floor or creating a carbon price reserve could also reduce the efficiency of the market, and would interfere with the market mechanism setting the price between supply and demand. The implications of these options would require careful review.

We note the Commission's options are non-exhaustive: as a contribution to the debate on the reform of the EU ETS, we observe that under Article 9a (4) - *Adjustment of the Community-wide quantity of allowances',* there is an amendment to the cap for Article 27 'opt-out' installations "...*the Community-wide quantity of allowances to be issued from 1 January 2013 shall be adjusted downwards to reflect the average annual verified emissions of those installations in the period from 2008 to 2010, adjusted by the linear factor referred to in Article 9."* However, there is no such adjustment to the cap for closed and/or partially closed installations.

In conclusion, the so called structural changes proposed do not appear to address the longer term structure of ETS within a broader climate and energy policy but seem more targeted at following on from an assumed back loading of allowances in the short term (pre 2020) to remove these set aside allowances on a permanent basis.

EUROPIA is ready to participate in a debate on true structural reform of ETS. We reiterate our position of supporting the EU ETS as the EU's 'flagship instrument' within its energy and climate policy framework, but, at the same time, EUROPIA is opposed to any regulatory intervention in the ETS with the overt intention to alter the EU ETS price.

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[i] Article 28 "Adjustments applicable upon the approval by the Community of an international agreement on climate change"

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