

European Commission
Directorate General Climate Action
Avenue de Beaulieu, 5
B-1049 Bruxelles

--- POSTAL ADDRESS:
Statkraft AS
P.O. Box 200 Lilleaker
NO-0216 Oslo, Norway

--- VISITING ADDRESS:
Lilleakerveien 6
NO-0283 Oslo

Att.: Unit B1 - Implementation of ETS

--- PHONE:
+47 24 06 70 00

YOUR REF./DATE: OUR REF.: PLACE/DATE:
Oslo, 27.02.2013

--- FAX:
+47 24 06 70 01

--- INTERNET:
www.statkraft.com

--- E-MAIL:
post@statkraft.com

--- VAT REG.NO.: NO-987 059 699

**CONSULTATION ON STRUCTURAL OPTIONS TO STRENGTHEN
THE EU EMISSION TRADING SYSTEM**

Statkraft AS is an organisation, registered in the EU Transparency Registry as Statkraft AS, Register ID Number: 96327066302-56

Statkraft welcomes the launch of this stakeholder consultation as the start of a debate on structural reforms of the EU Emissions Trading System (ETS).

Statkraft supports the EU's 2050 emission reduction ambitions, which are based on scientific recommendations to avoid dangerous climate change. We believe that becoming significantly less carbon-intensive is conducive to making Europe more sustainable and competitive in a future world. It is important, however, to choose the most cost-efficient instrument in order to follow that path and the ETS fulfils that requirement as it drives low-carbon investments according to technology-neutral, EU wide and market based principles.

It is important to link both the process on structural ETS reform to the overall post-2020 framework on long-term targets towards 2050, as well as the role of the ETS in relation to other policies, such as renewables and energy efficiency. The ETS should be reinforced as the central pillar of the EU's climate policy, as intended in the Climate and Energy package, and other instruments should be designed in a complementary and coordinated way. Failure to do so may result in a patchwork of national regulations and contribute to fragment the internal energy market.

Statkraft concurs with the Commission in its analysis of the current emission allowances surplus in the ETS. Based on that surplus, the current low carbon prices do not give strong enough signals to support the low carbon investments that are required if Europe is to move towards its long-term ambitions in a cost-efficient way. On the contrary, possible misallocated investments into technologies that lock-in unnecessarily high emissions for decades will hamper economic recovery and make future emission reductions more costly.

Statkraft believes that emission reductions should be achieved by all sectors covered by the ETS. At the same time we acknowledge the threat of carbon leakage, as long as other countries are not implementing similar systems to put a price on greenhouse gas emissions. In the absence of a more enhanced international carbon market, a fair compensation towards industrial sectors and energy intensive industries that are exposed to global competition may be necessary to maintain industry competitiveness and to minimize carbon leakage.

Statkraft view on the six structural reform options

Statkraft has assessed the six structural options outlined in the EC carbon market report in more detail below.

With the current oversupply in mind, Statkraft emphasizes the urgency of these reforms to prevent any lock-in of carbon intensive investments and to restore confidence in the ETS as the main instrument of EU climate policy. Structural reforms should be realistic to ensure that they can be implemented within the shortest possible time and should be linked to specific emission reduction targets beyond 2020. Furthermore, they should limit the need for future political interventions by ensuring that the ETS is robust and flexible enough to cope with external future “shocks” to the supply/demand balance, whilst at the same time enhancing predictability for market participants.

In terms of addressing the surplus and long-term ETS ambition level, Statkraft considers that option c) (early revision of the linear factor) should be implemented as a matter of priority, as this option addresses the fundamental shortcoming of the system that affects its effectiveness in the short and longer term, possibly combined with the permanent retirement of allowances in phase 3 (option b).

a. Increasing the EU reduction target to 30 % in 2020

Statkraft acknowledges the intention of this option to ensure that the EU's GHG reduction target is set at a level consistent with the 2050 low-carbon roadmap. However, given the time required for such a legislative decision, we would argue that setting binding targets for the period beyond 2020, namely 2025, 2030 and 2040 should be prioritized, as this would be more realistic and provide a clear, predictable guidance on the longer term direction for market participants.

b. Retiring a number of allowances in phase 3

With the current oversupply and the urgency to restore the market balance, Statkraft is of the view that option (b) is not sufficient in itself, but could be combined with a subsequent revision of the linear factor (option c) in order to bring the retirement into alignment with the post 2020 targets. While a permanent retirement of allowances in phase 3 would remove part of the excess supply and could be implemented relatively quickly, it does, in Statkraft's view, not provide the necessary long-term signal to investors in itself and consequently it does not provide a signal that the ETS remains the main instrument in EU's climate policy. The case for option (b) depends on when the revised linear factor can come into effect. Option (b) is viewed as a means to buy time while implementing option (c). We note that a retirement would affect only auctioned EUAs and not free allocations, thereby maintaining the regulatory stability of the wider legislative ETS framework for phase 3 for the industry sectors.

c. Early revision of the annual linear reduction factor

Statkraft gives highest priority to option (c). A revision of the linear reduction factor is necessary in order to put the EU on a pathway that is consistent with its long-term goals. This option has the clear merit of providing a stable long-term framework, allowing for the covered installations to anticipate in an early stage on the long-term targets. This avoids stranded investments and contributes to economic recovery. The decision to change the annual linear reduction factor should therefore be taken as soon as possible in order to restore trust in the ETS as an instrument, while providing predictability for market participants.

We note that revising the linear factor will not by itself solve the problem of the ETS surplus without an accompanying resolution of the problem of policy overlap, which needs to ensure that the deployment of mature renewables and energy efficiency is driven by the carbon price.

d. Extension of the scope of the EU ETS to other sectors

This is not Statkraft's prioritised option for structural reforms of the EU ETS, although we support the need for a full impact assessment on sectors and gases to be considered within a new energy and climate policy framework. Although extending the scope of the ETS to other sectors is consistent with the goal of cost-effective economy-wide carbon reductions and the completion of the harmonised internal energy market, the inclusion of other sectors is complex and should be investigated carefully. The discussion about which sectors to include and the caps in those sectors is likely to be lengthy and the inclusion of other sectors should in any case not be used as a tool to solve the oversupply of the currently covered sectors.

e. Limit access to international credits

Statkraft does not support option (e), but believes that the EU should aspire to finding ways to increase demand for emission reductions in third countries while maintaining the integrity and balance of the EU ETS. International credits were meant to facilitate global emission reductions by allowing EU companies to lower their compliance costs by using a limited amount of such credits stemming from investments in developing countries, thus also furthering technology transfer to these countries. In addition, international credits can be used in other national compliance systems and they therefore promote linking between different carbon markets and the development of a future global carbon market. For this reason, the use of international credits should be seen in connection with the ongoing UNFCCC process towards an international agreement and the overall ambition level in the EU and internationally.

f. Discretionary price management mechanisms

Statkraft is of the opinion that a mechanism to manage the supply within the ETS is preferable to a mechanism that manages the price directly. The carbon market is the only known market where there is no supply reaction to falling demand. Given the long time-horizon for setting reduction targets, the ETS could benefit from a mechanism addressing flexibility on the supply-side with the aim of increasing market confidence. Managing the price directly, however, removes the market aspect of the scheme, which could lead to inefficiencies and higher overall reduction costs. A well-designed mechanism to manage supply can make the ETS instrument more robust to external changes/shocks (e.g. economic downturn) and improve the overlap between the ETS and other complementary policies. Based on the above, Statkraft supports a full impact assessment on a supply management mechanism that would function in a

transparent and predictable way to ensure that the EU ETS is able to respond to changing external situations in the future.

In summary, the early establishment of a binding EU-wide GHG emission reduction target beyond 2020, consistent with the 2050 low-carbon ambition, should be the main driver for the EU ETS. A strengthening of the annual linear reduction factor is the preferred tool to reach these targets, possibly combined with the permanent retirement of allowances in phase 3. Statkraft welcomes the start of the debate on structural measures to reform the EU ETS, and we re-emphasize the urgency of such structural reforms and a clear post-2020 policy framework to restore the credibility of the EU ETS as the central pillar within EU climate policy.

Yours sincerely,
for Statkraft AS



Steinar Bysveen
Executive Vice President Corporate Development