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## **Contribution of Greenpeace European Unit to the European Commission consultation on structural options to strengthen the EU Emissions Trading System**

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### **Our main messages:**

- ✓ Greenpeace sees an important role for a well-functioning ETS in an integrated, coherent and mutually supportive mix of policy instruments driving the safe and sustainable decarbonisation of the EU economy.
- ✓ Greenpeace supports a 30% domestic greenhouse gas reduction target for 2020 to bring the EU on track towards meeting the higher end of the 80 to 95 percent reduction objective.
- ✓ Greenpeace supports the retirement of an auctioning volume of 2.2 billion allowances between 2016 and 2020. The retirement will rebalance the ETS, which is expected to build up a surplus of over 2 billion allowances by 2020. Moreover, permanent retirement will bring the EU's emissions pathway in line with its long-term climate objective.
- ✓ Greenpeace supports a stricter linear reduction factor as part of a 2030 climate and energy initiative.
- ✓ Greenpeace supports further EU restrictions on low-quality CDM and JI credits, such as coal-based CDM credits, in phase 3 of the ETS. Greenpeace is opposed to the use of offsets in phase 4 of the ETS (domestic greenhouse gas reductions only).
- ✓ Greenpeace is opposed to extending the scope of ETS to road transport. Greenpeace supports the inclusion of aviation and maritime transport in the ETS.
- ✓ Greenpeace does not support price management in the ETS.

## ***Our profile***

Greenpeace is an independent global campaigning organisation that acts to change attitudes and behaviour, to protect and conserve the environment and to promote peace.

Greenpeace is present in 40 countries across Europe, the Americas, Asia, Africa and the Pacific. To maintain its independence, Greenpeace does not accept donations from governments or corporations but relies on contributions from individual supporters and foundation grants.

Greenpeace European Unit is part of the international Greenpeace network. Based in Brussels, we monitor and analyse the work of the EU institutions, expose deficient EU policies and laws, and challenge EU decision-makers to implement progressive solutions.

## ***Introduction***

Greenpeace welcomes that the European Commission seeks the view of stakeholders regarding the six outlined options for structural measures in order to tackle the growing structural supply-demand imbalance in the EU's Emissions Trading System (ETS).

Climate change is creating a high number of socio-economic, security and environmental risks for the European Union. In particular, Europe is vulnerable to increased risks for coastal and river flooding, droughts and forest fires, and their damaging impacts on food production, water management, biodiversity and human health. With proposals for more ambitious EU climate and energy policies, including a well-functioning ETS, the European Commission can show that it is genuinely trying to mitigate climate change risks.

With global carbon dioxide emissions reaching a new record of 34 billion tonnes in 2011<sup>1</sup>, the urgency of climate action is greater than ever before. On a global level, pledged greenhouse emission reductions are not consistent with holding global temperature increase below two degrees Celsius (2° C). According to UNEP, an emission gap of 8-13 Gigaton exists between an emission pathway consistent with 2° C and currently pledged action for 2020<sup>2</sup>. The EU's inadequate emission reduction target of 20% by 2020 is contributing to this gap and falls outside the 25 to 40% emission reduction range indicated by the Intergovernmental Panel on Climate Change (IPCC) for holding temperature increase below 2° C.

Greenpeace sees an important role for a well-functioning ETS in an integrated, coherent and mutually supportive mix of policy instruments driving safe and sustainable decarbonisation of the EU economy. In addition to the ETS, other policy instruments and targets are required, such as performance standards (e.g. for cars or electric appliances), binding EU renewable energy and EU energy savings targets, as well as complementary carbon and energy pricing mechanisms.

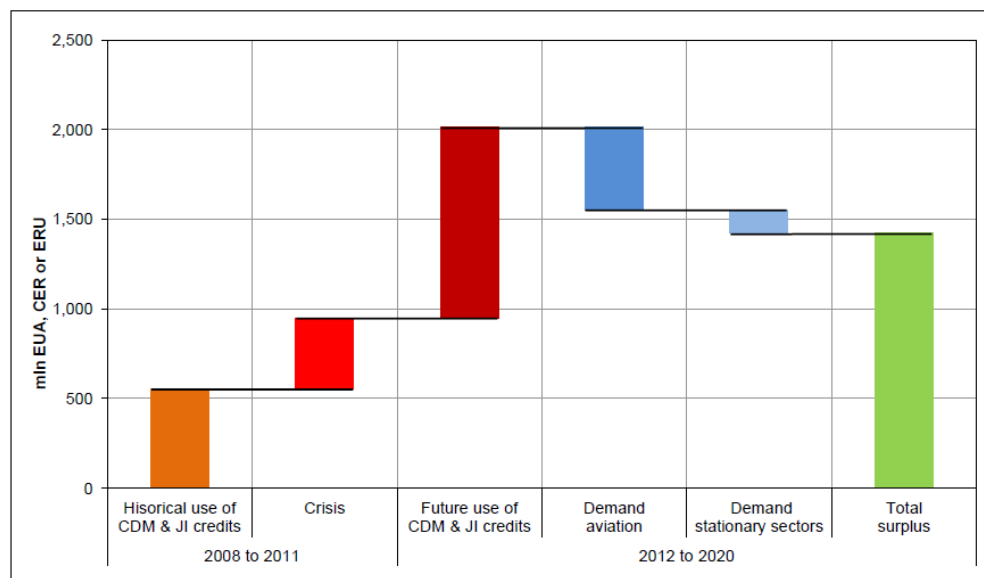
Greenpeace is concerned that due to the current lack of scarcity of emission allowances in ETS, the EU risks locking in costly and inefficient carbon-based infrastructure and will fail to drive investments in energy efficient and green technology. The burden of such a technology lock-in undermines economically responsible action to address climate change. We are especially concerned with the recent surge in European coal consumption, due to low carbon prices and changing dynamics in global energy markets.

***Evaluation of the current functioning of the market***

Greenpeace commissioned, jointly with WWF, a report by Öko-Institut assessing the current situation in the ETS<sup>3</sup>. The main findings of the Öko-Institut on the current situation include:

- Considering the cumulative surplus of emission allowances of 950 million in 2011, Öko-Institut projects the surplus to reach 1.42 billion emission allowances by 2020. The surplus would undermine the effectiveness of the EU ETS price signal until 2024.
- The main causes of the surplus are the major inflow of external emission reduction credits from the Clean Development Mechanism (CDM) and Joint Implementation (JI) and the long-term impacts of the economic crisis (see figure 1 below).
- Support for renewable energy sources had a negligible effect on the current surplus given that the share of renewable energy was taken into account when setting the cap.

*Figure: Evolution of the EU ETS surplus<sup>4</sup>*



Source: Calculations by Öko-Institut

### ***Options for structural measures to strengthen the ETS***

Following the numbering of the consultation document we have outlined per option our position and expectations regarding the impact on:

- emission reductions;
- the ability of the ETS to meet the EU long-term target of an 80-95% reduction in a cost-effective manner;
- employment and households.

Employment effects are provided on the basis of the Energy [R]evolution report prepared by DLR, institute of Technical Thermodynamics, Department of Systems Analysis and Technology Assessment (commissioned by Greenpeace and EREC)<sup>5</sup>. Only direct employment is included, namely jobs in construction, manufacturing, operations and maintenance, and fuel associated with electricity generation and direct heat provision.

#### *a. Increasing the EU greenhouse gas reduction target to 30%*

Greenpeace supports increasing the EU greenhouse gas reduction target to 30%, as this would help close the 2020 global emissions gap identified by UNEP<sup>6</sup>. Moreover, increasing the EU greenhouse gas target would contribute to the EU's long-term target of 80-95% reductions in a cost-effective manner.

But a move to a 30% target would only lead to additional greenhouse gas emission reductions when the reduction efforts are realised domestically (within the EU). The EU should not allow further use of offset credits in the ETS and Effort Sharing Decision when stepping up to a 30% target. In particular, the ban on the use of forestry credits and other low-quality credits must be continued. Also, under a 30% reduction target, LULUCF emissions should not be covered by the EU Effort Sharing Decision.

In the Energy [R]evolution scenario (delivering 30% domestic reductions by 2020) there are in 2020 1.4 million energy sector jobs (compared to 0.9 million in the Reference Scenario). According to the Energy [R]evolution report, electricity costs will slightly increase in the short term (up to 2030), but the difference will be less than 0.7 cents/kWh up to 2020. In the longer term (post-2030) electricity costs decrease compared to a scenario without additional action. However, the increasing demand for fossil fuels from emerging economies, higher extraction costs and closer integration of energy markets with global financial markets have increased fossil fuel prices, as well as their volatility. The EU can make households and industries also in the short-term more resilient to fossil fuel price shocks by improving energy efficiency and increasing the share of renewable energy in the EU energy mix. A stronger ETS could be an important driver for such measures.

*b. Retiring a number of allowances in phase 3*

The European Commission has proposed to postpone the auctioning of 900 million allowances in the years 2013-2015 (“back-loading”). Before these allowances return to the market (possibly in 2019-2020) the allowances should be permanently retired, so to sustain the positive impact of backloading on the functioning of the ETS. The retirement can be carried out without infringing ownership rights of ETS participants, and without reducing the amount of free allocation. On top of retiring already back-loaded allowances, an additional number of allowances entering the market between 2016 and 2020 should be retired.

Greenpeace calls for a permanent retirement of an auctioning volume of in total 2.2 billion in between 2016 and 2020. A proposal for permanent retirement of allowances must be presented by the European Commission in 2013 at the latest.

This measure would be consistent with 30% domestic emission reductions by 2020, and would bring the EU on track towards reaching 80-95% greenhouse gas emissions by 2050 cost-effectively.

*c. Early revision of the annual reduction factor*

In the context of a post-2020 EU climate and energy initiative, the EU should increase the linear reduction factor in the ETS. Greenpeace supports a set of binding ambitious post-2020 targets for renewable energy, energy savings and greenhouse gas emission reductions. Therefore, the revision of the ETS linear reduction factor should take into account the three targets, and compensate for the surplus of allowances expected to accumulate by 2020 (due to current imbalances in the system, provided allowances are not retired, see option b.).

In the Energy [R]evolution scenario, in 2030 delivering 55% domestic energy-related CO<sub>2</sub> reductions, there are in 2030 1.2 million jobs, against 0.7 million in the Reference Scenario. Renewable energy accounts for 76% of energy jobs by 2030.

*d. Extension of the scope*

Greenpeace supports the inclusion of the aviation sector (as outlined in Directive 2008/101/EC) in the ETS, and immediate enforcement of agreed EU rules. Moreover, we support the inclusion of international maritime emissions in the ETS, due to the lack of progress in the International Maritime Organisation (IMO).

Greenpeace opposes the inclusion of road transport in ETS. Existing EU legislation already covers these sectors (passenger cars, lorries, vans) and is better equipped to provide investor certainty and optimise the co-benefits of cleaner and more efficient transport (lower fuel costs, innovation and reduced pollution).

*e. Access rules to international credits*

Greenpeace supports the revision of quality criteria, extending the existing limits that apply to credits from nuclear, land use land change and forestry (LULUCF) and large hydro schemes to other categories of projects.

For instance, the Clean Development Mechanism (CDM) allows new coal-fired power plants to earn credits for claimed improvements in power plant efficiency. However, the coal plants would also have been built in the absence of the CDM, i.e. the projects that have come forward to date are ‘non-additional’ and will therefore generate carbon credits that do not represent real emission reductions. Moreover, the coal plants conflict with the CDM’s wider sustainable development goals.

Considering the uncertain future of international offset schemes, for phase 4 of the ETS no offsets should be allowed. The EU should adopt a domestic greenhouse gas emission reduction target, including for sectors covered by the ETS.

A shift in effort from the purchase of offsets towards investments in domestic abatement options will likely have a positive employment and investment effect for the EU.

*f. Discretionary price mechanism*

Besides promoting investments in energy efficient and green technologies, the objective of the ETS must be to ensure that the EU’s greenhouse gas reduction targets are as a minimum delivered. Greenpeace therefore supports the ETS as a quantity-based mechanism, which delivers a fixed amount of greenhouse gas emission reductions. Price regulation within ETS would change this funding principle

Greenpeace also considers bilateral links between carbon markets a potential stepping stone towards a truly multilateral climate regime (provided environmental integrity is maintained, linkages are phased-in gradually, and linkages are limited in terms of quantity). Price regulation in the EU carbon market will make it difficult or impossible to link ETS with other schemes.

**Unnecessary free allocation not addressed by the consultation document**

The consultation document does not explore options to reduce unjustified free allocation to installations participating in the ETS. A higher share of auctioning could prevent installations from receiving more emission allowances than necessary, and therefore help the build-up of a large surplus in the future. The current practice of free allocation of emission allowances to ‘exposed sectors’ has led to excessive overallocation, undermining incentives to reduce energy costs and emissions in an economically efficient manner.

The list of sectors exposed to carbon leakage (eligible for free allocation) was assessed and agreed on the basis of a carbon price of around €30 per ton. It did not take into account the emission reduction programmes that countries outside Europe are putting in place.

Contrary to claims by energy intensive industry lobby groups, European industries (including steel firms and refineries) have passed on costs related to the EU's emissions trading scheme to consumers<sup>7</sup>. Moreover, energy intensive industries, and in particular cement and steel firms, have built up a major reserve of carbon emission allowances that they obtained for free. Nevertheless, a limited number of energy-intensive subsectors may be exposed to carbon leakage as a result a stronger ETS. The European Commission must therefore re-examine the carbon leakage list on the basis of fact-based independent economic assessment. The fact that many industries can still reduce energy costs (and related emissions) with a net gain must be taken into account, as well as the possibility for industries to pass on carbon costs to consumers. New carbon pricing schemes, in e.g. Australia, South-Korea, California, and in particular China, must also be taken into account in new carbon leakage assessments<sup>8</sup>.

A more targeted approach to carbon leakage to explore is the establishment of an *EU Industrial Innovation Fund*, replenished by auctioning revenues from the EU's emissions trading scheme. The fund can leverage investments in innovative clean industrial technologies. Firms which are potentially exposed to carbon leakage, but are committed to investing in clean and innovative industrial processes in the European Union would be eligible for support. Investment support from such a fund should be matched with adequate private capital and involvement of institutional investors, such as the European Investment Bank.

**For more information, please contact:**

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**Notes:**

<sup>1</sup> JRC, PBL (2012), Trends in global CO<sub>2</sub> emissions

<sup>2</sup> UNEP (2012), The Emissions Gap Report 2012

<sup>3</sup> Öko-Insitut (2012), Strengthening the EU ETS and raising climate ambition. Facts, measures and implications

<sup>4</sup> Ibid.

<sup>5</sup> Ibid.

<sup>6</sup> UNEP (2012), The Emissions Gap Report 2012

<sup>7</sup> De Bruyn S., Markowska A., De Jong F. and Bles M. (2010a). Does the energy intensive industry obtain windfall profits through the EU ETS? Publication number 10.7005.36, CE Delft, Delft

<sup>8</sup> Climate Strategies (2012) International Industrial Competitiveness, Carbon Leakage and Approaches to Carbon Pricing