Contribution to the European Commission's public consultation on options to strengthen the EU Emissions Trading System

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Introduction

Centre for Transport and Energy welcomes the opportunity to participate in a consultation on options to strengthen the EU Emissions Trading System (EU ETS) outlined in the European Commission's "Report on the state of the European carbon market in 2012".

Centre for Transport and Energy is seriously concerned about the current underperformance of the ETS, surplus of allowances and extremely low carbon price, which decreases attractiveness of green investments and in consequence puts the EU at risk of dangerous high carbon lock-in.

The European carbon market is affected by an over-supply of allowances. At the End of 2011 85% of Czech companies included in the EU ETS were over-allocated. During 2008–2011 they have surrounded a surplus of 41,2 million allowances.[1]

Centre for Transport and Energy supports European Commission's proposal for back-loading and believes that this short-term measure must be urgently followed by structural adjustments in the long-term perspective in order to:

1. Address the problem of accumulated surplus of allowances and ensure that the ETS delivers uninterrupted and meaningful carbon price signal, which provides investors with a certainty that low-carbon investments are cost-efficient in the long-term perspective.

2. Ensure that it delivers cost-efficient abatement necessary to achieve the EU's stated objective to reduce emissions by 80-95% by 2050.

Measures to be adopted according to the view of Centre for Transport and Energy

1. Retirement of a number of allowances in phase III

To address the surplus of allowances properly it is necessary to retire permanently a certain amount of allowances. While the Commission did not propose a concrete number of allowances to be removed from the market, Centre for Transport and Energy is calling for retirement of 2.2 billion allowances. Additionally to 900 million allowances, so the volume proposed by the Commission for back-loading, retirement of 1.3 billion additional credits would be needed to address the current and future expected surplus of allowances.

2. Revision of the annual linear reduction factor

[1] Sandbag, Centre for Transport and Energy (2012). Czech Fat Cats 2011. http://aa.ecn.cz/img_upload/eafd8382e68de047a49213a9ed52af69/czech-fat-cats-2011_final.pdf

Centre for Transport and Energy suggests review of the linear emission reduction factor to be accelerated to 2014. The current linear reduction factor leads to a just over 70% reduction in the ETS cap by 2050 and therefore is not consistent with the EU's agreed long term objective of 80-95% reduction by 2050. 2014 early review of the linear reduction factor would allow to limit its increase to 2.6%, assuming simultaneous cancellation of 2.2 billion allowances. In case if correction of emission reduction trajectory gets delayed beyond 2014, or if the number of retired allowances is lower than 2.2 billion, the linear reduction factor would have to be steeper than 2.6%, to compensate for a delayed action. Increase of the factor governing the ETS cap should be taken into account in preparations of post 2020 climate and energy framework to ensure that targets for emission reductions, RES energy and energy efficiency are mutually supportive.

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

Centre for Transport and Energy strongly supports an increase of the EU's 2020 climate objective to 30% domestic emission reductions. Strengthening of the EU climate ambition would result in several benefits, like increased auctioning revenues and expansion of low-carbon investments, and would put the EU on the cost-efficient emission reduction trajectory by 2050.

Latest data on the EU's emissions has shown that the EU almost already reached its 2020 climate target, nearly 10 years ahead. If EU Member States fully implement already agreed policies, it is very likely that the EU will reach 25% domestic emissions reductions by 2020.[2] EU's domestic climate target of 30% can be therefore achieved with a little additional effort.

Increase of the EU's 2020 climate objective to 30% domestic cuts by 2020 would have to be translated into additional emission reductions in both ETS and non-ETS sectors. Centre of Transport and Energy recommends achieving more ambition in the ETS through cancellation of 2.2 billion allowances and increase of the linear emissions reduction factor to 2.6% as stated above.

4. Limit access to international credits

Centre for Transport and Energy strongly supports ban on use of offset credits in the EU ETS after 2020. By 2012 international credits have become a major driver for the build-up of the current surplus accumulated on the EU carbon market. According to the European Commission offset credits are responsible for "two thirds of the EU ETS over-supply" and could represent as much as three quarters of the expected glut of credits by 2020, if no action is taken[3]. A ban on offset credits after 2020 is needed to avoid the similar problem in ETS Phase IV and to preserve the environmental integrity of post-2020 global climate agreement. Furthermore limited access to offset credits would incentivise domestic emission reduction boosting investment and employment in renewable and energy efficiency sectors.

Centre for Transport and Energy also recommends an urgent review of quality criteria of offset credits available in the EU ETS for compliance: ban on offset credits coming from coal and large hydro investment as well as credits generated by business as usual, "non–additional", projects[4] which do not deliver additional emission reductions and undermine ETS environmental integrity and increase the over-supply in an already flooded EU carbon market. At the same time the EU must ensure that decreased financial support for clean investments in developing countries, a consequence of ban of offset credits after 2020, will be properly addressed and other financing mechanisms, will be put in place to assist developing countries in low-carbon transition.

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[2] CAN Europe (2012). Closing the ambition gap. http://www.climnet.org/images/Closingtheambitiongap.jpg
[3] European Comission (2012). The state of the European carbon market in 2012. http://ec.europa.eu/clima/policies/ets/reform/docs/com_2012_652_en.pdf
[4] Projects that would be realised even in the absence of the CDM mechanism.

Conclusions

Centre for Transport and Energy supports ETS structural reform that would not only address the surplus of allowances accumulated on the market but also correct the current emission reduction trajectory implied for the ETS sectors, to ensure that they deliver cost-effective abatement to reach EUs' stated 2050 climate objective.

Centre for Transport and Energy also supports a robust post-2020 climate framework, including GHG emission reduction target, target for renewable energy and energy savings target.

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