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## Recommendations on the ETS review

In general, Grian supports and upholds the recommendations made in the joint NGO position, as submitted by CAN-Europe, Friends of the Earth Europe, Greenpeace and WWF.

In particular, we support the principles that:

### General principles guiding the ETS:

- **Maximising the environmental and economic effectiveness** of the EU ETS;
- A **carbon price signal** resulting from short and long term cap setting;
- a **simple and harmonised allocation method** capable of generating a clear carbon price signal;
- Thorough and transparent **harmonisation in the design and implementation** of rules for allocation, auctioning, verification and compliance ;
- **Consistency** with the EU's leading role in international Climate Change negotiations and the historical responsibility for industrial countries to take the lead in reducing greenhouse gas emissions.

Grian's principal recommendations are that:

- An **ex ante Community-wide overall cap should be set** for a third phase of the ETS for the post-2012 period, **consistent with the EU target for 2020 of a reduction in EU emissions of at least -30% below 1990 levels;**
- **The Community-wide overall cap** should then be **devolved downwards to Member States** on the basis of common but differentiated responsibilities and respective capabilities (i.e. not assembled as an *ex post* aggregate of rather *ad hoc* individual national allocation plans);
- **Full auctioning of allowances** will create a clear price signal and is the most harmonised and transparent way to distribute allowances.;

- **Community-wide auctioning** furthers the ambition for harmonisation and offers less possibilities for gaming;
- A stringent **quantitative and qualitative limit on the use of CDM/JI** credits in the EU ETS is needed.
- **Expansion of the scope of the ETS** into other sectors and/or activities should only be considered as a means of enhancing the overall environmental effectiveness and integrity of the scheme and must therefore be considered very carefully and considerately. Particularly, in the case of **road transport**, Grian believes that the current direction and thinking behind its potential inclusion is misplaced and misguided. In the case of **aviation**, the need to include it in the ETS is urgent, but precise accounting methodologies and stringent compliance measures need to be formulated and applied well before inclusion can be contemplated.
- For the same reason, expansion of the ETS to include **LULUCF** (or links to it) is inadvisable at the moment, pending far more research, methodological development and institutional capacity-building;

Our specific comments and recommendations on the issues scoped by the Commission in the order requested are as follows:

## **(1) The scope of the Directive.**

**1.1 Scale of combustion installations:** Further development of clear and specific harmonised rules for determination of qualifying installations should be progressed and made operational for the next phase of the ETS.

We doubt there is an economic or administrative case for raising the current threshold, or de-qualifying small installations currently covered. If anything, consideration should be given to lowering it

Additionally, **mobile plant should be included**, with clear rules for bundling.

**1.2 Other gases:** We support (subject to the early and effective development of appropriate methodologies and inventories) the inclusion of:

- **N<sub>2</sub>O from the production of nitric acid;**
- **CO<sub>2</sub> from the production of petrochemicals** (other than to the extent CO<sub>2</sub> emissions from combustion installations are already covered);
- **CO<sub>2</sub> and N<sub>2</sub>O from the production of ammonia, other fertilisers than nitric acid and adipic acid** (other than to the extent CO<sub>2</sub> emissions from combustion installations are already covered);
- **CO<sub>2</sub> and PFCs from the production of aluminium** (other than to the extent CO<sub>2</sub> emissions from combustion installations are already covered)

- CH<sub>4</sub> from coal mines.
- CH<sub>4</sub> from pipelines.

### 1.3 Other sectors and activities

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#### 1.3.1 Aviation:

Given both the current and projected growth of the sector and its obvious and well-known multigas contribution to overall greenhouse gas forcing, there is an urgent need to limit its emissions and therefore also to potentially include aviation in the ETS. Grian therefore welcomes the Commission's Communication to this effect.

However, absent coherent, leak-proof rules and methodologies capable of accounting for the full forcing effect of the sector, we consider it premature to include the aviation sector in the next period of the ETS unless it can be conclusively proved that:

- a) forcing due to contrails, cirrus, N<sub>2</sub>O, indirect effects on CH<sub>4</sub>, O<sub>3</sub>, and all other radiatively active factors and agents are fully included,
- b) a cap consistent with the Community's target for 2020 of a reduction in EU emissions of at least -30% below 1990 levels is imposed on the sector, and
- c) stringent complementarity provisions are attached to use by the sector of flexible mechanisms.

#### 1.3.2 Road Transport:

Given both the size of the sector and its current and projected growth, there is, if anything, an even stronger case for the inclusion of road transport in the ETS. However, Grian believes that the current direction and thinking behind the potential inclusion of road transport in the ETS is misplaced, misguided and misdirected.

Attempts to decarbonise the motor fleet through rather minimal application of CO<sub>2</sub> standards does not currently address the emission problem at source either in terms of volume (with demand increasing) or in terms of combustion (no real fuel switching to e.g. electricity or hydrogen). Furthermore, under current policy, it is hard to see how this situation will change emission trends in real terms in anything like a foreseeable future.

Similarly, layering current biofuel policy onto the engine standards policy is fraught with danger, both in terms of cutting off real opportunities for the stimulation of genuine and effective technological change, and in terms of possibly not mitigating net emissions at all, once LULUCF from biofuels is included.

Grian believes an effective and deliverable option exists for tackling emissions from road transport, and, furthermore, that emissions trading should form a fundamental element of the mechanism. Such a scheme would involve the installation of a combustion-monitoring chip in the electronic control system of every vehicle made available for sale or lease within the Community. The chip should automatically log onto to a GPS-

controlled system <sup>1</sup> every time ignition occurs, and then remain online until such time as the engine is turned off again.

Using such a system, precise, geo-located emission factors can be monitored in real time for every vehicle in the Community with very little administrative burden, other than costs involved in development and establishment. Using this methodology, road transport could be easily integrated into a future period of the ETS on either a per-vehicle basis, per-person basis, or per-road basis. The difference between the approaches is fundamental and will require thorough examination and opportunity-costing for the purposes of determining the relative efficiencies and deliverabilities of each option. Grian will develop a scoping paper outlining the various options and possibilities if requested.

Under current EU transport and research policy, however, it is hard for us to see how such an approach can be developed and delivered before 2013

Absent this, and considering both the size of the sector and the strong possibilities for leakage under current policy, we cannot therefore currently recommend the inclusion of road transport in the next round of the ETS.

### **1.3.3 CCS:**

While, from a global perspective it is almost imperative that rules and accounting for CCS be developed as soon as possible, Grian does not believe that, under current policy and momentum such a framework can possibly be developed before the commencement of the next phase of the ETS, not least because even the earliest pilot plants are not due online before 2015.

However, in terms of wishing to lend support to the development of such rules in the future we would recommend:

- 1) That plant be liable for (and obliged, in the first instance to maintain) sufficient permits to cover gross emissions, i.e. including extra emissions caused by capture technologies and storage technologies, including transport to storage.
- 2) That standards and certificates for permanence of storage be developed at an early stage before any permits for combustion be made available
- 3) That certificates of guaranteed, permanent and safe storage (i.e. reduction credits) only be available for issue following allowance for sufficient time for thorough verification of environmental integrity, and that the operator carry full liability for all upstream emissions incurred until such time. (For example, storage credits would only be made available in the commitment period following that in which the storage first occurred, i.e. 5 years from initial storage at the earliest).

Furthermore, any such reduction credits should be appropriately discounted over time in order to adequately reflect the risk of lack of permanency on a precautionary basis.

Grian believes that the most effective environmental benefit to be gained by use of CCS is if and when it is ultimately applied to biofuel combustion, due to the extra mitigation

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<sup>1</sup> Preferably Gallileo, which would thereby enhance its chances of finding an identifiably useful role for its development and roll-out by providing such a service.

potential resulting from sequestration occurring during the growth phase and its subsequent recovery and storage. In our view, too little research and political effort is being aligned with this option. Given this situation, it is therefore no more possible to recommend its inclusion in the next round of the ETS than it is for the case of CCS applied to fossil fuels.

Furthermore, in the case of CCS applied to biofuels, there is also the additional problem of the requirement for leakproof rules for accounting, baselines, monitoring and verification of emissions caused during the growing cycle. Our lack of confidence in the stringency of current arrangements for monitoring these therefore also applies to our recommendation under the next heading.

#### 1.3.4 LULUCF:

For reasons of lack of certainty on the inventory side mentioned above (under CCS), we can therefore, and similarly, also not currently recommend the inclusion of sinks in the next round of the ETS, either as domestic projects or for off shore projects sourced through JI or the CDM.

In common with other NGO colleagues we share the following concerns about the use of credits (CERs/ERUs) from LULUCF projects to the EU ETS:

- **Non-permanence** - Fires, pest attacks, increasing weather extremes and increase in the need for agricultural land are likely to turn today's sinks into future sources
- **Additionality** – establishing additionality requires the establishment of a reliable baseline, which must represent what would have happened without the project
- **Leakage** – the implementation of a sinks project will influence emissions outside the project boundary to a much larger degree than non-sinks projects.
- **Uncertainties** – associated with the measurement of changes in carbon stocks and emissions of other greenhouse gases within the project area as well as uncertainties with calculation of the carbon offset itself.
- **Socio-economic and environmental impacts** – negative impacts need to be minimised and biodiversity benefits should be maximised, and there is no assurance that sinks projects are consistent with goals and objectives of the CBD or the CCD<sup>2</sup>. In fact, many sinks projects, including those that entered the CDM approval process, have already sparked controversies on the basis of their negative social or environmental impacts<sup>3</sup>.

#### 1.3.5 Domestic offsets:

While Grian strongly supports the potential of properly-organised domestic offsets to mitigate Community emissions, again (and most regrettably) it is hard for us to see how, under current policy and frameworks at least, we can possibly recommend their inclusion in the next period of the ETS, unless strong rules and accounting frameworks can be

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<sup>2</sup> Convention on Biological Diversity and Convention to Combat Desertification.

<sup>3</sup> For more information see: <http://www.wrm.org.uy/bulletin/76/dumps.html>

produced in the very near future. We are not currently aware of any momentum towards this end.

The most frequently-suggested proposals appear to be primarily oriented towards sinks. In this case, our foregoing reservations about rules obviously still apply, and we cannot therefore currently recommend domestic sink-based offsets for inclusion.

We feel, however that there are many other much more certain, achievable, and effective domestic offset projects which could be suitable for inclusion if appropriate rules and frameworks were to be developed. Examples are:

- Small-scale consumer co-ops investing in e.g. building insulation, small-scale renewables, CHP or community ESCO's;
- District, local, regional or even cross-border partnerships operating the same, or similar, options to the above;
- Transport co-ops;
- Energy management and decarbonisation consultancies delivering verifiable mitigation.

Evidently, what is urgently required in support of such options are harmonised rules, standards, monitoring, and compliance methodologies capable of delivering verifiable emissions reductions using such schemes. This is therefore also a recommendation to be re-iterated in the next section.

## **(2) Further harmonisation and increased predictability.**

Grian supports the widely-held view that experience gained in the ETS so far tends to strongly re-inforce the case for increased Community-wide harmonisation of rules in order to increase predictability and confidence in the next period. In particular we make the following recommendations:

### **2.1 Community-wide cap:**

- An ***ex ante* Community-wide overall cap should be set** for a third phase of the ETS for the post-2012 period, consistent with the EU target for 2020 of a **reduction in EU emissions of at least -30% below 1990 levels;**
- The Community-wide overall cap should then be **devolved downwards to Member States** on the basis of common but differentiated responsibilities and respective capabilities (i.e. not assembled as an *ex post* aggregate of rather *ad hoc* individual national allocation plans);

## **2.2. Auctioning:**

Grian concurs with the recommendations of the Ecofys report that conversion of the ETS to full auctioning poses its own difficulties in terms of deciding the relevant benefits and difficulties of different methodologies (e.g. Community-wide vs Member State auctions) as well as the finding that partial auctioning is likely to be inefficient in terms of allocation.

In general, we have a preference for **Community-wide auctioning** given that it furthers the ambition for harmonisation and offers less possibilities for gaming than e.g. a situation involving sequential auctions carried out by member States. (We assume that internal market rules, prevent the exclusion from national auctions of participants from other Member States).

- **Full Community-wide auctioning of allowances** will create a clear price signal and is the most harmonised and transparent way to distribute allowances,

## **2.3 Recycling auction revenues:**

### **2.3.1 Recycling auction revenues to operators**

Under full Community-wide auctioning, there is no need to recycle revenues to incumbent operators---they already have the full asset value of their previous allocation on their books and can therefore already afford a large part of the auction cost of any allowances they will be seeking in the next phase of the scheme.

Any additional cost operators face as a result of either (under our recommendations) the absolutely certain tighter cap they face, or any current (or proposed future) expansion of their activity merely reflects the required and expected mitigation effort they must expend.

A tight cap, a short market and a high price all act together to merely re-inforce and accomplish the most basic aim for which the ETS was established in the first place.

### **2.3.2 Recycling auction revenues to Member States:**

With full Community-wide auctioning, a top-down Community-wide cap is an absolute necessity, otherwise Member States will have even more motivation than is already the case to engage in gaming on their share of the cap, as they go in search of increased shares of revenue from auction recycling.

Similarly, the case for full Community auctioning enhances the argument for a top-down Community cap.

Further arguments for a Community cap and full Community auctioning occurring together are:

- Efficiency---sunk costs involved in establishing the mechanism can be recovered from auction revenues before recycling to Member States;

Similarly, fences can be created around new, centralised Community funds for:

- Funding for adaptation in developing countries
- Funding for technology transfer to developing countries;
- Green funds for Community investment in renewable energy, energy efficiency and low-carbon energy infrastructure;
- Environmental tax reform;

Remaining revenue from auctioning may then be recycled to Member States in strict proportionality to their share of the Community cap, subject to it being used by them purely for the creation of parallel and matching green funding at national level.

#### **2.4 New entrant reserve:**

Under this framework, there is therefore a strong case for a centralised and harmonised new entrant reserve (NER).

Sufficient reserve should be created *ex ante* for known planned developments (KPD's) with appropriate methodologies to confirm that KPD's have as a minimum the necessary preliminary planning and licensing consents.

Permits from the NER should then be made available at auction to new entrants on an annual basis as and when installations are expected to commence operation.

#### **2.5 Closures:**

Similarly, using this framework, there is therefore also a strong case for harmonised rules on closures.

Installations closing should be required to surrender permits at least equivalent to their current liability at time of closure, and such permits should thereby be retired from the ETS.

The centralised nature of this operation thereby also provides a fence (in extreme circumstances) against any potential unforeseen shortage in the NER.

Permits retired from closures are at least then available *in extremis* to top up the NER should this prove suddenly short at a time when security-of-supply considerations absolutely require new capacity..

#### **2.6 CHP:**

There is already a strong case for clear, harmonised Community rules for the treatment of CHP.



## **2.7 Supplimentarity:**

Stringent and harmonised limits on the use of CDM/JI credits in the EU ETS are urgently needed, both in terms of quantity and in terms of quality.

### **2.7.1 Quantitative limit on external credits:**

On the quantitative side, there is an urgent need for the speedy creation of harmonised Community rules on supplimentarity in the third (and subsequent) phase(s) of the ETS.

It is relatively easy to construct formulas that reflect the UN principle that access to, and use of, the Kyoto flexible mechanisms should be unequivocally supplemental to domestic action.

Rules can then be easily and automatically created and applied at the registry level to ensure such rules are not breached at the installation level.

Harmonised rules for supplimentarity in the third phase of the ETS should be created at an early stage to ensure that future domestic action is **assessed against historic baselines and the -30% Community target for 2020** (i.e. not against BAU, as at present).

### **2.7.2 Qualitative limit on external credits:**

Currently, only CDM projects accredited under the 'CDM GoldStandard'<sup>4</sup> can be positively guaranteed as both truly additional to BAU, while also supporting the overall UNFCCC objective to promote and assist the achievement of sustainable development in host countries

GoldStandard is the only fool-proof guarantee that emission reductions not taking place domestically are compensated by real and verifiable reductions taking place elsewhere in the world.

**Along with other NGO colleagues, Grian recommends that only CDM credits from 'CDM Gold Standard' accredited projects should be allowed to enter the EU ETS.**

## **(3) Robust compliance and enforcement.**

Grian strongly supports the case for Community-wide, harmonised rules in the third phase of the ETS for monitoring, reporting, verification and compliance. However, development of any such harmonised rules must obvious be oriented at achieving the maximal amount of environmental effect, while also enhancing economic efficiency.

We feel there is a strong case for a Community-wide Inspectorate.

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<sup>4</sup> [www.cdmgoldstandard.org](http://www.cdmgoldstandard.org)

**(4) Linking with emissions trading schemes in third countries, and appropriate means to involve developing countries and countries in economic transition.**

Linking the ETS with schemes proposed in other regions and/or territories can potentially improve the environmental and economic effectiveness of the scheme, subject, obviously, to guaranteed confidence that harmonised rules of appropriate stringency will apply to both the creation and subsequent fungibility of credits and/or reduction units.

Similarly, at the institutional and macro-scale, arrangements for monitoring, verification and compliance procedures must contain clear and harmonised rules that are properly configured, properly operated and properly respected.

Each possible external link with the EU ETS has to be considered carefully.

The following basic design elements in any other schemes to which it is proposed to link the ETS are therefore basic and essential:

- Cap and trade systems only. (i.e. no linking with baseline and credit systems or schemes with relative caps);
- Schemes must have at least similarly ambitious caps to the ETS (relative to 1990);
- No linking to schemes using "backstops" to create a price cap;
- Schemes must have a similar scope and reach as the ETS in terms of sectors and sources (i.e.CO<sub>2</sub> emissions from all large industrial point sources as a minimum);
- Schemes must have both quantitative and qualitative restrictions on use of project credits with stringent complementarity conditions applying, particularly to schemes in developed countries

----- ENDS -----

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