Green Budget Europe (www.green-budget.eu) welcomes the plans of the European Commission to back-load a certain number of EU-ETS auction volume in the third phase of the EU-ETS as a first step. This ambitious tool which was meant to be the most effective and powerful instrument to pave the way for the green economy in European industry will stay a bureaucratic and toothless tiger if there is no long-term policy with clear signals to incentivize investments into a competitive low-carbon European industry.

At stage, the EU-ETS fails in GBE's point of view in three respects:

- Due to the ongoing market distortion (over-allocation of allowances) and because of the low price for the emission trading rights, the EU-ETS is not taken into account by the industry when deciding upon long-term investment. This is a competitive disadvantage. The earlier industry incorporates the real prices of emissions, the earlier carbon marketing will become cost-efficient, and the earlier green economy will be reached.
- National governments lose important revenues as the price of CO_2 emission rights shrinks constantly.
- The number of allowances issued is reduced by 1,74% each year, which guarantees a fixed CO_2 decrease of 21% within the EU-ETS sector until 2020, compared with 2005. However, the EU-ETS will fail to send a clear carbon price signal in order to ensure additional emission reductions and to contribute substantially to the 2020 target.

One of our major arguments in favour of a more tightened EU-ETS policy is the urgent need of governments to *consolidate their national budgets in a cost-efficient way* and to *enhance the competitiveness* of the industry.

Green Budget Europe strongly recommends *back-loading 1.4 billion* allowances as proposed by the European Parliament to address the shortfalls of the current EU-ETS.

However, these short-term plans should be complemented by solid policies later this year. We urge the European Commission to *permanently pull theses allowances from the market*.

Our recommendations

Even though the EU-ETS allows Europe to reduce its greenhouse gas emissions by a predetermined volume, the system in its current design is not able to offer economic incentives to invest in further climate protection. Due to the low price of allowances, it does not either internalise social costs of CO_2 emissions which results in strong market distortion. A reform is needed urgently in order to have positive influence on consolidating both national and climate budgets.

Therefore, Green Budget Europe strongly recommends

- **In the short term to back-load 1.4 billion allowances** as proposed by the European Parliament to address the shortfalls of the current EU-ETS;
- **In the medium term to make use of several reform options within the EU-ETS** to sustain the price and accelerate the pace of measures, e.g.
  - Removal of existing exemptions and thereby broadening the scope of the EU-ETS
  - An increased share of auctioned allowances instead of allocation by grandfathering
  - A fixed floor price for CO_2 emission rights
- In order to **fundamentally strengthen the functioning of the EU-ETS**, the back-loaded allowances need to be **permanently pulled from the market.** This means that the inherent emission reduction targets of the EU-ETS need to be tightened in order to contribute sufficiently to the 2020 target.

  Back-loading some auction volume from 2013-2015 towards the end of phase 3 (2020) should level-off the supply and demand of allowances by reducing the surplus. However, as the allowances that had been set aside would have to re-enter the market later on during the 3rd stage, the benefit would only be felt until 2015, when the surplus would start emerging again. The higher the set-aside, the greater the downward pressure on prices in the second half of the 3rd phase.

- **Until the EU-ETS is able to deliver the right market signals**, there are effective options to internalise social costs of CO_2 emissions:

  An obligatory CO_2-tax on coal for electricity generation could internalise external costs and thus rebalance the competition with renewable energy sources. Considering the long-term perspective of investment cycles, it is essential to focus on the economic framework conditions today in order to reduce emissions tomorrow. Beyond, this model can be extended to a general CO_2-taxation complementing the EU-ETS.

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