

Dear Sir/Madame

please find below comments to the document: „Report from the Commission to the Council and the European Parliament – The state of the European carbon market in 2012”.

The main cause of oversupply of allowances on the European market can be traced back to the lack of a mechanism enabling the market to adapt to changes in supply and demand for allowances. Even if the Commission will temporarily reduce or eliminate the surplus, the absence of this mechanism may in the future lead to further cases of "imbalance". This situation results in a decline in the predictability and credibility of the EU ETS in the eyes of business community, with a negative impact on investment decisions, which is why the structural reform is urgently needed.

**EC proposals, however, do not address structural shortcomings of the EU ETS, since they do not eliminate the reasons behind the current situation and would not prevent possible future imbalances.** The structural reform should:

- be permanent and not a one-off action, should in fact prevent the recurrence of imbalance problems by removing their causes,
- ensure the achievement of reduction targets in a cost-effective manner and maintain the competitiveness of the EU companies,
- provide predictability and reliability of the system in the long term, in which companies are able to implement investment plans.

**None of the six EC proposals ensures that the above mentioned conditions are met.**

Moreover, the report of the Commission testifies to some misunderstanding of the underlying concepts. In the assumptions, the EU ETS is supposed to be one of the tools enabling further increase of the reduction targets. In the current EC document, the **Commission reversed the situation by proposing to increase the reduction targets as a way of "saving the EU ETS".**

The solutions proposed by the Commission can hardly be regarded as measures to improve the functioning of the carbon market, and above all the EU ETS, in a systemic and sustainable way. The concept of structural reform should be understood more broadly, as a solution changing the EU ETS and the management of the system in such a way that the fundamentals of a market remain stable. In this context, the proposed solution should take into account a number of other factors and conditions within the broader context of the climate policy.

At present, the Commission's proposals focus on solutions aiming at reinforcing the role of the EU ETS as the principal mechanism of transition to a low carbon economy. By forcing the investment in new technologies through price mechanism, the proposals undermine the original reasons for implementing the system, which was supposed to be a cost-effective mechanism for achieving reduction targets at international level. The **EU ETS was designed as a market mechanism, therefore interference in the market without a change to a long-term policy and structural reforms will lead to a stronger dependence of the system on administrative and political factors, as already the predictability of the market does not exist.**

The proposed mechanisms, especially a permanent reduction of the number of allowances to be auctioned, will certainly affect companies participating in the EU ETS. But this can be inconsistent with the objectives of the Directive, i.e. the reduction of emissions in a cost-effective and economically efficient manner. This will also have an impact on the increase in carbon leakage, and thus it will not contribute to a reduction of greenhouse gas emissions on a global level.

**Another issue is the legality of introducing structural change.** Adoption of the EC's proposal will lead to an increase in the reduction target, while the provisions of the preamble to the EU ETS Directive say that the increase of the target is conditional on the achievement of a global climate agreement. The process of approval of the Commission proposals will be time-consuming as such. The Commission will have to prepare an impact assessment, and to carry out a public consultation. Then the selected proposal must be accepted by the Member States, the Climate Change Committee, the Council and the European Parliament.

**Structural solutions should be considered in the long term.** They should not only respond to the current oversupply of allowances, and thus lower prices, but should lead to the achievement of the climate policy objectives in a cost-effective manner. They must also provide a predictability for investment. This cannot be achieved without a clear message in support of long-term goals, because 2020 is only a step on the road to long-term objectives for 2050. Solutions proposed by the European Commission are generally short-term interventions in the market as such, because they would not solve the problems underlying the reasons for the occurrence of surplus or shortfall in allowances in the EU ETS.

At the moment it is not clear how the 2050 EU's targets will be achieved, and thus how the mechanism contributing to the reduction of emissions, which is the EU ETS, should function. It is important to ensure that the EU ETS alone will fulfill its purpose regardless of **external factors**, such as economic crises or commodity prices. It is also necessary to **integrate** into delivery of the EU climate policy **other mechanisms** to reduce emissions, such as **energy efficiency and renewable energy**, in order to reach a clear market information about the actual price of the emission and to enable the the **optimal reduction path**. The emphasis on **innovation** cannot be forgotten, but with maintaining **cost-effectiveness**, which must be balanced with the need to preserve the **competitiveness of the European enterprises**. While retaining all the above-mentioned assumptions the **simplicity of the system** should be preserved, so that each of its participants is able to understand basic principles guiding him.

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