Interest representative
No. 0014082722-83
EUROCHAMBRES aisbl
Avenue des Arts 19 A/D
B-1000 Brussels

Position Paper

28 February 2013

EUROCHAMBRES response to the public consultation on structural options to strengthen the EU ETS

1. General Assessment

EUROCHAMBRES recognises the important role that the EU plays as a pacemaker in global climate and energy policy and supports the **20% reduction target** of greenhouse gas emissions set out in the Climate and Energy Package. As a key tool, the EU Emission Trading System (ETS) contributes significantly to the achievement of this target and ensures that cuts can be achieved at least costs (Article 1 of the EU ETS Directive 2003/87/EC). The ETS' "cap and trade" principle guarantees that, independent of the price level, this goal will be reached.

In accordance with Articles 10(5) and 29 of the EU Emissions Trading System Directive 2003/87/EC, the European Commission presented a **'report on the state of the European carbon market in 2012'** which addresses the current state and functioning of the ETS.

From the perspective of EUROCHAMBRES, the report of the Commission confirms the wide-spread view of the ETS as "a liquid market with a functioning infrastructure". The major objective of the ETS-Directive, namely reducing greenhouse gas emissions in a cost-effective and economically efficient way, has been achieved. **Against this background, it can be clearly stated that the EU ETS works**.

However, it is to be criticised that the report fails to recognize that the EU ETS is significantly influenced by interference arising from other mandatory EU policies and targets such as support given to renewable energy sources through subsidy schemes. Analyses of this influence from competing measures are missing completely.

The report correctly presents the fundamental changes of the last revision of the ETS directive within the framework of the climate and energy package. However, it does not consider that the options now being proposed require new interventions in the EU ETS, even before the rules of the last revision will be fully implemented. EUROCHAMBRES underlines that every suggested measure implies an **opening up of the climate and energy package** which covers the period up to 2020. At the same time, it must be kept in mind that – as agreed during the tough negotiations on the package – raising the CO_2 emission target before 2020 requires a prior global agreement that is currently far from being reached.

Apart from the environmental and political aim to reduce CO_2 emissions, the ETS should provide incentives for future investments. In this regard, the predictability of political actions is critical to building confidence among investors and entrepreneurs. For ensuring **planning certainty**, it is important that long-term rules are respected and remain unchanged. However, due to the recurring discussions about the carbon price and the emission reduction target for 2020, this principle has repeatedly been violated which considerably increased the general uncertainty among businesses. **Restructuring the Emissions Trading System can therefore only be discussed with a view to fourth trading period (after 2020).**

An artificially high CO_2-price and the lack of predictability significantly harm the **competitiveness of EU businesses** on the global level. Therefore, Chambers regard the proposed options as the **wrong measures at the wrong time**. At a date, when the economic situation is fragile and the sovereign debt crisis weighs heavily, businesses should not be subject to new burdens. Growth and employment would be jeopardized at a time when Europe needs an economic upturn more than ever before.

Therefore, EUROCHAMBRES strictly opposes any changes of the legal framework of the ETS before the end of the third trading period. Instead, a potential review of the ETS Directive should thoroughly be discussed with a view to the period after 2020. From our point of view, climate, energy and industrial policies in the European Union are not always sufficiently coordinated - sometimes they can even be contradictory. Given the current economic outlook, Europe should ensure its competitiveness as a production location. Therefore, competitiveness must be a cornerstone of any upcoming discussions on climate policy towards 2030. In order to facilitate the long-term planning process for businesses, Chambers welcome an early discussion on this issue, accompanied by stakeholder consultations, in-depth economic analyses and impact assessments both for EU and individual Member States on all options tabled.

2. The Emissions Trading System – A system for cost-effective reduction of GHG emissions

Against the background of potential interventions in the EU-ETS during the third trading period, EUROCHAMBRES calls on the Commission to take the following considerations into account:

- The Emissions Trading System was established with the aim of cost-effectively reducing GHG emissions in Europe. The environmental effect of an absolute cap on CO_2 emissions in the affected sectors will be achieved under the current system. By 2020, the ETS sector must reduce its emissions by 21% compared to 2005. It is widely expected that this target will be reached, or even exceeded[1].

- A functioning market should not lose its main characteristics through ad hoc interventions and regulation measures. It has to be ensured that the ETS remains a market-based instrument. Using the carbon market only as a complex CO_2-tax with a politically managed price mechanism would run counter to the basic idea of the ETS.

- Fluctuations in certificate prices are a natural process in a market based system. Under no circumstances can the success of the ETS be associated with the level of CO_2 prices. This criterion arises neither from the ETS Directive, nor from the political mandate of reducing emissions in a cost-effective way. Using the criterion of CO_2 price for assessing the ETS would be a fundamental shift away from the current system.

- The ETS should not be regarded as a fiscal instrument in order to maximize budget revenues. Governments and EU institutions must resist the temptation to use the ETS as a mean to increase revenue for public budgets.

- Besides the ETS, a variety of other EU policy measures (e.g. support for renewable energy sources and energy efficiency requirements) contributes to a decrease of CO_2 emissions in the ETS sector and

[1] As stated in several EU Commission documents (e.g. COM(2011) 112: “A Roadmap for moving to a competitive low carbon economy in 2050.”)

thus interferes with the Emissions Trading System and its objectives. The costs of these measures, even though they arise from outside of the ETS, weigh already heavily on businesses and households.

- In case of any political intervention, the confidence in the integrity of emissions trading would be seriously undermined.

3. Protecting the industrial site of Europe vs. unilateral efforts in climate change policy

On a global level, the gap between the EU and growth front runner countries is widening. Against the background of an increasingly tense international business environment, differing degrees of climate protection efforts will result in **competitive disadvantages** for EU businesses. An artificially increased CO_2 price and the lack of predictability of the ETS make it even more difficult for businesses to produce cost-effectively inside the EU. Thus, too ambitious actions by the Commission raise the risk of inducing a shift of carbon emissions from the EU to third countries (carbon leakage). Apart from the negative impact this would have on the EU's economy, it would also gravely undermine the international climate change response. It is imperative for the EU to prevent losing more and more energy-intensive industries, which are also an important supplier of components and base material for sustainable energy technologies.

In particular, the proposed actions would put EU-based industries at a further disadvantage in relation to its US-American competitors. Due to low energy prices, the industrial sector of the United States currently experiences a significant recovery. Therefore, any additional energy costs would considerably harm Europe's economic growth.

From today's perspective all of the options suggested by the "carbon market report" would lead to an increased price of non-CO_2 neutral energy sources. The report, however, neglects a comparison of energy price trends with other economic areas in the world.

4. Coordinated discussions with affected sectors necessary

In order to support the transition to a low-carbon economy and society, an extensive and integrated discussion about the EU's climate and energy policy, with a view to the period after 2020, will become necessary. At the same time the competitiveness of the European industry has to be strengthened. This discussion will become inevitable since Europe's current climate policy on the one hand and the industrial policy on the other, are largely incoherent.

For a successful climate and industrial policy resulting in sustainable growth, it requires mutual consideration on both sides. This is the only way how climate and energy policy can enable investment and technology development without harming the European industrial location.

5. Remarks on the suggested options for structural measures

General remarks

- All suggested options undo the EU climate and energy package and with that the defined targets until 2020. Against this background, **EUROCHAMBRES strictly opposes any change of the legal framework before the expiry of the third trading period.**

- The latest revision of the ETS Directive was integrated in the framework of the climate and energy package and was subject to various stakeholder consultations, an in-depth economic analysis and the result of political decision making at the highest level. Any other revisions and the discussion on various options for an alignment of the ETS until 2030 should follow this example.

- The arbitrary actions in the context of the European climate policy - especially in connection with the current discussion about the so called “backloading” - decreases and undermines the trust of affected firms in the European climate policy.

Option a: Increasing the EU reduction target to 30%

The EU should refrain from stand-alone actions, creating obstacles to growth and adversely affecting the competitiveness of the European industry. As stated in Article 1 of the ETS Directive, only if a global agreement on climate change is approved, the 20% CO_2 reduction target can be raised, however - as we all realize - none of the key international players have yet been sufficiently impressed by the European commitments to follow suit, nor seem likely to do so in the near future. Therefore, any unilateral increase of the GHG reduction target to 30 % would overstrain businesses covered by the ETS. For this reason, increasing the EU reduction target until 2020 depends on certain conditions (determined by the European Council), which are not fulfilled at the moment. From our point of view there is no reason to follow up this option under the current conditions. With a view to 2030, new targets must be subject to comprehensive feasibility studies and have to consider the global competitiveness aspects.

Option b: Retiring a number of allowances in phase 3 and Option c: Early revision of the annual linear reduction factor

Options b and c cause, just as the above mentioned option a, a unilateral increase in the EU reduction target until 2020 and therefore have to be rejected, under the current conditions.

Continuous modifications of the basic conditions regarding the emissions trading (retiring a number of allowances, early revision of the linear reduction factor) destroy sound planning procedures and endanger long-term investments. GHG reduction measures do not only have to be economically appropriate for businesses, but they also require forward planning (plant engineering companies cannot reconstruct all plants at the same time; financing has to be secured) where additional certificate purchases are necessary. Arbitrary changes of the regulatory framework causing the allowances to become more expensive or run short, would undo capital budgeting and consequently endanger investments. Projects under construction may have to be restarted or even cancelled.

Option d: Extension of the scope of the EU ETS to other sectors

Without any detailed information, the extension of the scope of the ETS to other sectors can only vaguely be assessed. An extension to international shipping would presumably cause similar resistance of third countries as currently observed in the aviation industry. The idea of including the air traffic is just to be suspended. It is important to gain third countries outside the EU-ETS as partners for emissions trading. However, it is also crucial to take into account the obstacles that go along with a potential extension.

The report lacks information on the relationship between the mandatory reporting on transactions costs of the ETS and the respective regulated emission level of new emissions trading sectors. Moreover, it does not deal with potential indirect effects on ETS businesses, caused by the integration of further sectors

The mentioned consequences of the economic crisis on the ETS and non-ETS sectors demonstrate the severe impact of global competitive pressure. Artificially increased CO_2-prices would weaken the energy- and emissions-intensive industry (which currently equates to the ETS-sector) on the one hand and the global competitiveness on the other.

Option e: Limit access to international credits

This option is considered critically since international credits form a component of the climate and energy package and therefore represent a calculable volume of the ETS. Up to this point international credits have been a cornerstone of the European strategy to “globalize” the idea of emissions trading. Further restrictions might therefore weaken EU positioning in international climate negotiations and definitely hamper the prospect of international emissions trading.

Option f: Discretionary price management mechanisms

Discretionary price management mechanisms can be interpreted as taxes and would undermine the characteristic of the ETS as a market-based instrument. The ongoing discussion concerning the “backloading” already offers a foretaste of what is considered as a discretionary price management mechanism and has to be viewed with great scepticism. On demand-interventions would render planning procedures completely impossible.

6. Way forward

For the above-mentioned reasons **EUROCHAMBRES opposes any intervention in the EU-ETS legal framework before 2020.** In conclusion, it must be stated that an implementation of one of the proposed options would create obstacles to growth and therefore adversely affect the competitiveness of the European industry. By moving towards unilateralism (e.g. by stepping up the emission reduction target), the EU is also further hampering its negotiation position in the international climate discourse. EUROCHAMBRES is convinced that unilateral actions will hinder growth and thus devalue Europe as a business location.

Notwithstanding, **Chambers urge the Commission to turn its attention beyond 2020** and basically welcome an early and broad discussion on the EUs future climate energy and industrial policy framework. However, we believe that this process must not only include the views and expectations of all stakeholders, but necessarily also a debate on the lessons to be learnt from the 20-20-20 targets. In particular, it has to be ensured that other policy measures are complementary to the ETS, rather than interfering. Before taking decisions on structural measures, the Commission has to provide in-depth impact assessments and comprehensive economic analyses both from EU and the individual MS perspective of all feasible and appropriate options. In this context, particular attention has to be paid to competitiveness aspects, long-term predictability of price developments and the cost-effectiveness of the future ETS.

Future role of ETS among other environmental and energy policies and measures including mutual interactions should be further analyzed and clarified. Other measures should be complementary to rather than competing with ETS. Future of ETS should thus be assessed in the context of the whole policy framework so that full alignment of objectives among different initiatives is ensured and possible overlaps are taken into account and eliminated as much as possible.

EUROCHAMBRES – The Association of European Chambers of Commerce and Industry represents over 20 million enterprises in Europe – 93% of which are SMEs – through members in 44 countries and a European network of 2000 regional and local Chambers.

Further information: Mr. Michael Steurer, Tel. +32 2 282 08 77, steurer@eurochambres.eu
Press contact: Ms. Guendalina Cominotti, Tel. +32 2 282 08 66, cominotti@eurochambres.eu
All our position papers can be downloaded from www.eurochambres.eu/content/default.asp?PageID=145