AFEP

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AFEP's position concerning the Commission's "backloading" proposals

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The Association française des entreprises privées (AFEP) wishes to express its views on the Commission initiative aiming at preparing a change of the timing for auctions of emission allowances, in the context of the public consultation opened on this purpose.

AFEP represents more than 95 of the top private sector companies operating in France. The French listed companies which belong to AFEP have more than 5.8 million employees and a combined turnover of over 1500 billion euros.

Our position is based on three messages:

1/ The current ETS system reflects a fall in greenhouse gas emissions, which is in line with its objective, but does not provide the medium to long-term visibility (2030 and beyond) required to stimulate investments

AFEP is keen to point out that the European Commission designed the ETS Directive as an instrument based on regulating the **quantities** of allowances permitted, in order to ensure a regular reduction in the **level of greenhouse gas emissions** (GHG) in absolute terms over time. In so doing, its stated principle was that:

- allowance prices **should reflect supply of and demand for** allowances (no price fixing),
- emissions reductions could come **either from operators improving specific emissions** (emissions per unit of production) via investments, **or from a fall in the level of production**. However, the Commission did not anticipate at the beginning of its project that activity levels would drop or decrease, which has led to the adoption of growth hypotheses which are too optimistic at this stage when it comes to calculating the volume of allowances.

Consequently, the current low allowance price does not mean that the ETS system "is not working". Quite the opposite. This low price simply reflects the fact that GHG emissions from the installations covered by the directive have actually fallen, due in particular to the economic crisis, and also to the efforts made by companies in order to reduce their emissions. The emissions reduction objective has, in fact, been met.

However, it should be noted that, in the current period of reduced growth, the ETS system by itself cannot provide the stimulus for low carbon investments in the long term, i.e. beyond 2020, which is the year when the third ETS period ends. Indeed, there is a **high level of uncertainty** for investors concerning EU GHG reduction requirements **beyond the 2020 time horizon**, despite the tacit application of the directive's annual linear reduction factor (-1.74% per year) beyond 2020 implying that, by 2030, the emissions reduction level compared with 2005 should be -38%. This uncertainty is linked to the fact that **a 2030 objective has not yet been adopted explicitly** by the Member States and **should be adjusted in order to take into account the surplus of allowances at the end of 2020** in relation to the EU objective of a reduction of -21% between 2020 and 2005 for installations under ETS.

2/ Companies need stability concerning the rules already adopted for phase 3 (2013-2020) and are of the opinion that the Commission's current proposals would bring added uncertainty to the carbon market for obliged operators

a) Concerning the Commission proposal for a decision modifying the ETS Directive

The proposed decision seems to give the European Commission **the power to amend the auctioning of allowances (particularly the auctioning regulation) at any time** and, as a result, grants it the **quasi-permanent and unsupervised power to regulate allowance prices.** This does not reflect the initial objective of the ETS Directive based on quota restrictions for emissions.

It should be pointed out that this amendment of Article 10 (4) of the ETS Directive **does not have a comprehensive legal basis.** Indeed, the fundamental rules for auctioning and determining the annual profile of the allowances to be auctioned with a linear coefficient of -1.74% per year are already laid down in Articles 9 and 9a of the directive. However, these Articles are not amended by the proposal.

Furthermore, the Commission has not yet provided **any impact assessment** showing the appropriateness of its proposal.

With regard to the amendment proposed by the Commission, while the recitals of the draft decision state that the Commission is able to adapt auctioning terms only **"in exceptional circumstances"**, the actual draft amendment states in a much more general way **"where appropriate".** Both wordings, but obviously the second even more, would create too much uncertainty for the market as it would enable the Commission to intervene without any real supervision. Thus the allowances price could be permanently subject to speculations regarding the Commission's possible interventions.

Finally, again in this amendment, the Commission **does not specify its assigned objective because the phrase "orderly functioning of the market" is not explained**. It is essential that the Commission **clarifies the meaning of this statement.**

b) Concerning the Commission's draft Regulation amending the Auctioning Regulation

The basis for the Commission's intervention is its conviction that the current allowance price is not sufficient to make long-term investments to reduce GHG emissions profitable. In order to respond to this issue, it is planning to resort to **"backloading", i.e. the withdrawal of allowances due to be auctioned over the 2013-2015 period in order to reintroduce them in auctions between 2016 and 2020**.

Yet we note that in point 11 of the Commission's Q&A concerning the draft auctioning regulation, the Commission states that: ***"It is not possible to determine with certainty the absolute impact of backloading on carbon prices over time"*** followed by ***"Over the longer term, the impact of a back-loaded auction time profile is likely to be limited given that total quantities over the 8 year period do not change."***

The Commission's analysis therefore appears to **contradict the very aim of its approach**, which is to raise allowance prices. The benefit of "backloading" is therefore in question.

If the Commission's intention were, in fact, to implement "backloading" today with the idea of withdrawing the surplus later during the 2013-2020 period, **the immediate consequence would be to introduce uncertainty concerning price levels throughout the 2013-2020 period up until the Commission's new initiative**.

c) Concerning the missing documents

The Commission launched its initiative on 25 July of this year with a view to its draft decision being adopted rapidly and the draft auctioning regulation being adopted early, without having made its **impact assessment** of these amendments public and without having formalised its **post-2020 vision** of the ETS system.

It seems **inappropriate to vote on these draft texts before the aforementioned two documents have even been published and analysed**.

Companies are therefore of the opinion that the European Commission's initiative has no legal foundation and will not enable a rise on allowance prices and will not improve the steadiness of the price signal. It does not provide a response to the visibility needed by economic operators to trigger medium to long-term investments.

3/ Companies recommend that medium to long-term visibility be provided (2030, 2040 up to 2050), since this alone can stimulate low carbon emission investments across the EU

To promote investments in low carbon emission technologies and processes in the medium to long term, it is essential for the authorities to **launch now at EU level a working group of Member States responsible for defining a future time horizon for reducing greenhouse gas emissions for 2030 and 2040**, in line with the energy production outlook.

Launching a working group for the 2030 time horizon (with a possible 2025 intermediate milestone) should **immediately generate a rise in allowance prices** given the facility to "bank" allowances from one period to the next. Furthermore, this working group should suggest to **deduct a volume of allowances considered surplus at the end of 2020 from the 2030 objective** given the Commission's objective to reduce the emissions of installations under ETS by 21% between 2005 and 2020. This initiative should also enable **allowance prices to rise now**, and support low carbon emission investments across the EU.

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