EUROPEAN COMMISSION
DIRECTORATE-GENERAL ENVIRONMENT
Directorate A - General and international affairs
ENV.A.2 - Climate Change

Brussels, 28 September 2000
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SUMMARY RECORD OF SECOND MEETING:
ECCP WORKING GROUP 1
19 JULY 2000

Present: see list attached (as Annex 1)

Chaired by Mr Jos DELBEKE, Head of Unit DG ENV.A.2

1. Opening

The Chairman welcomed the few new faces and introductions were made.

2. Adoption of agenda and record of previous meeting

The draft agenda and the draft record of the previous meeting were adopted without amendment.

3. Presentation of the results of the economic analysis done for the "Green Paper on greenhouse gas emissions trading within the EU" by DG Environment, Unit B2

Mr Peter ZAPFEL (DG ENV.B2) made a presentation of the findings of the economic analysis undertaken by the Commission's services to date. Further details of this analysis can be found at the following internet website: http://www.europa.eu.int/comm/environment/enveco/studies2.htm#13. The key message of the presentation was that, even acknowledging the limitations of model-based economic analysis, emissions trading would allow substantial economic benefits, as emphasised in the Annex to the Green Paper. Furthermore, it was clear from the presentation that a flat-rate reduction across all sectors within each Member State (the "cheese-slicer" approach) would be very costly and inefficient. Finally, the impact on competitiveness of reaching a pre-determined result with emissions trading is no more, and indeed potentially much less, than other policies and measures.

Participants posed a number of questions. Mr HEIN (BDI) disagreed with the model's conclusion that Germany would be a net seller of permits. Ms WOLLANSKY (AUSTRIA) also questioned the results in respect of Austria. The Chairman summarised recognising that good cost estimates are central to economic evaluation. Nevertheless, trading throughout the Community would reduce the costs more compared to trading within each Member State individually, and that costs could be further reduced by trading beyond the confines of the EU.

4. <u>Continuation of the exchange of views on Background Document 1 (revised): "Objective setting in the context of emissions trading and voluntary agreements"</u>

A lengthy discussion took place on the Background Document 1 (revised 1). A central issue was the possible combination of using both relative and absolute targets. Relative targets could deliver absolute reductions in practice. The difficulty was converting relative targets into absolute quantities, something that, it was acknowledged, could only be done with certainty *ex post* (conversion can also be done on the basis of forecasts, but with the uncertainties inherent in forecasting). Such trading as does take place before this *ex post* establishment of reductions means that trading before this time would be on a forward market basis, and subject to confirmation when the necessary verification of actual emissions can be made. Ms MOGFORD (ETG) suggested that distinction be made between "trading" and "transfers", the latter only being possible when relative targets have been shown to be met. Increasingly, the discussion focussed on whether relative targets for particular sectors or entities would exclude entities from engaging in international emissions trading governed by absolute targets. The role of relative targets being "topped up" by the purchase of absolute reductions was discussed (potentially from the project mechanisms as well as absolute trading schemes). Mr LEFEVERE (FIELD) suggested that it is necessary to ensure that relative targets converge with absolute targets, and as there is a risk that such convergence will not happen, someone has to assume this risk. Mr HAYDEN (DG ECFIN) believed that even if relative targets could be converted in to absolute numbers, such targets where incompatible with trading across borders with other "absolute" schemes unless the participants accept an absolute cap on their aggregate emissions". Mr COATES (UK) emphasised that, in the international context, trades must be backed by adjustments to the assigned amounts of the Parties concerned. If this is the case, Dr. KYTE (ETG) argued, relative targets could be compatible with cross-border trading.

There was also discussion on whether sectors or companies, or both, should have commitments, and whether having commitments was a pre-requisite to participation in emissions trading. Issues of difficulty included legal responsibility and enforcement, "free-riders" within a sector and competition issues within the same sector (including new entrants). Mr HEIN (BDI) believed that only those that had commitments could trade, and that if sectors had commitments, then they - rather than their companies - could trade. Other participants expressed doubts that sectoral associations could adequately enforce such schemes, especially in the case where the sector as a whole failed even though individual companies within it complied with the obligations of their sectoral commitment (or *vice-versa*). Ms GASTALDO (FRANCE) raised the question whether companies within a given sector would have to be obliged to join a scheme – even a "voluntary agreement" – for reasons of competition. Some sort of "incentive" (taxes or alternative technical standards) would have to be imposed on companies that wanted to stay out.

The Chairman summarised that it is flexibility that reduces costs, and that flexibility can exist on a number of levels: temporal, geographical, numbers of gases, and also emissions trading, which is another mechanism for providing flexibility. The Kyoto Protocol reflects each of these ways. However, the objective that we are seeking is not to create a new market in allowances for its own sake, but rather as a means of providing a greater degree of flexibility in obtaining a given outcome. In that context, post-verification trading, “topping up” voluntary agreements and allowance trading could each provide extra flexibility in different contexts.

5. Exchange of views on Background Document 2: “Allocation methodologies and recognition of early action”

A first exchange of views took place on Background Document 2. The imperfections of each method of allocation were acknowledged. It was agreed that combinations of allocation methodologies are both likely and desirable. What was most important was to get emissions trading started. Agreement on allocation remained a major hurdle to overcome before a start could be made.

Discussion centred on the legality of auctioning what was previously available for free. In this context, Mr LEFEVERE (FIELD) emphasised that in the regulated area of environmental protection, no one has been given an explicit right to pollute, so auctioning could not take away what has not been granted before in an explicit legal manner. It was agreed that auctioning is a forward-looking instrument, insofar as businesses will have to anticipate their likely future needs. Grandfathering, on the other hand, is an administrative procedure (involving no payment) that is essentially backward-looking. The difficulties of establishing benchmarks was widely acknowledged given the number of sectors and sub-sectors in respect of which benchmarks would have to be agreed. Mr CANEILL (EURELECTRIC) believed – on the basis of the Eurelectric “GETS2” simulation - that there are links between the basis of allocation and the strategy of the participants that might impact on the functioning of the market. Mr BRADLEY (CNE) maintained that it would be impossible to subsidise industry in one Member State (through over-generous grandfathering) without impacting on market efficiency. What is important, as the Background Document says, is that industry understands that early action will not be discriminated against. However, it was rightly emphasised that not everyone likes early action, in particular those who have *not* undertaken any.

It was widely felt by industry representatives that auctioning and taxation would be completely excessive, threatening competitiveness. Furthermore, any method of grandfathering (historical or benchmark) would require establishment of a base year against which future performance would be measured. Although for the Kyoto Protocol this was 1990, for companies the same year did not have to be taken. Indeed for practical reasons of data availability, a more recent period would be more feasible.

The Background Document being discussed looked at allocation methodologies from a static perspective, whereas it would be useful to suggest how allocation methodologies can, and even should, develop over time. The issue of new entrants was once again explored.

The Chairman once again concluded making the point that we were not trying to ensure as much trading as possible. What we were looking for was an incentive that makes all participants look critically at what potential reductions they could achieve on their own, before looking outside to see what opportunities for trading existed (very much domestic action). That is the opportunity that emissions trading offers, but getting a system in place is a pre-requisite to create such an incentive.

6. Any other business and close of meeting

Further written comments on both Background Documents were requested to be made by 22 August 2000.

Date of next meeting was confirmed as taking place on 26 September 2000 (10h00 until 18h00). It will take place in Room 0/C at the offices of DG Environment:
5, Avenue de Beaulieu, B-1160 Brussels.

Peter VIS
Principal Administrator
Secretary to Working Group 1

Annex 1

ECCP Working Group 1

Second meeting: 19 July 2000

(* means that attendance was for half a day only)

NAME	Organisation
DELBEKE Jos (Chairman)	DG Environment, Unit A2
VIS Peter (Secretary)	DG Environment, Unit A2
VANHEUKELEN Marc	DG Environment, Unit B2
ZAPFEL Peter	DG Environment, Unit B2
HAYDEN Mark	DG Economic & Financial Affairs
DOSCHKO Susanne	DG Enterprise, Unit E1
BOESHERTZ Daniel	DG Taxation and Customs Union, Unit C4
VON SCHOLZ Hans-Eike	DG Transport and Energy, Unit A3
FÜHR Vivien	DG Transport and Energy, Unit A3
CANEILL Jean-Yves	EURELECTRIC
DE LANNOY Rose	EURELECTRIC
JOHANSSON Niklas	Swedish National Energy Administration
WOLLANSKY Traude	Environment Ministry, Austria
GASTALDO Sylviane	Environment Ministry - France
COATES Ian	Department of Environment, Transport and the Regions, United Kingdom
KEMBER Mark	WWF
WRIGLESWORTH Mike	Union of Industrial and Employers' Confederations of Europe (UNICE)
BRADLEY Rob	Climate Network Europe (CNE)
KYTE Bill.	Emissions Trading Group, United Kingdom
MOGFORD Margaret	UKETG / BG. Plc
HEIN Joachim	BDI
BALOCCO Francesco	International Federation of Industrial Energy Consumers (IFIEC)
LEFEVERE Jürgen	Foundation for International Environmental Law and Development (FIELD)