The EU ETS review:
Implications for credit import

CEPS, 14 January 2009
Key elements

• In line with supplementarity principle in Kyoto Protocol
  – 50% of "needed effort"

• Levels out differences in phase 2 NAPs
  – But only to some extent

• Key issues to be decided later
  – CER/ERU import limit in 30% reduction scenario
  – Qualitative restrictions in phase 3
EU ETS: Quantitative limit

• Should be 50% of "needed effort"
  – About 1550-1750 Mt over 2008-2020 (EC calculation)
  – Needed effort = 2005 emissions – Allocation phase 2 and 3

• Will increase as new sectors and installations are included
  – Aviation (2012-20): ~ 50 Mt
  – New sectors (from 2013): ~ 40-50 Mt
  – New entrants (phase 3): ~ 50 Mt

• Could potentially increase to + 1900 Mt
  – But inclusion of new sectors will reduce credit import limit in non-trading sectors
What is the needed effort?

Total effort needed: 3500 Mt

Total effort needed: 3110 Mt

2005 emissions

Phase 2 cap

Phase 3 cap

Cap/emissions  Needed effort

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CER/ERU import: Operator level

• All operators will get a credit limit of at least 11% of the phase 2 allocation
  – All operators with a higher limit than 11% in phase 2 will keep the higher limit (e.g. Germany, Spain, Italy etc)
  – For other operators (will lower limit) the limit will be increased to 11%

• A credit limit beyond 11% will be given to the operators being "most short" (allowances and credits) in phase 2
  – (EUAs + credits)/2005-07 emissions equal to a certain percentage
  – Size of "additional reserve" decided later (essentially being what’s left)

• Not possible to use more than 1400 Mt in phase 2
Which countries will benefit?

<table>
<thead>
<tr>
<th>Country</th>
<th>Phase 2 NAP (2008-20, Mt)</th>
<th>New limit (11%) (2008-20, Mt)</th>
<th>Difference (2008-20, Mt)</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>99</td>
<td>135</td>
<td>36</td>
</tr>
<tr>
<td>Poland</td>
<td>104</td>
<td>114</td>
<td>10</td>
</tr>
<tr>
<td>Belgium</td>
<td>25</td>
<td>32</td>
<td>7</td>
</tr>
<tr>
<td>GER (+ 8 other MS)</td>
<td>453</td>
<td>453</td>
<td>0</td>
</tr>
</tbody>
</table>

- Increase will be even larger in UK due to additional import (beyond 11%)
- At least 11% to all operators: About 1550 Mt
Who will get additional credits (beyond 11%)?

![Bar chart showing EUA allocation, CER/ERU import limit, and Relative shortage for RWE, Vattenfall AB, E.ON, and Drax Group Plc.](chart.png)
Will CER/ERUs cover shortage?

Average phase 2 emissions forecast

<table>
<thead>
<tr>
<th>Phase</th>
<th>Allocation</th>
<th>Credit limit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Phase 2</td>
<td>2100</td>
<td>1800</td>
</tr>
<tr>
<td>Phase 3 (20%)</td>
<td>1800</td>
<td>2000</td>
</tr>
</tbody>
</table>
Qualitative restrictions: With agreement

- Once an international agreement has been reached, only credits from countries that have ratified the agreement will be accepted from 2013

- Credits will not be exchanged but used directly for compliance
  - But still within overall credit import limit

- Specific project types may be excluded from 2013
  - Commission and Member States can propose exclusion of project types
  - Decision to exclude projects will be taken in simplified decision-making procedure (Comitology)
  - Potential restrictions will only take effect from 2013
Qualitative restrictions: Without agreement

• Until international climate agreement enters into force:
  – Member States will exchange CER/ERUs with phase 3 allowances up to 31 March 2015

• What kind of credits can be exchanged with phase 3 EUAs?
  – Credits from all projects registered before 2013
  – Credits from projects started after 2013 in Least Developed Countries
  – Credits from countries based on bilateral agreement (in case an international climate agreement is delayed)

• All credits eligible for use in phase 2 can exchanged with in phase 3 allowances (subject to the above conditions)
Effort sharing

• 3% of 2005 emissions
  – And an additional 1% given to Austria, Finland, Denmark, Italy, Spain, Belgium, Luxembourg, Portugal, Ireland, Slovenia, Cyprus and Sweden
  – About 750 Mt over 2013-20 period

• Trading of credits allowed
  – But restricted to 3% for each Member State
  – Banking of credits is also allowed

• Similar qualitative restrictions as EU ETS
  – But forestry projects also accepted
Total EU credit demand

- Numbers for 30% target only indicative (in line with initial EC proposal, not the final outcome)

<table>
<thead>
<tr>
<th></th>
<th>20% scenario (Mt)</th>
<th>30% scenario (Mt) Only indicative</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU ETS 2008-20</td>
<td>1700-1900</td>
<td>2570</td>
</tr>
<tr>
<td>EU gov 2008-12 (CER, ERUs or AAUs)</td>
<td>870</td>
<td>870</td>
</tr>
<tr>
<td>EU gov 2013-20</td>
<td>750</td>
<td>1300</td>
</tr>
<tr>
<td>Total</td>
<td>~ 3300-3500</td>
<td>4740</td>
</tr>
</tbody>
</table>
Conclusions

• Complex CDM/JI market
  – Not everybody will bother to get engaged

• Uncertainty not removed
  – Credit demand in 30% scenario
  – Qualitative restrictions

• More diversified credit market towards 2020?
  – EU vs UN rules?
  – Harmoised rules in EU and US carbon markets?
Thank you for your attention!

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