
Strengthening the EU ETS: Objectives and options

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Objectives of EU ETS

Primary objectives:

- Deliver an environmental objective efficiently at a negotiated balance of acceptable cost
- Influence corporate investment towards low carbon investment

Secondary objectives:

- Contribute to EU's international commitments in assisting developing countries (eg. CDM)
- Raise finance including to support low carbon innovation (eg. NER 300)

Deliver an environmental objective efficiently at a negotiated balance of acceptable cost

- Environmental objective delivered
- Impact on investment choices reduced by volatility
- Balance of quantity and cost entirely different from that originally negotiated

Influence corporate investment towards low carbon investment

- I. *Capturing Companies' Attention* – still relevant
- II. *Providing Clarity for Decision Making* – little or none
- III. *Creating enabling environment for Low-Carbon*

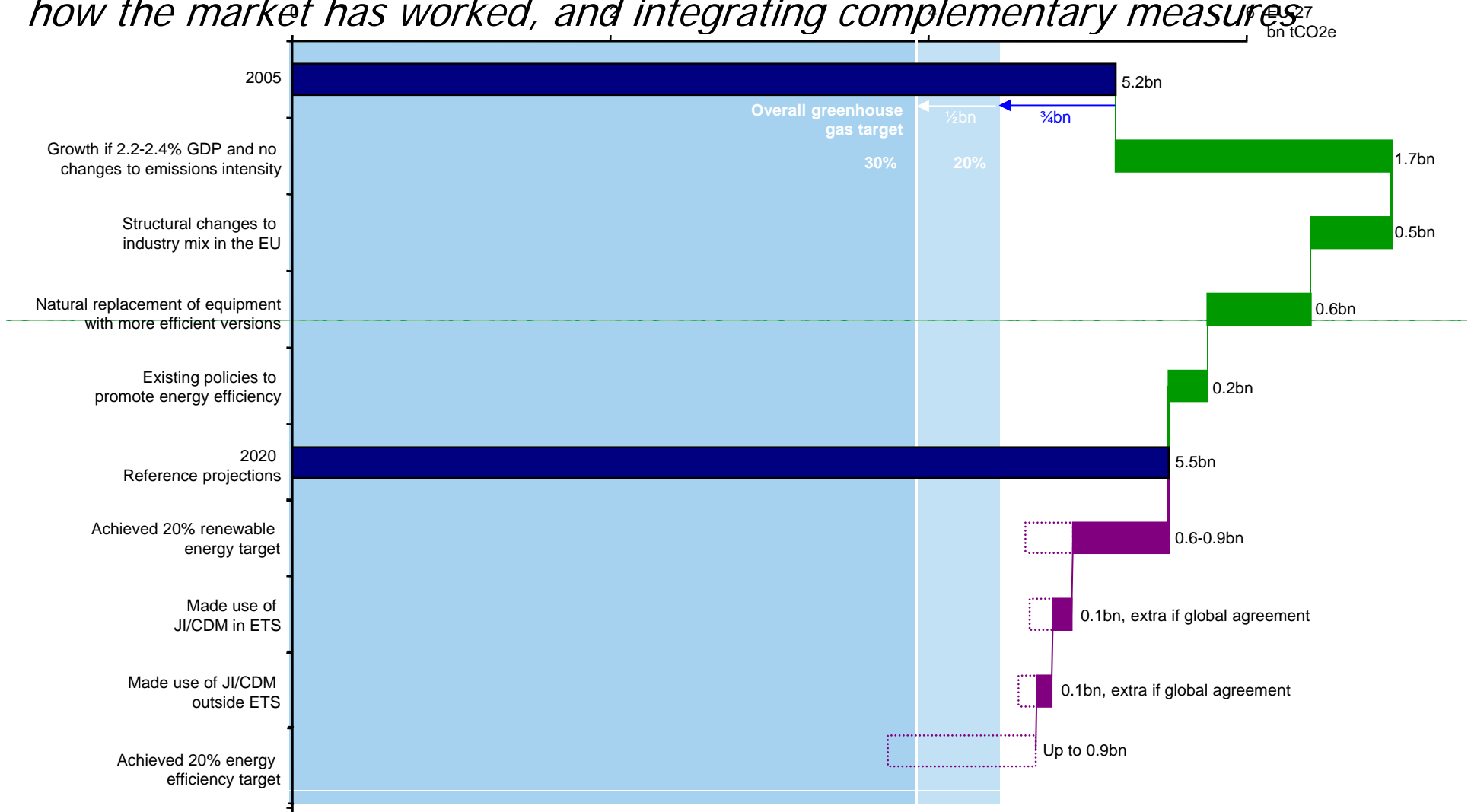
Secondary objectives – including revenue implications

- are *not irrelevant* either, though complex debate about use of revenues

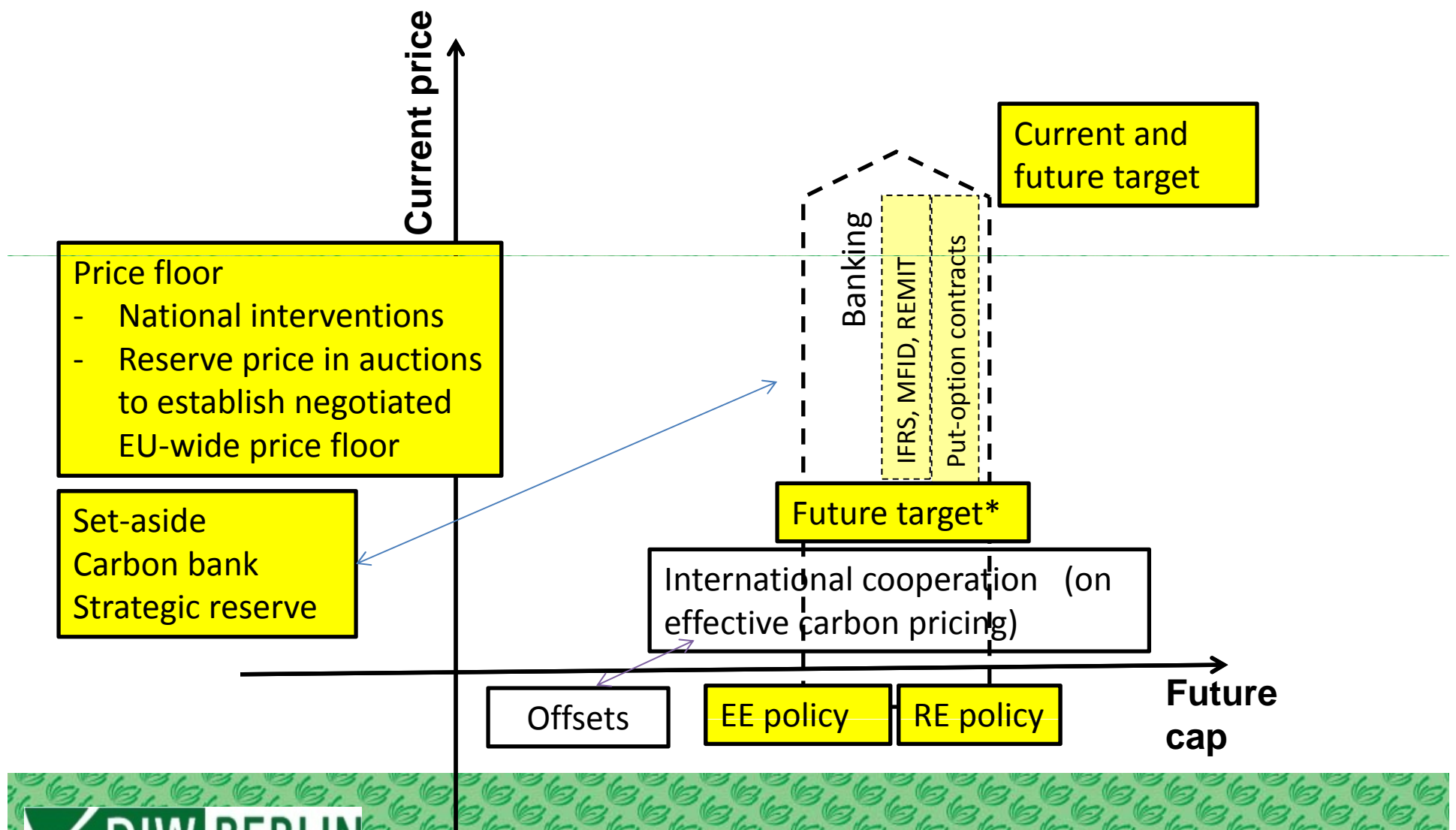
Country	Final auction rights entitlement (%)	€ million in revenues during Phase III of the EU ETS			
		20% (a) scenario (€17/tCO ₂)	20% (b) scenario (€25/tCO ₂)	30% (a) scenario (€30/tCO ₂)	30% (b) scenario (€55/tCO ₂)
		Power & manufacturing not at risk			
Austria	88	1,040	1,294	1,346	2,069
Belgium	96.8	2,194	2,737	2,844	4,379
Bulgaria	150.3	3,562	4,623	4,823	7,808
Cyprus	105.6	312	404	422	684
Czech Republic	117.4	5,878	7,632	7,962	12,889
Denmark	88	2,242	2,790	2,901	4,457
Estonia	145.2	1,567	2,033	2,120	3,431
Finland	88	2,554	3,179	3,304	5,071
France	88	4,299	5,357	5,570	8,569
Germany	88	36,591	45,551	47,354	72,740
Greece	103	6,530	8,125	8,444	12,959
Hungary	120.7	1,067	1,386	1,446	2,340
Ireland	88	1,335	1,668	1,734	2,673
Italy	89.8	14,365	17,888	18,599	28,580
Latvia	196.9	181	236	246	400
Lithuania	173.6	399	519	545	882
Luxembourg	95	5	7	7	11
Netherlands	88	4,869	6,062	6,301	9,682
Poland	128	16,878	21,907	22,857	36,998
Portugal	102.1	2,121	2,640	2,744	4,214
Romania	152	3,972	5,157	5,379	8,707
Slovakia	129.2	775	1,006	1,050	1,700
Slovenia	105.6	427	553	578	936
Spain	99.4	13,300	16,563	17,217	26,461
Sweden	96.8	684	852	892	1,371
UK	88	18,537	23,077	23,987	36,847
Totals	n/a	145,684	183,246	190,672	296,858

Surplus under 2020 cap was predictable (and predicted)

– *NOT* attributable purely to recession, raises interesting questions about how the market has worked, and integrating complementary measures



Many interventions impact on net cap and/or price



Options

1. Future EU GHG targets
 - After 2020
 - Renegotiate the 2020 target
2. Tightening the ETS cap/trajectory
3. Ex-post/policy linked set-aside allowances
 - One fixed withdrawal
 - Mandate eg. to match progress in energy efficiency
4. National floor price – domestic corrective mechanisms
5. Reserve price auctions for the ETS
6. “Carbon bank”

Short-run CS project, to assess with respect to:

- Extent to which contribute to primary and secondary Objectives
- Technical, political & procedural feasibility



Screening options: 1 Future EU GHG targets

- After 2020
 - Useful for strategic planning (framework – one dimension of investment)
 - However given current state of financial markets and market attitude to political risk, strengthening post 2020 targets alone might only have limited impact on current price (high discounting in financial markets)
- Renegotiate the 2020 target... ?
 - Maybe linked to post-Durban process notably KP-II: proposal to be tabled 1 May
 - Require renegotiation of burden sharing agreement including division between traded and non-traded sectors
 - after Durban, an option to evaluate but given politics of last year may be a difficult road

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2. Tightening the ETS trajectory

A conceptually simple measure that would lift price:

- In effect would be a re-run of cap setting negotiations
- Would require clear rationale for re-visiting cap so as to limit uncertainties for market participants
- Could be aligned with Roadmap
- Would not reduce price *uncertainties*
- .. Other attributes?

- *Study*



3. Set-aside / Strategic reserve

- Would need to be clear about the basis for quantification
- Would need to be clear about what precedent is this setting
- Withdrawal, or strategic reserve?

- Fixed quantity:
 - is there a clear process / timing for future caps (or renegotiation)?
 - is there credibility that it is a “once only”?
 - is there a “force majeure” case?

- Or Policy (eg. EED) linked:
 - Challenges of quantification and process
 - Attribution between EED and Member State implementation
 - Why just EED (not other policies and measures)
 - On its own wouldnt address current price level, merely partial protection against further reduction

- Fixed/strategic reserve less enduring problems but doesn't in itself resolve need for a more robust “enduring regime”?



4. National price floor(s)?

- As with UK top-up carbon tax
- Provides some price certainty for power sector investors in those countries
- Introduces competitive distortions *within* EU
 - Will they trigger compensatory measures and further distortions?
- Keeps revenues nationally
- Political implication
 - Signals commitment to strengthen ETS scheme?
 - or risk for Integrated European Climate Agenda?



5. Reserve price for allowance auctions

- In principle, an *ex ante*, though can be agreed at any time
- Allowances not taken up at auction could be either cancelled or banked forward
- With sufficient share of allowances sold in auctions, establishes a price floor – making explicit and protect the trade-off assumed at time of adopting the environmental target
- Negotiate a schedule of rising minimum reserve prices through Phase III (eg. €10/15 rising to €20/25 by 2020)
- Underpinning price certainty for investors
- Present allocations untouched (but their value is increased)

Implementation

- Needs to be agreed across all auction platforms
- Sets a *de facto* price floor, though potential complexity around credit imports



6. Carbon bank?

- Would require a clearly defined role and remit
 - Is mandate clear enough to provide credibility?
- How governed
- How capitalised / underwritten
- A major institutional undertaking



Proposed options for further evaluation

Criteria	Strategic reserve	Revise EU 2020 target	Revise ETS trajectory	Reserve price auctions (EU floor)
Environmental objective efficiently at acceptable cost				
Influence corporate investment				
Contribute towards EU's international commitments				
Raise finance (including for NER300)				
Technical feasibility				
Procedural feasibility				
Political feasibility / timescale				

Not necessarily exclusive, but may have different timing potentials