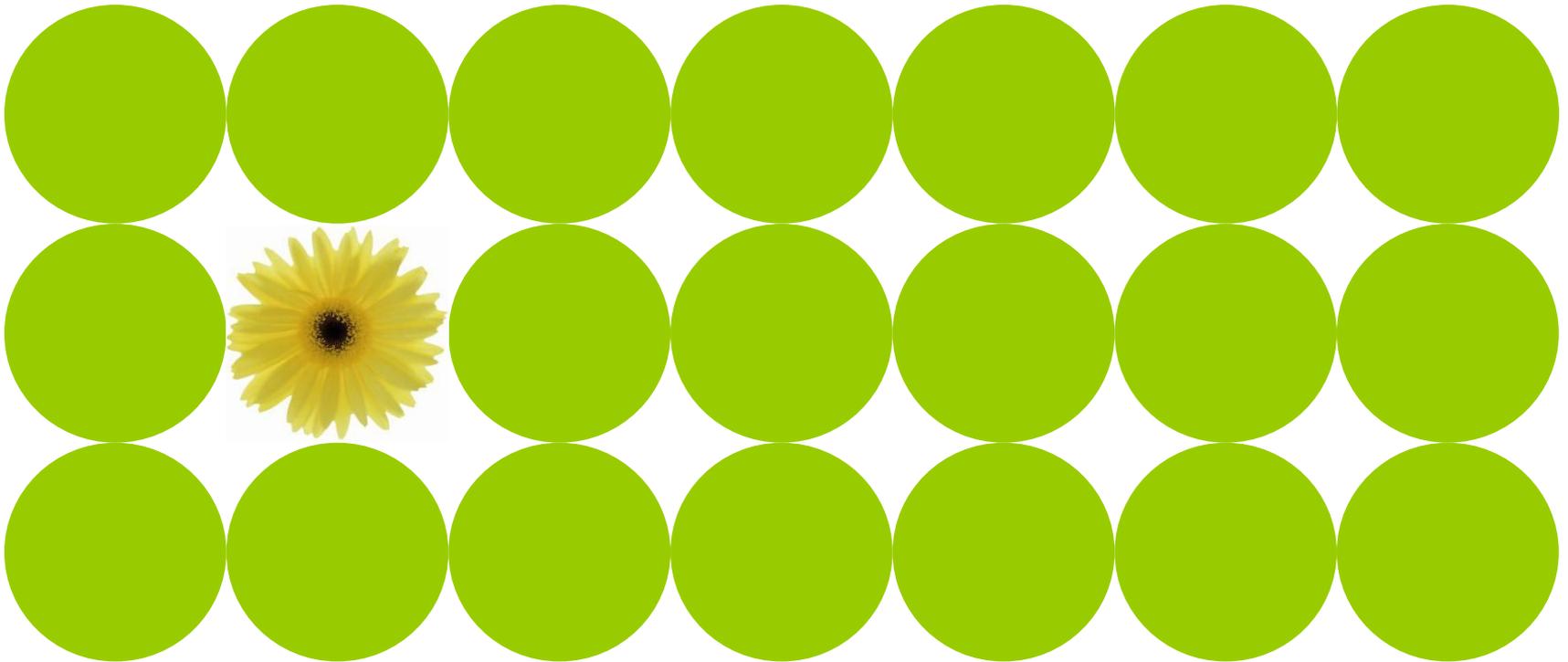


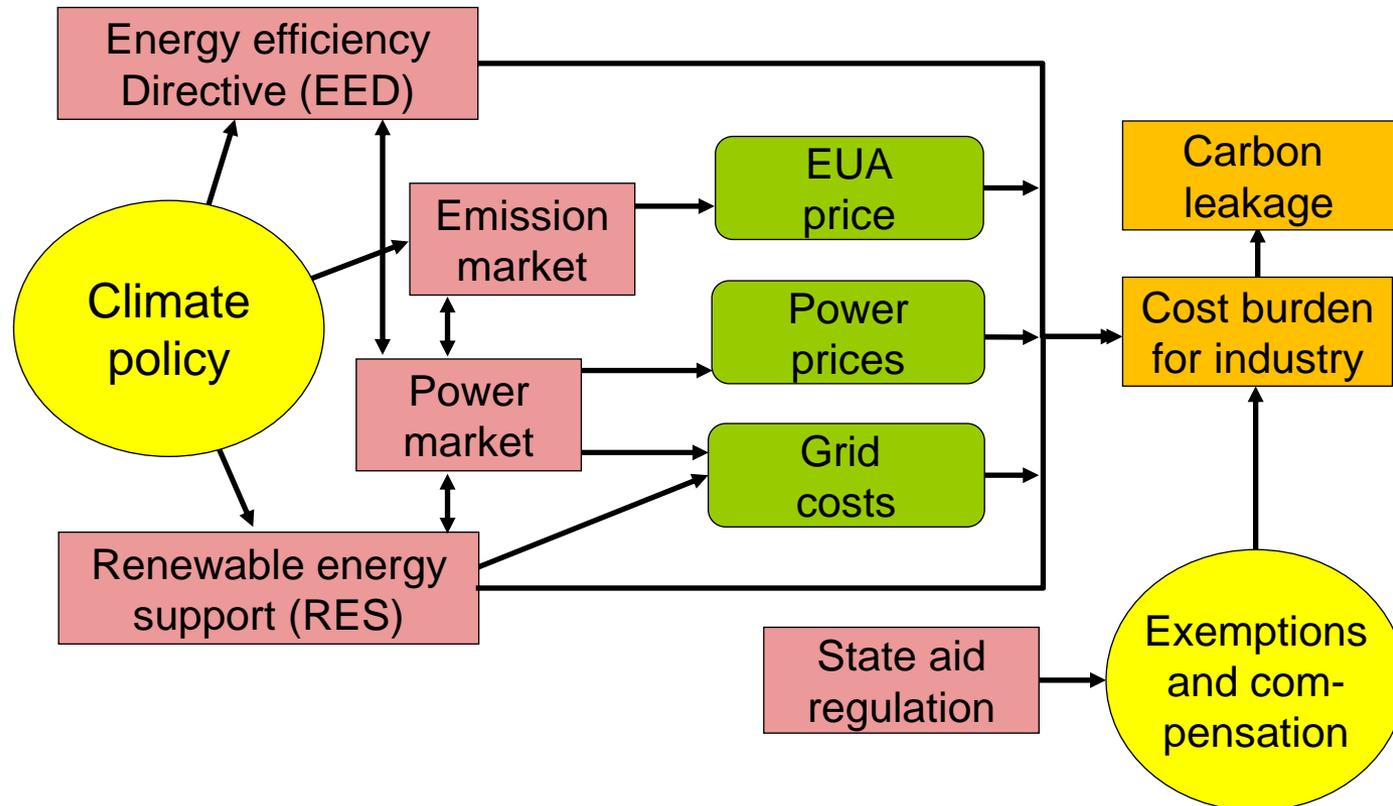
The role of emission trading in the EU C&E policy

CCMF Task Force on "Post-2020 EU Climate Change Policy"

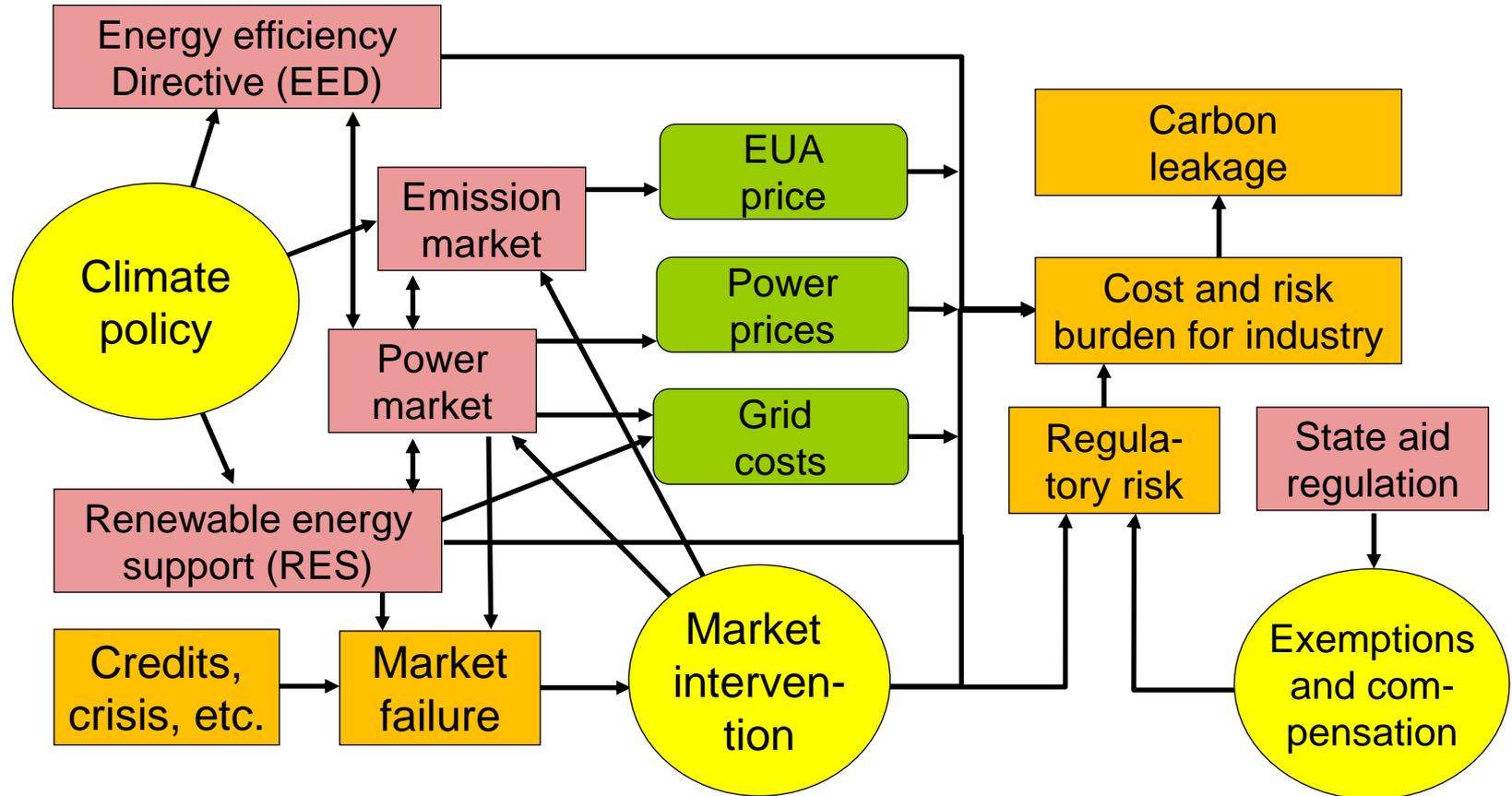


Petter Longva

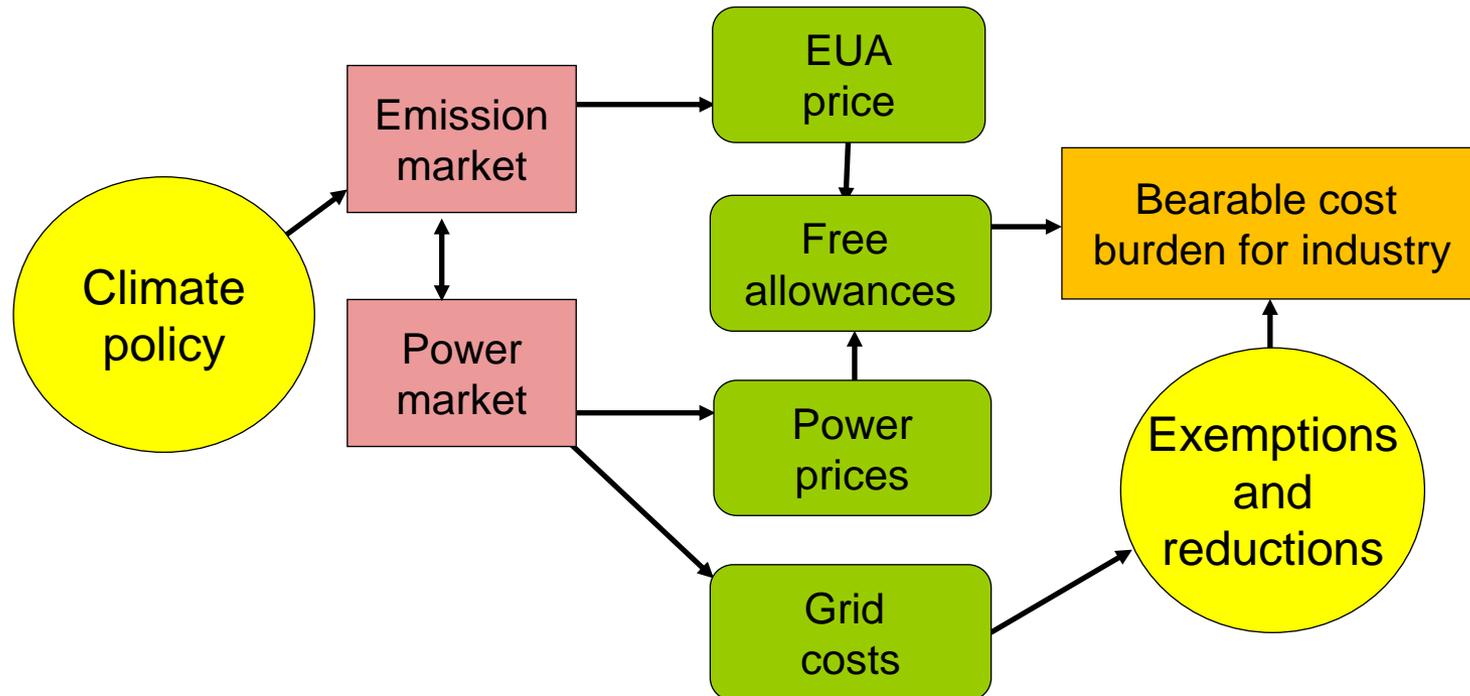
Climate, energy, and industry policies are linked through electricity and emission markets



With low EUA prices, regulatory risk is a key issue preventing industrial growth in Europe



Climate policy should provide built-in carbon leakage protection



- Internalising unintended effects of ETS
- Reduced role of state aid investigation
- Reduced roles for RES and EED

ETS should respond to the challenges of European climate policy

- International climate policy
 - ETS will remain a regional system
 - Help delivering on pledges
 - Avoid carbon leakage
- Fragmented EU policy
 - ETS will have to coexist with supplementary climate policies
 - The EUA market covers only a small share of emission
 - Political stalemate makes deep reform difficult
- Restarting European industrial growth
 - High European climate cost
 - Political risk increasing capital cost for investors
 - Restore industrial cost levels and investor confidence

The reform agenda

1. Built-in carbon leakage protection

- Objective: Making investment possible in industries that compete globally
- Free allowances based on actual output

2. Setting the ETS cap

- Objective: Secure a role for ETS in climate policy
- Rolling emission periods (e.g. between 10 and 20 years at any time)
- Updated to secure that the total EU cap is attained

3. Auctioning

- Objective: Stabilise pricing at levels reflecting long-term expectations
- Control open positions (the stock of unused allowances)
- Adapt supply of allowances to short-term variations in demand

4. Governance

- Objective: Reduce political risk; improve policy efficiency
- Predictable procedure for further system reform

Reform example:

Updating of the ETS cap and the auctioning volume

- The **EU cap** includes all relevant emissions in the relevant period
 - Set by politicians in international negotiations
- The **ETS cap** = The EU cap – Expected emissions outside ETS sectors
 - Periodically updated in tightly defined procedure
 - Deducting actual emissions from the remaining EU cap
 - Revising expected emissions based on revised policies, economic outlook etc.
- Expected allowance demand = Remaining ETS cap
 - Expected use of external credits and free allowances the rest of the period
 - Making sure that credits and free allowances do not jeopardise the integrity of the ETS cap
- Annual auctioning volume = A share of total expected allowance demand
 - Further adjustments to make sure that open positions are within a given band
 - Predetermined minimum auction selling price (reserve price)

Conclusions

- Regulatory risk prevents industrial growth in Europe
- Respond to political and economic challenges
 - Weak global collaboration
 - Weak EU coordination
 - Revitalising industrial growth
- Pragmatic process, avoiding deadlock
 - No industrial growth without ETS reform
 - No tightening of the market without carbon leakage mitigation
 - No carbon leakage mitigation without higher EUA prices
- Reform elements
 - Built-in carbon leakage protection
 - Secure the role of ETS as a climate instrument
 - Fix the market mechanism
 - Effective governance