



The EU ETS in the next decade

Reforming the EU ETS – the main instrument to achieve Europe's climate targets

Bijeenkomst BE stakeholders, 29 Sept 2015



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Introduction and context





EU ETS in a nutshell

- Europe's key instrument to reduce emissions
- In place for 10 years now
- Largest cap-and-trade system of the world: 84% (value) and 76% (volume) of global carbon market
- Cap on emissions of ~12,000 energy-intensive installations across EU
 - Electricity and heat producers, steel, chemicals, cement, glass, pulp&paper
 - Extended scope as from 2013: new sectors and gases: N₂O (chemicals), PFC aluminium, CO₂ from processes
- and aircraft operators
- Covering around 41% of EU CO₂ emissions;



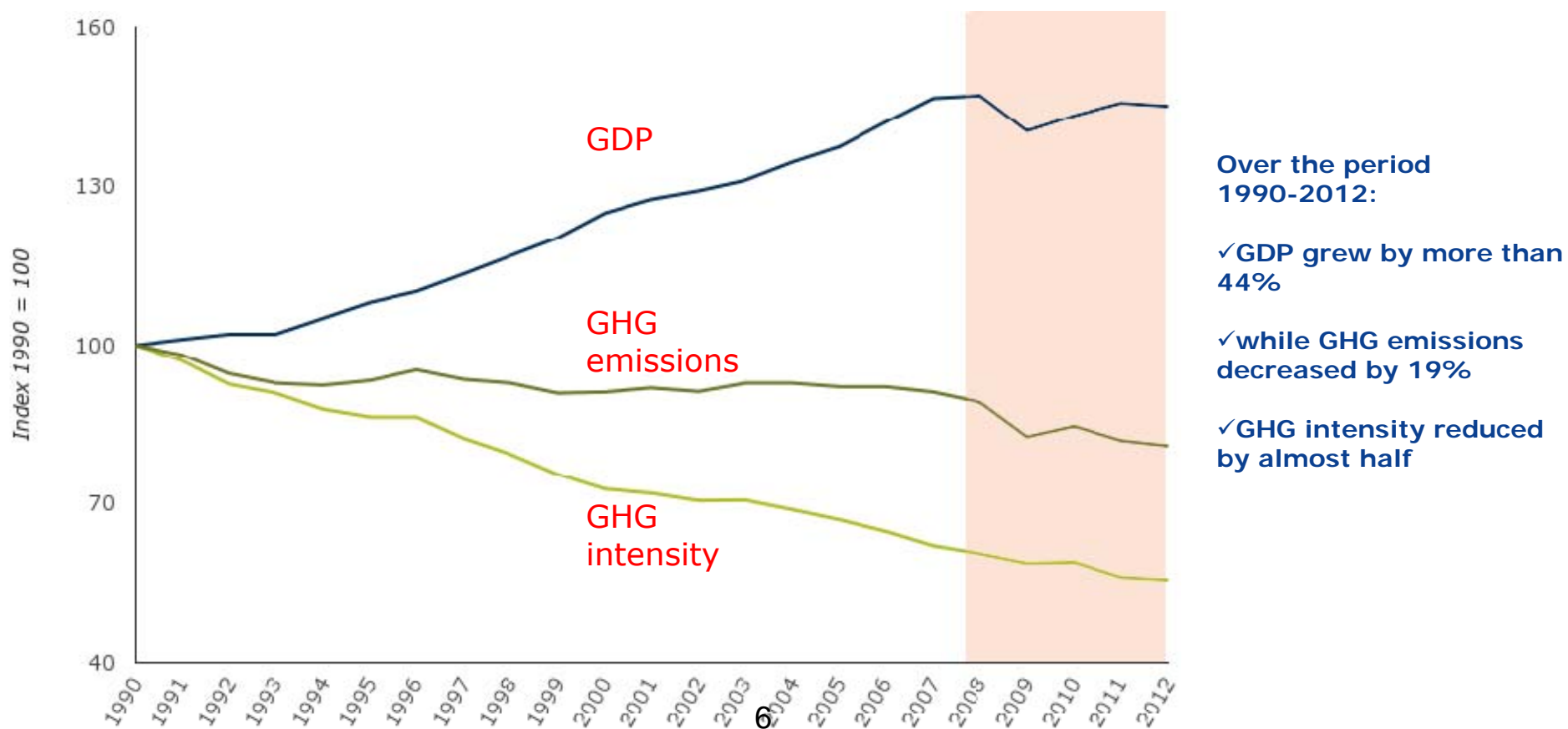


Functioning of the EU ETS: ensuring the environmental objective

- Cap-and-trade system:
 - ✓ Each allowance represents the right to emit one tonne of CO₂
 - ✓ Amount of allowances determines amount of emissions, i.e. emissions are "capped"
 - ✓ Allowances are distributed and can freely be traded on the market
 - ✓ Scarcity ("cap") and tradability of allowances determine price
- ✓ Cap determines and guarantees environmental outcome
- ✓ Market mechanism ensures that the objective (emission reduction) is achieved at least costs

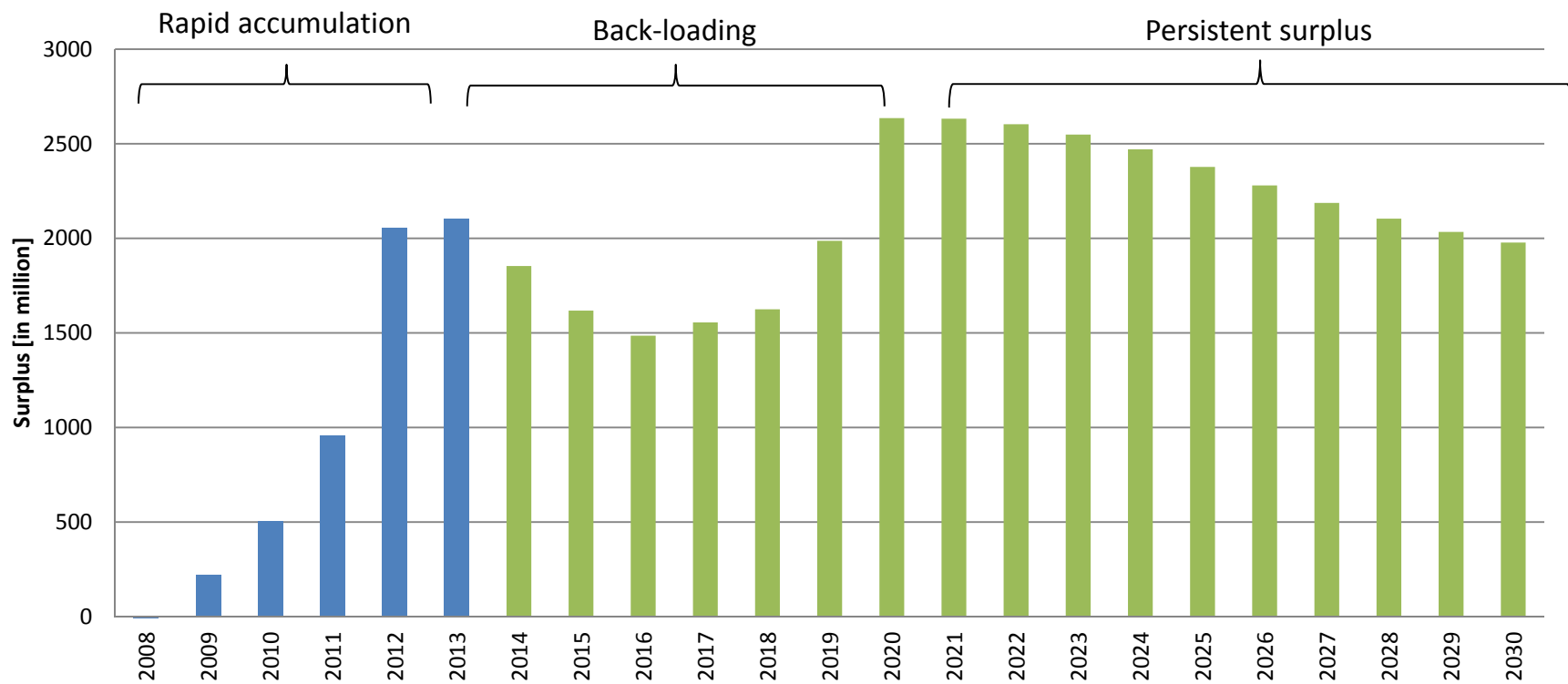


EU greenhouse gas emissions have reduced while GDP increased



Then came the double-dip recession – and the structural reform debate

- Large and persistent market imbalance
- Back-loading, i.e. postponing the auctioning of a number of allowances of March 2014: temporary measure



Blue columns are based on actual figures

Green columns are based on estimates

Structural reform of the EU ETS – Creating a Market Stability Reserve

- **Dual purpose**
 - address the current surplus
 - If not addressed, the imbalance would profoundly affect ability to meet the medium-term target in a cost-effective manner
 - make the ETS more resilient to possible future demand shocks
 - **More flexible auction supply through**
 - putting allowances in the reserve in case of too high surplus
 - releasing allowances from the reserve when allowances get scarce
- ➔ Carbon price will be more strongly driven by the mid- and long-term emission reductions



Agreed architecture of MSR

- MSR established in 2018 and operational as of January 2019
- Two block transfers:
 - 900 million backloaded allowances will be placed into the MSR in 2019/2020
 - Unallocated phase 3 allowances will also be put into the MSR in 2020
- Reserve works rule-based – no discretion / no new institutions
 - An indicator (total number of allowances in circulation) is calculated and published each year starting in 2017
 - if indicator \geq **833 million** allowances a volume of **12%** of the total number of allowances in circulation is put in MSR
 - if indicator \leq **400 million** allowances a volume corresponding to **100 million** allowances is released from MSR
- Allowances placed/released over 12 month period (Sept to Aug)
 - in 2019: additionally, between Jan and Aug **8%** put in MSR
- Regular review of the rules and thresholds



The EU ETS 2005-2015

- 10 years of EU ETS. Major improvements from 2013: e.g. EU wide cap and auctioning for power.
- Continuing emissions reductions, EU close to 2020 target. But: surplus of around 2 bio allowances.
- Back-loading followed by MSR reform agreed to address surplus. Reform efforts increasingly reflected in price signal.
- October 2014: European leaders agree on 2030 Climate and Energy framework, including 40% target (43% reduction for ETS sectors)



The European carbon market



Source: adapted from Bloomberg New Energy Finance (2015)

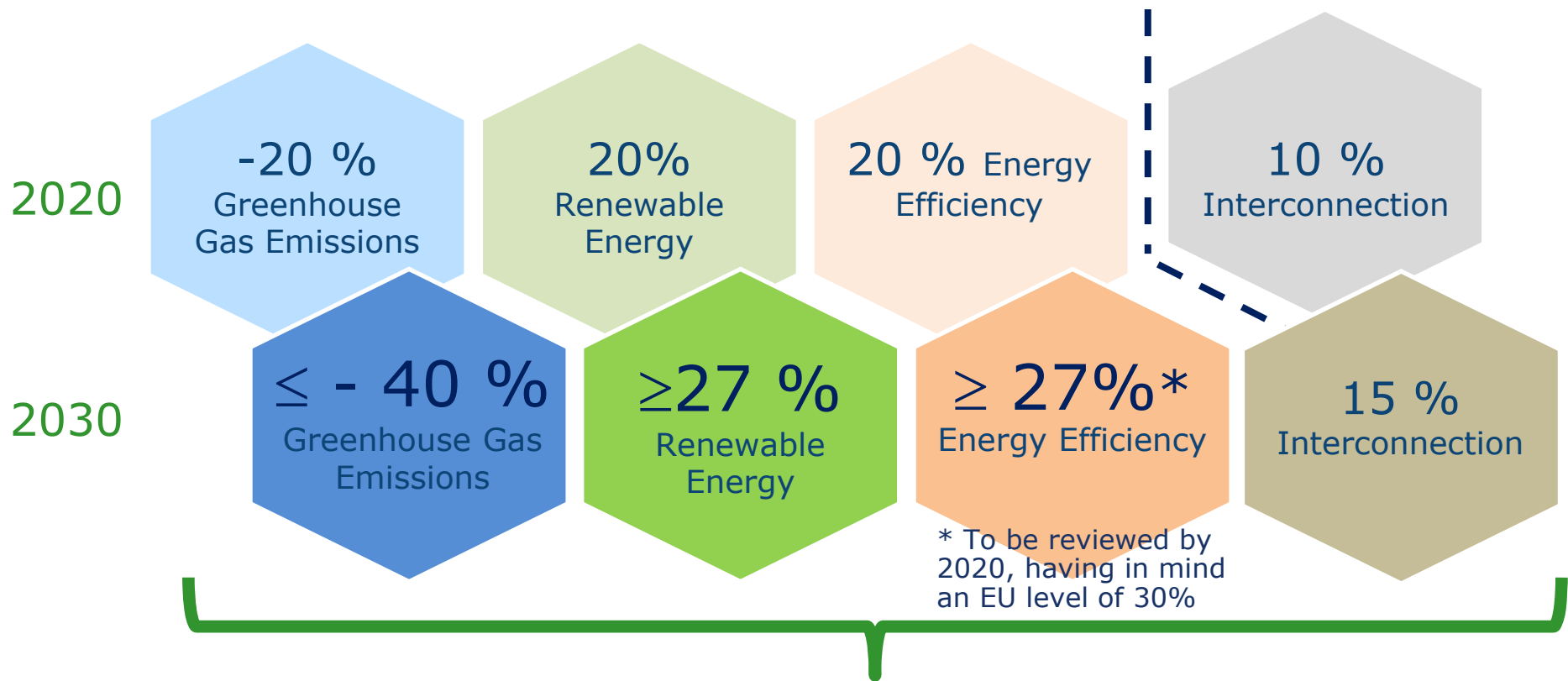


- 2013: start of EU ETS phase 3
- 2014: start of backloading, impact assessment 2030 package, legal proposal for Market Stability Reserve
- October 2014: European Council conclusions on 2030 Climate and Energy package
- 2015: proposal for ETS revision





Agreed headline targets 2030 Framework for Climate and Energy



New governance system + indicators



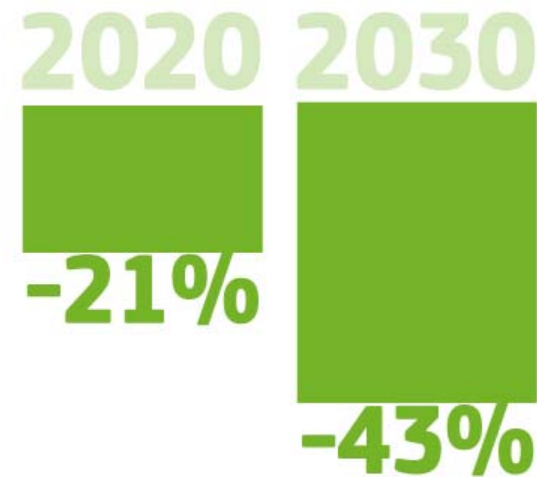
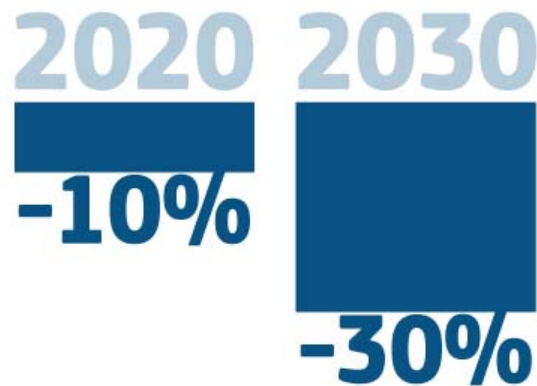
Revision of the EU ETS for phase 4





Domestic reductions in emissions from ETS and non-ETS sectors

EMISSION REDUCTIONS IN ETS AND NON-ETS COMPARED TO 2005

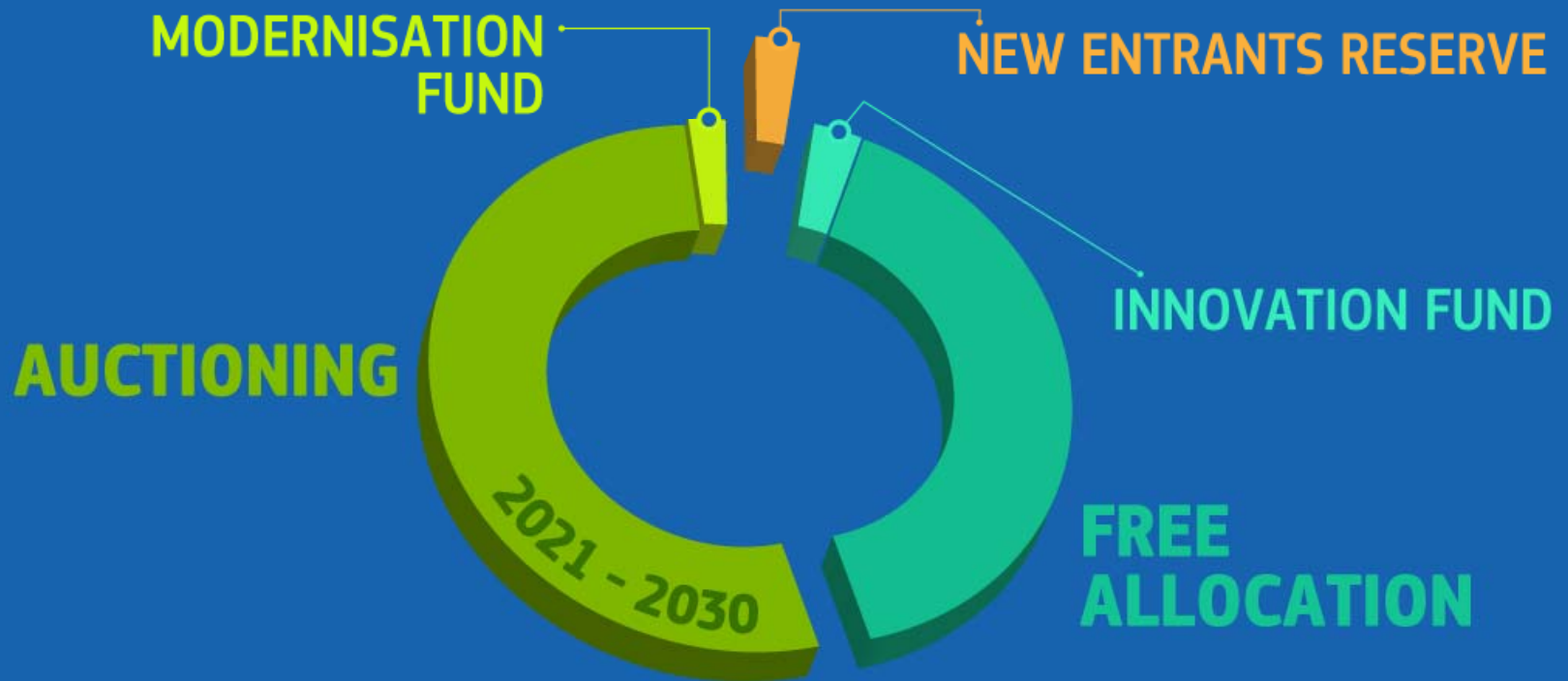


NON-ETS INCLUDING ROAD TRANSPORT, HOUSING, AGRICULTURE etc.

ETS INCLUDING POWER/ENERGY SECTOR & INDUSTRY

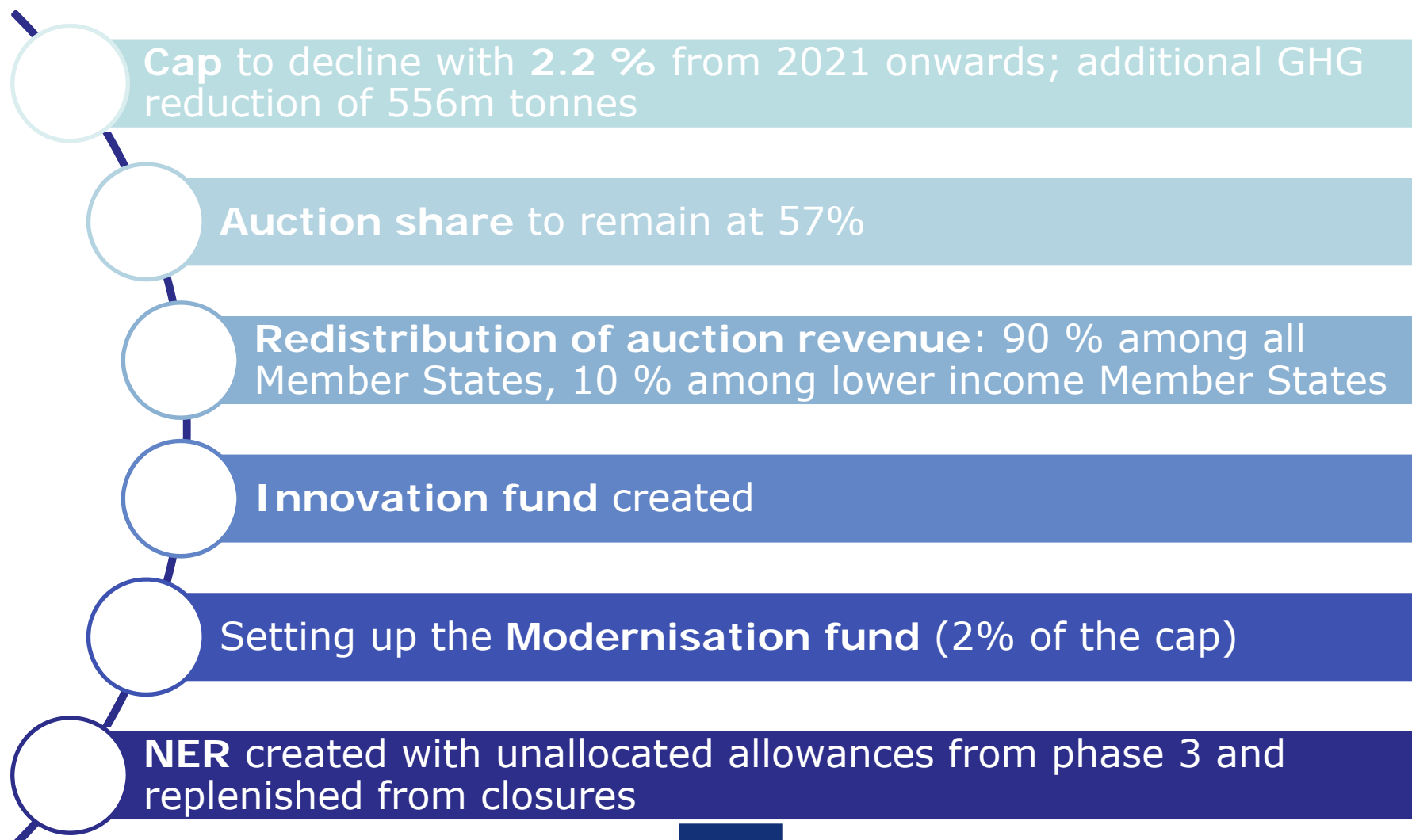


OVERALL ARCHITECTURE

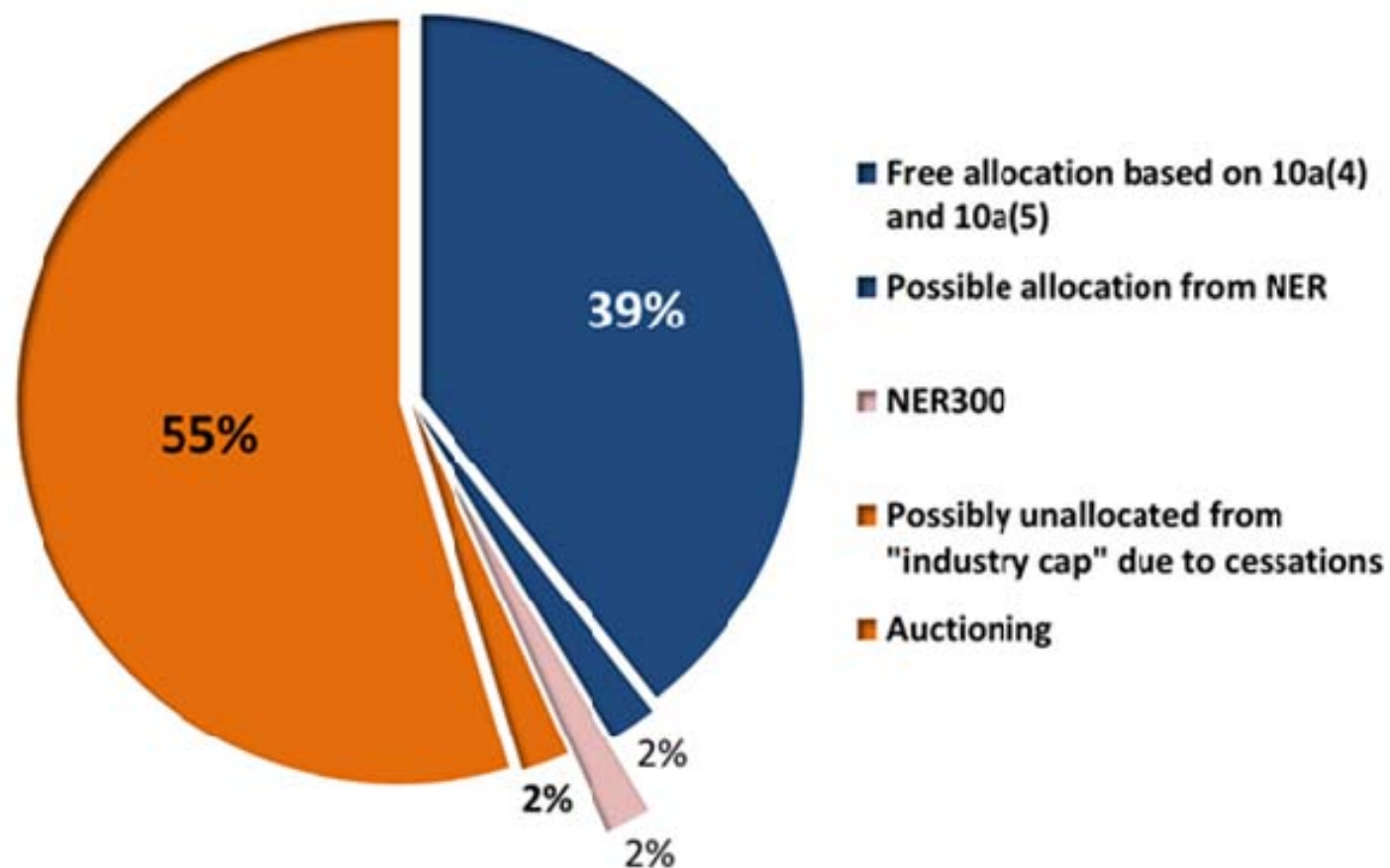




Overall architecture



Structure of total quantity in phase 3





Free allocation





MORE TARGETED FREE ALLOCATION



BENCHMARKS UPDATED TO
REFLECT TECHNOLOGICAL
PROGRESS



NEW ENTRANTS' RESERVE
MORE FLEXIBLE FOR NEW
& GROWING BUSINESSES

≈ **50**
sectors
on new carbon
leakage list



CLOSER ALIGNMENT
WITH PRODUCTION
DATA



COMPENSATING INDIRECT
COSTS TO ELECTRICITY
INTENSIVE INDUSTRIES



Free allocation

Benchmark updated twice based on a central flat-rate (1% per year since 2008)

The **real rate of improvement** will be verified based on real data with the possibility to adjustment to lower or higher flat-rate

Allocation decisions for 5 years to use more recent production data

NER to start with ~400m allowances for new installations and production increases; more flexible

Carbon leakage protection

2 carbon leakage groups: **High risk** – installations receive 100%* free allowances and **low risk** – installations receive 30%* (* at the level of the benchmark)

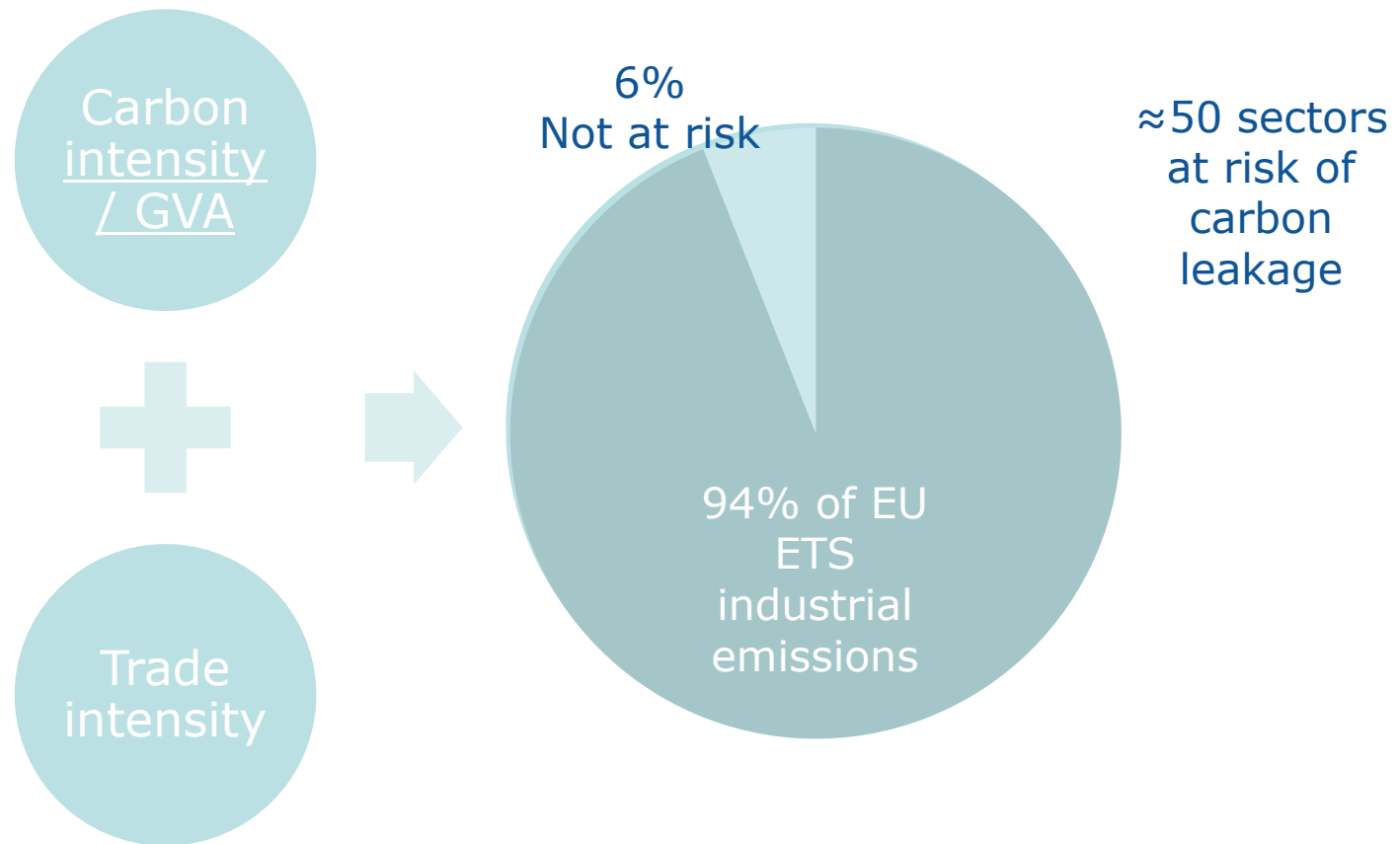
Approach based on existing criteria: trade intensity and emission intensity

Reclassifies some 100 trade-intensive sectors with very low emissions from high- to low-risk group (~3% of emissions)

Qualitative assessment of sectors for borderline cases possible

Increased stability as list valid for 10 years (2021-2030); to be adopted end 2019

Free allocation against carbon leakage – Phase 4



Indirect cost compensation

Currently: MS "may" compensate => divergent practices among MS

Compensation based on free allowances not feasible

Reinforce current approach based on State aid, MS to use auction revenues (*"Member States **should...**"*)

Increased transparency through reporting on the use of auction revenues



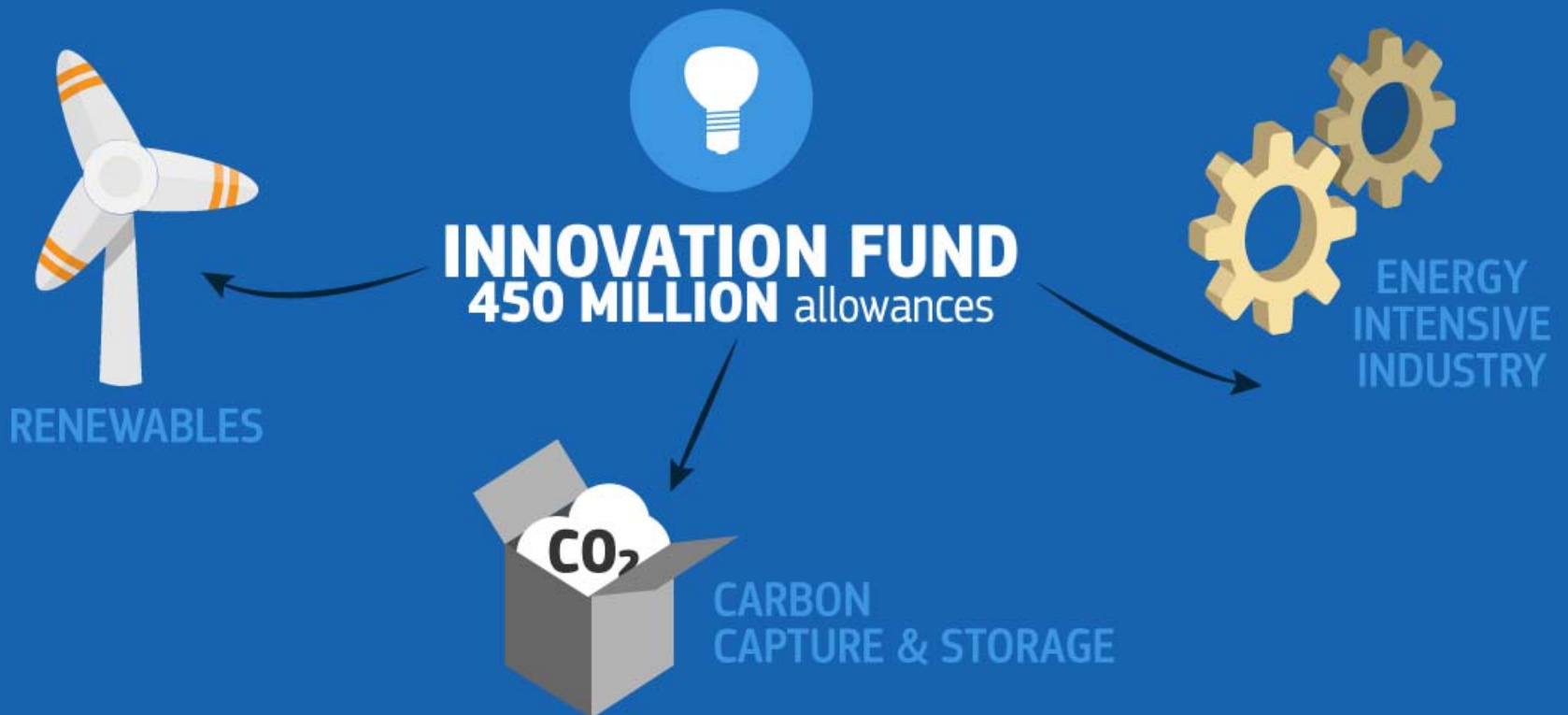
Low carbon funding mechanisms





MOVING AHEAD

TOWARDS A COMPETITIVE LOW-CARBON ECONOMY





Innovation fund

Support for low-carbon demonstration

400m allowances + 50m allowances from MSR, amount depending on carbon price

Building on existing NER300 program for carbon capture and storage and renewables

Extension of scope to low carbon innovation in industrial sectors

Increased **maximum funding rate** (60%) and possibility to receive funding when certain milestones are achieved



WORKING TOGETHER

SUPPORTING LOWER INCOME MEMBER STATES

EXISTING SOLIDARITY MECHANISM
OF AUCTION REVENUES



n€w

MODERNISATION FUND
310 MILLION allowances

10 Member States

Eligible for funding to modernise
their energy systems





Increased support for energy modernisation in lower income Member States

Continued preferential share of auction revenues (10% for solidarity)

Modernisation Fund to support investments into energy efficiency and modernise energy systems

Continued optional free allocation to power sector



Free allocation to the power sector

Continue existing provisions for lower income Member States

Limited quantity (up to 40% national auction budget)

Member States to set up a **competitive bidding process** for investments as of 10M€

Projects below EUR 10 million to be selected by MS based on clear and transparent criteria; list of investments by 30 June 2019

Increased transparency



General elements



NEW ELEMENTS ON AUCTIONING

MS AUCTION REVENUE FOR:



FINANCING CLIMATE ACTION IN
3RD COUNTRIES



AUCTIONS



PROMOTION OF
SKILLS FOR LOW
CARBON ECONOMY



COMPENSATION OF INDIRECT
CARBON COSTS TO ELECTRICITY
INTENSIVE SECTORS



Simplifications in proposal (1)

Validity of allowances – no banking operation needed

Combined data collection for benchmarks and activity levels – simpler data collection exercise

Stable carbon leakage list – more predictability





Simplifications in proposal (2)

Key parameters set in Directive – simpler and more predictable

Possibility to set simpler rules for small projects under low carbon funds

Renewed possibility for MS to opt-out small emitters, subject to equivalent measures.





Next steps

A decorative graphic consisting of a white circle with a light blue outline, partially overlapping a purple horizontal bar. Two dark blue curved lines extend from the top and bottom of the circle.

Legislative debate in the European Parliament and in Council





EU EMISSIONS TRADING SYSTEM

FOR CITIZENS, BUSINESS & THE CLIMATE

below **2°C** 

Paris
COP21



Reducing emissions by
at least
40%
EU wide

in **43%**
EU ETS

