



CAN Europe's Position on the ETS Reforms

CAN Europe GA

27 – 28 April 2016

Heading towards more 3°C warming!

The [Stern Review](#) on the Economics of Climate Change, published in 2006, predicts that a rise of 3°C would mean 550 million more people would be at risk of hunger, 170 million could suffer coastal flooding and nearly half the world's species could face extinction.

Impacts that different parts of Europe would experience in a 2C world, and it breaks those impacts down into different sectors - health, tourism, energy, agri, etc

<https://www.atlas.impact2c.eu/en/>

Paris is a call for action!

In the Paris Agreement all countries agreed to hold the temperature increase well below 2°C and furthermore to pursue efforts to limit it to 1.5°C.

Europe would have to reduce its emissions more than 95% below 1990 levels by 2050 to ensure a more than 50% chance to have no more than 1.5°C warming by 2100.

ETS target of 43% below 2005 emission levels would only lead to an 84% reduction in the ETS sectors by 2050.

- ETS targets have to be raised significantly to ensure the EU lives up to its commitments under the Paris agreement, including to pursue to keep temperature rise below 1.5°C.
- **The Commission proposal is weak and Member States show little appetite for substantial reforms.**
- **It will be up to the Parliament to make the ETS more fit for purpose!**

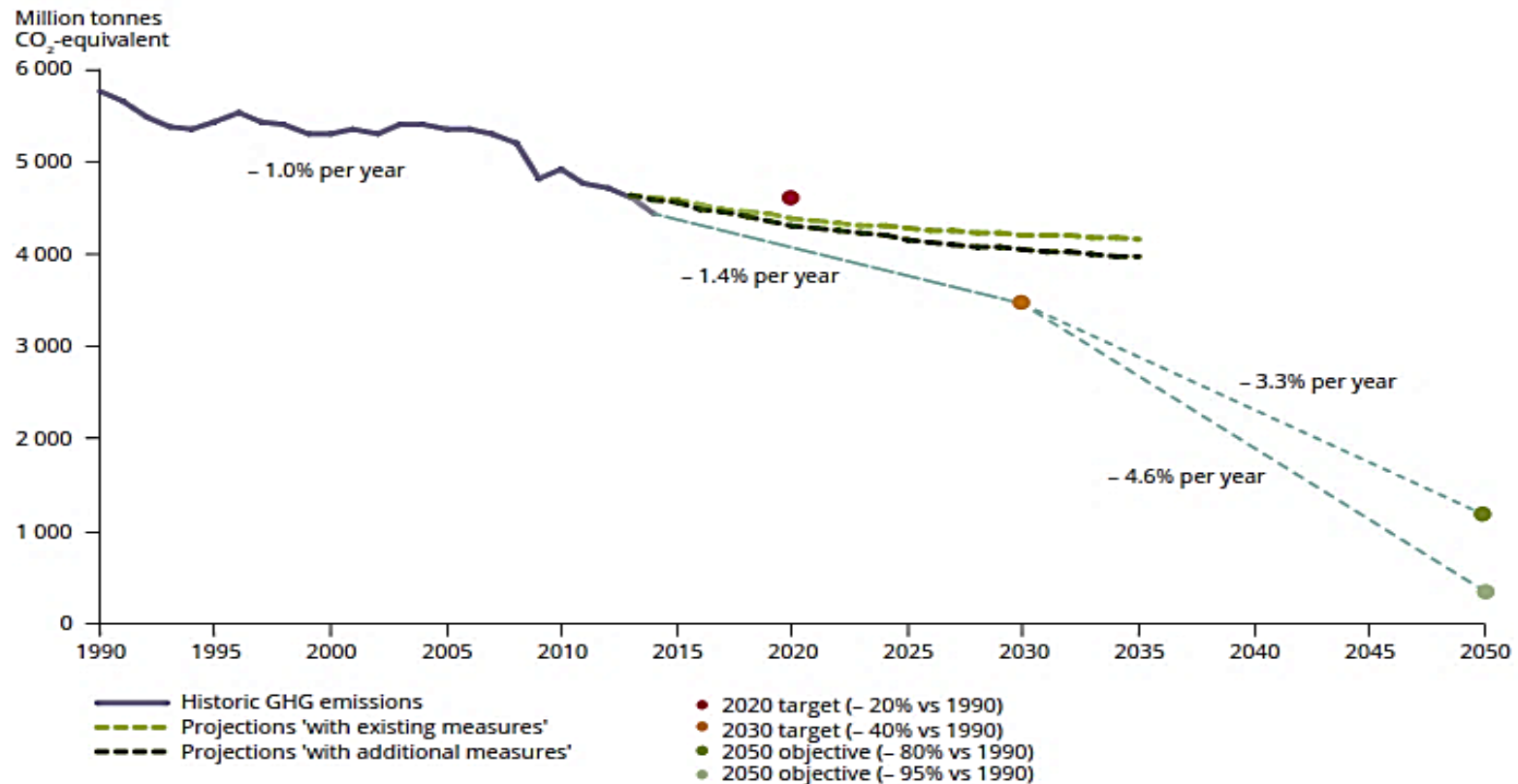
ETS reform timeline

ETS reform likely discussed together with the **Legislative proposals on the Effort-Sharing Decision and LULUCF**. Commission will publish them together in one proposal, expected **end of June 2016**.

Likely timeline:

- October 13th 2016: European Parliament ITRE vote
- December 8th 2016: European Parliament ENVI vote
- February 2017: European Parliament ETS plenary vote, followed by trioalogue
- Second half of 2017 or 2018: finalizing ESD, ETS and LULUCF legislation
→ *important to finalize well ahead of Paris review in 2018 to enable EU to raise target.*
- Presidencies:
 - 2016: Netherlands, Slovakia
 - 2017: Malta, United Kingdom
 - 2018: Estonia, Bulgaria

EU greenhouse gas emission trends, projections and reduction targets



ETS is failing to deliver

A weak reduction target, the massive use of international offsets, and inflexible policy design have led – together with the economic recession

→ gigantic oversupply of allowances

→ price drop

→ no signal to lower emissions

The Market Stability Reserve (MSR) is an important but insufficient first step to improve the ETS. The surplus is only temporarily removed and models predict that the market will be oversupplied until 2025 or later.

CAN Europe ETS Reform Position

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Download the full position [here](#)

1. Making the ETS fit for purpose

- 1.1 Starting point for 2021 at actual emission levels
- 1.2 Permanent cancellation of allowances
- 1.3 Raising Linear Reduction Factor
- 1.4 Raise Target Every Five Years
- 1.5 No use of International offsets, ETS linking only under certain conditions

Starting point for 2021 at actual emission levels

The starting point for 2021 should be at actual emissions and not at the current minus 21% ETS target for 2020.

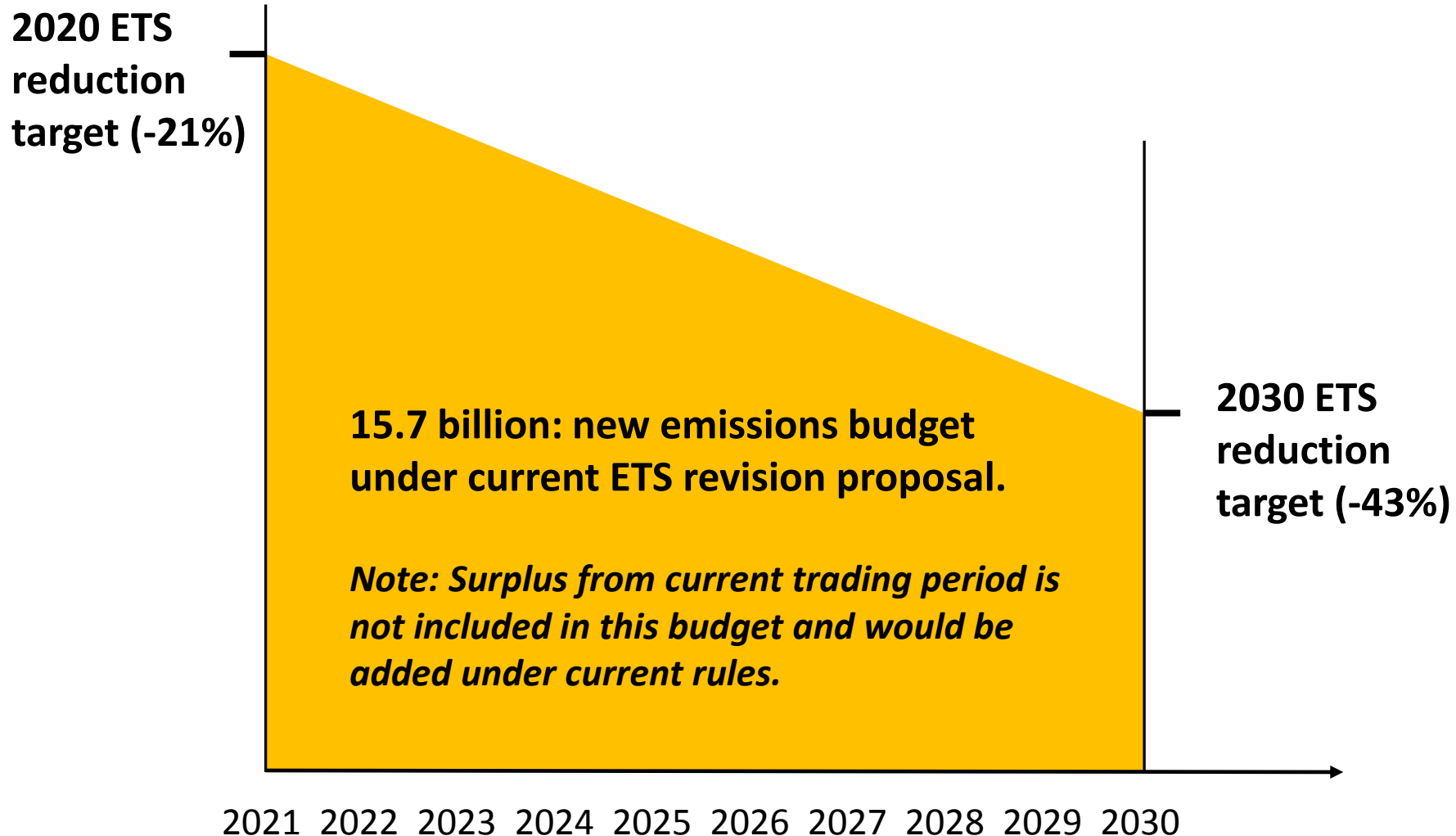
If the emissions will be, as projected, at minus 38% in the ETS sectors by 2020 starting at actual emission levels would significantly reduce total emissions under the ETS.

Please note that this measure would not eliminate the surplus from phase 3!

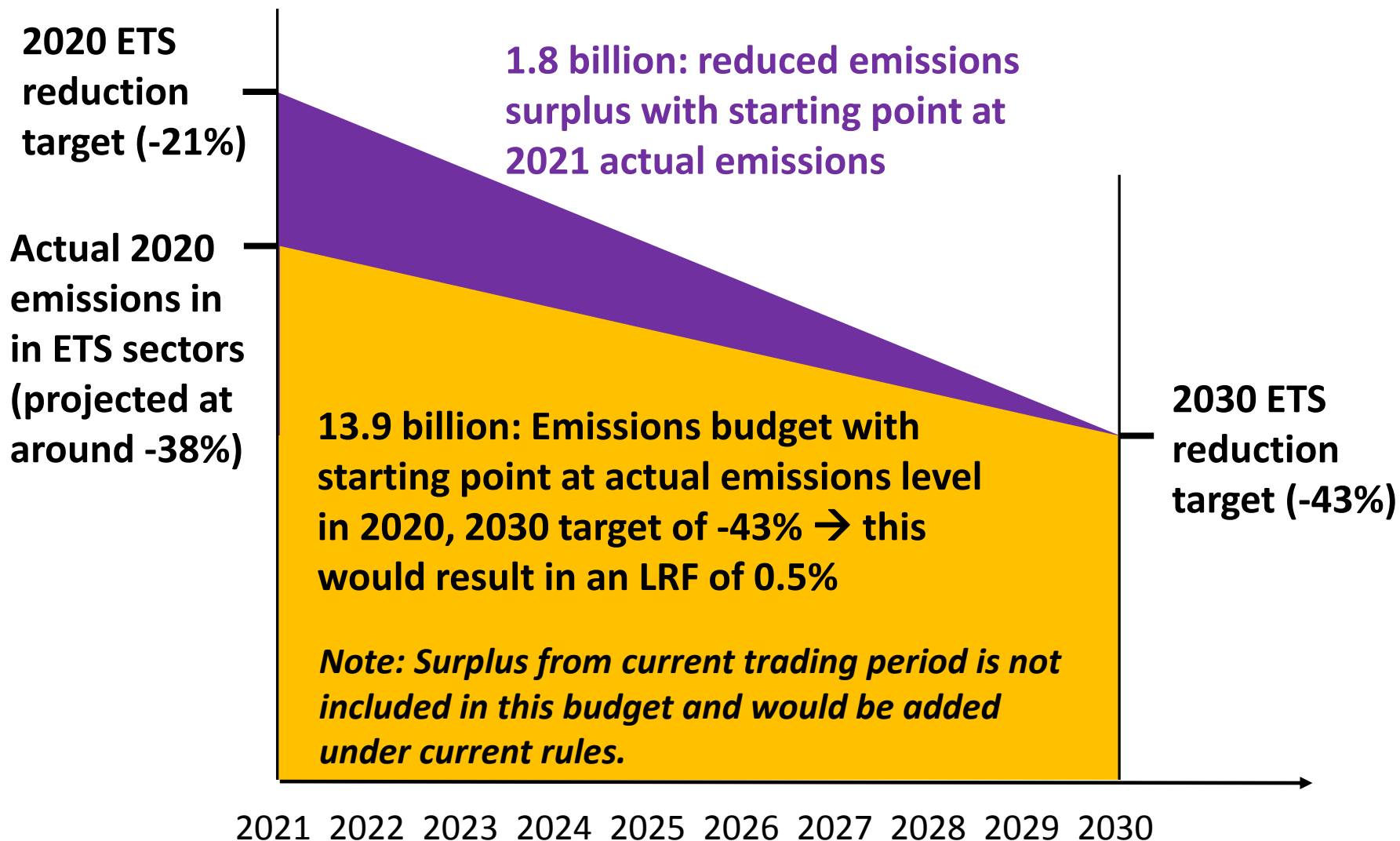
CAN EUROPE CALLS FOR

The starting point for 2021 to be at actual emissions and not at the ETS target for 2020 (21% below 2005 emissions).

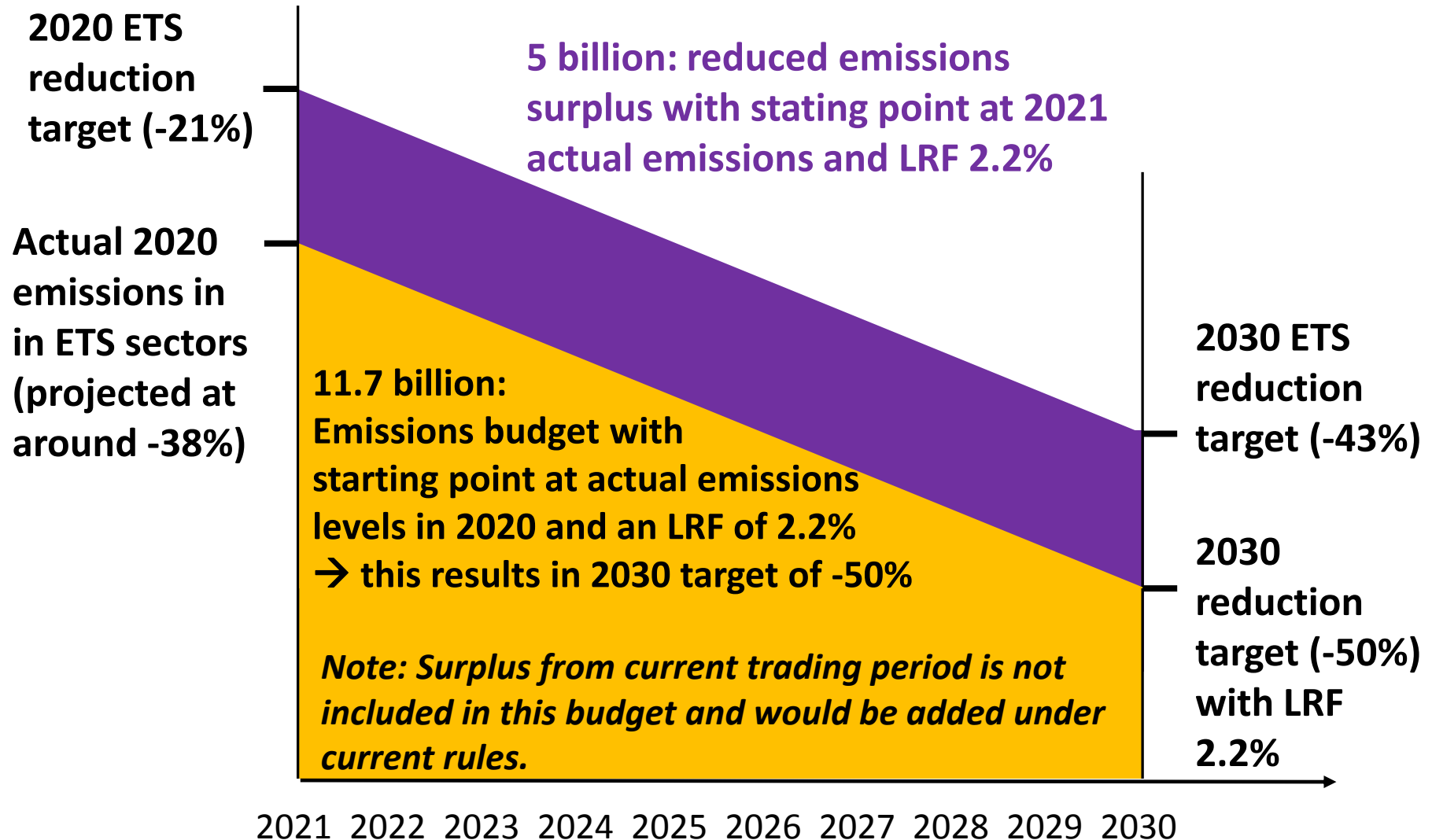
Starting Point: Currently proposed emissions budget



Emissions budget: starting at actual emission levels



Emissions budget: starting at actual emission levels with Linear Reduction Factor at 2.2%



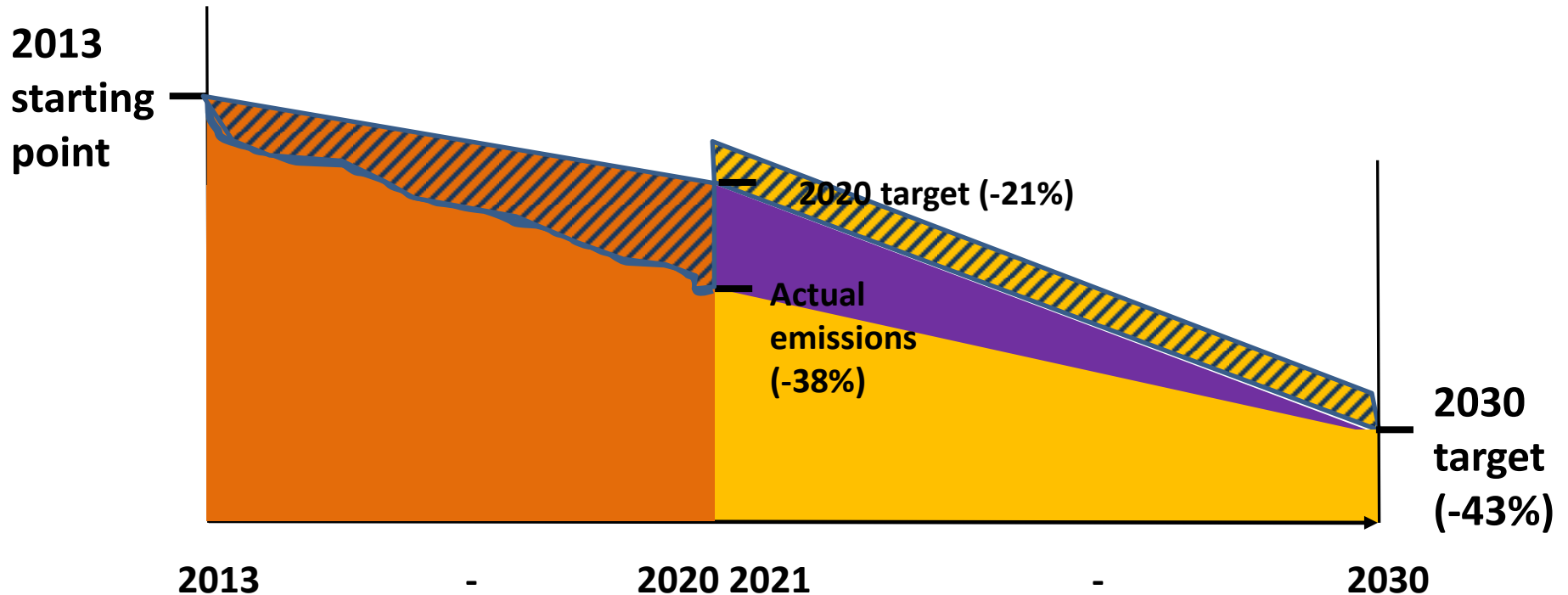
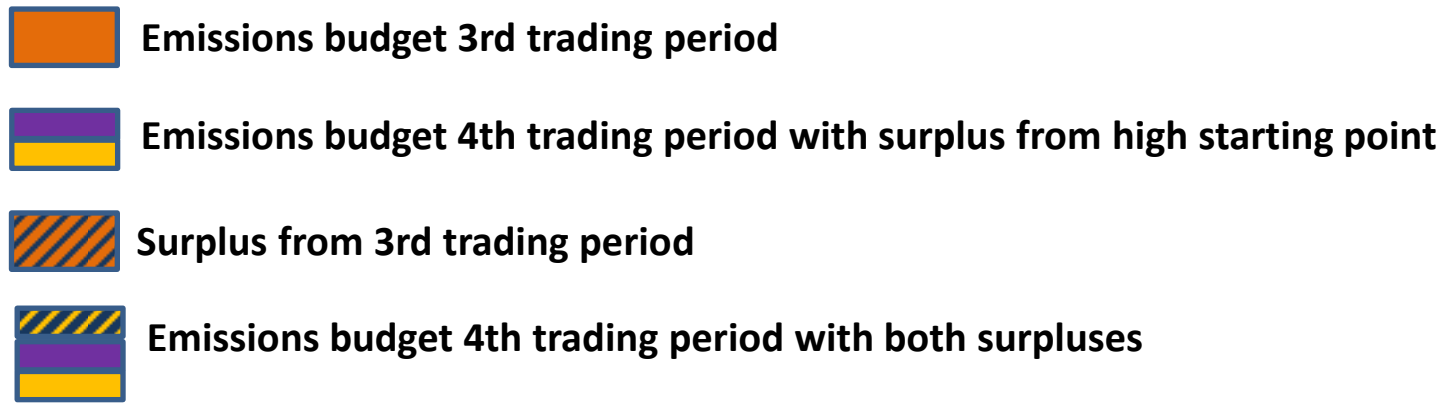
Permanent cancellation of allowances

By 2020 the ETS surplus will have grown to between 2.6 and 4.4 billion allowances.

The billions of surplus pollution permits that will have accumulated by 2020 can, under current rules, be fully carried over to the next trading period.

Scenario	Emissions budget 2021-2030 without estimated 4.4 billion surplus from phase 3	Emissions budget 2021-2030 with estimated 4.4 billion surplus from phase 3
Current proposal (start at 2020 target: -21%), LRF 2.2%	15.7 billion	20.1 billion
Actual emissions in 2021 (-38%), LRF 0.5%	13.9 billion	18.3 billion
Actual emissions in 2021 (-38%), LRF 2.2%	11.7 billion	16.1 billion

The two Big ETS surpluses: 1) starting point 2) carry over



Permanent cancellation of allowances

CAN EUROPE CALLS FOR THE FOLLOWING MEASURES WHICH SHOULD BE COMBINED WITH EACH OTHER:

- **The permanent cancellation at the end of 2020 of around two billion surplus allowances that will have accumulated in the MSR by that point.**
- **A limit on the number of allowances that can be stored in the Market Stability Reserve (MSR).** To avoid a large accumulation of allowances in the MSR should hold a maximum of allowances equal to 50% of the total ETS allowances made available in a given year. Allowances in the MSR above this ceiling should be automatically cancelled.
- **A limit on the validity of allowances in the MSR.** Allowances that remain in the MSR for more than five years should be cancelled permanently. This provision would also ensure that the MSR does not grow to be very large.
- **Allowing the unilateral cancellation of allowances by Member States.** If individual Member States choose a higher mitigation target or other measures that raise their mitigation levels, they should be able to cancel allowances that would enable them to unilaterally raise the stringency of their target without just making it easier for other Member States to reach the overall EU target.
- **Allowances that remain in the new entrants reserve at the end of each trading period should be cancelled.** A second best option would be to put them into the MSR. The phase 4 new entrants reserve should therefore only be filled with allowances from phase 4.

Raising Linear Reduction Factor

The Linear Reduction Factor (LRF) determines by how much the number of available allowances are reduced every year.

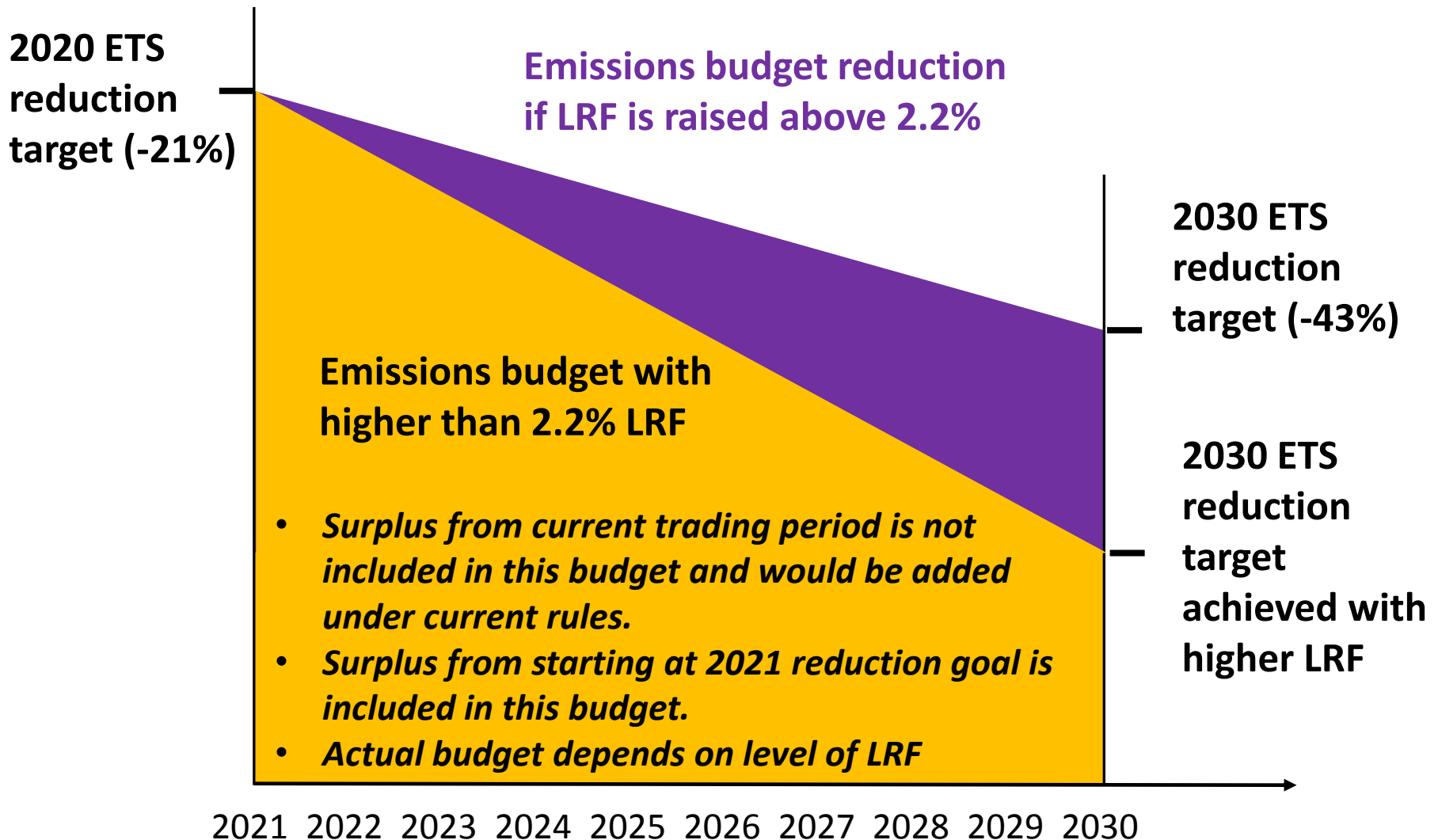
The proposed LRF of 2.2% would lead to ETS reductions by 2050 of only 84% compared to 2005.

Raising the linear reduction factor has a slower but longer term effect and is also an important option, especially in combination with the first two, to ensure the ETS is turned into a functioning mitigation instrument.

CAN EUROPE CALLS FOR

- **A Linear Reduction Factor which leads to a cost effective greenhouse gas reduction of at least 95% until 2050. The linear reduction factor (LRF) should be raised well above the 2.2% currently suggested. A sharper increase of the LRF will be crucial to the further credibility of the system as it sends a long-term signal for the decarbonisation of the economy.**

Illustrative graph to show effect of raising Linear Reduction Factor



Raising the Target Every 5 Years

The current ETS proposal is to have a ten-year trading period. This is longer than any ETS trading periods so far. Such a long trading period can lead to inflexibilities and make it difficult to improve the ETS during that period.

The Paris Agreement includes the requirement for all countries to come up with contributions to reduce emissions every five years.

CAN EUROPE CALLS FOR

- **Increasing ETS targets every five years.** ETS trading periods should also be five years. The ETS Directive should in any case include a revision clause that requires the European Commission to upwardly increase the ETS target every five years until the ETS is in line with **a linear pathway that will ensure the EU lives up to its commitments under the Paris agreement, including to pursue to keep temperature rise below 1.5°C.**

No use of International offsets, ETS linking only under certain conditions

CAN EUROPE CALLS FOR

- **International offsets not to be used for the ETS target.** International offsets means fewer reductions in the ETS. The quality of Clean Development Mechanism and Joint Implementation offsets have shown to be low. The use of low quality offsets leads to a rise in global emissions. In order to protect the integrity of European mitigation targets, international offsets should not be eligible for compliance.
- **Any linking would need to ensure that the EU's domestic target will still be met.** If the EU links to other ETSs, it could become a net buyer or net seller of units, depending on the ambition of the target and abatement costs in both schemes. If the EU would become a net buyer, it would no longer meet its domestic target. This could be addressed by e.g. only allowing one-way linking (only allowing transfers of EU allowances from the EU to abroad but not vice versa) or raising the ambition of the ETS target **and** putting a quantitative limit on the amount of units that can be imported in the EU to ensure that the domestic target is still met.

2. Ensuring rapid mitigation action

The higher the carbon price the more incentive companies have to implement low carbon strategies. If the carbon price rises sooner, companies will act sooner, even if there is no change in the overall ambition (e.g. if the 2030 targets remain the same). Earlier action can prevent lock-in of carbon intensive installations and technologies.

- 2.1 Unused Allowances should not be used for New Entrants
- 2.2 Supporting policies and measures at national level
- 2.3 Maximize Auctioning of Allowances

→ For more details, see our position paper

Maximize Auctioning of Allowances

- If companies have to purchase all their allowances, emitting greenhouse gas becomes more expensive and cleaner production becomes more cost-effective.
- This is one of the reasons why CAN Europe is in favour of rapidly moving to 100% auctioning of allowances.
- An increase in ETS auction revenues will allow national treasuries to increase funding for climate action programmes at home and abroad.

→ Industry handouts & windfall profits have to stop

3. Industry handouts & windfall profits have to stop

Auctioning is the most cost-efficient, simplest, fairest, and most transparent way to allocate allowances, fully reflecting the polluter-pays principle. Increasing the share of auctioning can support larger investments in the tools needed for further decarbonisation and climate resilience, in the EU and internationally.

- 3.1 Phase out free pollution permits, move to 100% auctioning
- 3.2 Avoiding windfall profits
- 3.3 Ensure meaningful benchmarks
- 3.4 Limit the hand-out of free pollution permits to those really at risk
- 3.5 No indirect costs compensation

→ For more details, see our position paper

4. Funding Climate Action

- 4.1 Innovation fund (formally NER 300)
- 4.2 Modernization fund
- 4.3 Article 10c
- 4.4 Auctioning revenues for EU & international climate action
- 4.5 Establish International Climate Action Fund
- 4.6 Establish a Just Transition Fund

Principles for all funds

- Only emissions reductions of at least 95% or higher by 2050 can ensure some chances of staying below 1.5°C warming: Therefore to be eligible for funding Member States must ensure full transposition of all relevant EU legislation;
- No financial support shall be given to fossil fuel based or nuclear energy production;
- All financial support shall give priority to investments for energy savings and sustainable renewable energy technologies;
- Only sustainable bio-energy projects shall be eligible for funding;
- Ensure „energy efficiency first“ principle;
- Priority shall be given to projects that promote co-benefits;
- Full transparency shall be ensured;
- Public consultations shall be set up before decisions are made.

→ **For full set of principles and more details, see our position paper**

CAN Europe ETS Reform Position

5. Ensuring ETS incentivizes only sustainable bioenergy use
6. Addressing emissions from Aviation and Shipping
7. Ensuring road transport reduces emission outside of the ETS

→ For more details, see our position paper

Final words

- **Absent reforms that go well beyond what the European Commission is proposing, companies can delay or cancel investments in cleaner and more efficient production.** This risks a lock-in of carbon intensive infrastructure for years to come, making Europe's climate goal more time-consuming and costly to achieve.
- **The ETS can at best support achieving the necessary long-term decarbonisation.** A price signal is important. But a price signal alone, even if it was considerably higher, will not be sufficient to facilitate transformational change.
- **Even if the reforms were to be bold and swift we will need other strong policies, such as for renewable energy and energy efficiency, and binding bioenergy sustainability criteria** that accurately account for emissions from biomass.



Thank you for your attention
For questions, please contact:

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