The EU Emissions Trading System (ETS)

Rationale and Lessons learnt

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Building a global carbon market

- The carbon market: cost-effective and flexible mitigation tool **and** source of finance for low-GHG technology development
- EU's aim: progressive development towards global carbon market
- Countries take part according to responsibilities and capabilities
- Backed by ambitious mitigation commitments in line with 2 degree objective
- Build on existing mechanisms, link schemes and develop new mechanisms

Role of domestic emissions trading systems

- Directly engage private sector
- The EU has gained experience in setting up the world's largest company-based emissions trading scheme EU ETS
- Linking emissions trading schemes across the world could help build the global carbon market
- Key = creating scarcity of tradable units
- Other key requirements: transparency, liquidity, long-term predictability and integrity (monitoring, verification and compliance)

Why EU ETS?

- Market-based instrument which allows for most cost-effective and targeted environmental policy- no market intervention!
- EU ETS is driver for carbon market: valued at around €40 billion globally (EU ETS: €28 billion) in 2007
- Cornerstone of Europe's strategy to implement Kyoto Protocol - major structural element for the post-2012 climate strategy
- EU ETS will contribute to reaching more than 40% of the EU15's Kyoto commitment 2008-2012 (i.e. 3.4%pts of -8% below 1990)!

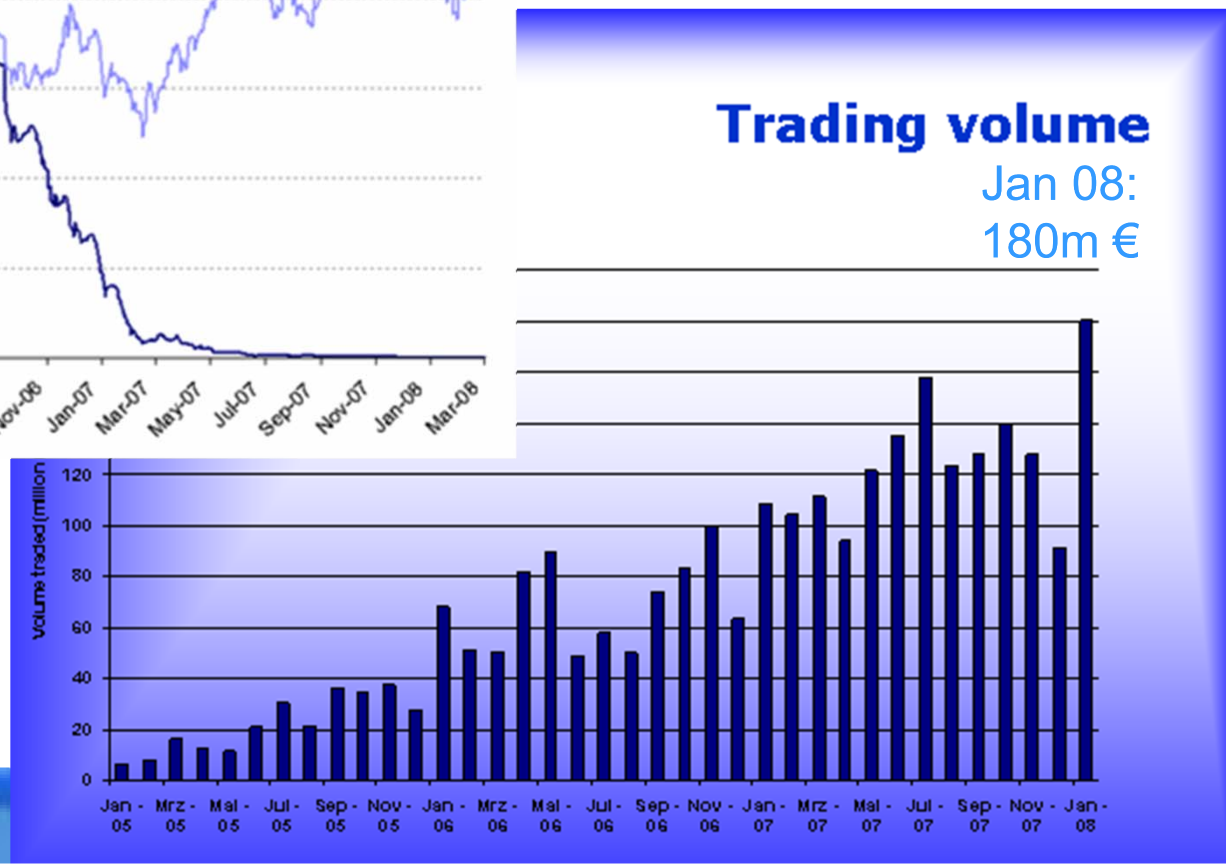
Staged introduction of the EU ETS

- 1st trading period
  - Designed as a learning by doing phase
  - Successful set up of necessary infrastructure
  - Growing trade of allowances across Europe
  - Thanks to experience gathered in 1st trading period, companies and authorities are much better prepared
- 2nd trading period
  - Commission assessment of allocation plans ensured stringent cap and equal treatment of Member States
  - On the basis of all plans, the approved cap is 6.5% below the 2005 verified emissions for the ETS sector
  - The EU ETS will be successfully reducing emissions in the trading sector
- 3rd trading period aimed at reductions needed by 2020 (20-30%)

Lessons learnt from EU ETS

- Get stakeholders involved early when setting up ETS
- Start with short pilot phase – also to avoid locking into over-allocation
- Emissions trading needs stringent cap with scarcity – no oversupply
- Need to have robust data to start with!
- Keep emissions trading simple:
  - Need for strong regulator to ensure environmental integrity
  - Central cap setting, no more national allocation plans
  - Auction large share of allowances is fairest allocation method, ensure due auctioning process
  - Use revenues from auctioning for financing fight against climate change
  - Ensure further harmonisation of monitoring, reporting and verification,
  - Maximise transparency and legal certainty – no ex-post regulatory intervention
- Keep use of offsets (CDM/JI) in balance to drive investments in low carbon technologies at home

Prices and trade volume in the EU ETS



Review of the EU ETS: enhancing financial flows

- EU Commission **proposes** auctioning as the principle allocation method and that Member States should use 20% of auctioning revenues for mitigation and adaptation, inter alia:
  - GHG reduction schemes, including GEEREF
  - Adaptation to CC impacts, including in developing countries
  - R&D for emission reduction (e.g. RE and CCS) and for adaptation
  - Measures to reduce emissions from deforestation
  - Commission analysis of the proposal estimates that revenues in the EU alone could increase to about 75bn€ annually by 2020 with 100% auctioning (at a price of 40€ per ton CO_2), even part of this is potentially a large source of funding
- Similar use envisaged for auctioning revenues from aviation under the ETS, here: 100% of revenues

Conclusions

- Europe has turned the concept of market-based climate policy into reality and a continent-wide carbon price signal has emerged that has a bearing on investments not only in the EU.
- The EU ETS in its current shape is the first step in an evolution to a global carbon market. The ETS provides for valuable lessons learnt – also for other schemes worldwide.
- The EU ETS will be even stronger and more effective in its current (2008-2012) and third phase (up to 2020). It can be a significant source of financial flows.
- The EU ETS is a key cornerstone of the broader EU approach to energy security, innovation, international competitiveness and its resolve to move towards a low-carbon economy.

Thank you!