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POSITION PAPER

An enhanced EU ETS – robust, predictable, recession-proof and capable to help strengthening EU economy

Since 2005 the European Emission Trading Systems (EU ETS) has been the central EU instrument to combat climate change and to drive the process of establishing a global approach for a real international climate change policy with a global carbon market at its centre.

Discussions are currently ongoing among stakeholders and policy makers on whether the scheme is working properly. The discussion is focused on a carbon price that is lower than expected. However the carbon price results from supply and demand being impacted by financial crises and support schemes for renewables that have led to additional CO₂ emission reduction. The clear statement on the current development is that the EU ETS will deliver the fixed emission cap in Europe. Proposed policy interventions would only aggravate the existing flaws of the scheme resulting in:

1. A distinguishable increase of global emissions due to carbon leakage in form of reduced production and emissions imported through imported goods not produced in the EU.
2. The achievement of the cap is not reached in the most cost-efficient way, due to a mix of instruments interfering with each other and with the system.
3. ETS is not perceived as a well functioning market system by the rest of the world because of
 - a. political arbitrary intervention.
 - b. loss of industrial growth within the EU.

IFIEC is against set-aside, because

1. it does not address but even increases the huge barriers and risks for industrial activity and growth in the European Union.
2. this would be a damaging political arbitrary measure¹ because of loss of trust in the carbon market,
3. it does not address the root cause of the low price (the poor system design and interferences of other policies).

Therefore, IFIEC Europe representing the European industrial energy consumers aims to enhance the current debate on the future of the EU ETS by making proposals to overcome the above mentioned concerns. **IFIEC suggests key improvements**, which aim at bringing in line the two central EU strategies:

1. To be the driver in combating climate change, not only in Europe but globally.
2. To strengthen its economic basis by enabling efficient economic activity and growth.

For that purpose it is absolutely crucial **to design EU ETS in a way that brings stable and long-term rules for preventing carbon leakage until we have a functioning global system with rules allowing or even incentivising growth and rewarding efficiency.**

The following changes to the current system are needed:

¹ What would be the next interference, what set-aside volume would be selected, what if the economy returns to a prosperous growth scenario.

1. Allocation must reflect the **actual rather than a historic production** level of installations in order
 - a. to avoid both over- (in times of crisis and recession) and under-allocation (in case of growth).
 - b. to avoid a highly complex and error-prone set of rules to cope with any dynamics between history and reality.
 - c. to mitigate limitations for growth.
2. Benchmarks have to be challenging but also must give **necessary time to adapt / invest**. Benchmarks in EU ETS 3rd trading period are set at a very challenging level (average of the top 10 % performers). This means, by achieving those results the 2020 target would be overachieved. It is misguided and overambitious though, to take this “target benchmark” already as the starting point in 2013. Benchmarks can in no means represent technological and economical impossible targets and must also be realistic after 2020.
3. The **new entrant reserve (NER) must be replenished**, if depleted, also after 2020:
 - a. Emitters must have certainty on the future allocation for any new investments.
 - b. No replenishment would shift investments to outside Europe which does not contribute to combating climate change. It actually does the contrary.
4. The unstable financial compensation for indirect emissions must be changed into a **long-term predictable system with indirect allocation** as a better option².
5. A review of the carbon leakage list should not jeopardise the carbon leakage status of the energy intensive sectors currently on the list. The carbon leakage assessment in the EU ETS Directive should be complemented with a comparison of the direct and indirect carbon costs for industry in the EU versus the rest of the world. Therefore the **category “exposed to the risk of carbon leakage” should be applied to all industrial sectors** until a global auctioning system is established. This would eliminate the risk of a carbon leakage exposure factor for all sectors:
 - a. By giving industry regulatory certainty to facilitate long term planning.
 - b. To avoid basing on unreliable statistical data.
 - c. Auctioning is fine, but only if and when auctioning is taking place globally.
6. **The linear factor** for new entrants and heat users receiving heat from co-generation being electricity generators **and the cross-sectoral correction factor** for incumbents **should be abandoned**.
 - a. To establish equal treatment between all industry incumbents and new entrants.
 - b. Any change in the allocation to industry shall be adjusted by the NER and if needed by adjustment of the auctioning volumes of the Member States.

It is vitally important that there will come a global ETS by around 2020. In absence of a realistic perspective for an effective global agreement by 2020 the principle of **the EU cap must be revisited before 2020**. Without global participation further adjustments will be needed to keep Europe’s industry competitive on the global market place.

The above mentioned suggestions for improvement are needed anyway, also in case of a global ETS. They will turn the EU ETS into a more robust, predictable, effective and recession-proof carbon trading scheme.

IFIEC Europe represents energy intensive industrial consumers where energy is a major component of operating costs and directly affects competitiveness.

² Thereby the system for indirect allocations must safeguard:

- a) Without reduction factors and restrictions on sectors or sub-sectors.
- b) It should be based on the CO₂ emission of the marginal power plant.