The evolution and consequences of the EU Emissions Trading System (EU ETS)

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Introduction

- What is the EU ETS?
- How did the EU ETS evolve?
- What are the consequences so far?

– The way that the EU ETS evolved has had significant consequences for how well the system has performed in practice

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What is the EU ETS?

- Grand policy experiment as the first and biggest international emissions trading system in the world
- Applies to 27 EU member states, covers 11,500 installations representing close to half of Europe’s CO₂ emissions
- Cap and trade system
- Proposed in 2001, adopted in 2003 and operational from 2005
  - Phase 1: 2005-2007
  - Phase 2: 2008-2012
- Revised system proposed for Phase 3: 2013-2020

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What is the EU ETS?

- Cornerstone of a climate package on how to reach the EU 20+20+20 targets

- Cut greenhouse gas emissions by 20% by 2020 (or 30% if adequate international agreement)

- Improve energy efficiency by 20% by 2020

- Secure 20% of Europe’s energy from renewable sources by 2020

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Evolution of the EU ETS

- Starting point: The EU was highly sceptical to emissions trading in Kyoto 1997
- EU turnabout on emissions trading starts in 1998, due to:
  - The Kyoto Protocol
  - Lack of climate policy instruments
  - Change of personnel in European Commission
- The Commission took the initiative to the EU ETS, built up knowledge and crafted support among stakeholders:
  - member states, industry and green organizations

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Evolution of the EU ETS

- Turning point: The US exit from the Kyoto Protocol in March 2001
  - The EU starts a diplomatic rescue operation for saving the Kyoto Protocol
    - The EU ETS became the tool for showing the world that the EU did more than talk regarding climate policy
  - But time was short:
    - Demonstrable progress by 2005 and compliance 2008-2012
- The price paid for adopting the system in time was that most significant interests got what they wanted

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Evolution of the EU ETS

- The member states got significant autonomy: Caps could be determined individually through 27 National Allocation Plans (NAPs)
  - Decentralized system: No common EU cap for the 2005-2007 phase

- Industry got allowances for free
  - Chemical industry even got off the hook
    - Some other industries and companies were more proactive
Consequences

- **2005-2007:**
  - Member-states "over-allocated" allowances
    - 2005: CO₂ emissions 4% lower than total allowances
      - Price for allowances drops to almost zero
        » Scant incentives for industry to invest in climate friendly technology
    - Decentralized system promoted high legitimacy

- **2008-2012:**
  - The European Commission has strengthened the system
    - Total allowances 6.5% lower than 2005 emissions
      » Effectiveness will depend on credits through the Kyoto Protocol’s flexible mechanisms: JI and CDM

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Consequences

- 2013-2020
  - 2008: Proposal to revise the EU ETS
    - Centralize the total allocation of allowances (the cap) to EU level
      - NAPs no longer needed
    - Industry must pay for allowances
      - Exception for industry at risk of 'carbon leakage'
    - No new CDM/JI credits after 2012
      - Inflow of such credits more liberal if 'satisfactory' international climate agreement
    - Additional sectors

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Conclusion

- Politics have determined the consequences of the EU ETS
  - Internally: struggle for competence and influence between the EU institutions, member states and industry
  - Externally: the Kyoto protocol
    - EU external events will also be important for the reform of the EU ETS

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