# International credits in the EU climate framework

European Commission
DG CLIMA B.3
International carbon markets, aviation, maritime

# Recap of EU regulatory framework

***Quantity limits***

- *EU ETS (2008-2020):*
  - **Installation limits determined by Regulation on International Credit Entitlements**
  - **Approximately 1.6 billion tonnes (< 50% of reduction effort)**
- *ESD:*
  - **3% of 2005 emissions**
  - **12 MS with stricter targets an additional 1% limited to credits from LDCs.**
  - **entitlements can be traded among MS**
  - **Approximately 700 million tonnes**
- *If new international agreement increase up to 50% of additional reduction*

***Quality requirements***

- *CDM projects registered prior to 2013*
- *CDM projects registered after 2012 in LDCs*
- *No ERUs from reductions after 2012 without new QELRCs*

# Recap of EU regulatory framework

- **Exceptions**
  - Provision to **restrict use of specific credits** from project types decided in CCC → industrial gas projects
  - Provisions for **bi- or multilateral agreements** for supply of credits if no international agreement concluded by Dec 2009 → opening for NMM
  - Provisions for **Community projects**
- **If there is an international agreement**
  - Only credits from projects in third countries that have ratified agreement
  - Types of credits to be agreed

# Evaluating past EU use of international offset

- **Main achievements**
  - **EU demand responsible for huge success of JI/CDM**
  - **Extended price signal beyond regulated markets, engaging DCs in climate action**
  - **Important financial and technological flows to DCs**
  - **Reduced compliance costs in EU**
  - **Buffer for short term fluctuations in demand**
- **Main concerns**
  - **Quantity limits turned out rather generous**
  - **International credits have become a major driver of the EU ETS surplus (half of accumulated surplus so far)**
  - **Quality concerns with some projects (additionality, pervese incentives, excessive rents, geographical distribution, human rights, …)**
  - **Existing mechanisms not adapted for future needs**
- **Calls for**
  - **UN supply-side reforms: CDM, development of NMM**
  - **Demand-side: more limited and selective use of international credits**

# Future international credit use in EU

- Framework is more or less fixed up to 2020
- But proposals in the pipeline for structural reforms of the EU ETS through two tracks of work:
- ETS reforms that can still have effect pre-2020 and can be proposed now
  - **Permanent set-aside**
  - **Reserve mechanism to render the auction supply more flexible**
  - **Changes in offset supply would have limited impact because 2/3 have already been used**
- ETS reforms in the context of the 2030 climate and energy framework
  - **Increasing the EU reduction target**
  - **Revision of the annual linear reduction factor**
  - **Extension of the scope of the EU ETS to other sectors**
  - **Discretionary price management mechanisms**
  - **Limit access to international credits**

# Limiting future access to international credits

- 2030 IA assesses different policy scenarios
- Default situation: no further access, excess allowances
- Role of offsets will depend on
  - **what is done with expected allowance surplus in phase 3**
  - **stringency of EU 2030 target**
  - **whether there is an international agreement**
  - **stringency of international targets**
- 2050 roadmap indicated limited scope for international credits
- If conditions are right and cap is strict, offsets could be used as cost containment
- Could be combined with more access in times of demand shocks
- White paper on climate and energy framework for 2030 expected by the end of the year, but legislative proposals will be for new Commission

# Some considerations in favour of limiting offset supply

- Less exposure to oversupplied CDM/JI market
- Lower risk of renewed surplus build up
- More investment clarity on domestic effort
- Less concerns about double counting with DC commitments and pledges
- Balance against lower financial and technology flows to DCs

# If credits are used then

- Guarantee that only high quality credits enter the EU
  - Element of net mitigation action (NMM)
  - Move away from project-based towards sectoral approaches (NMM)
  - Incentivise policies to reduce baseline emissions (NMM)
  - Remaining CDM should show clear mitigation benefits and include an element of own action
  - EU to determine unilaterally which credits to allow into the ETS
- Guarantee that our partners do the same
  - Fragmented market: centrally managed IET, JI, CDM, NMM vs. decentralised bilateral offsets, ETS, IET, NAMAs
  - FVA: establish common accounting standards and conformity checks for units or quantifiable outcomes crossing Party boundaries and used towards commitments under the Convention
- For a genuine level playing field EU interest lies in development and implementation of compatible ETS in view of possible future linking

# Expectations for Warsaw

- Review of CDM M&P
  - **create a bridge with NMM**
  - **Secretariat to prepare a draft for decision CMP.9 or 10 at latest**
  - **Main issues:**
    - report on SD, strengthen local consultation, regularly review baselines, reassess length of crediting period, voluntary net mitigation effects, avoid double counting (secretariat to evaluate options for solutions). Open to exclude HFC, N2O and coal projects from new project activities.
    - Appeals: EU open to explore possibility for appeal on + decisions and right of appeal for global and local stakeholders

# Expectations for Warsaw

- Agree on M&P for NMM
  - **Scope (broad segment, own contribution)**
  - **Criteria for baseline and threshold**
  - **Governance (eligibility, reporting, issuance, process for reporting, assessment, review and approval, ...)**
  - **Accounting and MRV**
  - **...**
- Swift establishment of FVA
  - **Requirements for reporting, criteria for assessment, eligibility**
  - **If not possible, then accept a transparency phase in advance of establishing the FVA**

# Concluding remarks

- **EC vision on international carbon market remains unchanged**
  - Link compatible domestic cap-and-trade systems to develop an OECD-wide market
  - New Market Mechanism for (advanced) DCs as a step towards cap-and-trade
  - Reform and better focus CDM (focus on LDCs)
- **Commission supporting these developments**
  - Negotiations on linking with Switzerland (and Australia)
  - Participation in World Bank PMR
  - Capacity building and outreach (ICAP and bilateral contacts)
  - Pilot projects for sectoral mechanisms
  - European acquis guides our international positions and outreach
- **There will only be a market if there is ambition and there will only be ambition if there is a market**

# Recent developments in EU ETS credit eligibility

- Registry Regulation review clarified quality requirements for ERUs
- ERUs issued after 31 Dec 2012 for reductions taking place until 31 Dec 2012 from non-EU ETS Annex B Parties can only be held in ETS accounts if:
  - **the amendment to the KP including a commitment for such a Party has entered into force OR**
  - **the Party has deposited an instrument of ratification OR**
  - **the credits are issued under track 2 OR**
  - **where track 2 issuance is not possible, the date of reduction (pre-2013) is certified by an AIE**

# Entitlement rules until 2020

| Type of operator | Entitlements rules |
|---|---|
| 1(1) Stationary installations with free allocations or an entitlement in 2008-2012 (incumbents, and phase 2 opt-ins and NE) | 11% of 2008-2012 allocation or amount allowed during phase 2, whatever is greater |
| 1(2) Stationary installations with no free allocation or entitlement in 2008-2012 (new sector), new entrants and opt-ins phase 3 | 4.5% of verified emissions during 2013-2020 |
| 1(3) Stationary installations with additional allocation following capacity increase under article 20 of Decision 2011/278/EU | Access during phase 2 or 11% of 2008-12 or 4.5% of verified emissions in 2013-20, whatever is greater |
| 1(4) Stationary installations with free allocations in phase 2 and extended scope in phase 3 | Amount allowed during phase 2 or 11% of 2008-2012 or 4.5% of verified emissions of full scope in 2013-20, whatever is greater |
| 1(5) Aircraft operators | 1.5% of verified emissions in 2013-2020 (on top of bankable 2012 entitlement) |