The EU Emissions Trading System

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Femke de Jong
EU policy director, Carbon Market Watch

femke.dejong@carbonmarketwatch.org

No evidence for production displacement due to the EU ETS

Ecorys study for the Commission (2013):

*"**We found no evidence for any carbon leakage** – according to the ETS Directive, defined as production relocation due to the ETS - **in the past two ETS periods**"*

Industry confirms lack of "carbon leakage" risks:

Energy intensive companies have reported to their shareowners that the competitiveness risks of the EU ETS are not an issue for them (see letter to Barroso here, 2014).

Industries have made windfall profits from the EU ETS, while claiming otherwise

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Very limited carbon leakage risks in the post-2020 period

- **No evidence for future "carbon leakage" risk**: even a ten-fold increase in carbon price and 100% auctioning will have an "extremely limited" impact on trade* (LSE study, 2015).

- **Many relocation destinations (will) have similar climate policies:** there are no carbon leakage risks when other countries take comparable climate measures. In light of the Paris agreement almost 200 countries have agreed to take climate efforts after 2020.

*Changes in energy prices explain less than 0.01% of the variation in exports and imports over the past 15 years, even in energy-intensive sectors.

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Despite limited risks, the EU ETS revision hands out free allowances to all industrial sectors

- The EU ETS revision proposes to continue with many of the existing “carbon leakage” rules, including the hand-out of **6.3 billion free emission allowances** in the post-2020 period.

- This represents a pollution subsidy of **€160 billion** to heavy emitters, at the expense of taxpayers.

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The EU ETS revision will result in windfall profits for heavy industry

The Commission's impact assessment shows that the steel, cement, refineries and chemicals sectors are able to pass through all their compliance costs to their customers and make **€19 billion from the EU ETS** in the 2021-2030 period.

Table 24 Overview table on estimated compliance cost per sector, taking into account cost pass-through rates

		With lowest cost pass through rates	
		compliance cost (million €)	% of turnover
Steel	Baseline B	-1.300	-0,8%
	Simple	-1.400	-0,9%
	Limited changes	-1.990	-1,2%
	Targeted	-1.930	-1,2%
Cement	Baseline B	-310	-1,9%
	Simple	-240	-1,4%
	Limited changes	270	1,6%
	Targeted	-230	-1,4%
Refineries	Baseline B	-190	0,0%
	Simple	-320	-0,1%
	Limited changes	-140	0,0%
	Targeted	-110	0,0%
Chemicals	Baseline B	-100	-0,1%
	Simple	-190	-0,1%
	Limited changes	-70	0,0%
	Targeted	-50	0,0%

€13 billion profits in 2021-2030 period

€3.1 billion profits in 2021-2030 period

€1.9 billion profits in 2021-2030 period

€1 billion profits in 2021-2030 period

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Industry's emissions are not projected to decline in the coming 15 years

- Free allocation of pollution permits **reduces the incentives** of heavy emitters to invest in low-carbon technologies or efficiency improvements.

- The European Environment Agency (EEA, 2015) projects that **industry's emissions will not decline from now until 2030**.

> *"We believe that business must be part of the solution. But to be so, business will have to change; there is not 'business as usual anymore'. Sustainable, equitable growth is the only acceptable business model. "*
>
> Unilever

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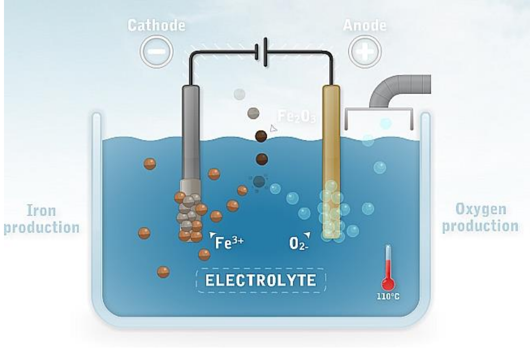
Creative, innovative technologies can bring industry's emissions to zero



Examples in the steel sector:

- **Electrolysis**: replacing the blast furnace with electrolysis of iron ore. Allows for carbon neutral steel production by using renewable power.
- **Electric Arc Furnaces**: using recycled scrap metal to produce flat or rolled steel. Can become carbon neutral by using renewable power (and charcoal).

Example in the cement sector:

- **BioMason:** using bacteria to grow biocement without the need for any heat. BioMason bricks could reach consumers by 2017, significantly reducing carbon emissions.

"Nature can produce materials with greater strength than [those made by] our manmade processes and with less energy, without polluting the surrounding environment"

Ginger Krieg Dosier, founder and CEO of bioMason

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Our recommendations

Enable a fully decarbonized industry by 2050 by:

- **Enlarging the Innovation Fund** and investing the revenues in Europe by supporting the frontrunners that want to invest in breakthrough technologies.
- Making free allocation conditional on the submission of a **sectoral roadmap + implementation plan** with milestones to a **fully decarbonized industry by 2050.**
- **Annually tighten the product benchmarks** in line with the overall EU ETS cap.
- **Removing all surplus allowances** in the Market Stability Reserve at the end of 2020 to help ensure that there is an adequate carbon price signal.

Phase out free pollution permits by:

- Gradually **increasing the share of allowances to be auctioned** from 57% to 100% in the future.
- **Introducing a tiered carbon leakage list** and targeting free allowances only to those that really need protection. The left-over free allowances can be cancelled or auctioned for innovation support.
- Restricting the **validity of the carbon leakage list** to no longer than **5 years**.
- Only compensating industry for the **share of carbon costs that are not passed on** to customers to avoid windfall profits.

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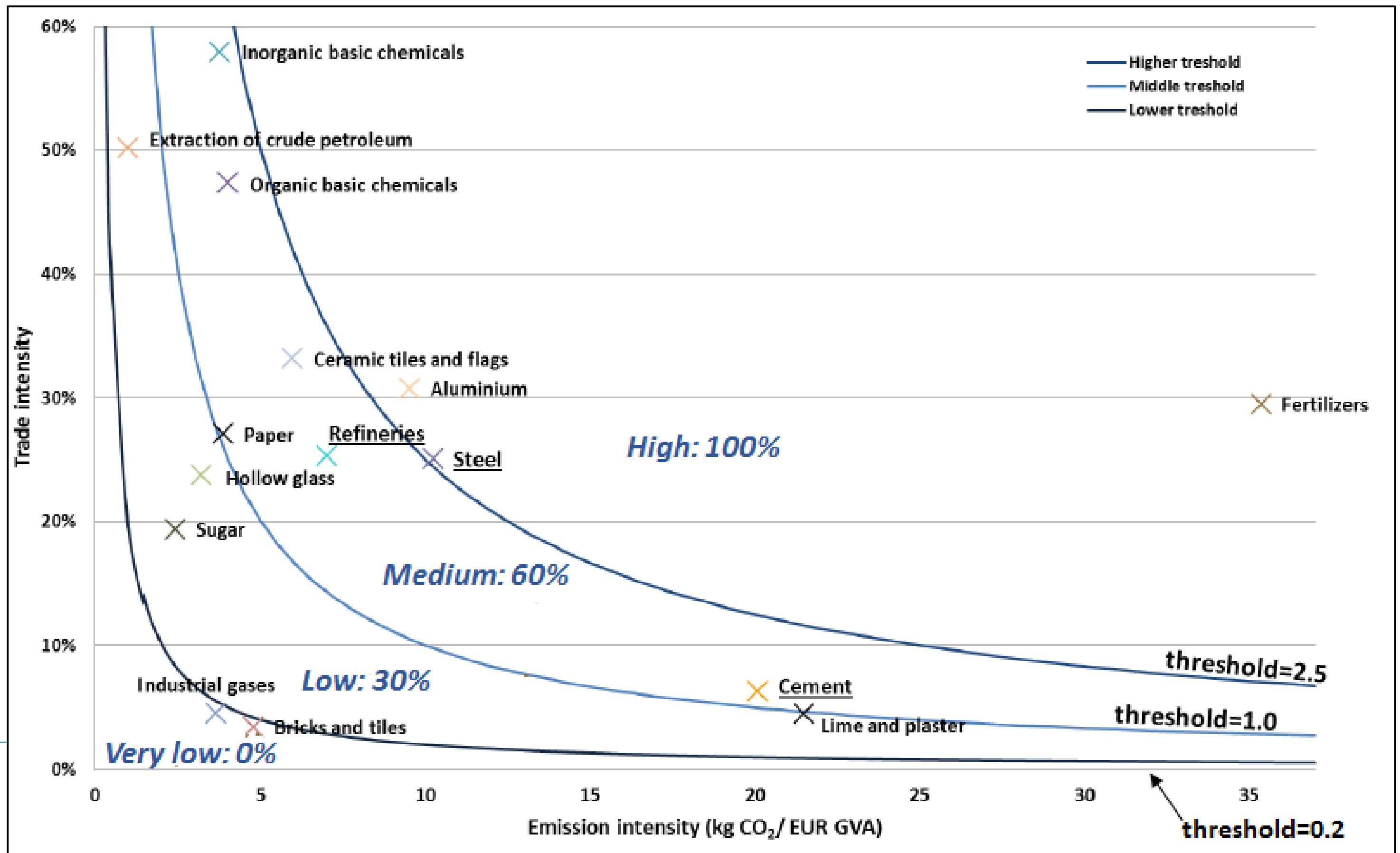
Tiered carbon leakage list can reduce the amount of allowances given away for free

A more targeted carbon leakage list can **free up more than 1.2 billion allowances** for enhanced innovation support or environmental integrity (cancellation).

Currently, the revision likely leaves industrial sectors at greatest risk of carbon leakage under-protected whilst over-compensating sectors at low or no risk



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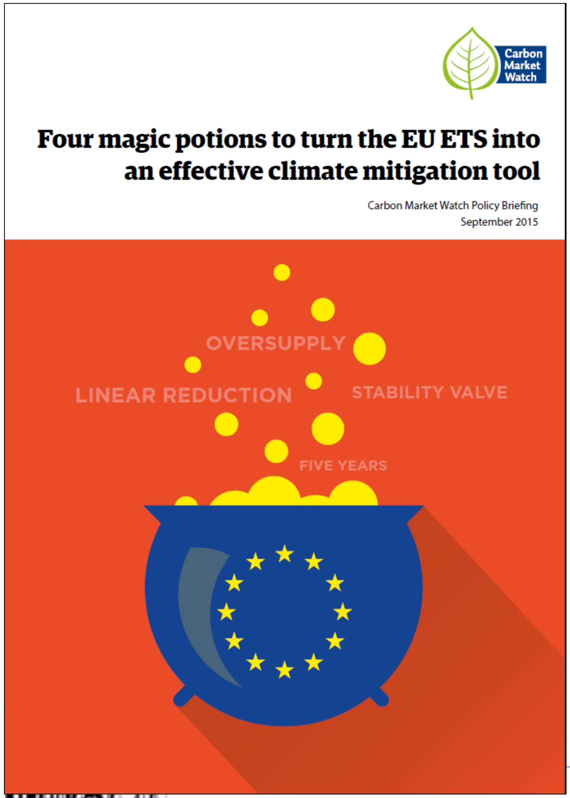
Read more …

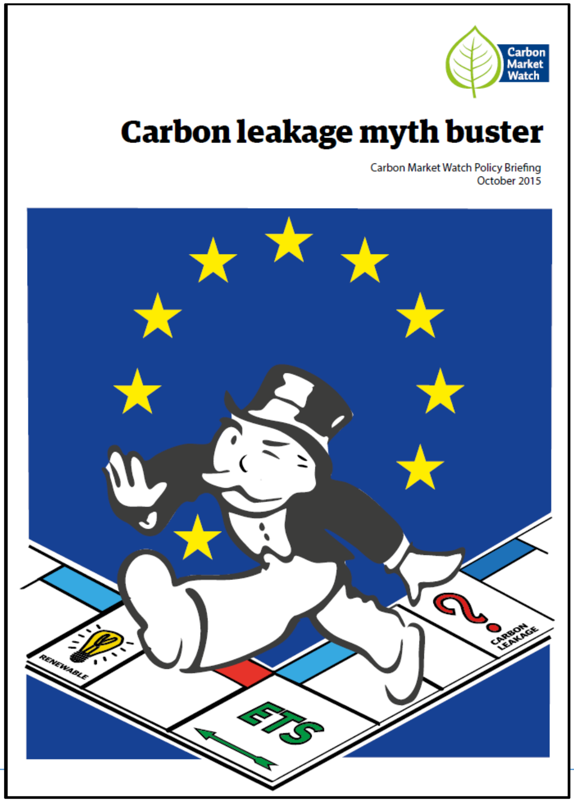
www.carbonmarketwatch.org

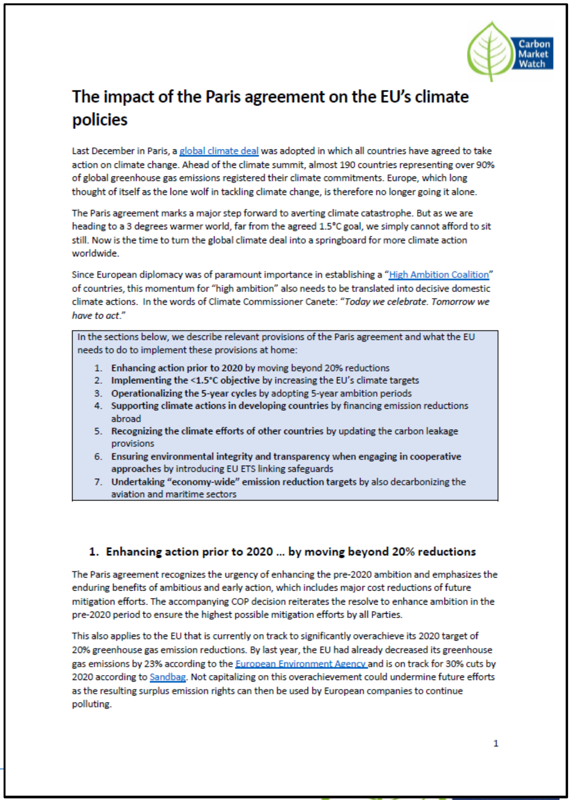
On increasing the environmental integrity of the EU ETS here

On our carbon leakage recommendations here

On the impact of the Paris agreement here







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The impact of the Paris agreement on the EU's climate policies

Last December in Paris, a global climate deal was adopted in which all countries have agreed to take action on climate change. Ahead of the climate summit, almost 190 countries representing over 90% of global greenhouse gas emissions registered their climate commitments. Europe, which long thought of itself as the lone wolf in tackling climate change, is therefore no longer going it alone.

The Paris agreement marks a major step forward to averting climate catastrophe. But as we are heading to a 3 degrees warmer world, far from the agreed 1.5°C goal, we simply cannot afford to sit still. Now is the time to turn the global climate deal into a springboard for more climate action worldwide.

Since European diplomacy was of paramount importance in establishing a "High Ambition Coalition" of countries, this momentum for "high ambition" also needs to be translated into decisive domestic climate actions. In the words of Climate Commissioner Canete: "*Today we celebrate. Tomorrow we have to act*."

In the sections below, we describe relevant provisions of the Paris agreement and what the EU needs to do to implement these provisions at home:

1. **Enhancing action prior to 2020** by moving beyond 20% reductions
2. **Implementing the <1.5°C objective** by increasing the EU's climate targets
3. **Operationalizing the 5-year cycles** by adopting 5-year ambition periods
4. **Supporting climate actions in developing countries** by financing emission reductions abroad
5. **Recognizing the climate efforts of other countries** by updating the carbon leakage provisions
6. **Ensuring environmental integrity and transparency when engaging in cooperative approaches** by introducing EU ETS linking safeguards
7. **Undertaking "economy-wide" emission reduction targets** by also decarbonizing the aviation and maritime sectors

1. Enhancing action prior to 2020 … by moving beyond 20% reductions

The Paris agreement recognizes the urgency of enhancing the pre-2020 ambition and emphasizes the enduring benefits of ambitious and early action, which includes major cost reductions of future mitigation efforts. The accompanying COP decision reiterates the resolve to enhance ambition in the pre-2020 period to ensure the highest possible mitigation efforts by all Parties.

This also applies to the EU that is currently on track to significantly overachieve its 2020 target of 20% greenhouse gas emission reductions. By last year, the EU had already decreased its greenhouse gas emissions by 23% according to the European Environment Agency and is on track for 30% cuts by 2020 according to Sandbag. Not capitalizing on this overachievement could undermine future efforts as the resulting surplus emission rights can then be used by European companies to continue polluting.

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