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Netherlands fits its new price floor

A draft law for the Dutch carbon floor price was recently published, raising the carbon price levied on electricity production to 43 euros by 2030. Carbon Market Watch is a proponent of carbon floor prices that better reflect the social costs of pollution, however several corporate stakeholders do not share our view. How can countries best price carbon in the absence of a Paris-compliant EU ETS?

Carbon floor prices essentially set a limit under which the CO2 price cannot fall beneath. This can make polluting less attractive to most heavy emitters, but also scales-up climate friendly investments, supports the phase-out of fossil fuels and raise revenues to fund the just, net-zero transition. Once the draft law is adopted, the Netherlands would be the second country, following the UK's example, to implement a minimum price on carbon pollution. The UK has shown that a carbon floor price can be an effective measure to phase out coal, as currently 60% of the EU-wide emission reductions in the power sector can be attributed to the UK.

Although carbon prices have tripled under the EU's Emissions Trading System (EU ETS), the current levels (€18[US$21]/tCO2) are still far below the prices that leading economists say are required to meet the Paris climate goals (US$40-80 by 2020).

Minimum carbon prices, set at the national or regional level, can complement the EU ETS when it is underperforming, acting as a safeguard and providing investors with a reliable and predictable return on low-carbon investments.

As noted in the Dutch explanatory memorandum, a carbon floor price is an important element in the greening of the financial system, as taxes are levied on what we do not want as a society (pollution), rather than what we want to encourage (jobs).

Opposition by corporate interests

It is hence surprising that several Dutch utilities and industries have voiced opposition to the carbon floor price during the public consultation on the proposal. The main reason cited by Dutch corporations is that a minimum price on pollution would not be effective, as it would not result in substantial CO2 reductions. A study by Frontier Economics for the Dutch government supposedly backs up this argument.

The contention is that by implementing a national coal ban and taxing Dutch power producers, emissions are reduced in the Netherlands, but more power is imported from other countries with a higher emissions intensity. The net effect of the floor price is alleged to 'only' be 4 million tonnes CO2 in 2030. This figure should be taken with a grain of salt however, as the study is based on several flawed assumptions.

Fool me twice…

First of all, it is assumed that the EU ETS price stays around €12 in the coming years and rises slowly to €17 in 2028. In reality, prices under the EU ETS have already reached €18, something Frontier Economics did not expect to happen until a decade from now.

Secondly, it is presumed that the Netherlands is the only country in the region phasing-out coal, while five of the eight modelled countries have also implemented coal bans by 2030 (or earlier) and two are currently contemplating the measure.

This means that, using more realistic assumptions, the Dutch carbon floor price and coal ban will result in even more emissions savings than currently predicted.

Tackling excess emissions permits

National coal bans and carbon floor prices should result in the maximum emissions savings possible and not allow companies in other countries to emit more. Fortunately, a new possibility has been created under the EU ETS revision that allows governments to cancel the excess emissions permits associated with closed-down power plants.

This can create a virtuous circle by driving up the carbon price, making remaining coal plants economically unviable and accelerating their closure, hence bringing immediate climate benefits.

Leading by example

In the absence of an EU-wide tightening of the EU ETS in line with a 1.5C pathway, it is up to national governments to implement additional measures, such as a carbon floor price and the cancellation of excess permits, to raise ambition.

The Dutch government has taken the right decision to not wait around for the next EU ETS revision, and has started to act by leading by example, thereby encouraging other countries, including France and Germany, to also introduce a minimum carbon price. The adoption of the draft law in the Netherlands will certainly help spur the ongoing conversations with other EU member states to link up national floor prices and develop a regional minimum carbon price.