

EU ETS – POLICY DEVELOPMENT TO 2012 AND BEYOND



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Melbourne 27 February 2007



“The first essential element of climate change policy is carbon pricing”

Stern Review

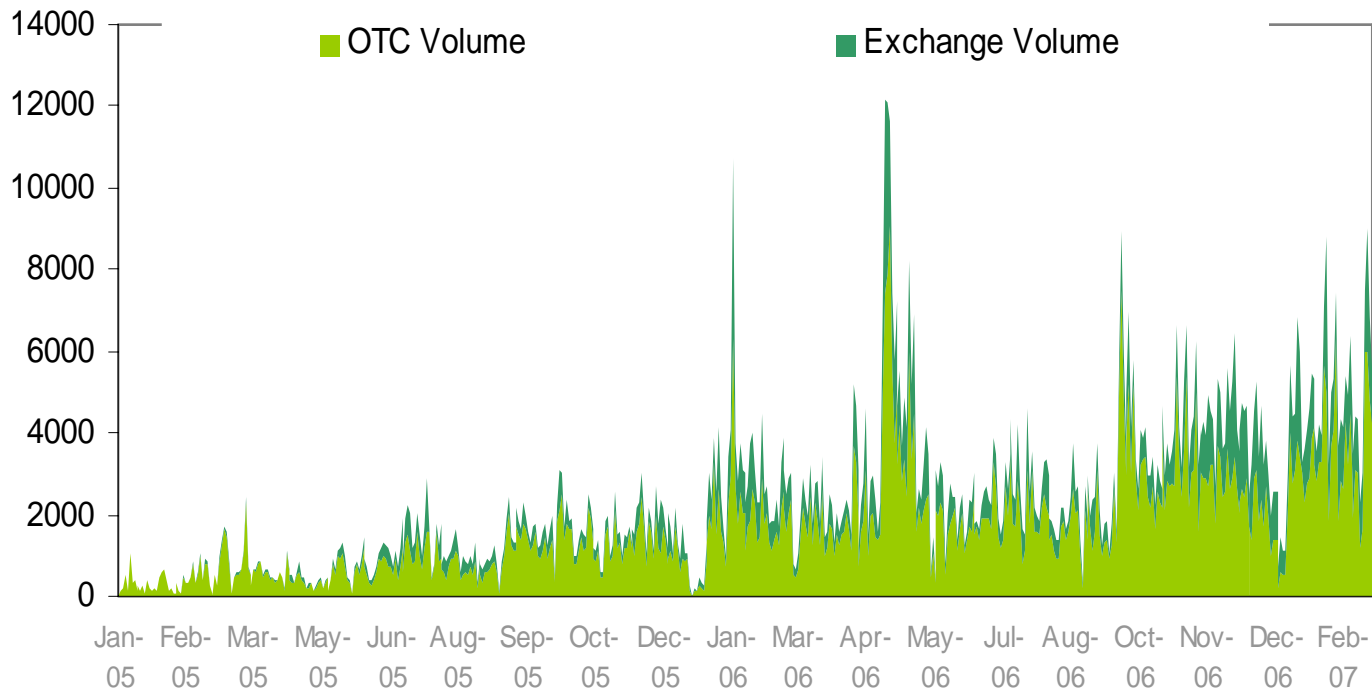
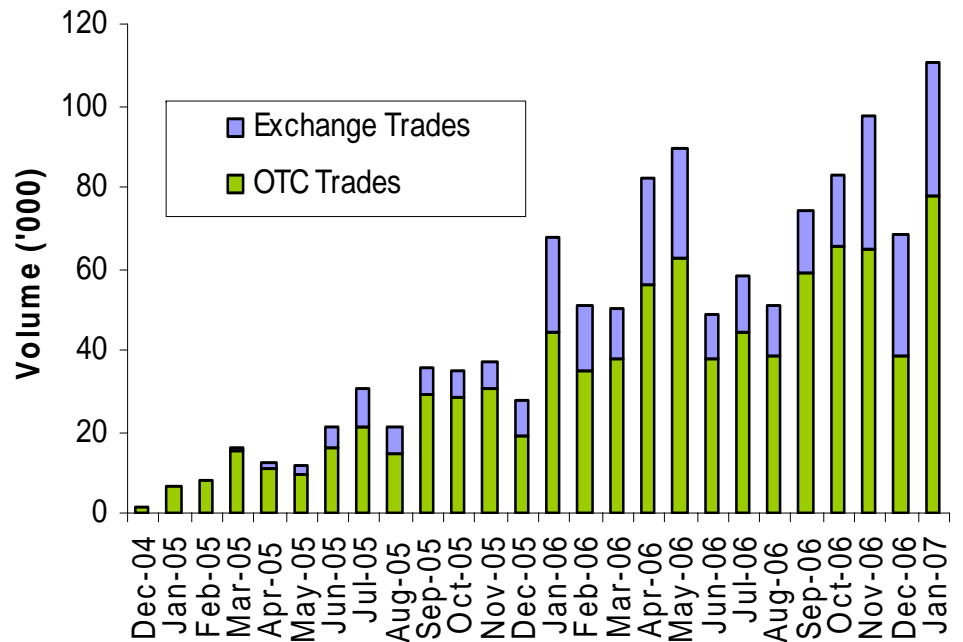
- it really works... (even in “a valuable learning period”)

EU-ETS CURRENT COVERAGE



- CO₂ emissions from energy intensive industry above specific capacity thresholds
(45–50 % of EU CO₂ emissions)
- Around 10,500 installations
 - electricity generators
 - heat & steam production
 - mineral oil refineries
 - ferrous metals: production & processing
 - cement, lime glass, bricks and ceramics
 - pulp & paper sector

EU-ETS MONTHLY AND DAILY VOLUMES since Jan 05



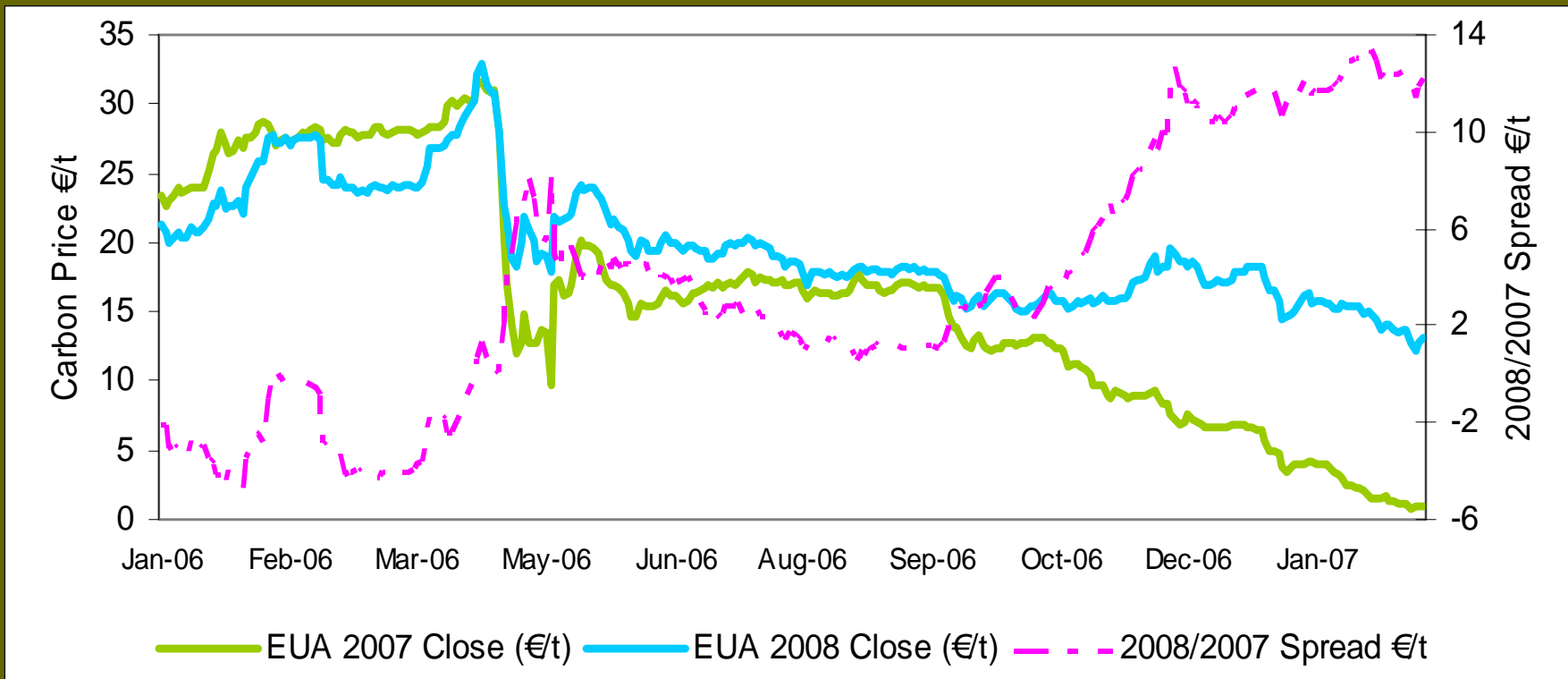
World Carbon Markets

	2005		Q1-3 '06	
	Volume (MtCO ₂)	Value (MUS\$)	Volume (MtCO ₂)	Value (MUS\$)
Allowances				
EU ETS	324.31	8,204.48	763.90	18,839.79
NSW	6.11	59.13	16.19	184.07
CCX	1.45	2.83	8.25	27.15
UK-ETS	0.30	1.31	2.26	9.27
Sub total	332.17	8,267.75	788.34	19,051.00
Project-based transactions				
CDM	359.08	2,651.44	214.26	2,260.96
JI	20.85	100.89	11.86	93.88
Other compliance	4.51	36.72	7.92	60.02
Sub total	384.44	2,789.05	234.05	2,414.87
TOTAL	716.61	11,056.79	1,022.39	21,465.87

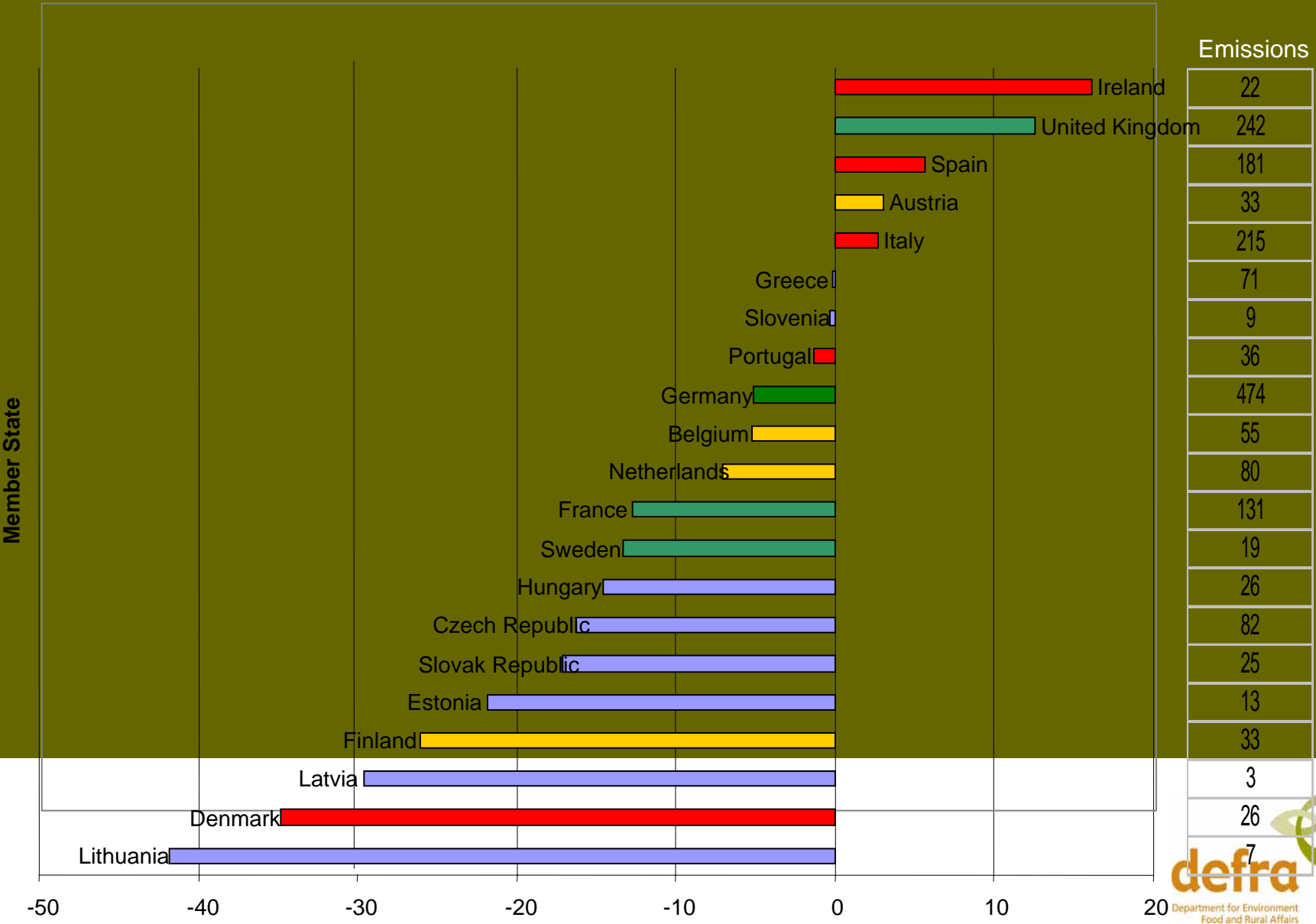
Source: World Bank/ IETA Sept. 2006

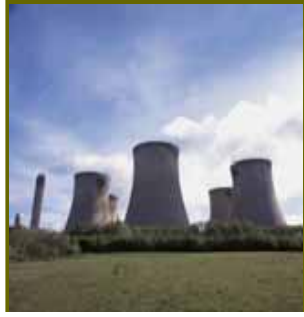
- caps and prices – getting it right (or better) in phase 2

PHASE 1 AND PHASE 2 PRICES



Percentage difference between allocations and emissions in 2005





Determination of the Total Quantity of Phase 2 Allowances in UK

- Projected Phase II business as usual (BAU) emissions (including expansion) – 275.51 MtCO₂
- Allocation based on 29.33MtCO₂ below BAU – Large Electricity Producers to take the cut, other sectors allocated BAU.
- Annual allocation for Phase II will be 246 million
- Of this 236.7 million will cover Phase I installations (including those opted out)
- A further 9.5 million will cover emissions that were not covered in Phase I

UK CHOICES FOR PHASE 2 – OTHER MS DIFFER

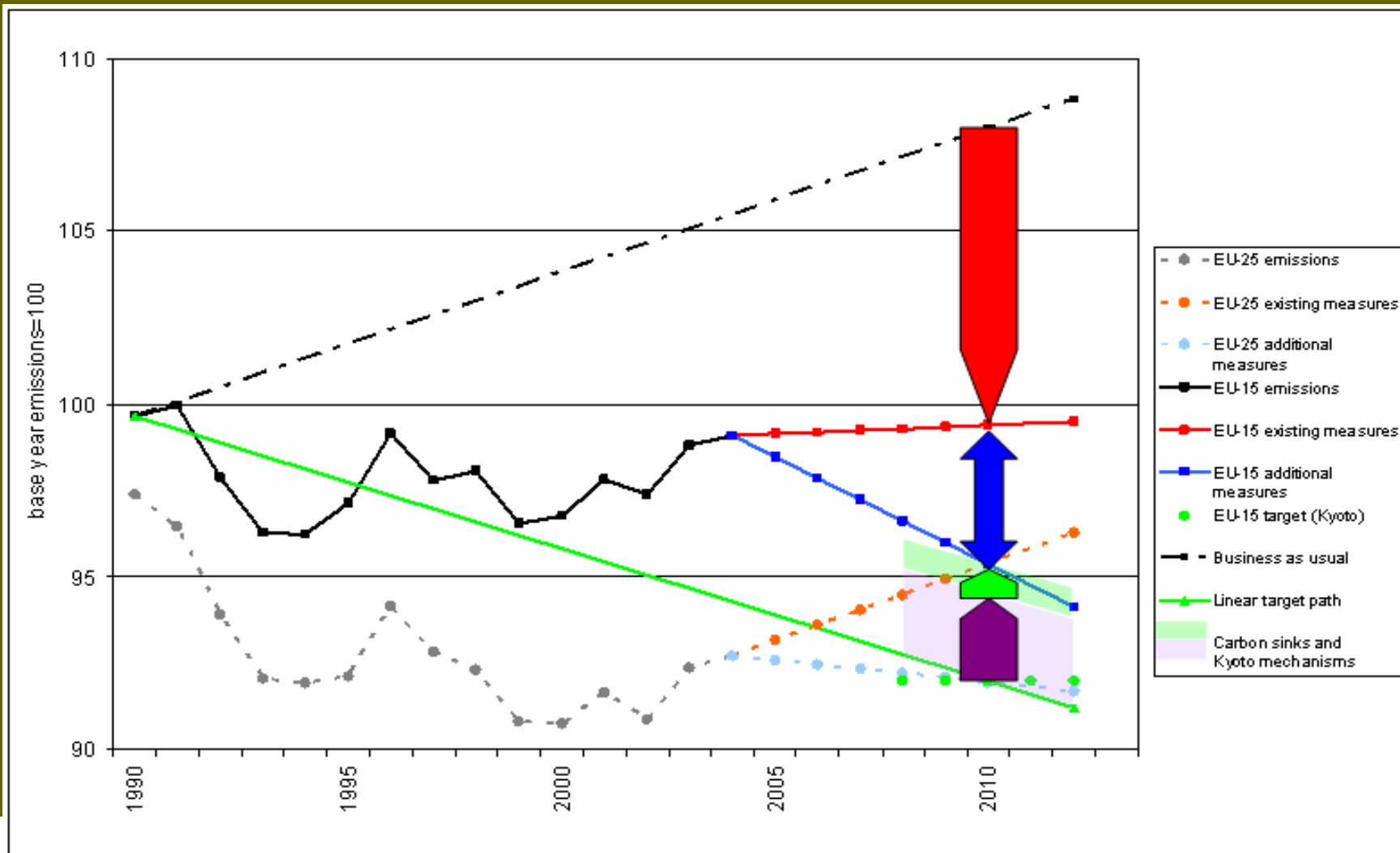
- Project credits: Installation level limit set at 8% of allocation – roughly 2/3 of effort (difference between projected BAU and cap)
- Auctioning: 7% of cap - 17,232,320 allowances per annum
- CCS: Aiming to allow CCS installations to opt in
- Small installations: de minimis rule
- Benchmarking for power sector

LATEST PHASE 2 NUMBERS (26.2.07)

MS	2005 outturn	2008-12 proposed	2008-12 approved
Belgium	56	63	58
Germany	474	482	453
Greece	71	76	69
Ireland	22	23	21
Latvia	3	8	3
Lithuania	7	17	9
Luxembourg	3	4	3
Malta	2	3	2
Netherlands	80	90	86
Slovakia	25	41	31
Slovenia	9	8	8
Spain	183	153	152
Sweden	19	25	23
UK	242	246	246

- relying on the CDM

The EU's Kyoto challenge



European Commission

Use of Kyoto Mechanisms: Planned purchases by Member States (in addition to company use)

	Million tonnes of CO ₂ eq.
Austria	35.00
Belgium	42.00
Denmark	22.50
Finland	At least 3.0
Ireland	18.50
Italy	198.00
Luxembourg	15.00
Netherlands	100.00
Spain	100.00
Sweden	At least 5.0

Almost 520 Million tonnes of CO₂eq (2008-2012)

Allocated resources thus far: € 2.7 billion

Total CDM Supply: Project & Credit Summary

	Projects	Mt CO ₂ e/year
CDM pipeline (under validation)	1300	250
Registered	408	103.63
Requesting registration	59	3.89
Credits Issued	96	18.81
Total CERs requested	-	24.51

Nairobi CDM Results

- Guidance to the Executive Board – especially on transparency, additionality and management planning
- Publication of rationales for decisions
- Changes of personnel
- Extension of prompt start deadline
- Further work on forestry projects, especially small-scale
- Cooking stoves - move to programmes?
- CCS – still very hard going but a good, if slow, outcome: submissions by May or September 07

- getting it even better in phase 3 (beyond 2012)

Commission Communication: *Building a Global Carbon Market*, Nov 2006

- Identified four areas for review:
 - Scope of the Directive
 - Further harmonisation and increased predictability (a single EU-wide cap?)
 - Robust compliance and enforcement
 - Linking with emission trading schemes in third countries
- Working Group will report by June 2007

UK Vision for EU-ETS

- **Setting safe, stable and affordable emissions limits**
 - EU –ETS primary place endorsed at European Spring Council meeting
 - EU commitment to reduce emissions by 30% by 2020
 - Commit to ensuring scarcity in EU ETS.
- **Building a global carbon market**
 - Cover more sectors and gases
 - Links to other cap and trade schemes
 - EU business to invest in emission reduction via CDM
- **Improving efficiency** through further technical changes
 - Length of trading periods
 - No anti-competitive distortions
 - More auctioning of allowances

Recommendations by High Level Group on Competitiveness, Energy and the Environment

EU ETS is the central instrument for GHG reductions towards the 2°C target

- Advance international debate beyond 2012
- Identify how EU ETS can be linked to emerging compatible systems and use of Kyoto credits can be facilitated
- Increase investor certainty
- Take account of regulatory stability and improve regulatory coherence
- Consider participation costs of small installations
- *Impact on competitiveness?*

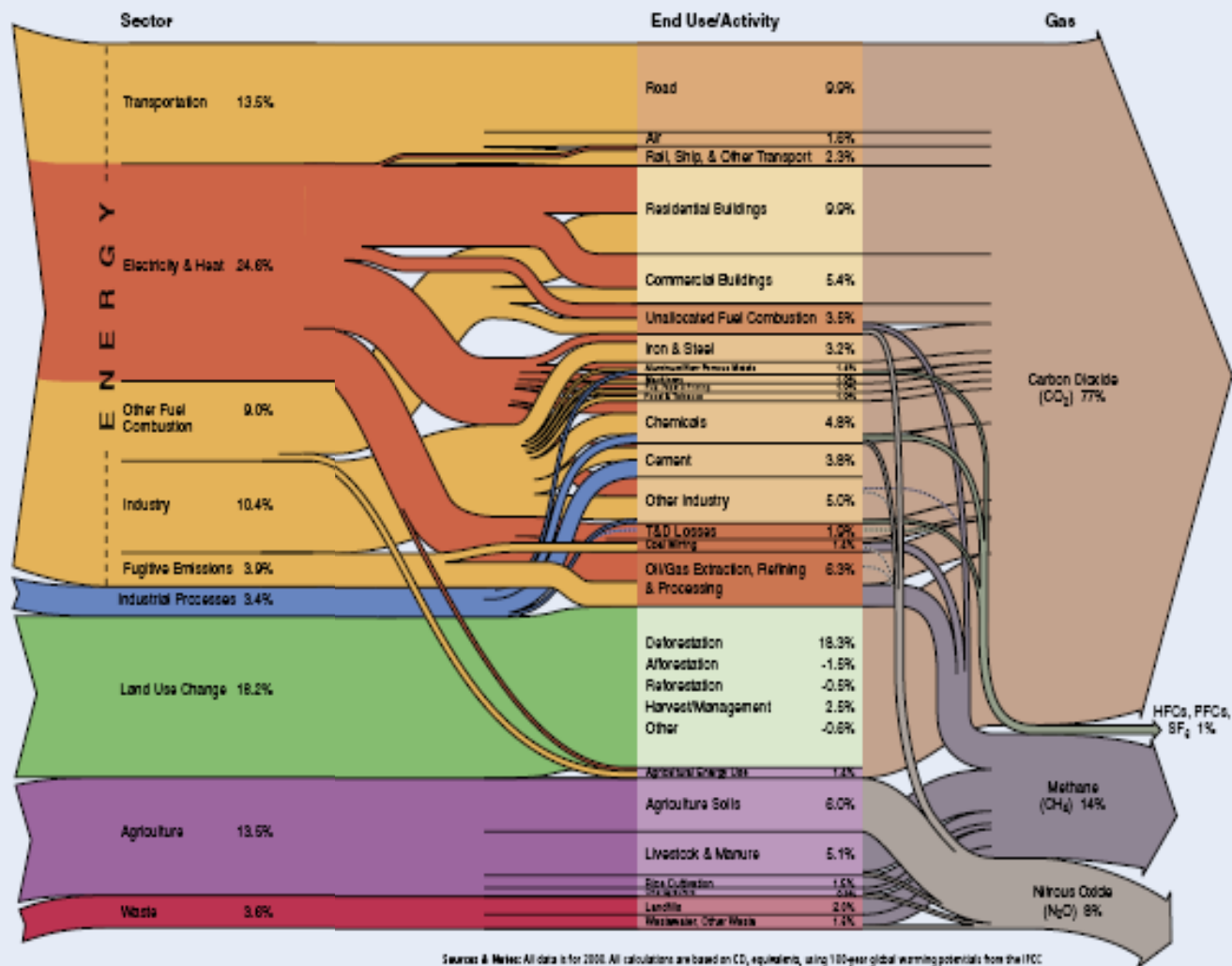
LINKING – WHAT ARE THE ISSUES?

- Maximising efficiency
- Other jurisdictions queuing up – Australia?
- Common environmental integrity – avoiding Gresham's Law
- Caps, floors and complementarity
- Is this Kyoto trading?

- expanding the coverage

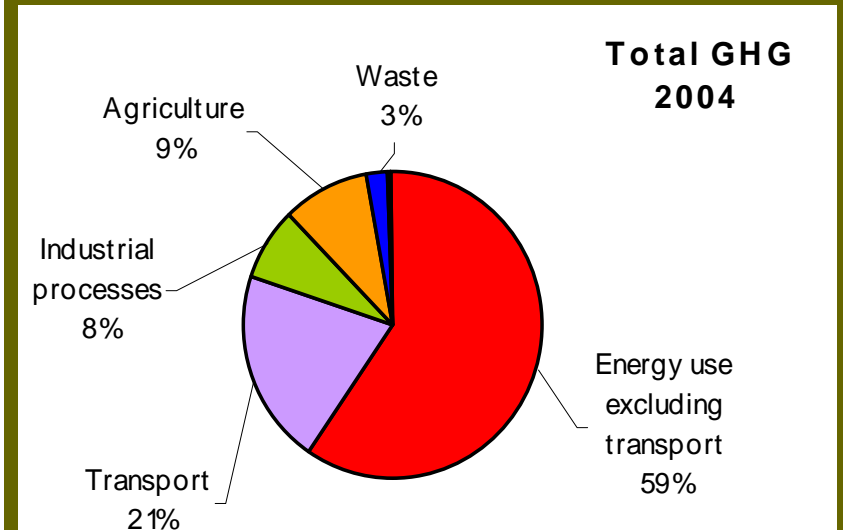
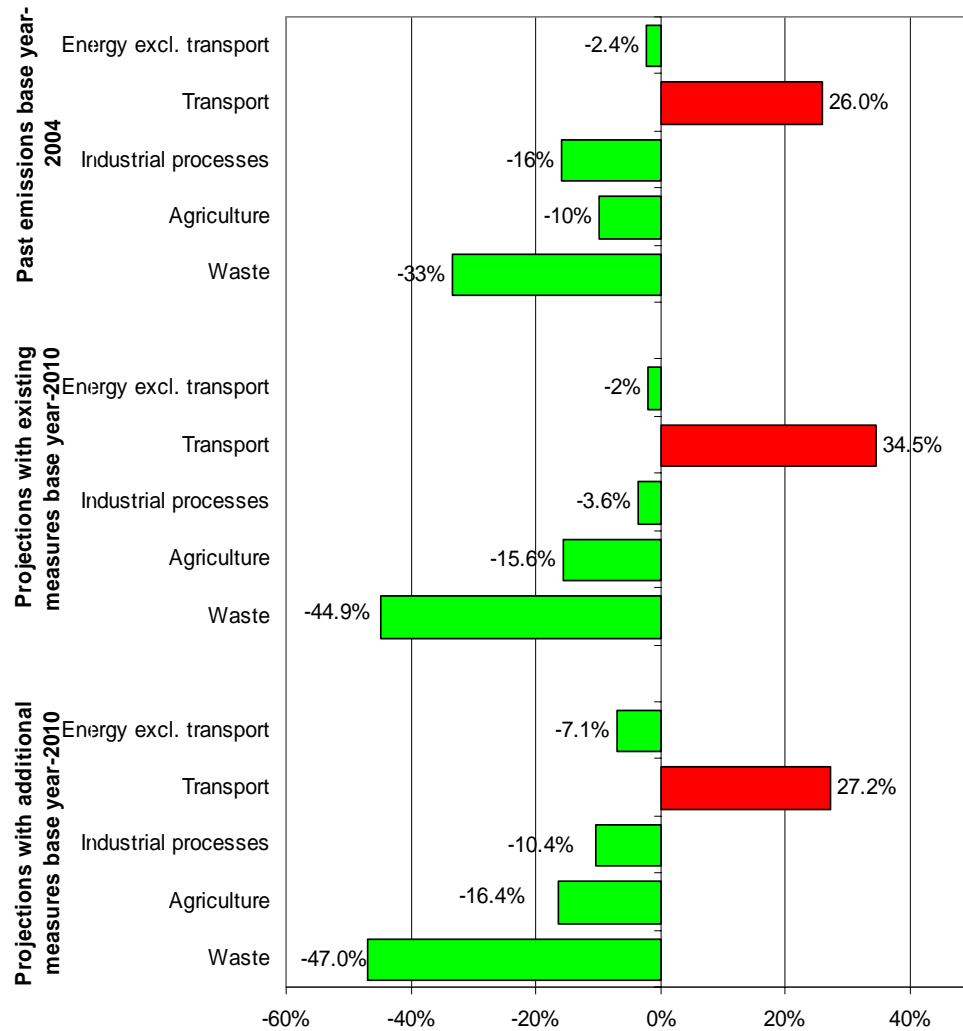
Global Greenhouse Gas Emissions

Figure 1.3. GHG Flow Diagram, Global Greenhouse Gas Emissions



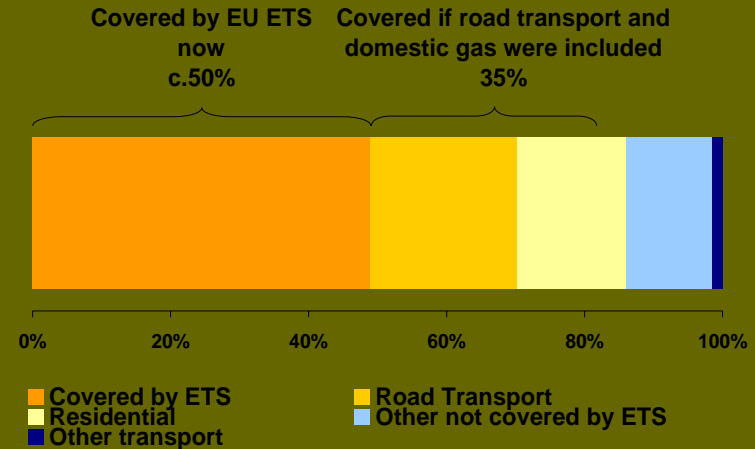
Sources & Notes: All data is for 2008. All calculations are based on CO₂ equivalents, using 100-year global warming potentials from the IPCC (1996), based on a total global estimate of 81,716 MTCO₂e equivalent. Land use change includes both emissions and absorptions, see Chapter 17. See Appendix 2 for detailed description of sector and end-use/activity definitions, as well as data sources. Dotted line represents flows of less than 0.1% percent of total GHG emissions.

Sectoral trends (EU): 1990-2004/1990-2010

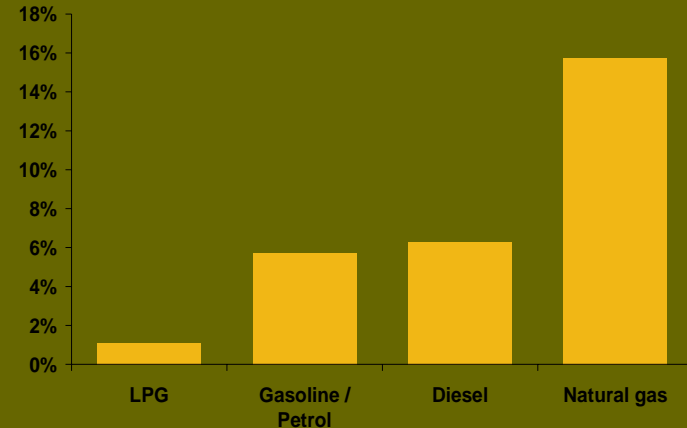


EXTENSION IN THE UK

- EU-ETS now covers 46% of UK CO₂ emissions;
- Addition of surface transport would extend the ETS' coverage of UK CO₂ emissions by 21%; inclusion of household and commercial gas supplies would add a further 15-20%
- Implicit carbon pricing in the UK economy today is far from consistent

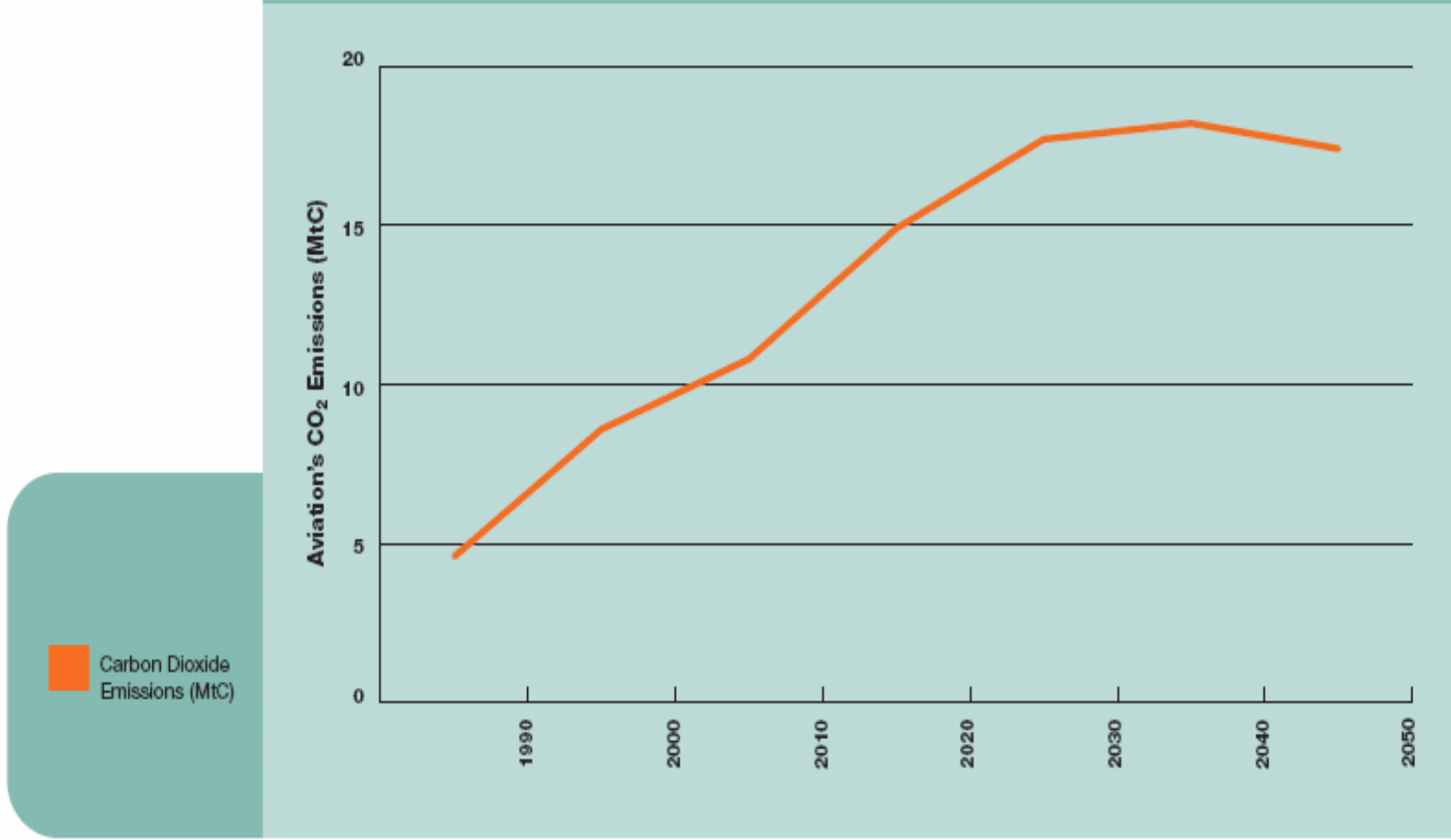


At €30/tCO₂, the inclusion of domestic gas in the ETS would add 15% to the price if costs were passed on in full to consumers



UK Aviation CO2 emissions

UK AVIATION'S FORECAST CARBON DIOXIDE EMISSIONS¹



Further Trading in the UK?

From the country that gave you the UK-ETS and tradable climate change agreements:

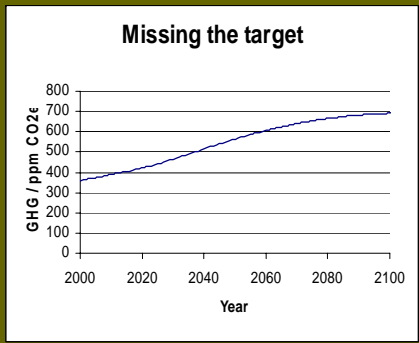
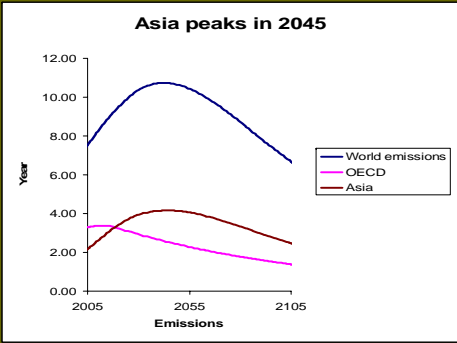
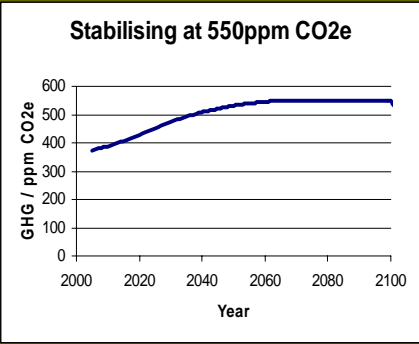
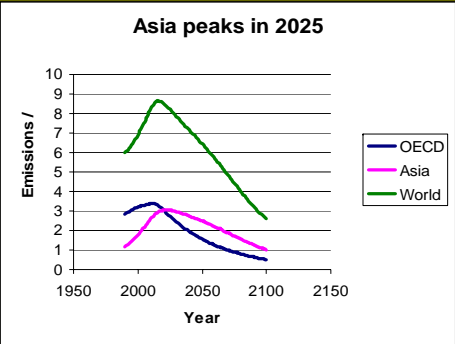
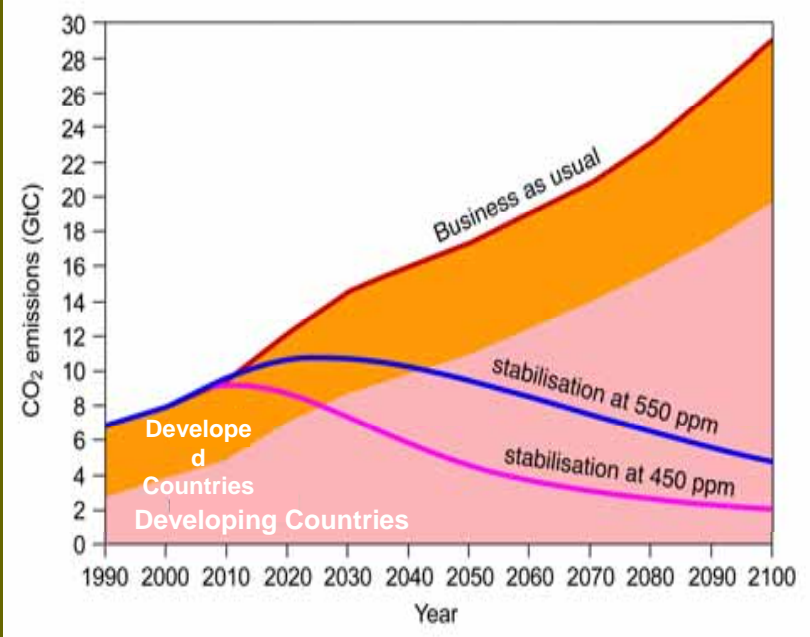
Energy Performance Commitment

- 3-5000 large non-energy intensives
- auction-based
- revenue recycled

Leading the way?

- long-term ambition and investor confidence

The challenge of stabilisation



EU LEVELS OF AMBITION

- 2 degrees target
- 60-80% by 2050
- -20% unilateral by 2020
- -30% if others act as well

CASHING IN ON ENERGY EFFICIENCY

Estimates for full energy saving potential in EU end-use sectors

Sector	Energy consumption (Mtoe) 2005	Energy Consumption (Mtoe) 2020 (Business as usual)	Energy Saving Potential 2020 (Mtoe)	Full Energy Saving Potential 2020 (%)
Households (residential)	280	338	91	27%
Commercial buildings (Tertiary)	157	211	63	30%
Transport	332	405	105	26%
Manufacturing Industry	297	382	95	25%

The UK's own ambition – the Climate Change Bill

- Enshrine in statute the Govt's target to reduce CO2 by 60% by 2050
- Set up independent Carbon Committee to work with Govt to reduce emissions
- Have enabling powers to put in place new emissions reductions measures
- Improved monitoring and reporting arrangements

WHAT DIFFERENCE WILL THIS MAKE TO INVESTORS IN CCS AND OTHER LOW CARBON GENERATION IN THE EU?

- Can a long-term price now be predicted?
- Is it enough to tip investment choices?
- What if there was also further regulation or lower transaction costs?
- Pros and Cons of an additional instrument

