

Lessons learned for design of national ETSs

Monique Voogt, 4 April 2023

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Choices for an ETS (or not)

- ❑ ETS has proven to be a cost-effective instrument to address climate change
- ❑ BUT ETS is not a silver bullet and cannot address all objectives or all inequities
 - Using sectoral caps or multiple methodologies for allocation results in a non-level playing field and in undermining the carbon price incentive
 - Additional policies are preferably used to address other objectives
 - ETS revenues can be used to address inequities
- ❑ NOTE it's a complex system and it takes quite some time before it functions well
 - Lessons can be learned from several ETSs; the designs are more and more converging
 - (more on the next slides)

Selected lessons learned - allocation

Comparing options

- Free allocation (FA) limits economic impacts and increases acceptance
- FA according to BaU emissions does not incentivise reduction
- Grandfathering (GF) can lead to perverse incentives
- Benchmarking (BM) provides better incentives and fairer treatment (compared to GF)
- Auctioning increases direct costs on participants, but generates revenues and reduces (govt) administration

Practical choices

- FA can be useful for early years
 - Lower economic impacts
 - Higher acceptance
 - Allows time for learning – setting up robust MRVA, identifying GHG reductions, understanding costs
- Auctioning is preferred in later yrs
 - Reflects polluter pays principle
 - Avoids perverse incentives and subjective allocation choices
 - Does not require rules for new entrants, closures, etc.
 - Does not require verification of data for free-allocation

Selected lessons learned – MRVA

- ❑ MRVA is a no-regret option to start with and has good value for several ETS issues
- ❑ Good quality data helps cap setting and distribution of effort (i.e. splitting cap over the participating sectors/actors)
- ❑ Good quality data supports understanding on the need of the specific climate measure and acceptance of its design choices
- ❑ Solids implementation of MRVA framework takes significant time, for all stakeholders involved >> better to learn before actual start of ETS
- ❑ Timely availability of good quality data helps operators to design a good carbon response strategy and thereby lower the costs of compliance
- ❑ Timely implementation lowers the costs of oversight and therewith lowers the administrative burden

Selected lessons learned - efficiency

System efficiency

Elements to support higher system efficiency:

- Central coordination
- Harmonisation (across countries, regions, activities)
- Simplified treatment of small emitters and de-minimis sources
- Use of auctioning (compared to developing BMs or defining FA)
- Harmonised compliance and administrative requirements (also across policy areas, where possible)

Efficiency for operators

Elements that support a higher efficiency for operators

- Harmonised templates for monitoring & reporting
- Market stability mechanisms
- Long-term political certainty (wrt targets, market, governance)
- Early and meaningful stakeholder engagement



Thoughts on a regional approach

- ❑ A well-functioning ETS takes time
- ❑ Yet the urgency to address climate change & the need to avoid high carbon costs requires swift action

What steps are recommended for the region?

- ❑ As a (pre-) EU accession country, build the market along the lines of the EU ETS to avoid having to make changes later
- ❑ Build on the lessons learned; adapt to local needs, strengths and capacities
- ❑ Take a step-wise approach to allow for own learning
- ❑ Use international cooperation where possible, to alleviate the burden and use opportunities for market stabilisation

Advantage of a regional approach to carbon pricing

Advantages

- Keeping benefits within the region
- Strengthening the common position
 - within countries to create buy-in
 - in international negotiations
- Avoid competitive distortion
- Avoid “weakest approach is the leading approach”

Note: a regional approach would not necessarily mean establishing a full, common system.

It can also mean sharing elements to the system or making similar design choices to enhance (future) cooperation.

Start with shared infrastructure/capacity

Advantages

- Allowing to focus efforts; avoiding having to implement too much in too short time
- Improving efficiency of time spending during implementation
- Allowing countries to leapfrog where preferred
- Using relative strengths of countries
- Improving cost-effectiveness of market elements and building stronger markets

Note: EU ETS is a fully integrated, international system AND part of the infrastructure is shared:

- **One registry; one dominant trading & auctioning platform**
- **International use of verifiers/NABs**
- **Standardised MRVA templates, tools and guidance**
- **Shared IT system**
- **Active sharing of expertise**
- **Joint training**

A similar strategy for joint learning and sharing leads to a significant reduction of effort and helps creating a liquid and stable market.

Thank you for your attention

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