

EU ETS

- state of play, review and perspective

Regulatory School of the Energy Community Secretariat in cooperation with EFET - Introduction into CO2 market - 15th December 2020

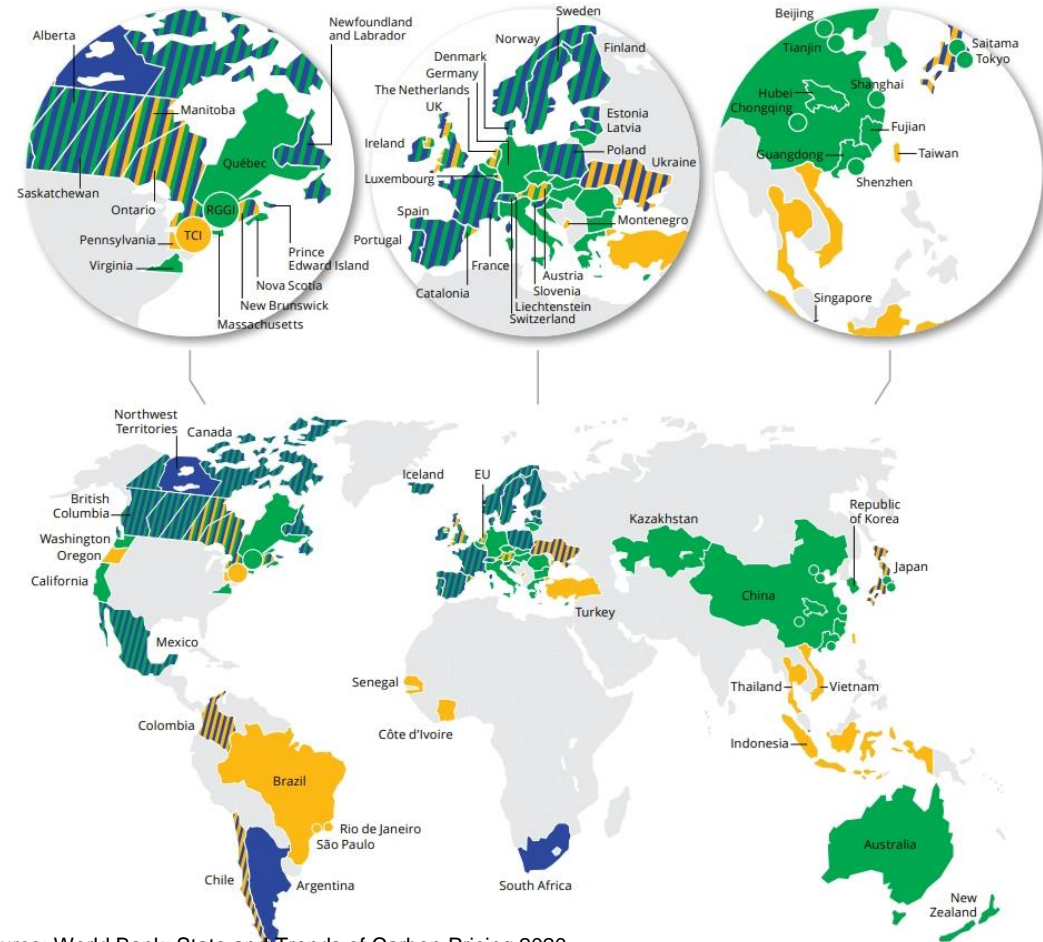
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Governance Expert

- ETS implemented or scheduled for implementation
- Carbon tax implemented or scheduled for implementation
- ETS or carbon tax under consideration

- ETS and carbon tax implemented or scheduled
- Carbon tax implemented or scheduled, ETS under consideration
- ETS implemented or scheduled, ETS or carbon tax under consideration
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GLOBAL STATE OF EMISSION TRADING

- ☀ 46 national and 32 sub-national jurisdictions have implemented or scheduled to implement carbon pricing;
- ☀ Overall 61 initiatives: 31 ETS & 30 carbon tax;
- ☀ Largest are EU, South Korea, California, Quebec, China;
- ☀ These translate to about 12 gigatons of carbon dioxide equivalent (GtCO₂e) or about 22 percent of global emissions;
- ☀ Around US\$45 billion globally in 2019.



Source: World Bank: State and Trends of Carbon Pricing 2020

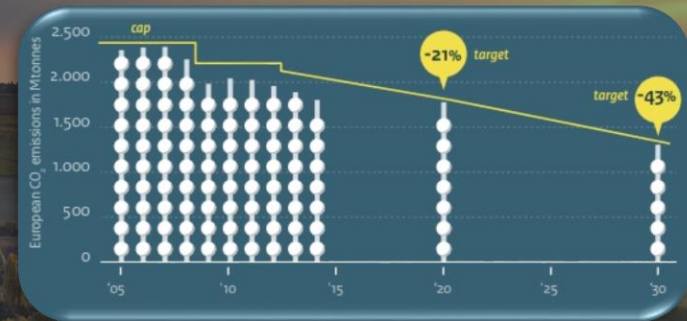
EUROPEAN UNION EMISSION TRADING SYSTEM

- ☀ Set up in 2005, the EU ETS is the world's first international emissions trading system;
- ☀ 31 Countries
 - ☀ All 28 EU Member States,
 - ☀ Norway, Iceland, Liechtenstein;
- ☀ >12.000 large installations
 - ☀ Including electricity and heat producers, steel, chemicals, cement, glass, pulp, paper, airlines operating between ETS countries, etc.
- ☀ ~2.000 Mt CO₂eq per year
 - ☀ 45% of the total EU annual emissions,
 - ☀ Carbon dioxide (CO₂), Nitrous oxide (N₂O), Perfluorocarbons (PFCs).



HOW THE EU ETS WORKS

- ★ The EU ETS works on the 'cap and trade' principle;
 - ★ Within this cap, companies receive or buy emission allowances which they can trade;
- ★ Emission allowances are the 'currency' of the EU ETS;
 - ★ Each allowance gives the holder the right to emit one tonne of CO₂eq;
 - ★ Allowances can be used only once and surrendered every year;
- ★ Cap decreases each year by a linear reduction factor of 1.74% until 2020 and by 2.2% between 2021-2030;
 - ★ A separate cap applies for the aviation sector;
- ★ Companies may receive free allowances to prevent carbon leakage;
- ★ Target for emissions in 2020 is 21% lower than in 2005, and 43% lower in 2030.



Source: Dutch Emissions Authority

EU ETS DEVELOPMENT PHASES

2005-2007: 1st trading period

- EU ETS was established as the world's biggest carbon market;
- process of 'learning by doing';
- number of allowances turned out to be excessive → Price fell to zero in 2007.

2008-2012: 2nd trading period

- Iceland, Norway and Liechtenstein joined;
- number of allowances was reduced by 6.5%;
- Economic downturn depresses emissions → surplus of unused allowances;
- Aviation was brought into the system.

2013-2020: 3rd trading period

- Major reforms were introduced;
- introduction of cap on emissions and a linear reduction factor of 1,74% annually;
- Shift from free allocation towards auctioning of allowances begins.

2021-2030: 4th trading period

- New 2030 emission-reduction targets introduced;
- number of allowances decline by 2,2% annually,
- new funds and support mechanisms.

EUETS

CHANGES IN PHASE 4 OF THE EU ETS

- ☀ EU ETS Phase 4 is starting on 1 January 2021 with new elements:
 - ☀ New reduction target up to 2030 will be 43%;
 - ☀ The linear reduction factor is increased from 1,74 % to 2,2 % in 2021;
- ☀ Market Stability Reserve (MSR) will be substantially reinforced:
 - ☀ Between 2019 and 2023, the amount of allowances put in the reserve will double to 24% of the allowances in circulation;
 - ☀ The regular feeding rate of 12% will be restored as of 2024.
- ☀ Better targeted carbon leakage rules:
 - ☀ Free allocation will be prolonged but eventually phased out;
 - ☀ Revised list of sectors at the highest risk of relocating.
- ☀ Low-carbon funding mechanisms will be set up:
 - ☀ Innovation Fund: demonstration of innovative technologies;
 - ☀ Modernisation Fund: investments in modernising the power sector.



STATE OF PLAY AND OPEN ISSUES OF THE EU ETS

- ✦ Emissions from installations covered by EU ETS declined by about 35% between 2005-2019, 9.1% only in 2019 from 2018 levels;
 - ✦ However under the current cap, EU ETS would only reach net zero in 2058;
- ✦ 43% of all allowances will be allocated for free until 2030:
 - ✦ 6,3 billion allowances will be handed out for free — valued at about €165 billion;
 - ✦ Between 2012-2018 with free allocation only 4,7% annual average drop VS. 22% with not free allocation
 - ✦ Because of free allocation companies sold surplus €25 billion over 2008-2015;
- ✦ EU ETS revenues rose from 90 million in 2012 (worth €620 million) to over 920 million in 2018 (raising €14 billion):
 - ✦ EU MS only used 67% to finance climate action;
- ✦ New EU climate targets mean the update of EU ETS targets and sectors.





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