

# Greenhouse gas emission allowance trading scheme of the Community

2008/0013(COD) - 23/01/2008 - Legislative proposal

**PURPOSE:** to improve and extend the greenhouse gas emission allowance trading system of the Community (EU ETS).

**PROPOSED ACT:** Directive of the European Parliament and of the Council.

**BACKGROUND:** on 10 January 2007, the Commission adopted an integrated package of measures in the area of energy and climate change, inviting the Council and the European Parliament to approve:

- an EU commitment to reduce greenhouse gas emissions by at least 20% by 2020 compared to 1990 levels, as well as the aim for a 30% reduction by 2020, subject to the conclusion of an international agreement on climate change;
- a binding target for the EU of a 20% share of renewable energy sources in energy consumption by 2020, and a 10% target for biofuels.

This strategy was approved by the European Parliament and EU leaders during the March 2007 European Council. The European Council invited the Commission to present concrete proposals, particularly on the provisions for sharing the effort between Member States to achieve this objective.

The series of measures here presented is the response to this invitation. It includes a proposed set of key interdependent measures to be taken, as outlined below:

- a proposal for a directive amending Directive 2003/87/EC, to improve and extend the European Union Greenhouse Gas Emission Trading Scheme (the subject of this document);
- a proposal for a decision on the effort to be made by Member States to reduce their greenhouse gas emissions, in order to respect the Community's commitments to reduce these emissions by 2020 (see [COD/2008/0014](#));
- a proposal for a directive aiming to promote renewable energy (see [COD/2008/0016](#)).

Included among the proposals that make up this set of measures are: a proposal for a regulatory framework on carbon capture and storage (see [COD/2008/0015](#)); a communication on the demonstration of carbon capture and storage; and a new Community framework on State aid in the area of the environment.

**CONTENT:** On 1 January 2005, the European Emission Trading System (EU ETS) started operation. It represents the spearhead and "one of the most important instruments" of EU climate policy due to its ability to achieve absolute emission reductions in an economically efficient manner.

The EU ETS developed into the world's largest single carbon market accounting for 67% in terms of volume and 81% in terms of value of the global carbon market and also worked as the driver of the global credit market and in that triggered investments in emission reduction projects today indirectly linking 147 countries to the EU ETS through JI/CDM projects. However, a review of the EU ETS showed that it is necessary to reinforce and update the system so that it can respond to the new targets assigned to it.

The proposed amendments to the EU ETS Directive are guided by **three overall objectives** to be achieved:

1. Fully exploiting the potential of the EU ETS to contribute to the EU's overall greenhouse gas reduction commitments in an economically efficient manner;
2. Refining and improving the EU ETS in the light of experience gathered;
3. Contributing to transforming Europe into a low greenhouse-gas-emitting economy and creating the right incentives for forward looking low carbon investment decisions by reinforcing a clear, undistorted and long-term carbon price signal.

**The scope of the EU ETS:** under the proposal, the scope of the EU ETS would be extended and would cover greenhouse gases other than CO<sub>2</sub>, as well as all large, polluting industrial installations. According to the Commission, the emissions trading system should only be extended to emissions which are capable of being monitored, reported and verified with the same level of accuracy as applies under the monitoring, reporting and verification requirements currently applicable under the Directive.

To ease the administrative burden, industrial installations which emit less than 10 000 tonnes of CO<sub>2</sub> will not be included in the system, subject to equivalent measures being implemented to ensure an adequate contribution by these installations to reduction efforts.

Furthermore, installations which undertake the capture, transport and geological storage of greenhouse gases should be covered by the system. Note that the current proposal does not include emissions due to shipping and road transport.

**Monitoring, Reporting and Verification:** the proposal contains measures aiming to improve monitoring and reporting rules, to harmonise rules for verification and accreditation and to update compliance provisions, in order to ensure that the penalties for non-compliance remain sufficiently high to ensure that the market functions properly. It also aims to increase confidence in and credibility of the EU ETS with a simple and robust registry system. With this in mind, EU ETS allowances issued from 1 January 2013 onwards should be held in the Community registry.

**Further Harmonisation and Increased Predictability:** the current system based on national cap-setting does not provide sufficient guarantees that the emission reduction objectives endorsed by the European Council will be achieved. It is therefore proposed to establish an EU-wide cap in the Directive. It also provides a long-term perspective and increased predictability, which is required for long-term investments in efficient abatement. This can be best achieved by an 8-year trading period until 2020 and a linear reduction of the cap that continues the reduction path beyond 2020, thereby giving a clear message to investors. The linear reduction which is consistent with this principle amounts to 1.74% per year, arriving at a reduction of 21% below reported 2005 emissions.

The Commission considers that auctioning should be the basic principle for allocation. In the power sector – responsible for a large proportion of emissions – full auctioning of quotas should be the rule from the launch of the new system in 2013. The majority of other industrial sectors, as well as aviation, will gradually be included in the auctioning system, which will be achieved by 2020.

Member States will be responsible for the auctions and the revenue will be transferred to their respective Treasuries. These auctions will, however, be public: all European operators will have the right to buy quotas in any Member State. Auctions will generate significant revenue for the Member States and will contribute to the process of adjustment to a carbon-free economy by supporting research and development and innovation in fields such as renewable energy and carbon capture and storage, by supporting developing countries and by helping those with lesser means to invest in more efficient energy measures. Member States should commit to dedicating at least 20% of their revenue from auctions.

Finally, the proposal contains measures aiming to establish links with emission trading systems in third countries, and on appropriate means to involve developing countries and countries in economic transition.