

David Buchan

Oxford Institute for Energy Studies

The EU climate and energy deal

- Overall effect on the ETS: less allowance auctioning = less auction money. Previous estimate Euros 30bn-50bn a year by 2020, now maximum of Euros 30bn.
- Consequence for global climate negotiations Poznan-Copenhagen. Harder for EU to find money for developing countries to induce them to sign up to a global deal. Vague EU promise to earmark 50 % for climate change purposes, but this will be 50% of smaller total.
- Will more free allocations undermine the 20% emission cut target? Formally no, because no increase in overall allocations.
- But could free allocations undermine the target indirectly by weakening the ETS carbon price? Less auctioning may mean lower volume/liquidity on the market and weaker prices, although Commission claims deal provides certainty of a market to 2020.

So just as well there is a renewable target.

- Controversy about whether the Commission was right to have proposed the renewable target as well the emission reduction target.
- Many economists argued having only one (emission) target would have been more efficient. Also possible conflict between the 2 targets. Because the renewable target could depress the ETS carbon price by artificially depressing demand for carbon permits.
- The main electricity generators also argued against a renewable target.
- But, in addition to the energy security and technology justification for renewable target, there is now greater uncertainty about relying too much on the ETS to deliver the emission target. The free allowances have conditions (benchmarking, investment requirements), but this is because they reinforce the status quo by providing a financial cushion.

Concessions to Poland (& other new members) in the power sector

- Auctioning for power sector to start at 30% in 2013, rising to 100% by 2020 for states ill-connected to EU grid or relying 30% on single fossil fuel. But on following conditions:
- Free allocations to be deducted from quota of allowances for auction.
- Invest in modernisation up to market value of free allocations.
- Free allocations only up to benchmark based on weighted average of most CO₂ efficient power generation. (In Poland the weighting can reflect dominance of coal). Generators wanting extra allowances beyond this benchmark must buy them at auction or on the ETS.

Subsidising CCS plants

- Best place to store CO₂ is under North Sea, so British and Dutch pushed for higher allowances to reward CCS operators. Summit agreed on 300m allowances (worth Euros 4.5bn at today's ETS price), but not on rate of subsidy. Ought to be of interest to Poland also.
- Summit also agreed a guideline on national state aid to the effect that governments could use auction revenue to pay for up to 15% of the total cost of new efficient power plants that are CCS-ready. The green groups dislike this - because of the encouragement it could give to coal, but for that reason the plan should be of interest to Poland.

Redistribution of auction rights (solidarity)

- Most (88%) of auction rights will be handed to all 27 member states in proportion to their past emissions.
- New member states were already due, under the original Commission proposal, to share out a further 10% of total allowances for auction.
- In response especially to Hungary – which wanted credit for past emission reductions under Kyoto – an extra 2% of total allowances for auction will go to new member states. 27 % of this extra 2% will go to Poland.
- This is in addition to the 2 other forms of burden-sharing: a) in sectors outside the ETS new member states can expand emissions, while old member states have to reduce emissions, and b) new member states have renewable targets that are less “stretching” than for old member states.

Concessions elsewhere

- Industry outside the power sector and not at risk of carbon leakage will have auctioning starting at 20% in 2013 and rising to 70% in 2020, and only 100% in 2027.
- Sectors judged to be at risk of carbon leakage if carbon costs add more than 5% to costs and if non-EU trade intensity is over 10%. Commission says these criteria apply to 90% of EU manufacturing. Free allocations up to benchmark level.
- Increased right to import credits under the Clean Development Mechanism for 11 EU states with high or difficult targets in increasing renewable energy or in reducing non-ETS emissions. Example of Sweden: Renewable target of + 49% (from 40% today), non-ETS emission reduction – 17%. Increasing the supply of credits/allowances will tend to weaken ETS price.

Volatility in the carbon price

- Weakening factors: a) Increased import of CDM credits from outside, and b) more free allocations and less volume/liquidity in the emissions market.
- Current recession is weakening today's price, but will be over by 2013.
- For fear of too high a carbon price, Poland suggested keeping the ETS price within in a 'corridor' with member states adding/subtracting allowances or speeding up/slowing down rate of auctions. Like a central bank managing the supply of money to influence the price of money (the interest rate).
- Wise of the EU not to adopt this Polish proposal. Constant state intervention, or the risk of it, would undermine confidence in the market. Better to meet Poland's concern by giving it exemptions from part of the system rather than by rigging the whole system.

Renewable energy targets

- National targets unchanged by summit. Both Poland and the UK have a target of 15% (of total energy consumption) by 2020, but UK starting point is under 2% while Poland's is 7.2%.
- Controversy in Poland, with some claiming power costs to Poland of EU policy were exaggerated by the assumption that the 15% target would have to be met in the electricity sector alone.
- Parallel in UK: recent House of Lords report said UK renewable programme was too focussed on the electricity (through intermittent wind power that requires back-up investment) and not enough on renewables in heat and transport.

Renewable energy trading

- EU missed opportunity to bring in unified system for cross-border trading in renewables as it has done for emissions with the ETS. Clearly harder to do this with 27 national renewable support schemes compared to only 2 national emissions schemes (UK, Danish) that predated the ETS. But EU-wide trading of ‘green power’ could have saved up to Euros 8bn a year according to the Commission.
- Crucial opposition from big operators of feed-in tariff schemes (Germany, Spain) to any EU-wide system under which they might lose control of their national schemes.
- So on basis of a Polish-UK-German proposed compromise, now to have government-controlled (like Comecon) trade or exchanges of renewable credits, or statistical transfers, joint projects or joint support schemes.

Biofuels

- Minimum 10% renewable share of transport fuel maintained, but this must meet a rising threshold of greenhouse gas saving over conventional petrol/diesel – starting at 35% and rising to 50% by 2017, with a 60% GHG saving for production facilities opening in 2017.
- Biofuels produced on certain types of land particularly good at storing carbon i.e. forests, wetlands cannot be counted towards the 10%. In addition, the Commission will report on the extent to which biofuel production in the EU is increasing the need to produce food elsewhere (the ‘displacement’ effect).
- Critics of biofuels (esp. in the European Parliament) hope that progressively tougher environmental criteria will limit production of 1st generation food-based biofuels, to the advantage of 2nd generation wood-based biofuels or green electricity powered cars/trains.

Managing east-west tension in the EU

- Further difficult energy adjustment for new member states, on top of their switch since 1990 from command-and-control economics of communism. This was recognised by the other EU states at the Brussels summit.
- A climate policy that meets the needs of new member states is important, given that other aspects of EU energy policy often seem to eastern and central Europe either irrelevant (market liberalisation) or non-existent (energy security).
- But new member states should remember the climate stakes go beyond Europe, that the EU is trying to set an example and be a model for world agreement on differentiated responsibilities between richer and poorer states.