



# The EU Market

*Public Forum: International Linking of Emissions Trading*  
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# Brief overview on EU ETS

- Cap-and-trade type scheme ...
- Operates in stages:  
phase I (2005-07), phase II (2008-12), phase III (2013-2020) etc.
- Covers 11,500 installations, about 45% of the EU27 total CO<sub>2</sub> emissions (2.2 Gt CO<sub>2</sub>e)
- Banking between phase I and phase II was not to allowed (Poland challenges EU Commission decision) but from 2008 unlimited
- Allocation rules given by EU Directive:
  - up to 95% for free 2005-07 and 90% in 2008-2012, rest option to auction, more auctioning in 2012-2020
- National Allocation Plans for phase I and II:
  - Define ET-budget (Macro) and rules on installation level (Micro)
  - To be approved by EU Commission
- Harmonised financial sanctions for non-compliance (100 €/t) + surrender missing allowances + public notification
- EU Commission proposal for Phase III

# EU Position on linking

- Positive attitude towards linking even to non ratifying countries
- Commission Communication COM(2006) 676, *Building a Global Carbon Market*. “*extending arrangements for linking emissions trading schemes to other mandatory emission trading schemes in third countries capping absolute emissions at national or regional level,*” be they “*planned or in operation.*”
- International Carbon Action Partnership (iCAP): working towards a global carbon market

# Legal basis for linking the EU ETS

Art 25(1) of ETS Directive: agreements should be concluded with third countries listed in Annex B to the Kyoto Protocol which have ratified the Protocol to provide for the mutual recognition of allowances between the Community scheme and other greenhouse gas emissions trading schemes in accordance with the rules set out in Article 300 of the Treaty.

Where an agreement referred to in paragraph 1 has been concluded, the Commission shall draw up any necessary provisions relating to the mutual recognition of allowances under that agreement in accordance with the comitology procedure referred to in Article 23(2) of ETS Directive.

# EU ETS Linkages

- **Bilateral linkages / Integration:**
  - Norway
  - Iceland
  - Liechtenstein
  - Linking agreements theoretically possible with Australia, Switzerland, Canada, Japan, Russia, Ukraine, Monaco, New Zealand
- **Unilateral linkages:**
  - Chicago Climate Exchange
- **Indirect linkages**
  - via Clean Development Mechanism (CDM), Joint Implementation (JI) and Emissions Trading
  - New Zealand

# EU ETS - Australian linking options

- Direct linking
  - Over Article 17 KP trading (government level only)
  - Bilateral link (fully link on company level)
  - Unilateral link (e.g. allowances of EU ETS can be used in Australian scheme for compliance but not the other way around, will need agreement from EU)
- Indirect linking
  - Project based mechanism of the Kyoto Protocol (CDM, JI)

# Direct Linking issues for Australia – EU ETS

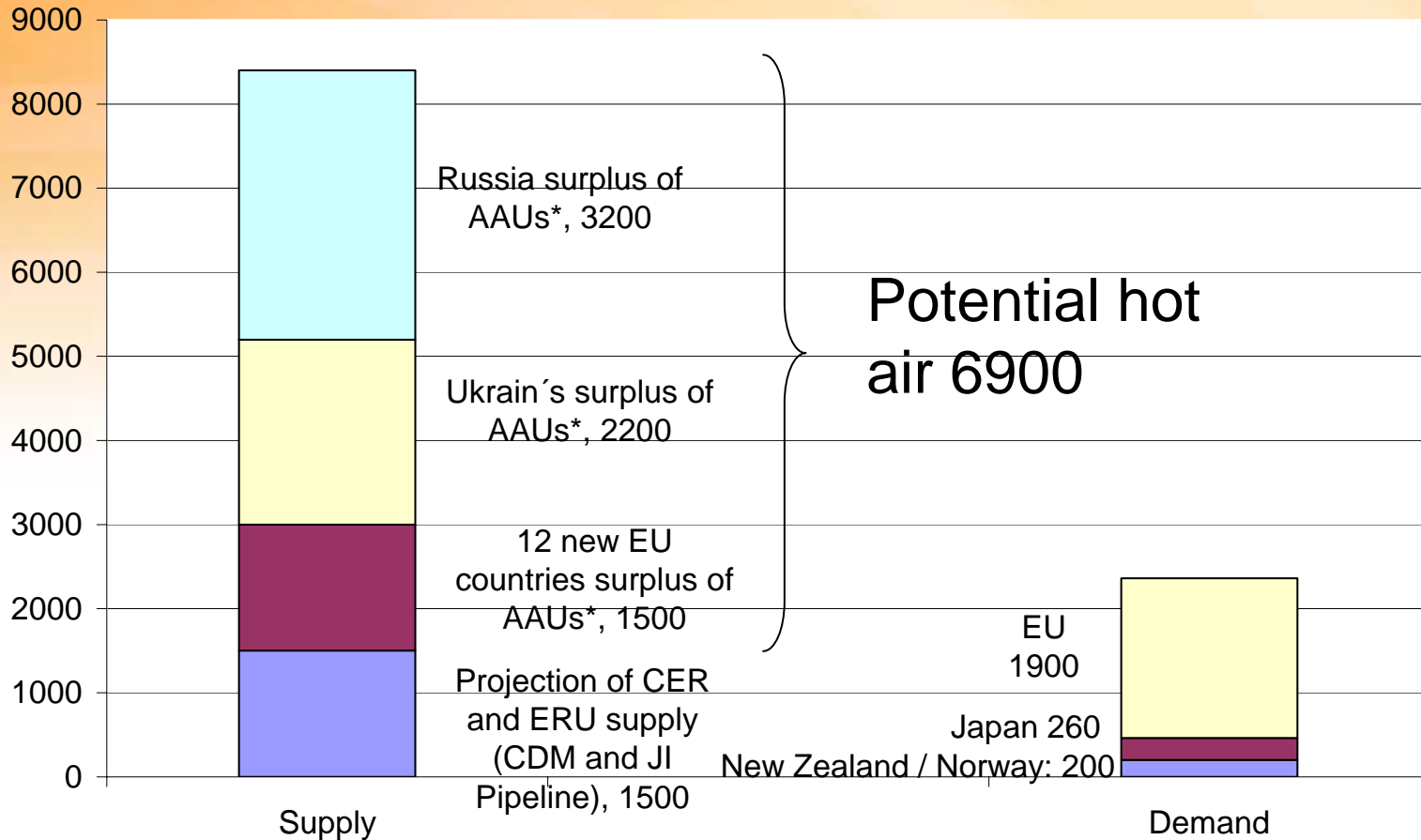
- Units used
  - Tagged AAUs (e.g. EUAs), AAUs, ERUs, CERs, RMUs, national units **HOT AIR ISSUE**
  - yearly vintages, compliance phase based units
- Complementarity: limit on use of Kyoto Units
- Banking and borrowing: EU allows unlimited banking, no borrowing between phases
- Coverage: inclusion of forestry and agriculture (currently not included in EU ETS)
- Monitoring, Reporting and Verification: equal stringency and transparency important
- Level and types of sanctions/penalty: no price cap in EU ETS (make good provision and penalty)
- Communication between registries (Kyoto Protocol standards)



# Risk of linking: Hot Air

- Hot air is the surplus of Assigned Amount Units resulting from restructuring of former Soviet Union
- Risk of lowering environmental effectiveness of schemes if linked
- Two options to bring hot air into company trading:
  - Assigned Amount Units (AAUs) are directly allocated to companies
  - Companies can exchange national permits for AAUs
- Options to keep hot air directly out:
  - EU ETS does not allow AAUs for compliance only EU tagged AAUs
  - Eastern European Hot air not allowed to be allocated

# Supply and demand (Mt CO<sub>2</sub>e 2008-2012)



# Conclusions

- EU ETS open for direct and indirect linkages
- Unilateral linking needs agreement
- Some (direct and indirect) linkages exist today
- Design differences do matter for linking: forestry inclusion could be potential problem for Australian – EU ETS linking
- Complementarity and Hot Air obstacle for linking with NZ
- Linking will make the national market depending on political decisions (e.g. target) in the other linked markets
- Linking will make systems more complex and therefore supply – demand less predictable



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