

EEX Consultation Response:**EU climate ambition for 2030 and the design of certain climate and energy policies of the Green Deal**

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EEX is the leading energy exchange in Europe and part of EEX Group, the largest electricity exchange, the second largest CO₂ exchange and third largest gas exchange in the world. EEX develops, operates and connects secure, liquid and transparent markets for energy and commodity products. At EEX, contracts on power, emission allowances as well as freight and agricultural products are traded or registered for clearing. EEX is part of Group Deutsche Börse.

EEX is involved in the EU ETS through its appointment as the Common Auction Platform for 25 EU Member States, as well as, the Opt-out Platform for Germany and conducting auctions for Poland, and as a secondary trading platform for emission allowances. Beyond Europe, EEX is actively supporting emissions market developments in China in collaboration with local partners. In North America, EEX Group's Nodal Exchange, in cooperation with IncubEx, develops and offers a wide range of environmental products for the North American market including trading in California and RGGI carbon allowances. From this perspective, EEX takes a global perspective on carbon pricing. EEX is a strong advocate and active supporter of increased cooperation and mutual learning between different emissions trading systems as a key policy tool to achieve global emissions reduction targets.

EEX supports increasing the EU's 2030 target for greenhouse gas emission reductions

EEX welcomes Europe's 2050 carbon neutrality ambition as a pivotal step to assert its role as global climate action leader. Energy markets, and in particular power and emissions markets, will be a key instrument in delivering on Europe's long-term climate ambitions. Against this background, EEX supports increasing the EU's 2030 greenhouse gas emissions reduction target to at least 55%. Achieving at least this level of ambition will be key not only to the EU's own climate policy efforts, but also to global cooperation with partners to reduce emissions and ultimately deliver on the goals of the Paris Agreement on climate change.

Emissions trading will be a key element for delivering on increased climate ambition

The EU ETS is the EU's central climate policy instrument, covering nearly half of EU emissions in 11,000+ installations at 7,000+ companies. It has delivered on the set reduction targets and guarantees an emissions reduction of 21% in the included sectors until 2020 compared to 2005. This is in contrast to emissions reductions in non-ETS sectors, where results are mixed. Despite widely diverging targets from a 20% decrease to a 20% increase in emissions, several member states are unlikely to meet their 2020 emissions reduction obligations in non-ETS sectors. While trading of annual emission allocations between member states can to some extent balance this afterwards, it is only a less efficient second-best option with limited transparency and costs which are difficult to predict. Against this background, emissions trading as a policy instrument will have a key role to play in achieving the EU's increased 2030 greenhouse gas reduction target, with focus on using the full potential of the joint EU ETS.

A strong carbon market price signal is key to efficient emissions reductions

The emissions trading price signal is the basis for the efficient attainment of greenhouse gas reduction targets, with free market pricing on the wholesale market being decisive for this. Combining diverse sectors with a multitude of emissions reduction options in one trading system ensures emissions are reduced at the lowest possible economic cost through a single, cross-sectoral price signal. Despite significant policy reforms in the past, the EU ETS has retained its nature as a volume-based cap and trade system with free price formation. This approach is the basis for the liquidity of the market, diversity and number of market participants in the system. For upcoming EU ETS reforms, it is of fundamental importance to the system's continued success to continue with this volume-based approach.

Hence, for the EU ETS to contribute its share to the 2030 climate target it's most important to set the cap at a level in line with ambitions. Market participants can then use the available short- and long-term trading products to efficiently manage their exposure to the carbon price signal, in parallel to other commodities. The Market Stability Reserve, based on volume triggers, provides an additional policy to manage market volumes.

We see proposals to add additional steering elements, such as a carbon floor price, critically. While different design options have been presented, an auction floor price would simply be another policy to manage volumes by withholding allowances, with interactions with the MSR difficult to predict. Additional risks and unintended consequences could arise from limiting market participants' possibilities to buy allowances in the auctions at regular and predictable intervals. In addition, introducing an auction floor price would only indirectly have an effect on secondary market price formation. This again shows that carbon floor prices fundamentally aim at reducing allowance volumes, which can be more efficiently dealt with through initial cap-setting in line with emission reduction targets. This would also facilitate future linking of trading schemes by avoiding additional complexity.

The EU ETS should be the backbone of the Europe's recovery plans

Commodity markets have proved to react well to the COVID-19 pandemic. Markets allowed businesses big and small to quickly adapt their strategies and operations to the rising volatility and fall in demand. In particular, the EU ETS price decreased in response to lower demand for allowances – exactly how the market was designed to respond to a drop in demand. This means that emissions reductions can be achieved at lower cost while the economy is recovering without putting at risk attainment of emissions reduction targets. The current crisis is the opportunity to establish the ETS as the backbone of climate action in Europe going forward. An extended and more comprehensive ETS could be used as the foundation of a European market-based approach to public support, making state aid conditional on transparent and shared criteria.

Emissions trading should be expanded to additional sectors of the economy

Today, emissions trading already provides a cross-sector price signal which can be expanded to further sectors. The entire EU ETS design is based on expandability both in a geographic and in a sectoral respect. In a geographic respect, the EEA-EFTA states (Iceland, Liechtenstein and Norway) have been included in the system. In a sectoral respect, the EU ETS has already been expanded several times both at a national and at a European level. Examples of this are the inclusion of air transport and of the aluminium sector at a European level and the national expansion with additional plants from the heating sector in several member states.

The EU ETS offers three options for expanding CO₂ pricing: Firstly, the joint expansion of the EU ETS with new sectors at a European level; secondly, the national “opt-in” of sectors into emissions trading; and thirdly, the creation of a specific ETS for additional sectors of the economy – separately from the existing EU ETS.

Inclusion in the EU ETS preferred option, national policy initiatives can be an intermediary step

From a market perspective, the preferred option for implementing carbon pricing in additional sectors is their inclusion in the EU ETS. As outlined above, wide sectoral coverage encompassing a great number of diverse market participants optimizes the efficiency of emissions reductions. Differing emissions reductions cost in different sectors show the potential of this, they are not an impediment to integration. It’s also important to note that while the EU ETS is the EU’s central climate policy instrument, it will not be the only policy to decrease emissions – as an example, CO₂ standards for cars will continue to exist.

Expanding the EU ETS to additional sectors offers the possibility to introduce a cap on carbon emissions for additional sectors for the first time, a real paradigm shift. Additional sectoral coverage can support linking of trading schemes, as the system becomes more attractive for global partners to link with. With EU ETS expansion, the market as whole including all market participants directly benefit from a larger, more efficient market with increased liquidity. This also contributes to fostering innovation in the market and increases support for carbon pricing in general. Against this background, EEX expressly supports the European Commission’s proposal to extend the EU ETS to additional sectors such as transport and heating.

Besides joint European level action, national opt-ins of sectors are a potentially faster way to include additional sectors in the EU ETS. Several studies¹ have recently discussed the benefits of this approach. These have found that, upon the approval of a national opt-in of sectors (such as transport or heating), the EU Commission could also permit other member states to directly integrate these sectors into the EU ETS at a national level. This could quickly lead to a dynamic development which would require the member states to “put their cards on the table” regarding their respective climate policy ambitions. Under this method, national measures will support the common European approach to reducing emissions.

Finally, establishing national or regional emissions trading schemes at first can also be a suitable intermediary step towards inclusion in the EU ETS. For such systems, policy compatibility and a clear commitment and timeframe for swift integration should be key principles of policy design right from the start.

Increased climate ambition should be combined with increasing the auctioning share

Auctioning is the default allocation method for allowances in the EU ETS. It is the most transparent allocation method, providing a transparent, harmonised and non-discriminatory process. The principle of auctioning, and the objective of gradually moving to full auctioning, is fundamental to the objective of emissions trading as it guarantees costs of carbon are internalized. Therefore increased climate ambition should also be used as an opportunity to increase the share of allowances which is auctioned to a higher level than 57% as currently foreseen for Phase IV. A linear and continuous increase of the auctioning share during the trading phase would provide the greatest possible predictability for market participants.

¹ See „Rechtliche Optionen und Konflikte einer Einbeziehung des Straßenverkehrs in den Emissionshandel“ (Ohms Law Firm); „Die Einbeziehung des Transportsektors in das Europäische Emissionshandelssystem“ (Prof. Dr. Nettesheim)

This is all the more relevant given that auctioning revenues make a significant contribution to climate action in Europe. In 2019, revenues from EU ETS auctioning amounted to more than 14.6 billion Euros. Member States spent around 80% of revenues for climate and energy related purposes between 2013-2018².

Global cooperation in carbon pricing and climate diplomacy need to be further intensified

Over the last few years, we have seen a rapid increase in carbon pricing globally, in particular in form of emissions trading schemes. There are now 21 systems covering 29 jurisdictions with an ETS in force. While significant differences in policy exist globally, the global policy landscape is gradually moving closer towards the vision of global carbon pricing. This also offers significant potential for cooperation between different trading schemes, for instance in the form of linking. The joint European approach of the EU ETS forms the basis on which Europe can use these opportunities. Encouraging such global cooperation needs to be a core priority for all stakeholders. A successful example is the completed link of the EU ETS with the Swiss ETS which went into effect in 2020. A possible link could also be established between the EU ETS and a future UK ETS, as both sides have stated their wish to link their systems. Significant opportunities also exist beyond Europe, in particular in cooperation with China on climate policy which should be further explored during the upcoming German Presidency of the Council of the EU.

Contact

Daniel Wragge

Director Political & Regulatory Affairs
daniel.wragge@eex.com

Timo Schulz

Senior Political & Regulatory Affairs Advisor
timo.schulz@eex.com

Transparency Register ID 09579576238-53

² Report on the functioning of the European carbon market, COM/2019/557 final/2