

UK Business Council for Sustainable Energy

Outline of Key Principles for EU ETS Phase II

The scientific community is now indicating that it is essential that significant reductions in carbon emissions are achieved by 2050. This will require significant investment shifts across the economy. This is particularly so in capital intensive sectors such as the energy sector.

It is therefore vital that market based mechanisms such as the EU Emissions Trading Scheme (EU ETS) – which the UK Business Council for Sustainable Energy¹ fully supports – are effective at delivering long-term reductions in carbon emissions. EU ETS needs to send strong, enduring and consistent signals to Industry to invest in a low carbon future.

Investment in a low carbon future will only occur if industry has confidence in the trajectory of the EU ETS beyond Phase II. To reinforce the UK on this pathway Phase II needs to establish a reasonably enduring and simplified set of market rules. These need to set the long-term architecture and direction for the mechanism for subsequent Phases.

To achieve this, we believe the following needs to be addressed:

The cap:

- The cap should be based on what the science suggests is needed and should be underpinned by realistic and accurate energy projections, formulated in close consultation with Industry.
- The size of the traded cap should be made known as soon as possible.
- There needs to be genuine burden sharing across all sectors, including the non-traded sector.

New entrants and closures

- Government needs to give early indication of its treatment of new entrants in Phase II.
- A new entrant reserve needs to be of a realistic size, and based on calculations that are genuinely transparent and understood;
- Decisions on new entrants will also have implications on Industry decisions to close plants, and Government must be aware of these implications and craft the closure rules accordingly.

¹ UKBCSE members are: Centrica, EDF Energy, E.ON UK, National Grid plc, RWE npower, Scottish Power, Scottish and Southern Energy, and United Utilities.

Allocation methodologies

- Allocation methodologies should be fair, consistent and simple:
 - *Fair*, in terms of not arbitrarily penalising market participants, and that broadly similar installations should be given broadly similar allocations to avoid the inadvertent distortion of competitive markets;
 - *Consistent* with the objective of EU ETS to send signals to invest in a low carbon future; and
 - *Simple* in terms of providing a relatively straightforward set of rules enabling transparency and ease of compliance.
- There is a recognised role for benchmarking methodologies, and increasingly, for auctioning.
- Continued signals as to the Government's long-term intentions about auctioning are welcome. The development of a roadmap towards, potentially, full auctioning, and the rate at which the Government believes this could be achieved would further reduce uncertainty.

Other:

- No additional restrictions should be placed on JI and CDM credits as a means of meeting liabilities. However, the availability and use of JI and CDM must not be used as a justification for inaction domestically.
- Decisions about changes to the ETS, such as the expansion to include other sectors or gases, must be based on their impact on the effectiveness of the scheme.

The Council believes that the capacity of the EU ETS to operate beyond the existing Kyoto compliance period of 2008 – 2012 means that it is vital that EUETS Phase II sends clear and strong directional signals across the economy as a whole. With this, the UK and the wider EU can maintain and enhance its investment in the actions that need to be taken in order to avoid the dangerous impacts of climate change.

UKBCSE
September 2005