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DG CLIMA

Evolution of Regional Carbon Markets and International Linkages

EU Objectives: a robust international carbon market

- In parallel to and supporting the UN process
- An international price for carbon
- Significant contribution to international climate finance

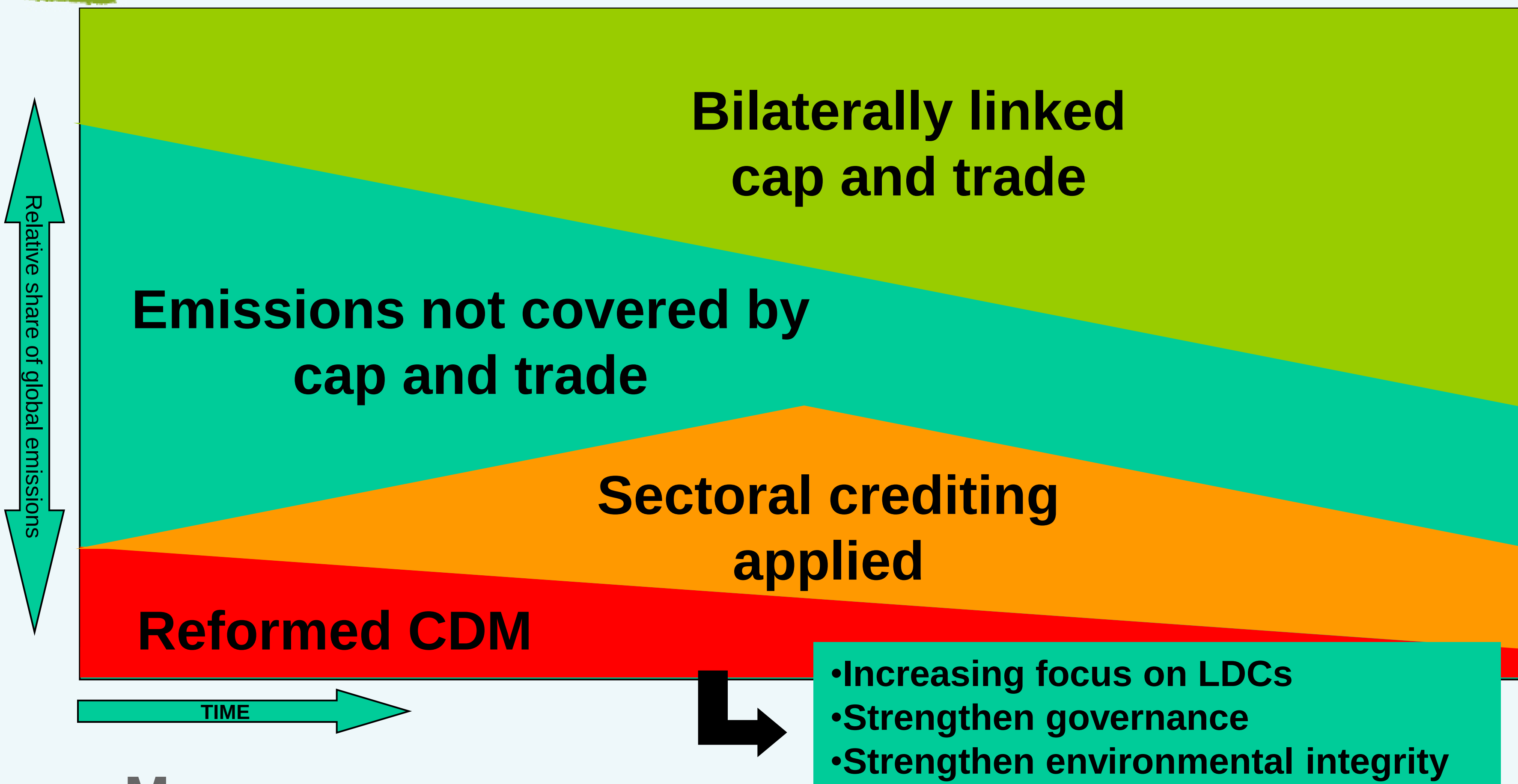
Where we are now

- EU Emissions Trading System -world's largest carbon market. EUAs were 84% of global carbon market value; EUETS drove 97% when CDM transactions included[1]
- Nucleus for the international carbon market
  - Major demand for international credits: EU private buyers account for around 80% of CDM and JI demand
  - Linking with other systems
  - Developments worldwide: RGGI, California, Switzerland, Korea, Australia, Chinese regional pilots…and growing interest eg through World Bank PMR.
  - Sharing experience for well designed systems

Building a robust international carbon market

- Through bottom up linking of cap and trade systems in developed countries
- Inclusion of advanced developing countries and competitive sectors
- Reform of CDM and replacement over time by a sectoral mechanism for advanced developing economies and sectors
- Sectoral crediting as a stepping stone to ETS

Carbon market transition



Means

- **Through UNFCCC supply-side** where possible
- **Through EU demand-side** where necessary

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EU legislation on linking

- EU ETS Directive: Art 25,1 bis and 2:

" Agreements may be made to provide for the recognition of allowances between the Community scheme and compatible mandatory greenhouse gas emissions trading systems with absolute emissions caps established in any other country or in sub-federal or regional entities."

" Where an agreement […] has been concluded, the Commission shall adopt any necessary provisions relating to the mutual recognition of allowances..."

EU linking policy

- Procedures for linking in EU legislation through mutual recognition of allowances from compatible mandatory cap and trade systems.
- In substance: no criteria for linking, although some clear areas that could cause concerns in terms of environmental integrity (level of ambition, number and type of offsets, price controls)
- In practice:
  - Linking negotiations with Switzerland (mandate from Council end December 2010)
  - Interest in other systems (eg Australia)
  - Early indirect linking through recognition of the same international credits

Working towards compatible systems: ICAP

- Public authorities committed to cap and trade
- Technical exchange on best practice to improve design and promote compatible systems

Members:

- EU: European Commission, Denmark , France , Germany, Greece , Ireland, Italy , Netherlands , Portugal , Spain , United Kingdom
- North America:
  - Regional Greenhouse Gas Initiative Members (RGGI)
  - Western Climate Initiative Members (WCI)

And Australia, New Zealand, Norway, Tokyo Metropolitan Government

Observers: Japan, Korea and Ukraine

See www.icapcarbonaction.com

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INTERNATIONAL icap Carbon Action PARTNERSHIP

Integration of aviation in the EU ETS

- The coverage of EU Emissions Trading System will be extended to aviation
  - Internal, outgoing and incoming flights
  - Legislation was agreed in 2008 and Implementation work is well on track
    - benchmark values for free allocation published last week
  - Incoming flights can be exempted where equivalent measures are in place
- EU is moving ahead, whilst being keen to collaborate with and further progress in ICAO to address global aviation emissions
- Approach is consistent with CBDR principle and ensures fair competition in international aviation
  - All flights between Europe and a given third country destination covered, independent of the airline operating the flight

Indirect linking: coordination of recognition policy is essential

- The number and type of international credits that we allow for compliance in our ETS
- An important incentive, if used responsibly, to support more ambitious action in emerging economies
- Use to ensure that demand supports progress in UN negotiations
- Coordination essential
- Key issue for linking: credits allowed into one system are allowed into linked systems

Quantitative use of international credits

- Under unilateral -20% target:
  - EU ETS in 2008-20: a quantity of approx 1600 million tonnes
  - In addition, approx 700 million tonnes additional quantity in non-ETS under Effort Sharing Decision
- Increased use of credits (CDM/JI/other) by up to 50% of the additional reduction effort in case of new international agreement (-30% target)
- Supplementarity: use of international credits should not exceed 50% of reduction below 2005

EU demand-side:
More selective use of credits

Provisions in EU ETS

- CDM projects registered prior to 2013 can continue to generate eligible credits
- Credits from CDM projects registered after 2012 can only come from LDCs
- No ERUs after 2012 without new QELROs
- Exceptions:
  - Provision **to restrict use** of specific credits from project types decided in CCC
  - Provisions for **bi- or multilateral agreements** for supply of credits (sectoral) if no international agreement concluded by 12/2009
- Once there is an international agreement
  - only credits from projects in third countries that have ratified agreement
  - types of credits agreed will be subject to a common EU approach

To conclude

- A strong international carbon market is needed, which will develop in parallel to the UN process
- Through bilateral linking of compatible domestic cap and trade systems
- Domestic ETS debates ongoing across the world, including in emerging economies: focus now mostly on developing robust domestic policies
- Indirect linking and the responsible recognition policy is an area where coordination is also needed now.