

Tackling climate change through ETS

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MORE than half a century ago it was energy - through the European Coal and Steel Community - that provided Europe with the means with which to rise to the enormous challenge of rebuilding a divided and war-ravaged continent. Today, it is energy once again that is set to unite Europe in its biggest challenge yet - the fight against climate change.

Last week the European Commission outlined the devastation that could be wrought across the continent as a result of global warming. From being one of the most fertile parts of the globe, there is a real possibility that huge areas of Europe could be plunged into environmental chaos with soaring temperatures rendering many areas uninhabitable and putting pressure on the very resources that are necessary for our existence; food and water.

And as the Stern report last year made clear, the economic consequences too are dire - we must invest now to save billions later. So the cuts in greenhouse gasses proposed by the European Commission are extremely disappointing to those of us who understand that if we are to keep temperatures below the two degree increase that would spell disaster, we have to be radical in our approach now, and that the EU needs to give courageous global leadership on this front.

The EU's main tool for tackling global warming is the Emission Trading Scheme (ETS), a scheme that has been brewing for about fifteen years and currently covers around half of the EU's carbon dioxide emissions, including those from electricity production. Under the current cap and trade system, heavy carbon users are allocated - for free - a set amount of carbon. If the industry or company expends less carbon they can sell the excess on the open market, while the 'bad guys' who exceed their allocation must buy the excess allocation.

This carrot-and-stick approach - penalising the bad and rewarding the good - is proven. Chicago's market in sulphur dioxide has helped to cut US sulphur emissions by 18 million to 9 million tonnes and the UK's experimental ETS saw voluntary participants over-achieving their annual targets.

But ETS is still very much in its infancy and there are unquestionably many problems with the current scheme. It is incredibly complicated; it allocates allowances free - contrary to the fundamental EU principle that the polluter should pay; it is limited to certain sectors and excludes key others - most notably transport and aviation.

Moreover, Member States are not making equal sacrifices which has led to market distortions and allowed windfall profits to be made by some. High-energy users who compete globally also face unfair competition from imports that do not have such systems. Nevertheless, ETS remains the only game in town; it can and it must be made to work.

There is widespread consensus that ETS needs to undergo a thorough review. Not least, the 2008-2012 period must see a much tighter allocation of carbon credits through the National Allocation Plans (NAP). At the moment there are very few Member States who take the system seriously. In fact, almost every Member State has recently had its NAP returned with only four out of 25 member States giving targets lower than their actual current emissions.

The methodology used in NAP allocations must also be standardised. Some member states fear that it will affect their industry adversely. But, after all, that is the point. The whole system needs to be geared so that future investments follow a low carbon route rather than pursue traditional investment patterns.

The crunch time for a fundamental review, however, will come prior to the start of the 2012 phase - the post-Kyoto strategy. At that point we must have a system that is credible, flexible and predicable. By then there must be a commitment to move towards full auctioning of credits. This could raise billions for the coffers of the EU or Member States, which could be earmarked

to tackle the EU energy issue, and in particular to contribute to the lamentable amounts currently spent on energy research and development.

Some of the money could be used to transfer clean technology to developing countries and emerging economies. It could also incorporate other large energy using sectors, in particular aviation and possibly surface transport, but equally could cut down on others currently included. In the UK 50% of the current installations covered contribute only 0.8% to the overall carbon emissions.

There is also a need for a clear long-term framework. Investors are making decisions today, for example on building conventional coal plants, which could lock in carbon for the next forty years. We need to give long-term signals on the price of carbon to drive the investments into the correct places.

We know that to meet the two degree target we have to make cuts of 30% by 2020 and 60-80% by 2050. The EU must allocate only as many carbon credits as is necessary to meet these targets. At the same time we also need to consider EU sectoral protection for high-energy industries like steel, which will simply collapse in the face of global competition.

The challenge is on during the German Presidency to deliver on the vision for a post-2012 framework of commitments, setting the EU's own clear standards and at the same time setting an example for the world while pushing for urgent international agreement. Climate change is a global challenge which requires a global solution. With the right focus the EU ETS can become the basis of this global action.

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