



Update

# **Barriers to Emissions Trading under the EU ETS**

EFET: Emissions Trading Task Force

June 15, 2004

# GENERAL COMMENTS

KEY	DESCRIPTION
Complete & Transparent	<ul style="list-style-type: none"> <li>• The National Allocation Plans (NAPs) have to be published (preferably in English) and have to be "complete" and "transparent"</li> </ul>
List of installations	<ul style="list-style-type: none"> <li>• Every NAP has to have a complete list of installations (name, address, place and assigned rights) which fall under the EU ETS to create clarity</li> </ul>
Freeze NAP	<ul style="list-style-type: none"> <li>• Freeze the NAPs for the first period (3 years) to create certainty in the market regarding the number of allowances on the market</li> </ul>
Use reserve	<ul style="list-style-type: none"> <li>• If installations are forgotten or have to be handled differently use the reserve for this</li> </ul>
Allowances per NAP	<ul style="list-style-type: none"> <li>• The national authorities should publish the total amount allocated and the total amount that is in reserve (e.g. for new comers) and which could go on the market</li> </ul>
NAP Period II	<ul style="list-style-type: none"> <li>• Develop and publish as early as possible (early 2006) the NAPs for the second period.</li> </ul>

# BARRIERS TO EMISSION TRADING UNDER THE EU ETS

- I. Uncertainty of supply/demand  
~ designed in uncertainty ~  
~ lack of clarity ~
- II. Inappropriate regulatory arrangements
- III. Fragmentation of the market
- IV. Realisation of the registries
- V. Other issues

I
II
III
VI
V

# Uncertainty of supply/demand ~ designed in uncertainty ~

## BARRIER

- The use of JI/CDM credits in the first and second Kyoto period
- The unpredictable use of reserves and auctions by the different MS can disturb the market
- Different NAP methodologies in the first and second period can undermine trading and investments
- Clarity is needed on the definition of new entrants, movements and closure of installations

## POSSIBLE SOLUTION

- No CAP on the use in the first period and provide information how to handle in the second period as early as possible
- The NAPs should be clear how the MS would treat the use of reserves when they will have an auctions under which conditions: how, when, who, how much, etc.
- The principles how to develop the NAPs for the second period should be made available as soon as possible
- The rules and definitions should be clear and harmonisation in the EU for the second period is preferred

I
II
III
VI
V

# Uncertainty of supply/demand ~ lack of clarity ~

## BARRIER

- **Legal certainty across MS which can result in fragmentation of the market**
- **There is no detailed and general product description of the EUA. Is it a commodity, financial, property, good, virtual commodity, or something else?**
- **The use of and the market activity in CERs/ERUs will not be encouraged as long as these issues remain unsolved/unclear. It hugely affects the supply/demand balance of the market, and will hence lead to less liquidity, more volatility and lower price discovery for operators**

## POSSIBLE SOLUTION

- **The legal status (similar for electricity and gas trading) can and probably will practical be solved. However, harmonisation between the MS is encouraged**
- **Linked to the legal position, it would be very useful to have clarity as to the status of EUAs across the EU and MS. A standardization of the product would improve the market**
- **Now the use of CERs/ERUs is non conditional on the entry into force of Kyoto, the EU should also commit itself more on the practical issues related: make sure a CER/ERU registry is ready, support the functioning of the CDM-EB or create an EU equivalent, speed up the process**

I
<b>II</b>
III
VI
V

# Inappropriate regulatory arrangements

## BARRIER

- **Obligations in some MS for price disclosure/transaction disclosure; transparency of the registries. If other players can the registry position in real time, then there will be problems starting the trading (as has been the case in the UK ROC market)**
- **Complex regulatory procedures which can lead to overly complex trading arrangements**
- **Onerous financial services regulation of allowance transactions**
- **Paperwork/control/legal requirements concerning the emission authority**

## POSSIBLE SOLUTION

- **Some MS are considering placing obligations which should be minimised**
- **The views of participants should be particularly useful in developing trading arrangements and avoiding unnecessary complexity**
- **Some pan-EU standardisation may avoid inappropriate regulation**
- **Some pan-EU standardisation with focus on best practice should help avoid inappropriate regulation**

I
II
III
VI
V

# Fragmentation of the market

## BARRIER

- **There is still a lack of clarity surrounding tax treatment, in particular regarding VAT which could lead to fragmentation**
- **Standardised contracts/Master Agreements**
- **Different timescales in each MS is a risk, particularly early in the development of the market which will lead to fragmentation**
- **Banking of allowances in a country from 2007 to 2008 can lead to different prices for the different CO<sub>2</sub> products and can fragment the market**

## POSSIBLE SOLUTION

- **Some standardisation, perhaps lead by EU wide guidelines could reduce this risk**
- **Experience of other traded markets suggest that a lack of standard documentation can cause barriers to trading. EFET is active in promoting standard documentation**
- **Deadlines should be published and enforced to prevent differences**
- **The general opinion in the current published NAPs is that banking is not used and it is preferred to have this for all the NAPs**

I
II
III
VI
V

# Realisation of the registries

## BARRIER

- **Uncertainty about registry performance, in particular duration of the transfer process which hinders traders to agree on transfer dates**
- **Responsibility in the case of an error made by the National and/or European registry system**
- **The MS are free to ask a reasonable price for the use of their registries which will lead to different transaction costs between MS**
- **Availability of user manuals and testing possibilities**

## POSSIBLE SOLUTION

- **Pre-condition: the registry has to be designed in such manner, that transfers can be executed are executed real time (less than 1 minute time)**
- **The (financial) responsibility of the registry should be made clear in the case of a failure**
- **The transaction cost should be standardised over Europe and kept as low as possible**
- **The participants in the EU ETS system should be able to test the system as early as possible (e.g. September 1, 2004)**

I
II
III
VI
V

# Other issues

## BARRIER

- **There will be VAT cash flow problems and there will be the issue who claims the VAT**
- **Non continuous market between the first and second period may lead to a concentration of trading close to the end periods**

## POSSIBLE SOLUTION

- **VAT problems is a known general issue in the European Union and with the start of the EU ETS we once urge the EU and the MS to work on solving this problem**
- **The use of two separate periods is fixed and banking will probably not used. It is therefore inevitable that this will happen. A possibility of reducing the effects can by publishing the methodology for the second period as early as possible**

# Process for the present update

- Starting point the document: *"Barriers to Emissions Trading under the EU-ETS"*, EFET Emissions Trading Task Force, Brussels, December 2003
- Consultation in April 2004 regarding updating the document based on the latest developments such as the draft NAPs and the "new" Linking Directive
- Discussion of the received input during the meeting on April 28 in Brussels (10 persons from 9 European companies)
- Consultation draft presentation in May under 53 EFET taskforce members
- Finalizing the updated presentation and document: *"Barriers to Emissions Trading under the EU-ETS UPDATE"*, EFET Emissions Trading Task Force, Brussels, June 15, 2004

# COMMENTS?

If you have any  
comments, remarks or suggestions  
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