Case Study

MF Case 6: EU-wide - Clean Development Mechanism

The Clean Development Mechanism (CDM), allows a country with an emission-reduction or emission-limitation commitment under the Kyoto Protocol (Annex B Party) to implement an emission-reduction project in developing countries. Such projects can earn saleable certified emission reduction (CER) credits, each equivalent to one ton of CO_2, which can be counted towards meeting Kyoto targets. It is the first global, environmental investment and credit scheme of its kind, providing standardised emissions offset instrument, CERs. A CDM project must provide emission reductions that are additional to what would otherwise have occurred. The projects must qualify through a rigorous and public registration and issuance process.

The CERs are traded on markets such as the EU emissions trading system (EU ETS). It is the the biggest international system for trading greenhouse gas emission allowances and one of the main cornerstones in the EU 2030 framework designed to help reduction in GHG emissions of industrial enterprises in a cost-efficient manner. Altogether the EU ETS covers around 45% of total greenhouse gas emissions from the 28 EU countries.

The EU ETS works on the “cap and trade”' principle. A cap works like a limit which is given to an enterprise specifying the amount of GHG that can be emitted. This cap is reduced over time to ensure a continuous reduction of GHG emissions. Within the cap, companies receive or buy emission allowances which they can trade with one another as needed. After each year a company must surrender enough allowances to cover all its emissions, otherwise heavy fines are imposed. Participation in the EU ETS is mandatory for companies operating in certain sectors, but in some sectors only plants above a certain size are included.

An over-supply of CERs occurred, largely because of the economic crisis which has depressed emissions more than anticipated. This has led to a severe decrease in prices.

The EU is taking actions to combat the oversupply of emission allowances. Even in the 3. Phase (2013-2020) the back log is not expected to declines significantly, which is potentially undermining the market substantially and thereby the ability of the EU to finance low carbon projects. Two measures are adopted to support the system:

1. Switch the auctioning to a later stage: this measure does not reduce the number of certificates but postponing the auctioning of 900 million allowances until 2019-2020 to allow demand to pick up. By shifting the auctioning to a later stage, at least in the short term, relief from oversupply is expected and prices can stabilize at a higher level.
2. Proposal of a market stability reserve: Beginning with the next trading period in 2021 a stability reserve should be in place that is able to balance demand and supply in the long term.

This structural measure would operate in a EU unified manner leaving no leeway for EU Countries to interpret the rules.

The EU endeavors to create international linkages to other national carbon markets based on compatible domestic cap-and-trade systems. The fist one of these links will be with Australia, which will become fully operational in 2018, but an interim link is expected to in place in July 2015. It would open the way for Australia to use EU allowances to cover emissions under the Australian scheme. Greenhouse gases and sectors covered are:

Carbon dioxide (CO_2) from

- Power and heat generation
- Energy-intensive industry sectors including oil refineries, steel works and production of iron, aluminium, metals, cement, lime, glass, ceramics, pulp, paper, cardboard, acids and bulk organic chemicals
- Civil aviation

Nitrous oxide (N2 O) from production of nitric, adipic, glyoxal and glyoxlic acids

Perfluorocarbons (PFCs) from aluminium production

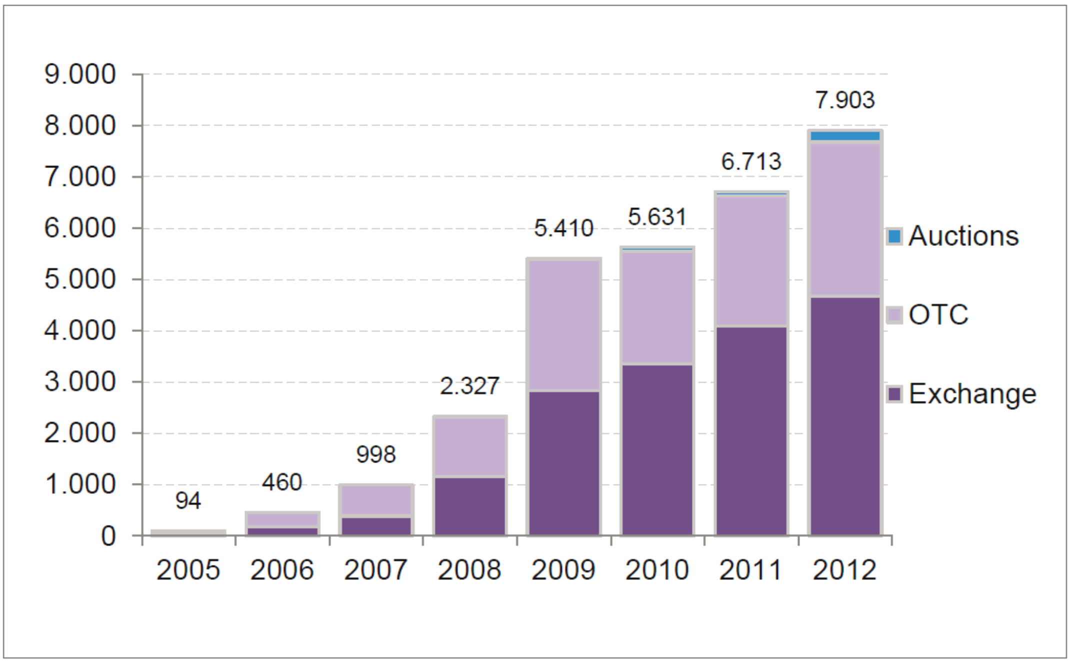
Because the EU tools are not linked to finance but mainly to monitoring and Reporting (MRR) and Accreditation and Verification Regulations (AVR) the following website is recommended which details and provides guidance to relevant topics:

http://ec.europa.eu/clima/policies/ets/monitoring/documentation_en.htm

The trading volume below shows clearly the upward trend and thus the importance of the EU ETS as a financial instrument. The relevance of carbon trading for GMF is still relatively small. It ranges between 1%-2% of overall contracts implemented. The main reason is that local authorities have only limited influence on industries. Therefore the SEAP as supported by the EU platform of Covenant of Mayors suggests excluding those industries that are covered by the ETS in the baseline analysis.

In cooperation also with the private sector initiative have started to include e.g. energy efficiency as one of the few spheres, where local governments can exercise direct influence into the overall calculation.

Trading Volume in EU emission allowances (in mill tons)



Source: http://ec.europa.eu/clima/publications/docs/factsheet_ets_en.pdf, http://mayors-adapt.eu

References

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Credentials

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