EURACOAL
European Association for Coal and Lignite
AISBL

# MINUTES

## EURACOAL'S 3rd EMISSIONS TRADING WORKSHOP

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**Participants**

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Dr. Diercks chaired the meeting. He welcomed the participants and recalled that in the first trading period 2005-2007, the individual Member States' approaches to Emissions Trading were fairly different. The Commission uses the NAP II approval process for partial harmonisation. It has already started to plan a third trading period after 2012.

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## 1. Experiences 2005-2007:

### Prices, influence on coal production and markets as well as specific national developments

During the Round Table on Phase I, the participants took the following views:

**The United Kingdom** took a rather different position than the other Member States: The Government wanted to use Emissions Trading to reduce emissions and the restricted allowances meant that a significant quantity had to be purchased. The relatively high prices for allowances in 2005 therefore provoked a temporary shift from coal to gas.

**The German Government** had decided to allocate sufficient allowances on the basis of historical emissions to all industries and established special rules for new power plants which also received free allowances.
A controversial discussion occurred when the electricity prices suddenly rose in 2005 with the argument that the prices for allowances (which were then free) had to be included into electricity prices. But even when the prices for $CO_2$ certificates went down, the electricity prices stayed the same. These developments show first that the interrelations which influence power prices are complex. Second, this simplified approach caused a debate on auctioning and on restrictions for the power industry in Phase II.

**In the Netherlands** as well, Emissions Trading did not affect coal use. When electricity prices rose, as in Germany, people thought that industry played a game with prices. Regarding NAP II, the question came up how to attribute allowances to industry. Public opinion opts for the idea that those who made the best efforts should receive more free allowances than those who did fewer efforts.

**Hungary** could fulfil its Kyoto targets already in the first trading period. Many old coal-fired power plants were closed before the accession of Hungary to the EU, which gives the industry many emissions credits compared to 1990. Especially in 2005, there was a high volume of biomass burned in power plants as the use of biomass was highly subsidised by the Government. Meanwhile, those regulations have changed, so that the possibilities to substitute coal with biomass to save $CO_2$ quotas decreased.

**The Czech Republic** shows a similar picture as the previous countries, the rather high certificate prices in 2005 came drastically down. The initial high prices had the consequence that several companies preferred to sell credits rather than produce electricity. Up to now, Emissions Trading did not have any significant impact on coal use or the general economy.

In the discussion, it was pointed out that it is difficult to draw many consequences from this period. As the $CO_2$ prices fell drastically during this period, the impact of $CO_2$ prices until April 2007 did not really represent a challenge for the EU economy. Phase II may therefore have to be regarded as another pilot phase. The Commission wants tougher emissions targets in the second trading period. The actual picture shows that 6 EU Member States (Germany, France, UK, Poland, Spain and Italy) represent 75% of EU emissions. There is a certain probability that they will achieve the given targets for 2012 but there is still no solution how to proceed after 2012.

## 2. Outlook 2008-2012:

### 2.1. Emission rights available in the EU according to NAPs

**In the United Kingdom,** the first trading period was already very tight; NAP II will be even more restricted. Drax for example will have to buy some 50% of its needed allowances for its power plant. Allowances for new entries will be benchmarked to gas CCGTs and it is certain that if $CO_2$ prices are higher than in Phase I, a switch from coal to gas will occur with regard to the construction of new power plants as well as the use of the capacity.

**In Germany**, NAP II was determined in such a way that industry will have its emissions nearly covered by the allocated allowances, the electricity sector will therefore have to carry the whole load to reduce emissions. One argument of the Government was that prices for $CO_2$ were already part of the high electricity prices, so the money was already available to buy allowances.
Allocation was changed from "historical emissions" to a benchmarking system. Therefore, the benchmarking rules were disputed. From the viewpoint of lignite, the German Benchmark system is not adequate because there are only two Benchmarks Gas (365 gr $CO_2$/KWh) and Solid Fuels (750 gr $CO_2$/KWh). This is not sufficient for lignite. It is important to prevent a fuel switch due to Emissions Trading, resulting from the Kyoto targets that would have major consequences on the European energy mix in the medium and long term. The design should promote modernisation in power generation and ask for the same effort when different fuels are used.

**In the Netherlands,** the picture looks similar. As the customers already pay high electricity prices, the Government wants to put the burden on buying allowances on the electricity industry.

**In the Czech Republic,** more than half of the electricity is generated by coal and lignite. Even if the burden on the electricity industry would be high, several trading periods would be necessary to replace the existing coal-fired power plants. It would therefore not be a solution to 'punish' the power industry.

**Hungary** just submitted its NAP II which restricts grandfathering compared with the first trading period by some 25% and which also cuts allowances for new entries. Nevertheless, the Commission already requested Hungary in its decision dated April 16$^{th}$ to further cut Hungary's allocation plan by 3,8 Mio. t/a (12,4 %) to 26,9 Mio. t/a. Furthermore, the proposed free allocation for new entries over a 6-year period is judged to become a subject of a separate State Aid investigation. As there are only few power plants planned in the near future and because of the limited potential of regenerative power it is questionable if Hungary will be able to achieve its targets. As there are no incentives and investment securities within the NAP II, Matra and its shareholders are actually rethinking their plans to build a new lignite fired 400 MW Unit.

Several general questions came up in the Member States when drawing up the NAPs II. The Member States who already achieved their Kyoto targets asked why they pay for allowances. Another concern for several Member States is the question if they will close nuclear power plants or not in the future and how these power plants could be replaced in a rather short period.

## 2.2. Role of JI / CDM, Possible influence on coal use

Nigel Yaxley gave an overview on the Kyoto Mechanisms and EUETS Phase II starting with the background and a short description of the Kyoto Mechanisms Clean Development Mechanism, Joint Implementation and Emissions Trading. Several examples were given of CDM projects worldwide, especially introducing Clean Coal Technologies. There are currently four projects under registration with regard to coal mine methane capture and utilisation and two running projects on efficiency improvement in coal-fired power plants, one Ultra-supercritical in China and one Supercritical in India.

Using the JI/CDM within the EUETS will have many benefits for the European Union: it will increase compliance options for entities, allowances prices and compliance costs will be reduced, and the EU Emissions Trading market will increase its liquidity. The system will contribute to the host countries' sustainable development and promote environmental friendly technologies in third countries. Exporting knowledge and technology will also contribute to sustainable development within the EU. Nevertheless, this should be supplemental to domestic actions which will constitute a significant element of the effort made by each industrialized country. Limits to use JI/CDM will be set up. It is estimated that some 181 million tonnes $CO_2$ from JI/CDM will be allowable per year. It is probable that JI/CDM will become a decisive balancing factor for Phase II. Additionally, it is a way of investing in developing countries. It will be interesting to observe how the development of CER prices and the percentage of JI and CDM allocated by the NAPs will influence emissions trading.

In Phase I, the over-allocation led to price collapse. Fuel, weather and economic performances will become the key price drivers in Phase II if credit supply will be less. But this could also drive to a fuel switch which would lead to a marginal emissions reduction during a given period.

The table below shows the emissions targets set up by the EU Commission compared to the emitted $CO_2$ in 2005:

| | EU-targets | $CO_2$ emissions in 2005 | Difference |
|---|---|---|---|
| Germany | 473,95 | 453,1 | -20,9 |
| France | 131,31 | 132,8 | 1,5 |
| Greece | 71,07 | 69,1 | -2,0 |
| Spain | 181,1 | 152,2 | -28,9 |
| Belgium | 54,5 | 58,5 | 4,0 |
| Netherlands | 80,4 | 85,8 | 5,5 |
| **EU-15** | **1 312,4** | **1 277,0** | **- 35,4** |
| | | | |
| Poland | 203,1 | 208,5 | 5,5 |
| Czech Republic | 82,5 | 86,8 | 4,4 |
| **New MS** | **328,2** | **348,5** | **20,3** |
| **EU-25** | **1 640,6** | **1 625,5** | **- 15,1** |

In the discussion, participants agreed that the relatively small gap between $CO_2$ emissions 2005 and the EU approved emissions may lead to JI/CDM being a decisive balancing factor. However, due to the economic development, a lack of certificates is still possible.

### 2.3. Possible EURACOAL activities

Participants recalled that after the second Emissions Trading Workshop, a questionnaire in the form of a table was sent to all members, in order to compare state-of-the-art in each individual Member State. All participants agreed to draft a similar table to exchange experiences on the NAP II Phase.

## 3. "Post Kyoto" Phase:

### 3.1. Status global negotiations on GHG , Status EU GHG and ETS policies, Future (> 2012) EU Framework for ETS and possible implications for coal

In the third part of the Workshop, Dr. Diercks made a presentation on the future EUETS framework. During COP 12 in 2006, it was decided to review the Kyoto Protocol by 2008. The EU reiterated that it would like to play a leading role in international climate protection. However, a fair and flexible global framework is needed. If other developed countries join in, the EU wants to reduce its GHG emissions by 2020 by 30%. With regard to a future EUETS, national circumstances will have to be taken into consideration. In November 2006, the Commission proposed to start a technical analysis of criteria immediately and to review the EUETS, including an extension to land use, land use change and transport. Furthermore, the participation of small installations, the inclusion of further sectors, gases and CCS are assessed. A harmonisation of the whole system within the EU is targeted. This relates particularly to how to allocate allowances and the treatment of new entries. Monitoring and reporting guidelines must be binding and emissions reports must receive better verification.

Additionally one must analyze how the EUETS can be linked to ET Schemes in third countries and also, to what extent JI/CDM is contributing to economies shifting to more sustainability.

### 3.2. EURACOAL position

It was agreed that a draft position should be developed within the next two months and presented to the General Purposes Committee. The three major topics of the position are the following:

- **Fair Burden sharing agreement** of the Member States
- Grandfathering: **Consistent benchmark rules** that are **fuel and technology specific**
- Sustainability and ensuring investment in Clean Coal capacity: **Instrument to create investment security** or new plants for an appropriate part of the power plant lifetime

Further topics to be included are:

- **Trading period** about 10 years
- Full **grandfathering** of certificates or slow start with auctioning
- Sustainability: **JI/CDM** recognized also after 2012
- EU competitiveness: Streamlining the EUETS with **third country systems**

- **Rule to transfer allowances** to new plants replacing « old » ones

The participants agreed on the proposition to discuss the outcome of the Workshop at the next Executive Committee and also to discuss certain topics with experts.

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