

Voting Recommendations for ITRE Committee on the Market Stability Reserve

20 January 2015

An effective Market Stability Reserve is important to help foster innovation and avoid the risk of European industries fall behind in deploying clean, renewable, and energy-efficient technologies and creating green jobs. We recommend the following amendments to the Commission's proposal to the Market Stability Reserve.

Voting recommendations in numerical order

Vote in favor of:

CA 1A, 2B, 3A, 3C and 53-59, 61, 62, 63, 69, 70, 71-75, 78, 82, 87- 92 96, 104, 105, 106, 110

Reject the following amendments:

CA 1B, 3B, and 8, 9, 52, 60, 76, 77, 79- 81, 85, 86, 93

1. Start the Market Stability Reserve in 2016

Under the Commission's proposal, the Market Stability Reserve would not become operational until 2021. This is too late. **In order to address the current market imbalance, the Market Stability Reserve needs to be enacted at the earliest possible date.** This would help address the growing supply and demand imbalance and could therefore help to send a clear price signal. Accordingly, **the Market Stability Reserve should then be reviewed in 2021** (and not in 2026, as currently proposed by the Commission).

- **VOTE IN FAVOUR amendments: CA 1A and 53-59, 73**
- **VOTE AGAINST amendments: NO to CA 1B, 1C and 52, 60**

2. Prevent back-loaded and unused allowances from re-entering the market

Not only will the 900 million back-loaded allowances return to market, but large volumes of additional allowances will also likely be released at auction in 2020. Given that the total surplus is projected to be 2.6-4.5 billionⁱ by 2020, additional allowances need to be permanently removed. Independent research has confirmed that a combination of permanently cancelling these allowances and an earlier start date of the Market Stability Reserve will avoid volatile prices and lead to a more stable carbon price.ⁱⁱ

- **The back-loaded and unused allowances should be cancelled permanently. This would improve the environmental ambition of the ETS while also helping to create an adequate pollution price signal.**
- **A compromise position would be to move all these allowances directly into the MSR.**

- **VOTE IN FAVOUR amendments: CA 2B, 3A and 61, 62, 63, 69, 104, 105, 106, 110 (underlined amendments are especially important)**
- **VOTE AGAINST amendment: CA 3B**

3. Make adjustments stronger when the market is strongly over-supplied

The Commission proposes that when the surplus of allowances exceeds 833 million, 12% of the surplus will be transferred into the Market Stability Reserve. If the surplus falls below 400 million, 100 million allowances are released again. These thresholds are said to be based on the amount of allowances that the power sector buys in advance and stores to ensure they have enough allowances for their planned power sales. This is known as forward hedging. Analysts agree that the amount of allowances needed by the power companies for hedging will decline as the power sector becomes less carbon intensive. The Market Stability Reserve should be designed to take such a decrease into account.

- **The upper and lower thresholds that trigger the removal or the release of allowances should therefore decrease over time. At the same time, surplus allowances should only be re-released to the carbon market when prices have risen (Article 29a) and the surplus threshold is at the same time met. In addition, the Market Stability Reserve should set aside surplus emission allowances more rapidly than the suggested 12% of allowances in circulation annually.**

Furthermore, the response time of the Market Stability Reserve should be shortened. Under the Commission's proposal it would take two years to make corrections for any under- or oversupply. This time-lag could see the Market Stability Reserve reacting to obsolete information. We therefore recommend that the **Market Stability Reserve alters the auction calendar in July each year based on the previous year's surplus.**

- **VOTE IN FAVOUR amendments: 70- 72, 74, 75, 78, 87- 92**
- **VOTE AGAINST amendments: 8, 9, 76, 77, 79, 80, 81, 85, 86, 93**

4. Limit the surplus from being used as future rights to pollute

Restricting the amount of surplus allowances in the Market Stability Reserve that can be used as future rights to pollute will help ensure that the EU ETS does not cancel out the greenhouse gas reductions from other existing and future policies. **Therefore, a limit should be put on the carry-over of allowances in the Market Stability Reserve from one trading phase to the next. Furthermore, an upper limit should be set on the number of allowances that the Market Stability Reserve can hold. If the limit is reached, allowances should be cancelled instead of being transferred to the Market Stability Reserve.**

- **VOTE IN FAVOUR amendments: CA 3C, and 70, 82, 96**

Background

The EU's Emissions Trading Scheme (EU ETS) is the world's largest carbon market, covering more than 11,000 installations in the EU, as well as Iceland, Liechtenstein and Norway. These installations include large-scale industrial entities, such as energy companies, steel and cement producers, as well as intra-EU flights. The EU ETS sets a limit on the amount of greenhouse gas emissions that can be emitted. Companies covered by the EU ETS receive or buy emission allowances which they can trade with one another: one emission allowance allows for one tonne of CO₂ to be emitted. After each year, companies must surrender enough allowances to cover all of their emissions, otherwise fines are imposed. The cap is reduced over time so that total emissions decline. The ETS aims to help the EU achieve its emissions goals more cost-effectively. Moreover, the EU ETS is supposed to encourage investments in low carbon technologies.

However, a large surplus of more than 2.1 billion emissions allowances has built up in the EU ETS. This is more than all companies participating in the ETS are allowed to emit in one year. The surplus is due to lower industrial output as a result of the economic downturn, and lenient rules that allowed the use of a very large number of international carbon credits. By 2020, the EU ETS surplus will have grown to between 2.6 and 4.5 billion allowances. As a result of this enormous oversupply of emission allowances, the price for these rights to pollute has dropped so significantlyⁱⁱⁱ that the EU ETS no longer facilitates the transition towards a renewable and energy efficient economy, and companies can delay or cancel investments in cleaner and more efficient production, risking a costly lock-in in carbon intensive infrastructure for years to come. An overhaul of the EU ETS is urgently needed to ensure that the EU ETS is in line with the EU's long-term objective of 80 to 95% emission reductions by 2050.^{iv}

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Climate Action Network (CAN) Europe is Europe's largest coalition working on climate and energy issues. With over 120 member organisations in more than 25 European countries, CAN Europe works to prevent dangerous climate change and promote sustainable energy and environment policy in Europe.

ⁱ EC (2014), SWD(2014)17, Impact Assessment accompanying the Proposal for a Decision concerning the establishment of a market stability reserve: 2.6 billion (see [here](#)) UK government: 3.1 billion, (see [here](#)); estimates by Sandbag: 4.5 billion, (see [here](#)).

ⁱⁱ http://ec.europa.eu/clima/events/articles/0094_en.htm

ⁱⁱⁱ The average allowance price in 2013 was €4.47 (source : Point Carbon).

^{iv} CAN Europe calls for a reduction of at least 95% by 2050, (see [here](#)).