CO_2 REDUCTION BEYOND 20%

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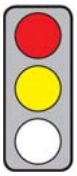
Centrum für Europäische Politik

MAIN ISSUES

Objective of the Communication: The Commission aims to examine a tightening of the EU greenhouse gas emission targets in 2020 from 20% to 30%.

Parties affected: The economy as a whole, in particular the energy-intensive industries



Pro: Currently, the Commission does not favour an additional reduction of greenhouse gases beyond the already agreed to 20% by 2020.

Contra: (1) The Commission keeps the option of a unilateral additional reduction of greenhouse gas emissions open and thus accepts an almost doubling of EU climate action costs in 2020.

(2) EU-wide emission taxes and regulatory measures for production lead to a double burden without any additional benefits for climate policy.

CONTENT

Title

Communication COM(2010) 265 of 26 May 2010: **Analysis of options to move beyond 20% greenhouse gas emission reductions and assessing the risk of carbon leakage**
and **Commission Staff Working Document SEC(2010) 650** of 26 May 2010 (Part I and Part II)

Brief Summary

- **Context**
  - Already in the run-up to the follow-up agreement of the Kyoto protocol, which expires at the end of 2012, the EU unilaterally committed itself to cutting 20% of its greenhouse gas emissions by 2020 compared to 1990 levels (European Council of 8/9 March 2007, Conclusions by the chair dated 2 May 2007, 7224/1/07 REV 1, No. 32; see CEP Policy Brief in German only).
  - At the same time, it committed to a 30% reduction in emissions provided that other developed countries, as part of the Kyoto follow-up agreement, commit to "comparable emission reductions" and the emerging countries to "contributing adequately according to their responsibilities and respective capabilities" (cp. European Council No. 31; cp. CEP Policy Brief in German only).
  - The Commission emphasizes that "this remains EU policy today", even though circumstances have meanwhile changed "rapidly" through the worldwide financial crisis and the failed UN Climate Conference in Copenhagen in December 2009 (p. 2).

- **Targets**
  - The Commission stresses that the present Communication's purpose "is not to decide now" to move to a 30% target since "the conditions set are clearly not met" (p. 2).
  - The Commission merely wishes to set out " the result of analysis into the implications of the 20% and 30% targets as seen from today's perspective", in order to facilitate a "more informed debate" on both targets in view of the changed framework conditions.
  - At the same time, the Commission meets its obligation to publish by June 2010 an analysis which covers the issue of carbon leakage from energy-intensive sectors to countries outside the EU (Art. 10b (1) Directive on the Emissions Trading System 2009/29/EC; see CEP Policy Brief in German only).

- **Analysis of the 20% reduction target**
  The Commission analyses the current baseline of the 20% target in order to assess the impact of a possible increase to 30%.
  - **Impact of the economic crisis on the 20% target**
    - The overall amount of greenhouse gas emissions in the EU dropped
      - between 2005 and 2008 by up to 10% below 1990 levels,
      - and due to the economic crisis in 2009 by 14% below 1990 levels.
    - In the sectors covered by the EU Emission Trading System (EU-ETS), greenhouse gas emission fell to 11.6% below 2008 levels.
    - The price for emissions allowances, which entitle the owner to emit carbon, dropped from € 25 per ton of CO_2 at the beginning of 2006 to € 8 at the beginning of 2009; in May 2010, however, prices had risen again to between € 12 and € 15.
    - The absolute costs for implementing the 20% target by 2020
      - were estimated at € 70 billion in 2008 (assumed GDP growth of 2.4% per year) and
      - are currently estimated at € 48 billion (assumed GDP growth of 1.7% per year).

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- The Commission ascribes the projected cost reduction to the fact that
  - efforts to cut CO_2 have slackened due to the economic crisis,
  - the demand for energy has fallen due to the expansion of renewable energy sources, improved energy efficiency and the rise in oil prices, and
  - the price of carbon is likely to remain lower as allowances not used in the recession are carried into the third phase of EU-ETS (2013-2020).

– **Boosted incentives to develop "green technologies"**
The Commission calls upon Europe to "boost still further the incentives" to develop "green technologies" in the transport (e.g. "green vehicles", see CEP Policy Brief) and energy sectors [e.g. CO_2 capture and storage (CCS), see CEP Analysis in German only] as it sees Europe's leading position as being under threat.

– **Long-term deficiencies of current EU climate action**
- In order to keep the global temperature increase below 2°C compared to pre-industrial levels, according to the Commission, by 2050 all developed countries will need to cut their emissions by 80-95% and the EU by "roughly 70%". The EU climate change measures adopted in 2008 are deficient if these targets are to be met by 2050 "at optimal cost" (p. 5).
- According to the Commission, the 20% target by 2020 is now "driving change less strongly" than expected in 2008 and thus there is a risk that EU climate efforts will become "more difficult and more expensive" after 2020. Therefore, according to the Commission a "long-term roadmap to 2050" is needed in order to plan investment ahead in the most cost-effective way. (p. 5).

► **Analysis of the 30% target**
Stepping up to the 30% target "would in all probability entail increasing the stringency of existing policies or introducing new policies" (p. 5 f.).

– **Options to meet the 30% target within the scope of EU-ETS**
- The Commission is considering lowering the cap for carbon emissions by reducing 15% of the auctioning rights over the period from 2013-2020 by "setting them aside" (p. 6).
- The current legal position allows for EU-ETS projects where CO_2 is reduced in third countries and such reductions are calculated against CO_2 caps in the EU ["Clean Development Mechanism" (CDM); see CEP Analysis, in German only]. The Commission is afraid that this EU-ETS practice might slow down incentives for innovation in the EU. To this end, it wishes to substitute part of the credits with new sectoral credits for projects with a greater reduction potential (e.g. in the power sector in advanced developing countries) [as already proposed in COM(2009) 475; see CEP Policy Brief]

– **Options to meet the 30% target outside EU-ETS**
- In sectors not covered by EU-ETS, the Commission favours carbon taxes in order to incentivise emission reduction at national or European level (p. 6 et seq.).
- The Commission intends to increase regulation regarding technology, notably energy-intensive products, e.g. through product standards as defined under the Eco-design Directive (see CEP Policy Brief in German only) or limits of CO_2 emissions from vehicles (Regulation No. 443/2009, see CEP Policy Brief in German only).
- The Commission wishes to regulate activities which have not yet been included, such as land use, land use change and forestry (LULUCF), due to their potential for reducing greenhouse gas emissions.

– **Costs of reaching 30% targets**
- The Commission estimates the overall costs for reaching the 30% targets in 2020 [SEC(2010) 650, Part II, p. 47] at:
  - approximately € 94 billion (additional costs compared to 2020 target: € 46 billion), provided the 30% reduction is practised throughout the EU,
  - approximately € 81 billion (additional costs compared to 2020 target: € 33 billion), provided 25 percentage points of the 30% reduction is carried out in the EU and 5 percentages points through the allowances carried into the third trading phase and CDM credits.
- According to the Commission, a "cost-effective split" (p. 9) of the 30% target requires a CO_2 reduction over the period of 2005-2020 of:
  - 34% (20%target: 21%) in sectors covered by EU-ETS and
  - 16% in sectors not covered by EU-ETS (20% target: 10%).

► **Risk of carbon leakage**

– The Commission intends to avoid the leakage of energy-intensive industries from the EU to third countries with less ambitious climate targets, since this would lead to a world-wide increase in carbon emissions ("carbon leakage", CEP Analysis, in German only).

– The Commission expects the following production losses (p. 10, cp. CEP-Table):

sector	20% target: production losses	30% target: additional production losses
organic chemicals	0.5%	0.9%
Inorganic chemicals	0.6%	1.1%
other chemical products	2.4%.	3.5%

– The Commission is currently discussing the following options to avoid a leakage of energy-intensive industries from the EU to third countries (p. 11):
  - According to the Commission, the "most obvious way" to level the playing field is to maintain the free allocation of allowances to energy-intensive industries.
  - In order to compensate for insufficient climate action in third countries, the EU could increase import costs for the products concerned, for instance by requiring the acquisition of allowances. However, this might infringe international trading rules.
  - The EU should strive to have climate change measures in third countries' upgraded to EU levels.
    - Within the scope of EU-ETS, the use of CDM credits from energy-intensive sectors in third countries should be limited.
    - The EU should support developing countries through the transfer of climate protecting technologies.

Statement on Subsidiarity by the Commission

The Commission does not address the issue of subsidiarity.

Policy Context

In order to stabilise the concentration of greenhouse gases in the atmosphere at a level that avoids damaging the climate system, the European Union and its Member States agreed in 1997 in the Kyoto Protocol on the UN Climate Agreement to reduce their greenhouse gas emissions by 8% over the period of 2008-2012 compared to 1990 levels.
The implementation of the EU climate policy targets is mainly based on the "Climate Package" of 23 April 2009 [see CEP Analysis in German only], which covers the Renewable Energies Directive [2009/28/EC, see CEP Policy Brief in German only], the Emissions Trading Directive [2009/29/EC, see CEP Policy Brief in German only], the Cost-Sharing Decision [406/2009/EC, see CEP Policy Brief in German only] and the CCS Directive [2009/31/EC, see CEP Policy Brief in German only].
During the Copenhagen Climate Conference in December 2009, the participating countries failed to conclude a binding follow-up agreement to the Kyoto Protocol, which expires at the end of 2012 [see CEP Policy Brief]. The "Copenhagen Accord", which was signed by 29 head of states and governments and merely " taken note of" in the Conference's conclusions, does not contain any binding targets.

Options for Influencing the Political Process

Leading Directorate General:	DG Climate Action
Consultation procedure:	Not planned.

ASSESSMENT

Economic Impact Assessment

Ordoliberal Assessment

The EU has failed to carry through its idea of an international climate protection agreement at international level; the Copenhagen climate summit clearly demonstrated this. In its Communication the Commission now reveals that without an international climate agreement it does not hold a clear position regarding the unilateral 20% reduction of greenhouse gas emission by 2020. Both the Communication and the accompanying working documents are written with the underlying, though recognisable, intention to commit the EU to an additional reduction target beyond 20%. Critical passages were added to the Communication later. **It is to be welcomed that**, following this correction process, **the Commission no longer favours an additional reduction of greenhouse gas emissions of (up to) 30%. However, it is alarming that the Commission continues to keep this option open**.
For while **going it alone would incur costs to the EU, it would not generate any benefits in terms of climate policy**. Firstly, this is due to the expected carbon leakage of energy-intensive sectors to territories outside the EU. Secondly, substantial amounts of fossil fuels that are not used in the EU are not saved globally but are burnt elsewhere in the world, for a reduced demand for fossil fuels leads to a fall in world prices for fossil fuels, which in turn boosts demand in other parts of the world.
The issue of "carbon leakage" can only be tackled within the framework of EU emission trading without a worldwide climate agreement if allowances are issued cost-free to the industries affected. However, such exceptions inevitably lead to distortion of competition, since the necessary boundaries are never selective enough and, besides, massive political influence can be expected. These distortions are all the more serious the higher the price for allowances is. This is another reason why additional reductions in greenhouse gas emissions should be rejected.
The announced "Roadmap to 2050" is to be welcomed in principle, as companies need certainty on the political framework conditions when it comes to investment decisions. However, this roadmap must not ignore the fact that a worldwide climate agreement shaped according to EU ideas is unlikely to be concluded. This sets limits to a reasonable EU climate policy – a fact which should not be ignored.

Impact on Growth and Employment

The Commission is right to point out that the fall in allowances prices is not only rooted in the economic crisis but also in the increased energy efficiency and the expansion of renewable energies. However, **considering** the fact **that the Commission has been for years pushing politically energy efficiency and the expansion of renewable energies, it cannot now criticise the resultant price-curbing effect on emissions trading**. It is a direct consequence of the EU energy policy which – contrary to the Commission's opinion – did indeed "drive change" strongly (p. 5). The Commission ignores the fact that the existing fall in emission prices was bought at a high price, namely through inefficient subsidies of renewable energies and energy efficiency measures. To this end, the price curbing merely mitigates the high costs of EU climate policies.

The economic crisis is accompanied by substantial burdens for companies. It is not useful to claim that efforts to meet the 20% target slackened during the crisis. In fact, the reason less climate protection action was necessary during the crisis was much more due to a fall in production. A positive, economically stabilising aspect of EU-ETS is that climate protection becomes cheaper in times of economic crisis without there having to be a lowering of climate targets. Therefore **it would be a mistake to impose additional burdens upon companies during an anticipated upswing** by tightening targets after a crisis. So allowances should not be "set aside" in order to reach the 30% target.

The Commission' idea to use emissions taxes in those areas not covered by emissions trading in order to meet the 30% target is not principally wrong. However, **it should be avoided that** in these areas – as considered by the Commission – **tax burdens and regulatory measures are applied simultaneously**. For that would lead to higher burdens without any additional benefits for the climate. A tax solution, on the other hand, would require a reduction in regulatory measures, for instance in the field of building heating and transport. **The Commission's announcement of increased regulation**, for instance in the Eco-Design Directive (2009/125/EC) and the CO_2 standards for passenger cars (Regulation No. 443/2009), **is therefore factually wrong**.

Impact on Growth and Employment

Should the EU decide unilaterally – and exclusively through savings within the EU – to reduce carbon by 30% instead of 20% by 2020, the Commission predicts an almost doubling of costs from 48 billion € in 2020 to 94 billion €. This would have a negative effect on EU growth and employment and is to be rejected, especially in light of the latest economic crisis, since Member states are currently hopeful that they are going to be able to recover at least a part of the losses incurred in the recession.

Impact on Europe as a Business Location

Additional carbon reductions would increase costs, notably for energy-intensive industries, and would thus worsen the quality of Europe as a business location.

Legal Assessment

Legislative Competence

The EU is empowered to adopt measures for climate protection (Art. 192 TFEU).

Subsidiarity

Unproblematic.

Proportionality

Unproblematic.

Compatibility with EU Law

Unproblematic.

Compatibility with German Law

Unproblematic.

Conclusion

It is to be welcomed that the Commission does not favour an additional carbon reduction by 30% instead of 20% by 2020. However, it is alarming that the Commission keeps this option open. For while going it alone would incur costs to the EU, it would not generate any benefits in terms of climate policy. Against this background, it is comprehensible why, according to the Commission's projection, the EU should bear almost the double costs for climate action in 2020. However, in view of the latest economic crisis, the economy should not be burdened with additional expenses. It is further mistaken to create – as requested by the Commission – double burdens through emission taxes and excessive product regulation when these have no effect on climate policy.