

# ETS POLICY COHERENCE MECHANISM V300

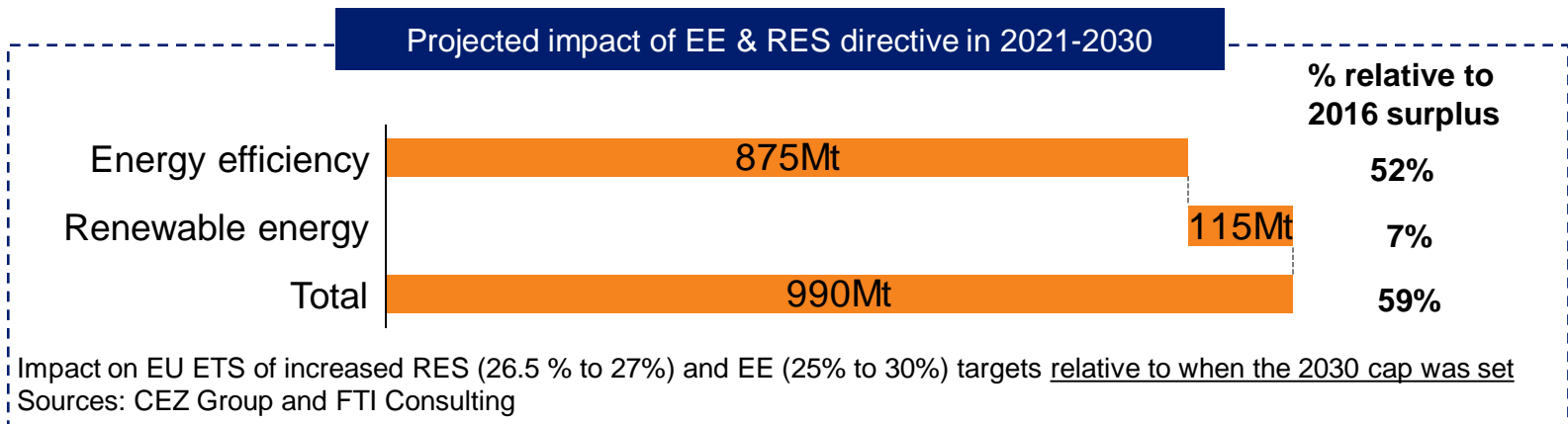
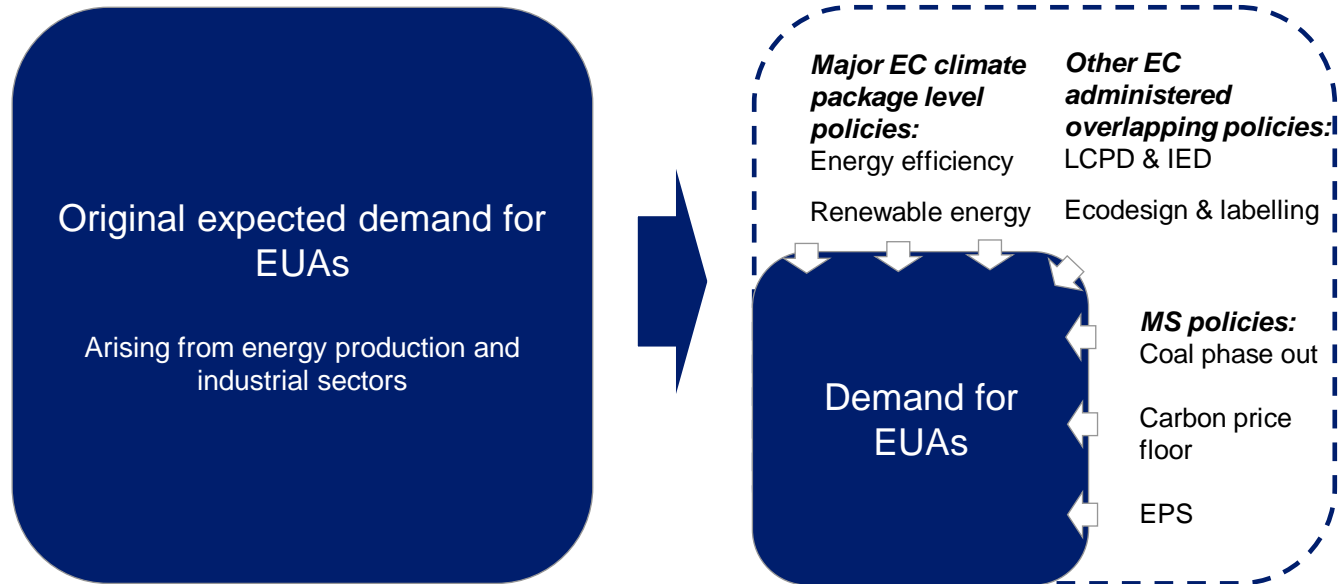
20 June 2017

Gareth Davies, Stuart Murray, Jenni Patronen, Mostyn Brown, Alex Luta



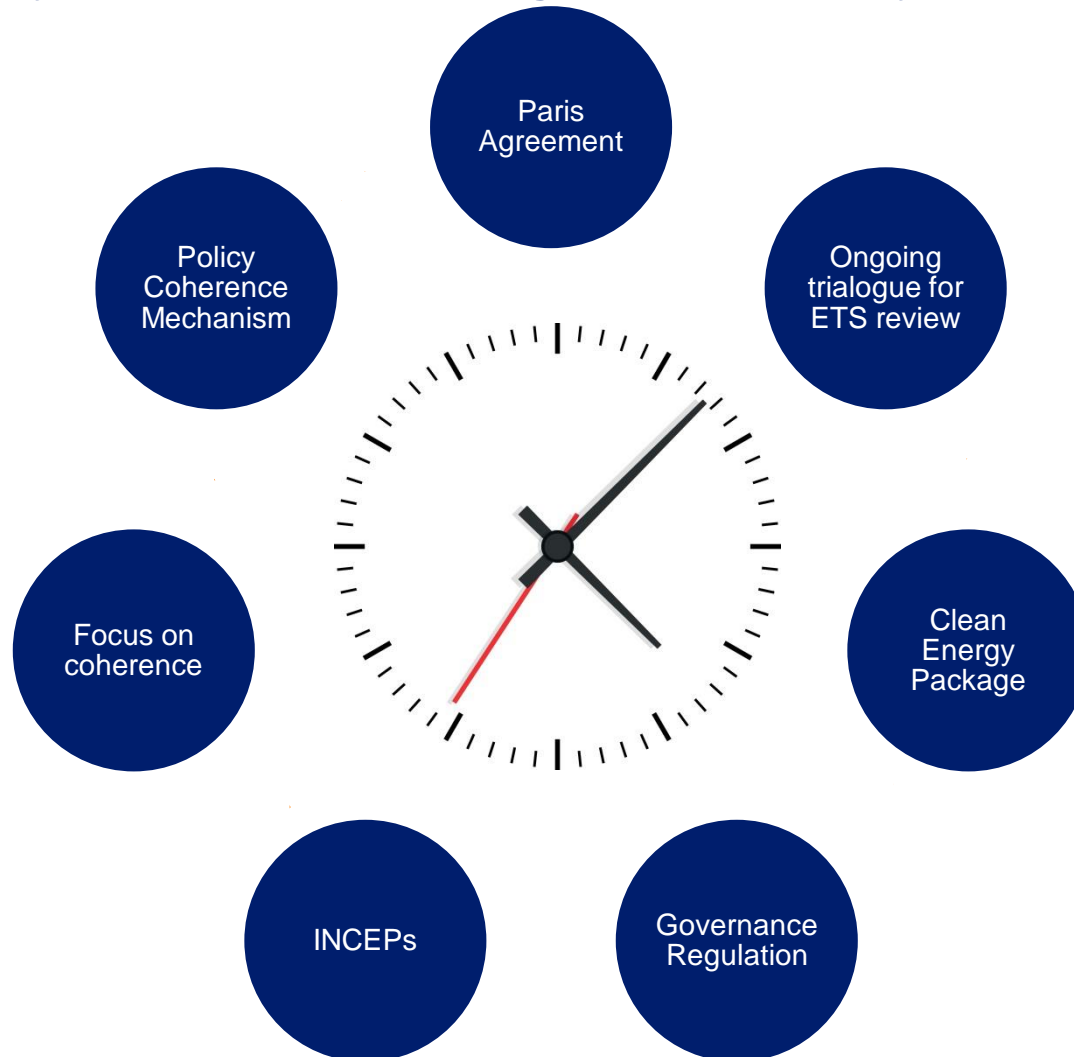
# POLICY COHERENCE ISSUES WILL NOT GO AWAY

Current proposals to strengthen MSR and so on do not address this problem



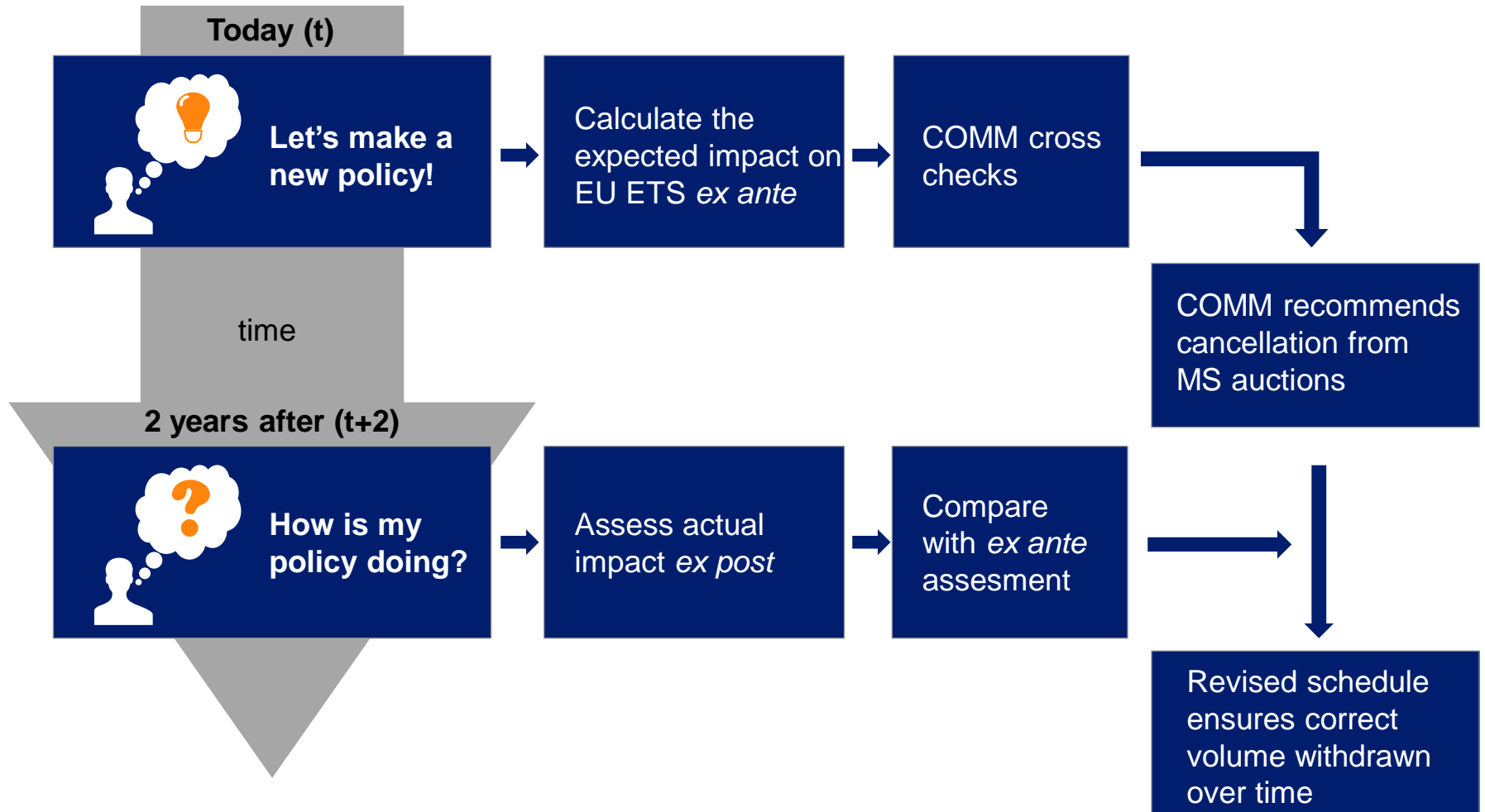
# NOW IS THE TIME TO ADDRESS THIS PROBLEM PRO-ACTIVELY

Next opportunity to address this issue again will be in early/mid 2020s

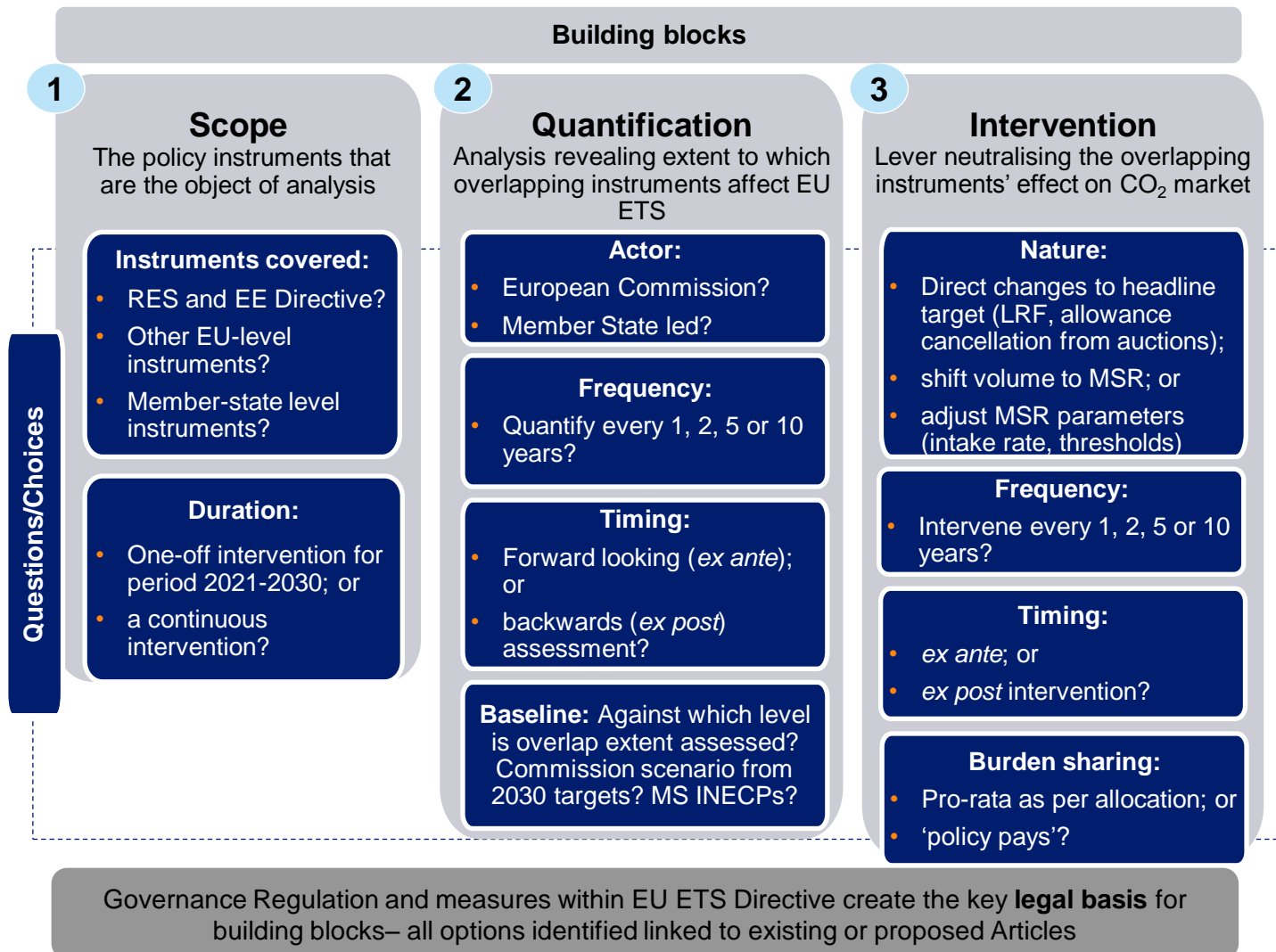


# OUR MECHANISM HAS A SIMPLE PREMISE

Scope covers all national and EU-level instruments on an ongoing basis



# OPTIONS FOR ETS POLICY COHERENCE MECHANISM



# THE MECHANISM IS EASY TO IMPLEMENT

A set of amendments have been identified that would have the mechanism operating almost entirely through the Governance Regulation

|               | Document  | Due date | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 |
|---------------|---|----------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| Member States | Long-term emission strategy                     | 15 Mar   |      |      | ✓    |      |      |      |      |      |      |      |      |      | ✓    |
|               | Integrated national energy and climate plans    | 01 Jan   |      | ✓    |      |      |      |      | ✓    |      |      |      |      | ✓    |      |
|               | Biennial progress report                        | 15 Mar   |      |      |      | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    |      |
| Commission    | State of the Energy Union report                | 31 Oct   |      |      |      | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    |
|               | Assessment of Member State submissions          | 31 Oct   |      |      |      | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    |      |
|               | Recommendation to individual MSs                | 31 Oct   |      |      |      | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    | ✓    |      |
|               | Union level action to ensure Energy Union goals | N/A      |      |      |      |      |      |      | ✓    |      |      |      |      |      |      |

Reporting requirements under the INECPs

No new data flows required

# WHY THIS MECHANISM?

We have investigated a range of alternatives but this mechanism was favoured

Comprehensive

- Broad scope



Timely

- Immediate impact



Accurate

- Regular quantification and intervention



Predictable

- Well defined responsibilities
- Enshrined in proposed regular reporting

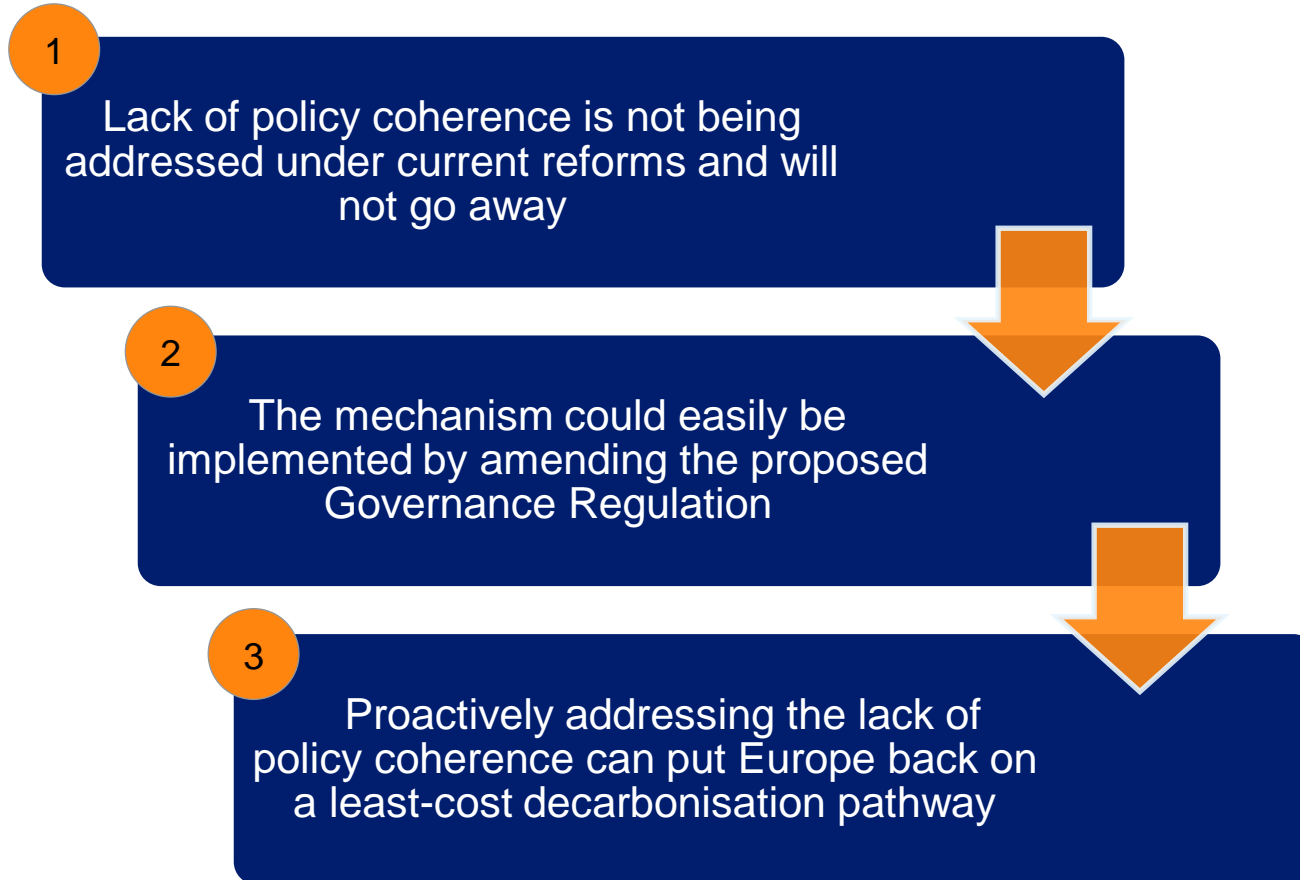


Feasible

- Complementary to the MSR
- Does not impact Free Allocation
- Implemented through amendments to Governance Regulation



# ETS POLICY COHERENCE MECHANISM CAN ADDRESS THE PROBLEM OF FUTURE OVERLAPPING POLICIES







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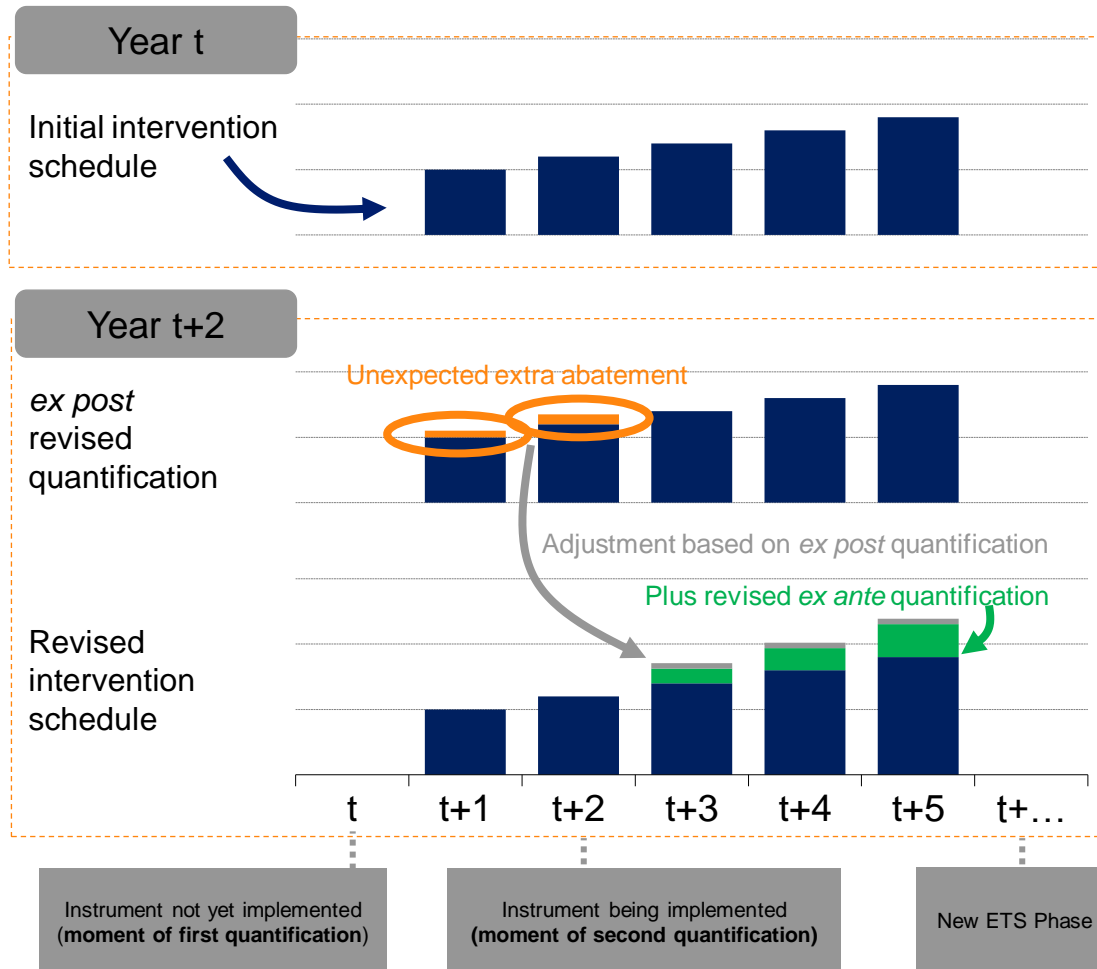
**Pöyry Management Consulting**



# WHAT MIGHT SUCH A MECHANISM LOOK LIKE?

| Building block  | Element            | Selected option  |
|---|--------------------|--|
| <b>1. Scope<br/>(i.e. coverage)</b>   | n/a                | <b>All national and EU-level instruments</b> , on an ongoing basis   |
| <b>2. Quantification<br/>(i.e. assessment of effect of overlapping instruments)</b> | Baseline           | Latest Integrated National Energy and Climate Plan/biennial progress reports   |
|   | Actor              | Member State, subject to verification by Commission, with possibility to reconcile discrepancies                           |
|   | Timing & frequency | <b>Ex ante, every two years from 2019 onwards</b> but with an ex post assessment/re-adjustment to correct volume over time |
| <b>3. Intervention<br/>(i.e. lever used to correct effect)</b>                      | Nature             | <b>Cancellation of allowances</b> from upcoming auctions   |
|   | Actor              | Cancellation by Member States on their own allocation, pursuant to recommendation by the Commission                        |
|   | Timing & frequency | <b>Ex ante, every year from 2021 onwards</b>   |

# ADJUSTMENT IS TIMELY AND RESPONSIVE



# CASE 1: AN 'EX ANTE ONLY' ADJUSTMENT WOULD LEAD TO INACCURATE INTERVENTION

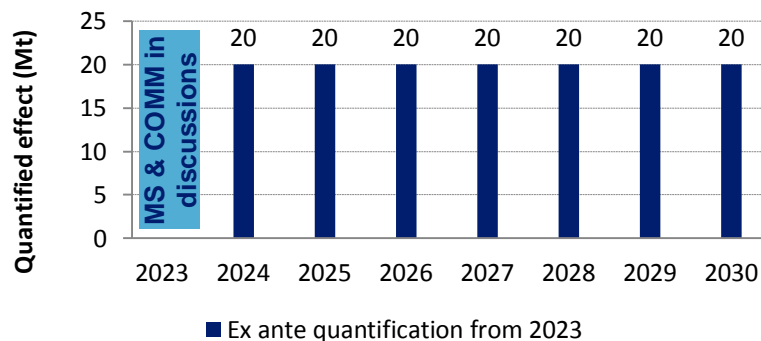
| Year                 | Event  | Cancelled EUAs | Actual abatement (Mt) |
|----------------------|--|----------------|-----------------------|
| 2023                 | <ul style="list-style-type: none"> <li>Germany announces the implementation of demand side management (DSM) to start in 2024</li> <li>In its 2023 biennial progress report reveals expected emissions reductions of 20Mt/year</li> <li>Commission agrees with Germany's cancellation schedule of 20M EUAs/year until 2030</li> </ul>                                   |                |                       |
| 2024                 | <ul style="list-style-type: none"> <li>Germany starts implementing DSM</li> </ul>  | -20            | 15                    |
| 2025                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per original schedule</li> <li>However, <i>ex ante</i> quantification in new biennial report suggests that the impact will be only 15Mt/year for the future</li> <li>Commission agrees with Germany's updated cancellation schedule of 15M EUAs/year</li> </ul> | -20            | 15                    |
| 2026                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM as per updated schedule</li> </ul>   | -15            | 15                    |
| 2027                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM as per updated schedule</li> <li>New biennial progress report confirms accuracy of 2025 quantification.</li> </ul>   | -15            | 15                    |
| 2028                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> </ul>   | -15            | 15                    |
| 2029                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> <li>New biennial progress report confirms accuracy of 2025 quantification</li> </ul>  | -15            | 15                    |
| 2030                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> </ul>   | -15            | 15                    |
| <b>PHASE 4 TOTAL</b> |  | <b>-115</b>    | <b>105</b>            |

Without *ex post* adjustment historic mismatches cannot be rectified

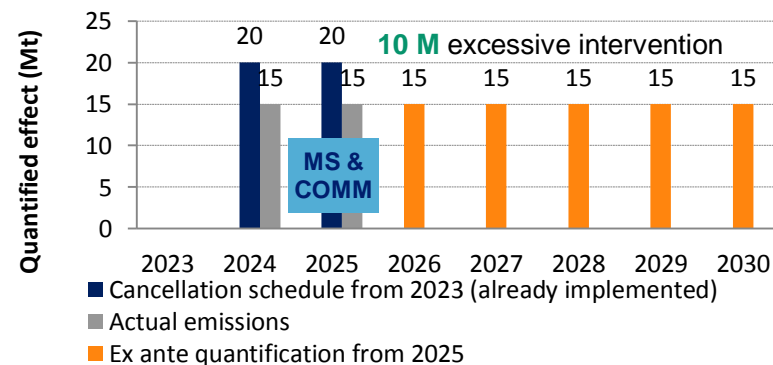
In this case this results in cancelling 10M EUAs too many

# CASE 1: AN 'EX ANTE ONLY' ADJUSTMENT WOULD LEAD TO INACCURATE INTERVENTION

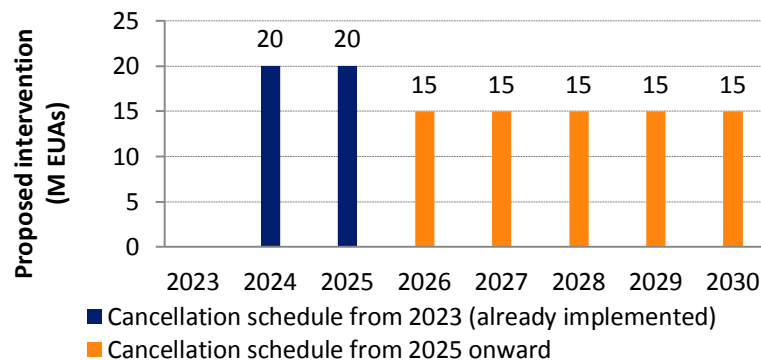
## First quantification (2023)



## Second quantification (2025)



## Actual cancellation schedule



## Lack of *ex post* adjustment is inaccurate

- The mechanism intervenes by cancelling **20M EUAs** until the quantification is updated
- The update revises interventions down to **15M EUAs** when new evidence is accepted
- But there is no mechanism to adjust for mistakes in the *ex ante* quantification resulting in cancelling **10M EUAs** too many

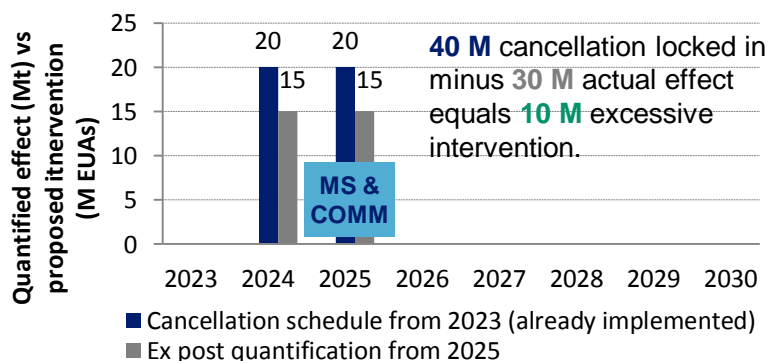
## CASE 2: POLICY COHERENCE MECHANISM

| Year                 | Event   | Cancelled EUAs | Actual abatement (Mt) |
|----------------------|---|----------------|-----------------------|
| 2023                 | <ul style="list-style-type: none"> <li>Germany announces the implementation of demand side management (DSM) to start in 2024</li> <li>In its 2023 biennial progress report, German <i>ex ante</i> quantification reveals expected emissions reductions of 20Mt/year</li> <li>Commission agrees with the German quantification, and recommends a cancellation schedule of 20M EUAs/year until 2030 (the remainder of Phase 4 of the EU ETS)</li> </ul>   |                |                       |
| 2024                 | <ul style="list-style-type: none"> <li>Germany starts implementing DSM and cancelling allowances</li> </ul>   | -20            | 15                    |
| 2025                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling as per original schedule</li> <li>However, <i>ex post</i> quantification in the new biennial report reveals that DSM only reduces emissions by 15 Mt/year. Given 2024 cancellations and scheduled cancellations for 2025, Germany will have cancelled <math>2 \times (20 - 15) = 10</math> M EUAs too much. With 5 future years still remaining in the Phase, Germany proposes recovering <math>10/5 = 2</math> M EUAs/year.</li> <li>Furthermore, <i>ex ante</i> quantification reveals that the future impact will also be only <u>15Mt/year</u></li> <li>The Commission agrees with the German quantification and recommends a cancellation schedule of <math>15 - 2 = 13</math> M EUAs/year</li> </ul> | -20            | 15                    |
| 2026                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> </ul>  | -13            | 15                    |
| 2027                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> <li>New biennial progress report confirms accuracy of 2025 quantification</li> </ul>   | -13            | 15                    |
| 2028                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> </ul>  | -13            | 15                    |
| 2029                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> <li>New biennial progress report confirms accuracy of 2025 quantification</li> </ul>   | -13            | 15                    |
| 2030                 | <ul style="list-style-type: none"> <li>Germany continues implementing DSM and cancelling allowances as per updated schedule</li> </ul>  | -13            | 15                    |
| <b>PHASE 4 TOTAL</b> |   | <b>-105</b>    | <b>105</b>            |

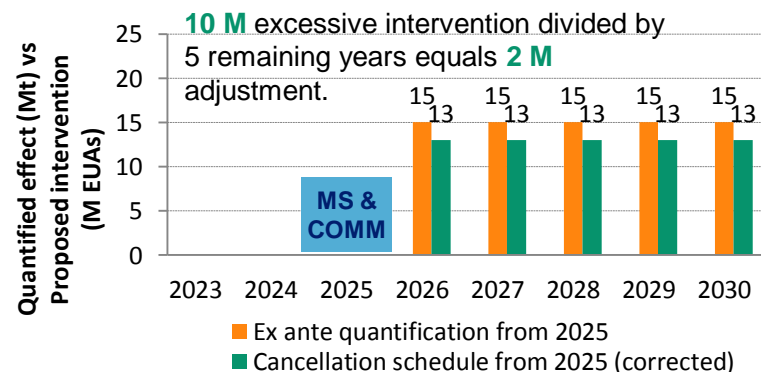
# CASE 2: POLICY COHERENCE MECHANISM

Through *ex post* adjustment the mechanism can correct for 10M EUA overachievement

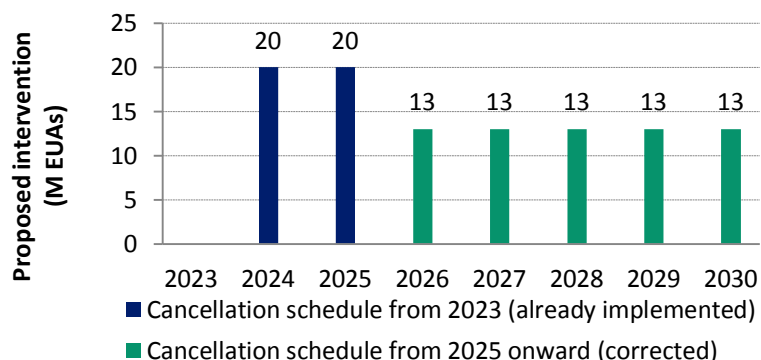
## Second quantification (2025): Looking back



## Second quantification (2025): Looking forward



## Actual cancellation schedule



## Flexible quantification enables accurate intervention

- The mechanism intervenes by cancelling **20M EUAs** until the quantification is updated
- The update revises interventions down to **13M EUAs** when new evidence is accepted
- The intervention still matches the actual impact of the overlapping policy:
  - Actual: 7 years x 15 M/year = 105 M.
  - Intervention: (2 years x 20 M/year) + (5 years x 13 M/year) = 40 M + 65 M = 105 M.