Open Letter: Scrap the Australian-EU ETS linkage

by Scrap the EU-ETS
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On 28 August 2012 the Australian Government and the European Commission announced their intention to link the Australian emissions trading scheme (ETS) with the European Emissions trading scheme (EU ETS). A joint consultation paper on registry options and proposed Australian regulations to facilitate the linking of these two emissions trading schemes has been released.

The EU-Australia ETS linking directive is the wrong move. We are writing to oppose the plans to link two fundamentally flawed schemes from being brought together. We reject emissions trading as a means to reduce emissions. It is ecologically ineffective, benefits polluting industries, distracts from progressive reform, and has shown to have serious social impacts. Itâ€™s time to move beyond the ideological disdain for direct regulation, and shift to policy and public investment strategies that work.

Emissions trading has failed to reduce greenhouse gas emissions in the EU; produced windfall profits for polluters; and now stands in limbo as the European Commission decides upon its fate. In linking to the EU ETS, Australia is exacerbating all of these structural failings. The solution is not to expand and complicate the ETS by linking it to more countries, but rather to scrap the schemes in favour of progressive and more effective regulation to reduce emissions and transition away from fossil fuel dependence.

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Background

The Australian Clean Energy Future (CEF) legislative package came into effect on 1 July 2012. It establishes a price on carbon (measured in equivalent tonnes of carbon dioxide CO2-e). For the first three years (1 July 2012 â€“ 1 July 2015) the carbon price is set by the government at $23/tonne CO2e (increasingly by 2.5% per year). On 1 July 2015 the scheme will shift to having a market-determined fluctuating price.

In order to facilitate the link two significant changes have been made to the Australian ETS:

- Removal of floor price. Under the CEF package there was going to be a â€˜floorâ€™ and a â€˜ceilingâ€™ on the price of carb least the first three years (1 July 2015 â€“ 1 July 2018) to make sure market-set prices were not too low to be environmentally effective. This floor price was set at AU$15/t CO2e (increasingly by 4% annually). Under the linkage arrangement this legislative guarantee of a minimum carbon price will be scrapped. Previous provisions for minimum auction prices for carbon credits (for the years 2015-2016, 2016-2017 and 2017-2018) have also been scrapped.

- Changes to offset rules. The CEF scheme includes a 50% cap on the use of international offsets until 2020. There have been some changes to the types of credits that will count towards this, but no meaningful solutions to the problems of carbon offsetting. An additional cap of 12.5% on Kyoto offsets units from the Clean Development Mechanism (CDM) and Joint Implementation (JI) has been included as part of the linkage arrangements. This sub-limit will apply from 1 July 2015 â€“ 30 June 2020. However, 37.5% of each companyâ€™s obligations can come from EU Allowance units (EUAs). There is a huge glut of EUAs in the EU ETS market system currently. Australian firms will be buying the free permits allocated to polluters in the EU.

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Two wrongs donâ€™t make a right: Problems with Australia-EU ETS link

- The EU ETS has not reduced emissions. The EU ETS has not reduced emissions across its first two phases (2005-2007; 2008-2012). Due to over-allocation of free permits (EUAs) to firms participating in the EU ETS in phase I (2005-2007) carbon prices dropped to nearly zero in December 2007. Prices have stayed incredibly low in the phase II (2008-2012). Since 2008, any emissions reductions that occurred are attributable to the financial crisis, not the carbon price mechanism.[i] International carbon offsets fed into the EU ETS through the UNFCCC CDM and JI programs. Offset projects have resulted in an increase of emissions worldwide: even conservative sources estimate that between 1/3 and 2/3 of carbon credits bought into the ETS â€˜do not represent real carbon reductionsâ€™.[ii] The most controversial of these are offset projects making minor technical adjustments to factories producing nylon and refrigerant gases (HFCs). In 2010 EU Climate Change Commissioner Connie Hedegaard stated â€˜There are too many examples of projects with industrial gases, primarily HFC-23, where if you dig into it you can find there is a total lack of environmental integrityâ€™.[iii] At May 2012, industrial gas projects made up 84% of CDM offset credits (CERs) in the EU ETS.[iv] Whilst industrial gas offsets have been discredited, the European Commission has been incredibly slow to remove these offsets from the scheme.

- The EU ETS is characterized by volatile and declining carbon prices. Carbon prices have been continuously unstable and declining overall since 2008. The historical minimum was reached in January 2013 with permits selling at â‚¬4.15 per tonne CO2e. According to market analysts, there is no prospect of prices reaching levels that would incentive any changes in energy-generating capacity.[v] Even if very predictable high prices could somehow be engineered â€“ which is the opposite of what the ETS is designed to deliver â€“ they would be insufficient to incentivise the structural changes needed to address climate change in the absence of other measures.

- The EU ETS is a subsidy for polluters. Whilst companies with obligations to participate in the EU ETS have been allocated more free permits than they need, almost all of the costs were passed on to consumers. Heavily compensated energy â€“intensive industries (iron and steel, refineries and (petro)-chemical utilities) enjoyed windfall profits â‚¬14 billion between 2005 and 2008.[vi] Electricity producers, too, are free to pass on to consumers the full â€˜opportunity costâ€™ of compliance by increasing electricity prices, resulting in windfall profits of anywhere between â‚¬23 and â‚¬71 billion in the second phase.[vii] Industry lobbying has guaranteed that over 75% of manufacturing industry will continue to receive permits for free at least until 2020 (meaning extra revenue to polluters instead of state coffers of around â‚¬7 billion per year). Every attempt to end this handout has met strong lobbying from energy-intensive industries. In Phase III (2013-2020), only the energy sector will be required to buy permits at auction, and even then, exceptions have been made for utilities in Central and Eastern Europe, including those with a high dependence on coal for electricity generation. Corruption in the market has even put a cost on the public purse. in 2010 a vast â€˜carousel fraudâ€™ in the EU ETS was revealed to have cost the public more than â‚¬5 billion in lost Value-Added Tax (VAT) revenues.[viii]

- Linking to the EU ETS means linking to an accumulated glut of excess emissions currently causing regulatory headaches in the EU. Analysts from Barclays have estimated that there is a 1.68 gigatonnes oversupply of emissions in the EU ETS the end of Phase II 2008-2012). The amount of over supply is almost as much Europeâ€™s predicted emissions for 2012 (1.952 gigatonnes). If no action is taken to address this over supply of emission credits it is estimated that there will be an oversupply of allowances equivalent to 2.512 gigatonnes CO2e by the end of Phase III (2013-2020).[ix] There is a proposal to address this problem by â€˜back-loadingâ€™ excess emissions. This proposal will be voted on by the European Parliament and European Climate Change Commission in April 2013 and the vote is expected to be tight. â€˜Back-loadingâ€™ would involve postponing the auction of 900 million gigatonnes of the Phase III allowances from 2013-2015 until 2016-2020. This problem simply defers rather than addresses the crisis of excess permits. Even the European Commission recognises â€˜backloadingâ€™ is only a short term fix.[x] The glut of EUAs in the EU ETS will further spread the failures of emissions trading.

- The Australian ETS repeats the EU ETS flaws. The Australian ETS installed in the Clean Energy Future (CEF) package has repeated the failures of the EU ETS, particularly in regard to compensation and carbon offset rules.

Compensation:Generous compensation in the form of free permits has been extended to the most polluting firms in Australia. The most polluting power stations stand to receive windfall profits, whilst passing on the costs to households nonetheless. Approximately $2.3billion and $5.4billion in windfall profits will go to brown coal generators who are passing on more than the full costs of the carbon price to consumers. Victorian brown coal generators will receive over 90% of a $5.5 billion "Energy Security Fund" cash payments and free permits issued to 2016-17.[xi] Grattan Institute analysis of the compensation and exemptions awarded to black coal, liquefied natural gas (LNG) and steel industries in the CEF is unjustified and costly. Taking into account recent commodity prices and exchange rates, they found even with no protection and a carbon prices rise to $40 per tonne of CO2e (well above the Treasury forecast to 2020) large job losses in these industries are unlikely.[xii]

Offsets: On top of this, the Australian ETS rules effectively put no limits on the amount of emissions reductions that can be replaced by carbon offsets. There is a 50% limit on international offsets and no limits on the number of credits from Carbon Farming Initiative (CFI) offsets. Under the EU-Australia ETS linking agreement, 37.5% of international offsets will be EUAs â€“ the same free permits that were heavily over-allocated to polluters in Europe in the first and second phases of the EU ETS! CFI offsets are a controversial type of land-based offset focused on agriculture and forestry. Land offsets like REDD+ and the CFI are incredibly problematic methods for reducing emissions. Land carbon should not be used to compensate for burning fossil carbon â€“ carbon embedded in land-water-atmosphere ecosystems are much more dynamic than fossil carbon contained within effectively inert fossil fuels underground. The CFI scheme has even weaker regulation than the Kyoto CDM and JI schemes.[xiii] Rather than a project-by-project measure of additionality (as is the case for the CDM and JI) the CFI projects are assessed against a list of â€˜positiveâ€™ activities which are deemed automatically additional to business as usual. Further, the novel methodologies for the CFI including culling introduced animals and the application of biochar to soil mean the CFI is an another step away from rigorous policy that addresses the drivers of land degradation and deforestation: clearing for forestry and agriculture.

- Scrapping the Australian floor price as part of the link is likely to produce a lower post-2015 carbon price in Australia than planned. Pricing carbon is already a weak approach to regulating transition away from fossil fuels. Demand for energy is inelastic, meaning that higher carbon prices do not guarantee reduced consumption (but they do guarantee high costs for consumers).[xiv] Putting the regressive impacts of carbon pricing aside, the price incentive is further weakened by EU linkage. There is a high level of uncertainty surrounding future predictions of the EU carbon price.[xv] Whilst the Australian Greens are optimistic that the EU carbon price in 2015 will be higher than the legislative floor price would have been[xvi] most modeling suggests that the EU price will be lower than the floor price would have been. [xvii] Carbon analysts Repu Tex expect that the price of EUAs will be trading at around AU$11.50 per tCO2-e between 2015 and 2020, which is below the planned AU$15 floor price. Therefore, the link allows businesses to meet their liabilities at a much cheaper rate than the original deal struck within the Multi-Party Climate Change Committee (industry lobby groups campaigned strongly for this change).

- The Australian ETS locks-in a fossil-fuel economy. There is no plan or vision to reduce emissions under the Australian ETS. The Australian government is assuming international offsets will account for 94% of recorded emissions reductions by 2050. A reliance on international offsets of all kinds is assumed by the Treasury modelling that accompanied the legislation. Treasury proposes it is â€˜inefficient to meet the whole abatement task through domestic actionâ€™.[xviii] The CEF modelling forecasts 434 Mt CO2-e in recorded emissions reductions will come from international offsets.[xix] The 2012 Energy White Paper has the same assumption that emissions will be outsourced overseas and for expanded coal and gas industries. Under the cover of carbon pricing, the report argued for further energy privatization, and the removal of other market measures in the energy sector â€“ the RET and feed-in tariffs for solar.[xx] We cannot support a climate policy that locks in emissions increases and is used as an excuse to abandon other energy policies.

- The ETS closes the door to other, genuinely effective climate policies. Public money is being squandered on setting up carbon markets that are unable to achieve a public purpose. Carbon markets cannot address the challenge of climate change in an effective or a just way. If we are serious about tackling climate change we should not be linking the Australia and the European schemes which is recipe for bigger disaster. Instead we need to take action to transform our energy infrastructure and to shift away from fossil fuels especially coal.

- We need direct regulation on climate change. There are effective and progressive policy options available now.[xxi]

- Supporting the roll out of 100% renewable energy, especially state-funded, community run renewable energy projects

- Transitions toward zero carbon in stationary energy, building, land use and transport.

- Hypothecated carbon income and corporate taxes could be imposed to fund renewables, to nance just transitions in coal-dependent communities, and to meet international obligations. These taxes would have a progressive e ect on income distribution.

- Stop using taxpayers' money to provide handouts to big coal and gas corporations and make the miners pay their fair share in taxes.

- Reject current development proposals for coal ports, mega-mines, dams and unconventional gas wells in significant areas.

- Put in place an urgent moratorium on coal seam gas and other unconventional gas mining.

- Full phase out the Australian coal export industry

- Decommissioning coal fired power stations

- Create no-go zones to protect productive agricultural land, national tourism icons and all residential dwellings from coal and gas mining.

- Strengthen the Federal environment laws to exclude coal and gas mining from important water sources, cultural heritage sites and sensitive environment areas.

- Put in place national standards on coal and gas pollution and enforce compliance.

Given the urgency of a just transition away from fossil fuel dependence, we are calling for the Australian and EU governments to scrap their carbon markets in order to make way for progressive climate policy. The struggle against emissions trading is the struggle for social, environmental and climate justice. It is a struggle for transforming our energy, transport, agricultural, production, consumption, distribution, disposal and financing systems. We call on civil society organisations and movements to endorse this call and join the fight to abolish the ETS.

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Signatories

Friends of the Earth Australia

Solidarity

Carbon Trade Watch

FERN

The Corner House

Friends of the Earth Canada

COECOCEIBA - Friends of the Earth Costa Rica

Maryknoll Office for Global Concern

Earth Peoples

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[iv] Point Carbon, "Use of offsets for compliance within EU ETS up 86% on 2011," Point Carbon, http://www.pointcarbon.com/aboutus/pressroom/pressreleases/1.1902674.

[v] FranÃ§ois Joubert, Head of EDF Trading told Risk.net stated that â€œA price above â‚¬45/tonne would currently be required to switch from coal to gas in the UK. Needless to say, these levels are currently out of sight.â€• Joubert in Maroo, Jay, "EU ETS faces back-loading test," Risk.net, 26 February 2013.

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[viii] Europol, "Carbon credit fraud caues more than 5 billion euros damage for European taxpayer," Europol, 9 December 2009.

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[x] EC, "Report From the Commission to the European Parliament and the Council," in COM(2012) 652 (Brussels: European Commission, 2012).

[xi] Victorian brown coal generators will receive over 90% of a $5.5 billion "Energy Security Fund" cash payments and free permits issued to 2016-17. CME, "Transitional Assistance, or Windfall Profits? The Financial Impact of the Carbon Price and Compensation Payments on Victoria's Brown Coal Generators," (Melbourne: CME for Environment Victoria, 2013).

[xii] Wood, Tony and Edis, Tristan, "The New Protectionism under Carbon Pricing: Case Studies of LNG, Coal Mining and Steel Sectors," (Melbourne: Grattan Institute, 2011).

[xiii] Macintosh, Andrew and Waugh, Lauren, "An Introduction to the Carbon Farming Initiative: Key Principles and Concepts," in CCLP Working Paper Series 2012/1 (Canberra: ANU Centre for Climate Law and Policy, 2011).

[xiv] Ackerman, F, "Carbon Markets and Beyond: The Limited Role of Prices and Taxes in Climate and Development Policy," in G-24 Discussion Paper Series, No. 53 (New York: UNCTAD, 2008).

[xv] For a discussion of some of the modeling available see â€˜Table 2 Selected forecasts for the EU ETS carbon prices, 2020â€™ Swoboda, K, Tomaras, J, and Talber, A, "Clean Energy Amendment (International Emissions Trading and Other Measures) Bill 2012," (Canberra: Hansard, 2012), 32.

[xvi] Greens Senator Christine Milne stated: â€˜From 2015 the price will be the European price and by 2018 I would expect that the European price will be greater than the floor price would have been so I think itâ€™s a good thing, it links the two trading scheme and it gets us into a good position with that experience to consider linking with other schemes as they develop over time.â€™ Milne, C and Bandt, A, "Joint press conference," (Canberra: Hansard, 2012), 4.

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