

Green is the Color of Money: The EU ETS failure as a model for the “green economy”

by Carbon Trade Watch
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Carbon Trade Watch will participate in the 10th International Biannual Conference of the European Society for Ecological Economics (ESEE) taking place in Lille, France from June 18 -21. CTW will present a poster during the conference titled, 'Green is the Color of Money, The EU ETS failure as a model for the “green economy”'.

Abstract: The European Union Emissions Trading System (EU ETS) is the cornerstone of European climate policy.

Here, we present a critical review, aiming to show that it has failed to achieve its objectives.

Emissions reductions in the EU ETS covered sectors have been modest. Carbon prices have been low and decreasing. Yet, windfall profits for major polluters have been significant.

Now that the second phase of the EU ETS has reached an end, the EC is preparing several changes in the system. Yet, none of these changes address the fundamental issues that the system raises.

The most pressing problems of carbon trading cannot be designed away, as they relate to how it gives an incentive to end-of-pipe solutions in detriment of a fair transition away from fossil fuel dependence.

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Green is the Color of Money

The EU ETS failure as a model for the “green economy”

Ricardo Coelho¹, Tamra Gilbertson², Joanna Cabello²

¹ Centre for Social Studies - University of Coimbra

² Carbon Trade Watch

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EU ETS Background: Failed Performance to Date

This report presents an overview of the first seven years of the system, aiming to show how it has failed to achieve its objectives.

The European Union Emissions Trading System (EU ETS) covers about half of the EU's CO₂ accounted emissions and has allowed for the creation of a broad range of financial products.

The first two phases of the EU ETS (2005-2007, 2008-2012) resulted in modest emissions reductions and considerable windfall profits for polluters.

As permits were allocated for free according to historical emissions, energy intensive industries were able to sell their excess of permits, while electricity producers, which faced relatively tighter caps, passed on their "opportunity costs" to consumers.

Prices of emissions permits and credits have been consistently low and decreasing.

Questioning the Validity of the EU ETS

A historical analysis of the drivers of emissions shows that other factors not related to carbon trading are much more relevant than the existence of a carbon price. Emissions reductions in the 1990s can be attributed to the "dash for gas" and the deindustrialization of the former German Democratic Republic. The large emissions reductions registered after 2008 can be attributed mostly to the economic crisis. Finally, the delocalization of industrial production to China and other countries in the global South led to a transfer of emissions, as the Kyoto Protocol accounts for emissions from production, not consumption. Estimates from the European Commission on the proportion of emissions reductions registered in the second phase of the EU ETS that can be attributed to carbon trading are not available, further bringing into question the validity of the scheme.

Fraud in the System

The European carbon market has also been impacted by several frauds. VAT frauds have cost the European taxpayers more than €5 billion (Europol, 2010). Phishing frauds have cost millions to affected companies. This has led to increased regulatory pressure on the market but has also implied its temporary shutdown.

Additions to the Third Phase

Now that the second phase of the EU ETS has reached its end and the third phase (2013-2020) is underway, the EC is preparing several changes in the system.

- Aviation has been included. The EC estimated the emissions reductions from this measure at the equivalent to one year's growth in emissions in a "business as usual" scenario. Moreover, airlines will join the "polluter gets paid" can pass on the "opportunity cost" of permits they got for free to consumers.

- "Grandfathering" will be replaced by benchmarking and auctioning as the method of allocation. Yet, most permits will still be given for free and the performance-based benchmarks have been set based on what the polluters want.

- Worries about low prices in the EU ETS led to the emergence of proposals by EU institutions to “backload” permits for use at a later date, thus reducing the excess supply that exists in the market. The European Parliament voted against this practice on 15 April this year but will reconsider after revision by the Environmental Committee.

- Offset credits rules will be changed. Clean Development Mechanism projects that eliminate HFCs or N2O will be excluded from April 2013, following accusations of lack of environmental integrity. More importantly, only offset credits from Least Developed Countries will be accepted for compliance, while the EU plans to implement bilateral or multilateral agreements with other countries in the South to generate credits from sectoral markets. Still, there will be an over-supply of offset credits in the third phase while the average limit to their use for compliance is set to increase.

Exporting Failure: The Financialization of Nature

None of these changes address the fundamental issues that the EU ETS raises: its lack of environmental effectiveness, its connections with industrial lobbying, its dependence on the uncertain outcomes of speculative moves in financial markets. Nevertheless, this system has been used as a blueprint for the creation of other carbon trading systems around the world, and was presented at the Rio+20 Conference by the EU as a model for the commodification and financialization of nature, through schemes like biodiversity offsets and Reducing Emissions from Deforestation and Forest Degradation (REDD+).

The most pressing problems of carbon trading cannot be designed away, as they relate to how it gives an incentive to end-of-pipe solutions in detriment of more ambitious and socially just policies that would facilitate the transition away from fossil fuel dependence. By focusing on abstract data or volume of trading as criteria for success, carbon trading legitimizes the continued use of fossil fuels, the over-production and consumption model, and actually makes the climate and environmental crisis worse.

Dropping the EU ETS would leave the field open to effective, just and democratic climate policies, which are now being blocked by its existence. Insisting on exporting the EU ETS failure to other countries, under the cover of “leadership”, hinders cooperation with the rest of the world.

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