

## INSIGHT

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### The future of the EU-ETS system

The European Union Emissions Trading System (EU ETS) is a pillar of the EU's climate policy and an effective tool for the goal of reduction of greenhouse gas (GHG) emissions by 20% of 1990 level as outlined in the Europe 2020 strategy.<sup>1</sup> Launched in 2005, the ETS now covers more than 11,000 heavy energy consumption installations in the EU plus Croatia, Norway, Lichtenstein and Iceland, representing 45% of the total EU GHG emissions.

Under the system, companies are allocated emission allowances, which give the holder the right to emit GHG<sup>2</sup>. If companies' emissions exceed the allowances, heavy fines will be imposed. In order to avoid penalties, companies need to buy additional allowances in the market. Similarly, companies who have surplus allowances can sell their quota to other companies. The



volume of supply and demand will determine the price of the allowances in the EU.

As a result of economic slowdown and the increased share of the clean energy, a total surplus of 955 million allowances has been recorded by early 2012 and the carbon price has dropped to below €5 in 2013.<sup>3</sup> The phenomenon has led to concerns over the effectiveness and the long term credibility of the ETS. In November 2012, the European Commission has drafted a "backloading"

policy to postpone the sale of 900 million allowances from 2013-2015 in order to diminish the supply of allowances in short term. Previously, the industry, research and energy (ITRE) committee voted against the measure arguing that such intervention would increase the cost for small and medium enterprises in times of economic slowdown whereas the environment, public health and food safety (ENVI) committee voted in favor. The European Parliament is expected to vote on the plan in mid-April 2013.

#### SPECIAL POINTS OF INTEREST:

- 1) To learn more about Europe 2020 strategy and the EU's environmental objective 20-20-20, please read [http://europe.hkbu.edu.hk/euap/business\\_files/Europe%20202020.pdf](http://europe.hkbu.edu.hk/euap/business_files/Europe%20202020.pdf).
- 2) Each allowance gives the holder the right to emit one tonne of CO<sub>2</sub>, or equivalent amount of nitrous oxide and perfluorocarbons.
- 3) Carbon prices were above €20 in 2008. Also note that the free allowance allocation will decrease gradually every year starting from 2013. The decrease in supply may bring up the carbon price in later years.. That explains why it is not viable to reduce the allocation quota indefinitely.

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Should you have any comments or feedbacks on the issue, please feel free to e-mail at [kpleung@hkbu.edu.hk](mailto:kpleung@hkbu.edu.hk)

#### REFERENCES

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<http://www.theparliament.com/latest-news/article/newsarticle/mixed-reactions-following-ets-backloading-vote/>

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