Consultation on the review of the auction time profile for the EU Emissions Trading System

SSE plc (EU Transparancy Register: 64436972598-17)

25 September 2012

Introduction

SSE welcomes the opportunity to respond to the public consultation of DG Climate Action, on the review of the auction time profile for the EU Emissions Trading System (EU ETS).

SSE believes that the EU ETS is a vital policy instrument for carbon mitigation and facilitates the most appropriate framework to address an international issue such as climate change. A market based approach is a cost effective way of ensuring a volume reduction in carbon emissions and to support investments in low carbon technologies. At the same time it's essential that effective national support schemes for renewables are in place, to secure the required deployment of these technologies.

The ETS has a fixed cap for the period 2013-2020. However, (economic) reality has departed significantly from the modelling that informed the original cap-setting. The resulting oversupply of allowances in the market has driven the price of EU ETS carbon allowances (EUAs) to less than 8 euro per tonne. Thus while the EU is on track to meet its ETS cap to 2020 at low cost, the ETS is failing to effectively stimulate low carbon investments.

SSE believes that a higher, less volatile carbon price is vital to support the transition to a low carbon economy, as detailed in the Commission's Low Carbon Economy Roadmap 2050. As such, the Commission should act urgently to strengthen the ETS.

Options to strengthen the EU ETS

There are different options to strengthen the EU ETS. SSE has a strong preference for a structural, longer term solution.

Setting an ambitious carbon reduction target for 2030

SSE believes that a more ambitious carbon reduction target for 2030 is the most desirable option, as it would provide the longer term perspective required to drive low carbon investments. Together with a Progressive Coalition of Energy companies, we have pledged for a 2020 target of 25% domestic carbon reduction[1] and a 2030 Climate and Energy Package[2], which includes binding 2030 targets for carbon reduction, renewable energy and energy efficiency. As noted above it's essential for SSE that effective renewables policies, including binding targets and support schemes, will continue to play a driving role as long as needed.

By setting a more ambitious 2030 target, the ETS cap – which is currently planned to deliver emissions cuts of 1.74% per year - would have to be tightened to ensure the ETS was able to deliver on the tougher targets. Furthermore, this would send a price signal which would strengthen the incentive effect of the carbon market.

[1] http://www.sse.com/PressReleases2011/EuropeanEnergyIndustry/
[2] http://static.euractiv.com/sites/all/euractiv/files/Open%20Letter_FINAL-2.pdf

SSE plc
Registered Office: Inveralmond House 200 Dunkeld Road PH1 3AQ
www.sse.com

Set aside allowances

The second best option would be to withdraw ('set aside') allowances from the EU ETS market. If sufficient allowances were set aside, the ETS cap would effectively have been lowered, which could increase prices.

The Commission has suggested[3] that reducing allowances in Phase 3 (2013-2020) by about 15%, representing about 1.4 billion allowances, could be sufficient. SSE doesn't share this view and agrees with EWEA[4] that at least 2.6 billion allowances should be set aside in order to provide the required scarcity and to avoid merely pushing back oversupply.

Furthermore, SSE believes that the removal of these allowances should be permanent, to give the strongest signal and certainty to the market about quantities available and to quickly restore the price.

Carbon floor price

An EU-wide carbon floor/ceiling would create certainty for investors, but looking at the present political reality, including subsidiarity objections related to European taxation, SSE does not have a strong preference for this option.

It should also be taken into account that the introduction of different carbon price regimes by member states, such as the UK's Carbon Price Support mechanism, will have an impact on the operation of the EU ETS, although it is unclear as to the scale of price differentials (and a range of other factors will trigger change in EU ETS carbon prices) and the arbitrage opportunities which may occur. At worst, emissions may be transferred to other member states netting off reductions in UK emissions.

Delaying auctioning - Looking at the Commission proposal

The Commission proposal suggests adjusting the volumes to be auctioned in phase 3 of the EU ETS, decreasing the volume in the first three years (2012-2015) and increasing the volume equivalently in the last three years (2017-2020). By reducing the auctioning volume in the first 3 years the carbon price is expected to rise, the increase in the last three years will have mitigating effect on the carbon price.

SSE believes that this proposal is an important step in the right direction, hopefully leading to a structural recalibration of the EU ETS – the introduction of an ambitious 2030 carbon reduction target.

The proposal has the benefit of being quickly realisable via the proposed Regulation. For it to be effective, the amount of allowances backloaded should be as large as possible. As noted above, we believe that a figure of 2.6bn allowances is the figure required to restore balance to the system. We would therefore encourage the Commission to go beyond the figures outlined in the Commission Staff Working Document[5].

If the Commission chooses to delay auctioning, we would urge it to clarify at the earliest opportunity its intention to review the ETS Directive in order to amend Article 9, allowing the

[3] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0265:FIN:EN:PDF
[4] http://www.ewea.org/fileadmin/ewea_documents/documents/publications/position_papers/120711_EWEA_Position_Paper_ETS.pdf
[5] http://ec.europa.eu/clima/policies/ets/auctioning/third/docs/swd_2012_234_en.pdf

SSE plc
Registered Office: Inveralmond House 200 Dunkeld Road PH1 3AQ
www.sse.com

Commission to cancel the delayed allowances, and thus permanently reducing the oversupply of EUAs in the system.

Conclusion

A strong EU ETS is – together with effective support for renewables - a key driver for carbon mitigation and investments in low carbon technologies. To strengthen the scheme SSE prefers a structural, longer term solution and is therefore strongly in favour of a more ambitious carbon reduction target for 2030, in combination with a binding 2030 target for renewables. The Commission proposal for backloading allowances is a welcome sign that the Commission is prepared to take the necessary steps to restore confidence in the ETS. To maximise the impact SSE prefers the most ambitious reduction available to the Commission, and swift clarity on whether and how these allowances would be reintroduced to the ETS.

SSE plc
Registered Office: Inveralmond House 200 Dunkeld Road PH1 3AQ
www.sse.com