

The EU ETS in Phase 3

Introduction

After much negotiation, the EU Parliament and the Council of Ministers finally agreed on the climate change package originally proposed by the European Commission (the "**Commission**") in January 2008. The agreed legislative package that will address the modifications to the EU Emissions Trading Scheme ("**EU ETS**") for Phase 3¹, has not yet been published. However, as the agreed text adopted by the European Parliament on 17th December 2009 and the text adopted by the Council of Ministers on 26 March 2009 has been published, no substantive changes are to be expected before final publication of the legislation in the Official Journal of the European Union.

The package has been welcomed by business as it introduces legislative certainty until 2020 but has been criticised by various environmental groups as not being sufficiently robust in creating incentives for emission reductions to occur within Europe. However, given the resistance to the proposals from certain countries including Italy and Poland and the backdrop of the economic climate in which it was being negotiated, the agreement between the 27 Member States to unilaterally adopt a climate change package such as this is a remarkable achievement. It sends a strong signal to other countries that are in the process of negotiating a post-2012 commitment period under the Kyoto Protocol.

The Background

The climate change package² contains legislation on a number of issues relating to climate change and renewable energy including the geological storage of carbon, the promotion of renewable energy and the changes to the EU ETS for Phase 3. The package includes:

- A directive on geological storage of carbon dioxide³.
- A directive on the promotion of the use of energy from renewable sources⁴.
- A directive to improve and extend the greenhouse gas emissions trading system of the EC (the "**EU ETS Reform Directive**").

Key Issues

The Climate Change Package in Context

Summary of Operational Reforms

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Table of key changes

¹ The EU ETS is divided into a number of compliance periods. The first of these was Phase 1 (from 2005-2007) and the current phase is Phase 2 (from 2008-2012). Under the package, the next compliance period, Phase 3, is to run from 2013-2020.

² Please see our earlier client briefing note: "*The shape of things to come -the EU ETS from 2012, perspectives on the EC's proposals*", February 2008.

³ For more information please refer to our sister client briefing note: "*Agreement on the Carbon Capture and Storage Directive and Funding Package*", January 2009.

⁴ For more information please refer to our sister client briefing note: "*Agreement of EU Climate and Renewable Energy Package*", January 2009.

- A decision on the effort to reduce greenhouse gases to meet the EU's commitments up to 2020 (i.e. burden sharing).
- A directive introducing a mechanism to monitor and reduce greenhouse gas emissions from the use of road transport fuels.
- A regulation setting emission performance standards for new passenger cars as part of the EC's integrated approach to reduce CO2 emissions from light-duty vehicles.

(together, the "**Climate Change Package**").

Although agreed ahead of the Climate Change Package, a directive to bring emissions from the aviation sector into the EU ETS has also been agreed ensuring that commercial aviation emissions will be included from 2012 onwards⁵ and should very much be considered part and parcel of the EU ETS Reform Directive.

This briefing note focuses on the EU ETS Reform Directive and Table A to this briefing note provides a summary of the key changes that are being proposed and a comparison with the current position.

The EU ETS Reform Directive

Overview

For the purpose of discussing the changes addressed by the agreed position for the EU ETS Reform Directive, they can be considered to have three principal themes:

- (1) Amendments to the scope, monitoring and allocation under the current EU ETS ("**Operational Reforms**").
- (2) Amendments that reflect the EU ETS's role in international efforts to reduce greenhouse gas emissions ("**International Effort Reforms**").
- (3) Amendments that impact on other existing efforts within the EU ETS ("**Cross-Sectional Reforms**").

The items falling within Operational Reforms are mainly mechanical in nature but make structural and practical changes to the way the EU ETS operates. The International Effort Reforms (e.g. the use of Certified Emission Reductions ("**CERs**") from Clean Development Mechanism ("**CDM**") projects beyond a certain agreed amount) are likely to be impacted by the direction of future international talks on climate change, including the fruition of the Bali Action Plan in Copenhagen and the establishment of any mandatory greenhouse gas schemes introduced in countries that are not Member States (e.g. Australia and the United States). Cross-Sectional Reforms cover the changes by the EU ETS Reform Directive that impact on other directives (such as the aviation directive) or legislation.

Operational Reforms

Certain of the Commission's original proposals did not sit well with a few of the newer Member States. The most notable of these was the proposal that all operators within the power sector would have their EU allowances distributed on a 100% auctioned basis. Eventually a carve-out to this proposal had to be agreed benefiting certain countries (see below) without which the entire Climate Change Package may have failed. The most significant changes set out in the agreed text of the Climate Change Package dealing with operational reforms are as follows:

- The EU ETS will be expanded to cover new gases and industrial sectors. Nitrous Oxide and Perfluorocarbons (in either cases along with CO2) from the chemical and aluminium sectors are to be brought within the EU ETS from 2013. In addition CO2 from Carbon Capture and Storage ("**CCS**") facilities and pipelines used for transportation to CCS facilities will also be brought within the scope of the EU ETS.

⁵ For further information regarding the Commission's proposals regarding aviation, please see our sister client briefing note: "*Clearer Skies: Aviation and the EU ETS*", September 2008

- The Phase 3 compliance period will be an 8-year period from 2013 to 2020 rather than the current 5-year period.
- The requirement of individual Member States to produce National Allocation Plans (“NAPs”) will be replaced with a single EU-wide allocation of EU allowances in accordance with harmonised rules.
- In order to meet the EU's target of a 20% reduction in greenhouse gases by 2020 compared with 1990, the total number of EU allowances in the EU-wide cap will decrease annually in a linear manner by 1.74% p.a. from the 'Community-wide quantity of EU allowances' for 2013 and this quantity will be published by the Commission before the 30th June 2010. This quantity is to be calculated on the total number of EU allowances issued or to be issued by Member States in accordance with the Member States approved NAPs in Phase 2⁶. The linear factor reduction also applies to allocations in the new entrants reserve. The purpose of this change is to give market participants regulatory predictability. The 1.74% reduction p.a. reflects a 20% reduction against 1990 levels under Kyoto. This 1.74% reduction p.a. will continue beyond Phase 3 into Phase 4 and will be reviewed by the Commission after 2020 with a view to a decision on the adjustment to the linear factor being made by 2025.
- The Commission's aim for 100% allocation of allowances by auction for all sectors not at risk of carbon leakage⁷ did not survive the co-decision process. However, the principle that any allowances not distributed for free must be auctioned did survive. The precise number of these allowances that are to be auctioned will be determined and published by the Commission no later than 31 December 2010. The Commission will, by 30 June 2010, adopt a regulation on the timing, administration and other aspects of auctioning to be carried out by Member States.
- The Climate Change Package provides different percentages of free allocation and auctioning depending on the sector under which the operator falls. There are four main approaches. These are (i) the electricity production sector, (ii) the industrial sector, (iii) the sector or sub-sectors that are exposed to a significant risk of carbon leakage, and (iv) the electricity production sector derogation for electricity producers in Member States that meet certain requirements.
 - a. For the electricity production sector in the majority Member States, all EU allowances will have to be purchased by way of auction. This also applies to installations that capture, pipelines that transport or to storage sites for CO₂.
 - b. For operators within other sectors (including aviation), 80% of their allocation will be distributed for free in 2013 but this percentage will reduce annually at an equal rate so that only 30% free allocation occurs in 2020. This reduction will thereafter continue into Phase 4 in a manner such that there is no free allocation in 2027.
 - c. For operators within sectors (or sub-sectors) at risk of carbon leakage, all allocated EU allowances will be distributed for free during Phase 3 at the level of the benchmark of the best technology available. The Commission will determine no later than 31 December 2009, following discussion in the European Council, which sectors or sub-sectors qualify for this treatment. In doing so, the Commission will have to work within a criteria specified by the EU ETS Reform Directive.
 - d. For electricity production sector operators in certain Member States that can rely on the derogation, the allocation of free EU allowances in 2013 will be limited to 70% but decreasing to 0% by 2020. There are a number of conditions that have to be met before a Member State can apply the derogation from the 100% auctioning requirement. For example, a Member State can apply the derogation if it can demonstrate its national electricity network was, in 2007, directly or indirectly connected to the network interconnected system operated by the Union for the Coordination of the Transmission of

⁶ According to Point Carbon's Carbon Market Analyst of 12 January 2009, for sectors already within the EU ETS, this will result in an allocation of about 1974 Mt in 2013 and will decrease to 1720 Mt in 2020.

⁷ Carbon Leakage describes the process in which production within an industrial sector in a country with a strict carbon emissions reduction policy moves offshore to a country with lower standards, leaving the former country at a competitive disadvantage in that sector and increasing carbon emissions in the latter country.

Electricity. This derogation was necessary as, without it, Poland was refusing to agree to the Climate Change Package.

- 88% of the total quantity of EU allowances to be auctioned will be distributed between the Member States according to the higher of either their relative share of 2005 emissions or the average of the period 2005-07. 10% of the total quantity of EU allowances to be auctioned will be distributed from Member States with higher levels *per capita* income in 2005 to those with lower *per capita* income to allow for their need to adapt to the effects of climate change. An additional 2% of the total quantity of EU allowances to be auctioned will be distributed amongst Member States who achieved a reduction of at least 20% in greenhouse gas emissions compared with their respective Kyoto Protocol reference year. Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania and Slovakia are expected to benefit from a share of this distribution.
- Initial estimates from the Commission suggested that revenues from auctioning could amount to €50bn per year by 2020. This amount is actually likely to be now lower in light of greater allocation of EU allowances for free compared to the original Commission proposal and the more recent fall in carbon prices. The Climate Change Package is clear that the choice of how to spend such revenues will be determined by each Member State. However, the Climate Change Package text states that at least 50% of such revenue should be used towards one or more of (amongst other things) the development of renewable energies, CCS, contributing to the Global Energy Efficiency and Renewable Energy Fund and the Adaptation Fund under the UNFCCC, and measures to avoid deforestation and increase afforestation and reforestation in developing countries that have ratified a future international agreement. In a recent clarificatory statement the Commission confirmed that allowance auction revenues may, between 2013 and 2016, also be used to support the construction of highly efficient power plans including those that are CCS ready.
- One of the consequences of the Climate Change Package being considered during the current economic climate was the introduction of a new measure in the EU ETS Reform Directive, applicable as of 1 January 2013, that would apply in the event of excessive price fluctuations. Pursuant to these measures, in the event the EU allowance price was more than 3 times the average price for EU allowances during the two previous years and this price continued for more than six consecutive months, then the Commission would convene a meeting of the Climate Change Committee. If these changes did not correspond to changes in market fundamentals, the Committee could either (a) bring forward auctioning by Member States, or (b) allow Member States to auction up to 25% of the remaining EU allowances in the new entrants reserve at such date. Given the scenario required before the Climate Change Committee would consider a measure, it is difficult to envisage this provision having much impact on the market.
- There are specific provisions in the EU ETS Reform Directive dealing with how up to 12 CCS demonstration projects and innovative renewable energy technology projects will be assisted with funding from the auction of up to 300m EU allowances⁸. This amount is available up to the end of 2015 but no single project may benefit from more than 15% of the 300m that has been set-aside for such purposes. Although not entirely clear, it appears that such EU allowances will be auctioned to raise the project contribution.⁹

⁸ See also footnote 3 above.

⁹ Please note that these revenues are separate from the Euro 1.05b that has been set aside under the European Energy Programme for Recovery towards CCS development in 2009-10. Currently each of the selected plants in Germany (2), UK (4), Netherlands (3), Spain (1), and Poland (1) will receive €180 million under the programme, while a plant in Italy will receive €100 million, and a plant in France will receive €50 million

International Effort Reforms

One of the key differences between the Commission's original proposal and the EU ETS Reform Directive determined under the Climate Change Package, is the quantity of offset credits under the Kyoto Protocol that compliance operators within the EU ETS will be allowed to use for compliance. With a view to encouraging reductions of greenhouse gasses to be achieved through efforts within Member States, the Commission had originally sought to tightly limit the amount of Kyoto offset units that may be used for compliance. Rather surprisingly, the EU Parliament was happy to relax these quantitative limits but, in exchange, sought certain qualitative limits on the type of Kyoto offset units that may be used.

The position on the banking and use of CERs and ERUs in Phase 3 under the Climate Change package depends on a number of variables. These lead to a number of different scenarios. In each scenario, the following qualitative and quantitative variables are common:

- (a) *Qualitative:* The CERs or ERUs to be banked or used for compliance must be from project types that were **eligible for use** in the EU ETS during the period 2008 to 2012 (i.e. Phase 2). Currently, the EU ETS only excludes CERs and ERUs from LULUCF and nuclear project activities. All other CERs and ERUs, including those from HFC-23 project activity are project types that are eligible for use in the EU ETS. However, the use of specific credits from certain project types may be restricted by measures that are to be adopted by the Commission after 1 January 2013. Once adopted, the use of credits under the scenarios in (1) to (4) below will be determined by these new measures from a date that is between 6 months and 3 years from the adoption of such measures.
- (b) *Quantitative:* Either (i) there must remain an unused portion of the levels of CER/ERU use allowed by an operator in Phase 2, or (ii) an entitlement to use credits must have been granted. As per their respective national allocation plans, operators are given a limit on the number of CERs/ERUs they may use towards meeting their compliance in Phase 2. Any unused portion of the limit from Phase 2 may be used to meet a compliance obligation in Phase 3. Alternatively, the operator may use an amount equal to a certain percentage that will be determined (but in any circumstances not less than 11%) of their allocation during Phase 2¹⁰. The operator may use the greater of either (i) or (ii) above towards its compliance targets. This entitlement to use will increase in certain circumstances but decrease (to no less than 4.5%) with respect to new entrants. The determination of the specific percentage levels referred to above will be dealt with by measures to be adopted by the regulatory committee assisting the Commission¹¹ so that the overall use of CERs/ERUs does not exceed 50% of the EU-wide reductions from sectors covered in Phase 2 and 50% of the EU-wide reductions below 2005 levels of new sectors and aviation during Phase 3¹².

Assuming (a) and (b) are satisfied, the following scenarios arise, of which (1)-(3) deal with the carry-over of CERs/ERUs and scenarios (4) and (5) deal with the use of CERs for compliance:

(1) *Exchanging of CERs/ERUs, issued in respect of greenhouse gas reductions achieved in Phase 2, in exchange for EU allowances issued in respect of Phase 3:* Operators may request such an exchange until 31 March 2015.

(2) *Allowing operators to exchange CERs/ERUs issued in respect of greenhouse gas reductions in Phase 3, in exchange for EU allowances issued in respect of Phase 3:* Operators may request such an exchange provided that the projects were registered before 1 January 2013 and the credits are not issued with respect to Phase 2.

¹⁰ For example, Germany, Spain and Italy have limits higher than 11% and will retain them.

¹¹ Composed of Member States representatives and chaired by a Commission representative. The committee delivers its opinion on measures submitted by the Commission, making its decisions by weighted voting (see Article 8 of Decision 93/389/EEC)

¹² Point Carbon estimates the import cap to be about 1800-200 Mt over the 2008-20 period.

(3) *Allowing operators to exchange CERs issued in respect of greenhouse gas reductions in Phase 3 from projects started after 1 January 2013, in exchange for EU allowances issued in respect of Phase 3:* Operators may request such an exchange provided that the projects are located in least developed countries¹³ and only until the earlier of 2020 and the date those countries have ratified an agreement with the EU.

(4) *Where negotiations on an international agreement on climate change are not concluded by 31 December 2009, allowing operators to use credits from project or other activities in accordance with agreements concluded between the EU and other countries outside of the EU:* Such agreements will include detail on the levels of use of such credits within the EU ETS.

(5) *Where an international agreement on climate change is concluded:* only credits from project activities in countries that have ratified such agreement may be accepted for use within the EU ETS after 1 January 2013. Host countries of CDM projects that do not ratify a new international agreement before 1 January 2013 will find that their credits will be not allowed to be used within the EU ETS.

The EU ETS Reform Directive allows for agreements that provide for the mutual recognition of allowances between the EU ETS and compatible mandatory schemes with absolute emission caps in another country (e.g. Australia), in sub-federal or regional entities (e.g. the Californian scheme and the Regional Greenhouse Gas Initiative (RGGI)). Probably knowing that the ability to enter into international agreements falls within US federal jurisdiction, the Commission has even included the opportunity for “non-binding agreements” with those sub-federal or regional entities allowing administrative and technical coordination in relation to allowances.

Notable political signals to China, India and the United States in the EU ETS Reform Directive include:

- Once an international climate change agreement has been concluded, not permitting the use of credits from third countries that have failed to ratify such agreement, for compliance purposes.
- Provisions dealing with ‘carbon-leakage’ where free allocations will be given to installations in sectors where they are competitively disadvantaged by imports into Europe from competitors in countries that do not have comparable constraints on their emissions or carbon footprint.
- Requiring Member States to authorise only project activities where all project participants have “headquarters” either in a country that has concluded the international agreement relating to such projects or is or is a country or sub-federal or regional entity linked to the EU ETS pursuant to Article 25. A provision such as this could impact off-shore vehicles and hedge funds that have been active in the carbon markets.

Joint Implementation

In the absence of a continuation of the Kyoto Protocol or any break between compliance phases under the Kyoto Protocol, which measures the Annex 1 countries¹⁴ emissions caps with Assigned Amount Units, no ERUs can be issued with respect to greenhouse gas emissions reductions from activities from JI projects achieved after 1 January 2013. The Climate Change Package, however, proposes that harmonised rules may be adopted for issuing EU allowances or non-Kyoto offset credits in respect of projects relating to gases that are outside the EU ETS. Projects that address gases or industrial sectors outside of the EU ETS in Phase 3 may therefore allow JI to survive as a form of domestic EU offset scheme.

Clean Development Mechanism

The Climate Change Package proposal originally reflected a tension between its ambition of achieving compliance with its international obligations in a cost effective manner and its other ambition of converting Europe into a low carbon economy. In the end, these tensions appear to have been resolved in favour of the

¹³ As at the date of this client briefing there are 49 countries listed as "Least Developed Countries" with the United Nations Framework Convention on Climate Change. These include Bangladesh, Bhutan, Nepal, Uganda and the United Republic of Tanzania.

¹⁴ Essentially industrialised and developed countries (such as the UK, France and Australia).

former by allowing a greater amount of CDM credits to be used compared to the original Commission proposal and by the potential to use international offsets as a means to enable the EU to take on greater GHG reduction targets.

Where an international agreement is reached in Copenhagen in 2009 and the European Community thereafter agrees a mandatory reduction target for GHG reductions exceeding the 20% compared to 1990 level currently envisaged by the EU ETS Reform Directive, the Commission will prepare a report assessing what, if anything, the EU should do to amend the EU ETS Reform Directive. If changes are proposed, the Commission will also submit a legislative proposal for adoption by the European Parliament and Council of Ministers. Such a legislative proposal shall address the increased use by operators of (as appropriate) CERs, ERUs or other credits from non-Member State countries that have ratified the international agreement. The recitals of the agreed text suggest that, to meet such additional compliance obligations, further offset credits of up to half of the additional reduction effort taking place in the EU ETS may be used, including "high quality" CDM credits after 2013 from countries that have ratified the new international agreement.

It is expected, that if project credits from Land Use, Land-Use Change and Forestry ("**LULUCF**") projects that absorb carbon from the atmosphere are to be permitted for use for compliance within the EU ETS in Phase 3 (they were not permitted in Phase 1 or 2), or project credits from activities that reduce emissions from deforestation and degradation ("**REDD**") are to be recognised for compliance use within the EU ETS in Phase 3, the above mentioned legislative proposals will be utilised to achieve this.

Cross-Sectional Reforms

The timing of the EU ETS Reform Directive is such that its legislative proposals sit immediately after the implementation of Directive 2008/101/EC (the "**Aviation Directive**") which itself amends the EU ETS Directive to allow for the aviation sector to be brought within the EU ETS. Though the Aviation Directive could not predict the outcome of the negotiations between the EU Parliament and the Council of Ministers that took place soon after its adoption, it made a number of Phase 3 EU ETS proposals in respect to aviation, while leaving certain aspects to be determined by the subsequent negotiations. The resulting EU ETS Reform Directive, in its current form, has not materially amended any of the articles added to the EU ETS Directive by the Aviation Directive. Nevertheless, as the Aviation Directive's 2013 figures for allowance allocation, auctioning and CER/ERU usage¹⁵ were subject to further review, and aviation is now included in the list of sectors affected by the EU ETS, the provisions of the EU ETS Reform Directive as set out above will apply to the aircraft operators for the remainder of Phase 3.

The only significant respect in which the EU ETS Reform Directive treats the aviation sector differently from other EU ETS sectors is in the minimum percentage of CER/ERUs that aircraft operators will be entitled to use, which is set at no less than 1.5% (in comparison to the minimum 4.5% for new entrants and minimum 11% for operators in general).

Conclusion

The EU ETS Reform directive is a compromise package. The difficulties faced by the French Presidency of the EU during negotiations in December 2008, in trying to reach an agreement on the Climate Change package are demonstrated in the various carve-outs and derogations afforded to certain countries. The uncertainty over whether a pro-climate change administration will win the US elections in November 2008 and whether an international agreement would be concluded in Copenhagen at the end of 2009, coloured the Commission's draft proposals that were the subject matter of the EU's negotiations.

There is clearly an element of the EU 'hedging its bets' in the way in which the EU ETS Reform Directive delegates to the Commission powers to decide on significant policy issues impacting the shape of the EU ETS Phase 3. These include:

- (i) what sectors are likely to fall within the risk of carbon leakage and therefore will benefit from free allocation of allowances;

¹⁵ Please see out earlier client briefing note: "*Clearer Skies: Aviation and the EU ETS*", September 2008

- (ii) what principles will have to be followed by Member States when carrying out any auctions (e.g. timing and administration);
- (iii) what types of projects within the CDM or JI will meet the qualitative standards to be determined after 2013, how will these relate to new sectors and new entrants;
- (iv) how will the 300m allowances in the new entrants reserve be utilised towards CCS project funding and how will CCS projects that benefit from this be selected;
- (v) what sort of measures will be applied to deal with excessive EUA price fluctuations; etc.

In fact, no fewer than 13 items are reserved to the Commission under the comitology process in relation to the EU ETS Reform Directive. Together with the uncertainty over the international treaty negotiations this has translated into a lot of uncertainty for the market. The market has not reacted with as much optimism as had originally been anticipated following the agreement over the Climate Change package. In fact, at the date of writing this briefing note, EU allowance prices are recovering from an all time Phase 2 low. When combined with the reduction of emissions caused by the slowing of industrial output as a result of the current financial crisis, this has left many investors in the market pausing before making further investments into the climate change sector. The EU has also signalled that its role as market maker for the CDM is coming to a close, perhaps in recognition of the passing of the baton to the nascent emission trading regimes developing in Australia and the US. The signal from the EU to the international community is simple - 'We have done more than our share to support efforts to create a carbon market. Let's see the other Annex I Countries do their bit now.'

Table A

Summary of the key changes proposed by the EU ETS Reform Directive

ISSUE	PHASE 2 (2008-2012)	PHASE 3 (2012-2020)	ADJUSTED PROPOSAL IF INTERNATIONAL POST KYOTO AGREEMENT
Gases covered by EU ETS	Carbon dioxide (CO ₂)	Carbon dioxide (CO ₂) Nitrous oxide (N ₂ O) Perfluorocarbons (PFCs)	
Sectors covered by EU ETS	Please refer to Annex I of Directive 2003/87/EC for a full list of sectors currently covered by the EU ETS. Sectors include the energy and mineral industries, the production and processing of ferrous metals and, beginning in 2012, the aviation sector	Production of: - (CO ₂ from) the aviation sector and the production and processing of certain non-ferrous metals; - (CO ₂ and PFCs from) Aluminium production and processing; - (CO ₂ and N ₂ O from) nitric, ammonia, adipic, glyoxalic and glyoxylic acid production - all six Kyoto gases captured under CCS;	
National Allocation Plans	Each Member State is obliged to submit a NAP.	Individual NAPs are to be abolished and a single-EU wide cap is to be introduced.	The EU wide cap will be strengthened to achieve any targets imposed by the post Kyoto agreement.
Allocation	EU allowances are allocated to sectors at no charge (subject to limited auctioning).	Free allocation is to be phased out and auctioning will become the preferred means for allocation, with certain carve-outs for sectors at risk of carbon leakage and certain power production sector participants that benefit from country derogations.	The Commission reserves the right to revise or repeal the EU rules in respect of free allocation following entry into the post Kyoto agreement.
Auctioning	After free allocation Member States auction EU allowances to the different sectors up to a maximum of 10% (15% for the aviation sector).	Auctioning will be the means in which EU allowances will be allocated to sectors with the phasing out of free allocation.	

ISSUE	PHASE 2 (2008-2012)	PHASE 3 (2012-2020)	ADJUSTED PROPOSAL IF INTERNATIONAL POST KYOTO AGREEMENT
Registries	EU allowances are currently issued by Member States in their respective national registries.	EU allowances should be issued and held in the Community registry and not national registries.	
Use of CERs and ERUs	<p>CERs and ERUs may be permitted to be used for compliance by Member States at their discretion so long as they do not arise from project activities relating to nuclear or LULUCF.</p> <p>For the aviation sector in 2012 CERs and ERUs can make up, at most, 15% of the allowances surrendered.</p>	<p>CERs from CDM projects that were registered after 2013 may be used if the host country for the CDM project has ratified the new international agreement. Where no international agreement has been reached, the use of such CERs will be subject to levels agreed by the EU with the host countries of such projects.</p> <p>In the absence of a post Kyoto agreement ERUs issued from 2013 onwards will not be permitted within the EU ETS.</p>	If the annual cap under the EU ETS needs to be reduced following the ratification of a satisfactory international post Kyoto agreement, then the limit on the use of CERs and ERUs within the EU ETS will be increased to half of the additional reduction effort.
Banking of CERs and ERUs between phases	Member States have discretion to limit the extent of banking of CERs/ERUs for companies in EU ETS, while remaining nationally below the 2.5% of assigned amounts limit for both JI and CDM.	<p>Surplus CERs and ERUs from Phase 2 will be exchanged for Phase 3 EU allowances until 31 March 2015, up to the amount of the unused portion of the operator's CER/ERU surrender cap in Phase 2, provided that the CERs and ERUs are from project types that are accepted by all Member States.</p> <p>CERs and ERUs issued during Phase 3 for projects registered during Phase 2 can be exchanged for Phase 3 EU allowances upon request, up to the amount of the unused portion of the operator's CER/ERU surrender cap in Phase 2, provided that the CERs and ERUs are from project types that are accepted by all Member States.</p>	

ISSUE	PHASE 2 (2008-2012)	PHASE 3 (2012-2020)	ADJUSTED PROPOSAL IF INTERNATIONAL POST KYOTO AGREEMENT
		CERs from CDM projects in Least Developed Countries that were registered and started after 2013 may be exchanged for EU allowances up to the amount of an operator's unused CER/ERU Phase 2 cap, provided that the project types are accepted by all Member States.	
Linking	The EU ETS can only be linked to countries that have ratified the Kyoto Protocol.	The EU ETS is to be extended to permit linking the EU ETS to any country or administrative entity which has established a mandatory cap and trade system.	

Clifford Chance Contacts

To discuss any of the issues in this publication, please contact:



Claude Brown, Partner (London)

Claude Brown is a partner in the Capital Markets Group and co-head of the firm's Climate Change Group. He has over 18 years' experience in the derivatives market as a practitioner and lawyer and specialises in emissions trading (including the EU ETS, JI and CDM credits) and other environmental issues.

T: +44 20 7006 1447

E: claude.brown@cliffordchance.com



Peter Zaman, Partner (London)

Peter Zaman is a partner in the Capital Markets Group and head of the firm's Environmental and Climatic Trading Group. He specialises in all aspects of over-the-counter and structured energy derivatives in gas, electricity, commodities and greenhouse gas emissions. In the greenhouse gas context, Peter specialises in CDM, JI, the EU ETS and the voluntary markets. He also specialises in advising on credit risk issues (including collateral structures) and the drafting and negotiation of derivative documentation for structured arrangements such as securitisations.

T: +44 20 7006 8827

E: peter.zaman@cliffordchance.com

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