THE CHURCH OF ENGLAND

ARCHBISHOPS' COUNCIL

House of Bishops' Europe Panel
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Chairman

A Submission by the House of Bishops' Europe Panel to the Defra Consultation on the Proposed EU Emissions Trading System from 2013.

Overview

1. The House of Bishops' Europe Panel is a sub-committee of the House of Bishops. It acts as a point of reference for items affecting the Church of England's relations with Europe and the European Union institutions.

2. The Europe Bishops' Panel (EBP) welcomes the opportunity to contribute to the Department for the Environment, Food and Rural Affairs' Consultation on proposed EU Emissions Trading System from 2013. Over the last three years the EBP has devoted a considerable portion of its time to the European Climate Change Programme in general and the proper functioning of the ETS in particular. This interest reflects the seriousness with which the Church takes the threat that climate change poses to the integrity of God's creation, the vocation of humanity to actively steward and care for creation, and the awareness that climate change is already impacting disproportionately on many of the world's poorest communities.

3. Recognising that British climate policy and the global process is largely being shaped in Brussels, not London, the Church appointed in November 2007 a representative to the EU institutions. Based in Brussels this office is responsible for articulating and advocating fresh thinking regarding the EU's progression to a low carbon economy. This submission is reflective of this work.

Executive Summary

4. The EU's ETS, the jewel in the crown in the EU's climate change programme, is the prototype for a global carbon market. It provides a cost effective and economically efficient way of cutting greenhouse gas emissions by enabling reductions to be made wherever they are cheapest. The EU deserves credit for establishing this project, even if its environmental impact to date has been limited. The ETS remains a project under construction. The Commission's proposals for ETS reform provide a crucial opportunity to learn valuable lessons from its early operation to improve both its simplicity and predictability. The Commission's proposals need to be judged from the perspective of environmental effectiveness and the degree to which a reformed ETS can stimulate the innovation necessary to achieve a low carbon and sustainable economy.

5. The Commission’s proposals present a significant advancement on the current arrangement.
    a. We support the decision to restrict the scheme’s scope to heavy industrial emitters, rather than widening its remit to include other sectors such as agriculture and surface transport. This should give the scheme greater market cohesion and simplicity.
    b. We hold that replacing national caps with an EU-wide cap comprising Europe-wide sectoral limits distributed to the individual member-states represents a significant breakthrough. It would remove one of the major variables that have contributed to the scheme’s volatility.
    c. We favour an automatic transition to 100% auctioning of allowances in 2013, but the proposal to progressively move to full auctioning ensures at least that the ‘polluter pays’ principle is central to the scheme’s operation.
    d. We welcome the proposal to remove current restrictions on the linking of the EU’s ETS to other cap-and-trade systems. This opens the way for greater international collaboration, not least with the USA.
    e. We welcome the move to tighten access to the offset market. External credits need to supplement rather than supplant the drive for domestic emission reductions, without undermining the EU’s wider international responsibility.

6. In a number of areas, however, the proposals are insufficient and more radical reform is needed:
    a. We remain concerned that the EU’s reduction targets are not aligned with prevailing scientific evidence. Setting more stringent emission reductions targets now would arguably provide additional incentives for companies to invest in innovative technologies.
    b. We recommend that the future management of the ETS be given to an independent European Carbon Bank. A carbon market is only as effective as the institutions that oversee it. The absence of a strong central and independent authority undermines the scheme’s effectiveness.
    c. We agree with the proposed redistribution of auctioning rights on the grounds of economic justice, but we think that the decision to permit some member states to increase emissions in the non-ETS sector is short-sighted both economically and environmentally.
    d. We are concerned that most of the emission reduction within the ETS will be achieve by a one-off shift from coal to gas, rather than by the introduction of new clean technology such as carbon capture and storage (CCS). Further consideration needs to be given to how technological innovation can be funded and commercialised.
    e. We believe that innovative green technology could be commercialised through public–private partnerships using the revenues accrued from the auctioning of allowances under the ETS. The Commission’s proposal allows for this possibility but it fails to make sufficient provision for it.

Response to Questions

Q1. Do you agree with using a broad definition of a combustible installation?

A broad definition of a combustible installation would provide greater consistency of coverage across Member States, which in turn would make monitoring and verification simpler.

Q2. Do you think the activities listed at Annex 1 of the revised Directive mean a broad definition has been achieved? If not, what amendments would be needed to the Directive to achieve this?

We are satisfied that the activities listed at Annex 1 of the revised Directive are consistent with a broad definition of a combustible installation.

Q3 Would a 10,000 tCO2 or 25,000 tCO2 emissions threshold be most appropriate?

A 10,000 tCO2 represents the best balance between ensuring the system's environmental effectiveness and reducing administrative costs for the smallest emitters. Moving to a 25,000 tCO2 emissions threshold would increase substantially the amount of emissions lost to the ETS so undermining the schemes environmental effectiveness.

Q4. Should all installations be eligible to apply to opt out, not just combustible installations with a thermal rated input of less than 25MW?

Allowing all installations with a thermal rated input of less than 25MW to opt out of the EU ETS would provide for greater consistency and transparency across the system.

Q5. Do you agree with the Commission's proposals to include:

- **CO2 emissions from petrochemicals production, ammonia and other chemicals including process emissions?**
- **CO2 and PFC emissions from the production of aluminium (both primary and secondary)?**
- **N2O emissions from the production of nitric, adipic and glyoxal and glyoxylic acid pollution?**
  Please give your reasons

The inclusion of these sectors would increase the system's scope and its environmental effectiveness. It would introduce new abatement opportunities and potentially lower abatement cost. We recognise the Government's concern regarding the inclusion of the aluminium sector, but we hold that its fears regarding the risk of carbon leakage are best addressed through the evidence based review that the Commission is mandated to undertake by June 2010. We also note that the Commission's own impact assessment, regarding the competitive intensity of the global aluminium sector, concluded that the risk of relocation, a trend already evident within this sector long before the ETS became operational, is likely to be affected by a range of variables (i.e. access to cheap energy, geographical location etc) rather than just one.

Q6. Do you support inclusion of methane from active coalmines in the EU ETS? If not, how else might this sector's methane emissions be regulated?

Including methane from active coalmines would improve the scheme's environmental effectiveness and its economic efficiency.

Q7. Do you agree with the proposed method for including CCS? If not, please provide your reasons and evidence

Although only a few CCS projects will be operational by the end of Phase III, explicitly bringing CCS within the EU ETS would send a clear signal as to the future of CCS under the ETS so increasing investor confidence in the technology.

Q8. What are the key issues to consider in any cost benefit analysis of whether and how surface transport (road and rail transportation, and inland shipping) may be included in the EU ETS?

See response to Q9.

Q9. What are the key issues for consideration in a cost benefit analysis of whether and how international shipping may be included in the EU-ETS?

The following response relates to both Q8 and Q9.

We are encouraged that under the current proposals the Commission has restricted the scheme to heavy industrial emitters. These sectors provide well-verified data and clear potential for reductions in emissions, which are essential ingredients for the effective working of any emissions trading scheme. It follows that we agree with the Commission's decision not to include surface transport or shipping within the ETS. Although both sectors generate significant greenhouse gas emissions, emissions that are predicted to rise in coming years, further analysis is required to decide whether the ETS is the most appropriate mechanism to deal with either sector. Reaching a global sector agreement through the International Maritime Organisation would be the most effective mechanism to address shipping. Rising transport emissions is best addressed by other regulatory means, such as by road pricing and by imposing stringent emissions standards for cars.

Q10. Do you agree that the EU agriculture, forestry and land management sector should not be included in the EU-ETS at this stage?

We agree with the decision to exclude agriculture from the scope of the scheme. The agricultural sector comprises a very large number of small businesses whose emissions would be hard to verify. Monitoring costs would naturally be very high.

Q11. Do you agree with the Commission that installations exclusively burning biomass should not be covered by the EU-ETS Directive from 2013?

On balance we support the move to exclude those installations exclusively burning biomass from the ETS from 2013. This would reduce administrative costs and would close of the opportunity of these installations accruing windfall profits by selling on allocated allowances.

Q12. Do you agree with the level of the Central Cap proposed by the Commission for meeting a 20 per cent EU GHG reduction target? If not, why

We think the 20 per cent target un-ambitious. It is clearly not aligned with prevailing scientific evidence. We accept, however, that the level of the Central Cap would meet the 20 per cent target.

Q13. Do you agree with the Commission's proposal for a linear reduction trajectory of 1.74 per cent per year to be reviewed by 2025? If not, why not?

The 1.74 per cent linear reduction trajectory provides much greater predictability and certainty for business and the wider public. It should, if implemented, deliver on the EU Central Cap within the timeframe provided by the EU.

Q14. Do you agree with the Commission's proposal for an automatic adjustment to a higher target when an international agreement is reached?

As per the response to Q12, we believe the existing reductions of 20 per cent by 2020 and 30 per cent by 2030, subject to an international agreement, woefully inadequate when set against the evidence provided by the 2007 Assessment Report by the Intergovernmental Panel on Climate Change that argues convincingly that industrialised countries should take on reduction targets of between 25 per cent and 40 per cent below 1990 levels by 2020.

Q15. Do you believe that there is a role for European Carbon Bank and what functions should it perform?

We recommend that the future management of the ETS be given to an independent European Carbon Bank. A carbon market is only as effective as the institutions that oversee it. The absence of a strong central and independent authority undermines the scheme's effectiveness. An independent body comprising technical, economic and financial expertise charged with managing the scheme's operation would be preferable to current arrangements. Just as the European Central Bank is mandated with the responsibility for controlling inflation within the Euro-zone, so an ECB could be mandated with taking whatever steps are considered necessary to create and sustain a transparent and efficient carbon market. Detaching the ETS from politicians' electoral cycles would eliminate the dangers of political horse-trading generally associated with 'comitology'. This would provide additional market assurances to business and investors. It is difficult to conceive how current arrangements are sustainable long term when the EU's ETS is linked with other trading systems.

Q16. In terms of amending the rules of the system, do you favour a continuation of five year phases or a shift to eight year phases? Please state the reasons for your views?

If the move to a European Carbon Bank is accepted the length of the phase become less important as corrective measures can be introduced to correct any market distortions so maintaining/restoring market confidence. In the absence of a European Carbon Bank, we believe that the shift to an eight year phase strikes the right balance between flexibility and predictability. In particular we believe that it would provide greater market certainty by better aligning the ETS with investment cycles.

Q.17 Do you agree with the Commission's proposals for banking and borrowing? If not, why not?

The proposals are necessary and important to smooth prices and also to protect against potential abuse of banking and borrowing opportunities.

Q18. Do you agree with the Government's position on harmonised minimum levels of auctioning across the EU?

We are sympathetic to the Government's position on harmonised minimum levels of auctioning across the EU, but we believe that such an approach while providing for some degree of market flexibility risks distorting the market and in turn creating an even playing field.

Q19. Do you agree with the Commission that on-site production of electricity should be faced with 100 per cent auctioning from 2013, being treated the same way as the electricity generators?

N/A

Q20. Do you agree that providing free allowances for electricity generators for heat producers under CHP is an adequate incentive for this technology? If not why not? How should emissions associated with hear be calculated

N/A

Q21 Do you agree with the Commission that all other sectors including aviation – with the exception of those demonstrably at significant risk from carbon leakage – should move to full auctioning with free allocation starting in 2013 at 80 per cent of their share of verified emissions for the period 2005-2007 and reducing by equal amounts each year? If not, why not?

N/A

Q22. Do you agree with the Commission's and the Government's criteria for determining which sectors are at significant risk of carbon leakage? If not, why not and explain the rationale behind any alternative criteria you propose.

It is crucially important that any criteria are stringent and credible.

Q23 Do you agree that free allocation helps to significantly reduce the risk of carbon leakage? If not, why not?

We agree with the Commission's prior assessment that auctioning of allowances, as the basic principle of allocation, is simple, transparent and efficient. It creates the greatest incentive for investment in a low carbon economy by forcing the market to factor in the cost of carbon. It best complies with the 'polluter pays' principle, and it avoids giving windfall profits to those sectors that have previously passed on the notional cost of allowances to their customers despite receiving them for free. We recommend that unless a pressing and convincing case can be made otherwise, 100 per cent auctioning of allowances should be the norm for all sectors covered by the ETS from 2013 onwards.

We are therefore disappointed that the Commission has deviated from its own assessment on the grounds that it is prudent to use the period 2013-20 to phase out the free allocation of allowances so minimising the risk of carbon leakage. Research provided by the Carbon Trust shows that except in a few sectors (steel and cement) the threat of companies moving to countries with less stringent environmental rules is exaggerated. The Carbon Trust estimates that just 1% of EU emissions will be off-shored by 2020 as a result of the ETS. Even if carbon leakage is a possibility, we question whether the free allocation of allowances is an effective counter-mechanism. The Commission's own impact assessment concluded: "Allocating allowances for free does not appear to be an efficient or even effective instrument to remedy impacts on competitiveness".

We hold that the more the EU deviates away from 100 per cent auctioning allowances the less transparent and efficient the ETS becomes. It potentially reduces the incentives for investment in a low carbon economy. It also threatens to create new areas of tension between member states as to how allowances to be allocated for free should be distributed. The Commission's proposal to resolve this issue through committee procedure, using a formula combining a top-down approach to determine the total level of free allocation and a bottom up approach to agreed benchmarks lacks clarity. The Commission's proposal risks distorting the market and diluting the 'polluter pays' principle.

Q24 Are there any alternative methods for addressing carbon leakage that you favour?

As explained in response to Q23, we believe that except in a few sectors (steel and cement) the threat of companies moving to countries with less stringent environmental rules is exaggerated. Although the ETS remains a project under construction, we believe that those sectors that fear a loss of competitive edge have sufficient time before the introduction of the new measures in 2013 to take corrective measures to ensure their competitive advantage without needing to consider relocating outside the territory of the EU.

Q25 Do you agree with the Commission's proposals to undertake a thorough evidence-based review of sectors which may be at risk of carbon leakage in time to propose solutions in 2011?

In view of the responses to Q22-24, we hold that it is imperative that the Commission's decision to undertake by 2010 an evidence-based review of sectors that may be at risk from carbon leakage is independent and resilient to industrial lobbying. If the proposal for a European Carbon Bank is accepted, such a review should fall within the Bank's remit of operations. We are encouraged, however, by the timing of this review. Securing an international framework agreement on climate change in Copenhagen in 2009 should help address the political concerns that member states have regarding the loss of competitiveness through carbon leakage.

Q26. Do you believe that sectoral agreements are a plausible solution to the risk of carbon leakage? If so, for which sectors and in what form and to what timescales do you believe they might be achieved?

Any decision on the feasibility and desirability of establishing sectoral agreements to manage the risk of carbon leakage needs to be informed by the evidence based review that the Commission is obliged to undertake by 2010.

Q27. Do you agree that free allocation should be based on EU-wide benchmarks? If not, how should free installation be distributed between installations

In those exceptional cases where the free allocation of allowance is necessary, the issuing of these allowances according to EU-wide benchmarks would best avoid competitive distortions and other adverse effects to the smooth operation of the ETS.

Q28 Do you agree with the Commission proposal that there will be no sector-caps with harmonised bottom benchmarks being used to decide the sub-cap for free allocation?

Provided that cross-sector harmonisation can be achieved to avoid market distortion, bottom-up benchmarking looks a like a plausible approach.

Q29. Do you agree that there should be an EU-wide NER, based on a percentage of the overall cap?

An EU-wide NER would help to ensure a level playing field in the internal market.

Q30. Do you agree with the Commission proposed level for the NER of five per cent of the overall EU cap or do you agree with the Government's position that it should be a lower percentage? What should the percentage be? Please give reasons for your answers

The exact percentage should be dependent on how competitive the market is predicted to be. This raises a broader question of whether the NER is intended to support competition in a broad sense, because removing trade barriers is a general EU aim, or is it a specific mechanism to reduce carbon emissions by involving new, low-carbon entrants in the market?

Q31 Do you agree with the Commission proposal that installations which close should not receive any further free EU-ETS allowances or that they should receive a longer period of free allocation? Please include why you support each approach.

N/A

Q32. Do you agree with the definition of a new entrant in the Commission's proposal? If not, why not?

Yes.

Q33. Do you agree with the UK position that there should not be a system of hypothecation or earmarking of auctioning revenues?

The Commission proposes that 20 per cent of revenue auctions should be ring fenced for climate related issues. We welcome the Commission's proposal in principle, but we think that the 20 per cent figure is far too low and needs to be reconsidered. Auctioning revenues should not be used or seen by member state governments as a 'windfall profit'. Rather, they present an opportunity to finance the substantial investments needed in technological responses to climate change within the EU as well a contributing to adaptation and mitigation projects in vulnerable countries in the developing world. We recognise the resistance of some member state governments, not least the British Government, to imposing legally binding hypothecation at an EU level, but we believe that, in the absence of clearer investment signals from national governments, as well as any progress in reforming the EU budget, the move would be warranted and in keeping with the findings of the Stern Commission.

Q34. Do you agree with the Commission's proposals to make the basis for distributing auctioning allowances a Member State's share of 2005 emissions?

Yes.

Q35. Do you agree with the UK position that there should not be a system of redistribution of allowances to be auctioned? If not, why not?

We support the Commission's proposal allowing for a 10 per cent redistribution of auction permits away from those members states that have an average income-per-head that is more than 20 per cent above the EU average, except where the whole climate and energy package is estimated to exceed 0.7 per cent of GDP. This makes economic sense given the weak economic performance of many newer member states. It is also equitable in that the arrangement takes account of the different levels of development across the member states. The level of redistribution suggested by the Commission would not, however, diminish the pressure on companies based in these countries to lessen their efforts to reduce emissions. In the absence of any reform to the EU's budget, the proposal would provide newer member states with additional auctioning revenue to assist with any structural adjustment programmes.

We believe, however, that the redistributive features of the Commission's proposals would carry greater weight if there were harmony across the EU regarding the distribution of emissions caps for the non-ETS sectors. Under current arrangements, poorer member states will be permitted to increase their emission in non-ETS sectors by up to 20 per cent while richer member countries will have to cut their emissions by up to 20 per cent. The analysis provided by Simon Tilford, from the Centre for European Reform, in his May 2008 article, *How to make EU Emissions Trading a Success*, provides a clear warning as to the dangers of such an unfettered approach. Internationally, the EU can hardly expect China and India to place caps on their own emissions, while it is at the same time exempting relatively wealthy countries such as the Czech Republic or Poland from taking similar action. Long term, once the burden-sharing agreement is phased out, such an arrangement risks leaving new member countries at a competitive disadvantage. A better solution would be to either use the EU budget more creatively or use the revenues accrued from auctioning to subsidise the costs of energy efficiency measures in poorer member-states.

Q36. Do you agree with the Commission's proposals for a Regulation to ensure auctions are open, transparent and non-discriminatory?
Yes, these are necessary ingredients for the effective operation of the EU-ETS.

Q37. Which elements of auction design would you support or oppose being set by the Commission?
N/A

Q38. Do you agree with the Commission's proposed timetable for the auction design regulation of 31 December 2010?
The timetable propose by the Commission provides sufficient time for the market to prepare for the auction s avoiding some of the problems associated with earlier phases of the scheme.

Q39. Do you agree with the Commission's proposal to include the possibility of linking to national, sub-federal or regional entities? if not, why not?
We welcome the Commission's proposal to removal of all restrictions on external linking to allow linkage with regional, national or sub-federal systems. Current provisions have enabled the ETS to link with those Annex B countries that have ratified the Kyoto protocol. This has permitted linkage arrangements with Iceland, Norway and Lichtenstein, but these same provisions have handicapped the EU in taking forward negotiations with other third parties. Ideally, the EU's ETS would only be linked with those systems covered by an international agreement, but the proposals are sufficiently flexible to allow linkage in the absence of such an agreement. The EU should continue to press the USA to sign up to a post-2012 agreement, but the revisions to the ETS directive sensibly provide the opportunity for closer collaboration between the EU and the US regardless.

Q40 Are the Commission's criteria for linking the EU ETS with other systems the right ones? If not, why not?

The decision by the Commission to list ten criteria against which any impact assessment study will be conducted is helpful. The question remains, however, whether the decision to link to another emissions trading system will be taken on political rather than technical grounds, and the degree to which any decision will inspire market confidence while preserving the environmental integrity of the EU's-ETS. We recognise that member states will ultimately want to reserve for themselves the final decision, but we suggest that the responsibility for any impact assessment study should be entrusted to an independent European Carbon Bank rather than being left to the Commission.

Q41. Do you agree that consideration should also be given to the type and limits on credits from baseline and credit systems.

Even a cursory glance at the diversity of emissions trading bills in front of the US Congress, with their differing scope and application regarding external credits, highlights the importance of taking this issue into consideration when undertaking any impact assessment study.

Q42. Do you agree with the Commission proposal to recognise credits post-2012 in anticipation of international agreement:

a. From projects approved before 2013 up to the remainder of credit limit in Phase 1?
b. From projects in less developed countries approved after 2012?
c. Subject to the potential exclusion of CERS from particular projects established before 2013 by individual member states?

If not, why not?

Q43. Do you agree with the Commission proposal that once an international agreement is reached:

a. Access to project credits to increase by 50% of the increase in absolute emissions reductions (i.e. half of the shift from the 20 per cent to the 30 per cent greenhouse gas emissions reduction targets).
b. Access is limited to project credits from third countries that have ratified the agreement.

If not, why not?

Q44. Do you agree with the Commission proposal that if an international agreement is delayed beyond 2013, the European Community should seek bilateral agreements with third countries to enable access to project credits to the extent that the limits from Phase II have not been used up? If not, why not?

Q45. Are the project credit limits that would result from the Commission's proposal at the right level? If not, why not?

Q46. Do you agree that the project credit limits in Phase III should be harmonised? If so, how can this be best achieved?

The following response relates to Q42-Q46.

We recognise that the CDM provides a market mechanism by which companies can earn emission credits by investing in developing countries. A 2007 report by Lehman Brothers, *The Business of Climate Change: Challenges and Opportunities*, indicates that by mid-2007 EU member states had committed to investing 7.5 million Euros by 2012 under the CDM and JI. These investments promise a reduction of more than 2 billion tonnes of carbon dioxide. The CDM therefore provides a source of technological transfer to assist developing countries in introducing cleaner energy.

In theory at least, it does not matter where the emissions reduction take place as the environmental effect is the same. In practice, however, the primary political purpose of the EU ETS is to provide a market mechanism by which the EU meets its emissions targets by decoupling economic growth and emissions. Unless the EU and other developed economies can drastically cut their own emissions it is difficult to see how they can persuade developing economies to stabilise and in time reduce their own emissions. It is self-defeating when a country such as Spain is only able to meet its Kyoto target by extensive use of the CDM and JI. The Commission calculates that in the absence of an international agreement carbon prices within the EU ETS could fall to as low as 4 Euro per tonne if the EU maintained its current stance on imported credits and if there was no successor to Kyoto.

It follows therefore that regulating access to the CDM must be done in such a way that it does not undermine the market incentive for companies to invest in new green technologies at home, nor close of developing countries access to clean technologies. The Commission is therefore right to impose stricter controls on the use of imported credits under the CDM, especially in the absence of an international agreement. However, it would be far more effective to make provision for the reduction targets to be met within the boundary of the EU and for the financial equivalent of an additional 15 per cent emissions reduction to be invested in developing countries to assist them with their adaptation and mitigation efforts.

Q47. What provisions should be made in respect of the scope of recognition of credits in advance of international agreement, in particular should particular sectors be included or excluded in advance, and if not what provisions should be made for inclusion and exclusion of sectors upon international agreement?
N/A

Q48. Do you agree that credits from LULUCF projects could potentially be included in the EU ETS in the future? If so, how can the problems with inclusions of these credits be overcome?
The problems associated with including credits from LULCUF projects in the EU ETS are well documented. Until these problems are resolved, it makes more sense to tackle this matter through specific mechanisms that operate independently from the EU ETS.

Q49. Do you agree with the Commission's proposals to provide credits from European Community projects? If not, why not?
In light of the response to Q42-46, it follows that this submission holds that domestic offset projects should continue to be excluded from the EU ETS. The

purchase of offset project credits should be additional to and not instead of a strong focus on domestic emission reductions. Inclusion of domestic offsets may make it more complicated to determine the direct contribution of the EU ETS sectors to EU greenhouse gas emission reduction targets and to determine whether they are playing their fair share or not. There is the risk of double counting of emissions reductions - both as a contribution to meeting the EU ETS cap, and towards achieving the effort sharing targets

Q50. Do you agree with the Commission proposal to introduce a Regulation (to be agreed by the Commission-chaired committee of Member State representatives) to replace guidelines on monitoring and reporting?

We note the Government's reservation with this proposal, but we hold that a Regulation will ensure a more consistent application of the MRG across member states than has hitherto occurred under existing arrangements.

Q51. Do you agree with the Commission proposal to introduce a Regulation (to be agreed by the Commission- chaired committee of Member States representatives) for harmonised verification and accreditation? If not, why not?

Harmonised verification and accreditation would remove the large diversity of systems currently employed across Member States so contributing to a more level playing field.

Q52. Do you agree with the Commission proposal that the excess emissions penalty index should increase automatically in line with the European Index of Consumer Prices? If not, why not?

It makes sense to move from a system of fixed financial penalties, which will decline in real terms with inflation, to a mechanism that allows the absolute level of the penalty to be increased with inflation.

Q53 Do you agree with the Commission's proposal for a central registry run by the Commission? If not, why not?

The proposal to set up a central registry is a necessary and welcome cost effective step that would provide the EU ETS with the infrastructure and technological framework necessary to run effectively. We think, however, that in view of the concerns expressed in the Defra consultation paper that consideration should be given to whether this central registry should be run and managed by a European Carbon Bank.

Q54. Do you have any further views on any aspect of the Commission's proposals to amend the EU ETS from 2013?

We suspect that the emissions targets for the sectors covered by the ETS will to a large extent be met by a one of shift from coal to gas, rather than through investment in low or zero emission technologies such as carbon capture and storage. This raises a number of related problems. A higher dependency on gas carries with it significant geopolitical and economic risks. The projected economic growth in China and India means that competition for gas supplies will become ever more intense with the threat of higher prices. The location of the principle sources of natural gas in many of the unstable regions of the world means that gas supplies are not necessarily dependable.

If as analysts predict, CCS could potentially reduce the EU's carbon dioxide emissions by half by 2050 then further efforts need to be made to commercialise this technology. The Commission's proposals to change the regulatory framework for CCS is helpful, but it will not lead to its adoption on an industrial scale. This will only occur when the price per tonne of carbon avoided by use of CCS is lower than the price of carbon. Ironically, the EU's drive on renewable energy could depress carbon prices and thereby reduce further the incentive for power companies and industrial plants to adopt new technologies.

Resolving this issue requires a concerted and coordinated effort at the European to provide the necessary political and financial support to those CCS projects currently underway in the EU. Commercialising CCS would have domestic advantages, in that it will provide the technological innovation necessary to meet the more stringent emission reductions that many scientists anticipate the EU will need to make in twenty or thirty years time. It would have wider commercial advantages in that European companies would be well placed to play a significant role in the development of a low carbon economy in China and India. The EU could subsidise the transfer of this technology to both countries in exchange for action to curb emissions.

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