INTERNATIONAL EMISSIONS TRADING ASSOCIATION

EPRI Energy & Climate Change Research Seminar

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Overview

1. Introduction
2. International Negotiations
3. Global Update
4. IETA Priorities, Challenges & New Ideas
5. Q&A

Durban Platform for Enhanced Action (DPEA)

- Establishes a negotiating process to develop a new post-2020 "protocol, legal instrument or agreed outcome with legal force" that will apply to all Parties under the FCCC.
- Establishes a 2nd Kyoto Protocol (KP) Commitment Period for interested Parties.
- Operationalizes the Green Climate Fund.
- Implements other key elements of the Cancun Agreements, including the MRV guidelines, the Adaptation Committee, the TEC and the CTCN.
- Negotiations for this year set for Doha, Qatar

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New KP 2nd Commitment Period

- To start 1/1/2013 when KP1 expires, and will run either for 5 years (2018) or 8 years (2020), to be determined next year by further negotiations

- KP 2nd commitment period to apply to 39 countries – mainly the 27 members of the E.U., Australia, New Zealand, Norway and several former Soviet states.

- U.S., Canada, Japan and Russia will not participate

- Canada formally dropped out of the KP, a few days after COP-17 in Durban ended

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New Agreement to be Completed 2015

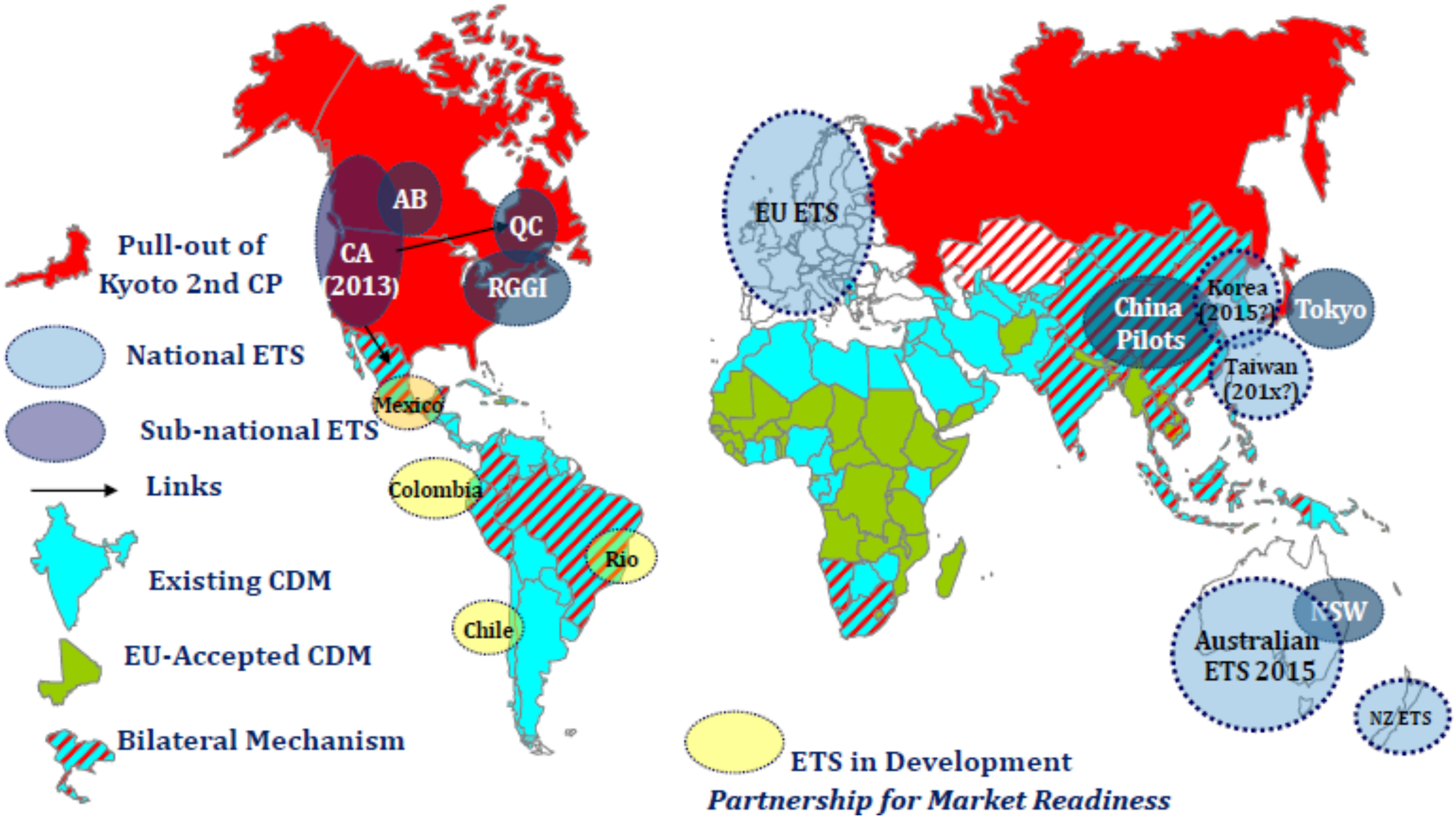
- Merge the current two-track negotiating process into one track called the "Ad Hoc Working Group on the Durban Platform for Enhanced Action" (AWG-DPEA)

- End the exemption from binding emissions reductions currently enjoyed by developing countries (e.g., China and India, Brazil, S. Africa, S. Korea, etc…) enshrined in the Berlin Mandate (1995) and the KP. This is a significant development in the climate negotiations.

- Parties that do not have binding emissions reductions commitments under the KP (e.g. US, BASIC) will be "politically" bound to meet their Copenhagen commitments, enshrined in the Cancun Agreements through 2020.

- Final language does not stipulate that all Parties will have to undertake equal actions, only that the agreement would apply to all Parties

The Trading World Jan 2012



Source: Perspectives, updated by IETA 2012

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ETS Implementation

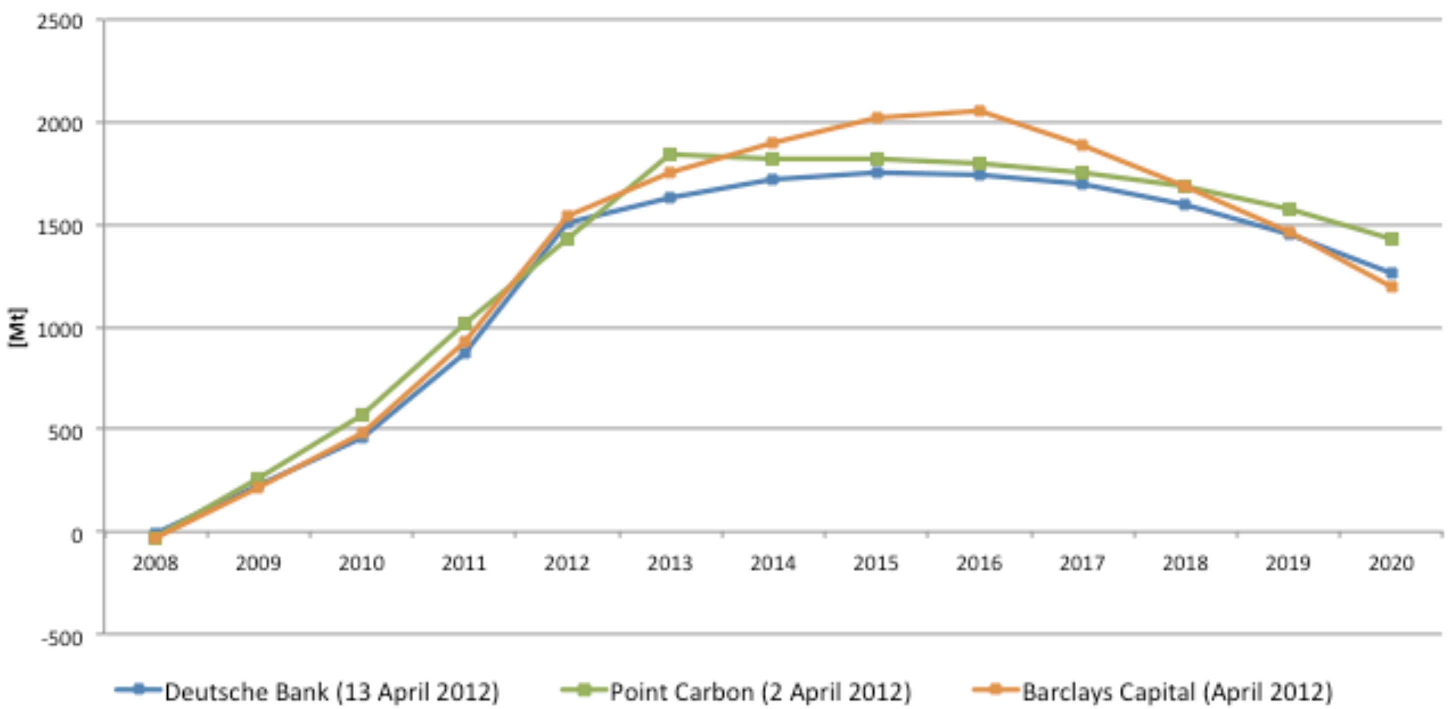
Done ✔	To be done ✖
Carbon leakage Sectors	Final offset use limit
Benchmarks for free allocation (52, plus fall-back BM)	2013 allocation (transitory free allocation, cross-sectoral reduction factor, auction profile)
Restrictions on ind. gas	Further offset restrictions?
Revised registry rules (security)	Transition to Union Registry
Revised auction regulation	Common transitory platform & auction monitor & annex opt-out platforms
NER300: 1st tranche (200m)	NER 300: 2nd tranche (100m)
Inclusion of int. aviation	Exclusion of outgoing flights where equivalent measures

Registry: security top of agenda last year

Type of fraud	Description	Loss*	ETS specific?	Stopped by regulatory action?
CER Recycling **Feb 2010**	Legitimate resale of offset credits that have been surrendered for compliance, recycling into EU ETS illegitimate.	800.000 offset credits	Yes.	Yes. Direct retirement upon surrender.
VAT fraud mid-2009	VAT-free cross-border sale of allowances followed by VAT-able domestic supply. Trader pockets VAT and disappears.	€ 5 bn	No.	Introduction of reverse charge rules in some but not all MS. Need for EU-wide action.
Phishing	Emails sent to account holders asking for refreshing log-in details via phishing website.	250.000 allowances	No.	No. Email of account holders remain visible in CITL.
Cyber-attack	Organized hacking into registries/companies: Trojan horse virus, email flood, etc. (5 MS concerned)	3.4 m allowances (0.001%)	No.	All ETS registries closed on 19 Jan 2011. Only 19 re-opened to date. Market activity 70% below pre-closure for spot market. Last attack end-2011 on Spanish Registry.

*Estimates from EU Commission/Europol.

EU ETS – Longer by the day….



Source: IETA based on Deutsche Bank. Point Carbon, Barclays Capital estimates of EUA surplus allowances

Proposals to 'fix' EU ETS

- **Tighten the target from 20% to 30% by 2020**
  - Pledged in Copenhagen, but no formal change made
  - Dependent on other countries taking significant targets
- **Create a "set aside" to act as a market reserve**
  - Market concern on terms/conditions of use of set aside in future
  - Effort to include it in Energy Efficiency Directive in EU Parliament
  - Some progress, but political process difficult
- **Set a minimum auction price and bank unsold units**
  - Not under active consideration
- **Shift the auction profile**
  - Why sell volumes in a long market?
  - Commission planned to auction more at beginning, declining during period
  - Potential shift to auction less at beginning, and more towards the end

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EU & Aviation – experiencing turbulence

- First compliance date April 2013 – expected to be second largest source of demand in EUETS
- International political pressure rising inexorably: 26 opposed nations met in Moscow on February 21
- US legislation passed in both Houses; demanding suspension of EUETS application to aviation; even least opposed airlines want EU airspace only
- Commission signalling willingness to move to departing-flights only if ICAO produces a global agreement fast
- Most airlines complying so far; but market could be disrupted

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Tomorrow's carbon markets

Declining Order of Size

EUETS	Yes
Kyoto Sovereign Purchases	Yes
Voluntary Market	Yes
RGGI	
Japan (Keidanren)	Yes
New Zealand	Yes
Switzerland	Yes
Tokyo, Alberta; NSW	

Declining Order of Certainty

India PAT	
California	Probably
Chinese Pilots	
Australia	Yes
British Columbia/WCI	Possibly
S Korea	Possibly
Taiwan	Possibly
Brazil	
Chile	
Japan	Yes

Future of the CDM

Market conditions

- Supply – demand balance
- Bad investment climate (regulatory decisions with retro-active effects)
- Use restrictions in existing and emerging emissions trading schemes
- Shrinking of market and withdrawal of capital, know-how, skills

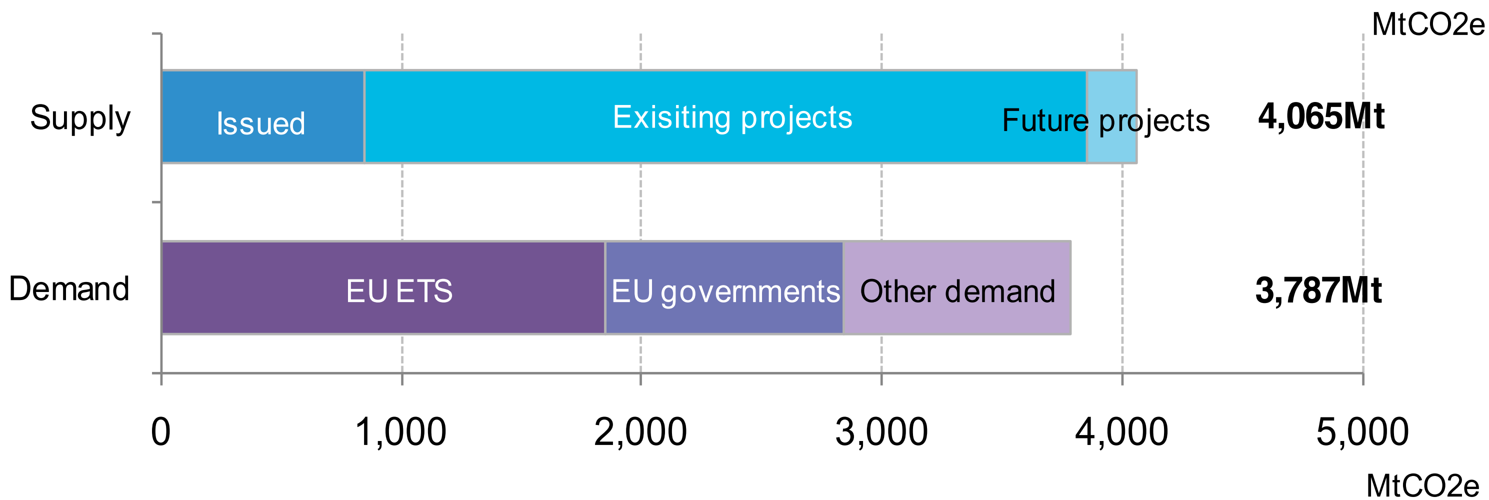
Political pressure

- Insufficient targets/domestic policy development in Annex I countries
- Developing countries refusing LoAs as instrument of pressure

Public opinion

- Bad image and increased anti-CDM NGO activities
- No offsetting/domestic investments
- Lack of progress on reforms in CDM EB

Lack of demand for new projects...



Source: Bloomberg New Energy Finance

February 2012

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Australia's emitters – thirsty new kids on the block

- The top 10 emitters in the Australian power sector have over 160 Mt of annual emissions covered by the new Clean Energy Package trading scheme

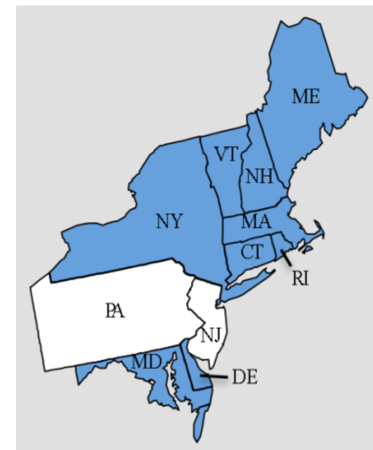
  (2009/10 emissions in millions of tCO_2e)

  - CS Energy *16.8* ; Delta *20.5* ; Eraring *12.1* ; Great Energy Alliance *19.8* ; International Power *17.2* ; Loy Yang *10.2* ; MacGen *23.4* ; Stanwell *15.7*; TRUenergy *15.6*
- Australian resources companies expect major growth in emissions in line with new mining and gas projects
- Most of these companies have no experience with international carbon markets
  - They can see international prices at record low levels
  - The political uncertainty is diminishing, but still very real
  - Floor prices and unit eligibility risks are key hurdles

California: Overview & Timeline

- California's Global Warming Solutions Act (AB 32) passes in 2006, requiring emissions to decrease to 1990 levels by 2020, a 25% reduction statewide
- AB 32 designates the California Air Resources Board (ARB) to develop reduction regulations and design the emissions trading market
- CARB passed preliminary draft regulations December 17, 2010, CARB to finalize rules 2011
- Market start date is currently set for January 1, 2013
- ARB focus on building systems (registry, auction platform, market overight system)
- Lawsuit underway challenging ARB authority to run offsets program

RGGI: Not wholly negligible



- Regional Greenhouse Gas Initiative (RGGI) is a regional GHG cap & trade program between 10 Northeastern states to reduce emissions from the power sector 10 percent by 2018
  - Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island and Vermont
- First mandatory market-based effort in the US to reduce GHG emissions launched in 2009
- Full Auction, with revenue channeled into RE/EE
- RGGI Offsets limited to 5 eligible project types, but price triggers in effect
- Governor Chris Christie has moved to pull New Jersey out of the program though he faces challenges from the State Legislature.
- Maine Governor Paul LePage wanted out, but seems to have given up
- 2012 review process has begun with a stakeholder meeting on September 19th. Big question - how much will the cap be reduced?
- Spring 2012: Present the comprehensive set of recommendations to stakeholders with potential changes to the RGGI program during the second control period (2012-2014)
- No-one expects big changes under current political circumstances. But over time….

Ambition and trading in Japan

- Aim to reduce emissions by 25% by 2020 compared to 1990 seems out of reach
- …premised on establishment of fair and effective international framework
- Policy and measures include:
  - Domestic Emissions Trading Scheme: Draft legislation ready, but buried for at least 2 years
  - Tax (on fossil fuels' carbon content) and FIT to come from 2012
  - Keidanren "voluntary" scheme has been powerful international driver
- Currently voluntary emissions trading scheme (JVETS) launched in 2005 (average price 2009: Euro 7.14)
- In future scheme: Entities may use domestic and international credits (s.t. qualitative and quantitative conditions)
- Variety of Japanese bilateral offset schemes in place of CDM under construction
- Tokyo ETS (April 2010): 1332 covered facilities, 40% of commercial and industrial sectors' emissions in Tokyo, allows for emission reduction credits from outside

Ambition and trading in China

- It started with the Twelfth Fiver-Year Plan
- Key mandatory targets for energy:
  - 16 percent energy intensity reduction,
  - 17 percent CO_2 emissions reduction per unit GDP
  - Increasing non-fossil energy sources to 11.4 percent of primary energy consumption from the current
    8.3 percent.
- In line with commitment of 40 to 45 percent reduction in carbon intensity
- Absolute caps not taboo anymore: State council-level think tank proposal
- Promotion of low-carbon pilot programs by 2015 (national scheme possible in next 5y plan)
- Will start in 6 provinces possibly as of 2013 but details remain open. More than 20 exchanges exist already.
- NDRC guidelines for 'transfer of post-2012 emission reductions' important
  - Project Review Council (to approve / deny sale of post-2012 credits to foreign buyers)
  - Increased government revenue sharing for HFC, N2O, PFC projects
  - Signals that Chinese government could be interested in use of non-EU ETS eligible credits for domestic consumption
- Could allow for use of CDM offsets from other provinces

South Korea

- **Cap-and-trade legislation announced** in November 2010
- **Draft bill approved** in cabinet meeting of April 2011
- **Recently passed National Assembly**
- **Offset mechanism**
  - International offsets allowed: UN credits and bilaterally-agreed foreign offsets
  - Details to be set out in Presidential Decree
- **Target management system (TMS)**
  - Official targets of entities to be announced
  - BAU caps very low according to industry ➡ government could raise them again
  - But learning process has started: Companies study GHG emissions and reduction options

2012 Priorities

- Improve existing systems: **EU ETS, RGGI, Japan**
- Promote trading concepts with industry and assist business affected by trading programs
- Work to improve **UNFCCC** Kyoto project mechanisms and the promotion of new mechanisms
- Promote other **offset mechanisms**
- Assist in development of **new arket approaches**
- Engage with **private finance issues** in the international climate finance field.
- Promote **common global standards** facilitating linking and fungibility

Thank you

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