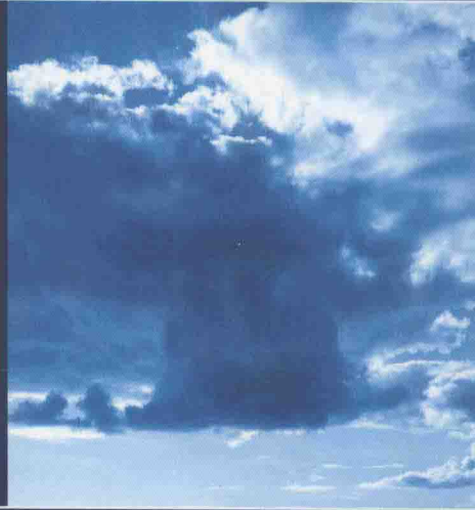


EU CLIMATE CHANGE POLICY

The Challenge of New
Regulatory Initiatives



Edited by Marjan Peeters and Kurt Deketelaere



EU Climate Change Policy

The Challenge of New Regulatory Initiatives

Edited by

Marjan Peeters

*Institute for Transnational Legal Research – METRO,
University of Maastricht, The Netherlands*

and

Kurt Deketelaere

*Professor of Law and Director,
Institute of Environmental and Energy Law,
University of Leuven, Belgium*

NEW HORIZONS IN ENVIRONMENTAL LAW

Edward Elgar

Cheltenham, UK • Northampton, MA, USA

© Marjan Peeters and Kurt Deketelaere 2006

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system or transmitted in any form or by any means, electronic, mechanical or photocopying, recording, or otherwise without the prior permission of the publisher.

Published by
Edward Elgar Publishing Limited
Glensanda House
Montpellier Parade
Cheltenham
Glos GL50 1UA
UK

Edward Elgar Publishing, Inc.
136 West Street
Suite 202
Northampton
Massachusetts 01060
USA

A catalogue record for this book is available from the British Library

Library of Congress Cataloguing in Publication Data

EU climate change policy : the challenge of new regulatory initiatives /
edited by Marjan Peeters and Kurt Deketelaere.

p. cm. — (New horizons in environmental law series)

Includes bibliographical references and index.

1. Environmental law—European Union countries. 2. Global warming—Law
and legislation. I. Peeters, Marjan. II. Deketelaere, K. (Kurt) III.
Series.

KJE6242.E9 2006

344.2404'6—dc22

2006040018

ISBN-13: 978 1 84542 605 7

ISBN-10: 1 84542 605 3

Typeset by Manton Typesetters, Louth, Lincolnshire, UK
Printed and bound in Great Britain by MPG Books Ltd, Bodmin, Cornwall

Contributors

Véronique Bruggeman

Faculty of Law, Maastricht University, The Netherlands

Javier de Cendra de Larragán

Maastricht University, The Netherlands

Kurt Deketelaere

University of Leuven, Belgium

Bram Delvaux

University of Leuven, Belgium

Claudia Dias Soares

Portuguese Catholic University (Oporto), Portugal and London School of Economics, UK

Wybe Th. Douma

TMC Asser Institute, The Netherlands

Mar Campins Eritja

University of Barcelona, Spain

Joyeeta Gupta

UNESCO-IHE Institute Delft and Free University of Amsterdam, The Netherlands

Ludwig Krämer

University of Bremen, Germany

Karen MacDonald

Imperial College London, UK

Zen Makuch

Imperial College London, UK

Birgitte Egelund Olsen

Aarhus School of Business, Denmark

Marc Pallemerts

Vrije Universiteit Brussel and Université Libre de Bruxelles, Belgium

Marjan Peeters*Maastricht University, The Netherlands***George (Rock) Pring***University of Denver, USA***Manfred Rosenstock***European Commission, Belgium***Bettina Schmitt-Rady***Heiermann, Franke, Knipp, Germany***Geert van Calster***University of Leuven, Belgium***Rhiannon Williams***Institute for European Studies, Vrije Universiteit Brussel, Belgium*

Contents

List of contributors

vii

PART I INTRODUCTION

- 1 Key challenges of EU climate change policy: Competences, measures and compliance 3
Kurt Deketelaere and Marjan Peeters
- 2 Climate change: The international and European policy framework 22
Marc Pallemmaerts and Rhiannon Williams
- 3 The European Union, Russia and the Kyoto Protocol 51
Wybe Th. Douma

PART II GREENHOUSE GAS EMISSIONS TRADING WITHIN THE EU

- 4 Reviewing the challenging task faced by Member States in implementing the Emissions Trading Directive: Issues of Member State liability 69
Mar Campins Eritja
- 5 A level playing field? Initial allocation of allowances in Member States 83
Bettina Schmitt-Rady
- 6 Linking the project based mechanisms with the EU ETS; the present state of affairs and challenges ahead 98
Javier de Cendra de Larragán
- 7 Emissions trading and the Aarhus Convention: A proportionate symbiosis? 125
Karen MacDonald and Zen Makuch
- 8 The IPPC permit and the greenhouse gas permit 153
Birgitte Egelund Olsen
- 9 Enforcement of the EU greenhouse gas emissions trading scheme 169
Marjan Peeters

| | | |
|---|---|-----|
| 10 | A decade of emissions trading in the USA: Experiences and observations for the EU <i>George (Rock) Pring</i> | 188 |
| 11 | Climate change taxes, emissions trading, and international trade law <i>Geert van Calster</i> | 205 |
| PART III ENERGY AND CLIMATE CHANGE MEASURES | | |
| 12 | EU energy policy and legislation under pressure since the UNFCCC and the Kyoto Protocol? <i>Véronique Bruggeman and Bram Delvaux</i> | 223 |
| 13 | Energy taxation within the EU <i>Manfred Rosenstock</i> | 240 |
| 14 | Critical issues in implementing energy taxation <i>Claudia Dias Soares</i> | 256 |
| PART IV GOOD GOVERNANCE FOR CLIMATE CHANGE: REFLECTIONS AND PERSPECTIVES | | |
| 15 | Some reflections on the EU mix of instruments on climate change <i>Ludwig Krämer</i> | 279 |
| 16 | Good governance and climate change: Recommendations from a North-South perspective <i>Joyeeta Gupta</i> | 297 |
| | <i>Index</i> | 317 |

PART I

Introduction

1. Key challenges of EU climate change policy: Competences, measures and compliance

Kurt Deketelaere and Marjan Peeters¹

1. INTRODUCTION

This book explores and comments on, from a legal perspective, the regulatory framework the European Union (EU) has established to meet the international greenhouse gas emission reduction obligation it has taken up in Kyoto and to anticipate further emission reductions after 2012.²

We start from the perspective that legally binding obligations, which can be imposed through several forms of regulatory instruments, are needed in order to steer society towards low-carbon behaviour. The market, as such, does not provide for a reduction of greenhouse gas emissions, and the liability regimes in place, thus far, do not include important incentives to avoid excessive greenhouse gas emissions. Governmental action by meaningful policies is inevitably needed. Specifically for the climate change problem, economic instruments are expected to be the most suitable ones, although complementary approaches are also needed.³ Moreover, perfect regulatory solutions probably do not exist for the complex climate change problem, and theory still develops different ideas for the best design and the best mix of instruments for climate change policies.⁴ Furthermore, the regulatory approach which is developed in the real world is of course highly influenced by the political process, which often leads to a flawed and/or confusing approach.

As a consequence of a number of circumstances, among which is the refusal of the USA to ratify the Kyoto Protocol, the EU has become a global green leader in climate change policies.⁵ However, are its current internal measures (such as the EU emissions trading scheme) a meaningful and sound approach? If a (and for the moment very unlikely to happen) ‘trading up’ effect might occur towards the EU’s trading partners – stimulated through a serious climate change approach by the EU – it is important that the current measures are real and are not to be qualified as a kind of window dressing.⁶ Within this respect, it is of utmost importance that the adopted regulatory arrangements within the EU are

and will be implemented, executed and complied with at best in practice. Adopting an approach is only a first step, but ensuring that the effects take place in practice is the second and even more difficult step to address.

For the short term, the main challenge for EU climate change policy is to comply with the international obligation to reduce emissions during the period 2008–12 as this is concluded in the Kyoto Protocol. The European Community (EC) itself has an emission reduction commitment of –8% compared to the reference years 1990 and 1995. This emission reduction commitment is related to the group of 15 Member States who joined the EU before 1 May 2004 (the so-called ‘EU-15’). Within the so-called EC Burden Sharing Agreement, the emission reduction commitments for these Member States, as stipulated in the Kyoto Protocol, are reallocated; each Member State has got a new emission reduction commitment which differs from the one in the Kyoto Protocol. For the Member States who joined in May 2004, the emission reduction commitments apply as agreed upon in the Kyoto Protocol. For Malta and Cyprus, the Kyoto Protocol does not mention any emission reduction commitment.

The EU has developed a mix of regulatory approaches in order to contribute to those targets, and a lot of discretion to set up climate change policies is left to the Member States. This already makes it hard to assess the real content of the climate change policies within the EU: we do have in fact one global problem, but 26 climate change policy approaches, ie one at the EU-level, and 25 Member State policies. However, as climate change is a transboundary environmental problem, with high consequences for the functioning of the internal market, there is a strong reason to develop a meaningful EU climate change policy.

This book argues that the current approach like emissions trading and energy taxation is not yet meaningful enough because of the fact that they, thus far, do not lead to impressive reductions. Nevertheless, these seeds, when carefully and seriously nurtured, may lead to a fruitful outcome.

For the longer term, after 2012, it is still very uncertain how or what kind of international agreements regarding climate change will be concluded. Of course there is the United Nations Framework Convention on Climate Change (UNFCCC), but experience shows that there are severe difficulties for the Treaty Parties to reach agreement on emissions reductions to be realized after 2012. The USA/Asia-Pacific Agreement, which was concluded in 2005, leads even to the assumption that a common global approach under the umbrella of the UNFCCC is almost impossible.

However, within the EU, some exploration of the necessary post-2012 policy options, including emission reductions, has been taking place. The 2002 Sixth Environmental Action Programme indicates climate change as a priority of the Community environmental policy.⁷ This means that the temperature rise worldwide should not exceed 2°C compared with the pre-industrial era, and that the

CO₂ concentration should stay below 550ppm.⁸ In the longer term, this means a reduction of 70% compared with the emissions of 1990.^{9,10} Whether within the EU the ambitiously sounding targets of the Sixth Environmental Action Programme will be pursued in the future and whether there will be a readiness to take further measures than other UNFCCC Parties is hard to predict. In the spring of 2005, the meeting of the Council of the EU made it clear that the EU does not want to take responsibility alone. The meeting resulted in some, but not too promising, pronouncements about the future development of climate change policies, among which was the formulation of a specific target to be pursued: developed countries – meaning not the EU Member States alone – would have to set themselves a target of an emission reduction of 15–30% in 2020, compared with 1990. Just before this Council meeting, the Environmental Council indicated further that the developed countries would have to take the road to an emission reduction of 60–80% in 2050. The Council did not give its opinion about so far ahead into the future, and did not go any further for the time being than indicating emission reduction percentages for the year 2020.

It is uncertain whether the political process of the EU will indeed stay adhered to the forecasted emission reduction targets when other big world players would not be prepared to take effective measures.¹¹ The global context will influence the content and seriousness of the internal regulatory measures taken within the EU – and it is not clear whether the accidentally short-term European ‘green leadership’ will be prolonged into a long-term leadership.

However, let us turn now to the legal instruments for climate change policy which currently have been adopted on the basis of the EC Treaty. This book discusses secondary EC-legislation covering greenhouse gas emissions and energy use. Remarkably, the approach towards the climate change problem rests mainly on a regulatory concept that is really new for the EU, as it is using emissions trading and taxation to induce society to decrease greenhouse gas emissions. The main European climate change policy instrument, the Greenhouse Gas Emissions Trading Directive (the ET Directive) has led to an EU-wide market for greenhouse gas allowances. This innovative instrument – which simultaneously raises a lot of legal questions – is expected to contribute towards a large part of the emissions reductions for which the EU Member States and the EC are legally responsible. However, there is more: the ET Directive is also accompanied by directives on energy taxation, energy efficiency, the promotion of electricity produced from renewable energy sources, by voluntary agreements with the car-industry, and by a proposal for a regulation for certain fluorinated greenhouse gases. In fact, a broad and complex package of regulatory measures has now been established at the EU level, representing a mix of instruments, among which soft law approaches (like labelling, indicative non-binding targets, and voluntary agreements), market-based instruments (taxation and emissions trading) and traditional command and control regulation (the

permit approach and the prescription of best available techniques through the Integrated Pollution Prevention and Control (IPPC) Directive). However, the policy regarding climate change within the EU is dependent on the interplay between the EU institutions and the Member States. Some of the EC measures, like the ET directive, leave a rather broad, maybe too broad discretion to the Member States to implement them, as is the case with the allocation of the greenhouse gas allowances. This multi-level approach makes the EU Climate Change Policy dossier, which is already hard to understand because of the diversity of measures undertaken at EC level, even more complex. The whole body of regulatory measures at EC level and at national level is of course meant to ensure that the internationally binding emission reduction targets will be complied with. From this perspective, the monitoring of the progress within the 25 Member States, and the enforcement actions by the Commission when measures and action are lacking, must be the ultimate part of the European climate change policies as well.

In this book, a group of distinguished authors discuss and comment upon the policy package as established at EC level, addressing from a legal point of view both theoretical and practical aspects. The overall finding is that the EC policy on climate change is still very 'green' and thus needs to be developed further in a comprehensive and meaningful way. We are indeed in a phase in which we need to learn about the usefulness of the instruments as adopted now, and try to improve them. With 'improvement' one should not only focus on another possible design of a specific instrument, but also on the way of implementing the regulatory framework in practice.

2. OVERVIEW OF THE BOOK

Part I: Introduction

After this chapter, which introduces the book, the exploration of the real meaning of the regulatory measures within EU climate change policy starts with an extensive discussion of the international and European legal framework concerning the climate change problem. In Chapter 2, Marc Pallemarts and Rhiannon Williams provide us with an historical overview of the development of the framework thus far. Key elements of the international framework are, of course, the UNFCCC, the Kyoto Protocol and the Bonn and Marrakesh Accords. The EU climate change policy can, of course, only be understood in the context of these legal agreements. Pallemarts and Williams pay attention to the concept of 'differentiated responsibilities', and explain the specific responsibilities and commitments of the developed countries. Within this context, the provisions in the Kyoto Protocol regarding burden-sharing between parties are particularly

interesting for the EC as such, and for the EU Member States. The Kyoto Protocol (art. 4) allows the EC and the Member States to agree internally on the reallocation of the emission reduction targets as concluded in the Kyoto Protocol. Consequently, the EC Burden Sharing Agreement includes different national targets, ranging from -21% (Germany and Luxembourg) to $+27\%$ (Portugal).

The historical overview shows that the EC and its Member States ratified, in 1993, the UNFCCC without having yet a concrete internal policy. Main initiatives were left to the Member States, to elaborate national emissions reduction programmes. Pallemmaerts and Williams explain that, until 2001, the climate change policy within the EC was merely a collection of soft law measures. From 2001, some more serious measures were adopted, like the ET Directive, which presently can be seen as the main instrument, and, among others, Directive 2002/91/EC on the energy performance of buildings. Pallemmaerts and Williams also show us in which policy context the legal measures are to be developed, like the European Council policy announcements in the Spring of 2005, following the 2004-presented Communication of the Commission with the title 'Winning the Battle against Climate Change'. They show that the European Parliament takes a more ambitious approach compared to the European Council, which in its Spring 2005 meeting refused to formulate a long-term target with regard to the reduction of greenhouse gases.

Chapter 3 provides us again with some historical insight, but now with regard to the difficult, sensitive and very important relationship between the EU and Russia regarding the ratification of the Kyoto Protocol. Building upon and improving the EU-Russia economic relationship, which is formalized in the 'Partnership and Co-operation Agreement' from 1994, was of crucial importance for the ratification of the Kyoto Protocol (KP) by Russia. The main idea is to develop a common European economic and sustainable space. However, Russia took rather a long time before it eventually decided to ratify the KP. It is well-known that the EU took a very active role in convincing Russia to ratify the Protocol, but that ratification was for Russia less attractive since the USA – the biggest big buyer – would not participate in the international emissions trading facilities. For Russia, the enlargement process of the EU was of bigger concern, as this would possibly lead to economic disadvantages (trade barriers for Russia to the new EU Member States), and as a consequence it demanded the relaxation of EU trade-related measures. The EU indeed dealt with the many trade-related concerns put forward by Russia, and extended the Partnership and Cooperation Agreement (PCA). After all, the author, Wybe Douma, argues that there indeed was a link between the agreements on PCA extension and the negotiations of the World Trade Organization (WTO) accession of Russia, and – finally – the Kyoto ratification, although this relationship is officially denied by the Russian leader. Douma ends with an outlook on the future cooperation between Russia

and the EU towards climate change, discussing the possibility of establishing Joint Implementation (JI) projects, for which many hurdles are still on the way. Russia's monitoring systems and inventory procedures for greenhouse gases still need, for example, to be improved, being a condition for conducting international emissions trading. In fact, the EU is supporting Russia financially to provide those necessary institutional provisions. Another concern is the so-called 'hot air trading' that could occur between Russia and the EU. However, this remarkable possibility was taken into account when agreement took place on the Kyoto Protocol.¹² Hot air trading is, in this respect, just part of the current international climate change deal, and could be used by the EU, although it is a remarkable and contestable part of international emissions trading.

Part II: Greenhouse Gas Emissions Trading Within the EU

Within Part II, the focus is turned towards the parade horse of the EC climate policy package, which is Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community. In Chapter 4, Mar Campins Eritja reviews the challenging task faced by Member States in implementing this Directive, and discusses from this perspective issues of Member State liability. The timetable for implementation as included in the ET Directive was remarkably short: the Member States had to prepare their national legislation in order to implement the new regulatory instrument within only a couple of months after the adoption of the directive. It is clear that this was hardly achievable. Moreover, one of the core and sensitive elements of the emissions trading scheme, the development of National Allocation Plans (NAPs), had to be executed by Member States within a very tight schedule.

Mar Campins Eritja explains more specifically the difficulties the Member States met in implementing the ET Directive and drawing up the NAPS. They had to do that under strong pressure from domestic industry, which caused most Member States allocated more emission allowances than would be desirable in order to reach the Kyoto emissions reduction target. Due to the short timetable and the complexities of the instrument, it is questionable whether all Member States were really ready in the year 2005 for the emissions trading scheme. This may even result in a distorted internal market. The Commission, however, lacks an efficient and effective instrument to stimulate and enforce compliance behaviour by Member States. Nevertheless, it is not excluded that infringement procedures will ultimately lead to high fines imposed by the European Court of Justice, although there is limited jurisprudence on the issue of penalizing Member States thus far. Reference is made to the last judgement of the Court of 12 July 2005, in which the Court explicitly refers to the fact that penalty payments and/or a lump sum are meant to place Member States under

economic pressure in order to induce it to put an end to its non-compliance behaviour.

Another liability issue is the possibility for European citizens and companies to hold Member States responsible for damages following from incorrect implementation of the ET Directive. More specifically, the position of the industry covered by the ET Directive is discussed. When a Member State fails to establish the necessary provisions for emissions trading, interested industries would be denied the right and full access to the EU allowance market and would suffer economic damage. The specific liability regime and its specific criteria are discussed, which shows that such a liability is not out of expectation. However, the assessment of the specific conditions to vest liability will depend on a rather detailed case-by-case analysis, and can thus not be generally predicted. Besides the internal EU liability concerns, attention is paid shortly to the external front, where Mar Campins Eritja explains that the shared nature of powers conferred to the EU and its Member States determines the issues related to the rules of standing within the international climate change framework.

Chapter 5 extensively assesses the allocation process within the greenhouse gas emissions trading system. The author, Bettina Schmitt-Rady, starts from the point of view that in an EU emissions trading scheme a level playing field between the covered industries should be the case. She gives, from a practitioner's perspective, a view on the chosen method of allocation as included in the ET Directive, and from this angle she concentrates on the allocation of allowances as done in Germany for the first trading phase 2005–07. Many concerns are addressed, and above all, the author states that the allocation as conducted for the first phase does not contribute to a level playing field between covered industries. The ET Directive is too vague, and the Commission has given Member States considerable lee-way in designing the specific allocation criteria. Even administrative over-regulation has taken place, especially in Germany, where many different allocation rules are established. Schmitt-Rady pleads for an improvement of the definitions stipulating the coverage of the directive, points at the variations between NAPs with regard to the treatment of new entrants, reveals the protectionist approach taken by the government with regard to the cessation of activities, and, among other things, argues against the possibility of ex-post allocation.

Chapter 5 makes clear that the present allocation framework needs to be critically reviewed, in order to make it simpler and ensuring as much as possible equal treatment of the industries covered. Of course, there is somehow a trade-off between on the one hand using simple formula, and on the other, treating industries fairly.¹³ Both goals can probably not be reached to the same extent. Equal treatment means that firms in equal positions need to be treated equally – but when their positions are not equal, differences should in principle be taken into account. Maybe it is too complicated to ensure this notion of 'equal treat-

ment' of the European industry within a system of free allocation of allowances, and the option of auctioning may be better. This option should at least be considered for the long term, especially now that emissions trading is seen as the main instrument for climate change policies in the EU, and because auctioning is the main approach recommended by economic literature.¹⁴

More or less a year after its adoption the ET Directive was already amended by Directive 2004/101/EC linking the KP's project mechanisms to the EU emissions trading scheme. In Chapter 6, Javier de Cendra de Larragán discusses these complicated concepts. The EU's position towards the project mechanisms evolved from a sceptical position to, ultimately, an adoption of the above mentioned directive by which the project mechanism will become an option for European industry, as far as indeed the Member States will allow them to make use of this. The linking directive also gives much discretion to the Member States. Again it can be said that the EU has run very fast, maybe too fast, with establishing the linking directive, as many questions regarding the practical application of the concepts of Clean Development Mechanism (CDM) and JI still need to be answered. Here again the EU follows a 'learning by doing' exercise in implementing a regulatory instrument. But already some shortcomings of the directive can be identified, like the possibility for industry to undermine the additional qualitative requirements stipulated by a Member State for the engagement in CDM or JI projects. A more uniform approach on the admissibility of projects would, in this light, be recommendable. The conclusion is that both from a perspective of environmental effectiveness and competitiveness many concerns can still be raised, and that more harmonization would be necessary. Moreover, with regard to the considerations on the EU level or on the Member State level to allow for CDM or JI projects, the precautionary principle should be taken into full account.

Emissions trading is recommended for its market-based approach, through which – at least, in theory – a cost-effective environmental policy can be reached. However, how does this new instrument fit into the fundamental rights for the public with regard to environmental policy? This basic and important question is extensively addressed by Karen McDonald and Zen Makuch in Chapter 7. They examine the extent to which some central elements of the EU emissions trading scheme (EU ETS) comply with the objectives of the 1998 Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters; thereby asking themselves whether 'environmental democracy' is ensured within the greenhouse gas emissions trading regime. It is important to note that 'Aarhus rights and obligations' are conventionally inscribed in traditional command and control legislation. McDonald and Makuch investigate how the rights of the public as ensured by the Aarhus Convention are to be applied within an emissions trading scheme. They point to the feature of emissions trading, which is that govern-