Review of the Balance of Competences between the United Kingdom and the European Union: A Response from the Sandbag Climate Campaign

Executive Summary

- Through the EU, the UK has greater influence on global climate negotiations, owing to the combined economic power, population and emissions of the European Community.
- Tackling climate change at an EU level ensures the UK’s ambition on emissions reductions are closely matched by 27 other countries, minimizing regional competitiveness distortions.
- With London as the trading hub for the EU ETS, the scheme has been uniquely beneficial to the UK economy.
- A third of British growth is now in the ‘green’ sector: environmental regulation, at a UK and EU level, can be very beneficial to the UK economy.
- The UK should ensure that EU climate targets and carbon budgets do not hinder national climate ambition or hold back the national carbon budgets set under the UK Climate Change Act. The UK government should protect and exercise its right to cancel any allowances issued to it under the EU Emissions Trading Scheme, or the EU Effort Sharing Decision which exceed its desired national budgets.

Introduction

Sandbag Climate Campaign is a non-governmental organisation (NGO) that campaigns for an effective carbon budgets and carbon markets, with a special focus on the EU emissions trading scheme (ETS). Our view is that if emissions trading can be implemented correctly, it has the potential to help affordably deliver the deep cuts in carbon emissions the world so badly needs to prevent the worst impacts of climate change.

Sandbag welcomes the opportunity to respond to this call for evidence. Whilst Sandbag does not have a formal position on the UK’s membership of the EU, we acknowledge the pivotal role EU legislation has played in driving climate ambition across Europe and creating the framework for a pan-European carbon market.

Given Sandbag’s focus on the EU ETS, our response to this consultation is done so through the prism of the UK’s relationship with the EU ETS and with closely related climate legislation.
Call For Evidence - Questions

1 What evidence is there that EU competence in the area of environment and/or climate change has: benefited the UK / your sector?; and has disadvantaged the UK / your sector?

ADVANTAGES:

- As climate change is a transboundary issue, global in its causes and effects, it is intrinsically difficult to address through unilateral policies at national level. The ideal route to prevent dangerous climate change is through a fair and environmentally adequate international climate agreement; however, the political complexities of forging such a deal mean a truly global response may yet be some time away. As the UK works towards reaching such an agreement, it should seek to control emissions at the next most manageable level, by incorporating the greatest number of actors (through country groupings such as the EU), and incorporating the greatest volume of emissions (including the largest polluters such as China and the USA). By tackling climate change in those regions and countries that pollute the most, the greater the effect that will be had in reducing emissions.

The EU Emissions Trading Scheme

- The UK piloted an emissions trading scheme in 2002 which acted as a forerunner to the current EU ETS. The UK remains one of the leading proponents of emissions trading and recently Secretary of State Ed Davey reaffirmed the UK’s support for a “strong EU ETS”.

- The flexibilities provided by the ETS as well as its least cost approach has allowed for a neat political compromise which has allowed for the introduction of a pan European carbon price. This has reduced the need for the potentially distorting effects of multiple unilateral policies that might place unnecessary burdens on companies operating across different European countries.

- Being part of an EU approach to tackle climate change magnifies the UK’s efforts and enhances its political power, as coordinated action by a large block of countries carries more weight than the UK acting alone. Internationally the UK has been able to use the EU’s pioneering ETS as a means of promoting its own climate outreach activities. For example, the FCO has ongoing projects building capacity and sharing knowledge on emissions trading in a number of countries, including China and South Korea.

- The UK benefitted uniquely by the introduction of emissions trading in that it has become the centre of the EU carbon market. The City of London’s financial knowhow has meant it was well placed to offer specialised financial services relating to emissions trading. The UK is the largest trader of EU allowances, as well as carbon credits originating from the UN Kyoto Protocol projects. The UK’s leading position has been widely recognised, including by Climate Change and

---

Davey calls for European Parliament to support EU ETS back-loading (2013) DECC
Energy Minister, Greg Barker who said, ‘The UK is really leading the way...reaffirming London’s position as a global hub for the market. Not only does this help incentivise significant emission reductions and behaviour change amongst businesses, but it also generates millions of pounds in revenue each year for the Treasury, at little or no cost to the taxpayer. This is a win-win, which makes both environmental and economic sense.’

- Participation in the EU ETS as well as environmental regulations and targets agreed at EU level have helped the UK forge ahead in developing a meaningful and vibrant green economy, offering sustainable goods and services. With a third of UK growth in ‘green’ businesses in 2011/12,³ the UK’s largest business group, the Confederation of British Industry (CBI), supports the principles of green growth. For instance, between 2000 and 2012, 51.2% of new power capacity in the EU has been in renewable energy,⁴ and the UK has now reached sixth in the world for installed wind power capacity, a position and expertise that offers enormous further economic growth. The CBI reports that UK green businesses are exporting successfully, and have amassed a £5bn trade surplus in green goods and services. Exports are facilitated by close connections across Europe, and standardised regulation. Lastly, the ETS has created a level playing field for carbon pricing and been positive for EU business. Rather than 28 different carbon-pricing policies and strategies, companies only need deal with one, reducing regulatory costs and trade barriers.

DISADVANTAGES:

- UK climate ambition hitched to burden sharing arrangements at EU level
One disadvantage is that the UK’s climate ambition risks becoming anchored to the targets and carbon budgets set for it under burden sharing arrangements in EU legislation. If the EU awards the UK more carbon allowances under the ETS and the Effort Sharing Decision than are prescribed by national carbon budgets set under the Climate Change Act, this represents a serious threat to the environmental integrity of the national budgets. To preserve the environmental integrity of these national budgets the UK must exercise its prerogative to cancel any EU allowances issued to it which exceed the budgets it has set itself under national law.

Cancellation of excess EU allowances in this way, allows the UK to go beyond its European Community commitments without the need to “gold plate” EU regulation. Cancellation does not add to the regulatory burden, but simply reduces the number of carbon allowances the UK releases into the market. In effect, this course of action allows the UK to unilaterally increase the ambition of EU wide carbon budgets.

---

² London hails position as carbon trading hub following latest auction (2013) Business Green
³ How the UK can make the most of green growth (2013) CBI http://www.cbi.org.uk/infographics/how-the-uk-can-make-the-most-of-green-growth/
We emphasize that where Europe awards the UK more allowances than the UK awards itself this should not be taken as evidence that the UK is more ambitious than Europe, but only that the UK’s obligations at EU level are weaker than those it has elected to set for itself. We note, that the burden sharing methodologies in Europe legislation are at times more preferential to the UK than the burden sharing methodologies applied under the Climate Change Act.

- **EU carbon price failing to drive low carbon investment in UK power sector**
  A related problem has obliged the Treasury to introduce the Carbon Floor Price. As the EU carbon price has faltered through the excess volumes of allowances in the system, the political will across Europe to reverse this trend during a time of recession has been slow and faltering. To stabilise the receipts from the EU ETS, and to bolster the signal to decarbonise the electricity sector, Treasury introduced a unilateral carbon price, currently set at £16 (€18.50). This price is in stark contrast to the current EU carbon price of €4.50 and threatens to undermine the UK’s competitiveness in Europe. What is more, the carbon floor price does nothing to strengthen the environmental ambition of the scheme, as under a fixed EU emissions cap, savings made in the UK are simply traded away to other Member States and thus perversely reduce the compliance cost for the UK’s competitors.

2 Considering specific examples, how might the national interest be better served if decisions:

i. currently made at EU level were instead made at a national, regional or international level? (What measures, if any, would be needed in the absence of EU legislation?)
   ii. currently made at another level were instead made at EU level?

- Given the global challenge of climate change, action to reduce emissions is best co-ordinated at the EU level or, where possible, at the global level. Sandbag believes that emissions are generally best reduced through flexible and market-based mechanisms to drive carbon abatement at least cost. We have proposed a *Sovereign Emissions Rights Framework* which sets out an equitable and flexible framework for avoiding 2 degrees of post-industrial warming.\(^5\)

- If the UK acted alone this would bring no guarantee that others would follow suit, potentially lead to fragmentation of the global debate, and no way to tackle the free rider problem, where some countries exploit the emissions space that should rightfully belong to others. It could also reduce the strength of the UK’s voice in climate negotiations. Only the very largest national governments have little leverage diplomatically when it comes to advocating more ambition globally, such as a legally binding global emissions reduction target. International decisions require consensus for success, and a common platform across the EU helps to build this. Leaving such decision-making to the regional or national level risks a loss of ambition, and the introduction of a piecemeal approach that increases costs for trading across the EU, and offers little to no benefit for the environment if standards are not harmonized and accounted for correctly.

---

\(^5\) The Sovereign Emissions Rights Framework (2013) Sandbag
• The transfer of power from domestic government to the EU with regards to taxation is a vexatious issue, but there are distinct benefits to a harmonised tax on energy across the EU, preventing competitive differences, preventing tax competition (avoiding a ‘race to the bottom’, as seen in other areas, notably with capital gains tax), and ensuring all energy costs accurately reflect externalities. Taxation changes at EU level require unanimity, and so there are difficulties in reaching agreement on legislation including the Energy Tax Directive. 

3 To what extent do you consider EU environmental standards necessary for the proper functioning of the internal market?

• Common EU environmental standards enable free trade between countries because no single good (such as a leaded car) is banned in one country but allowed in another. More importantly, perhaps, is the ability for common standards to drive innovation, giving industry a clear signal that there will be a market for green goods and services. The EU has a strong success story to tell regarding both energy efficiency standards for appliances and with car emissions standards. Both are cross-cutting initiatives which no one country would have the market power to do alone, and which have saved European consumers billions of pounds and cut carbon significantly.

• Consistency in environmental standards across the EU gives peace of mind that no one Member State is at an economic advantage. This in turn should allow the EU to take on more ambitious environment and climate targets, beyond what any one Member State would feel comfortable implementing unilaterally.

• With a focus on the EU ETS, standards for EU allowances as well as international offsets (from both Clean Development (CDM) and Joint Implementation (JI) projects) must be tightly controlled. If these offsets do not represent one tonne of avoided CO2 the basis of the trading scheme would be severely undermined. The EU has already acted to ban offsets originating from industrial gas projects over concerns around their “environmental integrity, value-for-money and geographical distribution”. Significant EU oversight and incorporation of EU legislation in UK law would remain a necessity even under a major renegotiation of competencies.

4 To what extent does EU legislation on the environment and climate change provide the right balance between protecting the environment and the wider UK economic interest?

• Some EU legislation is detrimental to UK environmental efforts. CAP has arguably had a significantly detrimental effect on European wildlife over its 50 years, and at great cost to the consumer. The UK is pushing for more money to be spent on environmental schemes but unnecessary food production still takes precedent.

• Some EU legislation is positive in principle but negative in practice due to pork barrel politics from member states. The amount of “hot air” in the EU ETS is an example of highly successful industry lobbying.

---

• Exaggerated competitiveness fears have seriously compromised the effectiveness of the EU ETS, and have led to an unnecessary transfer of assets from the government to industry. This can be observed in the excess ETS allowances that were awarded to industry in Phase 2 of the scheme (2008-2012), and also in the excessively wide number of sectors defined as at risk of carbon leakage, and thereby entitled to additional free allowances in Phase 3 (2013-2020). To date, there is little evidence that the ETS has harmed UK and EU manufacturing industries. On the contrary, selling spare EU allowances during the recession helped many companies to stay afloat during the financial crisis. Our latest ETS report Drifting Towards Disaster explores this issue in more detail. 8

5 Considering specific examples, how far do you consider EU legislation relating to the environment and climate change to be:
   i. focused on outcomes (results)?
   ii. based on an assessment of risk and scientific evidence?

• Framework EU environment and climate legislation is outcome focused. A prime example of such an approach can be seen in the EU Climate and Energy Package which set out three targets to be met by 2020, i.e. a 20% reduction in emissions base on 1990 levels, increase renewables share of energy consumption to 20%, and a 20% improvement in the EU’s energy efficiency.

• These outcome based targets aim to transition Europe to a low carbon economy and pull its weight in the global effort to avoid dangerous climate change. But these targets also represent Europe’s current efforts to strike a balance between fulfilling its climate responsibilities without carrying free-riders. Both parts of this equation are value judgements, made by individual countries before Member States bargain and debate their positions into a common European position.

• In our view, Europe’s internal targets are not yet based on an appropriate effort sharing model of how the emissions space should be divided. In our report The Sovereign Emissions Rights Framework, we propose that Europe’s emissions should not exceed 9% of the total global volume emitted between 1990 and 2050, corresponding to its population in 1990 when the dangers of anthropogenic climate change were internationally acknowledged. We also propose that Europe should aim to keep the risks of passing 2 degrees of global warming well below 33%. This would require adhering to a global budget of 2,274 Gt over 1990-2050 of which 1,024 Gt has already been exhausted. Europe’s equitable share of this 2 degree budget would therefore be 204 Gt for over 1990-2050, of which 116 Gt has already been exhausted. 9

6 How could the EU’s current competence for the environment be used more effectively? (e.g. better ways of developing proposals and/or impact assessments, greater recognition of national circumstances, alternatives to legislation for protecting/improving the environment?)

---

• The transboundary challenge of environmental and climate issue means that the burden of addressing these problems must be shared. However, there is a danger that a growing divergence in national interests could undermine the EU ability to act collectively. While excessive focus on national circumstances could undermine the legislative process, the EU could work more effectively to ensure divergent national interests are taken into account and Member States with genuine concerns and difficulties are factored into policy decisions, thus allowing all Member States to support a progressive position. This has already been incorporated into the EU ETS Directive with richer Member States receiving fewer allowances than countries with weaker economies.

• If the political will to reform the ETS cannot be found in the near terms greater consideration should be given to alternative forms of regulation, including emissions performance standards for emitters and mandatory CCS requirements.

7 How far do you think the UK might benefit from the EU taking:
   i. more action on the environment/climate change?
   ii. less action on the environment/climate change?

• More action from the EU would increase the chances of environmental and climate change policies being successful and effective:
  o in the UK, because a level European playing field would benefit UK businesses and reduce opposition to environmental regulation;
  o globally, because the EU is powerful enough to steer international decisions on climate change.

The transboundary nature of many of the issues, from invasive species to climate change, means that the UK has only a limited ability to deal unilaterally with these issues, as demonstrated by previous efforts to reduce acid rain and ozone destruction. Furthermore, through greater EU action the UK can magnify its position by working with and actively shaping the position of a larger, more influential negotiating bloc. Politically, greater EU ambition would also help the UK, for example with UK policies such as the Carbon Price Floor, as it would reduce the political risk of the UK moving ahead alone and damaging the competitiveness of domestic industry.

• Less EU action on the environment and climate change would simply serve to exacerbate the difference between the UK’s legally binding commitments to reduce greenhouse gases and the level of ambition in the rest of Europe, increasing competitiveness distortions. It would also increase the risk of dangerous global warming, threatening the UK with greater climate impacts.

8 Are there any alternative approaches the UK could take to the way it implements EU Directives on the environment and climate change?

• The EU and Member States must conduct consultations before introducing legislation, but still, the majority of people are unaware or uninvolved in contributing to the shape of legislation and how it is implemented. Those who do

participate tend to be the usual suspects, often with known and entrenched positions. To encourage ownership of the legal system within which individuals and organisations operate, there must be improvements in consultation and education after the EU legislative process, to better negotiate the flexibilities of transposition into UK law.

- Polls across Europe repeatedly show a majority believe governments need to do more to tackle climate change, even amongst respondents who are unsure of the climate science, and yet in recent years parliamentarians have been more hesitant about taking action, or indeed, championing the decisions they do make. An improved education process is needed, whereby representatives have greater contact with interested communities, the implementation of legislation is explained and discussed at public meetings and exhibitions, and the effects of new laws are more clearly set out after the fact.

9. a. What advantages or disadvantages might there be in the EU having a greater or lesser role in negotiating and entering into agreements internationally or with third countries?

b. How important is it for the UK to be part of "Team EU" at the UNFCCC?

- The EU is able to negotiate more effectively as a political bloc due to its increased economic clout. The EU has in the past set the international agenda and made headway even when other countries remain intransigent. For example, the EU was pivotal in ensuring the design and survival of the Kyoto Protocol, and maintained the momentum behind the UN climate negotiations at a time when others were unwilling to participate in the process.

- The EU represents some 500 million citizens who collectively make up - measured in terms of the goods and services it produces (GDP) - the world’s largest economy. The chances of successfully agreeing an ambitious legally binding international climate agreement are greatly increased if the EU negotiates as a block where its political, economic and civil society leverage is greater than the sum of its parts. Furthermore, the UK can use the EU’s negotiating clout to magnify its position.

- The influence of the EU is clearly demonstrated by the host of less-economically developed nations which often seek to team up with the EU at climate negotiations, allowing their voice a greater chance to be heard. It is better that the UK be at the heart of deciding the EU ambition before conferences, rather than seeking to negotiate a space to be heard amongst the largest economies and emitters.

- The EU is made up of 28 Member States and it can be difficult to present a coherent EU position, in particular when position differs nationally. There are also difficulties (and some benefits) from leading Member States wanting to carve out their own distinctive positions and diplomatic relations (for example the UK-USA ‘special relationship’). The EU taking on a greater role internationally without

---

aligning the position of its Member States effectively could exacerbate the conflict between the EU and national governments in negotiating agreements.

10. a. What future challenges or opportunities might we face on environmental protection and climate change?
b. Going forward what do you see as the right balance between action taken at international, EU, UK and industry level to address these challenges and opportunities?
c. What would be the costs and benefits to the UK of addressing these future challenges at an EU level?

- Environmental and climate protection look to face a number of challenges in the future, notably because the stresses inflicted by an increasing global population are set to increase demand for natural resources. For the EU one considerable stumbling block could be reduced political ambition around tackling climate change due, primarily, to the current economic situation. This is not to say that there are no politicians championing progressive legislation on the environment and climate but the recent difficulties in securing the “back-loading” of allowances in the EU ETS has highlighted a split in the European Parliament. One reason for this division is that economic concerns have raised the profile of national concerns, with some Member State reluctant to move forward on ‘big picture’ environmental and climate legislation in fear it might have a negative effect in their own Member State through increased business charges, or boosted energy prices. Diverging interests have started to appear, with Member States are increasingly becoming polarized in their views of the solutions to their needs and challenges. For example, the long-term vision of the UK and Poland highlights the gulf between some Member State positions. The cost of acting to avert climate change has challenged action, and despite the economic assessment of Lord Stern and others who argue prevention is cheaper now than emergency adaptation later, the cost of transitioning towards a low-carbon economy is set to remain a contentious issue.

- An international agreement on climate change is still the most effective way to tackle climate change. Despite setbacks, increased bottom-up action, particularly from China and the USA, is setting the ground for a possible breakthrough at the international level. The upcoming COP 21 in Paris will be a pivotal moment in the future of the drive in tackling climate change, and the level of EU ambition could set the tone for the conference.

- A major opportunity for growth in the UK increasingly comes from sustainable business. Effective regulation and incentives at an EU level can boost this potential, and build a future-proofed UK economy, and a competitive advantage over countries that move more slowly on tackling climate change.

- The Fifth Assessment Report (AR5) from the Intergovernmental Panel on Climate Change (IPCC) is due to begin publication in autumn 2013 and set to highlight the increasing threat and current effects of climate change. Acting to avert these worst effects of climate change offers incalculable benefits, but these include a functioning economy, biosphere and civilisation.
• In 2012 the EU spent USD$500 billion on importing oil. Reducing this figure, which dwarfs the national debt of Greece, would be hugely beneficial to the European economy, reduce energy costs for citizens, offer geopolitical benefits, and insulate Europe against further commodity price shocks. Action on steering economies away from fossil fuels is most effectively taken at the highest level, for example an EU-wide Fuel Quality Directive not only prevents the most polluting fuels reaching Europe, but calls into question their initial extraction, influence that the UK would be unable to exert unilaterally.

• The UK should ensure that ambitious action on climate change is actively pursued at all possible levels. The transboundary nature of environmental and climate problems means that the most effective level to address the problems would be at an international level. This should, however, not detract from seeking action at EU, and regional levels. Addressing climate change at these different levels offers different opportunities and potential gains. Furthermore, successes at one level can have a complementary effect of putting pressure on another. For example, despite the current lack of international climate agreements the bottom up move in countries implement climate policies and carbon market, such as Australia, Korea and China, has changed the dynamic of the international debate.

• Costs for the UK fall under the difficulty of unilateral action within the EU ETS; greater ambition in the UK only opens up extra pollution space elsewhere in the EU, if sustainability efforts are not explicitly linked with the removal of carbon permits. Otherwise, the main benefit offered to the UK by action at a European level is more substantial carbon cuts when compared with the global scale of the problem, and through magnified EU influence beyond the Urals and across the Atlantic.

• Policy at EU level also offers greater security to green investors, with a wider available market, and less likelihood of policy reversal through temporary domestic pressure. For instance, as an escalator, the UK Carbon Price Floor may suffer similar difficulties to domestic tax escalators on fuel and alcohol, as governments pursue short-term electoral gain. The dispersed nature of EU parliamentarians and the structure of EU governance offers longer-term certainty to decisions reached with 28 state consensus.

11 Are there any general points you wish to make which are not captured in any of the other questions?

• The EU ETS, for all its problems, remains the world’s largest market in climate change pollutants, offering the current ability to control and reduce half of Europe’s emissions. Through scope expansion, and through linking with new schemes (Australia, the Western Climate Initiative, China), it could become more powerful still. In the event of a substantial renegotiation (or referendum) on

---

competencies, Sandbag would expect a large number of EU environmental directives would need to remain incorporated in UK law to enable cooperation and continuing exports which met EU standards, but the UK would have the option to make more ambitious (or less challenging) emissions cuts, but in isolation. By remaining a key player in deciding EU climate policy, the UK greatly magnifies its global influence toward fighting climate change.