Germany parliament trims utilities' allocation by 38 million allowances/year

German parliamentarians last week adopted the legal basis for emissions trading in the second phase of the EU emissions trading scheme (ETS), with legislators cutting the free allocation to utilities by 38 million allowances per year.

The parliament decision for the biggest participant in the EU ETS also results in a reduction of 2 million allowances annually from the reserve. The reductions in free allowances were made to make room for auctioning 40 million allowances per year of the 2008-2012 second phase.

In addition, the government is allowed to auction allowances from the reserve to cover the expenses of administering emissions trading, and to cover costs that have occurred when replenishing the reserve for new installations in the current first phase of the EU ETS.

The environment ministry has estimated it needs to auction or sell five million allowances per year to cover the costs, and sources close to the government reckon Germany is likely to maximise the 10 per cent limit on auctioning laid down in EU law.

The parliament introduced auctioning as a means to curb windfall profits enjoyed by utilities, which have been accused of passing the cost of free allowances on to consumers.

In a related move, the parliament upped the limit on the use of Kyoto project credits to 22 per cent from 20 per cent. However, this does not mean German installations will be allowed to import more credits, as the figure is relative to the lower free allocation.

"The total quantity allocated is reduced by 40 million tonnes due to the start of auctioning. In the past it was intended that companies could use an emissions volume of 90 million tonnes CO2 per year, or 450 million tonnes for the entire second trading period," Tobias Dunow, a spokesman for the German environment ministry told Point Carbon.

"In order to keep this budget constant, the CDM/JI quota has been increased to 22 per cent in a parliamentary procedure," it said.

Still, an increased import would not be permitted by the European commission, because Germany failed to notify officials that it wanted to maximise its use of project credits.

"If the new limit meant an increased import potential, this would probably not be accepted by the commission. All changes to the national allocation plan would have to be reported to the commission by the end of 2006, and Germany reported in a 20 per cent limit on the 453-million cap," said Stig Schjoelset, Senior Policy Analyst with Point Carbon.

The German emissions trading association (BVEK) said the changes made by the parliamentarians were a "significant improvement" compared to the government's proposal.

However, the association was disappointed that the government was not forced to hold any auctions before 2010. In addition, the association would have preferred that the 25 million allowances that are expected to be auctioned over the five-year period to cover expenses were governed by the same rules as the 40 million allowances per year specifically set aside for auctioning.

"An auction should be held for the benefit of the market operation," Jurgen Hacker, chairman of the BVEK, said, indicating that the government might get an incentive to maximise its profits in selling the allowances from the reserve.

BVEK reckons that the "opportunity to significantly reduce the market price of allowances and thus the power prices through properly organised auctioning has thus been squandered."

It also regrets that since the entire cut in emissions allowances was made for the power sector, other industry sectors in the trading scheme will lose out on emissions reduction opportunities.

In a research note on the German allocation, Deutsche Bank on Thursday said it expected installations that were covered in the first phase of the scheme to have a deficit of up to 80 million allowances per year of the 2008-2012 trading period.

In addition, the Bank said it expected the reserve to be too small to cater to new entrants, increasing the deficit by 15 million allowances per year.

