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Lithuania blocking landmark reforms to EU climate policy

As European governments debate a proposal to fix Europe's oversupplied carbon market, the Lithuanian government continues its alignment with a small bloc of countries led by Poland, who seeks to not allow the reforms to start before 2021 and to allow hundreds of millions of additional allowances to flood into the market. A new study from climate change think-tank Sandbag highlights how Vilnius' position threatens to undermine the reform package, and could also lead to a significant loss of national revenue.

The EU emissions trading scheme is Europe's single largest climate policy, controlling carbon emissions for Europe's power stations, factories and internal flights by establishing a limited supply of tradable carbon allowances. However, the market is massively oversupplied with allowances, with the surplus standing at over 2 billion since 2013 – a volume larger than emissions for all covered companies over a full year. This has depressed prices in the scheme, diluting incentives to adopt low-carbon technologies and threatening to make the policy irrelevant for decades.

A welcome proposal to create a Market Stability Reserve, acting as a transparent system automatically adjusting the supply of allowances in accordance with market conditions, is now being debated in the European Council. The European Parliament's Environment Committee proposed in February to implement the reform already in 2018, while governments of EU Member States support in the Council starting already in 2017. However, the Lithuanian government has sided with a blocking minority of countries led by Poland. [1] Warsaw very vocally seeks to prevent the reforms from being enacted before 2021 to protect its fleet of CO_2-belching coal-fired power plants.[2]

Sandbag, an environmental-think tank based in London, estimates that, if left unchecked, the chronic oversupply of carbon allowances could roughly double from today's levels, reaching 4.4 billion by 2020.[3] Under these circumstances, even the most ambitious reforms being currently debated would not manage to get the oversupply back below current levels before 2030, effectively breaking the back of the EU's climate policy. Lithuania has thankfully agreed to prevent 900 million allowances whose auctioning was postponed as an emergency measure to 2019 and 2020 from re-entering the market, yet continues to oppose an earlier start date and is keeping silent about the forceful auctioning of a second avalanche of some 750 million of so-called unallocated allowances in 2020.[4]

If Vilnius adopted a more constructive position, the surplus would be diminished from today's sky-high levels in a gradual fashion, meaning that there are no grounds for industry to fear an escalation of the carbon price before 2020. Furthermore, Lithuanian industry enjoys the legacy of earlier years of the EU ETS, when companies received significantly more allowances than their verified emissions. This effectively insulates them from any negative effects that the ETS might have on their competitiveness. For instance, AB Achema had nearly 200% more allowances than emissions until 2012, after which it started competing on a fair basis with other EU companies, when its allowance allocation came to be decided by common EU-wide benchmarks. Similarly, although OrlenLietuva has competitors in 23 EU countries, because it is likely to receive more allowances than it needs until 2020, it will be protected from the carbon price for longer than companies in 14 EU Member States. Finally, the historical surplus coupled with recent

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[1] Such as Bulgaria, Croatia, Cyprus, the Czech Republic, Hungary, Poland and Romania.
[2] According to Eurostat, since 2004 Lithuania has had no net yearly imports of electricity from Poland.
[3] See Sandbag's briefing "The Eternal Surplus of the Spineless Market".
[4] These are made up of allowances reserved for companies that may have potentially entered the carbon market over 2013-2020 (new businesses, production lines, etc.) but never actually did, and for companies that exited the market over the same period (closures, diminished production, etc.). See Sandbag's briefing "Avoiding the Avalanche".

efficiency improvements ensure that Akmenės Cementas may not need to buy a single allowance before 2023.[5]

Taking forceful action on the surplus would also have positive effects on Lithuania's finances, as well. Poland's blocking minority has constrained the EU's Latvian Presidency to propose a 2021 start and no clear way of dealing with the unallocated allowances. However, PointCarbon, a Norway-based analysis company specialising in carbon and energy markets, has calculated that starting early and keeping the unallocated allowances off the market as well would boost Lithuania's auction revenues by EUR 80 million.[6] These revenues could for instance be diverted to offset increased electricity prices to sensitive sectors of Lithuanian society or industry.

Damien Morris, Sandbag's Head of Policy says
"The current proposals to curb the oversupply of carbon allowances in the ETS are already long overdue, and further setbacks can only delay the recovery of Europe's ailing carbon market. The Lithuanian government should join with progressive countries to support the swift implementation of a Market Stability Reserve and the removal of hundreds of millions of unallocated allowances poised to flood the market in 2020. The additional auction receipts this would generate mean this would not just be a win for the environment, but also for the Lithuanian taxpayer."

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[5] Assumes emissions continue at 2013 levels and current carbon leakage protections continue. These three companies accounted in 2013 for over 69% of Lithuania's ETS emissions.
[6] Revenues go up as because the price of auctioned allowances will increase relative to the less ambitious proposal. Estimate is for the period 2015-2024. These are unpublished figures Point Carbon provided to Sandbag on request.