

Remarks on ETS 3 auction design (COM consultation paper)

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Sale of EU allowances 2008-2009

During the first trading period (2005-07) all EU Allowances (EUA) have been given for free to German operators with compliance obligations under the EU Emissions Trading Scheme (EUETS). From 2008 8.8% of the total allocation have been reserved for sale. These 40 million EUAs per year have been sold by KfW via the two carbon exchanges in London (ECX) and Leipzig (EEX) since January 2008.

The sales are transacted on each business day with many small sale tickets over the course of the trading day to avoid any market influence. In 2008, sales were transacted exclusively via the most liquid December Futures contract. Since March 2009 sales are also carried out via the Spot markets on ECX and EEX.

The 2008 results of these screen traded transactions are convincing:

- 933 million EUR revenues
- 23.33 EUR/EUA average price realised
- no deviation from CFI Index
- very low transaction costs
- very little influence on carbon market
- highly appreciated sales procedure from market participants.

Remarks on ETS 3 auctions

ETS 3 auctions should:

- avoid market distortion and be as frequent as possible *à KfW sales experience shows, that up to 10 percent of the daily screen traded volumes can be easily sold without distorting the market. Given the huge amount of allowances to be auctioned in ETS3, this can be done by carrying out auctions daily or even several times daily. (à continuous auction). Secondary market prices on a liquid exchange which show real scarcity prices can be used as benchmark.*
- include Spot and Futures and be flexible regarding volume of Spot and Futures depending on market development *à The auctioneer should observe the development of the volumes traded on the carbon market and should respectively adjust the relation Spot vs. Futures contracts. Optimally Spot auctions should dominate between December until end of April (due to December Futures expiry and due to closing short position at the beginning of each year).*
- be open to allow selling of allowances as alternative to auctioning *à Selling allowances via exchanges over the course of the day is a very efficient procedure for non-free allocation (as Germany, Norway and the World Bank (Adaptation Fund) are currently doing). This is a proven and reliable method with a high market acceptance which can be implemented immediately. This is especially valuable in respect to selling ETS3 allowances already in 2010 or 2011 to provide liquidity to compliance companies trying to hedge their 2013 electricity sales. Moreover the secondary carbon market (exchanges or OTC) provides a high liquidity with real scarcity prices.*

moreover auctions should:

- be transparent, non discriminating, reliable and predictable for market participants
- have low transaction costs and therefore use available infrastructure (à existing exchanges)