

Overview of longer-term challenges to – and opportunities for – China's national ETS

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1. Improvement of System Design is a Continuous Process

- ETS operates not in vacuum and its design must coordinate with other policies to achieve the efficiency improvement expected
- The design of all existing ETSs are under continuous improvement to accommodate the impacts of evolving broad policy context
 - ✓ domestic policies e.g. enhanced mitigation target, RE and EE policies, other industrial development policies
 - ✓ international challenges, e.g. major mitigation policies (ETSs, board carbon adjustment measures, ...) in other countries
 - ✓ Responses of the covered sectors
- Effective improvement requires assessment to facilitate sufficient understanding of the possible impacts

2. Unnecessary Competing Policies should be Eliminated

- Many existing policies interact with China's national ETS, affecting its effectiveness and/or efficiency, including e.g. RE and EE policies, especially *Trading of Rights to Use Energy* (former *Energy Conservation Trading*)
- *Trading of Rights to Use Energy* is still at its initial phase, being piloted in four provinces
- The design of *Trading of Rights to Use Energy* is very similar to ETS in terms of almost all major elements: coverage, cap setting, allocation of initial rights, trading, compliance, etc.
- Interactions are well understood, but vested interests are a major barrier and those in the right higher post failed to deliver

3. Enhanced Mitigation Target should be Incorporated

- Characteristics of China's current overall mitigation target, e.g. intensity-based, have been fully reflected in the current design of China's national ETS
- Intensity-based de-facto emissions cap mainly determined by allocation approaches is an appropriate choice at the very initial stage, trying to overcome political difficulties and not making perfect the enemy of good
- With the announcement of China's new middle- and long-term mitigation targets, an absolute control cap should be introduced in the near future, to make ETS a real corner-stone policy instrument in China's mitigation policy tool box
- The transition period should be as short as possible

4. Auctioning should Play an Important Role ASAP

- Impacts of other policies, e.g. those on energy efficiency and over capacity phasing-out, have been reflected in the current allocation choice (real production-based benchmarking) of China's national ETS design
- This type of compromise is common and necessary in almost all ETSs
- To give full play of the impacts of ETS, auction should be attached more importance and hopefully play a significant role in the near future
- This is important in terms of both achieving the domestic mitigation targets but also addressing challenges imposed by board carbon adjustment measures

5. Long-term Policy Certainty and Flexibility Needed to Accommodate Changes should be Balanced

- Long-term policy certainty is as important as the stringency of current allocation approaches in terms of affecting the decision making of covered enterprises in China's pilot systems
- Flexibilities need to accommodate evolving broad policy context
- A possible balance
 - ✓ A strong legal basis establishing the long-term existence and general trend in terms of system design, e.g. cap setting, allocation, MRV requirements, compliance, etc.
 - ✓ Flexibility on detailed design leaving to the ETS authority to elaborate

6. Division of Responsibilities between the Central and Provincial Authorities regarding Mitigation

- Currently, the provinces are responsible for the achievement of differentiated whole-economy mitigation targets assigned by the central government
- Entities covered by the national ETS are crucial for the achievement of the provincial targets
- Uniform system design not compatible with the current management arrangement, and this is why the flexibility provision in terms of reducing free allowances was established to the provincial authorities in the original design of the national system
- A possible way out is that provinces are only responsible for the mitigation targets covering the non-ETS entities

Thanks

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