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European Climate Policy: Toward Centralized Governance?

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Abstract

The EU emissions trading system (ETS) is the first large-scale international emissions trading system and a 'cornerstone' in EU climate policy. A key element in the ETS implementation process is deciding upon the ceiling ('cap') for the emissions included in the ETS. Over time, a significant change and centralisation of this model has taken place. In order to understand this development, we need to acknowledge the increasing acceptance of stronger centralised governance among the member states due to ETS pilot phase problems; take into consideration frustration in the European Commission over complex and differing National Allocation Plans; and add the fact that the Kyoto Protocol target was getting nearer and a good performance of the 'flagship' ETS was becoming increasingly important. Hence, although the case supports the importance of acknowledging the multi-level character of the EU, it still emphasises the key role of changes in member states' interests and positions for understanding outcomes.

KEY WORDS: EU climate policy, emissions trading system (ETS), governance, intergovernmentalism, multilevel governance, regime theory

1. Introduction

The EU emissions trading system (ETS) is the first large-scale international emissions trading system in the field of the environment. No wonder it has been called 'the new grand policy experiment' (Kruger & Pizer, 2004: 1) and 'a fundamental systems change in environmental governance' (CEPS, 2002: 6). As indicated by the CEPS quote, the system raises questions of multilevel power and governance with implications far beyond the sphere of climate politics. The ETS is a system whereby companies are allocated allowances for their emissions of greenhouse gases and they can then trade these allowances with each other.¹ The main ETS directive was adopted in mid-2003 and established a three-year pilot phase (2005–2007) to precede the main commitment period of the Kyoto Protocol (i.e., 2008–12) (EU Council, 2003, Directive 2003/87).

The ETS was established as a fundamentally 'decentralized' system, i.e., key decisions about the amount and allocation of allowances were in the hands of the member states. In January 2008, the European Commission (hereafter the Commission) put forward a proposal for a revised ETS post-2012 (European Commission, 2008). This is a proposal for a much more centralized ETS, characterized as a 'revolution' in the division of power between the EU and Member States' (Carbon Trust, 2008: 17). The ETS reform proposal was then finally

adopted in December 2008 (Skjærseth & Wettestad, 2009). How we best may explain this possibly ‘revolutionary’ change of governance is the key question addressed in this article.

In the literature on governance in the undoubtedly multilevel EU, there are at least two main competing heuristic lenses for understanding and getting a grip on fundamental driving forces. The first and initially dominating lens is generally referred to as ‘intergovernmentalism’ (e.g. Moravcik, 1993, 1998; Schimmelfennig & Rittberger, 2004). Although scholars in this tradition do not reject the multilevel character of the EU, a key notion is that the EU can basically be understood as an international regime. At the anarchical international stage, sovereign states are the key actors and so is the case within the EU. Hence, the key variable and determining force is the interests and positions of member states, and the key EU body is the Council.

From the mid-1980s on, and not least related to the increasingly important co-decision role of the supranational European Parliament, there has been increasing scholarly attention to the notion of multilevel governance and ‘supranationalism’ (e.g. Stone Sweet & Sandholz, 1997; Hooghe and Marks, 2001, 2003; Bache & Flinders, 2004). The increasing powers of supra-national institutions such as the Commission and European Parliament mean that they have an independent influence on policy-making that exceeds their role as agents for national governments. These scholars emphasize that European integration has weakened the key role of states in EU governance.

Furthermore, emphasizing the multilevel aspect even further, other scholars have also increasingly pointed out that EU policy-making often takes place and is ‘nested’ in wider regional or global regimes, and hence that the interaction with such regimes should be given more attention in order to more fully understand EU decision-making (e.g. Weale et al., 2000; Skjærseth & Wettestad, 2002). This is then the general backdrop for the discussion in this article. Does the case of ETS reform add increased weight to the notion of weakening state power in the EU? Or does a closer scrutiny of the case add weight to the notion that – if cut to the core – intergovernmentalism is still ‘the dominant game in town’?

A key element in the ETS implementation process, and its ability to deliver the desired effects in terms of significantly reduced emissions, is deciding upon the ceiling (in ETS language called the cap) for the emissions included in the ETS. The level of the cap determines the availability of allowances in the system, subsequently the allowance price, and ultimately the incentives for companies to invest in new technologies and carry out more abatement. Given that the EU has declared a ‘cornerstone’ role for the ETS in EU climate policy, the cap-setting process hence becomes a central feature of EU climate policy governance.

As indicated, the initial ETS cap-setting model was fundamentally decentralized. The member states produced National Allocation Plans (NAPs) which set out the total cap for their domestic emissions and the more specific distribution among the relevant installations. The Commission was given a role as a watchdog regarding the extent to which NAPs adhered to the steering criteria formulated in the 2003 Directive, and particularly, whether the proposed cap was reasonably ‘ambitious’ (i.e. pointed towards real and significant emissions reductions).

The interesting, rather low-key first change of this model took place in the course of the NAP II process in 2006 (i.e. the process of producing and assessing NAPs for the 2008–12 period). Cap-setting criteria were boiled down to three key ones, among which assessing the cap in light of emissions verified in 2005 figured centrally. ‘Armed’ with this new model, the Commission took on a more active role in NAP II, cutting a number of proposed caps – in some cases quite significantly. The changing of the cap-setting model was then taken a significant step further in the Commission’s January 2008 proposal for the ETS post-2012. It was suggested to do away with NAPs completely, and formally centralize the cap-setting

process to a greater degree. This was then finally adopted as part of the final agreement on ETS reform in December 2008. The step-wise changing of this model is further documented in section 2 of this article.

In section 3 of the article a multilevel explanatory approach will then be utilized to shed light upon this fascinating change. In such a multilevel approach, as discussed above, the first and basic perspective is an ‘intergovernmentalist’ one, focusing upon the positions and roles of the member states. Adopting intergovernmentalist lenses, we posit that the changing of the cap-setting model can be explained by changes that took place in the positions of the member states. Although there were mixed emotions, key member states initially preferred a decentralized system. This may have changed after the ETS started functioning, possibly due to the member states coming to evaluate the costs of a ‘decentralized anarchy’ as higher than the sovereignty benefits of such decentralization. On this basis the member states may have instructed the Commission to change the cap-setting model.

The second perspective draws upon the mentioned field of literature highlighting the increasing ‘multilevel governance’ character of the EU, and in this context, particularly the enhanced role of supra-national actors such as the Commission and European Parliament in EU policy-making. The Commission also has formal executive powers to oversee the implementation of EU policy. As shown by previous research, the ETS can very much be described as the Commission’s ‘baby’, and the Commission built up a strong position in the ETS initiation and decision-making phases (Skjærseth & Wettestad, 2008). So the Commission may have acquired a special, independent interest in ETS success. Hence, adopting such multilevel governance lenses, we posit that the changing cap-setting model can be explained by the Commission acting independently of the member states. Although the Commission was initially given quite limited NAP and implementation watchdog powers in the 2003 ET Directive, factors such as the strong position acquired earlier and a loosely formulated NAP watchdog mandate may have opened up for independent moves by the Commission.

The third perspective draws upon the mentioned studies highlighting the fact that EU policy-making and implementation most often takes place within a wider regional and/or global political and institutional context. So in order to fully understand what goes on in the EU context, developments in such wider fora need to be taken into account. In the field of climate change, the most important such institutions for the EU are the 1992 United Nations Framework Convention on Climate Change (UNFCCC) and its 1997 Kyoto Protocol.

Since the early 1990s, the EU has increasingly sought to establish itself as a ‘soft power’ leader in global environmental governance in general, including the issue of climate change (e.g. Gupta & Grubb, eds., 2000; Oberthur and Kelly, 2008). As shown by e.g. Damro & Luaces Mendez (2003) and Skjærseth & Wettestad (2008), global developments strongly influenced both the initiation and decision-making phases of the ETS. Hence, adopting such ‘global lenses’, we posit that the changing of the cap-setting model can be explained by developments in the global climate regime. For instance, the Kyoto Protocol formally entered into force in February 2005, and made compliance with the Protocol’s 2008–12 targets a more pressing issue for all parties involved. For the EU, the Protocol called for an eight percent reduction of greenhouse gas emissions. Global targets and requirements may hence have ‘forced’ the Commission to acquire more centralized control over the cornerstone ETS, and particularly the emissions caps.

In the concluding section 4, we will sum up main findings and discuss important implications and prospects ahead. As the new and significantly changed cap-setting model now has been formally adopted, does this mean that member states have acceded significant new powers to Brussels? Or do more hidden elements in this development counterbalance this seeming turn towards more centralized governance? What does the case of ETS reform mean for the more general debate on the changing nature of EU governance?

2. From Decentralized to Centralized Cap Setting: What Has Happened?

2.1. *Baseline: The Initial Decentralized Cap-Setting Model in NAP I*

From the very first discussions on the ETS design from 1999 on, a key dimension and topic for discussion was that of decentralization versus centralization. This is a more generic and general topic of conflict and debate in the EU: should power regarding EU policy rest with and at the level of member states, or should Community institutions be given a more firm grip on the policy ‘steering wheel’?²

For instance, the ETS Green Paper put forward in March 2000 noted that EU emissions trading could be organized at several levels, with varying degrees of Community intervention (European Commission, 2000). A trade-off was noted between providing high equality of treatment and simplicity on the one hand (i.e. a centralized model) and high member-state autonomy on the other (i.e. a more decentralized model). The latter could lead to segregation, which would run counter to the objectives of the internal market (ibid.: 12). Concerning the allocation of allowances, that is the quantity of greenhouse gas emissions assigned to each participant in the system, an implicit plea was made for centralized setting of the national ceilings/caps.³ A more decentralized approach would require ‘detailed and tight guidelines on how allocations are made in individual sectors and companies, and close scrutiny of every single case’.

For reasons discussed in section 3, when the Commission put forward its directive proposal in October 2001, the cap-setting model was basically decentralized (European Commission, 2001). The member states were required to base their allocations – formulated as specific National Allocation Plans (NAPs) – on a number of different criteria, put forward in a specific annex to the directive. The NAPs could then be rejected by the Commission if these criteria were not observed (ibid.: 5–6). The Commission was hence given a watchdog role in relation to the NAP process. This approach was basically left unchanged in the decision-making process. Hence, Article 11 in the 2003 ET Directive stated that ‘each Member State shall decide upon the total quantity of allowances it will allocate for that period and the allocation of those allowances to the operator of the installation’ (EU Council, 2003). Furthermore, in Annex III, 11 criteria were put forward as guiding signals for the production of National Allocation Plans and the setting of caps:

- ‘Consistency between total quantity of allowances and the Member States’ commitments under the Kyoto Protocol.’ This reflected that the ETS is a main EU instrument to achieve the 8% reduction commitment taken on by the EU in the Protocol.
- ‘Consistency between quantity of allowances and assessments of emissions development.’ This criterion, as well as the next, were important in order to make governments avoid handing out more allowances than needed.
- ‘Consistency between quantity of allowances and potential to reduce emissions.’
- ‘Consistency with other Community legislative and policy instruments.’ This was important in order to avoid contradictory requirements.
- ‘Non-discrimination between companies or sectors.’ This criterion, as well as the next, were important to protect the internal market and create a level playing field.
- ‘Information on the treatment of new entrants.’
- ‘Information on how early action would be taken into account.’ This criterion, as well as the next, were important in order to avoid that frontrunner industries were punished for taking early action and installing cleaner technologies.

- ‘Information on how clean technology would be taken into account.’
- ‘Information on how the public would be involved.’ This was important in order to ensure transparent processes.
- ‘List of installations and their respective allowances.’
- ‘Information on how competition from outside the EU would be taken into account.’ This was important in order to get a better picture of the challenge of ‘carbon leakage’, i.e. EU industries relocating to less carbon-restrained countries.

Inevitably, these criteria were quite generally formulated. Hence, the need arose for a somewhat more specific guidance document. So the Commission published a Communication in the beginning of January 2004 (European Commission, 2004). Among other things, the document clarified that only four of the 11 criteria were to be considered as mandatory (i.e. assessments of emissions development; non-discrimination; public involvement; and list of installations).

On this basis, the NAP I process got into gear, as further elaborated in section 3. It was characterized by many delayed and incomplete plans; an overall modest level of ambition regarding emissions reductions aimed for, which was further confirmed when verified 2005 emissions figures were presented in May 2006 and showed 4 percent more allowances handed out than needed; and the Commission functioning overall as a rather lenient watchdog, cutting suggested caps by 4.5 percent (see Skjærseth & Wettestad, 2008: Chapter 6).

2.2. The Changed Cap-Setting Model in NAP II: Down to Three Key Factors

With regard to the NAPs for the second ETS phase (2008–12), the Commission published a new Communication in late December 2005 (European Commission, 2005). The Commission indicated that if the emissions-trading sector were to contribute a proportionate share of the reduction needed in member-states with a gap to close in order to reach the Kyoto target, then the overall cap for the second phase should be 6 per cent lower than in the pilot phase (ibid.: 6). Allocations to any member-states that were off-track from their Kyoto target compared to actual 2003 emissions should be further tightened.⁴ With regard to the latter, and as an additional criterion that did not apply in the first phase, member-states were required to specify a maximum amount of intended government purchase of Kyoto units. The established percentage should be consistent with the state’s supplementarity obligations under the Kyoto Protocol and decisions adopted pursuant to the UNFCCC or the Kyoto Protocol (ibid.: 7).

Furthermore, the first verified ETS emission figures, summing up 2005 emissions, were put on the table in May 2006. The publication of these figures changed the NAP II process further. In November 2006, it became clear that in addition to the earlier announced criteria (particularly the need for consistency with Kyoto commitments), also the 2005 emission data would figure as a central assessment criterion. Hence, the Commission’s press release published on November 29 stated that the Commission would require changes to NAPs where ‘the proposed total of allowances is not consistent with expected emissions and the technological potential to reduce emissions, *taking into account independently verified emissions in 2005, anticipated changes in economic growth and carbon intensity*’ (European Commission, 2006a; my italics). Hence, the Commission had now explicitly spelled out its procedure and ‘formula’ for NAP II assessments, in fact drawing upon very limited information from the submitted NAPs (primarily related to additional installations). The formula was hence: 2005 verified emissions * growth trend development 2005 to 2010 * carbon intensity trend development 2005 to 2010 * additional emissions covered by an extended scope of combustion installations (European Commission, 2006b : 5).

The main bulk of the information used by the Commission to assess NAPs came from the PRIMES energy system model. The work on the PRIMES model started back in the early 1990s and PRIMES is an energy systems model covering the energy demand and supply system in the EU member states (Vainio and Zapfel, 2006). The model includes considerations about market economics, industry structure, energy/environmental policies and regulation. It was conceived for forecasting, scenario constructing and policy impact analysis, in a medium to long-term horizon.

This meant that the Commission, quietly and almost unnoticed at first, had introduced a quite different model for the setting of caps than the one described in the 2003 Directive. On this basis, the Commission went on to demand considerable downward adjustments of particularly the Czech, German and Polish NAP II caps, something which only the Germans grudgingly accepted. Also several other NAP II cuts were demanded on the basis of this new model, something which sparked a more widespread ‘Eastern rebellion’ among the EU newcomers.⁵ All in all, the Commission managed to turn a proposed aggregate emissions *increase* of 5% from 2005 levels into a 5% *decrease* (Carbon Trust, 2007: 6).

2.3. The Significant 2008 Changes: Away with NAPs and a Centralized Approach

After consultations on ETS reform with member states and various stakeholders in four meetings in 2007, the Commission put forward a formal proposal for a revised ET Directive for the post-2012 period on January 23 2008, along with the rest of the EU’s new energy and climate package. In addition to important suggested changes to allocation methods, i.e. a move towards significantly more auctioning of allowances, the main suggested change of interest in this particular context regarded the cap-setting model. The Commission proposed to set a single EU-wide cap and to allocate allowances on the basis of fully harmonized rules. NAPs would therefore no longer be needed.

The level of the EU-wide cap for the ETS needed to be consistent with the March 2007 EU commitment to an overall reduction in greenhouse gas emissions of 20 percent by 2020. The linear reduction which is consistent with this principle amounts to 1.74 percent per year, arriving at a reduction of ETS emissions of 21 percent below 2005 emissions. This path had been calculated by starting at the mid-point of the 2008-12 period average annual total quantity of issued allowances (European Commission, 2008: 7). The Commission was to publish the absolute quantity of allowances for 2013 by June 30 2010 (Article 9, *ibid.*: 21). Hence, similar to the revised approach introduced in November 2006, 2005 emissions figured as a central baseline and foundation in the new approach. Most other elements were new, however – the common cap, the linear decrease factor of 1.74 percent, and the starting point for allocations in the average annual quantity in the 2008-12 period.

As noted, the Commission’s cap-setting proposal was then adopted in December 2008. According to several observers and analysts, this development represents a significant turn in the ETS centralization process. For instance, according to Hasselknippe, Schjølset & Ulset in *Point Carbon*, ‘the Commission has initiated a process towards *almost absolute centralization*, with caps and distributions being set in Brussels’ (Hasselknippe, Schjølset & Ulset, 2008: 7; my italics). *Carbon Trust* has commented that ‘in principle, this represents a *huge centralization of powers*, of the sort that EU Member States have resisted for decades’ and, as noted, characterized the development as a ‘*revolution...in the division of power between the EU and Member States*’ (Carbon Trust, 2008: 21, 17).

How, then, did this ‘revolution’ come about? And how ‘bloody’ was it?

3. Explaining the Development from Decentralized to Centralized Cap Setting: The Multilevel Three Lenses

3.1. *Did the Member States Change their Minds about the Virtues of Decentralized Cap Setting?*

The first main explanatory perspective adopted ‘intergovernmentalist’ lenses and posited that the changing of the cap-setting model could be explained by changes having taken place in the positions of the member states that initially favoured a decentralized system. This may have changed after the ETS started functioning and the member states realized that the costs of decentralization may be higher than the benefits of such a system, leading them to require the Commission to change the cap-setting model.

Let us first briefly clarify the initial mood among the member states regarding the basic design of the ETS. In the process of initiating the EU ETS and discussing various design issues and options, the Commission seemingly favoured a quite centralized approach, including the issue of cap setting. Although the responses from the member states to the 2000 Green Paper on the issue of harmonisation and cap setting was both mixed and somewhat unclear, an important element was that the UK, a key EU country, trading proponent and hence an important ally to the Commission, clearly preferred a decentralized system. Furthermore, except for Denmark, none of the other trading proponents in the EU preferred a centralized system (i.e. Ireland and the Netherlands). Germany did not respond to the Green Paper, but due to its general reluctance towards the ETS initiative, it was reasonable to assume that Germany would have least objections to a decentralized system (Skjærseth & Wettestad, 2008: Chapter 4). These countries favoured a decentralized approach because this provided them with maximum control when entering a new and uncharted regulatory territory.

So it is not surprising that when the Commission put forward its formal ET Directive proposal in October 2001, the approach was a fundamentally decentralized one. The member states were to propose caps in their National Allocation Plans, and no common ETS cap would be established. The ETS cap and overall ambitiousness in pointing towards real and substantial emissions reductions would emerge ‘from below’, as the sum of the national NAPs. In the subsequent decision-making process, the European Parliament sought to re-introduce a sort of common cap, but it failed.⁶ Hence, the 2003 Directive established a fundamentally decentralized ETS. It has thus been claimed that ‘the most fundamental political deal that enabled the EU ETS to be launched as a European-wide venture was that the Member States would retain the right to allocate allowances’ (Carbon Trust, 2008: 21).

As described in section 2, the first main change of the cap-setting model took place in November 2006, with the introduction of the model focusing on three main criteria. At this point in time the ETS had functioned for almost two years, and major upheavals – some would say ‘shocking events’ – had taken place. After surprisingly high allowance prices in the fall of 2005 and winter of 2006 (up to a peak around 30 euro), the verified emission figures for 2005 were put on the table in May 2006. These figures showed that the amount of allowances handed out was higher than actual emissions (and hence ‘over-allocation’ had most likely taken place), the allowance price dropped substantially and quickly. It is reasonable to assume that many actors, both within and outside of governments, saw this as a strong indication that the initial ETS design was far from perfect and changes were necessary.

Furthermore, when more and more NAP IIs were put on the table from mid-2006 on, alarm bells started to ring in Brussels. Member states seemed to produce NAPs and set caps with the same moderate ambitiousness that had characterized the pilot phase NAPs. This led Environment Commissioner Stavros Dimas to state ‘much to my regret, taking the first 17 notified national allocation plans, they propose a cap about 15 percent above actual emissions in 2005’ (ENDS Daily, October 23, 2006). Also some countries, such as the ‘ETS

frontrunner' the UK, expressed concern. For instance, a senior UK government official stated in October 2006 that the ETS needed 'real scarcity and *more harmonisation*' (EU Energy, October 20, 2006: 24; my italics).

Hence, when the Commission introduced the new cap-setting model in its first 'verdict' on the ten first NAP IIs in November 2006, it probably felt that it had sufficient backing among the member states to do so. But: was it *instructed* to change the cap-setting model? It should here be noted that prior to the Commission verdict, the NAPs had been discussed in the Climate Change Committee, which is an advisory body composed of member state representatives established in 1993. As a main NAP II guidance, the Committee had 'called on the Commission to assess all national allocation plans on a consistent, coherent and robust basis', also emphasizing the importance of using the 2005 verified emission figures as a significant assessment element (European Commission, 2006b: 2). So even if this cannot be considered an instruction, it was at least a clear request for tougher practices. Hence, the perspective of a change of positions of member states is clearly relevant in order to shed light upon this first change.

Parallel to the NAP II assessment process, the process of reforming the ETS for the post-2012 phase was initiated. In the course of 2007, four stakeholder consultation meetings were held in connection with this reform process, within the European Climate Change Programme working group on emissions trading on the review of the EU ETS. The issue of cap setting was first and foremost discussed at the third working group meeting, focusing upon 'further harmonisation and increased predictability' (European Commission, 2007). Judging from the official summary of the meeting, the mood among stakeholders, including member state representatives, was in favour of more harmonisation. According to the Chairman, 'there <was> a unanimous call for improved cap setting... <and> a general, very strong message calling for more harmonisation, if not a centralized EU cap' (ibid.: 3).

The report also noted that

<a>Ibeit not against more harmonisation, some Member States consider it important to take into account specific national circumstances, such as level of economic development, impact on economic growth, but also how the energy intensive or export dependent industry would be affected. For these reasons, in their view harmonisation should enable a certain degree of flexibility' (ibid.).

Seen in the light of the frustration and opposition to NAP II cap decisions by the Commission among the new EU member states (as noted in section 2), it is reasonable to assume that this call for continued flexibility was voiced first and foremost by these states. So it seems that this meeting sent a message to the Commission that a *majority* of the member states would not oppose centralized cap setting. Hence, at this point in time, the significant change in position that had taken place among member states came out more explicitly and visibly.

So what had happened? As suggested, a key factor seems simply to be that the ETS had started functioning and this had clarified that the costs of decentralized cap setting were higher than the benefits related to national control. There are several types of these costs. First, particularly NAP I led to free-rider suspicions and equity concerns among member states.⁷ Countries such as the UK, being frontrunners with regard to timeliness and arguably also cap ambitiousness, started to feel that other countries treated their industries more generously. As early as March 2005, *Point Carbon* reported that the UK was seeking more harmonisation and standardisation in NAPs and allocation processes (Point Carbon, 2005b). Furthermore, in May 2006, the UK Environment Minister Ian Pearson stated that 'the results across the EU *do raise questions about the stringency of the caps in some member states*' (Euractiv, 2006; my italics).

Other types of equity concerns appeared in the NAP processes as well. In the NAP II process, the Commission's cut of almost all the suggested caps by new member states, and quite considerably in the cases of the Czech Republic and Poland, led to allegations from

these states about unequal treatment. They found the Commission's approach 'unfair', 'discriminatory' and preventing their industries from catching up with those in western Europe (Point Carbon, 2007; Euractiv, 2007).

Second, the NAP processes have been politically complicated for many countries, as they have experienced significant industry pressure and lobbying. Take for instance the comparatively well-documented case of the UK. In February 2004, the journal *ENDS Report* reported that 'industry sectors are engaged in a frantic round of lobbying in order to maximize their allocations under the EU emissions trading scheme' (ENDS Report, 2004a: 5). In March, the journal noted that 'the Government has come under strong pressure from industry to set less stringent caps' (ENDS Report, 2004b: 47). This was followed up in May by the journal noting that 'the modeling process <i.e. energy projections> – in previous years a dry, academic exercise – has taken on enormous economic and political significance, and *industry sectors have been challenging every detail of the DTI's assumptions*' (ENDS Report, 2004c: 41, my italics). Furthermore, when James Cameron, CEO of 'Climate Change Capital' addressed a UK Parliamentary Committee in late 2004, he stated that 'claims on competitiveness around the UK's allocation plan – led by the CBI – have been very badly managed, ..very misleading, counterproductive and irresponsible, *but they have worked*' (ENDS Report, 2005: 30: my italics).

Similar statements can be found about the situation in Germany. For instance, when Franzjosef Schafhausen from the Federal Environment Ministry commented upon the seemingly moderate ambitiousness of the German NAP I in March 2005, he stated that 'the reason for this was *mainly the lobbying activities of the participating industries during the set-up of the first NAP*. This also led to many special rules and general non-transparency' (Point Carbon, 2005a: 5; my italics). There are good reasons to believe that all the member states experienced such challenges, although probably somewhat differing in strength and form.

Third, in addition to being politically complicated and, related to this, also administratively challenging, the NAP processes were in a more bureaucratic sense also administratively draining, not least for the new member states. A main element here was the general poor quality of existing emissions data. Hence, there was a need for collection of new emissions data (in order to clarify baselines), assessment of these data, and production of forecasts and projections (in order to justify proposed caps). At least in NAP I, the challenge was exacerbated by 'the extremely tight timeframe, which limits the ability of governments to ensure that they have accurate data and also limits the amount of consultation that is possible with the affected industries' (Mullins, 2005: 193). As further pointed out by Mullins, the general situation was one of 'small government teams typically ... struggling to understand all of the issues in the limited time, as well as advise ministers and communicate with industry' (ibid.: 198).

All in all, as summed up nicely by the *Carbon Trust*, 'the process of National Allocation Plans proved to be fraught with such difficulty that most Member States will be glad to see them fade into history. *Negotiating allocations proved to be cumbersome, contentious and time-consuming, with highly unsatisfactory outcomes*' (Carbon Trust, 2008: 21; my italics).

3.2. Did the Commission Independently Change the Cap-setting Model in Order to 'Save the ETS'?

As may be recalled, putting on multilevel governance lenses led to the assumption that the changing of the cap-setting model could be explained by the Commission acting independently, desiring to see its pet policy succeed.

As indicated in the discussion of the previous perspective, the Commission initially preferred a quite centralized ETS, which would naturally have given itself a quite prominent

position.⁸ The outcome was, however, a basically decentralized system, putting the member states firmly in the ETS driver's seat. The 2003 Directive's Article 9 stated that the National Allocation Plans should be considered within the Climate Change Committee. Then, within three months of notification, 'the Commission may reject that plan, or any aspect thereof, on the basis that it is incompatible with the criteria listed in Annex III or with Article 10' (i.e. handing out 95/90 percent of allowances for free) (EU Council, 2003). Hence, this was clearly a 'watchdog mandate', not a 'driver's licence'.

On the one hand, the criteria listed in Annex III and the fact that the NAPs should first be assessed in the member state Climate Change Committee, limited the maneuvering room for the Commission. As pointed out by Peter Vis, a central Commission ETS official, 'the Commission's role was always going to be one of moderate tightening as opposed to wholesale revision' (Vis, 2006: 201). On the other hand, there were numerous criteria; these criteria were inevitably somewhat generally formulated and the subsequent need for interpretation meant that there *was* some maneuvering room. This room was tentatively utilized already in NAP I, as the Commission had managed to shave off 16.4 percent of Poland's initial NAP I suggestion. So the watchdog had been able to bark quite loudly also in the first round.

As described in section 2, the NAP II process was initiated by the December 2005 Commission Communication. Did this Communication clearly point towards the changed model introduced a year later? Not really, although the Communication more generally signalled tougher times to come. As indicated, the Communication stated that the overall cap for the second phase should be 6 per cent lower than in the pilot phase, and allocations to member states that were off-track from their Kyoto target should be further tightened. An interesting thing to note here is the fact that the 6 percent ambition meant the introduction of a common cap for the EU ETS. This was an important milestone in the process of introducing such a cap, which was rejected in the process leading up to the 2003 Directive and more forcefully re-introduced in the Commission's 2008 ETS reform proposal. As noted in section 3.1, there were some clear signals from the member states in the Climate Change Committee regarding criteria to emphasize, for instance the importance of using verified emission figures from 2005 as a significant element. However, as noted, it can hardly be called an instruction. So the more specific design of the three-criteria approach presented in November 2006 was probably a more specific Commission construction. This should also be seen in light of the perspective that key personnel in the Commission's environment directorate (DG ENV), having worked around the clock to get the ETS adopted and up and running, had developed a strong 'personal' interest in seeing the ETS succeed.

With regard to the 2008 proposal, on the background of experiences from both the NAP I and II processes, the Commission probably also had other 'internal' reasons to go for further development and centralization of the cap-setting process. An important aspect was surely the sheer administrative workload related to the decentralized approach. As pointed out by Peter Vis, 'the Commission's job was a difficult one... Several plans were submitted to the Commission without elements that were nevertheless essential for the Commission's assessment... The assessment process of all national allocation plans <in the pilot phase> took 15 months in total, in contrast to the three months foreseen in the Directive' (Vis, 2006: 202, 203). Also, others have pointed out how the decentralized approach led to lacking harmonisation and transparency of NAPs in the pilot phase, including lacking availability of and access to the data upon which allocations had been based (CEPS, 2005). In addition, as indicated, both in NAP I and II the timeliness of countries was not very good, with both old and new member states delayed (Skjærseth & Wettestad, 2008). In NAP I, cases such as Germany, Poland and the UK went through several rounds (Vis, 2006). All this combined to

make the Commission's cap-assessment task quite burdensome under the 'decentralized regime'.

However, in order to more fully understand why Environment Commissioner Stavros Dimas was so disappointed and worried after scrutinizing the first bulk of NAP II's in the fall of 2006, we need to include the global perspective.

3.3. Did Kyoto Protocol Requirements Force the Commission to Change the ETS Cap-Setting Model?

Adopting 'global lenses', we put forward the hypothesis that the changing of the cap-setting model could be explained by developments within the global climate regime under the UNFCCC. In that context, an important event took place in early 2005: Russia decided to ratify the Kyoto Protocol and hence the Protocol entered into force in February 2005, adding formal legal weight to the Protocol's requirements of emissions reductions in the 2008-12 period.⁹

Although the Protocol would probably have had a normative force for the EU even if it had stayed unratified, as the EU became the Protocol's main international supporter from 2001 on, formal entry into force made it even more important for the EU to back up strong rhetoric support with practical results. Getting the ETS launched in January 2005 was a good way to fulfil the Protocol's requirement of showing 'demonstrable progress by 2005' (cf. Article 3, Annex I). The main challenge for matching rhetoric with reality, however, was achieving good internal-emissions reductions performance, so that compliance with the Protocol's 8 percent reduction target could be achieved without 'too much' reliance on the Clean Development Mechanism/Joint Implementation (CDM/JI).¹⁰ A main instrument for doing this was the ETS, described as the 'cornerstone' of EU climate policy by EU officials. Hence, both overall EU climate policy performance and the effective functioning of the ETS took on an added significance after the entry into force of the Kyoto Protocol.

So how had progress been in reducing EU greenhouse gas (GHG) emissions by fall 2006? According to the 2006 progress report from the European Environment Agency (EEA), the picture was not rosy (EEA, 2006). Half of the EU-15 member states projected that their emissions would be higher than allowed under the 1998 EU burden-sharing agreement. The required overall 8 percent cut could only be achieved 'provided that all actions planned by Member States are fully implemented and deliver the emission savings anticipated' (European Commission, 2006a). As noted above, Environment Commissioner Dimas expressed strong concerns about the disappointingly moderate ambitiousness of the second round of NAPs in the fall of 2006. He stated that 'only if national allocation plans are ambitious enough will each Member state be able to achieve its Kyoto obligations' (ibid.). Hence, achieving Kyoto compliance required the cornerstone ETS to do its part, and this arguably pointed towards both a more simple and tougher cap-setting 'tool' and a subsequent tougher practice in 2006. According to the *Carbon Trust*, the Kyoto targets 'proved to be the decisive tool in the battle to establish meaningful, if still modest, allocation cutbacks for European industry' (2007: 17).

In order to understand the further changes proposed by the Commission in 2008, it is important to consider that post-2012 prospects for global climate-change politics may have added further importance to a formalized and further stream-lined centralized cap-setting model. However, as the EU has adopted its main ETS post-2012 architecture *before* the key UNFCCC meeting to take place in Copenhagen in December 2009, global concerns have not lately influenced the EU and the ETS in the same way as in the wake of Kyoto. Rather, the recent dynamic seems to be the other way around. The reform of the ETS has taken place in a general context of EU leadership ambitions on the global stage. So even though global concerns may have mattered for the changed cap-setting model in 2008, such concerns have influenced in a somewhat different manner than before.

4. Conclusion: The Multilevel Drivers for More Centralized Governance

Summing up, the initial ETS cap-setting model was fundamentally decentralized. The member states produced National Allocation Plans (NAPs), which set out the total cap for their domestic emissions and the more specific distribution among the relevant installations. The Commission was given a role as a watchdog of the extent to which NAPs adhered to the 11 steering criteria formulated in the 2003 Directive, and particularly, whether the proposed cap was reasonably ambitious as to prospects for emissions reductions. On this basis, the Commission lowered the suggested caps of a limited number of pilot-phase NAPs rather moderately. The first change of this model took place in the course of the NAP II process in 2006, when NAPs for the 2008-12 period were produced and assessed. In November 2006, cap-setting criteria were boiled down to three key ones, among which assessing the cap in light of verified emissions for 2005 figured centrally. Subsequently, the Commission took on a more active role in NAP II, cutting a number of proposed caps, in some cases significantly. The changing of the cap-setting process was then taken a significant step further in the Commission's January 2008 proposal for the ETS post-2012. It suggested doing away with NAPs completely, setting an EU-wide cap and hence formally centralizing the cap-setting process. This change was then finally adopted in December 2008.

The first hypothesis for shedding light upon this development was that the member states had changed their minds about the superiority of a decentralized cap-setting model and 'ordered' a more centralized approach from the Commission. Overall, this hypothesis received substantial backing, as closer scrutiny revealed that the Commission was given significant encouragement to take tougher action in the Climate Change Committee prior to the changes in 2006. Furthermore, when ETS reform was discussed in 2007, a formalized and further developed centralized approach was given broad support, partly simply because the member states wished to be relieved of the burdens of producing complex NAPs. This meant that our second hypothesis for shedding light on the changing cap-setting model, suggesting that the Commission changed the model independently, was less on target. However, this does not mean that the Commission did not have its own reasons for introducing more centralization, not least the desire to see its flagship project back on track and succeeding.

Our third and final hypothesis, suggesting that the Commission changed the cap-setting model due to pressure from the global climate change regime, clearly provided further clues to understanding this development. Although the EU's compliance with the Kyoto Protocol does in no way depend on the ETS alone, the ETS covers almost half of the EU's CO₂ emissions and is seen as a key policy. Taking the full picture into consideration, the global perspective can probably best be seen as a *conditioning* factor in this context. More specifically, in order to more fully understand the change in mood among member states and the increasing frustration over ETS performance within the Commission, it is simply essential to take Kyoto Protocol requirements into consideration.

In order to understand the process of centralization, with the November 2006 changes as an important milestone and culminating in the 2008 reform proposal, a main finding in this article is that *it is essential to draw upon and combine evidence from all three perspectives and levels included in a multilevel analytical approach*. Hence, what may at first glance seem to be a puzzling Commission 'coup d'etat' (particularly the 2006 change) becomes more understandable when we:

- acknowledge the increasing acceptance of stronger centralized governance among the member states, coming to the forefront in the Climate Change Committee;
- take into consideration frustration in the Commission over complex and differing NAPs; and

- add the fact that the Kyoto Protocol target was getting nearer and a good performance of the ‘flagship’ ETS was becoming increasingly important.

In practice, these developments have interacted in intricate ways.

So what about important implications and prospects ahead? Does the new and significantly changed cap-setting model mean that member states have acceded significant new powers to the Commission? Or do more hidden elements in this development counterbalance this seemingly clear turn towards more centralized governance? Looking closer at the whole 2008 ETS reform, the development is perhaps somewhat more nuanced than it may seem to be at first glance.

On the one hand, compared to the 2003 cap-setting approach, the new design simply eradicates earlier powers and flexibility held by member states. In one sense, the change *is* profound. On the other hand, this is a development and a cap-setting model discussed by member states in stakeholder meetings. Furthermore, the member states have had the opportunity to further discuss and adjust the approach in the 2008 ETS reform decision-making process. So the outcome should have high legitimacy. As this outcome sets the post-2012 cap(s) and CDM limits, the Commission will lose the significant *de facto* powers that it exercised, particularly in the NAP II process.¹¹ In addition, the member states now will have a much more transparent and predictable system. In this sense, they may feel that they will have more control in the future than in the ‘decentralized anarchy’ in the early years of the ETS.

Finally, looking at the ETS reform overall, other elements of the reform may arguably further ‘bring the member states back in’. This is particularly the case regarding the auctioning revenues part. The 2008 reform means significantly more auctioning of allowances, which will result in considerable revenues for the member states. The possibility of revenues amounting to over 60 billion euros by 2020 has been indicated. According to the *Carbon Trust*, ‘after the eight years’ experience of Phase I and II, from 2012 governments will step in and claim the profit for the public purse’ (Carbon Trust, 2008: 24, 25). Hence, this can be seen as a strong ‘sweetener’ and to some extent a counterbalancing factor for the loss of cap-setting powers.

All in all, EU climate policy *has* taken a clear turn towards centralization. If this is a revolution, then it is certainly a broadly welcomed one. Although the case supports the importance of acknowledging the multilevel character of the EU, not least the independent role of the supra-national Commission, it still emphasizes the key role of changing member states’ interests and positions for understanding outcomes.

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Notes

- ¹ Allowances are denominated in metric tonnes of carbon dioxide equivalent. One tonne of carbon dioxide-equivalent is a unit of measurement reflecting the potency of greenhouse gases.
- ² According to the subsidiarity principle, the Community shall take action to the extent to which objectives can be better attained at the Community level than at the level of the individual member states.
- ³ See the statement that ‘If the Community were to agree on the quantity of emissions of the trading sectors in each Member State, possible distorting allocations to individual sectors or companies would be significantly limited’ (European Commission 2000, 18).
- ⁴ These states should aim for a balanced mix between lowered allocation for second phase; implementing additional measures in the non-trading sector; and ‘potentially supplemented’ by government purchase of Kyoto unit credits (European Commission 2005: 6).
- ⁵ By June 2007, except for Slovenia, all the East European EU newcomers had announced intentions to challenge the Commission’s cap cutting in the European Court of Justice. Slovakia has now decided not to do this.
- ⁶ This is further described in Skjærseth & Wettestad (2008): Chapter 4.
- ⁷ This dynamic is further elaborated in Chapter 6 in Skjærseth & Wettestad (2008).
- ⁸ Environmental NGOs and the European Parliament did not play important roles in this process mainly because these actors agreed with the Commission on the supremacy of a centralized model. See Skjærseth & Wettestad (2008).
- ⁹ Russia ratified the Kyoto Protocol in large part due to EU pressure and the interaction with Russia’s membership application to the WTO. I am thankful to an anonymous reviewer for this clarification.
- ¹⁰ This because the EU had expressed strong support for ‘supplementarity’ back in the 1990s, i.e. that the main part of abatement should be achieved ‘at home’ and not ‘abroad’.
- ¹¹ Thanks to Stig Schjølset for making me aware of this aspect of the development.