

THE EU ETS – IMPACT ON DOMESTIC CONSUMERS

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CRITERIA FOR ASSESSING IMPACT ON DOMESTIC CONSUMERS

- how does the EU ETS compare with other measures in terms of effectiveness and impact on consumers?
- should domestic consumers pay energy prices that reflect environmental costs ?
- What about the impact on low income consumers ?

ETS VERSUS TAX

- ETS and a carbon tax both economic instruments
- Design features are the key to effectiveness and cost – trading may offer benefits but not inherently superior
- All revenue from a tax goes to exchequer and taxpayer – some could from an ETS with auctioning
- Trading seems more politically feasible

ETS VERSUS REGULATION

- Alternative could be to ban carbon intensive power generation
- Costs for power producers and consumers if alternatives more expensive
- Precedent – CFCs ?
- Political feasibility ?

FEATURES AND IMPACT OF THE EU ETS

- Lack of auctioning – “windfall” gains
- Number of allowances issued
- Likely impact on domestic consumer prices
- Likely impact on consumer behaviour – will they reduce emissions ?
- Particular impact on low income consumers

LACK OF AUCTIONING

- Ilex modelling shows generators benefit from lack of auctioning
- Loss of revenue for the taxpayer
- Irish government and regulator will claw back revenue – should the UK ?
- Windfall is the result of a political decision on the design of the scheme
- Effects on low income households

NUMBER OF ALLOWANCES ISSUED

- Generous emission allowances will limit effectiveness in reducing emissions
- Other effects may reduce the value of emissions reductions and carbon price – e.g. fall in coal prices
- Price of allowances in February 2005 – 7 euros per tonne – lower than expected

IMPACT ON DOMESTIC CONSUMER PRICES

- Consumers should pay – will they ?
- New entry in retail – entrants cannot predict behaviour of vertically integrated incumbents
- New entrants have to enter retail and generation to compete with incumbents
- Pass through to retail prices likely but amount and timing uncertain

IMPACT ON CONSUMER BEHAVIOUR

- Price increase even with 100% pass through only around 4% on average
- Energy demand price inelastic
- However, other price increases – impact of gas costs, Renewables Obligation, Energy Efficiency Commitment
- Together could provide a signal and marketing opportunity for renewables and energy efficiency

LOW INCOME CONSUMERS

- Average household spends 3% of income on fuel ; but 2 million need to spend at least 10%
- Median price for lowest income decile is 3.29p/kwh; 2.8p/kwh for highest
- Fuel poverty is major political barrier to economic instruments that raise prices
- Auctioning allowances could have generated revenue to tackle fuel poverty

CONCLUSION

- EU ETS is a start but improvements needed – particularly auctioning
- Will enable trading with developing countries
- Need to tackle fuel poverty to remove a barrier to more effective economic instruments for environmental purposes
- Are more effective economic instruments politically achievable ?

CONTACT DETAILS

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