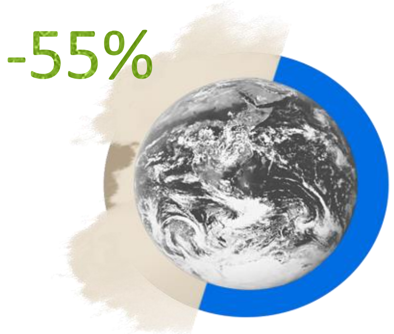
Fit for 55 package
Delivering our 2030 climate target

Revision of the EU Emissions Trading System

12th EU ETS COMPLIANCE CONFERENCE

24 November 2021

Revision of the EU ETS



Content

- The EU ETS in the context of delivering on our 2030 climate target
- Strengthening of the ETS for stationary installations (power, centralised heat, industry)
- Market Stability Reserve (including separate legal amendment proposal)
- Emissions trading for buildings and road transport
- ETS inclusion of maritime transport (and amendments to MRV regulation)
- Aviation related amendments and CORSIA (two separate legal proposals)
- Conclusion

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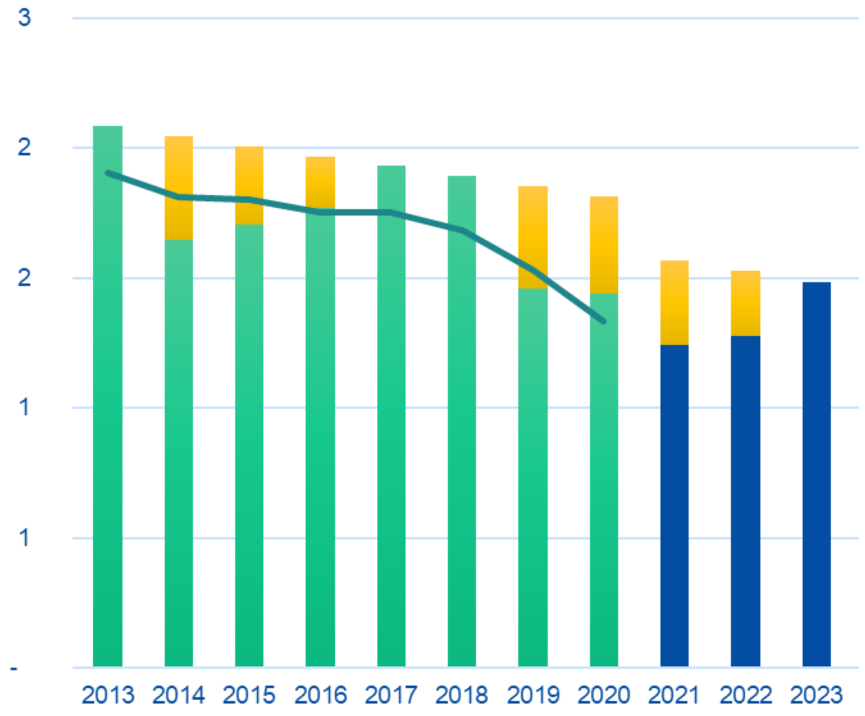
EU ETS is performing well: MSR stabilizes the market

- **Real emissions well below original cap**

- **Backloading and Market Stability Reserve reduce surplus**

- Carbon prices have increased since 2018 and reached levels above €50



2013 - 2020:
Yearly cap reduction: -1,74%

Since 2021: Yearly cap reduction: -2,2%

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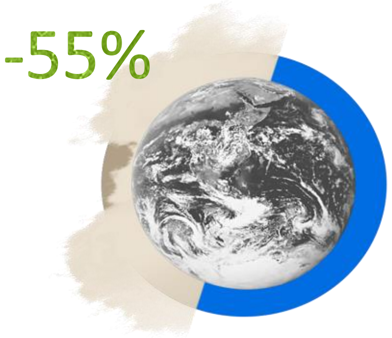

Coherence: EU ETS and the Green Deal

- The European Green Deal will require a transformational change across our economy
- EU-wide carbon pricing is cost-effective, however it **does not address all barriers**
- We need **renewable energy, energy efficiency policies** and **transport** emission standards and fuel policies revised in light of the at least 55% greenhouse gas emissions reduction target
- Important to **maintain national policies** supporting the decarbonisation of buildings and road transport, new sectors remain therefore covered by Effort Sharing Regulation
- Complementarity with the **Energy Taxation Directive**, which focuses on the energy content
- Provisions to **address the risk of carbon leakage** in EU ETS aligned with the proposed Carbon Border Adjustment Mechanism
- Adjustments to EU budgetary framework will be presented as part of the upcoming own resources package

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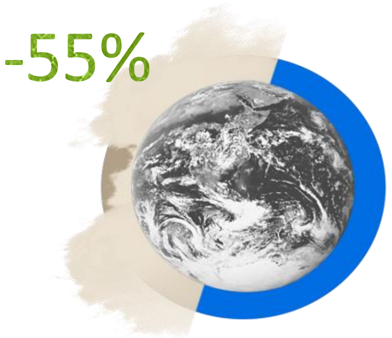

Strengthening the existing ETS: cap

- Need to **update the cap in line with -55%**: increase linear reduction factor (currently 2.2%) combined with an one-off cap reduction

- Cap and linear reduction factor need to take into account ETS extension to maritime

- Cost-effective contribution of ETS sectors to -55%, including extension to maritime, lead to a **new 2030 reduction objective of -61%** compared to 2005 (currently -43% without maritime)

➢ Increased EU ETS **linear reduction factor** from 2024: **4.2%**

- **One-off reduction of the cap** in the year of entry into force to align the cap with emissions (if 2024: 117 Mt), while at the same time cap increase through the maritime transport extension

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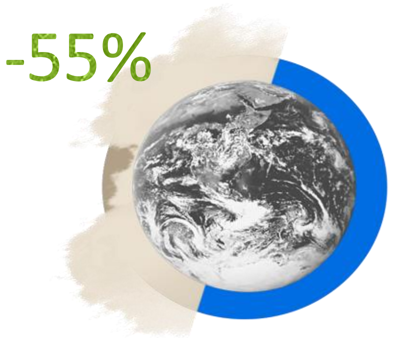

Strengthening the existing ETS: reviewing the Market Stability Reserve

- **Controlling the surplus:** maintaining the intake rate of **24%**
  - **Separate proposal** on this element to maintain a well-functioning and ambitious EU ETS to ensure market predictability
  - Change of intake rate mechanism to **mitigate threshold effects** applicable when the total number of allowances in circulation is close to upper threshold of 833 million but below 1096 million
- **Thresholds** determining the intake and release of allowances remain unchanged
- Including supply and demand from the **aviation and maritime transport** sectors

Fostering market certainty: invalidation of reserve volumes above 400 million allowances instead of above total number of allowances auctioned during previous year

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Strengthening the existing ETS: free allocation

- **Free allocation** continues to be based on benchmarks. No changes to the free allocation (FA) share (43% + 3% buffer)

- **Better targeted FA**: Maximum annual reduction rate of the benchmarks increased to 2.5% (currently 1.6%). Shifts more free allocation to sectors that are harder to decarbonise

- More targeted free allocation and inclusion of maritime sector **limit the risk / size of the** factor reducing free allocation for all sectors. Delays application of CSCF by around 1 year and reduces its value by around 6% as average for the period 2026 – 2030.

- **Scope of benchmarks broadened**: Remove barriers for the deployment of new technologies such as green hydrogen or hydrogen based steel to guarantee a level playing field among technologies.

- **Conditionality to decarbonisation efforts:** 25% reduction of FA for installations not implementing cost-efficient measures identified in energy efficiency audits or equivalent measures

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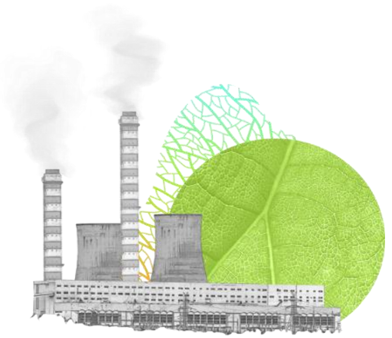
Strengthening the existing ETS: Protection against the risk of carbon leakage



- **Free allocation under the ETS and the proposed Carbon Border Adjustment Mechanism (CBAM) are interlinked**: To ensure compatibility with the EU's international obligations, and maintain incentives to decarbonize, free allocation will be phased out as CBAM is phased in for selected sectors

  - **Free allocation** will be **reduced by 10 percentage points each year** for CBAM sectors, starting at 90% in 2026 and reaching zero in 2035

  - **Industrial CBAM sectors** are iron & steel, cement, fertilisers and aluminium; they represent around 50% of the total free allocation in the period 2021–2025

  - Free allocation no longer provided to **these sectors**, **allowances** must be **auctioned** and the revenues accrue to the Innovation Fund

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Strengthening the existing ETS: accelerating investment in low-carbon innovation & improved auction revenue use

- **Increased Innovation Fund from 450 to 650 million allowances:** 150 of the additional 200 million allowances from the new emissions trading system for road transport and buildings

- Also allowances which would otherwise be allocated for free to industry sectors covered by the Carbon Border Adjustment Mechanism **added to the Innovation Fund** from 2026 to 2030

- **Supporting contracts for difference under the Innovation Fund**: a tool to provide support to the early deployment of innovative technologies and to complement the existing funding mechanisms in the Innovation Fund.

- **Improving the use of auction revenues:** a commitment for Member States to use the entirety of their revenues on climate and energy (including social) purposes

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Emissions trading for buildings and road transport (BRT)

- Direct emissions of buildings and road transport are responsible for 30% of total greenhouse gas and more than half of emissions under the Effort Sharing Regulation (ESR)
- In both sectors **emissions have increased** between 2014 and 2019, buildings by 2% and road transport by 7%
- Sectors under EU ETS are clearly decarbonising faster than sectors outside the ETS and estimations for 2030 including the Member State energy and climate plans confirm this trend (-51% ETS sectors, -31% non-ETS sectors in 2030 compared to 2005)
- **Separate upstream emissions trading system for buildings and road transport**

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Emissions trading for buildings and road transport (BRT): Social Climate Fund

- **Link with an operational new ETS**: commitment agreement may be concluded at the earliest one year before the year of the start of auctions under new ETS
- the Fund will address the social impacts from the new emission trading system for buildings and road transport on **vulnerable groups in the EU**
- in principle **25% of the expected revenues** from the new emissions trading for buildings and road transport used for the Fund
- **Member States** will add at least the same amount of money, mainly from their national revenues from the new emission trading for buildings and road transport, to finance the social climate actions they have identified as necessary.

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Building and road transport emissions trading: a smooth start of the system

- **Cap in initial years** set in-between projected trend under current policy framework and cost-effective emissions
- **Front-loading** of auction volumes to ensure a smooth start with sufficient liquidity (in 2026, 30% higher auction volumes than the total quantity of allowances for 2026)
- **Market Stability Reserve** for the new sectors will be a fully rule-based mechanism adapting the supply of allowances: initial volume of 600 million allowances and **volume-based** thresholds of 210 and 440 million allowances
- Additional **price increase-based** mechanism will be established to **counter** risks of **excessive price fluctuation**

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Call for expression of interest: implementation of ETS for buildings and road transport (BRT)

- Setting up a new separate upstream emissions trading system for buildings and road transport will require significant technical implementation work which needs timely and careful preparation
- In particular appropriate monitoring reporting and verification rules have to be designed, starting from current ETS MRV rules.
- This will benefit greatly from the expertise of MRV experts.
- **If you are interested in the Commission work on preparing the technical implementation of the proposed BRT ETS:**

please express your interest to CLIMA-U11-ARES@ec.europa.eu

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Extending the ETS to maritime transport: Context

- **All sectors need to contribute** to the low-carbon transition and to the Paris Agreement

- Maritime transport plays a **critical role in the EU economy** (75% of EU external trade, 31% of EU internal trade, 400 million passengers) but it only relies on fossil fuel and waterborne prices do not reflect the impact of the sector on climate and the environment

- EU **maritime transport CO_2 emissions** are significant (corresponding to 3-4% of EU emissions) and **expected to increase swiftly** (+34% at EU level by 2050 compared to 2015)

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Extending the ETS to maritime transport: Scope

- **Covering** around 2/3 of emissions related to EU maritime transport
    - all emissions from voyages within the EU (intra-EU)
    - 50% of the emissions from voyages starting or ending outside of the EU (extra-EU)
    - all emissions when ships are at berth in EU ports
- Only covering **large ships** (above 5000 gross tonnage), and maintains flag-neutrality on routes
- Regulating the **same companies** as the ones implementing the **EU MRV** maritime transport regulation (around 1600 entities)

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Extending the ETS to maritime transport Process

- **Same key principle as the other ETS sectors** - shipping companies will have to purchase and surrender ETS emission allowances for each tonne of reported emissions

- Monitoring, Reporting and Verification rules are built on the EU maritime transport MRV system but with a **new role given to administering authorities** (monitoring plans, aggregated emissions at company level)

- Rather than free allocation, a **phase-in period** of allowance surrendering
    - 20% of verified emissions reported for 2023
    - 45% of verified emissions reported for 2024
    - 70% of verified emissions reported for 2025
    - 100% of verified emissions reported for 2026 and after

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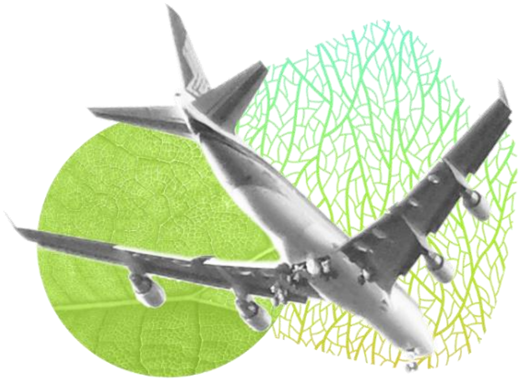

Aviation: report on ICAO CORSIA and costs passed through, required by EP and Council

- The study underlying the ETS aviation Impact Assessment assessed in detail, inter alia
  - The environmental ambition and integrity of CORSIA
  - Enforceability, level of participation, transparency, quality of offsets in CORSIA
  - The airlines’ ability to pass through the carbon costs

- The Impact Assessment contains also the official reports on these issues as required by European Parliament and Council
(Article 28b(2): item 1 and 2; Article 3d(2): item 3)

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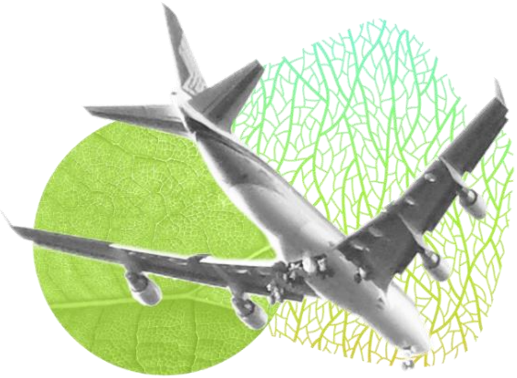
ETS aviation and CORSIA



- Implementation of ICAO's CORSIA through the EU ETS Directive
- **EU ETS for intra-European flights (including to UK and CH): no backsliding/ non-regression, CORSIA for extra-European**
    - ➢ **Maintains EU ETS ambition**, general EU ETS linear reduction factor applies
    - ➢ **Implementing CORSIA for EU-based airlines**, for flights to/from third countries participating in CORSIA
    - ➢ Using units coming from countries participating in CORSIA (condition applied from 2027) and party to the Paris Agreement and **avoid double counting**
    - ➢ Ensuring **level playing field** and maintaining competitiveness of EU airlines: same conditions on same routes

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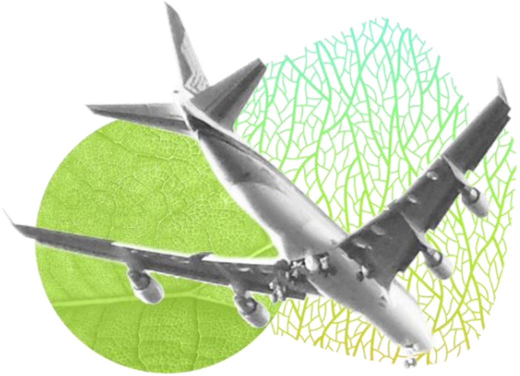
Stand-alone Decision on CORSIA notification



- **Member States should notify** CORSIA offsetting for 2021 emissions to EU-based airlines by 30 November 2022
- **2021 CORSIA offsetting will almost certainly be zero**:
  - Baseline for calculating is 2019 for the CORSIA pilot phase (2021-2023)
  - 2019 was the year of highest ever aviation emissions
  - Traffic decline due to COVID-19
  - The proposal establishes the **legal basis** for Member states to notify the zero offsetting
- The proposal is to be adopted once there is certainty about the level of 2021 emissions (after January 2022)

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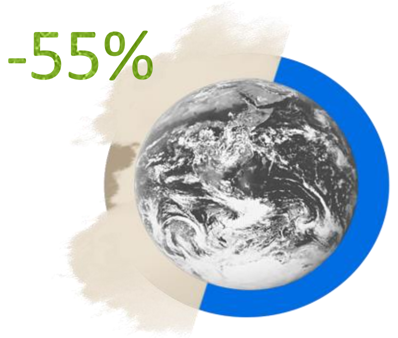

Conclusion

- Emissions trading is a **key instrument** to achieve -55% GHG reductions, in a coherent way
- **Strengthened EU ETS for stationary installations** (power, centralised heat, industry)
- **Appropriate protection of industry against carbon leakage risk** with link to the new Carbon Border Adjustment Mechanism and **increased Innovation Fund**
- **Intra-EU aviation** remains in the EU ETS, with adjusted cap and progressive **phase out of free allocation**
- **Progresive Maritime transport** proposed to be **included in the EU ETS**
- **Market Stability Reserve adjusted** to reflect lessons learned and the -55% target context
- **Emissions trading** proposed for **buildings and road transport**, with cost-effective 2030 cap
- EU is committed to a socially fair transition which leaves no-one behind:
  proposed **top-up** of **Modernisation Fund** and new **Social Climate Fund**

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Thank you

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