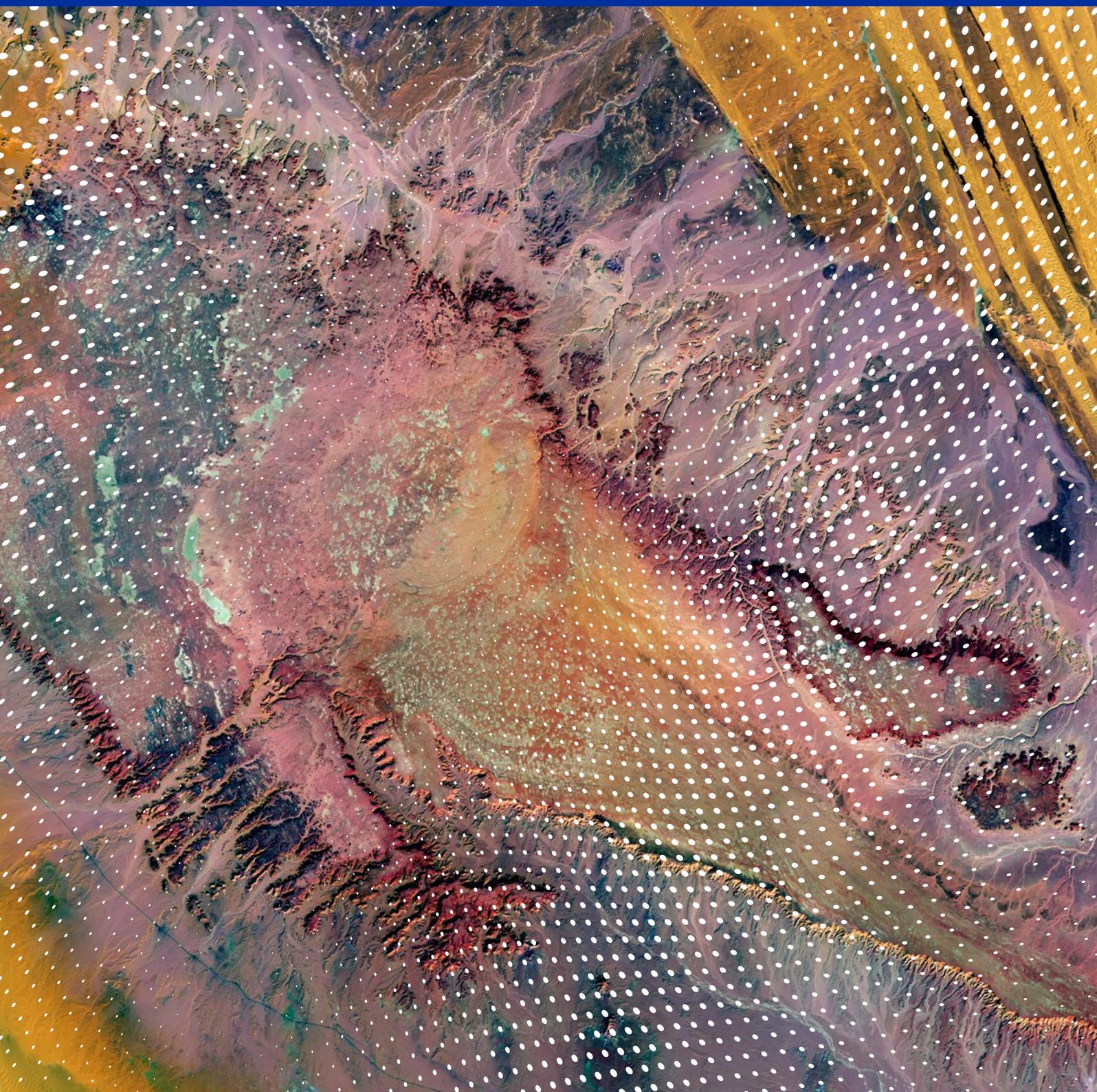


# HOW TO ADVOCATE FOR EFFECTIVE EU CARBON PRICING

LifeETX Guide



# LIFE ETX

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## FURTHER INFORMATION

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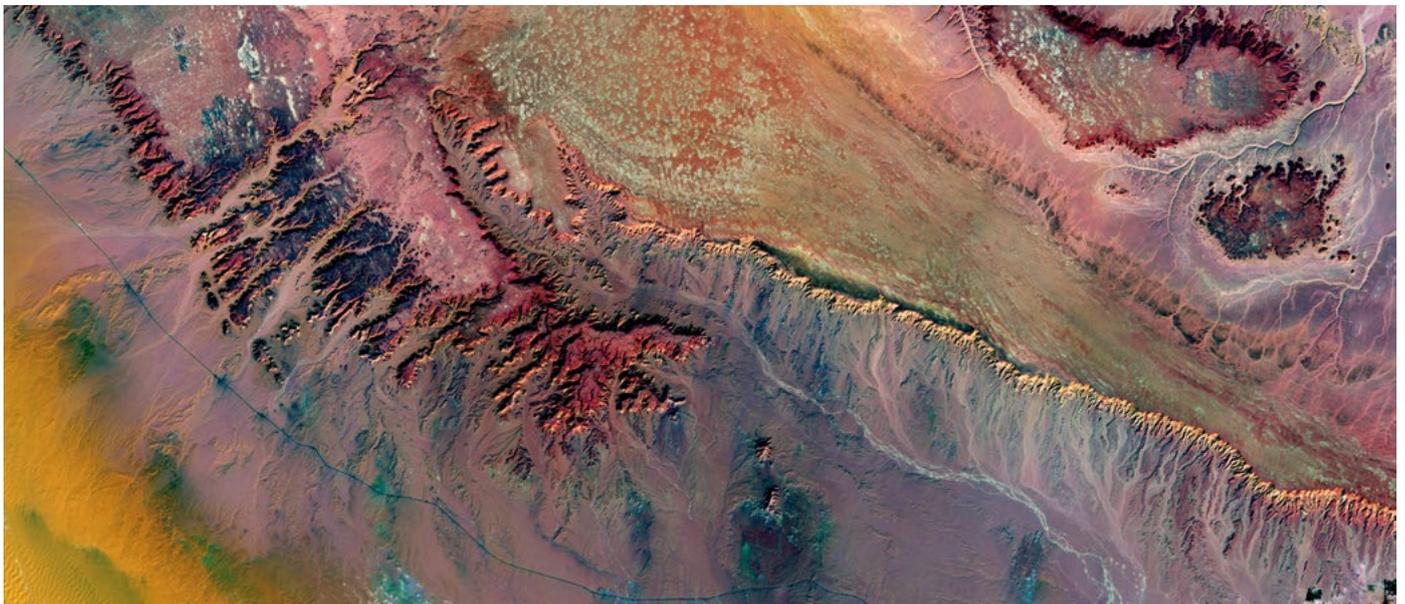
# EXECUTIVE SUMMARY

The Emissions Trading System (ETS) is one of the key EU climate policies and its reform is essential for the successful implementation of the EU Green Deal and the achievement of the Union's 2030 climate targets.

Advocating for a strong revision of the EU ETS is an inherent part of civil society's work to help policymakers improve EU policies and legislation, especially when they affect our present and the future of our planet.

This guide is meant to provide an overview of the key demands for the strong and effective reform of the EU carbon market, as well as to suggest a narrative and messages to successfully communicate these demands to policymakers, the media and the general public.

Finally, the guide also includes some practical tools for advocates, such as a timeline of the political process and an overview of the lead policymakers in the European Commission and the European Parliament in charge of the revision of the ETS Directive.



## To improve the European Commission's proposal for the revision of the EU ETS, the guide includes eleven key recommendations:

- 1** Ensure that the Linear Reduction Factor (LRF) and the one-off reduction of the cap result in a 70% decrease in emissions by 2030 for the EU ETS sectors
- 2** Increase the intake rate of the Market Stability Reserve (MSR) to 36% from 2024 onwards; adopt declining thresholds that reach zero in 2030, and an automatic cancellation of allowances held in the reserve for more than three years to effectively handle the market surplus
- 3** Phase out free allocation of emission allowances to energy-intensive industries
- 4** Strengthen the transparency and fairness of the Innovation Fund and Modernisation Fund
- 5** Include stricter criteria for spending ETS revenues to ensure that member states spending goes to support climate action
- 6** Require shipping companies to pay for 100% of their verified emissions as of 2023, and include all incoming and outgoing voyages under the EU ETS
- 7** Exclude Carbon Capture and Utilisation (CCU) from the EU ETS
- 8** Deleted Article 26 of the ETS Directive to ensure that limits on greenhouse gas emissions can be set in environmental permits under the EU Industrial Emissions Directive
- 9** Add Municipal Solid Waste incineration plants to Annex I of the ETS Directive to regulate this highly polluting sector and provide incentives for waste reduction
- 10** Revise the zero rating of biomass greenhouse gas emissions in order to ensure that it fully reflects the balance of the net effect of the production and use of bioenergy and gets rid of perverse incentives that can increase greenhouse gas emissions
- 11** Implement an ETS for road transport and buildings in parallel with strengthening the regulatory climate framework and without increasing the burden on low-income households



## POLICY CONTEXT

The launch of the European Green Deal and the commitment to achieving a 55% reduction in emissions by 2030, have led to the revision of key climate and energy legislation in the EU.

One of the key EU climate policies is the Emissions Trading System (ETS), and its reform is essential for the successful implementation of the EU Green Deal and the achievement of the 2030 climate target. The EU ETS revision is part of a large legislative package launched in July 2021 containing reforms of existing legislation and new policies.

Regulating around 40% of European emissions, the EU ETS is a crucial piece of the legislative package. An ambitious reform of this directive would yield deep emissions reductions in energy-intensive industries, the power sector and aviation.

The Commission's proposal includes some improvements to the current legislation as well as important new elements, such as the inclusion of maritime emissions and the implementation of a separate carbon market for road transport and buildings.

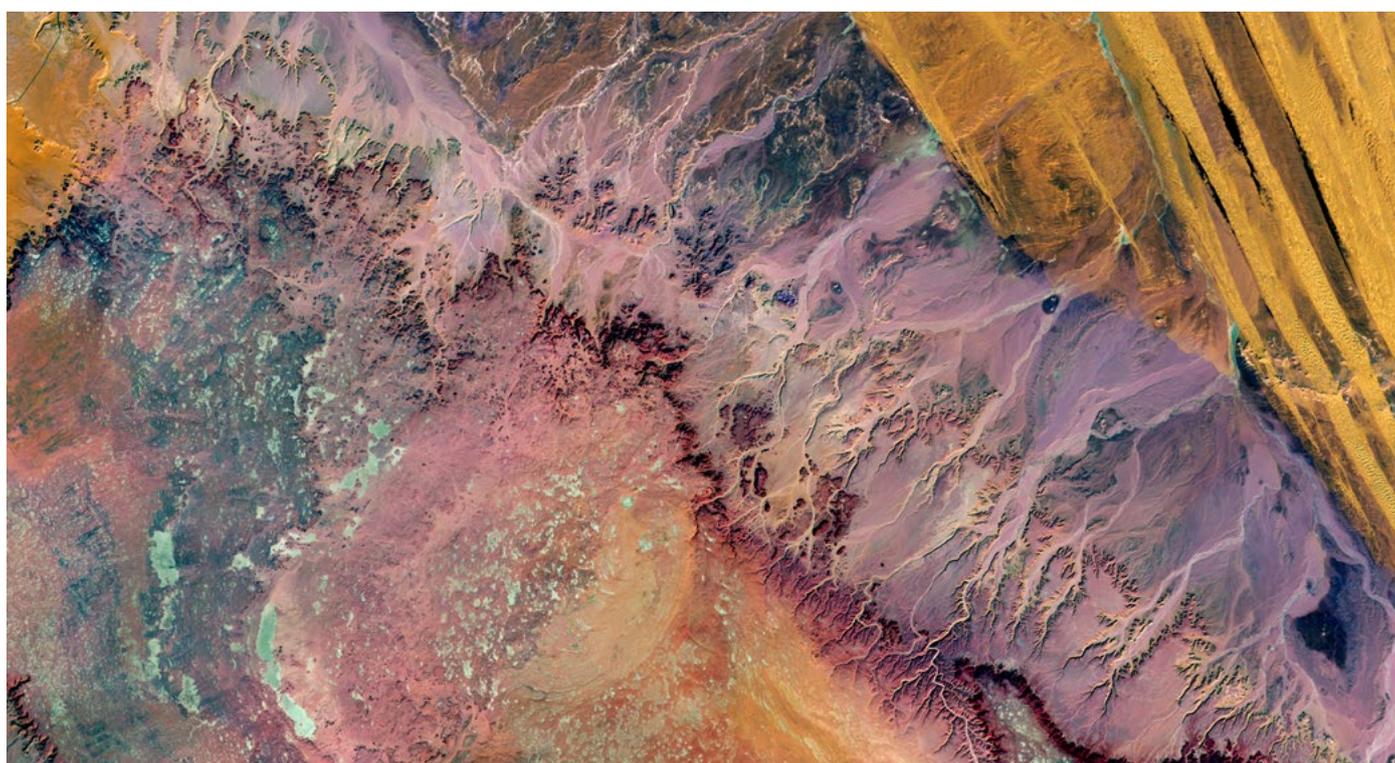
However, this proposal falls short on overall ambition and the proper application of the "polluter pays" principle.

This guide provides suggestions and recommendations to improve the EU ETS proposal.

# KEY RECOMMENDATIONS TO IMPROVE THE EU ETS PROPOSAL

The revision of the EU ETS represents a huge opportunity to strengthen the Directive to ensure it is in line with the 1.5°C target under the Paris Agreement. However, the European Commission's proposal includes two major shortcomings that should be reconsidered. Firstly, the EU-wide 55% emission reduction target proposed is inadequate to achieve the goals of the EU Green Deal and the Paris Agreement, and it should be increased to 65%. Secondly, the proposal neglects to properly implement the polluter pays principle. The free handout of emission allowances to large polluting industries represents a market failure that will lead to continued windfall profits to the sectors concerned.

Here are ten recommendations to improve the European Commission's proposal for the revision of the EU ETS:



## 1- ALIGN THE EU ETS WITH THE PARIS AGREEMENT

The proposal puts forward an increased **Linear Reduction Factor** to the number of allowances per year (4.2 %), combined with a one-off adjustment of the cap so the new linear reduction factor has the same effect as if it applied from 2021. However, the overall climate target to be achieved by the EU ETS by 2030 is 61% below 2005 level, which is not enough to fall in line with the level of emission reductions needed to limit the climate crisis. According to a recent report published by Climact<sup>1</sup>, the Commission's proposal risks falling short of reaching this target as the suggested parameters would only yield a 57-58% reduction in emissions in the ETS sectors.

A -70% target for current ETS sectors (compared to 2005) is needed, given the urgency of the climate crisis. To achieve this target, the one-off reduction of the cap proposed by the Commission should be increased. This would allow closing the gap between the ETS cap and actual emissions in order to better manage the market oversupply and ensure its resilience. Based on the impact assessment accompanying the 2030 climate target plan<sup>2</sup>, and the latest Commission Climate Action progress report published at the end of October 2021<sup>3</sup>, the gap stands at around **450 million allowances. The ETS cap should be reduced by the same number.**

## 2- ADOPT STRONGER PARAMETERS FOR THE MARKET STABILITY RESERVE

The Commission proposal to maintain the Market Stability Reserve (MSR) intake rate at 24% (instead of reducing it to 12%) until 2030 and cancelling allowances held in reserve above 400 million both help strengthen the MSR.

However, the tool is weakened by the inclusion of aviation and maritime emissions that reduce the amount of allowances absorbed by the MSR and its parameters are not strong enough to absorb re-emerging oversupply of emission allowances in the coming years.

The revision of the MSR must support a meaningful price signal and ensure stability and resilience of the EU carbon market, including in case of predictable external shocks such as the phase-out of coal and lignite power plants and post-Covid economy rebound. For example, as the new German government agrees to a faster timeline for phasing out coal and lignite use in the power sector, this will lead to outdated assumptions and an underestimation of the oversupply of allowances compared to the impact assessment as developed by the Commission. A higher intake rate and more dynamically declining thresholds for the MSR should be considered.

### In order to strengthen the MSR, the following key elements should be considered:

**1** The intake rate should be increased to 36% from 2024 onwards. Such a combination of a higher intake rate together with a one-off reduction of the cap can help to accelerate the system's responsiveness to sudden increases in emission supply, as shown by the Oeko-Institut 2021 study on the MSR<sup>4</sup>.

**2** All allowances held in the MSR for more than 3 years should be cancelled. This provision is an improvement building on the Commission proposal and would ensure market predictability as well as the environmental integrity of the EU ETS. It would entail the permanent cancellation of allowances from the system, thus avoiding the risk of future oversupply returning to the market.

**3** The MSR thresholds should decline to zero by 2030. This more dynamic design of thresholds would be better aligned with enhanced climate ambition and the actual hedging needs of the power sector. Since the hedging demand of power companies is likely to fall as the sector continues to decarbonise, the upper and lower thresholds that trigger the MSR intake rate should decrease over time and reach zero by 2030<sup>5</sup>.

### 3- PHASE OUT FREE EMISSION ALLOWANCES

The ETS proposal fails once more to apply the polluters-pay-principle by not putting an end to free emission allowances for resource- and energy-intensive industries during the 4th ETS phase. Evidence from the European Court of Auditors report (2020)<sup>6</sup> has proved that free allocation of allowances tends to slow down the industrial decarbonisation process. Over half of all EU ETS allowances have been given out for free since the ETS was created, with little emission reduction achieved in return.

This means the problem of pollution remains unaddressed and EU industry has often failed to shift to cleaner technologies and production processes. Those industries that have invested in low or zero-carbon techniques are being undermined by a system that continues to reward large polluting installations.

Free emission allowances should be phased out as soon as possible . Polluting for free in times of a climate crisis is unacceptable. Cosmetic changes that the European Commission proposed for “better targeting” of free emission allowances will not drive the necessary emission reduction needed to achieve climate neutrality by 2040.

In particular, the changes suggested to the current benchmark system fall short to implement the polluter pays principle and to phase out free emission allowances in a timely manner:

- Despite setting a higher maximum annual reduction rate of the ETS benchmark (2.5% instead of 1.6%), the proposal keeps the minimum annual reduction rate at 0.2%. This rate applies to some of the most polluting products such as steel, cement and ammonia and is much too slow to incentivise the decarbonisation of these sectors well before 2050. Moreover, as shown in the impact assessment accompanying the ETS proposal (see table below), the potential for emission reductions in ETS sectors is much higher than 0.2% a year<sup>7</sup>. The minimum annual reduction rate of the benchmarks should therefore be set at 1%. As well as this, the specific provision exempting the hot metal benchmark from a fact-based assessment of technological progress in the steel sector and limiting the improvement rate for this specific benchmark to 0.2% should be discontinued<sup>8</sup>.

### ASSUMED ANNUAL AVERAGE IMPROVEMENT IN THE GHG EMISSION EFFICIENCIES PER SECTOR FOR THE MODELLING OF EMISSIONS

SECTOR	ANNUAL AVERAGE GHG EMISSION IMPROVEMENT
Cement	1.0%
Lime	1.0%
Refineries	1.5%
Iron and steel	1.0%
Fertilisers	2.0%
Ceramics	1.0%
Non-ferrous metals	1.5%
Chemicals	1.0%
Pulp and paper	2.0%
Glass	1.0%

Reproduction of table included in EC impact assessment accompanying the EU ETS revision

## The 0.2% minimum reduction rate should be updated to 1% and Article 10a(2)'s last paragraph should be deleted.

- The 25% reduction of free allowances conditional on the compliance with energy audits is a step in the right direction. However, this only adds value if it leads to new and additional investments in energy savings, with the conditionality involving a 100% reduction of free allowances if the installation does not follow energy efficiency requirements. Moreover, the chosen payback time of 5 years is unnecessarily short and, for large energy consuming sectors under the EU ETS Directive, should be extended to 10 years, as sectors with long-living infrastructure require additional incentives to rationalise their energy consumption. The conditionality should also be strictly applied to the fulfilment of the energy efficiency recommendations without providing any opportunity for alternative investments that could lead to the same emission reductions.
- The Commission proposal to amend ETS Directive Art.10a includes a loose reference to the “Union-wide ex-ante benchmarks” to be reviewed before the period from 2026 to 2030 “in view of potentially modifying the definitions and system boundaries of existing product benchmarks”. This provision opens the possibility for a much deeper and structured revision of the ETS benchmarks. However, it remains very vague on the extent to which this revision would take into account the full potential of product substitution and the circular use of materials. In addition, there is no reason to delay this process until 2026, as the Commission clarified in June 2021 that

the review of Article 10a and final levels of free allocation may be subject to change for the allocation period from 2021 to 2025<sup>9</sup>.

## The revision of the ETS benchmarks should start much sooner than 2026 and within 6 months from the entry into force of the ETS Directive.

## In order to account for the full potential of product substitution and the circular use of materials, the definitions and system boundaries of product benchmarks should be revised to take these features into account.

- The European Commission has again missed the opportunity to include a provision in Art. 10b for tiering carbon leakage risk and for better targeting free allowances.
- As shown in the impact assessment<sup>10</sup>, a better targeting of free allowances is possible through a tiered approach that ranks sectors according to their real exposure to carbon leakage risk. This would reduce foregone revenues for member states and create more incentives for industries to invest in decarbonisation. However, this option is only discussed as an alternative to strengthened product benchmarks discussed above. As such, it is argued that the proposed changes to ETS benchmarks would be more impactful

and would lead to the application of the cross-sectoral correction factor earlier than the tiered approach. The best outcome would be in fact yielded by the application of both options discussed in the impact assessment. A much more meaningful and targeted approach would be the application of tiering of free allocation in addition to the proposed revision of the ETS benchmarks. The combination of the two would ensure that free allowances are allocated in full only to sectors at real risk of carbon leakage, and that new processes and technologies are properly accounted for to incentivise cleaner production and deeper emission reductions in line with climate neutrality before 2050.

## The two options for better targeting free allocation presented in the impact assessment (tiering and update of the benchmarks) should be complementary and applied simultaneously

- Additionally, the proposal includes a major departure from the Commission's stated aim announced as part of the EU Green Deal that a Carbon Border Adjustment Mechanism (CBAM) would be implemented as "alternative to the measures that address the risk of carbon leakage [i.e. free allowances] in the EU's Emissions Trading System"<sup>11</sup> Yet the Commission's CBAM proposal would maintain free allocation to sectors covered by CBAM until 2035. This is extremely counterproductive as the current ETS Directive contains no provisions extending free allocation beyond 2030.

**The revised ETS Directive should exclude any provision allowing the overlap between free allocation of emission allowances and CBAM. Moreover, for sectors not covered by CBAM, free allocation should be phased out as soon as possible**

## 4- STRENGTHEN THE CAPACITY AND FAIRNESS OF THE INNOVATION FUND AND MODERNISATION FUND

### Innovation Fund

Increases in the volume and scope of the ETS Innovation Fund (IF) are positive and greatly needed to incentivise industrial decarbonisation.

Currently, the Innovation Fund allocates the derivatives of auctioning 450 million ETS allowances. At an ETS price of 25 EUR/t, for the first call for projects, the fund could disburse a billion euros. However, the demand and variety of low-carbon projects that applied was more than 20 times what the fund made available in the call.

In the first call of the Innovation Fund, only one project on steel received funding. According to data released by the European Commission<sup>12</sup>, 48 projects out of the 70 selected in the first stage of the call met all the requirements but were beyond the available budget threshold. At least three of these projects were in the steel sector.

The increased flow of allowances resulting from the reduction of free allowances for sectors covered by CBAM into the Innovation Fund is particularly welcome.

However, if free allowances were phased out, more funding could be directed towards the Innovation Fund and contribute more substantially to zero-carbon projects in energy-intensive industries.

### Modernisation fund

The proposal very positively removes any support for energy generation facilities that use fossil fuels. Moreover, it expands the Modernisation Fund (MF)'s scope and resources, increasing the share of allowances that will be directed towards the Fund to 4.5% and the GDP per capita threshold thereby including Greece and Portugal among the countries that can receive funding through the MF. We consider this augmentation of the MF with new eligibility criteria referring to a more recent base year (average of 2016-2018) as more appropriate for the 4th ETS phase than merely applying the current criteria referring back to 2013.

It is crucial for these changes to be kept in the final Directive and also extend the exclusion of all investments in nuclear energy.

With regards to the selection of projects to be funded under the MF, the ETS Directive should ensure more transparency and accountability, as well as stricter criteria. Although the increase from 70% to 80% in the share of the MF, which funds projects in priority areas, is a step in the positive direction, we recommend that this share is increased to 100%.

Moreover, projects in the Just Transition priority area of the MF should be fully aligned with the Territorial Just Transition Plans, and only projects which are compliant with Articles 8 and 9 of the Just Transition Fund Regulation ((EU)1056/2021)<sup>13</sup> should be eligible for funding

from the MF. These provisions would ensure the firm exclusion of investments in any type of fossil fuels and full consistency across EU climate and energy legislation. It will also oblige governments to be coherent in their planning in the regions in transition and avoid having multiple disjointed plans that risk being incoherent and therefore inefficient.

## 5- INCLUDE STRICTER CRITERIA FOR THE USE OF ETS REVENUES

The proposal very positively mandates the full use of revenues for climate related purposes, which is an improvement compared to the current ETS.

The new requirement included in the proposal needs to be maintained. Indeed a recent report by WWF showed that several member states failed to channel the ETS revenues to climate action<sup>14</sup>.

However, the proposal fails to define the list of criteria and activities on which ETS revenues should be spent. While EU member states should be free to decide on what to spend ETS revenues, stricter criteria should be put in place to avoid the misuse of funding and resources financing unsustainable technologies and practices that are not in line with the goal of reaching climate neutrality by 2050.

**The list of criteria and activities on which the revenues should be spent must be refined and mandated to ensure that member states spending goes to support climate action. As suggested in WWF's report on the**

**use of ETS revenues<sup>15</sup>, projects funded through ETS revenues should contribute substantially to at least one of the six environmental objectives and be compliant with the ‘do no significant harm’ principle. They should also be consistent with National Energy and Climate Plans and the Just Transition Fund Regulation, and comply with minimum social safeguards.**

## **6- COVER ALL INCOMING AND OUTGOING VOYAGES AND APPLY FULL AUCTIONING IN THE SHIPPING SECTOR FROM THE START**

The proposal for shipping includes several good elements, including no free allocation, using the most recent data to set the baseline for expanding the cap and explicitly making shipping companies eligible for Innovation Fund finance.

However, there are still a few glaring issues which need to be addressed. The slow phasing in of full compliance requirements ignores the urgency of tackling emissions from the shipping sector. There is no need whatsoever for a slow phase-in as carbon leakage risks are close to non-existent and the shipping industry has already had a sufficiently long

phase-in due to the Monitoring, Reporting and Verification (MRV) system of carbon emissions for shipping regulation. The industry already conducts the MRV necessary, and knows perfectly well what they emit.

Second, the current geographic scope includes intra-EU voyages, ships at berth and 50% of incoming and outbound voyages (to and from EU ports). This should be expanded to cover all international shipping emissions. There are no stringent climate measures in place globally for this industry, and full-scope EU ETS inclusion would ensure more pollution from EU economies is priced. The coverage of voyages to third countries implementing similarly stringent climate policies could be revisited to ensure each country prices 50% of those trips. This would also be seen as a basis for international cooperation and incentivise third countries to price pollution from the shipping industry.

Establishing an Ocean Fund that finances climate action in the sector itself, including research and development related to real zero emission propulsion technologies and fuels, would be an important addition to the Commission proposal. All the revenues of auctioning pollution permits to the shipping sector would fund the Ocean Fund.

**Shipping companies should be required to surrender allowances equal to 100% of their verified emissions as of 2023, and all incoming and outgoing voyages should be fully covered.**

## **7- EXCLUDE CARBON CAPTURE AND UTILISATION (CCU) FROM ETS**

The addition of CCU to the EU ETS Directive (Articles 3 point (b) and Article 12(3b)) is highly problematic.

Under this proposal, companies would not be required to buy allowances to cover their CO<sub>2</sub> emissions, if the carbon captured and used in an industrial process is 'permanently chemically bound in a product' and does 'not enter the atmosphere under normal use'. The theory behind this is that industrial carbon would be captured by companies, and used to create other products (such as fuels, building materials or plastics). This carbon would then be automatically considered permanently stored if it was not released during use.

This ambiguous language is very problematic and could create damaging loopholes in the ETS legislation.

Products that release carbon after their normal use (for example while decomposing or in incinerators) should not be considered carbon storage: CO<sub>2</sub> can only be deemed permanently stored if it is never released into the atmosphere again.

Moreover, the capture of carbon and the process to turn it into a product could be highly emitting activities, such as when the carbon comes from fossil fuels and the electricity used is fossil fuel-based. Emissions throughout the value chain of the CCU product need to be calculated so that only products that truly decrease overall carbon emissions are incentivised. Otherwise, the EU would be promoting increased emissions instead of reducing them.

In addition, the inclusion of CCU could lead to EU ETS emissions being shifted to the ESR sectors increasing the burden on Member States to reach those targets.

## **The inclusion of CCU in the EU ETS should be excluded from the Commission's proposal**

If EU policymakers are keen to support carbon capture and utilisation, they should ensure that the product is a net permanent store of carbon over its entire lifetime. All emissions during production, use and recycling/disposal need to be counted and properly accounted for. Failing to do so would just create another

## **8- DELETE ARTICLE 26 OF THE ETS DIRECTIVE**

The Commission's proposal fails to recognise the potential for integrating the EU ETS and the Industrial Emissions Directive. Not amending Art. 26 to make the EU ETS and the Industrial Emissions Directive complementary and include GHG emissions within the scope of the IED was a big missed opportunity to set binding emission limits and energy efficiency standards in industrial permits.

While recognising that the decarbonisation of industry and power generation would also lead to reduced emissions of air pollutants and positive effects on air quality, and that the ETS and the IED have the potential to reinforce one another to reduce emissions, the proposal fails to better integrate these two crucial pieces of legislation.

The limitations imposed by Art.26 are counter-productive and incompatible with the European Green Deal and the integrated approach of the IED to prevent pollution at source. They also provide little incentive to industries to invest in more environmentally-friendly processes and move towards climate neutrality. In light of the urgent need to tackle the climate crisis, this oversight and shortcoming needs to be corrected.

**Article 26 should be deleted to ensure that limits on greenhouse gas emissions can be set in environmental permits under the EU industrial emissions directive.**

## **9- INCLUDE WASTE INCINERATION IN THE EU ETS**

The Commission's proposal fails to recognise the impact of waste incineration on the climate. Not including waste incineration under the EU ETS is another missed opportunity to better regulate this highly polluting sector and provide incentives for waste reduction.

As shown by a recent report from CE Delft<sup>16</sup>, including waste incineration in the EU ETS would benefit the climate and the environment by reducing waste and encouraging recycling. The study estimates a reduction of CO<sub>2</sub> emissions by 2.8 to 5.4 Mt per year in 2022 and 4.3 to 8.8 Mt per year in 2030, with the greater impact, as well as environmental benefits, coming from commercial and industrial waste.

## **Municipal Solid Waste incineration plants should be added to Annex I of the ETS Directive**

### **10- REVISE BIOMASS ACCOUNTING**

The proposed changes to the rating of biomass in the ETS proposal are not strong enough to ensure proper accounting and support only for the use of sustainable biomass. The zero rating of biomass greenhouse gas emissions should be revised in order to ensure that it fully reflects the balance of the net effect of the production and use of bioenergy and gets rid of perverse incentives that can increase greenhouse gas emissions.

To this end, the ETS review should include a link with proper life cycle accounting for biomass that accounts for the real effects on CO<sub>2</sub> levels in the atmosphere. Biomass should not be considered zero-rated and it should be brought in line with strict sustainability criteria.

As proposed by the European Academies Science Advisory Council<sup>17</sup>, this could require calculating the 'carbon payback period' for each biomass facility and its supply chain. Regulators need to know how long it takes for the initial negative effects of burning biomass on climate to be overcome and net reductions in atmospheric CO<sub>2</sub> concentrations achieved. Once this is established, the relative proportion of biomass emissions should be reported in the ETS and allowances should be surrendered for compliance by installations using biomass.

## **11- THE NEW ETS FOR THE TRANSPORT AND BUILDINGS SECTORS SHOULD NOT WEAKEN COMPLEMENTARY POLICIES AND MEASURES FOR ACHIEVING GREENHOUSE GAS EMISSION REDUCTIONS IN THOSE SECTORS. REVENUES GENERATED FROM PRICING CARBON POLLUTION FROM TRANSPORT AND BUILDINGS SHOULD SUPPORT INVESTMENTS TOWARDS CLEANER, MORE EFFICIENT ALTERNATIVES, ESPECIALLY FOR LOWER INCOME HOUSEHOLDS.**

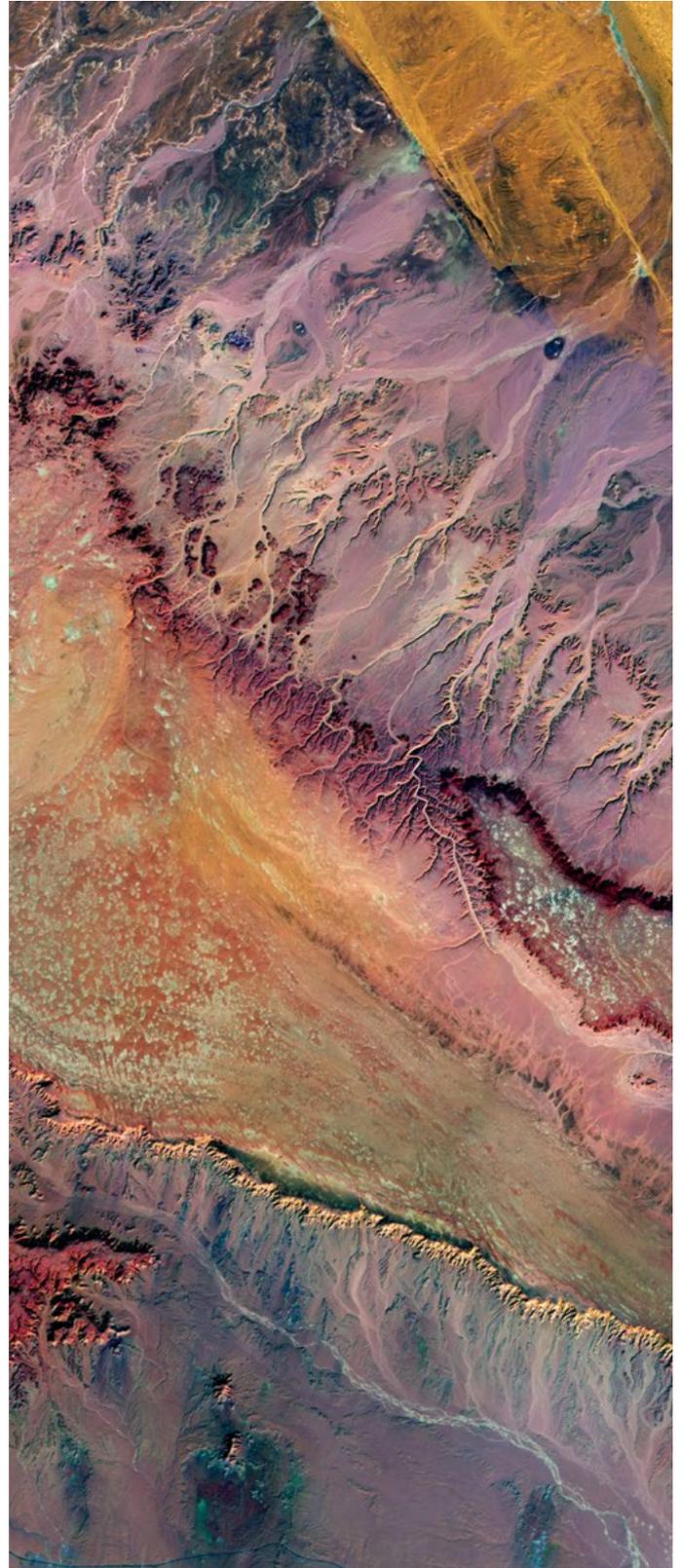
Introducing carbon pricing only makes sense if it goes hand in hand with increasing ambition in EU sectoral regulations<sup>18</sup> and improving compliance from Member States on Effort Sharing Regulation. To reduce demand for fossil fuels, carbon pricing is needed on top of more stringent regulatory measures. Member States must remain active contributors to the EU's climate ambition. Ambitious and binding national climate targets keep the incentive high to eliminate non-market barriers at national level.

As the negotiation for the new ETS runs in parallel with the main ETS, a fair distribution of efforts respecting the polluters pays principle should be ensured. To this end, industrial polluters in ETS should stop receiving free emission permits.

While the consumption of fossil fuels should become more expensive, we are looking for a gradual price increase (through CO<sub>2</sub> pricing) and not for sudden price hikes that come with considerable social impacts.

Revenues generated from carbon pricing schemes need to support investments

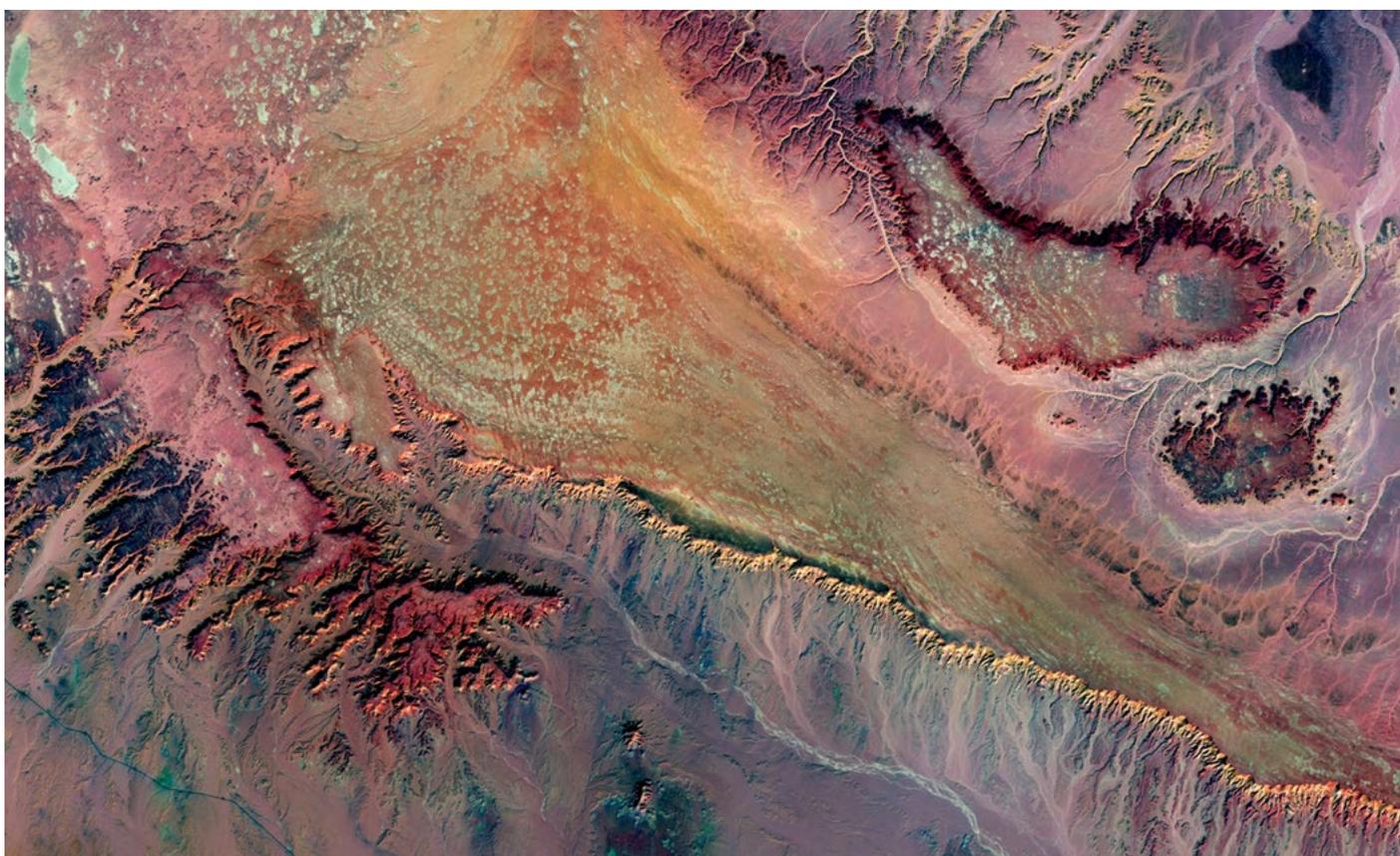
towards cleaner, more efficient alternatives, especially for lower income households who risk being unduly hit by higher energy prices without having the option to invest in cleaner alternatives.



# NARRATIVE AND MESSAGES

Communication activities are an inherent part of political advocacy. Non-governmental organisations and representatives of civil society have a crucial role to play in influencing political decisions that will affect their everyday lives.

When it comes to a technical piece of legislation such as the EU Emissions Trading System, powerful and clear messages facilitate the understanding of its key issues and ensure that civil society stakeholders have a say in shaping the public debate and putting pressure on policymakers for change that benefits society as a whole. In the context of this particular directive, communication is also a tool to create space in a policymaking debate which is heavily occupied by the incumbent industry lobby.



The relevance and the role of the EU carbon market needs to be highlighted in the context of the climate crisis. To this end, a communication campaign needs to tell the story along three lines: urgency, risks and opportunities, and fairness.

**Urgency:** The sectors regulated by the EU ETS are responsible for almost half of Europe's carbon emissions. Cleaning up industry is a make or break for our climate objectives, we can't afford another decade of low or no pollution reduction. Given the long life cycles of industrial investments, 2030 and 2050 are just round the corner. In the little time we have left to avoid the worst consequences of the climate crisis, we need to focus on concrete solutions and results. The atmosphere cannot be cheated.

**Risk and opportunity:** Continuing on a business as usual path that does not include a transformative reform of the EU ETS will very likely lead to stranded assets. At the same time, current rules are stifling innovators and keeping them out of the market since they reward the worst performers instead of the best ones. The ETS revision represents an invaluable opportunity to change this and provide an avenue for clean innovators to lead, ensure long-term competitiveness and clean jobs.

**Fairness:** Citizens are asked to make sacrifices while heavy industry pollutes for free. Everyone, citizens and industry alike, should play their part in tackling climate change.

Once the issue has been put into context, the communication efforts can be put on very clearly outlining the top three demands for the revision of the EU ETS:



**1 MAKE POLLUTERS PAY**



**2 SPEED UP EMISSION REDUCTIONS**



**3 DON'T ALLOW ANOTHER PRICE CRASH**

**These three demands together are the main ingredients for a successful and effective revision of the EU ETS.**

## MAKE POLLUTERS PAY

This demand needs to be supported by clear and powerful arguments since it is the main element of the ETS revision against which the EU energy-intensive industry focuses all its efforts.

It is crucial to explain that the reason for the current partial exemption of companies from paying the carbon price stems from a risk that so far has not empirically occurred. There has been no evidence of carbon leakage until now<sup>19</sup> and studies show that the risk is likely to materialise in the future only at very high levels of carbon price.

In fact, corporations have been profiting hugely from the EU ETS since its inception. It is estimated that between 2008 and 2018, industries covered by the EU ETS have made up to 50 billion euros in windfall profits from a system that is supposed to make them pay for their emissions.

Due to its flaws, the EU ETS provides virtually zero incentives for industries to decarbonise. This is witnessed by the fact that industrial pollution has not gone down in the last decade and it's not expected to do so over the next one either.

The main argument in favour of keeping free pollution permits to industries is the need to avoid carbon leakage and the consequent relocation of EU companies in other countries with less stringent climate legislation, which would likely lead to an overall increase in global emissions as well as losses of jobs and wealth in Europe. However, the Paris Agreement, ratified in 2015, has spurred climate action in most countries around the world, making the threat of EU companies relocating to other geographies less and less likely.

Moreover, the introduction of a carbon border adjustment mechanism (CBAM) in the EU would address the risk of carbon leakage thus making the need for free pollution permits redundant.

## SPEED UP EMISSION REDUCTIONS

The ETS revision needs to deliver much faster emissions reductions if Europe is to fulfil its commitments under the Paris Agreement. At the current rate, the power and industry sectors will stop polluting in 2058.

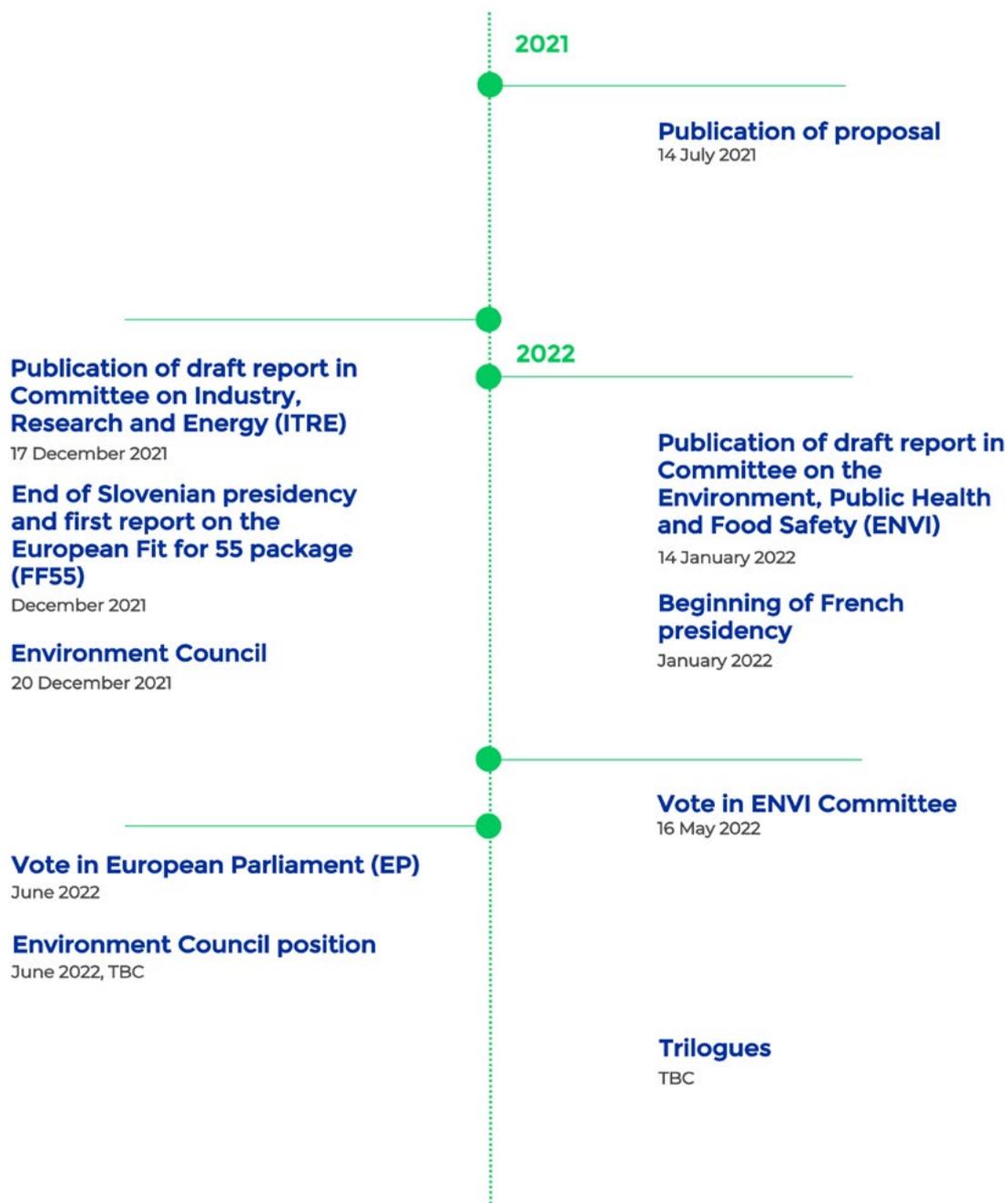
If the EU wants to be a global climate leader and carry its responsibility, it will have to bring its industrial pollution to zero by 2040. This is the only goal in line with the objective of keeping the rise in global temperature to 1.5 degrees.

As highlighted by CAN Europe's paper<sup>20</sup>, such an ambition level would be in line with the recent UNEP Emissions Gap Report underlining that a trajectory consistent with the Paris 1.5°C goal requires emissions to annually decrease by 7.6% between now and 2030. Both the net zero and 65% target need to be translated into further targets for tackling emissions under the Emissions Trading System (ETS).

## DO NOT ALLOW ANOTHER PRICE CRASH

A crucial element of the EU ETS is the Market Stability Reserve (MSR). The MSR has helped drive up the carbon price by absorbing historic surplus of allowances from the market but it is not fit to deal with the future surplus generated by the faster decarbonisation of the power sector or economic rebound after the covid pandemic. This tool should be strengthened to ensure stability in the market and avoid the risk of a price crash.

# LEGISLATIVE TIMELINE



# WHO'S WHO? KEY POLICYMAKERS

## EUROPEAN COMMISSION

The EU Emissions Trading System is a climate policy tool and it is therefore the responsibility of the Directorate-General for Climate Action (DG CLIMA) in the European Commission to oversee the implementation of this Directive and draft proposals for legislative changes.

DG CLIMA leads the European Commission's efforts to fight climate change at EU and international level. Its key mission is to formulate and implement EU climate policies and strategies, so that the EU can become the first climate-neutral and climate-resilient continent by 2050.

The Commission Executive Vice-President in charge of the European Green Deal is Frans Timmermans. Timmermans is a Commissioner and his cabinet, led by Diederik Samsom, is in charge of the political work and implementation of the European Green Deal and all the legislative actions under it.

The Director-General of Climate Action is Mauro Petriccione, the head of DG Clima. He sets the direction and oversees the work of the DG, following the political guidelines set by the Commissioner.

Within the DG, the unit in charge of the development and implementation of the EU ETS is Unit B, which is currently led by Beatriz Yordi. She oversees the unit's work on the ETS Directive and coordinates the different departments<sup>21</sup>.

## THE ENVIRONMENT COUNCIL (MEMBER STATES)

The EU Emissions Trading System is a Directive that falls within the remit of the EU Environment Ministries. It is thus discussed and agreed in the Environment Council.

As other pieces of environmental legislation, an agreement on the ETS reform requires a qualified majority in the Environment Council to be adopted.

It is therefore very important to understand EU 27 member states' positions on the different elements of the ETS Directive and reach out to the relevant ministries at key moments during the legislative process with compelling arguments to support your demands.

Environment Ministers in each member state will be the main target audience for the advocacy efforts. However, it is important to liaise with the permanent representations in Brussels and keep track of the Council meetings that take place there.

## EUROPEAN PARLIAMENT

The Committee responsible for the revision of the EU Emissions Trading System in the European Parliament is the Environment, Public Health and Food Safety (ENVI) Committee.

In this Committee, the Rapporteur of the file is MEP Peter Liese. He is in charge of drafting the Committee's report on the European Commission's proposal as well as consolidating the final version of the EP position on the Directive that will be voted in the plenary session by simple majority and will become the official position of the Parliament before triilogue starts.

The main parliamentary groups nominate a Shadow Rapporteur in charge of supporting the lead Rapporteur in the drafting of the report on the EU ETS in the ENVI Committee.

The shadow rapporteurs of the EU ETS in the ENVI Committee are:

- Jytte Guteland for Social Democrats
- Emma Wiesner for Renew Europe
- Michael Bloss for the Greens/EFA
- Silvia Modig for The Left (GUE/NGL)
- Danilo Oscar Lancini for Identity and Democracy (ID)
- Alexandr Vondra for ECR

For the revision of the EU ETS, the ENVI Committee receives input on relevant and specific issues from other parliamentary committees, namely the Industry, Research and Energy Committee (ITRE), the Budgets Committee (BUDG) and the Transport and Tourism Committee (TRAN).

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EU Commission	@EU_Commission
European Parliament	@Europarl_EU
DG CLIMA	@EUClimateAction
Useful hashtags	#EUETS #Fitfor55 #carbonmarkets #climateaction #OCTT #ClimateNeutralEU #climateneutrality #LifeETX #EnergyTransition #EUGreenDeal

# NOTES

1. Climact: <https://climact.com/en/is-the-eu-ets-proposal-fit-for-55/>
2. The gap between the cap and the actual emissions was estimated for 2019 equivalent to around 250 million allowances in 2019: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020SC0176>
3. In May 2021, the 2020 surplus was around 200 million allowances higher than in 2019: [https://ec.europa.eu/clima/system/files/2021-11/policy\\_strategies\\_progress\\_com\\_2021\\_960\\_en.pdf](https://ec.europa.eu/clima/system/files/2021-11/policy_strategies_progress_com_2021_960_en.pdf)
4. <https://www.wwf.de/fileadmin/fm-wwf/Publikationen-PDF/Klima/WWF-Studie-Emissionshandel-englisch-alt.pdf>
5. [https://wwfeu.awsassets.panda.org/downloads/making\\_the\\_eu\\_emissions\\_trading\\_system\\_fit\\_for\\_55\\_april\\_2021\\_.pdf](https://wwfeu.awsassets.panda.org/downloads/making_the_eu_emissions_trading_system_fit_for_55_april_2021_.pdf)
6. <https://www.eca.europa.eu/en/Pages/DocItem.aspx?did=54392>
7. [https://ec.europa.eu/info/sites/default/files/revision-eu-ets\\_with-annex\\_en\\_0.pdf](https://ec.europa.eu/info/sites/default/files/revision-eu-ets_with-annex_en_0.pdf) (page 87, Annex IV)
8. Specifically the provision in ETS Directive Art 10a(2) last paragraph: “the benchmark value for hot metal [...] shall be updated with an annual reduction rate of 0,2 %”
9. [https://ec.europa.eu/clima/news-your-voice/news/commission-publishes-national-allocation-tables-member-states-eu-ets\\_en](https://ec.europa.eu/clima/news-your-voice/news/commission-publishes-national-allocation-tables-member-states-eu-ets_en)
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14. [https://wwfeu.awsassets.panda.org/downloads/making\\_eu\\_ets\\_revenues\\_work\\_for\\_people\\_and\\_climate\\_summary\\_report\\_june\\_2021\\_2\\_.pdf](https://wwfeu.awsassets.panda.org/downloads/making_eu_ets_revenues_work_for_people_and_climate_summary_report_june_2021_2_.pdf)
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20. S. Verde, Journal of Economic Surveys (2020) “The impact of the EU Emissions Trading System on competitiveness and carbon leakage: the econometric evidence”
21. Dechezleprêtre A, Gennaioli C, Martin R, Muûls M and Stoerk T (2021) Searching for carbon leaks in multinational companies. Centre for Climate Change Economics and Policy Working Paper No. 187 8 Eugénie Joltreau & Katrin Sommerfeld (2019) Why does emissions trading under the EU Emissions Trading System (ETS) not affect firms’ competitiveness? Empirical findings from the literature, Climate Policy, 19:4, 453-471, DOI: 10.1080/14693062.2018.1502145
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