

# Consultation on revision of the EU Emission Trading System (EU ETS) Directive

## 1. Free allocation and addressing the risk of carbon leakage

**1.1 The European Council called for a periodic revision of benchmarks in line with technological progress. How could this be best achieved in your view and, in particular, which data could be used to this end? How frequently should benchmarks be updated, keeping in mind administrative feasibility?**

First of all we would like to highlight the importance of benchmarks as a means to allocate scarce resources in an efficient, transparent and non-distortive manner.

Ideally, one would have a revision of benchmarks every time a significant change in technologies or a technological break-through occurs, in order to align allocations to actual emission levels.

Since it would be very difficult to respond immediately to any of such events it could be argued that a revision of benchmarks before the beginning of each trading period, could be a good way to capture major technological improvements without de-stabilizing the market or create excessive administrative burden.

If the trading period is longer than 5 five years, a mid-term review in order to evaluate for possible adjustment in response to major events could be envisaged. The outcome of the mid-term review could follow the Comitology procedure, in order to allow the full involvement of all Member States.

Data feeding into the revision of benchmarks at the beginning of each trading period and any subsequent revision, should be collected ad hoc from Member States and the Commission, in a collective and transparent exercise that involves all relevant stakeholders and institutions.

The data regarding the most efficient installations for each sector should continue to be the main reference regarding the calculation of benchmarks. Additional indicators or data should be carefully evaluated by the competent committees before being adopted. In any case, benchmarks should create a level playing field between firms operating in the same industry independently of where they are located within the EU.

**1.2 The European Council has defined guiding principles for the development of post-2020 free allocation rules which provide inter alia that "both direct and indirect costs will be taken into account, in line with the EU state aid rules" and that "the most efficient installations in these sectors should not face undue carbon costs leading to carbon leakage" while "incentives for industry to innovate will be fully preserved and administrative complexity will not be increased" and while "ensuring affordable energy prices". Do you have views how these principles should be reflected in the future free allocation rules?**

A process that is fact-based, rational and harmonized at EU level should guide the definition of rules for carbon leakage in the 4th and possibly subsequent trading periods.

“The free allocation of allowances is the best way to preserve the competitiveness of firms exposed to direct carbon leakage, until all major countries have adopted comparable efforts in reducing carbon emissions.”

In order to ensure harmonization and avoid market distortions direct should be components of the free allocation process, taking into account that free allocation should be set in a way that doesn't lead to perverse incentives in terms of rewarding inefficient electricity consumers.

At the same time less and less allowances will be available in next decade, therefore the approach should be more targeted in order to address real risks of CL and allocate wisely a scarce resource.

Objective and quantitative criteria and indicators, or empirical evidence, collected at EU level and linked to different markets specificity, could be best suited in this regard.

### **1.3 Should free allocation be given from 2021 to 2030 to compensate those carbon costs which sectors pass through to customers? How could free allocation be best determined in order to avoid windfall profits?**

Regarding the issue of indirect carbon leakage, the current legislation, though in line with state aid rules, raises several sensitive issues, particularly in terms of intra-EU competitiveness. The actual use of the option of compensating firms for indirect carbon leakage may differ between Member states because of the different fiscal space they have for providing this type of financial compensation. As a consequence firms operating in different countries but within the same sector can be affected differently by current EU ETS legislation, even if all other conditions are equal. Free allocation could be a valid option to compensate the pass through of carbon prices onto final prices, but in the case of its adoption, this mechanism should replace the possibility to grant compensation as set in the current legislation. In any case, a main objective of the fourth period legislation should be, in our view, the establishment of a coordinated and fair mechanism to prevent direct and indirect carbon leakage. Windfall profits in the free allocation framework, as verified in the previous periods, should be minimized while the issue of indirect carbon leakage should be resolved through a harmonized mechanism that insures a fair level playing field for all Member states within the EU.

### **1.4 Are there any complementary aspects you would like to add to the replies given to the previous written consultation in the light of the European Council conclusions?**

We would like to reiterate that we need to provide the private sector with a reasonably steady carbon price level in the medium-long run. Any measure undertaken should be set taking so as to ensure an appropriate long term incentive to invest in low-carbon and climate resilient technologies and infrastructure, while at the same time taking into consideration concerns over possible international carbon leakage. The resulting increase

in stability of the carbon price would also reflect on auctioning revenues, giving Governments a higher degree of confidence in planning national and international policies in the transition towards a low-carbon and climate-resilient economy.

## 2. Innovation fund

**2.1 Do you see reasons to modify the existing modalities applied in the first two calls of the NER300? Are there any modalities governing the NER 300 programme which could be simplified in the design of the innovation fund? If you see the need for changes, please be specific what aspects you would like to see changed and why.**

It may be useful to identify a procedure for communicate a change in the project parameters that should have consequence in the project develop, especially for the date of entry into operation. The procedure should contain the manner of communicating and timing. In addition, it may be useful to insert a default range of tollerance for the parameters, like the changes subject of the last amendment to the Directive.

**2.2 Do you consider that for the extended scope of supporting low-carbon innovation in industrial sectors the modalities should be the same as for CCS and innovative renewable energy technologies or is certain tailoring needed, e.g. pre-defined amounts, specific selection criteria? If possible, please provide specific examples of tailored modalities.**

The extended scope of supporting low-carbon innovation in industrial sectors should be considered, especially in the matter of energy efficiency with similar modalities as for innovative RES technologies.

A potential area to explore is the possibility to offer specific guidance to industrial project, to facilitate the project design and co-financing.

As a general consideration also other sources in the EU budget (e.g. Horizon 2020) and at Member State level could be mobilized to support energy intensive industries to research, develop, pilot, demonstrate and commercialize low-carbon breakthrough process and product technologies.

**2.3 Are there any complementary aspects regarding innovation funding you would like to add to the replies given to the previous written consultation in the light of the European Council conclusions?**

None.

## 3. Modernisation fund

**3.1 Implementation of the modernization fund requires a governance structure: What is the right balance between the responsibilities of eligible Member States, the EIB and other institutions to ensure an effective and transparent management?**

The interaction among eligible Member States, EIB and other institutions should ensure that the implementation of the modernization fund is efficient, transparent and well targeted to promote decarbonization of the economies. A staged and result-based approach, where all relevant stakeholders and EU Institutions are informed of the progress achieved, could be useful.

**3.2 Regarding the investments, what types of projects should be financed by the modernisation fund to ensure the attainment of its goals? Should certain types of projects be ineligible for support?**

This question calls for a general consideration on interactions among different funds, see question n. 3.4. Clearly these projects should aim to optimally reduce greenhouse gas emissions and/or reduce energy consumption on a sustainable basis in the countries accessing the modernisation fund. Some types of projects to improve energy interconnections among member states may also be considered.

**3.3 Should there be concrete criteria [e.g. cost-per-unit performance, clean energy produced, energy saved, etc.] guiding the selection of projects?**

Yes, there should be concrete criteria to guide selection of projects and ex post evaluation of results achieved. These criteria should be aimed at fulfilling the objectives set out in the Climate and Energy Framework, namely reducing emissions in a way that is consistent with mid and long term EU targets, increasing the share of renewables and improving energy efficiency.

**3.4 How do you see the interaction of the modernisation fund with other sources of funding available for the same type of projects, in particular under the optional free allocation for modernisation of electricity generation (see section 4 below)? Would accumulation rules be appropriate?**

Interaction among funds should occur only when there is a clear and incontrovertible value-added. A possible way to avoid undesired interaction among different funds could be to devote any fund, or particular windows in it, to certain sectors of project types. So, if art. 10c is mainly devoted to electricity sector, the modernization fund could be more focused on other sectors or project types. In this regard accumulation rules would serve as an instrument to avoid undesired overlapping.

**3.5 Do you have views how the assessment of the projects should be reflected in the forthcoming 2030 governance process (e.g. national climate programmes, and plans for renewable energy and energy efficiency)?**

The use of funds available to eligible Member States from the Modernization Fund should be part of the governance process of these Member States, therefore included in their Low Carbon Development Strategies, but also in renewable energy and energy efficiency planning, if relevant.

### **3.6 Should the level of funding be contingent on concrete performance criteria?**

Yes.

## **4. Free allocation to promote investments for modernizing the energy sector**

### **4.1 How can it be ensured that investments have an added value in terms of modernizing the energy sector? Should there be common criteria for the selection of projects?**

The investments should be directed to projects that encourage the transition to low carbon technologies, improve the security of energy supply through a greater integration of the EU energy market and improved energy efficiency, improve the integration of renewable energy within electricity networks. Finally the investments should be oriented to projects with positive spillovers at the EU level. To this end projects in grid interconnections, energy storage and energy efficiency should be eligible.

### **4.2 How do you see the interaction of the free allocation to energy sector with other sources of funding available for the same type of projects, e.g. EU co-financing that should be made available for the projects of common interest under the 2030 climate and energy framework? Would accumulation rules be appropriate?**

See response to 3.4. Accumulation rules may be appropriate.

### **4.3 Do you have any views how the assessment of the projects should be reflected in the forthcoming 2030 governance process (e.g. as regards improving transparency)?**

The use of funds available to eligible Member States from art. 10c should be part of the governance process of these Member States, therefore included in their Low Carbon Development Strategies, but also in renewable energy and energy efficiency planning, if relevant.

### **4.4 The maximum amount of allowances handed out for free under this option is limited. Do you think eligible Member States should use the allowances for a period of time specified in advance (e.g. per year), or freely distribute them over the 2021-2030 period? (Please explain your motivation.)**

The time profile of release of these allowances should be designed in a way to avoid interference and turbulences on the market, where the market is also intended as allowances auctioned by Member States. Therefore any plan should be decided well in advance, shared with other relevant stakeholders including Member States, be publicly available and have a flat profile over time in order to release gradually the allowances and not create a supply-side shock.

**4.5 Should there be priorities guiding the Member States in the selection of areas to be supported?**

Yes.

**If so, which of the following areas, if any, currently supported through investments for modernisation of electricity generation up to 2020 should be prioritised for support up to 2030 and why?**

Interconnectors, smart grids, energy efficiency and storage, renewable energy.

**4.6 How can improved transparency be ensured with regard to the selection and implementation of investments related to free allocation for modernisation of energy? In particular regarding the implementation of investments, should allowances be added to auctioning volumes after a certain time period has lapsed in case the investment is not carried out within the agreed timeframe?**

If an investment is not carried out within the agreed timeframe, allowances should be added to auctioning volumes after a certain time period.

## **5. SMEs / regulatory fees / other**

**5.1 Are there any EU ETS administrative requirements which you consider can be simplified? Do you see scope to reduce transaction costs, in particular for SMEs? If yes, please explain in detail.**

As defined by the EU recommendation 2003/361, the definition of SMEs at EU level might not provide the best basis for identifying installations eligible for a simplified rules approach under ETS, as it can be referred to installations that represent a significant source of emissions. As ETS is meant to rule GHG emissions from industry sector we would better see the application of simplified requirements to small emitters, rather than to SMEs, as it's in the current text.

In terms of simplified administrative requirements, the monitoring, reporting and verification activity might still offer possibilities of simplification. While recognizing the importance of such phases in the compliance cycle as well as fully sharing its principles there is still room for improvement in terms of simplification of procedures and implementation of operational

requirements which might result in cumbersome activities for operators and competent authorities without a concrete added value in terms of monitored/communicated/verified emissions.

**5.2 Member States had the possibility to exclude small emitting installations from the EU ETS until 2020. Should this possibility be continued? If so, what should be the modalities for opt-out installations to contribute to emission reductions in a cost-effective and economically efficient manner? Should these be harmonised at EU level?**

The possibility to opt-out for small emitting installations from EU ETS must be assured also in the fourth period of EU ETS. Measures could be harmonized at the EU level.

We've always welcomed the possibility of excluding small emitters from the ETS scheme. A general revision of the scope of the ETS Directive would be useful in order to ensuring that small sources of emissions are treated appropriately in Phase IV. This can be done in two ways: a) opt out as in the current system, but with a more flexible and fully harmonized system at EU level b) upward adjustment of the thresholds, to be fully evaluated in light of thorough assessment of value-added and absence of market distortions at EU level and taking into consideration other relevant environmental permitting directives as IPPC. A revision of the scope could also lead to harmonization on other aspects such as inclusion/exclusion of waste treatment installations, or a less difficult and controversial application of the ETS to the aviation sector.

**5.3 How do you rate the importance of a high level of security and user-friendliness of the Union Registry? Do you think the costs for providing these services should be covered via Registry fees?**

Security and user-friendliness are both very important and should be considered in a balanced way. We believe that those elements can be seen in a synergic way and in many fields they are already well merged together, i.e. simple home-banking websites currently seem to have reconciled successfully the two aspects.

The costs related to Registries should be covered by fees, as already happens in many Member States.

**5.4 Do you consider discrepancies in Registry fees in different Member States justified? Should Registry fees be aligned at EU level?**

The discrepancies in Registry fees are unjustified and we support the alignment of fees at the EU level in order to avoid differences among firms located in different Member States. An European fee could be useful to solve this point.

**5.5 Under the current EU ETS Directive, at least 50% of the revenues generated from the auctioning of allowances should be used by Member States for climate-related purposes. For the calendar year 2013 Member States have reported to have used or to plan to use 87 % on average to support domestic investments in climate and energy. Do you consider the current provisions regarding the use of the revenues adequate for financing climate action? If not, please explain why?**

Provisions aimed at signaling the importance of climate action both at national and international level in a balanced manner are important and could be further enhanced. Believing that the current provisions regarding the use of the revenues are adequate we are opposed to any form of earmarking of revenues generated by the auctioning of allowances.

## 6. General evaluation

**6.1 How well do the objectives of the EU ETS Directive correspond to the EU climate policy objectives? How well is the EU ETS Directive adapted to subsequent technological or scientific changes?**

EU ETS is the cornerstone of EU climate policy.

The objective to create a scarcity, therefore a price signal for the private sector has been achieved. The definition of benchmarks based on actual data from most efficient installations to be periodically revised and the auctioning as default rule for allocation allow the system to respond to technological or scientific changes.

Further improvements are nonetheless needed. The current market imbalance and the absence of an instrument (pending the approval of the Market Stability Reserve) that allows the system to adjust to external shocks can lead to a lock-in effect in carbon intensive technologies.

**6.2 What are the strengths and weaknesses of the EU ETS Directive? To what extent has the EU ETS Directive been successful in achieving its objectives to promote emission reductions in a cost-effective manner compared to alternatives, e.g. regulatory standards, taxation?**

Different instruments are fit to serve for different purposes, the challenges ahead of us are such that the question is not which instrument we should use to achieve our goals, but how to integrate in structured and harmonic way what we have at our disposal. For the time being we cannot rule out any option.

While taxation could provide a more stable, clear price signal to operators, the ETS has the advantage of allowing firms to choose the best, most cost effective measures for



reducing emissions. This is the major strength of the ETS, but in order for it to work over the medium to long run it must also serve as a guide for low carbon investments. An adequate carbon price is required to foster investments in low carbon technologies; without a clear carbon price signal, market operators do not know whether investing in low-carbon technology will be a profitable strategy. This uncertainty risks leading them to postpone low-carbon investments, at a time when a considerable part of the capital stock in the energy sector needs to be replaced. Since the launching of the ETS in 2005, the actual carbon price has, on several occasions, dipped beneath the expected price. Given the surplus of allowances generated during the economic crisis, the present (and future) carbon price is considered to be too low and unstable to incentivize low carbon investments. In this situation, some degree of supply flexibility must be introduced within the mechanism. Furthermore, the current enormous surplus of allowances must be dealt with as effectively and timely as possible. At the same time, we consider that any intervention needs to minimise possible negative impacts on the market and, as such, should be built on clear, predictable rules, so as to allow a transition period. In our view, this would allow operators to adjust their expectations, avoiding excessive discontinuities in the market.

The price trend observed in recent year poses various issues, a mechanism allowing for a reversible adjustment of supply, without altering the cap, is the option that would best support the carbon price in the long run.

Harmonization at the EU level is the one (or even THE) greatest strengths of the EU ETS. This is of the utmost importance since national policies that affect the energy sector can alter intra-EU competitive conditions.

**6.3 To what extent are the costs resulting from the implementation of the EU ETS Directive proportionate to the results/benefits that have been achieved, including secondary impacts on financing/support mechanisms for low carbon technologies, administrative cost, employment impacts etc.? If there are significant differences in costs (or benefits) between Member States, what is causing them?**

The costs and the benefits have to be compared in an appropriate time horizon. It is clear that EU ETS as it is now, in the third trading period, is more balanced, effective and efficient than in the past. The learning curve of a system built from scratch, that involves more than 12.000 installations in 28 Member States has taken time. But we think that we are close to a system that is really harmonized at EU level, that represents a best practice also for other types of EU policies, and that has still potential for example related to linking with other trading systems across the world, and that should not present different costs for different MS (except for the usual exemptions and special funds for some Member States).

#### **6.4 How well does the EU ETS Directive fit with other relevant EU legislation?**

As stated in the previous answer EU ETS represents a best practice also for other EU policies as EU harmonized policy.

It is not yet legislation but we see a lot of value added in having a specific pillar on decarbonization in the Energy Union context.

All policies need to go hand in hand and be mutually reinforcing.

Policies to address emission reductions inevitably interact with interventions in other areas and the risk of overlapping and creating frictions or undesired effects is real. In particular there are several studies that emphasize the relationship between the support scheme for RES and the price of permits. To this end policies and instruments that affect emission reductions should be aligned. All energy policies should take into account in one way or another the EU ETS in order to ensure coherency of action and avoid undermining the effectiveness of the ETS.

#### **6.5 What is the EU value-added of the EU ETS Directive? To what extent could the changes brought by the EU ETS Directive have been achieved by national measures only?**

The same results could probably not have been achieved at national level, not without creating competitive distortions in the EU-wide market.

Climate change policy, in particular the reduction in GHG emissions in the industrial sector, is most effective at the EU level. National measures tend to produce uneven results, may be less effective and even undermine other Member states actions.

#### **6.6 Do you have any other comment on the revision of the EU ETS Directive that you would like to share?**

More harmonized, more stable, more simple.

In order to strengthen its environmental integrity while guaranteeing a level playing field at the international level for EU industries, the EU ETS should progressively move to a product based logic, which was for example adopted for CL measures. This approach would allow to tackle also non-EU emissions driven by EU consumption, while restoring the level playing field between EU industrial production subject to the EU ETS and non-EU production. A serious assessment of how importers could be included in the scope of the actual EU ETS could be a significant step forward toward this approach.