



# **TOWARDS AN EMISSION TRADING SCHEME THAT DELIVERS A GREEN AND JUST TRANSFORMATION OF EUROPEAN ENERGY AND INDUSTRY**

Greens/EFA position on a revised ETS





## INTRODUCTION

This decade will be pivotal in halting the worst effects of the climate emergency and living up to the Paris Agreement. In order to keep the EU in line with a 1.5°C compatible pathway the EU must achieve at least 65% overall emission cuts by 2030, which will require all climate related legislation to be radically revised. The European Parliament, and in particular the Green/EFA group will need to inject ambition for the Commission's 'fit for 2030 package' to be sufficiently ambitious. The global race to climate neutrality is afoot and the EU needs to be bold to ensure European industry leads the way in the green and just industrial transformation.

The EU Emissions Trading System Directive (ETS) is supposed to be a central piece of legislation to establish the polluters pays principle and incentivising the decarbonisation of power generation, industry and aviation. Yet despite the recent rising price of carbon, the environmental and societal cost of GHG-emissions is still much higher<sup>1</sup>. A surplus of emissions allowances and free allocation has led to insufficient price signals to trigger the systemic shift away from fossil fuels towards green solutions. This ETS revision must trigger this shift and help transform Europe's industry and support the shift to renewables.

The revision is not only about a higher carbon price, but also about creating the best possible instrument that works for climate and the green transformation of the power sector and the EU industry. The ETS is part of a toolbox, alongside other legislation such as Renewable Energy Directive (RED), Energy Efficiency Directive (EED), the Energy Performance of Buildings Directive (EPBD), Carbon Border Adjustment Mechanism (CBAM), the Energy Taxation Directive (ETD), which should phase-out fossil fuels and phase-in carbon neutral technology. Ambitious carbon pricing therefore needs to be accompanied by rapid and massive deployment of renewables and energy efficiency measures.

In this paper, we outline our position on this year's revision of ETS. The EU must:

- **Get the price right** by getting rid of the surplus allowances, ending free allocation and setting a carbon floor price;
- **Get the scope right**, by including aviation and shipping and excluding road transport and heating;
- **Get the incentives right**, by investing back into climate action and create an international level playing field. These are our 3 priorities for the revision of ETS. In order to make ETS the true cornerstone of EU climate policy.

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<sup>1</sup> <https://www.umweltbundesamt.de/presse/pressemitteilungen/konsequenter-umweltschutz-spart-der-gesellschaft>

Part 1

## The right price

The current EU ETS legislation aims at delivering a 43% emissions reduction in ETS sectors by 2030 compared to 2005, coherent with an EU economy-wide emissions reduction target of at least 40% by 2030. Recent research shows that a 65% climate target by 2030 would require around 70% emissions reductions in ETS sectors (compared to 2005)<sup>2</sup>. Delivering such a emissions reduction requires a fundamental reform of the EU ETS, in particular by ensuring a faster reduction of the cap, getting rid of the structural surplus, full auctioning of allowances and establishing a carbon floor price to avoid short-term price drops due to external events and facilitate investment in energy efficiency.

### **ENSURE A FASTER REDUCTION OF THE CAP**

A large structural surplus of allowances combined with the uptake of renewables and energy efficiency has meant that installations covered by the ETS today are already emitting less than the cap. The European Commission estimates that this surplus amounted to around 250 million allowances in 2019, but the economic downturn caused by the current pandemic is likely to increase this surplus even further. A recent analyst poll shows the average decrease estimate at 13.3%, which would represent the largest annual percentage fall in the scheme's greenhouse gas output since it started in 2005<sup>3</sup>.

Since the last revision of ETS (phase 4, 2021-2030), the cap on emissions is subject to an annual linear reduction factor of 2.2%, based on an EU economy-wide emissions reduction target of at least -40% by 2030. The so-called LRF has to be increased in order to be compatible with the new 2030 climate target but also with the climate-neutrality objective by 2050 at the latest, which requires a steeper reduction of emissions from ETS sectors. Carbon Market Watch finds that in order for the ETS cap to reach -70% by 2030 (in line with EU economy-wide target of -65% by 2030), the LRF will have to be increased to 5.8% as of 2023<sup>4</sup>. A Sitra study<sup>5</sup> finds that in order to

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2 <https://www.umweltbundesamt.de/en/publikationen/raising-the-eu-2030-ghg-emission-reduction-target>

3 [https://carbon-pulse.com/124071/?utm\\_source=CP+Daily&utm\\_campaign=44a1395b2c-CPdaily16032021&utm\\_medium=email&utm\\_term=0\\_a9d8834f72-44a1395b2c-110321846](https://carbon-pulse.com/124071/?utm_source=CP+Daily&utm_campaign=44a1395b2c-CPdaily16032021&utm_medium=email&utm_term=0_a9d8834f72-44a1395b2c-110321846)

be in line with an economy-wide 60% emissions reduction target (as adopted by Parliament in October 2020), the ETS would need an LRF of 4.57% if applied from 2021, and 6.94% if applied only from 2026. Such steep reductions are likely to drive an important short-term surge in EUA prices. By modelling different ETS revision, ICIS finds that applying a one-off reduction of allowances (rebasement of the cap) would result in a smoother upward trajectory for EUA prices<sup>6</sup>, which could help emitters better manage their carbon risk and plan decarbonisation investments. Carbon Market Watch finds that if the cap is decreased by a one-off reduction of 450 million allowances in 2023, the LRF will have to be increased to 3.1% as of 2023<sup>7</sup>.

**The Green/EFA group demands that:**

- A significant one-off reduction is required in 2023 to remove excess allowances, rebasing the cap. A later implementation will require a steeper LRF and a larger one-off reduction;
- The Linear Reduction Factor needs to be increased in line with a pathway to achieve 65% emission reduction cuts in the EU, depending on the size of the one-off reduction the LRF should be increased to as much as 5.8% in 2023.

**IMPROVE THE MSR**

The ETS revision will also include the first review of the Market Stability Reserve (MSR), foreseen within three years of the date of its start of operation. The Market Stability Reserve rules under the ETS aim at tackling structural supply-demand imbalances. Each year, if the total number of allowances in circulation (TNAC) is greater than 833 million, 24% of the TNAC will be placed in the reserve. From 2024 onwards, this share is set to decrease to 12%. If, on the contrary, TNAC is lower than 400 million, then 100 million EUAs will be released from the MSR. Finally, the amount of certificates in the MSR is limited to the amount that is auctioned yearly<sup>8</sup>.

The MSR lived up to its aim, but was not designed to handle the current and future oversupply, as expected in the wake of the covid crisis. This means that a significant amount of allowances will add to the current surplus of allowances and negatively affect the carbon price signal. We therefore need to further improve the MSR.

**The Green/EFA group demands that:**

- Excess allowances need to be cancelled after a maximum of 5 years and no allowance should be released from the MSR if the previous year's emissions exceeded the cap;
- Significant increase in the intake rate of the MSR should be gradually phased out as of 2023 and by 2026. Without a higher intake rate, there is a risk that from 2024 onwards, more new allowances are released to the market than are needed which could increase the surplus again<sup>9</sup>;

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4 <https://carbonmarketwatch.org/wp-content/uploads/2021/02/Response-to-EC-public-consultation-on-updating-the-EU-ETS.pdf>

5 <https://media.sitra.fi/2019/10/07112628/the-role-of-the-eu-ets-in-increasing-eu-climate-ambition.pdf>

6 <https://carbon-pulse.com/121555/>

7 To be in line with the objective of reducing ETS emissions by -70% by 2030, compared to 2005 (65% EU economy-wide climate target) -<https://carbonmarketwatch.org/wp-content/uploads/2021/02/Response-to-EC-public-consultation-on-updating-the-EU-ETS.pdf>

8 <https://carbonmarketwatch.org/wp-content/uploads/2021/02/Response-to-EC-public-consultation-on-updating-the-EU-ETS.pdf>

- Reevaluate the MSR threshold with a focus on the industrial sectors to ensure that the MSR continues to fulfill the purpose of ensuring market stability and removing excess allowances<sup>10</sup>;
- Member states should be encouraged to unilaterally delete an amount of allowances equivalent to the emissions saved by the national measure (e.g. national coal phase out)

#### **END FREE ALLOCATION WHILE STILL PROVIDING CERTAINTY FOR THE INDUSTRY AGAINST THE POTENTIAL RISK OF CARBON LEAKAGE**

Under the current directive around 6.3 billion allowances, worth as much as €160 billion, are expected to be allocated for free to companies between 2021 and 2030<sup>11</sup>, with the justification of carbon leakage risks. This risk of carbon leakage<sup>12</sup> for most sectors covered however is limited<sup>13</sup> or non-existing (e.g. intra EU aviation). At the same time heavy industries show few signs of rapid decarbonisation (0.55% annual reduction of emissions in phase 3<sup>14</sup>), while emissions in the power sector - where free allocations are in short supply - have dropped significantly. The EU Court of Auditors recently concluded that free allocation of allowances have slowed down decarbonisation<sup>15</sup>. While the real risk of carbon leakage is still to be proven for many sectors, the introduction of a Carbon Border Adjustment Mechanism (CBAM) would be more effective in addressing that potential risk, while still incentivising emissions reduction both within and outside the Union. Finally, free allocations are unsustainable in the medium- to long-term as the total number of allowances decreases.

Free allowances are in contradiction with the polluters pays principle enshrined in the EU Treaties (TFEU 191). The risk of market failure is evident, since the external cost of the carbon pollution is not internalised by the industry receiving the free allowances. Finally free allocation distributes the responsibility for reducing greenhouse gas emissions between citizens and large polluters in an unfair way. Free allowances are an inadequate tool to achieve decarbonisation and allow industry to prosper in Europe.

#### **The Green/EFA group demands that:**

- End free pollution by 100% auctioning by 2023 in sectors with no or limited carbon leakage in order to incentivise rapid decarbonization in heavy industry, shipping and aviation;
- The introduction of CBAM should gradually but rapidly replace (by 2026 at the latest) current carbon leakage provisions. During the transition period, it shall not lead to double protection for EU industry by applying a simple principle whereby one tonne of carbon cannot be protected twice.

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9 <https://media.sitra.fi/2019/10/07112628/the-role-of-the-eu-ets-in-increasing-eu-climate-ambition.pdf>

10 <https://sandbag.be/wp-content/uploads/2020/12/Sandbag-Feedback-to-ETS-Roadmap.pdf>

11 <https://www.consilium.europa.eu/en/policies/climate-change/reform-eu-ets/>

12 [https://www.umweltbundesamt.de/sites/default/files/medien/1410/publikationen/2020\\_10\\_20\\_climate\\_change\\_32\\_2020\\_analysen\\_carbon-leakage-risiko.pdf](https://www.umweltbundesamt.de/sites/default/files/medien/1410/publikationen/2020_10_20_climate_change_32_2020_analysen_carbon-leakage-risiko.pdf)

13 <https://carbonmarketwatch.org/wp-content/uploads/2021/02/Response-to-EC-public-consultation-on-updating-the-EU-ETS.pdf>

14 <https://sandbag.be/wp-content/uploads/2020/12/Sandbag-Feedback-to-ETS-Roadmap.pdf>

15 European Court of Auditors special report 2020 “The EU’s Emissions Trading System: free allocation of allowances needed better targeting”

- The phase out should be accompanied by a decarbonization strategy for heavily globalized sectors, accompanied by sustainable investments from the modernization and innovation funds;

#### **CARBON FLOOR PRICE**

In the wake of the financial crisis in 2008 the ETS price crashed, leaving no incentive to decarbonize heavy industry. This creates high market uncertainty, while a stable, ascending market price is needed in the decades to come.

Industry has so far contributed little to reducing emissions. So it is important to in particular look at what the abatement costs are for key sectors will look like in 2030. Steel would require at least a price of 100 Euros, Chemicals a price of 170 Euros and Cement 70 Euros. To begin to seriously affect change in these sectors, the price of carbon will need to increase to 150 euros in 2030<sup>16</sup>.

#### **The Green/EFA group demands that:**

- A minimum carbon floor price is introduced in order to drive innovation, create manageable expectations for investment and avoid price speculation;
- This price needs to drive out coal and gas and drive innovation and should therefore increase every year from at least 50 Euros, increasing to 150 Euros in 2030. Additional rules should be introduced to avoid speculation on ETS allowances, e.g. by limiting the amount of ETS allowances to be held by financial market participants.

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16 Dietz et al (2018). The Economics of 1.5°C Climate Change. Annual Review of Environment and Resources.



Part 2

## The right scope

After many years of the ETS price being very low, the instrument is starting to lead to shifts away from fossil fuels towards renewables and other solutions, in particular in the energy sector. It is essential to agree on the right scope for the ETS so as to not jeopardise the progress made over the last years. The Greens/EFA group demands that road transport and buildings are not included in the ETS, because they don't respond to price well, which could cause public backlash.

### TRANSPORT AND BUILDINGS

Transport and buildings are without a doubt sectors which will need to see more rapid decarbonisation rates and therefore require increased European coordination. Transport is the only sector in which the emissions grew in the last decade and the built environment is part of the private sphere of individuals and is therefore incredibly complex in terms of property rights, coordination and societal sensitivity. Although action is needed, the inclusion of road transport and buildings is a high-risk, low-reward measure. This policy approach is complex and politically sensitive and - even in the best case scenario - would have little to no impact on emissions before 2030.

The road transport sector is very price inelastic, even a significant carbon price is unlikely to encourage citizens to switch to cleaner technologies and it would do nothing to address the real (market) barriers to the low carbon transition. At the same time, there are real social risks associated with such measures as it will penalise low-income households who may not have the possibility to choose cleaner alternatives. In order to have any meaningful impact on reducing emissions in the transport sector, the ETS price would need to reach hundreds of euros on top of the implicit carbon taxes of around 200 Euros/tCO<sub>2</sub><sup>17</sup>, which would be socially extremely

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<sup>17</sup> <https://www.transportenvironment.org/newsroom/blog/road-transport-eu-ets-high-risk-low-reward-strategy>

difficult and only achievable by setting up a separate ETS system. Setting up a separate ETS would undermine more effective regulatory measures for the years to come and threaten improving the current regulatory measures, such as tighter CO2 standards, an internal combustion engine (ICE) phase out or an ambitious review of the Euro-charging Directive. Phasing out new ICEs will, however, still leave the challenge of decarbonising the existing car park. This can be addressed by a smart combination of increased carbon pricing at national level (either through an EU-wide carbon-based fuel tax through the upcoming revision of the Energy Taxation Directive or through obligations at Member States level) and recycling of those revenues to finance infrastructure to ensure modal shift and schemes to replace old vehicles by zero-emission vehicles.

Even more than with transport, including buildings in ETS is a socially regressive policy measure, which puts the burden of the required transition on citizens, many of whom would just be forced to pay higher prices without having the possibility to choose cleaner alternatives (e.g. financial constraints, renting property). Widening the single ETS cap to include transport and buildings (with an ETS price of 80 to 90 euros/ton in 2030) would for instance push up average spending on gas-fuelled household heating by 30%<sup>18</sup>. This will indeed mean that it is more attractive to insulate buildings, but even with an ambitious renovation rate of 3%, most citizens will only switch to low carbon solutions after many years, while the energy bill increases on day one of the ETS inclusion. This would particularly hit vulnerable populations hardest, who are already suffering disproportionately from the Covid-19 crisis. At a time when the Commission is attempting to galvanise citizen support for the Green Deal, it should not risk public backlash similar to the gilets jaunes in France.

In addition, by removing these sectors from the Effort Sharing Regulation (ESR), Member States will have less incentives to deliver national measures to decarbonise buildings, such as fiscal measures or building renovation schemes and targets. Moreover the EU is not able to put up direct redistribution schemes to balance the effects on low income households. Moreover, unlike the EU budget, national or local budgets are better equipped to ensure the massive direct support/redistribution schemes needed for ensuring a just transition, in particular for low-income households (e.g. public transport vouchers, bonuses for the purchase of zero-emission vehicles, Energiegeld). Double coverage, by including it in ESR and ETS, increases the risk of weakening ESR during the negotiation process. A risk we should not take, as setting up a separate ETS is a high risk process from which the benefits are very uncertain.

Other avenues should be explored to increase carbon pricing on road transport and buildings, e.g. by aligning the Energy Taxation Directive with the Paris Agreement objectives.

### **The Green/EFA group therefore demands that:**

- Transport and buildings are not included in the EU ETS, nor are they included in a separate ETS. Commission and Member States shall instead focus their attention on other measures to decarbonise these sectors that have been proven successful in the past, like strengthening the EU CO2 standards, the Energy Taxation Directive and the Eurovignette, national and local incentive schemes to replace old vehicles by zero-emission vehicles, and stepping up investment in infrastructure to ensure modal shift and for building renovation. Moreover,

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<sup>18</sup> <https://europeanclimate.org/wp-content/uploads/2020/06/01-07-2020-decarbonising-european-transport-and-heating-fuels-full-report.pdf>



member states can introduce national carbon pricing or trading schemes for those sectors in order to meet their Effort Sharing targets.

#### **NO CARBON SINKS IN ETS**

The European Commission is considering bringing carbon sinks into carbon markets. However the commodification of nature is one of the main drivers of biodiversity loss and climate change. There is already a big conflict between forests needing to be carbon sinks, raw materials for construction and used for bioenergy and the inclusion of carbon sinks in the carbon market will further exaggerate this tension. Governments need to encourage rewilding and improving biodiversity of forests, not implement schemes that will encourage monocultures. Further, if this model were to be exported internationally, this could increase threats for biodiversity hot spots such as the amazon rainforest.

The other possibility is to create a market for 'Carbon Dioxide Removal' technologies (e.g. CCS, CCU, DAC) under the EU ETS. We believe this debate is way too premature as there is at the moment no regulatory framework to ensure that such technologies permanent, safe and reliable removal and storage of CO<sub>2</sub>.

Finally, the climate law excludes international credits and this must continue to be the case. As the Commission is looking into integrating CORSIA within ETS, this should not be used as a way to reintroduce international credits in the ETS through the back door.

Europe has one of the highest per capita emissions and is one of the wealthiest regions, which means the EU should focus primarily on reducing emissions, not on providing loopholes for European companies and consumers to continue to emit, expecting nature to counteract these emissions. Nature is already under stress and the focus should be on emission reduction to protect our sinks.

#### **The Green/EFA group demands that:**

- ETS continues to exclude any type of international credits as EU's climate targets are to be achieved domestically, as confirmed by the European Parliament and the Council in the framework of the EU Climate Law.
- ETS continues to exclude domestic carbon sinks, i.e. no flexibility with LULUCF/AFOLU and no CDR credits under the EU ETS will be introduced, as GHG removal is not permanent and will weaken the incentive to decarbonise industry.

#### **AVIATION AND SHIPPING**

The emissions from international maritime and aviation are insufficiently regulated and emissions continue to increase<sup>19</sup>. In theory, all flights from within the European Economic Area (EEA) as well as extra-EEA flights with either departure or destination in the EEA are covered by the ETS. However, since 2012, the EU ETS does not apply 'temporarily' to extra-EEA flights ('stop the clock' derogation) due to negotiations at the International Civil Aviation Organisation (ICAO)

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19 <https://www.transportenvironment.org/state-aviation-ets>

to establish a global regime to offset aviation emissions (CORSIA). It is important to note that there is a major difference in nature between CORSIA - which aims at offsetting global aviation emissions beyond their 2019 level - and the EU's climate-neutrality objective that implies all sectors of the economy to reach close-to-zero emissions by 2050 at the latest. CORSIA will therefore fall short of the necessary emissions reduction in line with the EU economy-wide objective of reaching climate-neutrality by 2050 at the latest<sup>20</sup>. Without undermining our efforts to regulate aviation emissions at international level, the EU should go beyond CORSIA to make sure aviation emissions are not left unchecked. To make matters worse, the EU has so far failed to address the non-CO2 impacts of aviation, which have been estimated to have a climate impact three times worse than CO2<sup>21</sup>. Current targets and measures envisaged by the International Maritime Organisation (IMO) would also fall short of the necessary decarbonisation pathway to be in line with the Paris Agreement and global CO2 emissions are expected to increase by 90% - 130% by 2050 (based on 2008), if we do not take more ambitious action. Emissions from international maritime emissions have so far not been included into the EU ETS and remain unregulated.

#### **The Green/EFA group demands that:**

- Domestic, intra-EU and international aviation and shipping emissions to comply with the EU's 2030 climate goal and be subject to the ETS;
- As there is no risk of carbon leakage either in the aviation sector<sup>22</sup> or in the maritime sector<sup>23</sup>, free allowances to the aviation sector should be abolished and both sectors should be subject to 100% auctioning, as requested by the European Parliament<sup>24</sup>;
- Non-CO2 impacts of aviation to be regulated (e.g. through NOx and methane charges);
- Extension of ETS to shipping to be accompanied by ambitious energy efficiency targets to be applied at fleet level.

#### **BIOMASS**

Europe's academies of science have called for a "radically new standard" in the bloc's Emissions Trading Scheme (ETS) to ensure net carbon emissions from biomass power stations are "properly accounted for and declared"<sup>25</sup>. Bioenergy is currently treated as if it were carbon neutral, but evidence is clear that the climate impact is significant<sup>26</sup>, even compared to fossil fuels. The EU's bioenergy policy also leads to tensions with food and fibre production, habitat destruction, land use change and biodiversity loss. It is therefore essential that the Renewable Energy Directive, LULUCF Regulation and ETS properly accounts for the carbon emissions of bioenergy, to ensure that bioenergy is not over subsidised.

#### **The Green/EFA group demands that:**

- The net carbon emissions from biomass are accounted for under the ETS.

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20 [https://www.transportenvironment.org/sites/te/files/publications/2019\\_09\\_Corsia\\_assesement\\_final.pdf](https://www.transportenvironment.org/sites/te/files/publications/2019_09_Corsia_assesement_final.pdf)

21 [https://ec.europa.eu/clima/news/updated-analysis-non-co2-effects-aviation\\_en](https://ec.europa.eu/clima/news/updated-analysis-non-co2-effects-aviation_en)

22 [https://www.transportenvironment.org/sites/te/files/publications/2020\\_11\\_Oko\\_Institute\\_analysis\\_potential\\_reforms\\_aviation\\_inclusion\\_ETS.pdf](https://www.transportenvironment.org/sites/te/files/publications/2020_11_Oko_Institute_analysis_potential_reforms_aviation_inclusion_ETS.pdf)

23 [https://www.transportenvironment.org/sites/te/files/publications/ETS\\_shipping\\_study.pdf](https://www.transportenvironment.org/sites/te/files/publications/ETS_shipping_study.pdf)

24 [https://www.europarl.europa.eu/doceo/document/TA-9-2020-0219\\_EN.html](https://www.europarl.europa.eu/doceo/document/TA-9-2020-0219_EN.html)

25 <https://www.euractiv.com/section/emissions-trading-scheme/news/scientists-call-on-eu-to-correct-biomass-carbon-accounting-rules/>

26 <https://ember-climate.org/project/the-burning-question/>

## Part 3

# The right incentives

### INVEST IN CLIMATE ACTION

The number of permits that are auctioned has increased steadily since 2012 – from 90 million in 2012 (worth €620 million) to over 920 million in 2018 (raising €14 billion). By removing free allowances and expanding the EU ETS to aviation, shipping, waste incineration and bioenergy would bring in more revenues.

A recent study by McKinsey<sup>27</sup> suggests that the transition to net-zero in Europe will cost €5.4 trillion. Of this, about €1.5 trillion would be invested in the buildings sector (29 percent), €1.8 trillion would be used for power (33 percent), €410 billion for industry (8 percent), €76 billion for agriculture (about 1 percent), and €32 billion in transportation (less than 1 percent). About €1.5 trillion (28 percent) would fund infrastructure to improve energy transmission and distribution in all sectors.

These revenues have largely gone to Member State coffers, with separate smaller streams going to EU-level funding instruments, such as the Innovation Fund. According to the EU ETS Directive, Member States are supposed to use at least 50% of these revenues for further climate action (such as deploying renewable energy, energy efficiency, innovation and research, avoiding deforestation and supporting reforestation) and report on this to the European Commission. While over 2013-2015 Member States used over 85% of ETS revenues to finance climate action, this share had decreased to just 64% by 2018<sup>28</sup>. In 2019 the Commission estimates that 77% of EU ETS revenues were spent or planned to be spent by member states on climate action<sup>29</sup>. Stricter rules to ensure that all ETS revenues are used to trigger the green industrial revolution are required in this revision. Therefore binding provisions and fully transparent tracking should ensure that 100% of EU ETS revenues allocated to Member States go to additional green investments. ETS revenues that become EU revenues as new own resources must not be used to substitute spending

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27 <https://www.mckinsey.com/business-functions/sustainability/our-insights/how-the-european-union-could-achieve-net-zero-emissions-at-net-zero-cost#>

28 [https://wwf.panda.org/discover/knowledge\\_hub/?357181/Strategic-spending-how-the-EU-Emissions-Trading-System-can-fund-fair-climate-action](https://wwf.panda.org/discover/knowledge_hub/?357181/Strategic-spending-how-the-EU-Emissions-Trading-System-can-fund-fair-climate-action) (google.com)

29 [https://ec.europa.eu/clima/news/carbon-market-report-emissions-eu-ets-stationary-installations-fall-over-9\\_en](https://ec.europa.eu/clima/news/carbon-market-report-emissions-eu-ets-stationary-installations-fall-over-9_en)

on climate action from the EUs budget. But must be used to further increase climate action ( not be used as an opportunity to increase financing for climate action under the EU budget). According to the WWF analysis, between 2016 and 2018, EU ETS revenues spent on climate action could have been multiplied by a factor of 2,5 had all allowances been auctioned and had all ETS revenues been spent on climate action<sup>30</sup>.

Investing in innovative zero-carbon/climate neutral industrial technologies faces many risks, one of which is the uncertain revenue that might be obtained in the carbon market by selling carbon reductions or excess allowances. Future carbon prices are very difficult to predict due to intrinsic regulatory uncertainty regarding taxes or carbon markets (which drives supply), and also to the uncertain evolution of low-carbon technologies (which drives demand). Regulation, investments and new forms of governance and contracting can ensure a more predictable price and stable investment environment.

### **The Greens/EFA group therefore demands that:**

- 100% of revenues allocated to Member States should be used in a redistributive way to enhance climate action and support a just transition for communities as well as counteracting the negative redistributive effects of the policy for poorer households, for example by encouraging, as part of a wider set of national redistributive measures, direct redistribution schemes for low-income households in Member States such as Energie Geld/Green vouchers. Revenues from the EU ETS that flow to the EU budget as new own resources should mean greater support for climate action at EU level (including through the Just Transition Fund).
- Revenues from the EU ETS that flow to the EU budget as new own resources should mean greater support for climate action at EU level (including through the Just Transition Fund). Priority should be given to those projects which address climate action and simultaneously reduce inequality and energy poverty by redistributing revenues fairly - such as those promoting community energy, energy efficiency and good non-fossil jobs in fossil fuel dependent regions - or improve air quality.
- Explore new ways and instruments like contract for differences, public procurement for green industrial products, standardisation and cooperation in order to enhance predictability for and support green investment and reduce risk for European industry.
- Reinvest ETS revenues swiftly. Revenues that are not planned for investment into the transition within 2 years should be transferred to the EUs own resources to be invested in the transition.

No money should go to fossil fuels including fossil gas and fossil hydrogen, nor nuclear energy. The funding should contribute towards achieving 100% sustainable renewable energy as soon as possible;

- Full transparency should be ensured in the selection and implementation of all projects and investments. Public consultations should be set up before decisions are made on the selection criteria and on all projects that will receive financial support;
- Create a new fund with a portion of revenues from shipping and aviation to finance cross-border trains in the EU.
- ETS revenues are also needed to ensure the EU delivers on international climate finance commitments, with particular attention to adaptation, resilience building and finance for loss and damage.

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30 [https://wwfint.awsassets.panda.org/downloads/strategic\\_spending\\_\\_\\_how\\_the\\_ets\\_can\\_fund\\_fair\\_climate\\_action\\_jan\\_2020\\_full\\_report.pdf](https://wwfint.awsassets.panda.org/downloads/strategic_spending___how_the_ets_can_fund_fair_climate_action_jan_2020_full_report.pdf)



## **CARBON BORDER ADJUSTMENT MECHANISM**

As part of the "Fit for 55 Package", the Commission will also propose the introduction of a WTO-compatible Carbon Border Adjustment Mechanism (CBAM). For the Greens/EFA group, carbon border adjustment is key to ensure that we do not only address emissions linked to the EU industry and power sector, but also tackle emissions embedded in our international trade/imports (consumption-based emissions). Exporters to Europe will have to pay the same price for GHG emissions as heavy industry in Europe does under ETS. This way both EU products and imports are faced with a similar carbon price, thereby incentivising climate action both within the Union and by our trading partners. The development of CBAM and ETS are strongly intertwined and therefore the CBAM is dependent on an ambitious revision of ETS and vice versa. Here are our key demands for CBAM:

### **The Greens/EFA group therefore demands that:**

- CBAM should start as of 2023, for sectors like cement, steel, aluminium, chemicals, fertilisers, but also the power sector. Price of CBAM should mirror price of the EU ETS, but through a separate pool of allowances ('mirror' ETS);
- The introduction of CBAM should gradually but rapidly replace (by 2026 at the latest) current carbon leakage provisions. During the transition period, it shall not lead to double protection for EU industry by applying a simple principle whereby one tonne of carbon cannot be protected twice.
- CBAM must have a clear climate impact and must be WTO-compatible. Any form of potential export support should be transparent, proportionate and not lead to any kind of competitive advantages for EU exporting industries in third countries, and it should be strictly limited to the most efficient installations so as to maintain incentives for emissions reduction for exporting companies;
- The revenues from CBAM - 5-14 billion EU per year - should be recycled towards climate action, both within and outside the EU;



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*Jason Blackeye (cover)*



**THE GREENS/EFA**  
in the European Parliament

60 rue Wiertz/Wiertzstraat 60  
1047 Brussels, Belgium  
[www.greens-efa.eu](http://www.greens-efa.eu)  
[contactgreens@ep.europa.eu](mailto:contactgreens@ep.europa.eu)