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**SENSITIVE\***

**COMMISSION STAFF WORKING DOCUMENT**

**EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT**

*Accompanying the document*

**Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directive 2003/87/EC and Decision (EU) 2015/1814 to strengthen the EU Emissions Trading System and extend it in line with the Union's increased climate ambition for 2030**

[Mandatory element]

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<b>Executive Summary Sheet</b>
Impact assessment accompanying the proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC and Decision (EU) 2015/1814 to strengthen the EU Emissions Trading System and extend it in line with the Union's increased climate ambition for 2030
<b>A. Need for action</b>
<b>What is the problem and why is it a problem at EU level?</b>
There are three types of problems. First, those associated with the need to strengthen the existing EU Emissions Trading System (ETS) in a commensurate way with the increased net greenhouse gas emissions reduction target by 2030, compared to 1990, of at least 55%, while avoiding supply/demand imbalances. Second, certain sectors contribute insufficiently to the achievement the increased target. Finally, both the required strengthening of the existing ETS and the possible expansion of emissions trading to additional sectors will require increased investment and greater capacity to address the distribution of impacts of emission reduction measures, while funds remain limited.
<b>What should be achieved?</b>
The objective is to revise the ETS in a cost-effective and coherent way in line with the increased climate target, while taking into account the need for a just transition and the need for all sectors to contribute to the EU climate efforts.
<b>What is the value added of action at the EU level (subsidiarity)?</b>
Climate change is a transboundary problem. As a carbon market, the ETS incentivises emission reductions by the most cost-efficient solutions first across the activities and countries it covers, achieving greater efficiency by virtue of its scale. Implementing a similar measure nationally would result in smaller, fragmented carbon markets, risking distortions of competition and likely lead to higher overall abatement costs. The same logic holds for the extension of carbon pricing to new sectors.
<b>B. Solutions</b>
<b>What are the various options to achieve the objectives? Is there a preferred option or not? If not, why?</b>
A key element is the strengthening of the existing ETS to increase its ambition in line with the net at least -55% 2030 target. The options differ in when the linear reduction factor is tightened and if the tightening starts from the current cap trajectory or from a new basis. Any of the options would be effective and efficient to achieve the 2030 objective. The choice between the different ETS strengthening options and related packages with other options, e.g. on the Market Stability Reserve, remains therefore a political one. There is a need for a more targeted protection against the risk of carbon leakage, which could take the the form of strengthened benchmarks for free allocation. There are four main options to extend the climate policy framework to maritime transport: integration in the current ETS, possibly combined with a carbon intensity standard, a separate ETS and an emission levy. The preferred option is the integration in the current ETS, which could cover emissions from intra-EEA voyages or, depending on political choices, could also extend further, to include half of the emissions from extra-EEA voyages in the form of incoming voyages. For the possible extension to other sectors, the transitional set up of a separate ETS either for buildings and transport or for all fossil fuel combustion emissions are the two main options retained, complementing other policies, which target non-price related barriers and specific national

circumstances. The scope covering only buildings and road transport has clear benefits in terms of economic efficiency compared to an extension to all fossil fuel combustion, notably as it would avoid the creation of a new carbon leakage risk protection regime. There is a need to support low carbon technologies by increasing the Innovation Fund. However, the selected amount is ultimately a political choice which is linked with the decisions on existing ETS ambition and with the decision on whether or not to extend the ETS to new sectors. The solidarity provisions to address distributional challenges between Member States could be further developed, without prejudice to an ETS contribution to new EU own resources. All indications of the preferred measures are to be considered preliminary as preserving overall effectiveness, efficiency and coherence may require adjustments as the final “Fit for 55” policy package takes shape.

### **What are different stakeholders' views? Who supports which option?**

Stakeholders responding to the public consultation support the strengthening of the existing ETS to increase its ambition in line with the new 2030 target. A large majority of respondents agrees with the Market Stability Reserve as instrument and is in favour of amending the carbon leakage framework, but with mixed views on the different policy options. As regards a possible extension to other sectors, there is some support to include maritime transport in the current ETS, while respondents, and notably private sector actors, prefer the set up of a separate ETS, complemented by other policies, either for buildings and transport or for all fossil fuel combustion emissions. Private sector actors, trade unions and NGOs are rather sceptical on an integration in the existing ETS, while citizens and academia tend to favour it. A large majority of respondents expressed support for an increase in the Innovation Fund.

### **C. Impacts of the preferred option**

#### **What are the benefits of the preferred option (if any, otherwise of main ones)?**

All options would ensure achieving the necessary additional emission reductions to achieve -55% by 2030 compared to 1990 in a cost-efficient way and with more certainty than other instruments. The annual revenues could be used to increase the Innovation and Modernisation Funds, foster low carbon investments including in industry, address distributional impact between Member States, social impacts on households and contribute to EU own resources. The strengthened and extended ETS contributes to avoided health damages through reduced air pollution of EUR 17.6 to 35.2 billion in 2030 and to improved energy security. The Impact Assessment for the Communication on Stepping up Europe’s 2030 Climate Ambition (2030 Impact Assessment)<sup>1</sup> has quantified benefits for growth and jobs.

#### **What are the costs of the preferred option (if any, otherwise of main ones)?**

The projected 2030 carbon prices of €50 to 85, assuming strong complementary Green Deal policies of various strength as well as the anticipation of future decarbonisation requirements, increase average fuel prices for industry and households. Relative increases are stronger for buildings than for transport and industry. If cost-efficient investments are realised, then the share of fuel expenses for buildings in household expenditures would not increase and could decrease for low income households by up to 0.3 percentage points. However increases of cost-effective annual capital costs could be double in lower income households, increasing by 0.7 to 1.4 percentage points of consumption expenditures. For vulnerable households this raises an affordability issue. The analysis in the 2030 Impact Assessment has shown that distributional measures could compensate for that. The analysis also quantified negative sectoral activity and employment impacts in particular in fossil fuel extraction and to a limited extent in

<sup>1</sup> SWD(2020)176

some fossil fuel intensive industries.
<b>What are the impacts on SMEs and competitiveness?</b>
Competitiveness impacts for industry are mitigated by more targeted free allocation. For most options the need for an application of the Cross-Sectoral Correction Factor reducing free allocation for all beneficiaries is limited. Small emitters, still falling under the scope of the ETS (albeit not necessarily SMEs) can still be exempted from the existing ETS if equivalent measures are taken by respective Member State. The envisaged extension to maritime would build on existing monitoring, reporting and verification mechanisms that exempt small ships. The new ETS for other sectors would apply upstream, building on existing provisions regulating tax warehouses or fuel suppliers. The additional administrative costs would be moderate for gas and oil. For coal, which is only used in a few Member States for heating, administrative costs would be higher, as it is often less regulated and there are many small suppliers.
<b>Will there be significant impacts on national budgets and administrations?</b>
Under the existing ETS, most of the auctioning revenues accrue to Member States. There are potentially significant positive impacts on national budgets if there will be a new ETS for road transport and buildings. The direct impact on national budgets also depends on to which extent additional revenues will be directed to EU own resources. For the existing ETS, there are no additional administrative impacts on national administrations. The impacts of the extensions/new ETS could be limited by using the same administrative infrastructures.
<b>Will there be other significant impacts?</b>
Depending on its geographical scope, an extension of EU climate policies to maritime transport could impact third countries and trade and investment flows.
<b>Proportionality?</b>
All main policy options are proportional to what is necessary to achieve the at least -55% emission reduction objective. They do so in an as cost-efficient way as possible.
<b>D. Follow up</b>
<b>When will the policy be reviewed?</b>
As currently the case, a regular review will be foreseen in the legislation. It will be aligned with the review of other legislation such as in the proposal for the Effort Sharing Regulation and the CO <sub>2</sub> standards for cars and vans.