**Questions for stakeholder consultation on revision of the EU Emission Trading System (EU ETS) Directive**

In red: EGEC responses.

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**Introduction**

On 24 October 2014, the European Council agreed on the 2030 framework for climate and energy\(^1\), including a binding domestic target for reducing greenhouse gas (GHG) emissions of at least 40% in 2030 as compared to 1990. To meet this target, the European Council agreed that the emissions in the EU Emission Trading System should be reduced, compared to 2005, by 43%. A reformed EU ETS remains the main instrument to achieve the emission reduction target. The cap will decline based on an annual linear reduction factor of 2.2% (instead of the current 1.74%) from 2021 onwards, to achieve the necessary emission reductions in the EU ETS. The European Council furthermore gave strategic guidance on several issues regarding the implementation of the emission reduction target, namely free allocation to industry, the establishment of a modernisation and an innovation fund, optional free allocation of allowances to modernise electricity generation in some Member States.

The strategic guidance given by European leaders on these elements will be translated into a legislative proposal to revise the EU ETS for the period post-2020. This constitutes an important part of the work on the achievement of a resilient Energy Union with a forward looking climate change policy, which has been identified as a key policy area in President Juncker's political guidelines for the new Commission.

The purpose of the present stakeholder consultation is to gather stakeholders’ views on these elements. This consultation focuses on issues not yet addressed in the consultations recently conducted for the 2030 Impact Assessment\(^2\), the Impact Assessment for the carbon leakage list for 2015-2019\(^3\) and the consultation conducted on post-2020 carbon leakage provisions\(^4\).

In order to take stock of the EU ETS\(^5\) as a policy measure, this consultation also contains questions concerning the general evaluation of this policy measure. The questionnaire consists of 7 chapters. You are invited to answer questions on the chapters which are relevant to you.


\(^3\) [http://ec.europa.eu/clima/policies/2030/documentation_en.htm](http://ec.europa.eu/clima/policies/2030/documentation_en.htm)


\(^5\) Established by Directive 2003/87/EC
0. Registration

0.1. What is your profile?

Trade association representing businesses

0.2. Please enter the name of your business/organisation/association etc.: (maximum 500 characters) European Geothermal Energy Council

0.3. Please enter your contact details (address, telephone, email):

0.4. If relevant, please state if the sector/industry you represent falls under the scope of the EU ETS:

b) Partly (Yes: electricity generation and district heating; Partly: manufacturing; No: Service providers)

0.5. If relevant, please state what sector your represent:

0.6. The results of this stakeholder consultation will be published unless stated otherwise. Can we include your replies in the publication?

a) yes

0.7 Register ID number (if you/your organisation is registered in the Transparency register): 11458103335-07

1. Free allocation and addressing the risk of carbon leakage

The European Council has concluded that free allocation to prevent the risk of carbon leakage should not expire as foreseen in the current legislation, but should continue also after 2020 as long as there are no comparable efforts to reduce emissions in other major economies.

Extensive stakeholder consultation was already carried out on the post-2020 carbon leakage provisions, as well as on aspects related to innovation support. The process included three full-day stakeholder meetings (June, July and September 2014) and a written consultation conducted for 12 weeks (8 May – 31 July, 2014). The written consultation covered 23 multiple choice questions with space for motivations, and a question allowing respondents to bring up any other issue they felt was important or insufficiently covered.

The documents and minutes of the meetings, as well as the submissions and the analysis thereof in the case of the written consultation, are available on the Commission website.

Information from the stakeholder meetings:
http://ec.europa.eu/clima/events/articles/0090_en.htm
http://ec.europa.eu/clima/events/articles/0095_en.htm
http://ec.europa.eu/clima/events/articles/0097_en.htm

Replies and summary of the written consultation:
http://ec.europa.eu/clima/consultations/articles/0023_en.htm

The results of the above mentioned public consultation are being taken into account in the preparation of the legislative proposal. In order to reduce the administrative burden for stakeholders and the Commission, the present consultation focuses on issues not already covered in this recently finalised public consultation. Respondents are nevertheless invited to add to the replies provided in the earlier consultations if deemed necessary in the light of the conclusions of the European Council in this area.

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?

The large over-allocation of free allowances has compromised the ETS, and needs to be fixed. In the long run, free allocation must be abandoned, if we want to set a reasonably fair price on GHG emissions. In the short run, it can be accepted for sectors with a serious risk for carbon leakage and not for other sectors such as district heating or cogeneration, where competitive carbon-free alternatives exist.

Distributing free allowances according to benchmarks is a preferred method. From 2021 onwards, the benchmarks should be set at the level of the best available (in terms of greenhouse gas emission performance) product on the global market. Benchmarks should then be revised at regular intervals according to technological advancement, and tightened to promote improvements in technology and energy efficiency.

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?

As mentioned above, the objective should be to phase-out free allowances so that all carbon emissions are priced. In this regard, it is worth highlighting that for sectors outside ETS, including for heat installations below 20 MW, this can be done through a mandatory tax covering all GHG emissions.

In the short-term, free allocation should only be given for direct costs, while compensation for indirect costs should be avoided.
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?

If a sector can pass through the carbon cost to customers it should not be eligible for free allocations. The purpose of the ETS is indeed to make products and services with high embedded carbon content more costly. In this regard, the most reliable way of avoiding windfall profits is the full auctioning of all emission allowances.

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?

Carbon leakage is mainly due to the international context and to the poor climate policies of EU’s major competitors. However, many more countries are setting a carbon market. Therefore a carbon leakage list and a limited number of free allocations to sectors facing global competition should be phased-out as soon as EU’s competitors will have a carbon market in operation.

2. Innovation fund

The European Council has concluded that 400 million allowances in 2021 to 2030 should be dedicated for setting up an innovation fund to support demonstration projects of innovative renewable energy technologies, carbon capture and storage (CCS) as well as low carbon innovation in industrial sectors. To make this fund operational, a legal basis has to be created in the EU ETS Directive while further implementation modalities can be set out in secondary legislation. The work can build on the experience with the existing “NER300” programme which made available 300 million allowances for CCS and innovative renewable energy technologies.

With regard to establishing a legal basis for the innovation fund as part of the revision of the EU ETS Directive, the Commission seeks feedback on the following questions:

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.

The NER300 is providing a much needed boost to the demonstration of innovative geothermal technologies. However, the experience from the European Geothermal Council’s members in the NER300 programme suggests that there is much room for improvement as the NER300 is not solving the essential problem for the further development of geothermal technologies.

Indeed, geothermal projects are not only capital intensive and take several years for exploration and drilling, but also have a very specific risk profile, mainly due the geological risk not to find adequate resources. Therefore, only after careful exploration and the first drilling can developers have the certainty to successfully realise their project.

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6 http://ec.europa.eu/clima/policies/lowcarbon/ner300/index_en.htm
In order for the NER300 and its successor to optimally serve the purpose of demonstrating innovative geothermal technologies, the European Geothermal Energy Council strongly recommends the following:

- With current rules, the actual implementation of an EGS project heavily depends on the Member State and project developer’s capability to cover the geological risk. Under these conditions, the two-year deadline to achieve the key milestones was indeed too challenging and therefore revised.

- **Upfront funding should be made available as soon as possible.** One of the main drawbacks of the current NER design is indeed that the disbursement of funding is only based on amount of energy produced.

- **The European Union should really bear part of the project risks in the form of non-repayable grants.** In case a project failed to enter into operation for technical reasons which cannot be directly attributable to the project developers, the EU should bear these costs. This is the only way to alleviate the very high risks of pilot projects.

- NER 300 was open to electricity and cogeneration, limiting the options for demonstrating innovative renewable technologies for industrial processes. Therefore, *heat only projects, notably for industrial process, should be eligible under NER400.*

- **The European Commission should study the possibility to co-fund a pan-European geothermal risk insurance scheme.** Governance and structure of such a scheme have already been assessed. Public support has been instrumental also for the offtake of geothermal energy in resource-rich countries such as Iceland. A major effort to introduce EGS and low temperature geothermal could create a substantial base-load and flexible renewable power and heat production, as geothermal energy is available independently from weather conditions.

Therefore, in the light of the new NER 400, EGEC calls on the Commission to take the necessary steps for the adjustment of the current programme and to use the lessons learnt to boost even further the development of geothermal and other renewable energy technologies.

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.

Tailoring should as much as possible be avoided. In principle the same criteria should apply. All technologies should be evaluated according to their potential to reduce carbon dioxide emissions as well as to their medium and long term cost- reduction potential. The purpose is to speed up the commercialisation of proven innovative and sustainable 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?
It is important that the Innovation Fund has a fair geographical coverage and maintains its objective to test innovative technologies and to reduce their cost.

3. Modernisation fund

The European Council has concluded that 2% of the total EU ETS allowances in 2021 to 2030 should be dedicated to address the particularly high investment needs for Member States with GDP per capita below 60% of the EU average. The aim is to improve energy efficiency and to modernise the energy systems of the benefitting Member States. The fund should be managed by the beneficiary Member States, with the involvement of the European Investment Bank (EIB) in the selection of projects. To make this fund operational, a legal basis has to be created (in the EU ETS Directive), while further implementation modalities can be set out in secondary legislation.

With regard to establishing a legal basis for the modernisation fund as part of the revision of the EU ETS Directive, the Commission seeks feedback on the following questions:

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 European Geothermal Energy Council believes that general criteria should be defined at EU level. Approval and implementation of projects should be done at national and regional level. Member States should then report back to the European Commission and the EIB.

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?

The modernisation fund should support projects in accordance with EU energy and climate objectives. Post-2020 financial support for the transformation of lower income Member States’ energy systems must be conditional on these countries pursuing policies designed to attract renewable energy and energy efficiency investment, including the integration of renewable heat technologies in large building renovation and the modernisation of district heating systems,

Additionally, the fund must be conditional on these countries phasing fossil fuel subsidies out as well as the full timely implementing the revised legislation within the EU’s 2030 climate and energy framework. Lastly, fossil fuels projects must be ineligible for support.

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 strict criteria for the selection of projects. They should be transparent and need to be followed by an open and objective award process. Overall, the criteria should prioritise energy
efficiency and the replacement of fossil fuel by renewable energy, taking into account the societal benefits, system costs as well as the specificities of small-scale projects, including in the building sector.

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?

For this specific case, overlapping funding should be avoided.

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)?

As part of the governance process Member States should be required to submit plans covering renewable energy policies for each technology, for energy efficiency and modernization. In this context it is also worth highlighting that the building sector must be considered an integrated part of the energy system.

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

Yes. These criteria, however, should be taken into account the different risk profile of certain renewable energy technologies. Additionally, they should take into account the challenge of attracting small-scale financing.

4. Free allocation to promote investments for modernising the energy sector

The conclusions of the European Council provide for the continuation after 2020 of the mechanism foreseen in Article 10c of the EU ETS Directive, which allows some Member States to opt to hand out free allowances to power plants in order to promote investments for modernising the energy sector. The current Article 10c modalities, including transparency, should be improved to promote investments modernising the energy sector, while avoiding distortions of the internal energy market.

With a view to reviewing and improving the current modalities as part of the revisions to the EU ETS Directive, the Commission seeks feedback on the following questions:

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

EGEC is very concerned that the continuation transitional free allocation for power generators will jeopardise the EU’s long-term decarbonisation by enabling windfall profits and distorting competition.
Additionally, this will hamper the completion of the EU Internal Energy Market. For the post-2020 period, therefore, the preferred approach should be to ensure power producers in all EU Member States buy 100% of their allowances at auction.

As mentioned above, the modernisation fund should prioritise efficient district heating and high-efficient CHP plants, including their infrastructure as well as the large-scale modernisation of the EU building stock.

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?

In this context, funding overlapping should not be allowed. It is also worth highlighting that project of common interest should not cover natural gas infrastructure so as to make this investment compatible with EU’s decarbonisation targets.

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)?

N/A

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)

N/A

4.5 Should there be priorities guiding the Member States in the selection of areas to be supported? 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?
(i) Interconnectors
(ii) Smart Grids
(iii) Super-critical coal
(iv) Gas

**(v) Renewable energy**
(vi) Energy storage

**(vii) Energy efficiency**
(viii) Other (please elaborate)

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?

N/A

5. SME's / regulatory fees / other

In order to allow taking stock of the EU ETS aspects beyond those examined by the European Council, respondents are also invited to provide feedback on certain other questions.

The Commission ensures that better regulation principles govern all of the policy work, including that the specificities of small and medium sized enterprise (SMEs) are taken into due consideration. Member States can exclude certain small installations from the EU ETS in the current trading period (2013-2020) if taxation or other equivalent measures are in place that will cut their emissions. If such a possibility was to be reviewed, a legal basis would have to be created in the EU ETS Directive.

The accurate accounting of all emission allowances issued is assured by a single Union Registry with strong security measures. The operations were centralised in a single Registry operated by the Commission, following a revision of the ETS Directive in 2009. This has replaced Member States' national Registries. Despite the considerable resources from the EU budget required for maintaining the EU Registry, as does supporting work on auctioning, the Commission does not have the possibility to charge any fees. However, Member States administrators may still charge Registry fees to account holders administered by them. There are discrepancies in fees across different Member States.

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.

N/A

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?
All GHG emissions within the European Economic Area should be paid according to “polluter pays principle”. This can either be under the EU ETS or by a carbon tax. In other words, it is crucial that every GHG emitting installation should pay for emissions either within the ETS or with a carbon dioxide tax.

For administrative reasons, combustion installations smaller than 20 MW should continue to be excluded from the EU ETS. However, in order to avoid market distortions between small and large scale installations as well as to incentivise GHG emission reductions across the economy, the ETS Directive should require Member States to impose a carbon tax to installations not covered by the ETS, including small-scale heating installations. This tax would be a sufficient incentive to reduce emissions and will avoid market distortions.

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?

N/A

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

N/A

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?

The current reporting is a step in the right direction to ensure that Member States deliver on their commitment of using at least 50% of ETS auctioning revenues for climate-related purposes. The European Commission should work closely with member states to ensure that all ETS auctioning revenues are earmarked for supporting further climate policies.

6. Overall 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?

Article 1 of the ETS Directive provides that the objective of the system to promote reductions of GHG emissions - in the sectors covered by the system - in a cost-effective and economically efficient manner. But the ETS alone cannot deliver adequate emission reductions in the medium term and in line with the necessary reductions according to the IPCC (by 80-95% by 2050 compared to 1990 levels).

Economic efficiency, however, should be evaluated taking into consideration long-term objectives. So far, the price on emissions has been low and unstable. This is proof that the system has not been fully efficient. Therefore the EU ETS should include the objective to incentivise innovation in renewable energy technologies and for doing this there is a need to strike an optimal balance between the carbon price signal, the renewable energy investment that is needed now, and the investments that will be needed in the future. The market stability reserve is a step in the right direction. Yet for a fully functioning ETS there is a need to phase-out free allowances, notably for the electricity and the heat sectors, where competitive alternatives are and will be even further be available in the future.

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?

The strength of the ETS is that it is a EU-wide system aiming to reduce GHG emissions and to internalise their external costs. However, the framework has not delivered mainly because of over allocation of free allowances. The European Geothermal Energy Council, however, strongly believes that “fixing” the EU-ETS is important to provide a carbon signal but this cannot be seen as the only instrument to promote the no-regrets options identified in the Energy Roadmap 2050, namely more renewable energy, more energy efficiency, and smart infrastructures.

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?

N/A
6.4 How well does the EU ETS Directive fit with other relevant EU legislation?

The ETS directive fits well with the EU legislation with which it was developed, namely the directives aiming to increase energy efficiency and the share of renewable energy in the electricity and heating sector. However, regarding the heat sector there is a gap for small-scale installations below 20 MW. In order to avoid market distortions as well as to incentivise GHG emission reductions across the economic sectors, the ETS Directive should require Member States to impose a carbon tax on installations not covered by the ETS, including small-scale heating installations. This tax would complement the EU ETS Directive and avoid market distortions.

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?

Because industry works across Europe, when possible it is important to have a system aiming to internalise the cost of GHG emissions at a common minimal level in the whole European Economic Area.

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

The ETS is a valuable instrument and could potentially deliver meaningful results if it will effectively become an economic instrument rather than a political instrument as it has been so far. In other words, the EU ETS should create benefits for the society and not please vested interests. It is of utmost importance that the system is tightened in a way that the price level of allowances increases. In order to do so, the system must urgently phase-out free allowances and be based as much as possible on auctioning.