



Brussels,
D(2015)

Opinion

Title **DG CLIMA– Impact Assessment on a Proposal for a Directive of the European Parliament and the Council to amend Directive 2003/87/EC establishing a scheme for greenhouse gas emission allowance trading within the Community**

(draft version of 24 April 2015)*

(A) Context

Building on the Commission's Communication on a policy framework for climate and energy in the period from 2020 to 2030 and the accompanying Impact Assessment, the European Council agreed on the 2030 framework in October 2014, including a binding domestic reduction of GHG emissions of at least 40% in 2030 as compared to 1990. This implies emission reduction in sectors falling under the EU Emissions Trading System (ETS) amounting to 43% by 2030 compared to 2005. Furthermore, the European Council gave strategic guidance on several issues regarding the implementation of the emission reduction target, namely on a linear emission reduction factor, free allocation of emission allowances to industry, the establishment of a modernisation fund, reserving 400 million allowances for carbon capture and storage (CCS), innovative renewable and low carbon industrial projects (NER400), and optional free allocation of allowances to modernise electricity generation in some Member States. This impact assessment focuses on possible modalities for free allocation, addressing the risk of carbon leakage, as well as on options for making a modernisation fund and NER 400 facility operational.

(B) Overall opinion: NEGATIVE

The Board gives a negative opinion. A clearer presentation and explanation of the options and their impacts is required, in particular, for the sectors most affected. The readability of the report also requires significant improvement.

The IA Report should clarify the following key aspects:

- 1) What method was used to determine the choice of values for carbon leakage criteria, the percentage of free allocation, as well as the funding rates and conditions for award for the Innovation fund?**
- 2) The impacts on the various industrial sectors associated with the different options for the free allocation of allowances in relation to carbon leakage. How are the impacts likely to change compared to the current legal regime up to 2020?**

* Note that this opinion concerns a draft impact assessment report which may differ from the one adopted.

3) The coherence between the Modernisation and Innovation funds and other EU funding mechanisms. In addition, what are the options and foreseen impacts of the funds beyond the governance aspects?

Once revised, the IA must be resubmitted to the Board on which it will issue a new opinion.

(C) Main recommendations for improvements

(1) Clarify the methodology. The report should explain how the specific values for the carbon leakage criteria (trade intensity and emission intensity) as well as the particular percentages for free allocation for low, medium, high or very high carbon leakage risk categories were chosen. When defining the carbon leakage risk categories, the report should clarify why a relationship between emission intensity and trade intensity is assumed. Moreover, when classifying sectors in different carbon leakage risk categories, the report should explain how the use of the proposed carbon leakage criteria compares to sectors' ability to pass on costs linked to the carbon market. The coherence of the arguments presented should be improved, while at the same time addressing the differences in ranges of cost passed through, where relevant. The report should clarify if any of the option packages consider using unallocated allowances for addressing the risk of carbon leakage and what the implications would be of this.

(2) Clarify the modelling assumptions. The report should better explain the underlying methodology for modelling of employment effects and energy prices for households as well as clarify if the assumptions used for the 2030 climate and energy package impact assessment (e.g. regarding oil price) are still valid for this report.

(3) Better present the impacts and the trade-offs between the options. The report should more clearly explain and illustrate the impacts on the sectors most affected by the changes in the rules for free allocation of allowances, for example, by explaining how the different carbon leakage criteria proposed would affect them compared to the situation today. Where possible, sectoral impacts should be complemented with quantitative assessments relating to possible cost increases or savings due to changes in the free allocation. In doing so, the report should present and discuss the value and/or use made of different evidence sources such as cumulative cost assessments conducted by Commission services for individual sectors as well evidence generated by industry association themselves. Furthermore, the report should better link the competitiveness assessment to the analysis of impacts for the individual sectors by building in a more comprehensive manner on available studies, such as the OECD study on the impact of carbon pricing on competitiveness. It should explain in more depth the foreseen social impacts and specify if any sector would be particularly affected (e.g. employment, costs for district heating). When summarising the impacts of different options, the report should clearly present the trade-offs for sectors concerned and clarify if the options do not introduce additional distortions and complexity. In addition, it should explain if changing any of the individual elements in option packages for free allocation would have significant impact on the sectors concerned and on carbon leakage risks. Furthermore, the report should clarify how different stakeholders views and arguments have been weighed in the options assessment (national authorities, power sector, energy intensive industries, NGOs, etc.), in particular with regards to free allocation of allowances.

(4) Clarify the coherence with other EU funding mechanisms. The report should explain how the proposed low-carbon funding mechanisms complement other EU funding mechanisms, which serve a similar purpose. As the options considered for the Innovation and the Modernization funds present only general aspects of governance, the report should clarify whether the details of the implementation of those funds will be subject to future impact assessment. If this is not the case, it should further elaborate the type of projects funded and support provided (grants, financial instruments or mix of both), including possible leverage effects, as this seems closely linked to the governance structure.

Some more technical comments have been transmitted directly to the author DG and are expected to be incorporated in the final version of the impact assessment report.

(D) Procedure and presentation

The report should be simplified and shortened to make it more relevant for decision making. For example, detailed screening of the options can be simplified. The drafting should be made more understandable for a non-specialist reader. For example, a brief description of the EU ETS and how the choices considered by this initiative relate to its original objectives could be included in the introduction.

(E) IAB scrutiny process

Reference number	2015/CLIMA/001
External expertise used	No
Date of IAB meeting	20 May 2015