IFIEC Europe's response to

EU Inception Impact Assessment:
Climate change – updating the EU emissions trading system (ETS)

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IFIEC welcomes the opportunity to participate in the consultation on the roadmap to update the EU Emissions Trading Scheme and supports the EU Commission's discussion on an improved emissions trading scheme.

In order to meet possible increased greenhouse gas targets, the **EU needs a competitive energy-intensive industry to drive the transition** and that continues to develop sustainable innovations, products and jobs in Europe. It must be ensured that the planned reform of emissions trading does not lead to additional cost increase for industrial installations in Europe, and thus to a decrease in competitiveness of the European industry. This would lead to the departure of production facilities to non-European countries, so-called carbon leakage.

IFIEC therefore emphasizes the **importance of continuing carbon leakage protection** for European industry. In this context, existing measures such as the free EU ETS allowances and indirect cost compensation should remain and even be reinforced in line with the new climate targets.
The Inception Impact Assessment states that, in order to achieve the planned increase in the EU's climate targets related to greenhouse gas emissions by 2030, the linear reduction factor together with the level of carbon leakage protection might be modified. This option for a more rapidly shortage of allowances will lead to an increase in CO2 prices, which will put additional pressure on the competitiveness of European industries. As global competitors do not incur these costs, the risk of carbon leakage increases.
Future free allocation of emission allowances must be modified in parallel in order to ensure adequate protection against carbon leakage. The European Commission should therefore assess all possible options to increase the level of protection by free allocation or to complement free allocation with additional policy instruments to ensure effective carbon leakage protection throughout the fourth trading phase. (IFIEC has presented its view on how to increase carbon leakage protection in our response to the public consultation on the Carbon Border Adjustment Mechanism.)

Specifically, the level of carbon leakage protection is currently linked to the overall cap. This overall cap decreases based on the esteemed potential for reduction of both the energy-intensive and the power sector. Since both sectors have highly differing estimations of potentials (25% for energy intensive industries .vs. 70% for the power sector), the carbon leakage protection level is decreasing much quicker than energy intensive sector's emissions can be reduced.
IFIEC asks to **decouple the level of carbon leakage protection from the overall ETS cap** and to match it to the economic protection needs of the energy-intensive sectors.

With regards to adjusting the Market Stability Reserve (MSR) and the idea of a one-off reduction of the ETS cap, IFIEC would like to point out that this would change again the ETS framework and will render the market for allowances in Europe unpredictable. Besides, it will decrease the necessary flexibility in the ETS to cope with fluctuating economic cycles. Therefore, it might lead to high costs for the energy-intensive sector in particular. Again, it must be stressed that reliable legal and economic framework conditions are of the utmost importance for the energy-intensive industry in order to maintain international competitiveness while at the same time enabling investment in climate-friendly technologies. Moreover IFIEC proposes to **increase the outflow rate of the MSR and to avoid a one off reduction of the ETS cap** in order to make the ETS better fit for economic cycles.

When it comes to the option of extending emissions trading to maritime transport, it is important to **prevent inserting new sectors in the existing ETS**, that has to cope already with different sectors with different elasticities and risk on carbon leakage in one system.
Similarly, with regard to the potential option of extending emission trading to the 'buildings' and 'road transport' sectors, it must be noted that this may pose a risk to the EU ETS-sector. While a significant reduction in CO2 emissions has already been achieved in the EU ETS-sector over an extended period of time, transport and building sectors fall behind the targets. Low price elasticities in the building and transport sectors, together with long investment cycles, indicate that market-based climate protection instruments such as carbon pricing are likely to have less impact than in other sectors and not to the same extend as in the existing ETS. This would lead to a delay in emission reduction for non-ETS sectors on the one hand, but also to a disproportional increase of financial burden for the ETS sector on the other hand. The consequence will be a significant imbalance in CO2 costs and avoidance measures and a further distortion of competition.

Taking this in consideration, IFIEC asks the Commission to **thoroughly assess and substantiate the economic impact of revising the ETS Directive**. As explained above, the costs for energy-intensive industries are likely to rise. This will be reflected in higher CO2-costs, as well as in higher total energy costs (driven by energy prices, grid tariffs and taxation). In the Inception Impact Assessment, the Commission claims that this initiative would likely to contribute to higher investment and growth in the ETS, improve energy security and reduce the energy imports bill. But, the Impact Assessment does not include any substantiation. Positive sectoral impacts are highly dependable on global action. As for the energy import bill, a total assessment of the expected total final energy demand (including technologies leading to more energy demand) was not done. Sufficient, secure and affordable low carbon energy sources need to be available for energy-intensive companies to successfully invest in CO2 avoidance. This requires infrastructure development and likely imports into the EU at a large scale.

A robust and consistent GHG accounting is necessary. Therefore ETS should be adapted in order to **recognize the avoided emissions by implementation of CCU and the created sinks by storing biogenic CO2**.

In conclusion, IFIEC re-emphasizes that secure legal and economic framework conditions with effective and adequate carbon leakage protection are crucial for the energy-intensive industry in order to maintain international competitiveness and at the same time enable the transformation towards a climate-neutral economy.

About IFIEC Europe

IFIEC Europe represents 13 national European associations that comprise - on a cross-sectoral level - those industrial sectors for which energy is a significant component of production costs. IFIEC´s membership represents a diverse set of industries including: aluminium, automobile, brewing, cement, chemical, copper, fertilizer, food, glass, industrial gases, metals, paper, pharmaceutical, plastics and steel.

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