

REVISION OF THE EU EMISSION TRADING SYSTEM (ETS) - Q2 2021

[EXPECTED ARRIVALS]

> FIT FOR 55 PACKAGE UNDER THE EUROPEAN GREEN DEAL

CONTENT

On 14 July, as part of the 'Fit for 55' package, the Commission published a legislative proposal for a revision of the EU Emissions Trading System (ETS), to align it with the target of a 55 % reduction of EU net greenhouse gas (GHG) emissions by 2030, compared to 1990 levels.

The EU ETS was launched in 2005 and covers about 45 % of EU greenhouse gas emissions. The latest revision of the EU ETS Directive, adopted in 2018, sets the total quantity of emission allowances for phase 4 (2021-2030), in line with the previous EU emission reduction target (40 % reduction below 1990 levels by 2030).

The Commission proposal to amend Directive 2003/87/EC concerns the ongoing phase 4 of the ETS (2021-2030). It consists of five main elements:

1. a reduced cap and more ambitious linear reduction factor for GHG emissions,
2. revised rules for free allocation of allowances and the market stability reserve
3. extension of the ETS to maritime transport
4. a separate new ETS for buildings and road transport
5. increase of the Innovation and Modernisation Funds and new rules on use of ETS revenues

To align the EU ETS Directive with the increased GHG emission reduction targets set in the European Climate Law, the Commission is proposing to reduce the emissions from the EU ETS sectors (including the extension to the maritime sector) by 61 % by 2030, compared to 2005 levels. To achieve this target, the proposal increases the linear emissions reduction factor from 2.2 % per year to 4.2 %.

The proposal would extend the EU ETS to cover CO₂ emissions from maritime transport, specifically from large ships above 5 000 gross tonnage. The requirement to surrender allowances would be gradually phased-in during 2023-2025.

Protection against carbon leakage will still be in place through allocation of free allowances. However, the number of the free allowances will gradually be reduced with a decreasing emissions cap and the proposed introduction of a Carbon Border Adjustment Mechanism (CBAM, see separate file).

Decision (EU) 2015/1814 establishing the ETS market stability reserve (MSR) would be amended to enable a smoother intake of allowances to the reserve. From 2023, allowances above the level of auction volumes of the previous year would be invalidated, and the number of allowances in the MSR would be limited to 400 million.

A separate self-standing emissions trading system for fuel distribution for road transport and buildings (ETS II) would be established starting from 2025. The regulated entities (fuel distributors) would need to report the amount of the fuels placed on the market starting from 2024. From 2026, they would have to surrender a corresponding amount of allowances, based. The cap on emissions would be set in 2026 and would gradually decrease to amount to a 43 % reduction of emissions in 2030 compared to 2005 levels for these sectors. All allowances would be auctioned and none provided for free. Indirect social impacts from rising prices of road transport and heating fuels are addressed through a legislative proposal for a Social Climate Fund (see separate file).

The Commission presented separate legislative proposals for strengthening the ETS Market Stability Reserve and including aviation in the ETS (see separate files). In December 2021, the Commission presented a legislative proposal for a Council Decision amending the system of own resources of the European Union by adding new sources of revenue, including the EU ETS and the CBAM, complemented in March 2022 by a proposal for a Council Regulation on the methods and procedure for making available own resources based on ETS and CBAM.

On 18 May 2022, as part of the REPowerEU initiative, the Commission presented a legislative proposal that amends the EU ETS Directive and the MSR decision to auction €20 billion worth of allowances from the market stability reserve. The auction revenue would be made available to the Recovery and Resilience Facility.

The European Economic and Social Committee adopted an opinion (rapporteur: Stefan Back, Employers – Group I, Sweden) on the proposal on 8 December 2021. The European Committee of the Regions adopted an opinion entitled 'Making ETS and CBAM work for EU cities and regions' (rapporteur: Peter Kurz, PES, Germany) on 28 April 2022.

In the European Parliament, the proposal has been referred to the Committee on Environment, Public Health and Food Safety (ENVI). Peter Liese (EPP, Germany) was appointed as rapporteur and presented his draft report in January 2022. The ENVI Committee adopted its report on 17 May 2022. It was rejected in the June I plenary session, referred back to the Committee, and then adopted in the June II plenary. The adopted text aims to reduce GHG emissions in the ETS sectors by 63 % by 2030 and introduces a bonus-malus system to incentivise best-performers and innovation. It aims to raise the ambition for the maritime transport sector and establishes an Ocean Fund to support maritime decarbonisation. Free allowances in sectors covered by the CBAM should be phased

out between 2027 and 2032. The adopted text sets the starting date for the ETS II to 2024 for commercial buildings and road transport, while residential buildings and private road transport would be included from 2029.

In the Council, environment ministers held a first exchange on the 'Fit for 55' package on 20 July 2021. The Council adopted its general approach on 29 June 2022, maintaining the overall ambition proposed by the Commission.

Trilogues started in July 2022 and concluded with a provisional political agreement on 18 December 2022.

In the Council, Coreper endorsed the agreed text on 8 February 2023.

The ENVI Committee approved it on the same day. The file was split into two parts, with a separate file for the maritime transport aspects. The Parliament approved the files on 18 April 2023 (and the Council adopted them on 25 April 2023). They are now awaiting signature and publication in the Official Journal.

References:

- EP Legislative Observatory, [Procedure file on Revision of the EU Emissions Trading System](#), 2021/0211A(COD)
- EP Legislative Observatory, [Procedure file on Monitoring, reporting and verification of carbon dioxide emissions from maritime transport: inclusion of maritime transport activities in the EU ETS and of other greenhouse gases than CO₂](#), 2021/0211B(COD)
 - European Commission, [Proposal for a directive amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision \(EU\) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation \(EU\) 2015/757](#), COM/2021/551
 - European Commission, [Communication on 'Fit for 55': delivering the EU's 2030 climate target on the way to climate neutrality](#), COM/2021/550 final
 - [Directive \(EU\) 2018/410 of 14 March 2018 amending Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments, and Decision \(EU\) 2015/1814](#)
 - European Parliament, [Amendments adopted by the European Parliament on 22 June 2022 on the proposal for a directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision \(EU\) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation \(EU\) 2015/757 \(COM\(2021\)0551\)](#), 2021/0211(COD)
 - Council, [Fit for 55 package Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision \(EU\) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation \(EU\)](#)

- European Economic and Social Committee, [EESC opinion: Revision of the EU Emissions Trading System \(ETS\), including maritime transport and Market Stability Reserve](#), NAT/833-EESC-2021
- European Committee of the Regions, [Making ETS and CBAM work for EU cities and regions](#), CDR 4546/2021
- Council, [Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision \(EU\) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation \(EU\) 2015/757](#), 6210/23

Further reading:

- European Parliament, EPRS, [Review of the EU ETS: 'Fit for 55' package](#), Briefing, July 2022
- European Parliament, EPRS, ['Fit for 55': Revision of the EU Emissions Trading System](#), initial appraisal of the Commission's impact assessment, Briefing, January 2022

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