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EU ETS to become the key driver for 2030 targets after directive reform

Finnish Energy represents around 260 power and heat companies operating in Finland. The sector is aiming at carbon neutrality by 2050. We strongly support the ETS as the driver of decarbonisation in the covered sectors and welcome the reform proposed by the commission in July 2015.

The reform fits in the big picture

There is need for a clear view on the long term development of the carbon price mechanism and related policies. The long anticipated decisions to strengthen the ETS and establishing it as the centerpiece of EU climate policy have been taken, the directive reform finalising this process. The key decisions prior to this ETS directive proposal have been the 2030 targets, backloading decision and the market stability reserve. Together these decisions will make the ETS business relevant in for the whole period of 2021-2030. Tilting the linear reduction factor towards 2030 and 2050 targets is a must.

We regret that in the context explanation, included in the proposal, there is little notion given on the interaction of the ETS and national renewable power subsidy schemes, stemming from the unbalanced target setting for 2020. There is a potential positive impact on ETS of the balanced approach of the 2030 targets. The recent EU decisions should signal the member states that no subsidies in the power sector are needed post 2020. This would allow the development of an internal energy market and an energy union.

Carbon leakage action continued but with streamlined approach

As Paris climate conference approaches, it is still unclear how long it will take until competing economies have taken on carbon pricing to the extent that carbon leakage is no longer an issue. As it is likely that the risk of emission leaking outside the EU continues post-2020, we welcome the continuation of carbon leakage measures. The risk is mitigated through dual approach; free allocation for the direct emissions and compensation of rising electricity costs for the indirect impacts.

We support the commission's stronger call for the member states to compensate rising electricity costs. This can be funded by recirculating some of the auction revenues. However, the proposal is lacking a harmonised approach for the compensation of indirect costs of ETS to industry. The indirect cost arising from increasing energy prices should be compensated based on EU-level criteria. Calculations show that even for Finland with its high share of heavy industry, the compensation can be completely funded with auction revenues. Furthermore, it is to be recalled that these measures to avoid carbon leakage do not undermine the carbon price signal or the mitigation efforts.

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While free allocation is continued, we welcome the clear signal that auctioning is the main channel to release allowances to the market. Together with well guided use of auction revenues this can maximise the cost efficiency of mitigation efforts and keep the market mechanism well-functioning as the amount of allowances declines. There should also be some clarity how the increasing efforts of competing economies impact the need for free allocation in the EU ETS.

Don’t forget heating - district heating is an efficient technology platform

District heating makes available system level approach for mitigating heating emissions and allows for renewable energy sources and fuels to be used in heating. It can also drastically improve energy efficiency when produced in combined heat and power plants. Therefore we welcome the continuation of free allocation to district heating, although at the low level of 30 %, throughout the period 2021-2030. Most of the district heating operations in Finland are within the ETS. The system covering all densely populated areas is operating on a free market with low regulation. The successful approach could be introduced elsewhere in Europe with the help of extending the scope of the ETS to the heating sector as a whole.

There have been many significant steps taken towards harmonizing the ETS rules. However, some potential areas to continue harmonization are heating and waste incineration, where opt-in or opt-out measures create differences and confusion in these sectors across member states.

Open issues: one-off transfer, extension of the scope, international cooperation

The directive proposal leaves many questions open, some of them mentioned in the council conclusions in 2014. One is the so-called one-off transfer of EUAs by member states to help with their ESD sector target. This subject should be clarified in the ETS discussions and synchronized with ESD sector decisions.

There have been talks on extending the scope of the ETS. We see the heating sector as one potential addition to the system. According to a study (Greenstream 2015), some potential exists even in the short term and the apparent practical issues are solvable. Long term potential of low-cost abatement should be studied further.

The proposal does not consider the international development of carbon pricing. The EU should promote carbon pricing mechanisms worldwide and be prepared for cooperation through linking of regional systems or other forms of international trading.

The possible re-evaluation of the EU's ambition level after Paris should be linked to the possibility to use international emission reduction credits. Use of those credits can facilitate linking of the regional trading schemes that is crucial in developing a global carbon market.

Solidarity mechanisms are confusing the system

There are plenty of mechanisms transferring funds to lower-income member states. These mechanisms altogether constitute a remarkable share of EUAs entering the market. While there should be other means available for solidarity than the ETS, at least the market impact of the funds proposed and the treatment of unallocated phase 3 allowances in the MSR should be further clarified. Timing of the capitalisation of NER400 and the Innovation Fund has to be synchronised with MSR in order not to be counterproductive for the market. Additional allowances should enter the market as late as possible and evenly throughout phase IV.

There is time for thorough discussion

Adequate time should be taken to discuss the ETS reform proposal and its implications, as well as compatibility with the ESD and even LULUCF sector decisions later on. We welcome the idea to finalise these decisions parallel to each other, even if it means extending the process to 2017.

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