T&E’s response to the Effort Sharing Regulation Inception Impact Assessment consultation

November 2020

Analysing the three options described in this consultation, **T&E expresses concerns**:

The Commission seriously envisions the possibility to repeal national targets and integrate road transport, as well as buildings, into the ETS. **These options, based on a theoretical vision of carbon pricing will not deliver emissions reductions in the real world.**

T&E regrets that the Commission did not include the option of maintaining the current architecture by raising both the ambition of the ETS and the ESR.

The risk is high that the whole architecture may crumble for lack of ambition. In these conditions, the target of 55% may never be achieved by 2050.

1. Context

In December 2019, the European Commission announced the European Green Deal, a renewed ambition to make the EU's economy sustainable by turning climate and environmental challenges into opportunities.

As a part of the European Green Deal, the European Commission suggested strengthening the European-wide climate ambition, raising the target from 40% of emissions reductions (against 1990) to 55% by 2030.

This new climate ambition implies much more than a quick fix. The overall climate architecture must be adapted and most of the European measures for climate change must be strengthened (CO2 standards, AFID etc.). The European Commission is now planning to pursue these discussions in the "Fit for 55%" package.

The European climate architecture, at the heart of the revised ambition, will need to be adapted.

Historically this climate architecture is composed of two pillars:

- The European-wide Emission Trading Scheme for large industries and the power sector
- National targets for road transport, buildings, waste, the agriculture and small industries in the framework of the Effort Sharing Regulation.

Last October, the Commission published an Inception Impact Assessment on the ESR. In this consultation, the European Commission proposes three ways forward to build a new architecture.

Analysing the three options described in this consultation, T&E expresses concerns. The Commission seriously envisions the possibility to repeal national targets and integrate road transport, as well as buildings into the ETS - a scenario based on carbon pricing theories, designed by economists and that deliver emissions reductions only on paper, but not in the real world.

The risk is high that the whole architecture may crumble for lack of ambition. In these conditions, the target of 55%, although adopted on paper, may never be achieved by 2050.

2. The missing "Option zero", maintaining the existing climate architecture, strengthening the ESR

T&E regrets that the Commission did not include the option of maintaining the current architecture by raising both the ambition of the ETS and the ESR.

The ESR has proved to be an efficient tool to incentivize climate action:

- At national level, the targets have been - and will continue to be - an important driver for domestic investment in infrastructures such as charging, low emission zones and building renovation. They have led to ambitious taxation reform in some countries (see graph below)

- At EU level, member states have supported ambitious EU regulatory measures (e.g. CO_2 standards) to more easily achieve their national objective.

Purchase subsidies and scrappage schemes in favor of electric vehicles (EV) in 2020. [1]

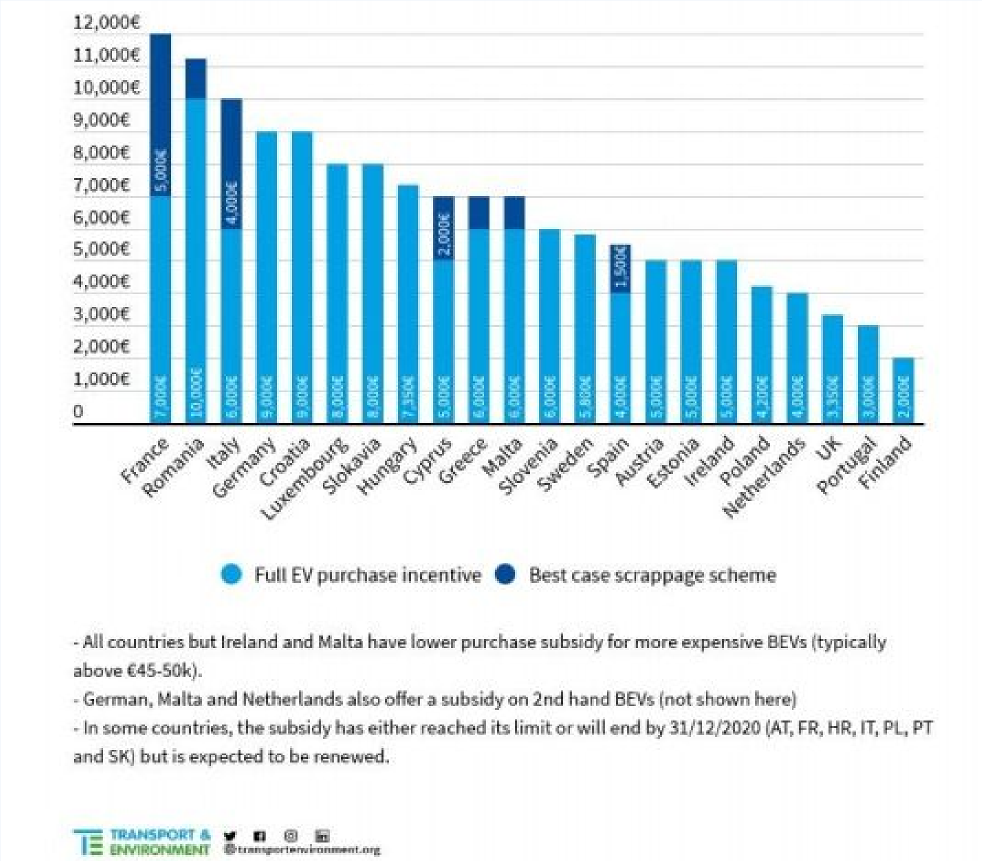


Figure 3 - BEV purchase subsidies and scrappage schemes in Europe (as of summer 2020)

[1] Source : Transport & Environment (2020). Mission (Almost) Accomplished. Available at https://www.transportenvironment.org/publications/mission-almost-accomplished-carmakers-race-meet-202021-co2-targets-and-eu-electric-cars

The ESR faces some challenges. T&E identified weak governance and inefficient flexibilities as main issues to address in this review:

- An improved governance that includes more transparent annual carbon budgets, and a strengthened compliance framework, including fines and annual checks.

- Although cross-country exchanges are allowed, the mechanism is rarely used. A joint projects platform for cost-effective projects EU-wide should be created, with the help of e.g. the EIB. Wealthy countries with highest targets may be able to support investments in countries with low abatement costs and benefit from the reductions.

3. Options 1 and 3: why carbon pricing is not the holy grail

Repealing the ESR

- National targets at risk. The ESR contributed to the adoption of national policies, and more will be needed this decade. The EC must factor the risk of domestic policies to slow down in the case where national targets would be repealed.

- EU policies in danger. The repealing of the ESR will also alter the motivation of the Council to adopt ambitious EU sectoral measures. The Commission should factor the potential for an extended ETS to jeopardize increased ambition in many other climate regulations.

Extended ETS

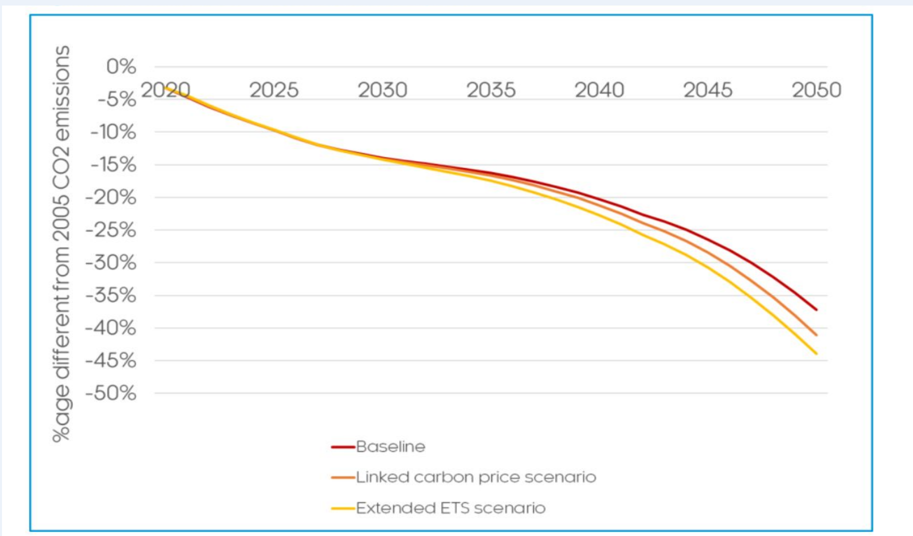
- Inefficient measure for the climate. Analysis shows that under an extended ETS, additional emissions reduction in road transport will be about zero in 2030 and less than 10% in 2050 due to its inelastic demand (see graph below). Additionally, within an extended ETS, a carbon price significant enough for road transport would be exorbitant for energy intensive industries.

- The fuel price increase resulting from the inclusion of road transport into the ETS will hit the low-income population the most, without addressing existing market barriers. The EC should really consider if it wants to link the Green Deal with impacts on the most vulnerable.

- Carbon pricing in road transport does not lead to fuel switching or timely investments into zero emission technology. To achieve 2050 targets, the last ICE car should be sold in 2035 at the latest. The Impact Assessment of the Climate Target Plan shows that ambitious CO2 standards compete politically with the road ETS. Standards have been the only tool that brought the transition from combustion to electric cars.

- A European-wide ETS will leave the door open to domestic compensations, as illustrated by the German system. Starting in 2021, Germany will start a “cap and trade” for road transport. While this cap and trade resemble a tax (the CO2 price is determined by law - unlike), compensation measures have already been announced by the German ministry to compensate lorries for the additional cost. [2]

Extended ETS : an inefficient solution for road transport decarbonisation
Source: Cambridge Econometrics[3]



[2] https://www.cleanenergywire.org/news/german-government-wants-reimburse-heavy-lorries-co2-price
[3] Cambridge Econometrics (2020). Decarbonising European transport and heating fuels. Available at https://www.transportenvironment.org/sites/te/files/publications/2020_06_Decarbonising_European_transport_and_heating_fuels_report.pdf

4. Option 2: Limited damage under conditions

A carefully-crafted and fair carbon pricing could be explored for road transport if some conditions are met:

- If national targets remain in place and are strengthened.
- If car CO2 standards become annual and reach 65% in 2030. Other measures must be taken to accelerate road transport CO2 cuts. If not, the carbon price will spiral out of control.
- If it is a system exclusively for road transport, with clear considerations on how the revenues could be used to contribute to the transition in the sector, particularly the most vulnerable.
- If no flexibility exists between this system and LULUCF and the EU ETS.

Administratively, it is possible to maintain road transport in the ESR and create a separate carbon pricing mechanism. Article 2 should be modified to integrate the list of sectors covered in the ESR, using UNFCCC categories.

Further information

Diane Strauss
Director France
Transport & Environment
diane.strauss@transportenvironment.org
Mobile: +33(0)652065400