

## **ETUC's position on the creation of a second ETS on road transport and building and of a new Social Climate Fund**

Adopted at the Executive Committee meeting of 8-9 December 2021

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### **Background**

On 14 July 2021, the European Commission published its Fit for 55 Package. This package consists in 13 legislative proposals that aim at aligning EU climate and energy policies with the new climate targets set by the recently adopted Climate Law – a GHG emission reduction of 55% by 2030 compared to 1990 levels, and climate neutrality by 2050.

As part of this package, the Commission proposes to create a new ETS as from 2026, covering road transport and buildings. This new separate self-standing ETS would focus on upstream fuel suppliers. Emissions from road transport and building sectors would be capped, with the cap reduced over time so that total GHG emissions for these sectors are reduced by 43% by 2030 as compared to 2005. This system would aim at creating a price incentive for companies and consumers to switch to low carbon solutions while raising additional revenues to finance the transition<sup>1</sup>. Overall, this new system is expected to raise €288,8 billion over a seven-year period.

In parallel to this second ETS, the Commission also proposes to create a new Social Climate Fund. The objective of this new fund would be to counter the negative impact of the new ETS on building and transport by financing activities that would principally benefit vulnerable households, vulnerable micro-enterprises or vulnerable transport users, in particular by ensuring affordable and sustainable heating, cooling, and mobility. To benefit from the fund, Member States would need to develop Climate Action Social Plans, as part of their National Energy and Climate Plans. In terms of budget, the new Social Climate Fund is expected to raise around €72,2 billion over a seven-year period, equivalent to 25% of the revenues to be generated by the new ETS. In addition, Member States would have to co-finance their Climate Action Social Plans by dedicating another 25% of the revenues they generate through the new ETS. The total amount spent on those plans would therefore be around €144 billion.

### **Concerns about the creation of an Emission Trading System covering road transport and buildings**

ETUC does not reject the idea of creating carbon pricing mechanisms per se. Indeed, in some cases, such mechanisms can help provide the right incentives to companies and consumers to move towards more sustainable alternative solutions. However, such mechanisms should always be designed in a way that they create the right conditions for a just transition and do not lead to more inequalities and poverty.

In that regard, ETUC has expressed several concerns about the idea to create an ETS covering road transport and buildings:

- First of all, it is widely documented that carbon pricing policies on road transport and buildings produce regressive distributional effects, affecting proportionally

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<sup>1</sup> The European Commission estimates that based on a carbon price of ~€50/tCO<sub>2</sub>, this new ETS would generate around €47 billion of annual revenues.

more low- and middle-income households than high income households. This is because low-income households dedicate a higher share of their revenues to energy related expenses. This could result in more inequalities and in an increase in energy poverty since the additional costs generated by this second ETS would likely be passed on to the consumers. It should be noted that energy poverty is already a widespread problem across Europe. Indeed, the European Energy Poverty Observatory estimates that more than 50 million households in the European Union are already experiencing energy poverty today. The introduction of a new ETS on transport and buildings would therefore add an additional variable to an already unsolved problem.

- It is also clear that an EU carbon pricing mechanism on road transport and building would affect differently people, depending on the country or region they live in. A common carbon price will not impact citizens in the same way if they live and work in a country with high or low wages, and with high or low energy price levels. Besides, the reliance on coal in the energy supply, or the ageing car fleet of households, will mean higher costs for countries that are already affected by high energy poverty. Within these countries, citizens would also be affected differently whether they live in an urban area or a rural area. Without sufficient national social policy and adequate solidarity mechanisms in place, this will result in an increase in regional inequalities.
- Another concern is that the effect of such a carbon pricing mechanism might be limited in terms of GHG emissions reductions, since road transport and building markets are often depicted as relatively inelastic to higher carbon prices<sup>2</sup>. Indeed, the necessary upfront investment costs as well as the different obstacles to the renovation of buildings or adoption of cleaner transportation solutions can prevent many households from modifying their consumption, even if carbon prices rise. This is especially true for low-income households. Ultimately, this means that those affected by the price of this ETS will be the ones who will not have been able to invest in low carbon alternative solutions. Hence, the need to massively mobilise funding to support those households, and to invest in public transport and building renovation.
- We cannot separate the transportation mode of workers from the geographical location of their companies and the possibilities to reach them, which is largely determined by business choice, on which workers have limited influence. In many regions the public transportation means to reach these companies are insufficiently developed and must be scaled up to allow alternative options for a modal shift<sup>3</sup>. Regarding clean individual transportation solutions, the stability of this business model is yet not consolidated to completely substitute internal combustion engines vehicles by the time of the introduction of the second ETS, and its current non-affordability might be a challenge in the transition. Policy makers must implement measures to accelerate the uptake of zero and low emission vehicles notably by boosting the development of the charging infrastructure and the electricity grid.

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<sup>2</sup> Hence the need to boost the roll out of the charging infrastructures needed to enable the uptake of electric vehicles and to accelerate the uptake of energy efficiency and decarbonisation solutions in buildings.

<sup>3</sup> It should be noted that trade unions also have a role to play to negotiate with the employers – through social dialogue and collective bargaining – mobility solutions to accelerate the uptake of low carbon transportation in companies and modal shift.

- Finally, the uncertainties related to the future price of carbon, which can fluctuate quite a lot with such a system, constitute an additional worry. Relying on a cap-and-trade system means that policy makers have limited control on future prices, which could be subject to market fluctuation and speculation. This uncertainty creates a volatile investment environment and, in case of sudden price spikes, measures for social compensation might become inadequate.

If not addressed properly, all these effects combined could result in a lack of political acceptance of climate policies by EU citizens and in some sort of political backlash, such as the gilets jaunes movement in France. Far right, climate sceptic or Eurosceptic movements would also use any real negative effect of a second ETS on revenues of working people and vulnerable households to fuel their own political agenda. The EU cannot take the risk of jeopardising the unprecedented efforts of the European Green Deal.

The Commission's proposal to create a new Social Climate Fund tries to address some of these concerns through several mechanisms: (1) it would redirect part of revenues generated to help compensate vulnerable households; (2) it foresees an allocation criteria to ensure solidarity among Member States to correct the effects of a common EU carbon price; (3) it creates a separate self-standing ETS decoupled from the current ETS to avoid inadequate carbon pricing; and (4) it foresees a transition period with frontloading of money one year before the second ETS enters into force. We acknowledge these proposals, but they appear to be insufficient to fully address the worries expressed above.

Indeed, the creation of a Social Climate Fund to mitigate the effects of the second ETS only partially answers the concerns expressed by ETUC: for example, the current Commission's proposal of combining a second ETS with a new Social Climate Fund does not solve the issue of inelasticity to higher carbon prices of the road transport and building market, nor does it provide sufficient resources to both compensate workers and their households from higher energy prices and to finance the transition to clean solutions. It is also not clear how the current proposal would provide sufficient fund to both compensate the regressive effects of the ETS2 and eradicate already existing energy poverty. Finally, the Commission does not answer concerns related to the potential political backlash the creation of a second ETS could create.

In order to answer those concerns and to guarantee workers' support to the climate agenda, ETUC is of the idea that a Social Climate Fund is needed and opposes the proposal of a new ETS for road transport and building.

### **A new Social Climate Fund without a second ETS on road transport and building**

The idea to create a Social Climate Fund as proposed by the Commission is welcomed and supported by ETUC. A new fund to support households in dealing with rising energy prices and in investing in energy efficient, and clean, housing and mobility solutions is indeed needed urgently. Along with adequate resources to secure a just transition of the workers in the construction and transport sectors.

ETUC therefore suggests creating a new Social Climate Fund as a standalone proposal and to finance it with other – more progressive – sources of revenues. For example, part of the revenues generated by the existing ETS could be used to compensate vulnerable households for rising energy prices. The additional money available due to the phase out of subsidies to environmentally harmful activities would

also help to finance the fund. Other sources of revenues related to a fairer taxation system could also be mobilised, such as the introduction of a Financial Transaction Tax, a minimum corporate tax, a Common Consolidated Corporate Tax Base with an appropriate apportionment formula, a digital tax or a Wealth Tax.

At the same time, it should be kept in mind that both the transport and the building sectors need to rapidly accelerate the pace of their emissions reductions. Efforts made in the building sectors have, so far, been largely insufficient to achieve climate targets while emissions in the transport sectors have increased since 1990.

It should be clear that cap and trade mechanisms such as ETS are not the only policy instrument available to achieve GHG emissions reduction and should not be the core of EU's climate action. In that regard, ETUC welcomes the Commission's proposal to revise existing standards and regulations to increase the uptake of clean mobility solutions on the market (e.g. through CO2 standards for cars and vans) and to reduce the energy consumption of buildings. It should, however, be made sure that these changes are accompanied by sufficient measures to ensure the just transition of the workforce in these sectors, as well as sufficient financial support to guarantee affordable renovation costs and adequate public transport infrastructures. To complement these standards and regulations, ETUC believes that a possible alternative to the creation of a new ETS on road transport and building could be to use the Energy Taxation Directive to provide a price incentive, while ensuring a control over energy prices and a progressive taxation based on the revenues of households, the share of urban versus rural, and the country reality. The revenues generated by such taxation would, in any case, need to be recycled to support workers and their households and ensure a socially fair transition and could also be used to finance the new Social Climate Fund.

If unanimity procedure prevents these proposals to be deployed and if – despite the above recommendations – EU policy makers decide to go ahead with the creation of a second ETS covering road transport and buildings, ETUC calls for a much stronger Social Climate Fund to mitigate the effects of the new ETS with a truly progressive redistribution of the revenues generated and a just transition.

### **Mitigating the effects of the new ETS with an improved Social Climate Fund.**

Boosting the Social Climate Fund would require the following changes to the current Commission's proposal:

- The size of the fund should be significantly increased. The amount currently proposed – taking into account the co-financing of Member States – would result in an average budget of €527 per year per household if the entire amount was only distributed to the 20% poorest households in the EU. This amount may be sufficient to partly compensate these households for the rise in energy prices, but it would clearly be insufficient to both compensate and offer them solutions to decarbonise. ETUC therefore calls on EU and national policy makers to dedicate 100% of the revenues generated by the second ETS – or an equivalent amount – to compensate workers and their households, finance clean mobility and energy efficiency alternatives, and reduce energy poverty. Climate taxes should be earmarked to finance climate and social action<sup>4</sup>. Furthermore, the redistribution criteria should make sure that workers and their households receive more from the fund than what they pay and that there is no unfair treatment between rural

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<sup>4</sup> See ETUC resolution on EU taxation and own resources, March 2021

and urban territories and between countries. To ensure this and to fight against the already widespread energy poverty, those revenues should be complemented by other sources (see point 11).

- The timing of the availability of funding compared to the applicability of the new ETS is also a crucial element. If the money comes at the same time when the carbon price is introduced, households will not have the ability to make upfront investments in clean alternative solutions and would be hit hard by the rise in energy prices. ETUC acknowledges that the Commission is proposing a frontloading of money one year before the new ETS would enter into force but believe this still comes too late. ETUC calls upon policy makers to ensure that funding is available at least three years before the introduction of a new ETS, to ensure sufficient time for vulnerable households to anticipate the transition. Besides, public authorities should also make the necessary upfront investment to ensure the development of alternative low carbon infrastructure, for example in public transportation. Here again, this frontloading of money could be financed by revenues coming from the existing ETS or from more progressive sources of revenues such as an FTT, a minimum corporate tax base, a CCCTB with an appropriate apportionment formula, a digital tax or a wealth tax<sup>5</sup>.
- In terms of governance, ETUC supports the idea that Member States would have to develop Climate Action Social Plans as part of their NECPs. The NECPs should be the translation of climate ambition into concrete measures, ensuring just transition and social ambition. However, it should be guaranteed that social partners are properly involved in the design and implementation of those plans, along with local actors and civil society. Those plans should be developed in line with the best implementation practices of the European Code of Conduct on Partnership, through social dialogue with social partners and in close consultation with local authorities and civil society.
- The activities to be financed by the Social Climate Fund should be additional to what already exists in the different Member States. This would not be the case in the current Commission's proposal where, if Member States already have existing policies or funding in place, they could simply account it as part of their expenses without the need to do more.
- Finally, ETUC believes that the new Social Climate Fund should also be used as a leverage to promote high quality employment and decent working conditions. Activities related to the world of work that will be financed by the fund should be subject to social conditionality. In other words, any funding of activities by the Social Climate Fund that requires hiring workers should be conditional to decent wages, decent working conditions (including health and safety aspects and direct employment contracts), proper trade union representation, social dialogue and the right to bargain collectively. Also, the Social Climate Fund should not be used to finance projects related to unabated fossil fuels, in accordance with the "do no significant harm" principle. EU policy makers should also take adequate measures make sure that a new ETS on road transport and building does not lead to carbon leakage in those sectors.

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<sup>5</sup> Cf. discussion related to EU own resources.

ETUC believes that the Fit for 55 package can only be socially fair and acceptable for EU citizens if it does not lead to loss of revenues for low- and middle-income households. In that regard, a new ETS on road transport and buildings risks to fail the test of public opinion. ETUC recalls that carbon pricing policies should not be the core of EU climate action. When it comes to road transport and building, we believe that regulation and standards also have a role to play. More should also be done to implement the energy efficiency first principle, notably through strong measures to support low- and middle-income households. Boosting initiatives under the EU renovation wave and the EU Smart and Sustainable Mobility Strategy could significantly contribute to that objective. In parallel to that, the Commission should put more focus on the need to increase living standards of people to avoid energy poverty and to make sure households can afford the green transition. Measures to increase wages and to implement the European Pillar of Social Rights should be higher on the political agenda. An adequate Social Climate Fund to support vulnerable households is part of the answer.

Trade unions have been front runners in asking for a socially fair and ambitious climate action. Furthermore, trade unions do not wish to allow the opportunity for the far right to use the regressive effects of the new ETS on road transport and buildings on workers and their households as a reason to challenge climate policies. Nor can we gamble workers' support for climate policies on the belief that governments that have allowed fuel poverty and low wages to grow will, with the Social Climate Fund, really tackle strongly and genuinely the regressive consequences of the introduction of the new ETS. The urgency of climate action and just transition requires from us to fight the climate sceptics while proposing solutions that will improve the living conditions of workers and their households. This is also what we expect from the EU and national policy makers.

## **Annex: Context of rising energy prices**

It should be noted that these proposals were tabled in the context of rising energy prices. Indeed, after a decline during the first lockdown period, energy prices – and especially gas prices – have been skyrocketing over the last few months, raising significant concerns about a potential stagflation and the ability of vulnerable consumers and companies to bear those costs. This sudden rise in energy prices can be explained by a combination of several factors: first, a strong recovery in gas demand – especially in Asia – resulting from the ease of COVID19 related measures that created a sudden rebound in consumption and economic activity. Second, a tighter than expected oil and gas supply to the EU due to geopolitical reasons. Third, last winter having been a particularly cold and long heating season in Europe, which resulted in lower gas storage levels in the EU. Fourth, a lower than usual availability of wind and solar energy in recent months. Fifth, a lower production of liquefied natural gas worldwide due to a series of unplanned outages and delays across the globe and delayed maintenance from 2020. Finally, it seems the recent price increase in carbon emission allowances on the European Emission Trading System has also somehow contributed to the rise in electricity prices.

ETUC believes that climate policies are not the main causes of this sudden price increase, which is mostly explained by a coincidence of other factors. A well-managed just transition toward clean energy production is, in the middle and long-term, the most logical and rational solution to those problems of energy supply, energy security, energy affordability and fluctuation of energy prices. Achieving the objectives of the European Green Deal should therefore remain the top priority of policy makers.

Even though not directly related to the proposals of creating a new ETS for road transport and building as well as a new Social Climate Fund, such a crisis however highlights the necessity to consider the impact of higher energy prices on vulnerable households when designing future policies. It also stresses the need for policy makers to look at the current functioning of the EU energy market to identify potential structural causes of the crisis. Issues such as EU dependence on energy imports, price setting mechanisms on electricity markets and impacts of speculation and hedging on the existing EU ETS are indeed all highly relevant. This position does not intend to tackle these issues; however, we believe it is important to keep them in mind when discussing the proposal of creation of a second ETS and of a new Social Climate Fund.