ETUC POSITION ON THE STRUCTURAL REFORM OF THE EU EMISSIONS TRADING SYSTEM

Approved at the Executive Committee Meeting of 16-17 December 2015

In July 2015, the European Commission published a proposal for the reform of the EU Emissions Trading system (EU ETS) for the period 2021-2030. This proposal is based on the guidelines defined by the conclusions of the European Council of October 2014. The present resolution aims to update the ETUC's position on this essential element of the European framework on the fight against climate change and to reiterate both the need to better articulate industrial and climate policies, as well as the importance of operationalising the "just transition" through concrete measures. These comments and proposals are based on extensive consultations among trade unions across the EU as well as on an ongoing ETUC research project into low carbon industrial strategies across seven key industrial regions.

List of the ETUC key demands

- The European Commission must develop an integrated and coherent sustainable industrial strategy and should set up a policy platform to that aim.

- After Paris COP 21, the EU must make an in-depth assessment of the risk of carbon leakage and the policy instruments it has to effectively tackle it

- The EU must create a Just Transition Fund to support workers which would be negatively impacted by the transition to a low-carbon economy.

- The EU must effectively implement the Innovation Fund and the Modernisation Fund and involve social partners in their management

- At least 90 % of ETS auctioning revenues should be used by Member States to support activities which are clearly climate-related.

Context

In order to help limit global warming to 2°C maximum, the EU has committed itself to precise targets to reduce its greenhouse gas emissions. More specifically, the EU must reduce its emissions by 20% by the year 2020, by at least 40% in 2030 and by 80% to 95% in 2050. To that end, the EU has developed a political and regulatory framework, the cornerstone of which is the European Emission Trading Scheme (EU-ETS). The goal set for 2030 for sectors covered by the EU-ETS is to reduce emissions by 43% compared with the 2005 levels. (For their part, sectors not covered by the EU-ETS must reduce their emissions by 30% compared with the 2005 levels).

The EU-ETS was set up in 2005 to reduce greenhouse gas emissions from energy generation and most of the manufacturing sectors, which correspond to about 45% of gas emissions. It covers CO_2, nitric oxide (N_2O) and perfluorinated hydrocarbon (PFC) emissions from more than 12,000 electric power stations and industrial sites in 28 Member States as well as Iceland, Lichtenstein and Norway. Based on the cap and trade model, the EU-ETS limits the volume of annual emissions whilst authorising emitters to trade their emission quotas. This volume is reduced annually by a certain percentage (1.74% at present). The price signal from the cap must guide investments to the technologies with the lowest emissions whereas the flexibility left to the participants in the system helps reduce the cost of emission reduction measures.

The free allocation of quotas by the Member States which had prevailed in the first two phases of the system (2005-2007; 2008-2012), was replaced in the third phase (2013-2020) by a centralised allocation system which will progressively rely more on the quota auction process. In this system, 57% of the emission quotas will be auctioned, whilst the remaining 43% will be distributed to companies free of charge. Electricity generation facilities must in essence acquire their emission quotas through the auction process, whilst the share of the free quota allocation of the industrial sectors will be reduced from 80% in 2013 to 30% in 2020.

Additional measures have nonetheless been planned to address the risks of “carbon leakage” (i.e. relocations to countries with less ambitious climate policies brought about by the EU-ETS). The sectors and subsectors which are concurrently CO2 emission intensive and whose production is in significant measure intended for the international markets are placed on what is known as a “carbon leakage” list which is reviewed every five years. This list enables the industries concerned to receive, free of charge, a volume of emission quotas, calculated on the basis of a reference level of 10% of the most efficient facilities in the EU for a given product. The current carbon leakage list comprises 177 industrial sectors and covers 97% of emissions of these sectors.

The European legislation also enables the Member States to offset the increase in the price of electricity which would be caused by the EU-ETS through State aid granted to the companies concerned.

The free allocation of the first two phases, the extensive use of CDM credits, combined with the effects of the economic crisis, has generated an over-allocation of emission quotas which is partly responsible for the surplus of emission quotas that has driven the prices of quota emissions down. Two measures have been taken to deal with this surplus problem and restore the price signal of the system: first, the auction of 900 million quotas has been postponed until 2019-2020, and second, a market strategic reserve is to be put in place to stabilise the volumes of emission quotas present on the market.

The key changes proposed by the European Commission for the period 2021-2030 are:

- The linear reduction factor would go from 1.74% to 2.2%, which entails an intensification of the annual reduction of the quotas put on the market.

- A higher differentiation and more frequent revision of the reference levels used for the allocation free of charge.

- 250 million quotas would be allocated to a reserve for new entrants or strong growth production activities.

- The carbon leakage list would comprise of no more than 50 sectors and would cover no more than 90% of industrial emissions.

- A fund for innovation will be created. It will be fed by revenue generated from auctioning 450 million emission quotas, i.e. €10 billion according to the Commission’s estimates. The fund is intended to provide greater support for renewable energies, CO2 capture and storage, and the deployment of low carbon industrial technologies.

- A fund for modernisation will also be created to provide financial support for the modernisation of energy systems in Member States where per capita GDP in 2013 is below 60% of the European average.

General principles of the ETUC's position

In line with its previous positions, the ETUC strongly reaffirms its support for policies to counter climate change which not only provide a fair contribution from Europe to the global reduction of greenhouse gas emissions but also guarantee the creation of quality employment, the reduction of fossil imports and the improvement of air quality. The EU ETS reform must help achieve the decarbonisation objectives of the European economy whilst allowing a "just transition" for all workers without undermining quality of life or generating windfall profit.

In calling for a "just transition", the ETUC has always refused to pit maintaining jobs against environmental protection. The two goals must be pursued with equal determination. The ETUC has adopted the same approach to the reform of the EU ETS. Industrial activities and the quality jobs they generate are absolutely essential to a prosperous and fair society. European climate policies must stimulate the transformation of these sectors through investment and innovation, but must certainly not precipitate their decline. The side effects of a relocation of production activities may under no circumstances be pursued in lieu of a climate change policy. The EU must adopt a real low-carbon industrial policy and take appropriate measures to ensure the EU ETS effectively contributes to an effective and socially fair transition to a low-carbon economy.

The ETUC's demands

The European Commission must develop an integrated and coherent sustainable industrial strategy and should to that aim set up a policy platform

The ETUC calls on the European Commission to launch an initiative aimed at developing a real, proactive and visionary European sustainable industrial policy, one that includes all the dimensions of this problem, and in particular the following elements: innovation, infrastructure and facilities, raw materials1, financing, training for the workforce, and international trade. In spite of remarkable initiatives, the European Commission's current approach remains fragmented and far too dependent on one instrument – the EU ETS – which is functioning more on the basis of financial rationales than as a real project to build a European sustainable industry. A European platform for the development of a sustainable industry, that brings together industrialists, the public authorities, trade union representatives and experts from the civil society in a balanced manner could certainly contribute towards that goal. Collecting data through indicators showing resource and carbon intensity of industrial products, in the EU and globally, should be a priority in order to monitor the transformation of the EU industry and ensure that the targets are met through investment and innovation and not through delocalisation of activities.

After Paris COP 21, the EU must make an in-depth assessment of the risk of carbon leakage and of the policy instruments it should have to effectively tackle it

Trade Unions are increasingly concerned about the loss of jobs and investment in many important industrial sectors and see imports from non EU competitors – and the related dumping risk – as a concrete threat which could become even more serious in a scenario of unilateral deep decarbonisation strategy from the EU.

[1] *Synergies with the EU action plan for the Circular Economy should be enhanced*

The mechanism to fight against carbon leakage, mainly based on the free allocation according to a reference level for each sector, which the Commission plans to extend whilst adjusting it to the margin, seems inadequate to us. For one, it does not provide a response to the main of driving forces behind relocations which include the price of raw materials, the weakness of internal demand, the development of important markets in other geographic areas, the import of cheap industrial goods from emerging economies and overcapacity in certain sectors. Furthermore, this mechanism provides only a very small incentive to invest in low-carbon production technologies. The system protects – often in an abusive manner – but does not provide sufficient incentives to invest and innovate. The ETUC consequently calls on the European co-legislators to consider alternative – and possibly complementary -- options to the free allocation and in particular those which rely on a taxation based on the carbon content of goods placed on the European Market, of which the exporting companies would be exempted, fully or partially.

The ETUC also demands that free allocations be reserved for sectors and sub-sectors that are actually exposed to a significant relocation risk, mainly driven by climate policies, and conditioned by the effective implementation of measures to reduce greenhouse gas emissions and the use of best available technologies as identified through the revision of benchmarks every five years. Additionally, the methodology used to make the carbon leakage list should use the real carbon price and not assumptions.

State aids are absolutely crucial, notably to compensate the indirect impact the ETS has through electricity price on industrial production costs. The use of state aids must be better coordinated at EU level since in the current situation, some Member States provide significant state aid to compensate the ETS impact on electricity price for industry whereas others do not compensate at all. Such compensation should be limited to the share of carbon cost which is not passed on to customers in order to avoid windfall profits.

Last but not least, the process whereby the Commission analyses demands to use state aids from the Member States must be as quick as possible.

The EU must create a Just Transition Fund to support workers which would be negatively impacted by the transition to a low-carbon economy

The ETUC regrets the weakness of the mechanisms presented in the Commission's proposal to support workers in regions that will be adversely affected by the transition to a low-carbon economy. The insertion of "training and the reassignment of workers affected by the transition" in Article 10 B of the proposal to amend the Directive, leaves the issue of whether to support the workers concerned entirely at the discretion of the Member States. Not only is said provision – which concerns the use of proceeds from the auctioning of emission quotas by Member States – not legally binding, but it also comprises a list of 12 possible assignments which make the actual support for such workers highly improbable. The ETUC therefore calls on the European co-legislators to consider other options to provide such workers with the support they need. A "Just Transition Fund," which would be intended to finance support measures for workers in regions and localities affected by the transition, could be fed in part from the structural funds and in part through the auctioning of a certain volume of emission permits. It should not, in any event, mobilise the resources of the European Social Fund, and it should be managed with the full participation of the social partners, as stipulated in the European Code of Conduct on the Partnership Principle.

The EU must effectively implement the Innovation Fund and the Modernisation Fund and involve the social partners in their management

Investment is one of the main levers of the transition to a low carbon economy. The ETUC very much endorses the creation of a fund for innovation which will boost the resources already available thanks to the existing financial instruments, and which is going to broaden the spectrum of eligible activities. The deployment of renewable energies and other low carbon industrial technologies are absolutely necessary in order to achieve the long-term goal of reducing emissions while maintaining a strong industrial base in Europe. Technologies such as Carbon Capture and Storage (CCS), which allow on the one hand to drastically reduce emissions from power production and manufacturing industries, while on the other hand are compatible – among other processes – with fossil fuel combustion, have been identified by several reports as essential to reach long term deep emissions reduction targets. In order to get these technologies ready in regions and sectors where they are necessary to build credible long term deep emissions reduction pathways, the financial resources available should be dramatically increased. The innovation fund should contribute to that objective, but industries and member states who have identified these technologies as priorities should also contribute to provide the level of investment needed. However, the deployment of these technologies only makes sense where it is cost effective in a long term perspective compared to other measures and provided that it is consistent with long term emissions reduction objectives and with the strongest health and environment standards.

The Modernisation Fund, which is used to support the modernisation of the energy system of low-income Member States, is also a proposal that the ETUC welcomes inasmuch as it brings home the need for solidarity between European countries. The ETUC demands that these two funds be effectively implemented and that appropriate measures be taken to maximise the impact thereof, notably through a search for synergy with other EU financial instruments, in particular the EFSI.

At least 90 % of ETS auctioning revenues should be used by Member States to support activities which are clearly climate-related

The "just transition" supposes a fair sharing of the burden. The ETUC would not accept that measures taken to fight against a presumed risk of carbon leaks actually generate windfall profits for large industrial groups whilst exposing an increasing number of households to energy poverty. The measures that increase the quantity of emission quotas placed at the disposal of companies free of charge automatically reduce the volume of auctioning. This deprives the public authorities from sources of financing, and that in turn creates unfair profits for certain companies, whereas households cannot escape the repercussions of the price of emission quotas on their electricity bill. The ETUC shares the objective of protecting industrial activities significantly at risk of carbon leakage, but this must be done without exacerbating the distributive effects leading households to pay heavy industry's CO_2 cost. In addition to the focus of free allocation for the sectors and subsectors really exposed to a risk of relocation driven by carbon cost, one way to mitigate the regressive impact of free allocation is to ensure that auctioning revenues benefit to society's as a whole and in particular should contribute to financing a just transition towards a low-carbon economy. The ETUC demands that the EU require Member States to devote at least 90% of the proceeds to activities which are clearly climate-related, and notably industrial low-carbon innovation, energy efficiency, training and upskilling programmes, measures against energy poverty and international climate finance. In this framework, Member States should be free to define the criteria for the selection of investments to be financed with the auctioning revenues they collect.