

The European Commission has asked for responses to its proposal on the Effort Sharing Regulation, which came out on July 20<sup>th</sup> 2016. This document provides Sandbag Climate Campaign's response. Further details of our analysis can be found in our recent reports<sup>1</sup>.

### Our key recommendations are:

- The target needs to be made more relevant
- The latest possible starting point should be used for calculating the level from which emissions must be reduced
- Any use of flexibilities should be accompanied by a matching increase in the target
- Some of the proposed flexibilities are unsuitable, notably the link with the EUETS and the use of LULUCF, and should be excluded, at least for the present phase
- A European Project Mechanism should be developed
- Compliance should be on an annual basis

### Detailed assessment

#### 1. The ESR target needs to be made more demanding

The proposals recognise that Council conclusions mandate a reduction of "at least 40%" from 1990 levels by 2030. The proposed reduction of 30% from 2005 from sectors covered by the ESR corresponds to meeting 40% rather than going beyond it. The target itself should be tighter. This would be in line of the "at least" nature of the targets, which implies the desirability of going beyond the minimum.

Furthermore, the Impact Assessment shows that under its Reference scenario, existing policies will generate savings of 24% from present levels, so that an additional reduction of only 6% will be needed over the entire ten-year period<sup>2</sup>. We do not think this is enough to put the economy on the necessary long-term track.

The currently proposed track would, among other things, be likely to lead to increased costs and the need for rapid emission reductions after 2030 if the EU is to meet its 2050 target. This would be in direct contradiction with the Council Conclusions' focus on cost-effectiveness as an important objective for the scheme, as well contradicting the commitment to have a rigorous scheme for emissions reductions in the non-traded sectors.

It is also clear that a number of countries should be set more stringent national targets, if cost effectiveness of the reductions is to be taken into account. Countries should not be in a position of surpassing their targets on the basis of existing policy measures alone. The chart below shows those countries (bars below the axis) that are projected to meet their targets set out in the Commission proposal through existing measures.

### About Sandbag

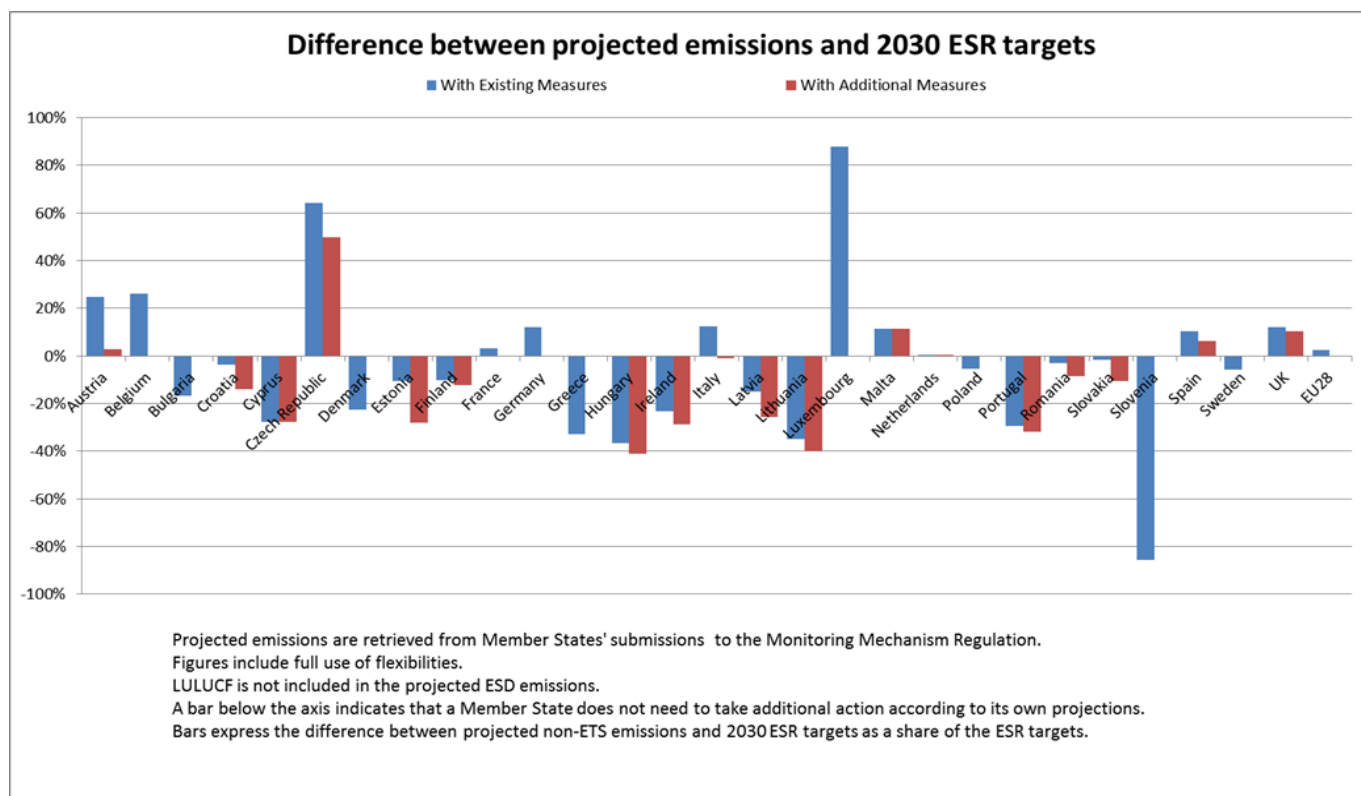
Sandbag is a London and Brussels-based not-for-profit think tank conducting research and campaigning for environmentally effective climate policies.

Our research focus includes reforming the EU Emissions Trading System and the Effort Sharing Decision; accelerating the phase-out of old coal in Europe; deep decarbonisation of industry through technologies including Carbon Capture & Storage.

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<sup>1</sup> <https://sandbag.org.uk/reports/bend-it-dont-break-it/> and <https://sandbag.org.uk/reports/effort-sharing-dinosaur/>

<sup>2</sup> Impact Assessment, section 1.3



Source: *Do "effort sharing decision" targets drive energy efficiency in buildings? 2016* Filippas Anagnostopoulos, Buildings Performance Institute Europe; Robert Harmsen, Utrecht University, NL – updated following contact with authors

Furthermore, all sectors need to contribute to this reduction, as the Council Conclusions highlight. It is not guaranteed in the Commission’s proposal that this would happen because targets are not sector-specific. **As such recommend minimum thresholds to be attached to reductions in each sector**, in order to put them on an appropriate track for the deep decarbonisation required by 2050, and to ensure compliance with the Council recommendations.

## 2. A later starting point for the baseline is preferred

It is also important that the benefit of continuing emissions falls is realised. Our previous research shows that even with a starting point based on the average of 2018-2020 real emission levels, the ESR would still have a surplus of 300 Mt accumulating by the end of 2021. Starting two years earlier and the new Art 10(2) flexibility introduced would most certainly contribute to doubling this amount by the end of only the first year of the scheme. A later starting point is therefore desirable.

## 3. The target should be achieved entirely from within the ESR sectors. Any reductions from alternative methods of compliance should be in addition to this.

The 30% is the minimum that must be done in these sectors, and so must correspond to actual emissions reductions in those sectors themselves, rather than elsewhere. Emissions reductions from other sources such as the proposed link with the EUETS and LULUCF should not be counted towards the targets. If any of them are permitted under the Regulation they must be matched by a tightening of the total target. For example, if other sources of emissions reductions deliver a 5% reduction, the target should be increased to at least 35%. Otherwise, there would clearly be weakening of the target for ESR sectors, as the Commission’s own Impact Assessment (IA) itself points out.

In addition, any further dilution of the target through reductions from other sources would represent an even smaller requirement on the ESR sectors, and further fail to set the sectors on the appropriate cost-effective long-term pathways to decarbonisation.

The weakening of effort implied is severe. The total reduction required for the 30% target is 875MtCO<sub>2</sub>e. Under the EU Reference Scenario, 741Mt would be delivered, so a net additional reduction of only 134MtCO<sub>2</sub>e (875MtCO<sub>2</sub>e – 741MtCO<sub>2</sub>e) is required.

The flexibilities to include emission reductions from other sources proposed by the Commission add up to 420Mt. This is 286MtCO<sub>2</sub>e greater (420MtCO<sub>2</sub>e - 134MtCO<sub>2</sub>e) than the emissions reductions required in the Reference Scenario. With emission reductions from the proposed flexibilities added to the total budget, the system would thus move from an expected small shortfall (with a need to reduce emissions) to a surplus, with no need for additional action by Member States.<sup>3</sup>

This is clearly at odds with the EU's long term goals and not in line with the Paris Agreement.

**The evidence therefore shows that emission reductions from flexibilities must be additional to reductions in the ESR sectors in order for adequate levels of effort to be maintained.**

We now look more closely at each proposed flexibility and its impact on the overall environmental integrity of the scheme.

#### **4. The import of allowances from the EU ETS should be excluded from the next phase of the ESR**

The Council conclusions from October 2014 requires that the 30% reduction applies strictly to the non-ETS sectors, as the ETS sectors have their own target of -43% reductions from 2005 by 2030. Allowing the EUETS to contribute to non-ETS sectors risks going against this principle.

We recognise that in principle linking the EU ETS and the ESR could have a number of advantages, if there were substantial scarcity of allowances in the sectors covered by both two instruments. In particular, such a move could help secure cost-effective emission reductions across different parts of the economy.

However, at present the EU ETS has very large surplus of around 2.7 billion allowances, including allowances available to the market immediately and those due to be placed in the Market Stability Reserve (MSR). Prices are correspondingly low at around €4/tCO<sub>2</sub>, compared with a level of €30/tCO<sub>2</sub> used in the Commission's IAs.

The market is likely to remain oversupplied into the 2020s despite the introduction of the MSR and even in the event of many of the proposals to reform the EU ETS of the type currently under discussion being adopted<sup>4</sup>. It is likely therefore that the EU ETS allowances used to meet obligations under the ESR would simply be taken from the EU ETS surplus rather than representing additional emission reductions in the EUETS sectors. There would be a fall in emission reductions in the ESR sectors with no corresponding increase in the EU ETS sectors. Additional policies would need to be introduced to ensure that real emission reductions take place.

**EU ETS allowances should therefore be excluded from the next phase of the ESR, but their inclusion could be considered again for period after 2030.**

#### **5. LULUCF credits are both unnecessary and detrimental to the effectiveness of the mechanism**

Emissions from LULUCF are uncapped at the moment, and a target for emission reductions is needed before it should be considered as a flexibility. Even then, issues with permanence of sinks and very high uncertainty due to accounting methods chosen mean that it is not suitable as a flexibility mechanism. **LULUCF credits should therefore not be included.** This would be in line with the treatment of international LULUCF offsets under the EU ETS.

#### **6. The new “top-up” flexibility for specific Member States proposed under Art 10(2) should not be allowed**

In art. 10(2) of the proposal, the 2021 allocations for certain Member States that were already allowed to increase their emissions in the period to 2020 are further increased. This has been put forward despite the fact that the

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<sup>4</sup> <https://sandbag.org.uk/reports/getting-touch-reality/>

Commission already establishes these countries' national reduction targets based on the relative GDP/capita for solidarity reasons. The current targets have therefore already addressed their needs.

While the amount (39MtCO<sub>2</sub>e) is a small addition, the principle sets a damaging precedent and undermines the environmental integrity of the ESR.

Furthermore, this action is again likely to lead to increased costs over time because, of the larger and costlier emissions reductions that will be needed between 2030 and 2050, exposing counties which are already economically more vulnerable to the risk of transitional shocks.

## **7. A European project mechanism should be developed**

We support the development of a European Project Mechanism to allow more effective and efficient routes to the EU's long term climate targets and to enhance EU wide cooperation. Sandbag's research shows that a rebalancing of emission reduction efforts among the MS under the ESR could contribute to achieving an additional cost-effective reduction of 2 billion tonnes of CO<sub>2</sub>e over the period.

This is further supported by evidence from the 2030 IA, which the current IA refers to on page 19:

*"According to the 2030 Impact Assessment, five Member States with GDP per capita above the EU average have cost-effective mitigation potentials in effort sharing sectors below 30%, the required average total non-ETS reduction, and thus would see high costs per ton reduced emissions if targets would go well beyond 30% in 2030."*

This would enable a higher target for the whole instrument to be achieved at a lower cost.

An EPM would equalise these possibilities across the EU, enabling MS to "collectively reach their targets" as stipulated in the EUCO 2014. This would also enable future fungibility of credits/allowances with the EU ETS post 2030 as part of a wider architecture.

## **8. Compliance should be on an annual basis**

A legal instrument is only as strong as its compliance mechanism. The compliance mechanism set out in the ESR proposal, for reviews every five years, weakens the ESR and is not in line with the yearly reporting and the baseline proposed.

The change in compliance checks has been justified by the Commission in terms of saving administrative costs of approximately €0.5 million per year. However, this amount amounts to less than 0.001% of the EU yearly budget (approximation on the basis of the 2016 and 2015 budgets). When taking into account that the ESR covers 60% of the Union's emissions and that the cost of non-action on climate change can be much higher than the yearly compliance checks, we find this proposal to be contradictory to the principle of proportionality given the dimension of the challenge and the governance level required.

**Member States must be made accountable for their compliance with the ESR, with meaningful penalties for non-compliance.**

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