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From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
Subject:	Impact of the European Union carbon market on different EU policies - Information from Poland

In view of the meeting of the Council (General Affairs) on 27 June 2023, delegations find attached a note from the Polish delegation.

Polish explanatory note on the exchange of views concerning the impact of the EU carbon market on different EU policies, including energy, competitiveness of the EU economy, social standard of living in the EU

The need for a horizontal debate on the impact of the EU's carbon market on different EU policies

The EU is entering the period of increased ambition on reduction of greenhouse gas emissions with new challenges ahead. In recent years EU has developed climate legislation that affects many different EU policies. Therefore, it has an impact not only on environment but also on energy, industry, costs of transition, employment and other social issues. At the same time we already experience significant impact of carbon prices on energy prices. The consequences are twofold. On one hand, the costs of industrial production in the EU rise, thus adversely affecting global competitiveness of the European companies and economies. On the other hand, many European citizens are confronted with the growing risk of energy poverty. Therefore, we need to discuss the impact that the EU ETS has on prices of energy and all main socio-economic challenges that come with it, mainly the competitiveness of EU economy and the issue of energy poverty that threatens many of our citizens.

Why do we need this debate?

It is clear that significantly higher energy prices and their volatility should be attributed to a combination of factors. While some of them are positive and were expected (such as increased demand connected to post-pandemic economic recovery), others are beyond our control and unpredictable (extraordinary weather conditions, the record-high prices of natural gas, geopolitical situation). Thus, we shall focus on those factors that may be controlled as they are connected with the EU policies and actions, namely the EU ETS.

This is particularly pressing as the circumstances have changed significantly since the presentation of the Fit for 55 package. Various factors have led to record-high prices of EU allowances that put additional pressure on the increase and volatility of energy prices. Therefore, the Impact Assessments accompanying 2030 Climate Target Plan and the proposal of the revision of the EU ETS Directive are disconnected from current reality and not fit for purpose anymore. The current level of EUA prices has dramatically surpassed all of the scenarios for 2025 and 2030 that were presented in those documents. Yet, today our citizens and industries are facing growing challenges imposed by high prices of energy and EU allowances. Circumstances have changed and the time has come to take them into account in EU not in multiple sectoral debates but in a truly horizontal manner. Even though the impact of the prices of EU allowances on energy prices might differ from one Member State to another, it cannot be neglected. There are Member States characterised by high emission intensity of electricity and heat generation, which results in significantly higher share of EU allowances purchase costs in the energy price (in case of Poland the average share in the wholesale prices of electricity in 2022 amounted to 50%, while for the EU it was 20%).

The EU's share of global GDP dropped from 25% in 1990 to 17% in 2020 . This means that the global economic growth of the past three decades mainly took place outside the EU – in Asia and especially China. While part of this decline can be attributed to different starting points, it is worth noting that the EU's growth – and especially growth in the eurozone – was also slower compared to the US. The EU's relative share of global trade has decreased either. Comparing firms – the backbone of competitiveness – in Europe with their counterparts in the US reveals a substantial gap. Between 2014 and 2019, European businesses grew on average 40% slower than their US peers.

In 2022 compared to 2021, energy-intensive industries including basic metals, chemicals, non-metallic minerals and paper experienced a reduction in industrial production, while other manufacturing sectors saw an increase in output. For example, year-on-year, the manufacture of chemical products decreased by more than 6% and the production of basic metals dropped by 4% in 2022. This is followed by examples of enterprises reallocating their business activity outside the EU. For example, the world's largest chemical company by revenue announced it will shift away production from Europe due to high energy costs. This will lead to a loss of approximately 2,600 jobs.

Even though the energy prices have recently shown signs of stabilising, it had happened partly due to policies and interventions by the Member States' governments. However, it needs to be underlined that all the measures applied have burdened governmental accounts, thus reducing capacity for providing financial support to other areas (such as energy transition) . Moreover, taking into account that in 2022, increases in energy bills were contained, thanks to government interventions and fixed-price contracts, we must prepare for an another rise ahead of winter 2023 as Europe faces mounting competition for energy supplies from China.

While excessive energy prices increase the cost of living for all Europeans, the burden is not evenly distributed across the population. The adverse consequences are particularly felt by low-income households in poorly insulated dwellings without heat pumps in their cellars or solar panels on their roofs. According to Eurostat's figures, about 35 million EU citizens (approximately 8% of the EU population) were unable to keep their homes adequately warm in 2020. The surge in energy prices that started in 2021 and worsened with Russia's invasion of Ukraine in February 2022, along with the impact of the COVID-19 crisis, are likely to have worsened an already difficult situation for many EU citizens. Moreover, data from the EU Energy Poverty Observatory indicate that the estimated number of energy-poor citizens in the European Union could be up to 125 million people with the high energy prices being one of the three key factors causing this phenomenon. Inclusion of buildings and road transport sectors into the EU ETS may make the situation even worse.

Why the General Affairs Council is the right forum for this debate?

The General Affairs Council has a unique role in coordination of EU policies and horizontal dossiers. In line with Art. 16 para 6 of the Treaty on European Union the General Affairs Council shall ensure consistency in the work of the different Council configurations. As stated in Art. 2 para 2 of the Council's Rules of Procedure: "It shall be responsible for overall coordination of policies, institutional and administrative questions, horizontal dossiers which affect several of the European Union's policies, such as the multiannual financial framework and enlargement, and any dossier entrusted to it by the European Council, having regard to operating rules for the Economic and Monetary Union". Council configuration responsible for dealing with the EU ETS is the Environment Council. Yet, the impact of this scheme is multidimensional. It is closely related to issues that lie within the competences of other Council configurations. Firstly, Transport, Telecommunications and Energy Council dealing with high prices of energy and their volatility. Secondly, Competitiveness Council which is responsible for the competitiveness of European industry. Thirdly, Economic and Financial Affairs Council that deals with the costs of climate transition. Finally, Employment, Social Policy, Health and Consumer Affairs Council that is responsible for energy poverty.

The EU ETS system is one of the main instruments of EU climate policy. However, its direct impact on energy prices generates many risks for industrial production in the EU and growing risk of energy poverty (which will be increased by inclusion of buildings and road transport into the new ETS). Given the cross-cutting nature of this problem it should be urgently discussed in a manner enabling coordinated response to identified challenges. Therefore, we suggest that the General Affairs Council is tasked with holding a comprehensive dialogue on this matter. We need to coordinate EU policies affected by this scheme properly and provide more certainty for our citizens and industrial sectors.