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Delegations will find attached document SWD(2021) 552 final.

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COMMISSION STAFF WORKING DOCUMENT

Subsidiarity Grid

Accompanying the document

DECISION THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Decision (EU) 2015/1814 as regards the amount of allowances to be placed in the market stability reserve for the Union greenhouse gas emission trading scheme until 2030

{COM(2021) 571 final}

Subsidiarity Grid

1. Can the Union act? What is the legal basis and competence of the Unions' intended action?
1.1 Which article(s) of the Treaty are used to support the legislative proposal or policy initiative?
The legal basis for this proposal amending Decision (EU) 2015/1814 of the European Parliament and of the Council is Article 192 of the Treaty on the Functioning of the European Union (TFEU). In accordance with Article 191 and 192(1) TFEU, the European Union shall contribute to the pursuit, inter alia, of the following objectives: preserving, protecting and improving the quality of the environment; promoting measures at international level to deal with regional or worldwide environmental problems, and in particular combating climate change. The Decision established a market stability reserve (the MSR or the 'reserve') in 2018, to address the structural imbalance between the supply of and demand for allowances in the market and to improve the resilience of the EU Emissions Trading System (ETS) to major shocks. The reserve functions by triggering adjustments to the annual auction volumes.
1.2 Is the Union competence represented by this Treaty article exclusive, shared or supporting in nature?
In the case of environment, the Union's competence is shared.
*Subsidiarity does not apply for policy areas where the Union has **exclusive** competence as defined in Article 3 TFEU[1]. It is the specific legal basis which determines whether the proposal falls under the subsidiarity control mechanism. Article 4 TFEU[2] sets out the areas where competence is shared between the Union and the Member States. Article 6 TFEU[3] sets out the areas for which the Unions has competence only to support the actions of the Member States.*
2. Subsidiarity Principle: Why should the EU act?
2.1 Does the proposal fulfil the procedural requirements of Protocol No. 2[4]: - Has there been a wide consultation before proposing the act? - Is there a detailed statement with qualitative and, where possible, quantitative indicators allowing an appraisal of whether the action can best be achieved at Union level?
In order to collect evidence and ensure greater transparency, the Commission first invited feedback on an inception impact assessment, outlining the initial considerations and policy options of the revision[5]. The Commission then organised an online public consultation, receiving almost 500

[1] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E003&from=EN
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E004&from=EN
[3] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:12008E006:EN:HTML
[4] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12016E/PRO/02&from=EN
[5] The inception impact assessment was open for feedback from 29 October 2020 to 26 November 2020 and received about 250 contributions. The outcome can be found on the following website: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12660-Updating-the-EU-Emissions-Trading-System.

replies[6]. In addition, the Commission held (virtual) bilateral and multilateral stakeholder meetings, including with industry representatives across different sectors, trade unions, non-governmental organisations and Member States and participated in virtual conferences. Finally, the Commission instructed a contractor to organise two expert workshops[7] on the review of the Market Stability Reserve (MSR). The results of the consultation activities are reported in the impact assessment accompanying the proposal amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union (ETS Directive), and Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme (MSR Decision).

Articles 191 to 193 of the TFEU confirm and specify EU competencies in the area of climate change. Climate change is a trans-boundary problem, which cannot be solved by national or local action alone. Coordination of climate action must be taken at European level and, where possible, at global level. EU action is justified on grounds of subsidiarity as set out in Article 5 of the Treaty on European Union. Since 1992, the European Union has worked to develop joint solutions and drive forward global action to tackle climate change. More specifically, action at EU level will provide for cost effective delivery of the 2030 and long-term emission reduction objectives while ensuring fairness and environmental integrity.

In light of the emission reduction target for 2030, and in the perspective of the climate neutrality objective to be achieved by 2050, stronger EU action is needed, including with a more ambitious, well-functioning and resilient carbon market.

The explanatory memorandum of the proposal, and the impact assessment under chapter 3, contain sections on the principle of subsidiarity.

2.2 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the conformity with the principle of subsidiarity?

Yes, they do. The explanatory memorandum (as well as the accompanying impact assessment) explain that climate change is by its very nature a trans-boundary challenge that cannot be solved by national or local action alone. Coordinated EU action can effectively supplement and reinforce national and local action and enhances climate action.

Although initiatives at the national, regional and local level can create synergies, alone they will not be sufficient. On their own, individual Member States' carbon markets would represent too small a market to achieve the same level of results. Therefore, an EU wide approach is needed to drive industry level changes and to create economies of scale.

2.3 Based on the answers to the questions below, can the objectives of the proposed action be achieved sufficiently by the Member States acting alone (necessity for EU action)?

Article 3 of the MSR Decision tasks the Commission with reviewing the functioning of the MSR before 1 January 2022, on the basis of an analysis of the orderly functioning of the European carbon market.

[6] This was open for 12 weeks from 13 November 2020 to 5 February 2021. The outcome can be found on the following website: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12660-Updating-the-EU-Emissions-Trading-System/public-consultation.

[7] https://ec.europa.eu/clima/events/expert-workshop-market-stability-reserve_en, https://ec.europa.eu/clima/events/2nd-expert-workshop-market-stability-reserve_en.

The review of these elements should be considered together with the effects for market stability of increasing the ambition of the EU ETS, and is therefore proposed together with the *Proposal for Directive of the European Parliament and the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, and Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme*.

Nevertheless, it is necessary to separately amend the MSR Decision to maintain the current rate of allowances to be placed in the reserve each year after 2023 (intake rate). If the intake rate reverts to 12% after 2023, a potentially harmful surplus of allowances in the EU ETS may form. In addition, the rate of 24% after 2023 should be established as early as possible to ensure market predictability. This continuation of the 24% rate is necessary in the context of the proposal to increase the contribution of emissions trading in a manner commensurate with the overall EU emissions reduction target of at least -55% for 2030. This objective cannot be achieved by the Member States alone as it requires cost-efficient emissions reductions across the Union and increased resources that can only be achieved through the EU-level carbon market. The changes to the EU ETS to increase ambition for 2030, as well as the impact of external factors such as COVID-19 or national measures such as coal phase-outs, mean that the basic rules of the MSR must remain fit to continue tackling structural supply-demand imbalances.

(a) Are there significant/appreciable transnational/cross-border aspects to the problems being tackled? Have these been quantified?

Climate change is a trans-boundary problem and both international and EU action can effectively complement and reinforce regional, national and local action. The European Climate Law[8], as agreed by the co-legislators, makes the EU's climate neutrality target legally binding, and raises the 2030 ambition by setting a target of at least 55% net emission reductions by 2030 compared to 1990. The ETS covers 41% of the EU's greenhouse gas emissions. The environmental contribution of the ETS needs to be increased in a manner commensurate with the overall EU target for 2030. If the legislation remains unchanged, sectors currently covered by the ETS would together achieve a 2030 emission reduction of -51% compared to 2005 (see Section 5.1 of the impact assessment). This would be an insufficient contribution to an overall target of -55% compared to 1990. The policy scenarios that achieve around 55% reductions project a cost-effective contribution of the sectors currently covered by the ETS in the range of -62-63% compared to 2005. The MSR is essential for the orderly functioning of the European carbon market.

(b) Would national action or the absence of the EU level action conflict with core objectives of the Treaty[9] or significantly damage the interests of other Member States?

Urgent economy-wide emission reductions to combat climate change are necessary to fulfil the objectives of Article 192 TFUE, of preserving, protecting and improving the quality of the environment, protecting human health, as well as to promote measures at international level to deal climate change. The absence of EU level action could lead to 'environmental dumping' between the Member States, where Member States compete for the least stringent climate change measures to benefit their own economies, damaging the internal market and weakening climate action. An urgent climate transition requires a high degree of investments. As a result, foregoing the benefits of

[8] Regulation (EU) 2021/... of the European Parliament and of the Council of ... establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law') (OJ L ...).

[9] https://europa.eu/european-union/about-eu/eu-in-brief_en

economies of scale and the possibility of reducing emissions where they are more cost-effective, would result in a slower climate transition due to increased costs and less available funds.
(c) To what extent do Member States have the ability or possibility to enact appropriate measures?
Member States are able to act to reduce greenhouse gas emissions that are under the scope of the EU ETS through other policies than emission limits adopted pursuant to Directive 2010/75/EU. However, they are not able to establish an EU-level carbon market. In particular, national action remains important in the areas of buildings and road transport, for which a separate EU level emissions trading system is proposed as additional economic incentive to achieve cost-effective emission reductions.
(d) How does the problem and its causes (e.g. negative externalities, spill-over effects) vary across the national, regional and local levels of the EU?
The effects of raising the contribution of emissions trading towards a higher emissions reduction target will not be felt equally across the EU, as their starting point in terms of the emissions in the sectors covered by the Directive are not the same. Some Member States will be more affected than others. Increasing the contribution of the ETS to achieve the revised target will require investments in the energy systems and the greening of industrial processes in Member States where modernisation needs are already the highest. Regions and local communities in which employment is linked to fossil fuel production are impacted more significantly than others. Furthermore, there are distributional concerns within Member States, as low-income households across the EU will bear a relatively higher burden notably in terms of heating fuel expenses compared to wealthier households. Hence, there are likely to be different distributional issues that emerge if the EU emissions trading is expanded to new sectors. At the same time, there will be also positive social impacts, like an improvement concerning health issues linked with air pollution. In addition, emissions trading generates auction revenues which can be used by Member States to address these problems, including if there were specific problems at regional or local level.
(e) Is the problem widespread across the EU or limited to a few Member States?
The need to address climate change is widespread across the EU.
(f) Are Member States overstretched in achieving the objectives of the planned measure?
The ETS Directive establishes a carbon market in the EU, without specific targets per Member State. Emission reductions take place where they are most cost-efficient. Nevertheless, the ETS Directive includes measures to mitigate the distributional and social effects of the ETS explained in point 2.3(d) above, reinforced by the proposal. In addition, Decision (EU) 2015/1814 establishes a market stability reserve for the ETS with an intake until 2025 that is only based on the 90% regular auctioning shares, exempting the 10% solidarity shares, continued in the ETS Directive proposal. The proposed new Regulation on a social facility for climate action addresses the social impacts of carbon pricing in the new emissions trading system for buildings and road transport.
(g) How do the views/preferred courses of action of national, regional and local authorities differ across the EU?
The ETS is widely supported across the Union. The different views or preferred courses of action do not relate to the use of the ETS in itself, but to aspects of its design.

2.4 Based on the answer to the questions below, can the objectives of the proposed action be better achieved at Union level by reason of scale or effects of that action (EU added value)?

The objectives of the proposed action be better achieved at Union level by reason of the cost-efficiency of emissions reductions, coherence of EU action, preserved functioning of the internal market and strengthened EU position to foster global action on climate change. By extension, as the MSR is a tool for stability of the market established by the EU ETS Directive, its objective also cannot be sufficiently achieved by unilateral action by the Member States.

(a) Are there clear benefits from EU level action?

Yes. The benefits from EU level actions relate to the economies of scale and improvement of the EU internal market explained below. In addition, EU action can also inspire and pave the way for the development of market based measures at global level, e.g. as regards the maritime transport within International Maritime Organisation. EU action also allows the EU to have a stronger position internationally to apply a Carbon Border Adjustment Mechanism, which will be based on the ETS to ensure compliance with the World Trade Organisation rules.

(b) Are there economies of scale? Can the objectives be met more efficiently at EU level (larger benefits per unit cost)? Will the functioning of the internal market be improved?

Yes. As a carbon market, the ETS incentivises emission reductions to be made by the most cost-efficient solutions first across the activities it covers, achieving greater efficiency by virtue of its scale. Implementing a similar measure nationally would result in smaller, fragmented carbon markets, risking distortions of competition and likely lead to higher overall abatement costs. The same logic holds for the extension of carbon pricing to new sectors.

Many of the policy elements of the proposal have an important internal market dimension, in particular the options related to the carbon leakage protection and the low-carbon funding mechanisms.

(c) What are the benefits in replacing different national policies and rules with a more homogenous policy approach?

The benefits of a more homogenous approach are highlighted in point 2.4(b) above. Emission reductions take place where they are most cost-effective, thus reducing the overall cost of the climate transition for the EU. Emissions reductions also take place without distorting the internal market, and preventing environmental dumping. As highlighted in point 2.3(c) above, for the new ETS for buildings and road transport, the aim is not to replace but to complement national policies.

(d) Do the benefits of EU-level action outweigh the loss of competence of the Member States and the local and regional authorities (beyond the costs and benefits of acting at national, regional and local levels)?

The benefits of EU-level action outweigh the loss of competence of the Member States and the local and regional authorities, because reducing greenhouse gas emissions is fundamentally a trans-boundary issue that requires urgent effective action at the largest possible scale. The EU, as a supranational organisation is well-placed to establish effective climate policy in the EU. Concretely, the benefits are the cost-efficiency of emissions reductions, coherent EU action, preserved functioning of the internal market and strengthened EU position to foster global action on climate change.

(e) Will there be improved legal clarity for those having to implement the legislation?

Yes.

3. Proportionality: How the EU should act

3.1 Does the explanatory memorandum (and any impact assessment) accompanying the Commission's proposal contain an adequate justification regarding the proportionality of the proposal and a statement allowing appraisal of the compliance of the proposal with the principle of proportionality?

This proposal complies with the proportionality principle because it does not go beyond what is necessary in order to achieve the Union's objectives of reducing greenhouse gas emissions by establishing a well-functioning carbon market to reduce emissions in a cost-effective manner, while ensuring fairness and environmental integrity.
The European Climate Law has endorsed an overall economy-wide and domestic reduction in greenhouse gas emissions of at least 55% below 1990 levels by 2030 and climate neutrality by 2050.
All options analysed for the strengthening of the existing ETS are based on the already existing instrument, the ETS Directive. The initiative is limited to ETS adjustment needs that are triggered by this increased emissions reduction target of at least 55%.
The instrument of emissions trading ensures that additional costs for industry due to the increased level of ambition of the EU's climate policies are expected to be kept to a minimum, given that the ETS incentivises emissions reduction by operators with the lowest abatement costs. Moreover, the use of the existing instruments minimises any additional administrative costs. In this context, the proposal to amend the MSR Decision does not extend the scope of EU action, as it only ensures that its current parameters continue to work as they currently do until revised in the context of the proposal to review the ETS.

3.2 Based on the answers to the questions below and information available from any impact assessment, the explanatory memorandum or other sources, is the proposed action an appropriate way to achieve the intended objectives?

The proposal is the appropriate way forward to ensure that the intake rate of the MSR does not revert to 12% after 2023, preventing the formation of a potentially harmful surplus of allowances in the EU ETS.

(a) Is the initiative limited to those aspects that Member States cannot achieve satisfactorily on their own, and where the Union can do better?

Yes, the proposal is limited to continuing the intake rate of the market stability reserve of the EU ETS, which is implemented by the Commission, so it does not entail further limitations to Member States' competences.

(b) Is the form of Union action (choice of instrument) justified, as simple as possible, and coherent with the satisfactory achievement of, and ensuring compliance with the objectives pursued (e.g. choice between regulation, (framework) directive, recommendation, or alternative regulatory methods such as co-legislation, etc.)?

The objectives of this proposal can be best pursued through a Decision. The MSR is an existing EU policy instrument adopted in 2015. A Decision is the appropriate instrument for this single amendment to the Decision establishing the MSR.

(c) Does the Union action leave as much scope for national decision as possible while achieving satisfactorily the objectives set? (e.g. is it possible to limit the European action to minimum standards or use a less stringent policy instrument or approach?)

Yes.
(d) Does the initiative create financial or administrative cost for the Union, national governments, regional or local authorities, economic operators or citizens? Are these costs commensurate with the objective to be achieved?
The EU ETS generates significant revenues for Member States' budgets. Most of the auctioning revenues accrue to Member States. The proposal affects national budgets and administrations primarily because of this link. Maintaining the current intake rate of the MSR will reduce the auction volumes of the Member States. However, this is expected to be compensated by the effect on the price of a reduced surplus of allowances. The direct impact on national budgets will also depend on to which extent revenues will be directed to EU own resources. In line with the inter-institutional agreement on the budgetary matters[10], the Commission is proposing an own resource based on the EU ETS[11]. The MSR is implemented by the Commission, so it entails no administrative costs for national governments, regional or local authorities. In addition, extending the application of the intake rate of 24% will not create further administrative burden for the Union because it implies the same administrative process as applying a 12% intake rate.
(e) While respecting the Union law, have special circumstances applying in individual Member States been taken into account?
Yes, see point 2.2.(f).

10 OJ L 433I , 22.12.2020, p. 28–46.

11 […].