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From:	General Secretariat of the Council
To:	Working Party on the Environment
N° prev. doc.:	WK 123/2022
Subject:	Fit for 55 package - ETS: Comments from delegations

Following the call for comments on the above set out in WK 123/2022 regarding clusters 4 (Cap and Linear Reduction Factor), 7 (Market Stability Reserve) and 8 (Miscellaneous), delegations will find attached comments from the CZ and EE delegations.

CZECH REPUBLIC

CZ non-paper: A proposal for measures dealing with excessive allowance price fluctuations in the EU ETS, Article 29a and Article 30h (20. 1. 2022)

CZ acknowledges that Art. 29a is an instrument for preventing very steep (thus relative) price increases, rather than keeping the price from rising above any subjective level, it is not intended as some sort of price corridor mechanism. CZ is fully aware of the elements that have led to current energy price spikes and we would like to stress that this paper does not intend to correct the current situation on energy markets. Nonetheless, the situation with the allowance price fluctuations proved that Art. 29a cannot in fact be activated at all. That is why CZ proposes to alter the mechanism so that it better serves its purpose in the future, if needed. The revision of Directive 2003/87/EC contains two elements focussed on potentially harmful increases of the emission allowance price, Art. 29a and Art. 30h.

Firstly, current version of Art. 29a is designed to release additional allowances on the market in case of a rapid increase of the price, based on the comparison of price averages from previous 6 months and preceding 2 years, making it a tool for a correction of rather long-term trends. Therefore, the applicability of the measure pursuant to Art. 29a is very limited and actually decreases with increasing allowance price. This is because the mechanism of triggering Art. 29a uses the relative increase of price for comparison of absolute numbers (price averages). A twice or three times increase on the price level of e.g. 10 EUR is thus hardly comparable with the same relative increase on the price level around 80 EUR (compare an increase by 20 EUR and by 160 EUR!). Additionally, according to Art. 29a the conditions must be fulfilled continuously for six months, so the rolling average moves forward, incorporating the increasing prices in the calculations and making Art. 29a even less likely to apply. As such, we fear that current version of Art. 29a cannot be expected to apply at all in the future.
The second measure is Art. 30h, proposed for the allowance market in the sectors of buildings and road transport. Art. 30h seems much more flexible, using shorter and more recent reference periods (last 3 months and preceding 6 months). However, the multipliers required for a release of allowances from Market Stability Reserve (MSR) pursuant to Art. 30h seem still too high to enable the application of that measure. Furthermore, some additional clarifications with regard to MSR and practical applicability of the mechanism are needed.

Since we recognize a need for a functioning tool to correct extreme potentially harmful price increases on the market (not the price level as such), CZ suggests the following:

1) **Delete current wording of Art. 29a**
2) **Modify and extend Art. 30h to make it clearer and better applicable**
3) **Replace Art. 29a with amended text of Art. 30h (with adjusted references)**

CZ suggests concrete changes of Art 30h and Art. 29a in para (1) and (2), and new paras (3) and (4). Additional adjustment is mirrored also in Art. 1(7) of MSR Decision. CZ stresses that proposed measures are not intended to reduce or manipulate long-term allowance price. The aim is to prevent excessive price fluctuations and increase predictability of the EU emission trading system.

Initial proposal for wording of Article 29a (Chapter III) and Article 30h (Chapter IV):

(New) Article 29a of Directive 2003/87/EC (changes in **red** compared to CION proposal of Art. 30h):

Measures in the event of excessive price increase

1. Where, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than ~~**twice**~~**[1,4] times** the average price of allowance during the six preceding consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, as a matter of urgency, adopt a decision to release 50 million allowances covered by this Chapter from the Market Stability Reserve in accordance with **Article 1(7)** of Decision (EU) 2015/1814 **equally distributed within auctions during a period of [three] months**.

2. Where, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than ~~**three**~~ **[2,1]** times the average price of allowance during the six preceding consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, as a matter of urgency, adopt a decision to release 150 million allowances covered by this Chapter from the Market Stability Reserve in accordance with **Article 1(7)** of Decision (EU) 2015/1814 **equally distributed within auctions during a period of [three] months.**

(New) 3. When measures pursuant to paragraph (1) or (2) of this Article are adopted, similar measures pursuant to paragraphs (1) or (2) shall not be adopted earlier than [three] months thereafter.

(New) 4. When measures pursuant to paragraph (1) or (2) of this Article are adopted, the amount of allowances subsequently released from the Market Stability Reserve shall not be included in the calculations of total number of allowances in circulation in accordance with Article 1(4) of Decision (EU) 2015/1814 in that respective calendar year or if not possible[1] for the following calculation.

Corresponding adjustment of Article 1(7) of Decision (EU) 2015/1814 (MSR):

7. In any year, if paragraph 6 of this Article is not applicable and measures are adopted under Article 29a of Directive 2003/87/EC, ~~100 million~~ **the amount of** allowances **referred to in paragraph (1) or (2) of that Article** shall be released from the reserve and added to the volume of allowances to be auctioned by the Member States under Article 10(2) of Directive 2003/87/EC. Where fewer than ~~100 million~~ **the amount of** allowances **referred to in paragraph (1) or (2) of Article 29a** are in the reserve, all allowances in the reserve shall be released under this paragraph.

[1] *Ad para 4: In case the measure is activated after September and allowances have already been withdrawn to / released from the MSR in that year.*

<u>Article 30h of Directive 2003/87/EC:</u>

Measures in the event of excessive price increase

1. Where, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than ~~twice~~[1,4] times the average price of allowance during the six preceding consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, as a matter of urgency, adopt a decision to release 50 million allowances covered by this Chapter from the Market Stability Reserve in accordance with Article 1a(7) of Decision (EU) 2015/1814. **<u>Where fewer than 50 million allowances are in the reserve, all allowances in the reserve shall be released under this paragraph.</u>**

2. Where, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than ~~three~~ [2,1] times the average price of allowance during the six preceding consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, as a matter of urgency, adopt a decision to release 150 million allowances covered by this Chapter from the Market Stability Reserve in accordance with Article 1a(7) of Decision (EU) 2015/1814. **<u>Where fewer than 150 million allowances are in the reserve, all allowances in the reserve shall be released under this paragraph.</u>**

(New) <u>3. Where measures pursuant to paragraph (1) or (2) of this Article are adopted, similar measures pursuant to para (1) or (2) shall not be adopted earlier than [three] months thereafter.</u>

(New) <u>4. When measures pursuant to paragraph (1) or (2) of this Article are adopted, the amount of allowances subsequently released from the Market Stability Reserve shall not be included in the calculations of total number of allowances in circulation in accordance with Article 1a(4) of Decision (EU) 2015/1814 in that respective calendar year or if not possible[2] for the following calculation.</u>

[2] *Ad para 4: In case the measure is activated after September and allowances have already been withdrawn to /released from the MSR in that year.*

→ **Justification for changes in paragraphs (1) and (2):**

Change of multipliers (29a, 30h) – Based on the data of the most recent 2021 relative increase of allowance price, the measures pursuant to Art. 30h are yet not applicable with the currently proposed multipliers even if the increase is definitely steep. With a steadily growing price the probability of application based on these relative multipliers actually even decreases. Based on historical development of EUA price in 2019-2021 (see Annex below), the lower required multiplier should be **between 1.2 and 1.6** instead of 2 to enable effective activation of this measure, and the higher multiplier adequately as well. The multiplier in para (2) is thus adjusted by the same ratio.

Explanation for the case of insufficient amount of allowances in MSR (30h) – This paragraph in the case of Article 30h newly specifies the situation, when there are not enough allowances remaining in MSR for full application of proposed measures. Even though there is still a significant surplus of allowances on the market at the moment and the reserve is sufficient, this paragraph may become relevant after future cancellations of allowances from the MSR and potentially also after the application of Art. 6 of Decision (EU) 2015/1814 (MSR) or as a consequence of repeated application of Art. 29a and/or 30h. In case of **Article 29a**, the provision is already included in the legal text; therefore, we use the exact same wording. Nonetheless, the numbers concerning the amount of allowances need to be adjusted also in Art. 1(7) of the MSR Decision to reflect the proposal in para (1) and (2) of Art. 29a.

Distribution of allowances over time (29a)– The proposals keep currently applicable distribution between Member States in both Articles. It additionally clarifies, that in the case of Article 29a, the distribution within auctions should happen equally during three months period. A provision that is already proposed by the Commission in the case of **Article 30h**.

→ **Justification for new para 3:**

Restriction on repetitive application (29a, 30h) – The proposed change specifies, what happens when the criteria for a release of allowances from MSR are met for a longer period, enabling a repetitive application of these Articles. Considering that more or less 15 auctions per month take place and auction volumes should be increased gradually with caution, the suggested minimum three months break between the applications of the measure seems reasonable. Applied during suggested three months, the estimated auction volume increase would be in low millions of allowances per auction, enabling relatively fast release of the allowances on the market, while not distorting the auctions too much one at a time.

→ **Justification for new para 4:**

Compatibility with MSR – The effects of the Art. 29a/30h measures on the functioning of the MSR must be taken into account. It does not make sense to release allowances based on Art. 29a/30h and then withdraw them at the same time to MSR (or contra-wise) if the thresholds are triggered after the calculation of the total number of allowances in the circulation (TNAC), possibly due to adopted Art. 29a/30h measures. However, it would also be confusing to over-complicate or even jeopardise the functionality of the MSR itself. Therefore, at this point, we suggest not to count the allowances released due to Art. 29a and/or 30h for the purposes of calculating TNAC for triggering MSR (Art 1(4) and 1a(4) of MSR Decision) in the respective year or, if not possible, at least for the next MSR application.

<u>Questions for consideration that impact the proposal above:</u>

1. What measures are preferable:

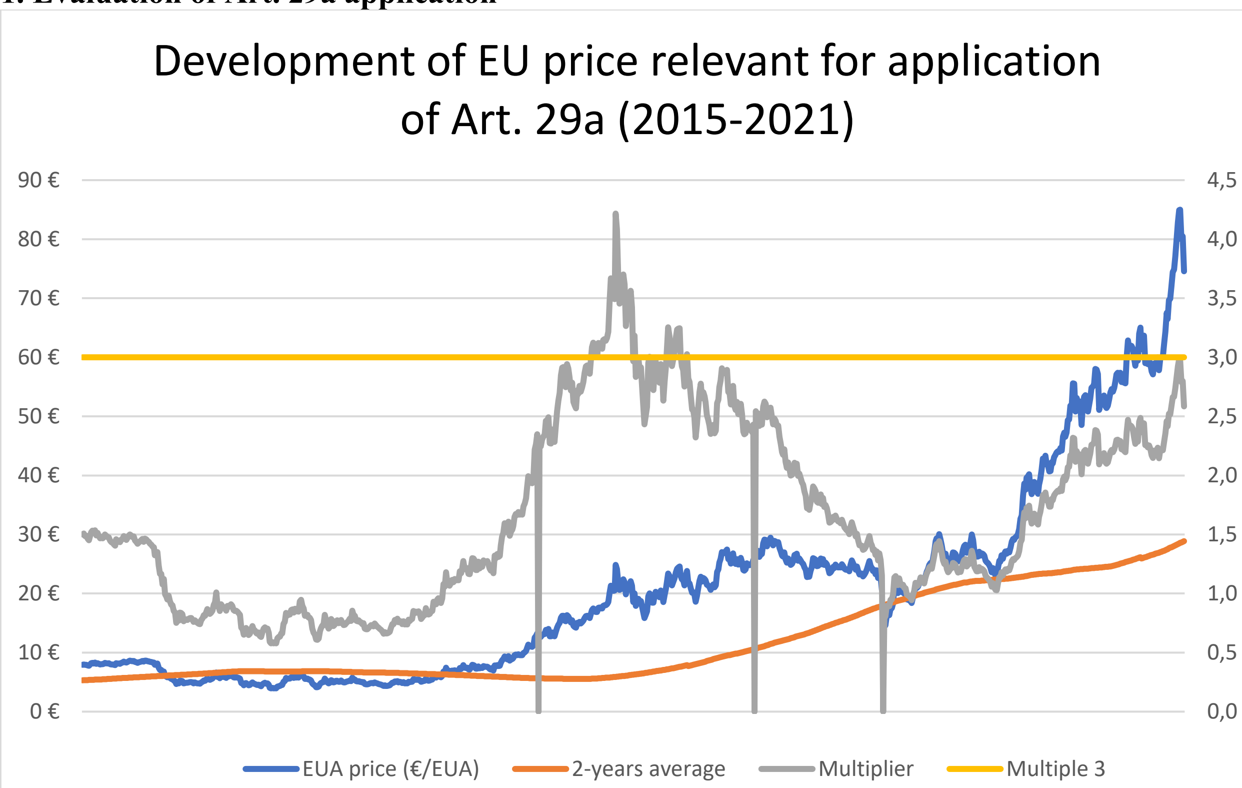
- Regulation of potentially harmful short and medium term EUA price fluctuations by an automatically applicable measure such as one proposed? What other options available?
- Regulation of long-term EUA price?
- Both? Others?
- No measures regulating price fluctuations by releasing new allowances on the market?

2. If such measures should be considered, what is the optimal setting of used parameters:

- Length of reference periods?
- Level of Multipliers? Should they be identical for "old" ETS and ETS BRT?
- Amounts of allowances to be released? Should they be identical for both ETSs?
- Minimal period between application of measures pursuant to paragraph (1) or (2?
- Are there any other factors that should be included in order to make the mechanism more functional and responsive while preserving the stability and predictability of the market?

<u>Annexes</u>:

1. Evaluation of Art. 29a application



The chart illustrates that the requirements for application of Art. 29a have been met only for very short time periods during the previous years and that even the most recent rapid price increase is not sufficient for this. Source: EEX, 2021, CZ Ministry of the Environment 2022.

2. EUA price multiples for 3- and 6- months periods according to Art. 30h proposal

Real price 2021 (month averages)				
	EUA price	6 month average	3 month average	Multiple
2019/1	22,99	x	x	x
2019/2	20,99	x	x	x
2019/3	21,80	x	21,92	x
2019/4	25,25	x	22,68	x
2019/5	25,49	x	24,18	x
2019/6	24,93	x	25,22	x
2019/7	28,05	x	26,15	x
2019/8	27,19	x	26,72	x
2019/9	25,66	23,57	26,96	1,14
2019/10	24,56	24,42	25,80	1,06
2019/11	24,56	25,45	24,93	0,98
2019/12	24,53	26,09	24,55	0,94
2020/1	24,40	25,98	24,50	0,94
2020/2	23,89	25,82	24,27	0,94
2020/3	19,84	25,76	22,71	0,88
2020/4	20,08	25,15	21,27	0,85
2020/5	19,51	24,60	19,81	0,81
2020/6	23,33	23,63	20,97	0,89
2020/7	27,47	22,88	23,44	1,02
2020/8	26,45	22,04	25,75	1,17
2020/9	27,60	21,84	27,17	**1,24**
2020/10	25,09	22,35	26,38	1,18
2020/11	26,31	22,78	26,33	1,16
2020/12	29,75	24,07	27,05	1,12
2021/1	30,92	24,91	28,99	1,16
2021/2	37,45	26,04	32,71	**1,26**
2021/3	40,42	27,11	36,26	**1,34**
2021/4	44,75	27,69	40,87	**1,48**
2021/5	52,15	29,52	45,77	**1,55**
2021/6	52,64	31,66	49,85	**1,57**
2021/7	53,59	34,93	52,79	**1,51**
2021/8	56,30	39,24	54,18	**1,38**
2021/9	61,55	43,05	57,15	**1,33**
2021/10	59,52	46,83	59,12	**1,26**
2021/11	65,68	49,97	62,25	**1,25**
2021/12	80,62	53,50	68,61	**1,28**

The table illustrates what multipliers in the sense of Art. 30h proposal are currently met. If the recent EUA price increase should be regulated by that measure, the required lower multiplier would need to be set between 1.2 and 1.6 to release 50 million allowances.

<u>ESTONIA</u>

Comments on the proposal for a directive amending the EU ETS Directive (2003/87/EC) and decision of the market stability reserve (EU) 2015/1814

Estonia would like to express appreciation for an opportunity to provide comments on the EU ETS proposals. Estonia still has the parliamentary scrutiny on the proposals and these comments should be viewed as preliminary. Parts to be deleted are ~~strikethrough~~. Added wording is in **bold**.

1. <u>Amendments on the Article 29a, Linear Reduction Factor in the Directive 2003/87/EU</u>

Rationale: For Estonia, it is important that changes to the directive would not cause extensive changes to the auctioning of the ETS, which would affect the availability of allowances. Therefore, we would prefer to not have a rebase of the cap and instead have a slightly higher LRF. According to the Impact Assessment accompanied the Commission proposal, the LRF should be 5.1 % without the rebase. In addition, this would help avoid the implementation of CSCF and would allow us to reach to the same emission reduction target by 2030. Estonia would also support a LRF that would increase over the 2024-2030 period, while ensuring the achievement of the 61% target.

- We propose the recital 27 to be deleted.
- Article 9: "I~~n [the year following entry into force of this amendment], the Union-wide quantity of allowances shall be decreased by [-- million allowances~~ ~~*(to be determined depending on year of entry into force)*~~]~~. In the same year, the Union-wide quantity of allowances shall be increased by 79 million allowances for maritime transport.~~ Starting in [the year following entry into force of this amendment], the linear factor shall be ~~4,2~~ **[X,X]** %. **In the same year, the Union-wide quantity of allowances shall be increased by 79 million allowances for maritime transport.** The Commission shall publish the Union-wide quantity of allowances within 3 months of [date of entry into force of the amendment to be inserted].";

2. <u>Amendment linked to Article 29a</u>

Rationale: The proposal would allow a swifter operationalization of Article 29a without changing the overall market fundamentals. If this proposed wording for the Article 29a provision would have been in place last year, the article 29a would have been triggered in 2021, when the price was above 49 euros for more than 2 consecutive months and by the end of June 100 million allowances would have started to be released to the market.

- Recital 26 a (new): **In order to prevent excessive price hikes and provide stability to the market, respective safeguards should be in place. To that end, measures provided in the Article 29a of the directive 2003/87/EU should be reviewed.**
- Article 29a (1): If, for more than ~~six~~ **two** consecutive months, the **average** allowance price is more than ~~three~~ **two** times the average price of allowances during the two preceding years on the European carbon market, the Commission shall immediately ~~convene a meeting of~~

~~the Committee established by Article 9 of Decision No 280/2004/EC.~~ **adopt a decision to release 100 million allowances covered by this Chapter from the Market Stability Reserve in accordance with Article 1(7) of Decision (EU) 2015/1814.**

- Article 29a (1a) (new): **If a decision referred to in paragraph 1 has been made, the Commission shall not make any subsequent decisions referred to in paragraph 1 in the 12 months following the adoption of such decision.**
- Article 29a (2) should be deleted.
- Article 29a (3): 3. **The decision referred to in Paragraph 1 of this Article** ~~Any measure~~ shall take utmost account of the reports submitted by the Commission to the European Parliament and to the Council pursuant to Article 29, as well as any other relevant information provided by Member States.

3. Amendments to the decision on the Market Stability Reserve (EU) 2015/1814

Rationale: With the reducing cap, the higher intake rate would not be necessary to achieve the targets set out in the Directive. In our view, the total allowances in circulation (TNAC) has already been significantly reduced to the point where the system is functioning in the way it is intended. 2021 has shown that the current level of TNAC there is no significant oversupply on the market due to the increased hedging. Therefore, the MSR intake rate should be kept at 12% between 2024 and 2030. We would also like to propose that the maximum intake of allowances should be capped at 25% of the auctioning amount.

- Recital 62: Considering the need to deliver a **stable and** strong~~er~~ investment signal to reduce emissions in a cost-efficient manner and with a view to strengthening the EU ETS, Decision (EU) 2015/1814 should be amended ~~so as to increase the percentage rate for determining the number of allowances to be placed each year in the Market Stability Reserve~~. **Considering the decreasing supply of allowances due to a higher overall greenhouse gas reduction target, a cap should be set to the number of allowances to be placed each year to the Market Stability Reserve in order to maintain a steady supply.** In addition, for lower levels of the TNAC, the intake should be equal to the difference between the TNAC and the threshold that determines the intake of allowances. This would prevent the considerable uncertainty in the auction volumes that results when the TNAC is close to the threshold, and at the same time ensure that the surplus reaches the volume bandwidth within which the carbon market is deemed to operate in a balanced manner.
- Article 5 (1): In any given year, if the total number of allowances in circulation is between 833 million and 1 096 million, a number of allowances equal to the difference between the total number of allowances in circulation, as set out in the most recent publication as referred to in paragraph 4 of this Article, and 833 million, shall be deducted from the volume of allowances to be auctioned by the Member States under Article 10(2) of Directive 2003/87/EC and shall be placed in the reserve over a period of 12 months beginning on 1 September of that year. If the total number of allowances in circulation is above 1 096 million allowances, the number of allowances to be deducted from the volume of allowances to be auctioned by the Member States under Article 10(2) of Directive 2003/87/EC and to be placed in the reserve over a period of 12 months beginning on 1 September of that year shall be equal to 12 % of the total number of allowances in circulation. ~~By way of derogation from the last sentence, until 31 December 2030, the~~

~~percentage shall be doubled.~~ **The number of allowances to be placed in the reserve during the next 12 months should not exceed 25 % of the number of allowances to be auctioned during the next 12 months.**