MAY 2021

CAN EUROPE'S POSITION ON THE REVISION OF THE EFFORT SHARING REGULATION (ESR)

Climate Action Network (CAN) Europe is Europe's leading NGO coalition fighting dangerous climate change. With over 170 member organisations from 38 European countries, representing over 1.500 NGOs and more than 47 million citizens, CAN Europe promotes sustainable climate, energy and development policies throughout Europe.

EU and Member State climate legislation remains off track with the international commitments to stop climate change and limit temperature increase to 1.5°C as agreed in the Paris Agreement. The Effort Sharing Regulation (ESR) needs to be substantially strengthened and nationally binding targets increased to ensure a robust overall policy architecture that can achieve at least 65% overall emission cuts in the EU by 2030.

CAN EUROPE'S DEMANDS FOR THE ESR

1. **The collective ambition of the upcoming legislative package must go well beyond net 55% greenhouse gas emission reductions.** In light of Europe's historic responsibility and its capacity to act, CAN Europe is calling for the EU to reduce its domestic greenhouse gas emissions by at least 65% by 2030, as compared to 1990 levels. **The Effort Sharing Regulation should achieve at least 50% emission reductions by 2030, compared to 2005 levels.**

2. **National binding targets under the Effort Sharing Regulation have to be retained and substantially increased; compliance, governance and reporting strengthened.** The fight against climate change is the biggest collective challenge of our time and Member States need to take full responsibility and remain accountable to achieving emission reductions in key economic sectors such as transport, buildings and agriculture.

3. **Road transport, buildings and agriculture emissions should be kept in the Effort Sharing Regulation.** Extending emissions trading to sectors currently outside of the EU Emissions Trading System (ETS) is not a silver bullet. While carbon pricing is essential to ensure the Polluter Pays Principle, it is insufficient to address key non-market barriers to deploying clean energy solutions at scale in the transport and building sectors.

4. **Adjust allocated emissions allowances to reality**: the upcoming revisions need to improve the integrity of the EU climate policy framework and emission reduction

trajectories, by ensuring that the starting points for both the EU ETS and the Effort Sharing Regulation reflect real emission levels and loopholes for carbon accounting are fully eliminated.

5. **Closing existing loopholes/limit flexibilities** - Carbon removals must not serve as offsets for emission reductions. Including carbon sinks into the EU's climate target creates a dangerous precedent and effectively creates trade-offs between sink enhancement efforts and mitigation action, while both are urgently required and need to be maximised separately. The possibility for countries to use surplus allowances from the ETS to reduce efforts in the non-ETS sectors must also be revoked. All sectors must contribute to the climate target.

While this position paper addresses key issues for the revision of the ESR, please refer to our accompanying position papers with regards to our general demands on the overall EU climate policy architecture, the revision of the EU Emissions Trading System (ETS), the revision of the EU energy targets and carbon pricing and LULUCF.

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BACKGROUND AND DETAILED POSITION

The review of the climate legislation - 'Fit for 55' package

The EU Emissions Trading Scheme (ETS) Directive, together with the Effort Sharing Regulation (ESR) and the LULUCF Regulation are the EU's main climate instruments implementing the EU's 2030 climate target. While the LULUCF Regulation mainly deals with net carbon emissions and removals from land based sources, the EU's overall emission reductions are divided into a contribution from the sectors covered by the ETS (mainly power, industry and aviation) and the ESR (mainly agriculture, transport, buildings and waste). Under the previous EU climate target of at least 40% emission reductions by 2030, ETS sectors were set to decrease emissions by 43% compared to 2005 levels while sectors covered by the ESR had to reduce their emissions by 30% compared to 2005 levels. The ESR target is divided into 27 nationally binding targets (and the national ESR target is translated into 10 annual targets for the period 2021-2030 for each of the 27 EU Member States).

Following the increase of the EU's economy-wide climate target to achieve at least 55% net emission reductions by 2030, compared to 1990 levels, the European Commission is preparing a comprehensive review of EU energy and climate legislation, including the Effort Sharing Regulation (ESR). What they call the 'Fit for 55' package, a comprehensive revision of key EU energy and climate legislation including the ESR, is going to be released in July 2021. The revised laws might modify the scope and overall ambition level of the ESR, how Member States share this ambition, the flexibility mechanisms and the monitoring, reporting and compliance systems in place.

CAN Europe's demands for the ESR

1. Bring the ambition of the ESR in line with the 1.5°C of the Paris Agreement

In order to reflect its capacity to act and its responsibilities as a major historic emitter, the European Union should achieve at least 65% emission cuts by 2030 in order to honor the 1.5°C goal of the Paris Agreement. The EU's implementing legislative framework needs to be upgraded and each policy piece needs to be brought in line with this higher level of ambition and **go well beyond net 55% greenhouse gas emission reductions. This means for the ESR to achieve at least 50% emission reductions by 2030, compared to 2005 levels[1].**

CAN Europe calls for:

- Each piece of the EU 2030 climate and energy framework as well as the entire policy package as a whole **to be in line with a 1.5°C compatible pathway**. The ESR and the EU ETS should jointly achieve at least 65% overall emission cuts by 2030. For further details on our demands regarding the overall climate policy architecture, please refer to our respective position papers.[2]
- The ESR must contribute its full share to the achievement of an EU overall 2030 climate objective of at least 65%. This means, sectors covered by the **ESR should achieve at least 50% emission reductions by 2030, compared to 2005 levels.**

2. National binding targets under the Effort Sharing Regulation have to be retained and substantially increased, compliance and governance strengthened

One option the European Commission is exploring in the revision would mean repealing the ESR altogether, shifting emissions from road transport and buildings into the EU ETS and merging the agricultural sector with the LULUCF sector (into a new 'AFOLU' pillar), while tackling the remaining non-ETS emissions through dedicated regulation. This would also imply the removal of nationally binding targets for Member States. This would be unacceptable. On the contrary, the sectoral scope of ESR should be maintained, the regulation strengthened to deliver the overall climate target and make sure each and every Member State does its fair share of the reduction.
All countries must prioritise urgent action addressing the climate emergency with the aim of implementing the Paris Agreement's ambition to limit temperature rise to 1.5°C.

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[1] https://www.umweltbundesamt.de/sites/default/files/medien/376/publikationen/w_p_04_paper_raising_the_eu_2030_ghg_emission_reduction_target_with_german-language_summary_rev.pdf + own calculations

[2] Position paper on climate policy architecture (under construction: https://docs.google.com/document/d/1XmfE83X1PIle1dOx3-x1xEoKeNOao-CI0BF98kIN40g/edit#)

This will need a substantial increase in climate action in the short term, with the aim of setting clear pathways for reducing greenhouse gas emissions to almost zero and substantially increasing the removal capacity of natural sinks within the next two decades. According to the EEA national action across all sectors is needed to reach the Effort Sharing targets[3].
In order to underpin the achievement of these increased efforts, governance mechanisms at EU and national level should be enhanced and further streamlined in order to ensure effective verification and accounting of emissions and robust and transparent monitoring and reporting of progress. **Member States should be obliged to meet their binding national targets and compliance should be annually monitored and enforced** through prompt infringement procedures and/or monetary penalty.

CAN Europe calls for

- **Binding, increased national emission targets** - designed with clear alignment with the 1.5°C goal of the Paris Agreement and the EU climate neutrality goal. All Member States will need to step-up their efforts and national targets will need to be increased.
- All EU Member States should be obliged to meet their binding national targets and **compliance should be enforced** through prompt infringement procedures and/or fines.
- Maintaining li**near reduction and the annual emission budget** approach that incentivizes early reductions and makes yearly compliance checks possible.
- National energy and climate plans (NECP) must be improved and updated – in line with the EU Governance Regulation.
- When defining increased targets, the equity principles of the UN Framework Convention on Climate Change - based on historical responsibility and capability to act - should be taken into account.
- All countries should be encouraged to set **higher targets than the minimum** requirements set at EU level. However, such emission reductions beyond the target must no longer be used to offset other Member States' failure to achieve their targets.

3. Transport, building and agriculture sectors must remain part of the ESR

Another review option the European Council is considering is a possible extension of the EU ETS to the transport and buildings sector, either while retaining these sectors in the ESR or by removing them completely. **Carbon pricing[4] is essential to implement the Polluter Pays Principle, but should not be the only reduction instrument. It must be embedded in a broader policy framework to address social impacts and enable citizen support for effective climate policy.** Carbon pricing is necessary to reduce emissions but also to reduce

[3] https://www.eea.europa.eu/themes/climate/trends-and-projections-in-europe/national-action-across-all-sectors

[4] Carbon pricing can mainly be implemented in two ways: as a cap and trade system (like ETS) which creates a market of emission allowances, or carbon taxation. On the carbon market (with a real cap on emissions) prices are less predictable. Both systems need to be embedded in a robust policy framework to balance the impact on households and fairly redistribute revenues.

social injustice and inequalities, and - with fair revenue distribution - could provide the financial resources for compensating and supporting the transition of those in need.

The road transport and buildings sectors have significantly higher levels of abatement costs and show overall lower price elasticities. Including them in a single EU ETS would risk shifting pressure away from these new sectors.[5] Including these sectors into the ETS could also distract attention away from direct CO_2 taxation and other EU regulatory instruments (e.g. energy labelling, standards) with much more decarbonisation potential.

A dedicated and strong policy framework, consisting of binding targets and measures such as those included in the Energy Efficiency Directive and the Energy Performance of Buildings Directive, will also be needed[6]. Other supporting measures like car CO_2 standards have also proven to be effective to drive change. Therefore, in addition to the ESR, these policies need to be strengthened and improved[7] and implemented at national level. Research confirms that the ESR is an important driver for national action to deliver energy savings (especially in the building sector) and thus to ensure cost-effective and equitable GHG reductions.[8] Binding national targets provide incentives for governments to deploy the full arsenal of decarbonisation tools: rules and regulations, carbon pricing, support for households or launch of green infrastructure projects, etc.

CAN Europe calls for

- **Road transport, buildings and agriculture emissions to be further regulated under the ESR.** National governments should remain responsible for their own emissions in these sectors.
- Carbon pricing should be used as a **supportive** measure, as part of a broader policy infrastructure. A strong sectoral regulatory framework for transport, buildings and agriculture sectors is necessary to ensure environmental and social integrity and compliance. Carbon price should be designed in a socially-fair manner with appropriate compensation for those in need.

4. Adjust allocated emissions allowances to reality

Under the Effort Sharing Regulation, each Member State receives a distinct emissions budget each year which declines at a linear rate towards its individual nationally binding ESR target for 2030. These budgets are called Annual Emissions Allocations (AEAs). The Regulation allows Member States to use a number of flexibilities to cover up any gap to

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[5] https://www.transportenvironment.org/sites/te/files/publications/2020_06_Decarbonising_European_transport_and_heating_fuels_report.pdf

[6] https://static.agora-energiewende.de/fileadmin/Projekte/2021/2021_03_Silver_Buckshot/A-EW_206_Fit-for-55-Package_WEB.pdf

[7] https://www.umweltbundesamt.de/sites/default/files/medien/376/publikationen/w_p_04_paper_raising_the_eu_2030_ghg_emission_reduction_target_with_german-language_summary_rev.pdf

[8] https://www.stefanscheuer.eu/wp-content/uploads/2021/01/20210201-Synergies-between-ESR-EED.pdf

their national binding targets. First, Member States are allowed to borrow AEAs from the following year to bridge shortcomings in the running year, up to 10% in the period until 2025, and 5% in the second half of the decade. Second, the ESR allows Member States to bank up to 30% of excess allocations up to that year for use in later years. Third, Member States can transfer allowances to other Member States (5% of its annual emission allocation for a given year in the period until 2025, and 10% in the second half of the decade).

Member states are expected to collectively overachieve the 2020 target set for the non-ETS sectors in the Effort Sharing Decision, which is to reduce emissions by 20%. **In addition, current AEAs, still aligned with the old 40% overall EU climate target, do not reflect the impacts of the pandemic-induced economic downturn, possibly further inflating the surplus in 2021 and 2022.** The Commission should take real emission levels in 2020 into account in order to ensure that the overall emission reductions in the ESR are not artificially inflated, but adjusted to the latest available real emission data in 2020.

CAN Europe calls for:

- Rejecting carry over of surplus allowances to post 2020;
- **Emissions Allocations (AEAs) to reflect the latest available emissions levels** (2020 as a starting point). Should these be lower than the Member State's 2020 target under the Effort Sharing Decision, the remaining gap shall be deleted;
- Only Member States that fulfil their annual obligations should have access to flexibilities the following year.
- In order not to delay mitigation action and decrease the risk of compliance problems at the end of the ESR period, **flexibilities should be minimised** along the following:
    - Limit borrowing to 2% from its annual emission allocation for the following year
    - Limit banking to 5% of a Member State's budget for that year
    - Limit transfer capacity to 5% its annual emission allocation for a given year until 2030

5. Closing loopholes - no usage LULUCF, ETS credits

Currently, under the Effort Sharing Regulation, Member States can use legislative loopholes that allow them to cover gaps in actual emission reductions for achieving their 2030 ESR targets. The Regulation provides for the use of ETS allowances (100 million), LULUCF credits (280 million over the ten years) and a safety reserve for lower income Member States (105 million) to be used by Member States to cover up failed efforts to reach their annual emission allowance limits.

The removals in the LULUCF sector must not be used to offset lack of action in other sectors. **Emissions from agriculture must be tackled locally and remain national responsibility.** The required structural and behavioural changes should be governed and incentivised at national level, under the scope of the ESR, while relevant EU policy, such as relevant EU funds and the Common Agricultural Policy (CAP) should be made fully consistent with the EU's international climate commitments.

Including carbon sinks into the EU's climate target creates a dangerous precedent and effectively creates trade-offs between sink enhancement efforts and mitigation action, while both are urgently required and need to be maximised separately. Carbon removals must not serve as offsets for emission reductions.

ETS allowances should also not be used to offset carbon emissions in ESR sectors either. **ETS reductions must come on top of national efforts in order to bring the maximum reductions to deliver on the climate goal.**

CAN Europe calls for:

- **Deleting the possibility for countries to use offsets from the land use sector to reduce efforts** in the non-ETS sectors. Emissions and removals in the land use sector and emissions from fossil fuels must not be fungible.
- **Deleting the possibility for countries to use surplus allowances from the ETS to reduce efforts in the non-ETS sectors.**
- **Limiting the bonus** granted to low-income Member States to 20 million in total.