

Eighth CEPR/EAERE Webinar on Climate Policy: *Fit for 55: Why do we need a coherent carbon pricing mechanism in Europe?*

Monday 13 June 2022 - 17:30 - 19:00 CET (Frankfurt/Paris/Amsterdam)

The European Union has agreed to pursue a very ambitious climate target aimed at reducing its global emissions by 55% between 1990 and 2030. The “Fit-For-55” package proposed by the EU Commission in July 2021 is designed to translate this ambition into actual climate actions. Among these policies, there is the key issue of extending carbon pricing to the transportation and heating sectors (ETS2). On June 8, 2022 - after the ETS2 had been amended by the Environment Committee of the Parliament - the European Parliament rejected this reform, among others of the package.

For the Eighth CEPR/EAERE Webinar on Climate Policy, [Jos Marie R. Delbeke](#) (EUI School of Transnational Governance and KU Leuven), [Andrea Tilche](#) (NTNU and MIMS) and [Adrien Fabre](#) (ETH Zürich) met for a roundtable discussion to exchange on the decision of the Parliament, the reasons for and against this extension, together with possible alternative policies to attain the EU target. The roundtable and Q&A session with the audience was moderated by [Carlo Carraro](#) (Università Ca' Foscari di Venezia and CEPR).

Panellists:



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Context

Currently, emissions from large industrial installations (power plants, steel mills and cement factories, etc.) are subject to the Emission Trading Systems (ETS). A cap on the number of emission permits put into circulation ensures that the planned emission target is respected, while the emissions of industries are verified. At the core of the "Fit for 55" package, is the creation of the second market of emissions permits in the EU, the ETS2, starting in 2026 and which would encompass all emissions from the heating and transport sectors, which constitute 41% of the EU emissions.

On 17 May 2022, the Environment Committee of the European Parliament amended this reform of the carbon trading system. According to these changes, the ETS2 would only apply to commercial usage and could be extended to private ones, following a positive assessment of the EU Commission and new legislative procedure in the future. On the other hand, the price of the emissions permits would be capped at 50€/tCO₂ until at least 2030, with a deadline for surrendering postponed if fuel prices are higher than in March 2022.

On 8 June 2022, the European Parliament voted to reject this reform of the EU carbon trading system - as well as a carbon border tax (the Carbon border adjustment mechanism (CBAM)) and the creation of a Social Climate Fund (SCF). Green and Socialist Members of the European Parliament (MEPs) judged the plan watered down in Committee and insufficiently ambitious.

Key Points of the Webinar

- **The importance of the ETS2 to reach the EU carbon target**

The ETS has shown to be a very effective measure in terms of emission decrease in the concerned sectors over the last 15 years, while also being a predictable tool. By including all emissions from heating and transport sectors, the ETS2 as initially proposed by the Commission will allow to also cap those at a level which is coherent with the carbon target of the EU. Under competitive pressure, the concerned companies will then pass the additional cost to consumers, thereby encouraging them to reduce their fossil fuel consumption.

Furthermore, the ETS2 also included that auctioning revenues from the ETS2 will be used to support vulnerable households: 75% will go to the States where emissions occur and 25% into a Social Climate Fund (SCF), which will be allocated to the States, following a formula ensuring an equal right to emit for

capita in the European Union. States shall also take complementary measures aiming at helping people and companies to reduce their emissions, which will lower the carbon price. The ETS2 thus acts as a guarantee to meet emissions reduction if those measures are not enough or not put in place and appears as a guarantee to achieve emission reductions in an efficient, fair, and binding way.

In that regard, the amendments adopted by the Environment Committee greatly undermine the goal of the ETS2: by excluding household emissions which constitute the bulk of the transport and building sector's emissions and by adopting a price cap of 50€/tCO₂, judged insufficient to encourage a reduction.

- **The pivot role of the Social Climate Fund (SCF)**

One of today's current risks is that people perceive climate reforms as a policy for the middle class. Without support, a large part of the population might fall into a fuel poverty trap and not be able to pay for and adopt the currently expensive low-carbon alternatives for transport and heating. The SCF can thus act as pivoting energy to address the distributive issues generated by increases in carbon prices and support a large part of the population facing difficulties in the current context.

Frontloading the SCF can also constitute a key element to respond to the political risk that populism movements use the unpopularity of fuel price increases to generate instability. If the recycling of the auction revenues can provide a well-defined inequality adjustment, it may allow a change in the public narrative regarding the translation of the climate policy.

- **A missed opportunity that does not put into question the essence of the EU climate policy**

By leaving the extension of the ETS2 to uncertain future legislative procedures, the EU Parliament decision is a missed opportunity that might waste precious time. However, despite the Parliament failing to find an agreement, the overall target of the climate law has not been put into question and the discussions mainly concerned the modalities and timeline of its application. In the current situation of the Russian invasion in Ukraine, natural gas as a fuel-switching possibility has been severely weakened, while other solutions (hydrogens, heat pump, etc.) are still very costly. If in the long term, the extension of the carbon trading system to the transport and heating shall not be questioned, this crisis context might encourage the EU to refrain to do more now and rather spread and schedule the reduction of emissions over the period.

- **The ETS and the rest of the world**

The Ukrainian conflict strongly highlighted the need for comprehensive European geostrategy related to energy and transition. If the question of strategic autonomy and the reinforcement of energy independence is crucial, the Union cannot be isolated and need to develop new links and strong relationships with the rest of the world, without reproducing the errors of the past and relying on undemocratic countries.

Furthermore, a possible risk is that the reduction of emissions in Europe may be irrelevant and jeopardized if other countries, both developed and developing, do not adopt similar measures on carbon pricing. Low-income countries shall be on the table and included in the decarbonization debate (e.g., an international treaty, in which all the countries could be offered to join ETS and receive free permits in proportion to their population to ensure redistribution).

Finally, the ambitious goal of carbon neutrality in 2050 can be used as an example to showcase to the rest of the world the possibility to build a carbon-neutral economy, while the EU can gain a strong advantage in the economy of the 21st century from this front-runner position.