



GREATER ENERGY EFFICIENCY AND STRONGER EMISSIONS TRADING SYSTEM: BOTH NEEDED FOR HIGHER CLIMATE AMBITION

April 2017

Climate Action Network (CAN) Europe is Europe's largest coalition working on climate and energy issues. With over 130 member organisations in more than 30 European countries - representing over 44 million citizens - CAN Europe works to prevent dangerous climate change and promote sustainable climate and energy policy in Europe.

EXECUTIVE SUMMARY

As the European Parliament and the Council of the European Union enter the phase of intense negotiations on the Clean Energy for All Europeans package, it is important to underscore that a higher energy efficiency target will help the EU in reducing its greenhouse gas emissions and thus also in implementing its commitments under the Paris Agreement. Therefore, increasing the energy efficiency target should be welcomed as an opportunity to revise the EU's inadequate climate target and further strengthen the relevant tools, such as the Emissions Trading System (ETS).

In this briefing, CAN Europe first addresses the need to increase the level of ambition of all EU climate and energy targets in line with the long-term objectives of the Paris Agreement. This starts from the recognition that strong climate and energy targets and policies are mutually reinforcing, not conflicting with each other. Secondly, the paper highlights that it is important to acknowledge that the ETS's own shortcomings, including the existence of a large and growing surplus of unused allowances, will continue to undermine its effectiveness and the price of carbon, unless policy makers show the necessary willingness to tackle them. Last but not least, it reiterates that the Market Stability Reserve (MSR), although not enough to fix the ETS, can help to recalibrate the effect of additional policies, including energy efficiency.

Taking into account that energy efficiency provides multiple benefits for the society and that the ETS is no silver bullet to deliver the vast potential of energy savings in Europe, it is time to focus on the real task ahead, which is scaling up action to reduce greenhouse gas emissions in line with the Paris Agreement.

INTRODUCTION

On 30 November 2016, the European Commission published its Clean Energy for All Europeans package, including a proposal to increase the EU's 2030 energy efficiency target from 27 percent to 30 percent. As the European Parliament and the Council of the European Union enter the phase of intense negotiations regarding the package, it is important to reiterate that a higher energy efficiency target and a strong EU Emissions

Trading System (ETS) are essential to raise overall climate ambition and accelerate action in line with the Paris Agreement. This briefing elaborates CAN Europe's views on this issue.

ALL CLIMATE AND ENERGY TARGETS NEED TO BE RAISED IN LINE WITH THE OBJECTIVES OF THE PARIS AGREEMENT

EU Heads of State and Government, in October 2014, agreed on the following targets for 2030:

- at least 40% greenhouse gas emission reductions in the EU, as compared to 1990 emissions;
- at least 27% of renewable energy consumed in the EU;
- at least 27% target for improving energy efficiency in 2030 compared to projections of future energy consumption, having in mind a 30% target

These targets are insufficient and not compatible with the objectives of the Paris Agreement to keep temperature rise well below 2°C and pursuing efforts to limit it to 1.5°C. These long-term objectives require additional effort from all countries, including the EU. In its most recent Emissions Gap Report, the United Nations Environment Programme calls upon the major emitting countries to reduce their 2030 emissions by another 25% on top of the existing commitments, in order to keep temperature rise below 2°C. **The end goal of the Paris Agreement is the full decarbonisation of our society.** This task is not trivial and will require multiple policies and instruments to deliver the needed change in all sectors responsible for carbon pollution. **The significant potentials of energy efficiency and renewable energy should serve as the basis for the EU to review and increase its emission reduction targets, both for the ETS and for emissions not covered by the ETS.**

THE ETS NEEDS TO BE FIXED FROM WITHIN

The ETS aims to help the EU achieve its emission reductions more cost-effectively. **Despite being hailed as the flagship of European climate policy, the ETS has failed to be a real driver in the transformation of the economy away from fossil fuel pollution, due to a lack of political willingness to adequately reform the system.** A weak emission reduction target, the massive use of international offsets and the economic crisis are some of the main reasons that have led to an enormous oversupply of pollution permits. As a result, the price for emission permits is so low that it cannot incentivise the shift to clean energy investments and the decarbonisation of the economy.

The EU is currently finalising the reform of the ETS for the 2021-2030 period. **Regrettably, neither the initial weak proposal by the European Commission nor the proposed amendments by the European Parliament and the Council currently on the table are anywhere near what is needed to make the ETS a functioning tool.** It is therefore highly unlikely that the final negotiations will conclude with a deal that will substantially correct the crippled carbon price in the short- and medium-term, meaning until well after 2030.

The ETS's own shortcomings will continue to undermine its effectiveness. It is estimated that up to 4.4 billion surplus allowances will accumulate by 2020, which under current rules can be fully carried over to the next trading period. **The unwillingness of the decision-makers to align the starting point for the 2021 to 2030 period with actual emission levels creates an additional surplus of almost 2 billion tons¹.** This immense amount of surplus has a devastating impact on the price of carbon.

These structural deficiencies will need to be tackled in order to fix the ETS. Any efforts to misuse the failing ETS as an argument to limit the energy targets simply neglect the real challenges the ETS is facing and hamper greater climate ambition. This will lead to missed opportunities for decarbonising our economy, as policy developments such as increasing the 2030 energy efficiency target will have a positive impact on reducing greenhouse gas emissions.

¹ Further information on the essential ETS reforms for post-2020 can be found in the relevant CAN Europe position paper <http://www.caneurope.org/docman/emissions-trading-scheme/3029-can-europe-ets-reform-position-21-12-2016/file>

THE MARKET STABILITY RESERVE WILL HELP CALIBRATE THE IMPACT OF ADDITIONAL POLICIES

The Market Stability Reserve (MSR), which will start operating in 2019, **although not enough to fix the ETS, is supposed to partly address the large surplus of emission allowances by automatically taking part of this surplus out of the market.** While different aspects of the MSR are still subject to negotiations (including whether some of the allowances in the MSR would be permanently cancelled or could come all back to the market at a later date), the European Commission confirmed² **the MSR will respond to changes in the demand of allowances, regardless of whether these result from economic factors or from policy developments.** In other words, if further emission reductions are achieved by additional policies, including **for example in relation to improved energy efficiency,** the resulting emissions permits will be stored in the MSR without affecting the number of permits available on the market.

ENERGY EFFICIENCY POLICIES ARE MAINLY TARGETING SECTORS OUTSIDE THE ETS

Energy efficiency measures mainly target sectors such as buildings or transport that are currently covered by the Effort Sharing Decision (ESD) and after 2020 by the Effort Sharing Regulation (ESR). This leads to reduced greenhouse gas emissions mostly in these sectors and consequently facilitates the achievement of the targets set under the ESD/ESR. In this context, the impact on activities in the ETS sectors of increasing the energy efficiency target will be limited.

THE ETS IS NO SILVER BULLET FOR DELIVERING ENERGY SAVINGS

The carbon market cannot address non-market barriers to deploy energy savings at scale. These include lack of upfront finance, lack of awareness and information on why and how to save energy and split incentives between owners and tenants. A study commissioned by the European Commission on the energy efficiency and energy savings potential in industry³ highlights that some of these barriers also exist in industries covered by the ETS. According to the study, these barriers can prevent energy efficiency solutions from being implemented, even if they are economically viable⁴. **A carbon price signal alone is not sufficient to provide incentives to grasp the energy efficiency potential** in the short or medium term, therefore a dedicated energy efficiency policy framework is needed.

ENERGY EFFICIENCY HAS MULTIPLE BENEFITS

Reducing energy waste through appropriate energy efficiency measures is the most direct way to reduce greenhouse gas emissions. Moreover, **energy efficiency offers multiple benefits that go beyond greenhouse gas emission reductions,** such as lower dependency on energy imports, job creation and improved health. The Impact Assessment accompanying the Commission's proposal⁵ shows that higher levels of ambition deliver significantly greater benefits (see Table 1 for increased benefits with different levels of ambition).

² Non paper on the interaction of energy efficiency with ETS and Effort Sharing
<http://www.politico.eu/wp-content/uploads/2017/03/03-07-WK-2519-2017-INIT-copy.pdf>

³ ICF, 2015, Study for DG Energy on energy efficiency and energy saving potential in industry and on possible policy mechanisms

⁴ In the study, energy efficiency measures are screened for economic viability based on a simple payback approach for two scenarios. For the first scenario, a 2-year simple payback has been selected, which, according to the study, represents a closer perspective of what industry might consider to be economically feasible. For the second scenario, the study assumes a 5-year simple payback.

⁵ Impact Assessment accompanying the Proposal for a Directive of the European Parliament and of the Council amending Directive 2012/27/EU, Brussels 30.11.2016, SWD (2016) 405

Table 1. Increase of benefits with higher levels of energy savings⁶

	30%	33%	35%	40%
Reduction in gas imports	12%	23%	29%	41%
GDP increase in 2030	0.39%	1.45%	2.08%	4.08%
Additional jobs	396.950	1.587.800	2.428.400	4.856.800
Savings in fossil fuel import bills (bn) for 2021-2030	69.6	147.3	199.3	287.5
Reduction in pollution control and health damage costs (bn/year)	4.5-8.3	15.2-28.4	19.9-36.6	30.4-55.9
Total GHG emissions reductions (% to 1990)	41%	43%	44%	47%

It is clear that the European Commission's proposal for an EU binding 30% energy efficiency target for 2030 does not maximise the benefits for citizens and society. **A binding energy savings target of at least 40% is needed to substantially improve EU energy security, create jobs and reduce pollution.** A higher energy efficiency target also facilitates the transition towards a 100% renewable energy system.

CONCLUSIONS

The Paris Agreement requires a complete overhaul of all climate and energy policies. This means increasing all climate and energy targets and restoring the ETS by addressing the massive surplus that really weakens its effectiveness. Strong climate and energy targets are mutually reinforcing, while bold instruments will help the EU achieve these targets. It is time to focus on the real task ahead, which is scaling up climate action.



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⁶ Change compared to the benefits delivered under a level of ambition of 27% energy savings (GDP and additional jobs numbers are from the non crowding out scenario). Data are taken from Commission's Impact Assessment accompanying the proposal to review the Energy Efficiency Directive.