What does the 2030 climate and energy framework mean for Ireland?

November 2014

On 24 October EU leaders set out the policy vision to 2030, and committed to reduce greenhouse gas emissions by at least 40% compared to 1990 levels, and increase energy efficiency and renewables by at least 27%.

In the final weeks leading up to the EU summit, three distinct camps emerged with very different agendas and the hope of achieving consensus on the headline targets seemed elusive. A lot was dependent upon achieving consensus at this Council meeting: the timetable of securing an EU wide agreement was designed to coincide with the international climate framework as the EU (along with other global leaders) had committed to pledge their emissions reduction target by early 2015 as part of the negotiations which conclude in Paris in December 2015.

The 2030 climate and energy policy framework could in essence be called "half a deal" as we don't yet know what the individual member state targets will be in the non-ETS sector (agriculture, buildings, transport and waste) and uncertainty remains over what substantive parts of the agreement means in real terms.

This note is not an in-depth analysis of each part of the agreement, but more so a discussion note addressing some of the headline elements of the agreement. It starts with the original Commission proposal of January and moves to the targets in the text of the Council conclusions. It also looks at the priorities of the Irish government in the run up to the EU summit on 23/24 of October, and lists some of the areas of significance to Ireland.

Background

On 22 January, the European Commission published a package that included legislative and non-legislative proposals to determine climate and energy policy out to 2030.

The central plinth of the proposed Communication on a Policy Framework for climate and energy in the period from 2020 to 2030 is a greenhouse gas (GHG) emissions reduction target of 40%below 1990 levels, to be achieved through domestic measures alone and without international offsets.[1] This non-legislative instrument was an explicit statement of the EU's ambition to assist in meeting the aspirational objectives of reducing GHG emissions of 80% to 95% by 2050. The target will be split between the ETS and a collective effort among Member State in the sectors outside of the ETS.

- For the power sector and heavy industry (ETS[2]) a reduction of 43% in 2030 (compared to 2005) – this would result in an increase in the annual factor from 1.74% to 2.2% after 2020;
- For agriculture, buildings, transport and waste (non-ETS sectors) a reduction of 30% (compared to 2005).

The timing of the proposal was important, to meet the EU commitment to pledge a GHG emissions reduction of 40% by early 2015 as part of the negotiations which conclude in Paris in December 2015. The proposal said the target will be subject to continuous appraisal to take account of the international dimension. In the event of a more ambitious commitment stemming from the UN Climate Conference, the additional effort could be balanced by allowing access to international credits. In terms of protecting the competitiveness of Europe's energy-intensive industries, it suggested an improved system of free allocation will be needed after 2020 for those sectors at most risk of carbon leakage as long as no comparable efforts are undertaken in other major economies.

The proposal concluded by inviting the European Council and the European Parliament (EP) to approve an EU level target of at least 27% as the share of renewable energy to be consumed in the

[1] European Commission, *A policy framework for climate and energy in the period from 2020 to 2030*, COM(2014) 15 final.
[2] Under the EU's Emission Trading Scheme, a cap is set on the total amount of greenhouse gases that can be emitted by all participating installations. 'Allowances' for emissions are then auctioned off or allocated for free, and can subsequently be traded.

by 2030, based on the reasoning that a target of 40% GHG emissions reduction should by itself encourage a greater share of renewable energy in the EU of at least 27%. A new governance process was suggested to enable EU level delivery mechanisms and indicators, and to manage and coordinate the EU delivery of renewable and energy efficiency targets. An impact assessment accompanied the proposal, outlining and modelling a number of scenarios combining targets and ambition levels with a view to presenting the most cost-effective route to meet the EU's long term climate objectives out to 2050.[3] In June, the European Commission proposed an energy savings target of 30% following a review of the Energy Efficiency Directive.

The package also consisted of a legislative proposal to modify the Emissions Trading Scheme and establish a market stability reserve at the start of the next trading period in 2021.[4] As the proposal currently stands, it would permanently remove up to 150 million surplus allowances each year from 2021 onwards, or possibly even from 2018 onwards if the wishes of some of the larger member states were granted. This would quickly shift the supply/demand balance, resulting in sharply increased EUA prices – feasibly 400% higher than at present. The text of proposal states that the increased linear reduction factor (1.74% to 2.2% after 2020) of the 2030 policy framework is insufficient to address the negative implications of the stark market imbalance. It is subject to the ordinary legislative procedure and requires the co-decision of the European Council and the European Parliament.

In the European Parliament, ENVI (Environment, Public Health and Safety) is the lead committee on MSR, and ITRE (Industry, Research and Energy) will provide an opinion. The ITRE rapporteur will participate in the ENVI meetings and trilogue negotiations with shadow rapporteurs. Environment ministers are set to discuss the progress of the proposal during the December Council meeting. MEPs in the ENVI Committee will vote on 23-24 Feb 2015.

The European Council conclusions: what was agreed?

In terms of targets, a binding commitment at EU level of at least 40% domestic GHG reduction by 2030 compared to 1990. The overall target is to be split into 43% reductions in the ETS including the power sector and heavy industry and 30% in the non-ETS sector (agriculture, buildings, transport, and waste) by 2030 compared to 2005. The European Council also agreed to an EU wide, binding target of at least 27% renewable energy by 2030 and an indicative, EU level target at the of at least 27% energy efficiency by 2030.

The central piece of the framework is the overall binding target to reduce EU domestic GHG emissions by **at least** 40% below the 1990 level by 2030. A special "flexibility clause" was added to the final text, making it possible for the European Council to return to the targets after the UN Climate Conference in December 2015.[5] The international context will be discussed in greater detail below, but commentators noted that agreement would not have been reached without the inclusion of the term "at least" and well as the promise to keep all "*elements of the framework under review*" under the auspices of the European Council.

The Emissions Trading Scheme and fate of energy intensive industries

While there is an overall commitment to reduce by 40%, the effort is split between the ETS and the non-ETS. Therefore the ETS, which includes the power sector and energy intensive industries, has a target of 43% compared to 2005. It is important to note that it is not only the target that will materially impact the energy-intensive manufacturing sites covered by the ETS, measures to prevent carbon

[3] European Commission, *Impact Assessment accompanying* a *policy framework for climate and energy in the period from 2020 to 2030*, SWD (2014) 16 final.
[4] European Commission, *Proposal for a Decision of the European Parliament and the Council concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and amending Directive 2003/87/EC*, COM/2014/020 final.
[5] As noted in the opening paragraph of the Council conclusions (1), the "European Council will keep all elements of the framework under review and will continue to give strategic orientations as appropriate, notably with respect to consensus on ETS, non-ETS, interconnections and energy efficiency".

leakage as well as the Commissions proposal to create a MSR.[6] The current EU legislation already includes a legally-binding target for 2020, with further reductions at a fixed annual rate indefinitely thereafter. So even in the absence of any new deal, the ETS sector would have been obliged to achieve an emissions reduction of about 38% by 2030. As a result of the European Council conclusions, that reduction target effectively increases from 38% to 43%. On its own, a slightly tighter ETS target would probably not have a material impact on the market price of EU Allowances. However, the Council meeting crucially also endorsed the European Commission's proposal to create the MSR, and the need for "*a well functioning, reformed Emissions Trading Scheme (ETS) with an instrument to stabilise the market in line with the European Commission proposal".*

In an effort to assuage the fears energy intensive operators, free allocation will not expire and the option of compensating energy intensive industries for direct and indirect costs (i.e. electricity costs) is available, on the proviso that they do not contravene state aid rules. Measures to prevent carbon leakage will continue to so as long as competitors located outside the EU operate without the costs associated with meeting climate policy objectives. However, this could also mean that Europe's existing measures to combat carbon leakage may actually be weakened rather than strengthened. BUSINESSEUROPE believes this part of the agreement lacks specificity, and recent discussions at working group level pointed to the cloudy language used in paragraph 2.4, for example "…***undue*** *carbon costs leading to carbon leakage*" – who is to decide what is "undue" and how will this be measured?

The non-ETS sectors: half a deal?

In the weeks in the leading up to the European Council, the basis for deciding the legally binding reductions in the non-ETS sectors (agriculture, buildings, transport, and waste) proved to be the most contentious element of the agreement. It could be said that "half a deal" was reached: while the European Council outlined the main principles to achieve a 30% reduction compared to 2005, these still need to be translated into Member State targets.

We don't yet know what the individual Member State targets will be, which is a source of considerable concern given the raw deal that Ireland got handed for 2020. This comprised of a -20% target for 2020 that was manifestly unfair and disproportionate, and will prove very costly for the Irish economy in the coming years. While the methodology as introduced by the *Effort Sharing Decision* will continue as the criteria to measure individual Member States targets, there is an important distinction introduced to counter the concerns of those countries with above average GDP, such as Ireland, Finland, Netherlands etc.

Targets for those Member States with a GDP per capita above the EU average "*will be relatively adjusted to reflect cost-effectiveness in a fair and balanced manner".* Ireland stated that it could only accept the overall targets on the understanding that when it comes to setting national targets, Ireland's specific economic situation would be taken into account. Therefore, when the "cost-effectiveness" is considered alongside Ireland's financial circumstances, a simple GDP per capita criterion is unlikely.

The text also reaffirms the "*use of existing flexibility instruments within the non-ETS sectors will be significantly enhanced*". In his press statement welcoming the 2030 conclusions, President of the European Council Herman Van Rompoy brought the merits of statistical transfer to life, "a country for instance Denmark-which already has double-glazing everywhere – can decide, instead of going for triple-glazing, rather to help finance a double-glazing project elsewhere in Europe. That way, it can get more emissions-saving value for its money".[7] In terms of what this could mean for Ireland, a fully functioning market (not just intergovernmental transfer of non-ETS credits) could provide a more cost-effective way to realise our yet to be decided nationally binding non-ETS targets for 2030. Furthermore, the option of including the transport sector within the framework is referenced in the document. There has been a mixed reaction to this proposal, with some welcoming the flexibility and others critical of the potential effect of increasing the cost of allowances.

[6] Carbon leakage is the term used to describe the situation that may occur if, for reasons of costs related to climate policies, businesses were to transfer production to other countries which have laxer constraints on greenhouse gas emissions.
[7] European Council, *Remarks by President Herman Van Rompuy following the first session of the European Council*, Brussels 23 October, EUCU230/14.

The European Commission is invited to propose a methodology to offset agricultural emissions through afforestation. This is a significant development for Ireland and a key priority for Ireland's negotiators. While the envisaged policy proposal should bring important concessions for Ireland's unique emissions profile, the benefits are somewhat dependent upon the timely incentivisation to plant trees in the run up to 2030.

The paragraphs on the non-ETS sectors (2.10-2.14) leave a trail of unanswered questions and the inability to reach a consensus agreement on this substantive part of the text will bring parts of it back into the fold of the European Council, where it will be subject to consensus.

Renewable and energy efficiency targets

An EU wide target of 27% share of renewable energy consumed The EU level target is not legally binding at the national level or EU level and will be reviewed in 2020 "having in mind" a 30% EU-level target, according to the Council conclusions.

In terms of how this will all be managed, the European Council conclusions built on the original 2030 proposal from January, and notes the agreement to develop a "*transparent **governance system** without any unnecessary administrative burden…to help ensure that the EU meets its energy policy goals, with the necessary flexibility for Member States and fully respecting their freedom to determine their energy mix*".

What does it mean for Ireland?

Ireland's two main negotiating objectives at the European Council meeting on 23-24 October were the inclusion of agriculture, including afforestation, into the framework after 2020 and burden sharing. Feelings expressed by government officials after the Council and in response to Ibec's press statement on the Council outcome were that:

- Ireland scored a success on agriculture and lives to fight another day on burden sharing;
- Progress made but there is along way to go in firming up many of the details, both at future European Council meetings and in the ordinary legislative process.

It is understood that Ireland suggested that the concept of deciding any further steps in terms of ETS, non-ETS, energy efficiency etc. (as noted in the introductory text of Council conclusions) be taken by consensus at European Council level. This may mean that the final breakdown by Member State of targets in the non-ETS sector will be decided by consensus in the European Council rather than qualified majority voting in the ordinary legislative process. It is understood that Ireland also tabled a statement to be included in the formal minutes of the European Council saying Ireland only accepted the overall targets on the understanding that when it comes to setting national targets, Ireland's specific economic situation would be taken into account. However this is going to be a long and fluid process that needs to be monitored closely.

The coming months will be telling terms of what the principle of "cost-effectiveness" and "flexibility" could mean for a country like Ireland, with higher than average GDP per capita and a unique emissions profile. Furthermore, the governance system could provide a further important concession for Ireland if Member States are free to pursue the maximum flexibility possible meet the binding GHG target.

In summary, the final text contains a number of clauses that provide hope of securing a fairer, cost-efficient outcome for Ireland, including:

- Continued involvement of the EU Council implying unanimity is required on final non-ETS targets.
- Targets for higher GDP states to be relatively adjusted to reflect cost-effectiveness.

- Availability of existing flexibility to be significantly enhanced.[8]
- An acknowledgement of the lower mitigation potential of agriculture.
- The European Commission is requested to examine sustainable intensification of food production, while optimising its potential.
- The European Commission is requested to propose an approach for the promotion of emissions reduction, electricity and renewable fuels in transport.

Next steps:

International	The major economies are due to pledge their emission reduction commitments in the first quarter of 2015 and the UN summit is scheduled for take place in Paris, December 2015. Three preparatory meetings are scheduled in the run up to Paris. BUSINESSEUROPE has called for the rapid conclusion of a comprehensive legally-binding international climate change agreement committing all major economies to the measurement, monitoring, reporting, control and reduction of greenhouse gas emissions. It is important to recall that the -40% target represent a minimum level of political commitment. The possibility exists of even more being committed in the event of a global deal finally being concluded at next year's UN Climate Conference in Paris.
European Union	Progress in terms of the 2030 climate and energy policy framework will fall under the auspices of a recently elected European Parliament and a brand new European Commission. It is difficult to predict whether there will be a directional shift in the policy focus. While the European Council may have agreed upon a policy framework, a legislative framework is necessary to underpin and implement the policies it proposes.

[8] Section 2.12 references "new flexibility" for non-ETS to be achieved through "a limited one-off reduction of ETS allowances".