

# AGFW-Contribution

Climate change – updating the EU emissions trading system (ETS)

Public consultation

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AGFW, the German association on district heating and cooling and CHP (Combined Heat and Power), welcomes the possibility to voice its opinion on the amendment of the European Emission Trading System Directive. AGFW is convinced that the extension of the European ETS poses a unique opportunity to develop a working carbon price signal, which would sufficiently incentivize an efficient market based energy transition across carbon emitting sectors. It has to be taken into account that the necessary carbon price signals heavily vary between energy, buildings and transport. The price signal therefore needs to give the right incentives and a carbon level playing field needs to be developed.

In light of these considerations, AGFW would like to emphasize several aspects that should underscore our decarbonisation efforts within this reform process:

- **Focusing on maintaining cost efficiency in the current ETS framework**
- **Applying a “one system per sector”-approach to establish a carbon level playing field that allows for sectoral accommodations**
- **Addressing the existing imbalances of carbon pricing between ETS and non-ETS sectors**

With respect to adapting the ETS to the common climate ambitions, AGFW favours a cost efficient increase of the current ETS contribution consistent with the new targets. However, AGFW also emphasizes that an increase of the ETS contribution must be accompanied with the establishment of a carbon level playing field between the emitting sectors currently outside the ETS. In the absence of such equal footing, ETS-covered sectors will still require free certificate allocations to offset the inconsistencies in carbon pricing. Regarding the adjustment of ETS pricing instruments, an increase of the linear reduction factor in conjunction with an early application of the strengthened cap should be favoured over one of reductions or additional changes to the MSR mechanism to ensure market stability.

Regarding the possible extension of the European ETS to further sectors, AGFW strongly supports the idea to establish a separate trading system for buildings to create a carbon level playing field within the sector in the medium term. Regarding the buildings sector, CO<sub>2</sub> Pricing by higher carbon taxation in the energy taxation would also be a feasible option, since an immediate inclusion of new sectors into the existing ETS framework would require a complete rebalancing of an otherwise functioning system and carbon avoidance costs also greatly differ

across sectors. On the question of carbon trading AGFW favours the creation of individual and separate trading systems outside the current ETS framework. Following the approach of “one system per sector” separate and standalone trading systems could be established to allow for individualized sectoral accommodations. Especially with respect to buildings an efficient carbon price signal would directly yield considerable steering effects within the European heating and cooling sector and unlock the industry’s substantial decarbonisation potential.

In order to secure the necessary price signal in a carbon pricing system and to maintain technological neutrality, any future trading system furthermore needs to be separated in such a way that CHP plants larger than 20 MW already covered through the current ETS receive no double CO<sub>2</sub> price. Moreover, the future trading system must be aligned with the European energy taxation regime to prevent competitive distortions, especially to the detriment of small CHP plants. Regarding the technical design of a future carbon pricing system for the buildings sector, the Commission should follow an upstream solution focused on wholesale fuel trading. Extending the scope to individual households would be entirely unfeasible and risk a significant slowdown of the transition process. These differing technical characteristics between the current ETS and a trading system for the buildings sector should also be considered when contemplating about inter-system flexibility or a possible future integration of the trading systems. As for the EU level funding capacities, the Innovation Fund should be prioritized as the primary allocator of additional resources with a separate funding line for targeted assistance to innovative DHC projects building on the Commission’s flagship-approach with respect to the NextGen credit lines.

Lastly, with respect to the future relationship between the Effort Sharing Regulation and the European emission trading, AGFW again strongly emphasizes the need for a clear sectoral distinction to establish sufficient carbon pricing signals. Furthermore, some Members States have already adopted carbon pricing mechanisms on a national level. The Commission should therefore evaluate the impact of the extension of the ETS on existing national legislation before introducing a new system at EU level in order to avoid a possible distortion of steering effects. Hence, AGFW favours the development of a clearly framed European carbon pricing system along the lines of Option 1 put forward in the published Inception Impact Assessment for Regulation 2018/842 (Effort Sharing).

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