Understanding the Climate Action Regulation

How effective will the EU’s largest post-2020 climate tool be?

Carbon Market Watch Policy Brief, April 2018

Introduction

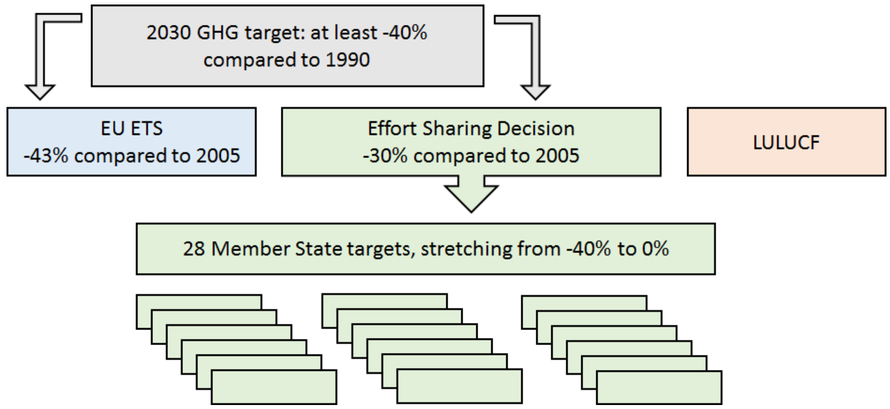
The Climate Action Regulation (CAR), also known as the Effort Sharing Regulation, is Europe’s tool to reduce the climate impact of sectors not covered by the EU Emissions Trading System (EU ETS). Covering 60% of the EU’s greenhouse gas (GHG) emissions, the law sets binding national emission reduction targets for the 2021-2030 period for sectors such as transport, buildings, agriculture and waste.

The CAR sets the pace of decarbonization of the sectors it covers, but its effectiveness as a climate instrument will depend on the policies adopted by each Member State that should enable the transition to net-zero societies. In the coming months, Member States will develop National Energy and Climate Plans (NECPs), in collaboration with stakeholders, to show how they plan to meet their climate commitments.

This policy briefing sets out what has been decided in the Climate Action Regulation and what it means for future climate policy in different EU countries.

The Climate Action Regulation explained

Under the Climate Action Regulation, the EU-wide GHG reduction effort is shared between all the EU Member States. This is done mostly on the basis of a country's wealth as measured by GDP per capita. The wealthiest Member States need to reduce their emissions by 40% below 2005 levels by 2030 and the poorest is allowed to keep its 2005 emissions stable until 2030. These national targets add up to an overall 2030 target of -30% compared to the 2005 emission levels for the EU as a whole.



The covered greenhouse gas emissions

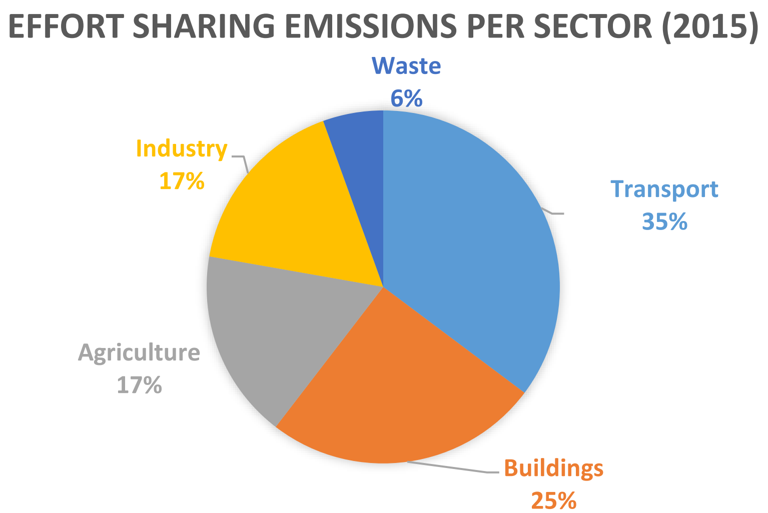
The Climate Action Regulation covers the emissions from the following sectors:

- **Transport**: including road transportation, domestic shipping, non-electric railways and other transportation (pipelines, off-road).
- **Buildings**: mostly energy use in households and services such as heating from fossil fuels. Electricity consumption is excluded as it falls under the EU ETS.
- **Agriculture**: including the non-CO2 emissions (methane, nitrous oxide) from enteric fermentation, manure management and fertilizer use on agricultural soils.
- **Industry**: including smaller energy industries not included in the EU ETS and F-gases used in inter alia air-conditioning and refrigeration.
- **Waste**: including solid waste disposal on land, wastewater, waste incineration and other waste management activity.

The CAR sets an overall GHG reduction target for the sectors it covers, but it does not specify where, how and with what policies a country should reduce its emissions. The choice of measures is therefore the responsibility of each Member State, although existing and new EU policies such as CO_2 standards for cars and trucks and the Energy Performance of Buildings Directive will help Member States to achieve their targets.

National carbon budgets

The Climate Action Regulation sets climate targets for each year in the 2021-2030 period, prescribing the amount of greenhouse gases a Member State is entitled to emit annually. This is called the Annual Emission Allocation (AEA). Under the CAR, the carbon budget for the 2021-2030 period (the total amount of allowed GHG emissions or AEAs) is determined by a trajectory from the starting point to the reduction target for the year 2030. The starting point is determined on the basis of the country's average emissions in the years 2016-2018; the starting date for the linear trajectory has been set at 1 June 2019 or 2020 (whichever is lower).



Flexibility mechanisms

Member States have an obligation to keep their GHG emissions below their Annual Emission Allocations. To make it less costly to comply with these climate targets, Member States are allowed to make use of different flexibilities:

Flexibility over time: Member States can borrow AEA units from following years for up to 10% of their annual target in the 2021-2025 period and up to 5% in the years 2026-2029. They can moreover bank overachievement of the target in a certain year for use in a future year (for up to max. 30% of a country's Annual Emission Allocation).

Flexibility between countries: Member States can trade emission reduction units with each other: They can transfer any surplus as well as a part of their Annual Emission Allocation (5% of its AEA in 2021-2025 and 10% of its AEA in 2026-2030) to other countries.

Flexibility with the EU ETS: Each year, certain Member States can use a limited amount of the EU ETS allowances to offset emissions under the Climate Action Regulation (up to a total of 100 Mt CO_2e). If a country chooses to make use of this flexibility, the ETS allowances will be subtracted from its auctioning volumes, leaving it with less revenues. This will not impact the functioning of the Market Stability Reserve under the EU ETS.

Flexibility with the land use sector: Each year, all Member States are allowed to use a limited amount of forestry and land use (LULUCF) credits if these sectors absorb more carbon from the atmosphere than they emit (up to a total of 280 Mt CO_2e).

Flexibility allowing the use of pre-2020 surplus: Some Member States may benefit from a so-called 'safety reserve' (up to a total of 105 Mt CO_2e) in the 2026-2030 period which should in principle be not more than 20% of the country's pre-2020 surplus. Only Member States that meet certain criteria are eligible. The reserve can only be used provided that it does not jeopardize the achievement of the EU's 2030 climate target.

Pitfalls of certain flexibility mechanisms

The CAR flexibilities have the aim of allowing targets to be met more cost-effectively. Some of them, however, undermine the carbon-free transition of the non-ETS sectors by allowing more greenhouse gases to be emitted in these sectors up to 2030. This applies for example to the flexibilities with the EU ETS and the land use sector, and the flexibility that allows the use of pre-2020 surplus. They, therefore, amount to '***loopholes'***.

The compliance regime

Each year, countries will need to report their greenhouse gas emissions. Every two years, they also need to report on the implemented and planned national policies and measures, as well as on their projected greenhouse gas emissions.

If a country fails to meet its climate target, after taking the flexibility mechanisms into account, it will be faced with an automatic penalty. This penalty takes into account the environmental cost of delaying emission cuts: the excess emissions are multiplied by a factor of 1.08 and added to the emissions of the following year, so that this target becomes more stringent. Every five years (in 2027 and in 2032), the European Commission checks if the Member States complied with their annual targets. If not, a penalty will be applied to the future Annual Emission Allocations.

Implementing the Climate Action Regulation at the national level

The success of the Climate Action Regulation to decarbonise the transport, building, agriculture and waste sectors depends on how it is implemented across Europe. In the coming months, EU Member States will develop National Energy and Climate Plans (NECPs), in collaboration with stakeholders, that will detail which policies and measures will be adopted to meet the climate commitments. The sectors covered by the CAR need to undergo radical changes both in the short and longer term in order to meet the Paris climate goals. Decisions taken in the next few years, in relation to e.g. city planning, agricultural subsidies, public transport infrastructure, building renovations and waste collection, will not only determine how many emissions will be cut up to 2030, but, most importantly, must also set in motion the transition to carbon-free societies.

Required emission cuts in the 2021-2030 period (Mt CO_2e) as a result of the Climate Action Regulation

	2030 target	Emissions cuts (theoretical)[1]	LULUCF credits (max.)	EU ETS credits (max.)	2021 starting bonus	Emission cuts (after flex)[2]
Belgium	-35%	73	3,8	15,7		53
Bulgaria	-0%	-40	4,1		1,6	-46
Czech Republic	-14%	-28	2,6		4,4	-35
Denmark	-39%	33	14,6	7,4		11
Germany	-38%	232	22,3			210
Estonia	-13%	-2	0,9		0,1	-3
Ireland	-30%	59	26,8	19,1		13
Greece	-16%	-96	6,7			-103
Spain	-26%	-38	29,1			-67
France	-37%	234	58,2			176
Croatia	-7%	-16	0,9		1,1	-18
Italy	-33%	96	11,5			85
Cyprus	-24%	1	0,6			0,04
Latvia	-6%	-3	3,1		0,5	-7
Lithuania	-9%	-4	6,5		2,2	-13
Luxembourg	-40%	22	0,25	4,0		18
Hungary	-7%	-59	2,1		6,7	-68
Malta	-19%	-0,03	0,03	0,2		-0,25
Netherlands	-36%	107	13,4	23,6		70
Austria	-36%	29	2,5	11,7		15
Poland	-7%	69	21,7		7,5	39
Portugal	-17%	-44	5,2		1,7	-50
Romania	-2%	-37	13,2		10,9	-61
Slovenia	-15%	-4	1,3		0,2	-6
Slovakia	-12%	-3	1,2		2,2	-6
Finland	-39%	10	4,5	6,9		-2
Sweden	-40%	12	4,9	8,6		-2
United Kingdom	-37%	18	17,8			0
Total	**-30%**	**621**	**280**	**97**	**39**	**205**

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[1] Emission cuts (theoretical): the difference between the climate targets under the Climate Action Regulation and a business-as-usual scenario (the EU 2016 Reference Scenario). Red figures indicate that emissions are allowed to increase compared to business-as-usual.

[2] Emission cuts (after flex): assuming countries make maximum use of the different flexibility mechanisms defined in the table. No use of the 'safety reserve' was assumed. If this reserve is also fully used, the Climate Action Reserve could potentially incentivize merely 100 Mt CO_2e emission reductions in the 2021-2030 period.