



EUROPEAN
COMMISSION

Brussels, **XXX**
[...](2021) **XXX** draft

Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Directive 2003/87/EC and Decision (EU) 2015/1814 to strengthen the EU Emissions Trading System and extend it in line with the Union's increased climate ambition for 2030

(Text with EEA relevance)

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

- **Reasons for and objectives of the proposal**

The **European Green Deal Communication**¹ launched a new growth strategy for the EU that aims to transform the EU into a fair and prosperous society. It reaffirms the Commission's ambition to increase its climate ambition and make Europe the first climate-neutral continent by 2050. The necessity and value of the European Green Deal have only grown in light of the very severe effects of the COVID-19 pandemic on the health and economic well-being of the Union's citizens.

Tackling climate change is an urgent challenge. In line with the scientific findings of the Intergovernmental Panel on Climate Change (IPCC) Special Report, global net-zero CO₂ emissions need to be achieved around 2050, and neutrality for all other greenhouse gases as soon as possible later in the century. This urgent challenge requires the EU to step up its action and demonstrate global leadership by becoming climate neutral by 2050. This objective is set out in the Communication '**A Clean Planet for all**' - A European strategic long-term vision for a prosperous, modern, competitive and climate-neutral economy'².

Based on the European Green Deal strategy and a comprehensive impact assessment, the Commission's Communication of September 2020 on **Stepping up Europe's 2030 climate ambition**³ ('2030 Climate Target Plan') proposed to raise the EU's ambition and put forward a comprehensive plan to increase the European Union's binding target for 2030 towards at least 55% net emission reduction, in a responsible way. Raising the 2030 ambition now helps give certainty to policymakers and investors, so that decisions made in the coming years do not lock in emission levels inconsistent with the EU's objective to be climate neutral by 2050. The 2030 target is in line with the Paris Agreement objective to keep the global temperature increase to well below 2°C and pursue efforts to keep it to 1.5°C.

The European Council endorsed the new EU binding target for 2030 at its meeting of December 2020⁴. It also called on the Commission "*to assess how all economic sectors can best contribute to the 2030 target and to make the necessary proposals, accompanied by an in-depth examination of the environmental, economic and social impact at Member State level, taking into account national energy and climate plans and reviewing existing flexibilities*".

¹ COM(2019)640 final.

² COM(2018) 773 final.

³ COM (2020) 562 final.

⁴ European Council Conclusions 10-11 December 2020 EUCO 22/20 CO EUR 17 CONCL 8.

To this end, the **European Climate Law**, as agreed with the co-legislators, makes the EU's climate neutrality target legally binding, and raises the 2030 ambition by setting a target of at least 55% net emission reductions by 2030 compared to 1990.

In order to follow the pathway proposed in the European Climate Law, and deliver this increased level of ambition for 2030, the Commission has reviewed the climate and energy legislation currently in place that are expected to only reduce greenhouse gas emissions by 40% by 2030 and by 60% by 2050. This '**Fit for 55**' legislative package, as announced in the 2030 Climate Target Plan, is the most comprehensive building block in the efforts to implement the ambitious new 2030 climate target, and all economic sectors and policies will need to make their contribution.

The European Council also invited the Commission in December 2020 to consider exploring ways to strengthen the EU Emissions Trading System (EU ETS), while preserving its integrity and taking into account the need to address distributional concerns and energy poverty. The European Council also invited the Commission to consider proposing measures that enable energy-intensive industries to develop and deploy innovative climate-neutral technologies while maintaining their industrial competitiveness.

The current ETS legislation was revised in 2018 to deliver a 43% reduction in EU ETS emissions by 2030 compared to 2005, coherent with an EU economy-wide emissions reduction target of at least 40% by 2030 compared to 1990. More recent analysis by the Commission services, however, indicates that, if the legislation remains unchanged, the sectors currently covered by the EU ETS would instead achieve emission reductions of -51% in 2030 compared to 2005⁵.

Even though this would mean outperforming the contribution of -43% referred to above, it would still be an insufficient contribution to an overall target of at least -55% compared to 1990. Therefore, the general objective of this initiative is to revise the ETS Directive in a manner commensurate with the 2030 climate ambition to reach at least 55% net greenhouse gas emission reductions by 2030 below 1990 levels and with a gradual and balanced trajectory towards climate neutrality by 2050, in a cost-effective and coherent way while taking into account the need for a just transition and the need for all sectors to contribute to the EU's climate efforts.

As explained in the impact assessment, contribution of the sectors currently covered by the EU ETS of [-XX%] compared to 2005 is considered as best reflecting the 2030 Climate Target Plan results and is taken as the EU ETS cost-efficient ambition contributing to an overall target of at least -55% compared to 1990. Increasing the EU ETS's environmental contribution entails adjusting primarily the total number of allowances issued under the EU ETS (the 'cap'). However, a reduced amount of allowances available to the market affects other pillars of the EU ETS and the carbon price. It impacts core principles such as the need for market stability, the protection against the risk of carbon leakage, the carefully balanced

⁵ Per the EU Reference Scenario 2020 (REF) which serves as baseline for the impact assessment (see section 5.1 of the impact assessment).

distributional effects between Member States, and the availability of funds for the increased investment needs in low-carbon technologies.

At the same time as the EU ETS is brought in line with the overall target of at least -55% compared to 1990, this increased climate ambition also needs to be reflected in the contribution to the EU's climate efforts of sectors currently outside of the EU ETS. The impact assessment accompanying the 2030 Climate Target Plan found that in the absence of additional measures, emissions in certain sectors would not decrease as much as required to be on a path to achieve an economy-wide 55% reduction in emissions. In fact, in maritime transport, emissions today are higher than in 1990, and maritime transport emissions are expected to grow further in a business-as-usual scenario. All pathways assessed as part of the 2030 Climate Target Plan and the Sustainable and Smart Mobility Strategy⁶ envisage 80-82% emissions reductions from international shipping by 2050 relative to 1990 (equivalent to 88-89% emissions reductions relative to 2008)⁷, in order to be consistent with the increased level of climate ambition. Therefore, the European Commission undertook the commitment to extend the EU ETS to maritime transport as part of a basket of EU measures to address emissions from maritime transport, along with action agreed within the IMO.

As specified in the 2030 Climate Target Plan, the building sector is currently responsible directly and indirectly for 36% of energy-related greenhouse gas emissions in the EU and has a large cost-effective potential to reduce emissions. More than half of those emissions are already covered by the existing ETS, notably the provision of electricity for use in buildings and most emissions of district heating. However, many homes are still heated with outdated systems that use polluting fossil fuels such as coal and oil.

The sector of road transport also has a significant cost-effective reduction potential. Today, road transport accounts for a fifth of the EU's greenhouse gas emissions and increased its emissions by over a quarter since 1990. As already considered in the European Green Deal Communication, the Commission is proposing to include the building sector and road transport into emissions trading. The coverage of these sectors by emissions trading, when put in the context of other appropriate regulatory and investment measures for the sectors in question, would provide for increased and more harmonised economic incentives to reduce emissions across these sectors in the EU and increased certainty of delivery of the emission reductions for those sectors.

Building on data coming from the current monitoring, reporting and verification system for shipping established through Regulation (EU) 2015/757, emissions from maritime transport should be included in the existing emissions trading system. To ensure a smooth transition, a phase-in period should be introduced where shipping companies would only have to surrender allowances for a portion of their verified emissions, gradually rising to 100% over 3 years. As around 90 million tons of CO₂ would be added through the extension to maritime transport to the existing ETS, the impact on the other sectors covered would remain limited.

⁶ Source: https://ec.europa.eu/transport/themes/mobilitystrategy_en

⁷ The choice of 2008 as a base year for the emissions reduction projections in maritime transport is made to allow consistency with the IMO objectives that are all expressed in relation to 2008.

Emissions trading for the buildings and road transport sectors should be introduced through separate but adjacent emissions trading. This will avoid any disturbance of the well-functioning emissions trading system for stationary installations and aviation, given the different reduction potentials in those sectors and different factors that influence the demand. Any possible merger of the two systems should be assessed only after a few years of the functioning of the new emissions trading, and based on information and collected market experience. The extension to buildings and road transport requires an upstream approach to regulated entities.

Market stability is crucial for the EU ETS to function correctly to achieve its targets. To ensure the market stability, Decision (EU) 2015/1814⁸ established the market stability reserve (MSR). It began operating in January 2019. The objectives of the MSR are to tackle historical supply-demand imbalances and to make the EU ETS more resilient to major imbalances. The mechanism must preserve regulatory stability and ensure long-term predictability. Article 3 of the Decision requires the Commission to review the functioning of the reserve within three years of the start of the operation. This review needs to be considered together with the effects for market stability of increasing the ambition of the EU ETS, so the necessary amendments to the reserve are proposed together with the amendments to the EU ETS with this proposal.

In this context, this proposal, as part of the Fit for 55 package, has the following specific objectives:

- Strengthening the EU ETS in its current scope in order to provide the appropriate contribution to an overall target of at least -55% GHG emissions compared to 1990.
- Ensuring continued effective protection for the sectors exposed to a significant risk of carbon leakage while incentivising the uptake of low-carbon technologies.
- Addressing the distributional and social effects of this transition, by reviewing the use of auctioning revenues and the size and functioning of the low-carbon funding mechanisms.
- Ensuring that the other sectors than those currently included in the EU ETS contribute cost-effectively to the emission reductions needed in line with EU targets and Paris Agreement commitments notably by including emissions from maritime transport and emissions from buildings and road transport under the rules of the EU ETS while ensuring synergies with other policies targeting those sectors.
- Reviewing the MSR in line with the corresponding legal obligation and examining possible amendments to its design, to fulfil the legal objectives in the MSR decision and to address any issues that may be raised in the context of the increased ambition.

⁸ Decision (EU) 2015/1814 of the European Parliament and of the Council of 6 October 2015 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and amending Directive 2003/87/EC (OJ L 264, 9.10.2015, p. 1–5).

- **Consistency with existing policy provisions in the policy area**

All sectors of the economy should contribute to the reduction of greenhouse gas emissions. The ‘Fit for 55’ climate and energy package is a comprehensive step in overhauling Union legislation to align it with the EU’s increased climate ambition. All initiatives in the package are closely interlinked, and each one depends on the design of the others. This legislative proposal is complementary to the proposals made in the package and maintains consistency with them.

Sectors outside the EU ETS are at present covered by the Effort Sharing Regulation⁹ (ESR), which establishes an overall EU-wide greenhouse gas emission reductions target, as well as binding annual targets for individual Member States to be achieved by 2030. The ESR covers among others the road transport and buildings sectors, as well as emissions from domestic navigation. Contrary to the EU ETS, the sectors covered by the ESR are not subject to an EU-wide carbon price signal. By providing the additional economic incentives (through carbon pricing) necessary to achieving the cost-efficient emission reductions in buildings and road transport, the new ETS would complement the Effort Sharing Regulation in the current scope, which maintains incentives for national action.

Directive (EU) 2018/410 states in recital 4 that action from the International Maritime Organization (IMO) or the Union should start from 2023, including preparatory work on adoption and implementation and due consideration being given by all stakeholders. Also, reducing maritime transport emissions is part of the EU economy-wide reduction commitment under the Paris Agreement.

To date, no adequate measures are in place, either at the global level or in the EU, to achieve the emission reductions necessary from the maritime transport sector to be in line with the EU’s increased level of climate ambition. At the EU level, CO₂ emissions from ships above 5000 gross tonnage travelling to or from ports located within the EEA are being monitored, reported and verified (through the EU Maritime MRV Regulation)¹⁰ since 2018. At the global level, a regulatory framework on the energy efficiency of new ships is in place and energy efficiency measures for existing ships have recently been approved. The IMO has also adopted an Initial Strategy on Reduction of Greenhouse Gas Emissions from Ships, which sets a greenhouse gas emission reduction objective of at least 50% by 2050 compared to 2008 levels. While the recent progress achieved in IMO is welcome, these measures are insufficient to decarbonise international shipping in line with international climate objectives.

Given this situation, the European Commission undertook the commitment to propose a basket of EU measures to increase the contribution of maritime transport to the EU climate efforts, along with the measures agreed at global level within the IMO. Beside the extension

⁹ Regulation (EU) 2018/842 of the European Parliament and of the Council of 30 May 2018 on binding annual greenhouse gas emission reductions by Member States from 2021 to 2030 contributing to climate action to meet commitments under the Paris Agreement and amending Regulation (EU) No 525/2013 (OJ L 156, 19.6.2018, p. 26–42).

¹⁰ Regulation (EU) 2015/757 on the monitoring, reporting and verification of CO₂ emissions from maritime transport, OJ L 123, 19.5.2015, p. 55–76

of the EU ETS to maritime transport, the basket of measures contains the FuelEU Maritime initiative, which aims to increase the demand and deployment of renewable alternative transport fuels, as well as a proposal to review the Energy Taxation Directive (ETD)¹¹ with regard to the current exemption of fuel used by ships from taxation.

Currently, the EU ETS directly or indirectly covers around 30% of buildings emissions from heating. This is related to the system's coverage of district heating and electricity used for heating purposes. Covering all emissions of fossil fuel combustion in this sector and integrating them in the EU emissions trading would present important benefits in terms of effectiveness of emissions reduction. In road transport, emissions trading would have the advantage of capturing fleet emissions under the cap and simultaneously incentivising behavioural change with lasting effects on mobility solutions through the price signal. Nevertheless, the CO₂ emissions performance standards for cars remain the main driver to ensure the supply of modern and innovative clean vehicles, including electric cars. In parallel to applying emissions trading to road transport, the Commission is proposing to strengthen the CO₂ standards for cars and vans for 2030 to ensure a clear pathway towards zero emissions mobility. A part of the revenues generated by emissions trading in the new sectors could be used to address the social impacts arising from the new emissions trading in these sectors and invested in measures intended to accelerate the building renovation wave as well as the uptake of zero-emission vehicles and to develop the necessary infrastructure, such as strategically located, smart and intelligent refilling and charging stations for zero-emission vehicles.

The ambition level, emissions cap and trajectory for the new ETS is proposed to be set coherently in line with the cost-efficient emission reductions of buildings and road transport stemming from a combination of carbon pricing and strengthening the existing regulatory framework for these sectors. [Support measures to promote energy efficiency in vulnerable or low-income households, would be necessary to avoid excessive distributional effects, via inter alia directing part of the revenues from carbon pricing on buildings to this purpose.]

- **Consistency with other Union policies**

The European Green Deal, its climate neutrality objective, and the twin green and digital transition are a core priority of the European Union. The 'Fit for 55' package, the Next Generation EU and the Multiannual Financial Framework for 2021-2027 will help achieving the twin green and digital transitions that Europe is aiming for. The combination of these policies will address the economic crisis and accelerate the shift to a clean and sustainable economy, linking climate action and economic growth.

Reducing net GHG emission by 2030 compared to 1990 at an economy wide scale by at least 55% calls not only for changes to the current climate, but also energy policy framework. The 'Fit for 55' package provides a comprehensive review of the climate and energy legislation to achieve this objective. The ETS amendment proposal is part of this large set of coherently designed policy proposals. The ETS is a core instrument to help the EU achieve the increased

¹¹ Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity (OJ L 283, 31.10.2003, p. 51–70).

2030 target and a successful and just transition towards the 2050 climate neutrality. As such, this initiative is linked to many other policy areas, including the Union's external policies. For example, as a market-based EU-wide instrument, the ETS is consistent with and further strengthens the EU's internal market.

Consistency with other Union policies is also ensured through the coherence of the impact assessments for the EU ETS with those for the remainder of the 2030 climate, energy and transport framework¹², such as the complementarity of extending emission trading with the Energy Efficiency Directive¹³, and with other measures presented as part of the basket of measures to address greenhouse gas emissions from maritime transport. A common baseline and common core policy scenarios with other initiatives of the package are used. These scenarios take into account all relevant EU actions and policies.

Additional administrative costs of the extension to road transport and buildings are envisaged to be limited by using, where possible, existing structures used for the Energy Taxation Directive and for Energy Savings Obligations under the Energy Efficiency Directive. In turn, additional energy savings would be enhanced by the new ETS, with its potential link to energy savings under Article 7 of the Energy Efficiency Directive.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

• Legal basis

The legal basis for this proposal is Article 192 TFEU. In accordance with Article 191 and 192(1) TFEU, the European Union shall contribute to the pursuit, inter alia, of the following objectives: preserving, protecting and improving the quality of the environment; promoting measures at international level to deal with regional or worldwide environmental problems, and in particular combating climate change.

• Subsidiarity (for non-exclusive competence)

The ETS Directive is an existing EU policy instrument adopted in 2003. In accordance with the principle of subsidiarity set out in Article 5 of the TFEU, the objectives of the proposal amending this instrument can only be achieved through a Commission proposal at EU level.

Climate change is a trans-boundary problem and EU action can effectively complement and reinforce regional, national and local action. Increasing the 2030 target for EU greenhouse gas

¹² Notably the ESR; the Land Use, Land Use Change and Forestry (LULUCF) Regulation; CO2 Emissions Performance Standards for Cars and Vans; the Renewable Energy Directive (REDII); the Energy Efficiency Directive (EED); and, at a later stage, the Energy Performance of Buildings Directive. Other relevant initiatives include the revision of the Energy Taxation Directive; the Zero Pollution Action Plan and the revision of the Industrial Emissions Directive; initiatives on mobility, such as those on transport fuels (FuelEU maritime initiative and ReFuelEU aviation initiative) and a proposal for a Carbon Border Adjustment Mechanism (CBAM).

¹³ Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency, amending Directives 2009/125/EC and 2010/30/EU and repealing Directives 2004/8/EC and 2006/32/EC (OJ L 315, 14.11.2012, p. 1–56).

reductions will impact many sectors across the EU economy and coordinated action at the EU level is therefore indispensable and has a much bigger chance of leading to the necessary transformation, acting as a strong driver for cost-efficient change and upward convergence. Furthermore, many of the elements of this proposal have an important internal market dimension, in particular the options related to the carbon leakage protection and the low-carbon funding mechanisms.

As a carbon market, the EU ETS incentivises emission reductions to be made by the most cost-efficient solutions first across the activities it covers, achieving greater efficiency by virtue of its scale. Implementing a similar measure nationally would result in smaller, fragmented carbon markets, risking distortions of competition and likely lead to higher overall abatement costs. The same logic holds for the extension of carbon pricing to new sectors.

The cross-border dimension of the maritime transport sector calls for coordinated action at European level. EU action can also inspire and pave the way for broader action, e.g. as regards maritime transport within IMO and by third countries.

- **Proportionality**

As set out in section 7 of the impact assessment, the proposal complies with the proportionality principle because it does not go beyond what is necessary in order to achieve the objectives of implementing the EU's greenhouse gas emission reduction target for 2030 in a cost-effective manner while at the same time ensuring the proper functioning of the internal market.

The European Council has endorsed an overall economy-wide and domestic reduction in greenhouse gas emissions of at least 55% below 1990 levels by 2030. This proposal covers a large part of these greenhouse gas emissions, and revises the Directive in order to achieve this objective.

- **Choice of the instrument**

The objectives of this proposal can be best pursued through a Directive. This is the most appropriate legal instrument to make amendments to the existing ETS Directive (Directive 2003/87/EC).

A Directive requires Member States to achieve the objectives and implement the measures into their national substantive and procedural law systems. This approach gives the Member States more freedom when implementing an EU measure than does a Regulation, in that Member States are left the choice of the most appropriate means of implementing the measures in the Directive. This allows Member States to ensure that the amended rules are consistent with their existing substantive and procedural legal framework implementing the EU ETS, in particular regulating permits for installations as well as enforcement measures and penalties.

A Directive is also the appropriate instrument to amend Decision (EU) 2015/1814 establishing the MSR because its review needs to be considered together with the effects for market stability of increasing the ambition of the EU ETS.

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

- ***Ex-post evaluations/fitness checks of existing legislation***

There was no *ex-post* evaluation or fitness check related to this proposal due to the early stage of implementation of the current ETS legislation, which started to apply in 2021 as amended by Directive (EU) 2018/410 of the European Parliament and of the Council¹⁴. Consequently, limited data was available for an evaluation.

- **Stakeholder consultations**

At various steps in developing this proposal, Member States, industry representatives from the private sector, non-governmental organisations, research and academic institutions, trade unions and citizens were involved.

The revision of the EU ETS builds upon the feedback on the 2030 Climate Target Plan and interlinkages of the EU ETS with parallel policies and the broader objectives of the European Green Deal. The main objective of the consultations on the EU ETS revision was to gather stakeholders' views on the strengthening of the existing EU ETS, the extension of the EU ETS to new sectors (maritime transport as well as buildings, road transport or all fossil fuel combustion) and the review of the MSR. The consultation also looked for inputs on how to address the risk of carbon leakage, the use of revenues and low-carbon support mechanisms.

The Commission first invited feedback on an inception impact assessment, outlining the initial considerations and policy options of the revision¹⁵. The Commission then organised an online public consultation with a questionnaire for each of the proposals of the 'Fit for 55' package, receiving almost 500 replies¹⁶. To support the initiative concerning carbon pricing for maritime transport, a targeted stakeholder survey was carried out accompanied by a targeted interview programme¹⁷. In addition, the Commission held (virtual) bilateral and multilateral stakeholder meetings, including with industry representatives across different sectors, non-governmental organisations and Member States and participated in virtual

¹⁴ Directive (EU) 2018/410 of the European Parliament and of the Council of 14 March 2018 amending Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments, and Decision (EU) 2015/1814 (OJ L 76, 19.3.2018, p. 3–27).

¹⁵ The inception impact assessment was open for feedback from 29 October 2020 to 26 November 2020 and received about 250 contributions. The outcome can be found on the following website: <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12660-Updating-the-EU-Emissions-Trading-System>.

¹⁶ This was open for 12 weeks from 13 November 2020 to 5 February 2021. The outcome can be found on the following website: <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12660-Updating-the-EU-Emissions-Trading-System/public-consultation>.

¹⁷ The stakeholder survey run from December 2020 and February 2021, and the targeted interview programme from January 2021 to February 2021.

conferences. Finally, the Commission instructed a contractor to organise two expert workshops¹⁸ on the review of the MSR.

The results of the consultation activities are reported in the impact assessment accompanying this proposal and have been taken into account for the current proposal to the extent possible.

In general, the public consultations showed broad support for the EU ETS as a policy instrument.

Many stakeholders support the strengthening of the existing EU ETS to increase its ambition in line with the new 2030 target and based on cost-efficiency considerations. Only some respondents from the private sector and from civil society argued for, respectively, a lower or higher contribution compared to the cost-efficiency principle. To achieve the strengthened ambition, stakeholders generally found the adjustment of the linear reduction factor important, while some stakeholders also highlighted the importance of a combination with a one-off reduction in the quantity of allowances, as reflected in this proposal.

On free allocation and the risk of carbon leakage, a large majority of stakeholders is in favour of amending the current carbon leakage framework, while some industry stakeholders want to maintain the current carbon leakage framework without changes. Opinions on the specific amendment options are mixed and the introduction of other measures to further incentivise greenhouse gas reductions received the largest support. The proposal provides such incentives by making free allocation conditional on investments in techniques to increase energy efficiency. The modification of the benchmark values to ensure faster incorporation of innovation and technological progress obtained support from a wide range of stakeholders except from some parts of the private sector. The proposal includes this approach as it is considered to deliver a fairer and more transparent distribution of free allocation than a higher cut for all sectors by the cross-sectoral correction factor.

As regards the use of auction revenues, the proposal reflects the view expressed by many stakeholders that stricter rules are necessary to ensure Member States spend their EU ETS auction revenues in line with climate objectives.

With regard to low-carbon funding mechanisms, stakeholders generally welcome an increase in the size of the Innovation Fund as well as the introduction of additional supporting instruments such as carbon contracts for difference. This is duly reflected in the proposal by increasing the size of the Innovation Fund and extending its scope.

With regard to the Modernisation Fund, a majority of stakeholders, in particular from civil society and parts of the private sector, supports an increase in the Modernisation Fund, as reflected in this proposal. Stakeholders generally support the streamlining of the types of investments that can be financed by the Modernisation Fund and enhancing the Modernisation Fund's coherence with the European Green Deal. The proposal contributes to this objective

¹⁸ https://ec.europa.eu/clima/events/expert-workshop-market-stability-reserve_en,
https://ec.europa.eu/clima/events/2nd-expert-workshop-market-stability-reserve_en.

by removing the exception for the financing of fossil fuel-fired district heating in certain Member States.

The MSR has wide support across stakeholder groups; however, there is no consensus about the necessary changes to its parameters. Civil society expressed relatively more support for a strengthening of the parameters of the MSR than the private sector. There was support for maintaining the invalidation rule, either unreservedly or with an amendment, while some stakeholders suggested that the invalidation rule should be abolished. At the expert workshops, some stakeholders saw a need for a variable intake rate to avoid large threshold effects and more frequent reviews. The proposal strikes a balance between the need to ensure a reduction of the market surplus over a reasonable time horizon, the predictability of the mechanism as well as its complexity. In addition, the proposal to include aviation allowances and emissions in the calculation of the surplus corresponds to the preferred option of the majority of stakeholders.

With regard to maritime transport, the vast majority of stakeholders that took part in the targeted survey indicated that the maritime sector should contribute more to climate action than it currently does. The extension of the existing EU ETS to maritime transport is the preferred carbon pricing option expressed by stakeholders, while the shipping industry stressed the importance of measures at international level. The proposal addresses views expressed by stakeholders by covering voyages from incoming ships and including a review clause in relation to the work in the IMO towards global market-based measures. Emissions from incoming ships is one of the five approaches which are still under consideration in the United Nations Framework Convention on Climate Change (UNFCCC) context.

With regard to the road transport and buildings sectors, the preferred policy option of a wide range of stakeholders is to start with a separate self-standing system, as reflected in this proposal. Views are divided on whether the EU ETS revision should already determine when and how emissions trading for the road transport and buildings sectors could be gradually integrated with the existing EU ETS. In particular, non-governmental organisations pointed to the risks associated with a linking of the two systems. The proposal duly takes into account such concerns by proposing separate but adjacent emissions trading and a review clause.

- **Collection and use of expertise**

This proposal builds upon evidence gathered in the impact assessment for the previous EU ETS revision concluded in 2018, the impact assessment accompanying the 2030 Climate Target Plan, analysis conducted in support of the Commission's Long-Term Strategy and relevant evidence compiled in other concurrent Green Deal initiatives, as well as earlier studies related to maritime, road transport and buildings greenhouse gas emissions. It builds on emissions data and experiences from the implementation of the EU monitoring, reporting and verification systems. It makes use of updated EU Reference Scenario¹⁹, which includes

¹⁹ Modelling-based projections of energy, transport and greenhouse gas emissions trends to 2050, building on consistent set of assumptions across EU, Member States and EU policies, Member States specific characteristics; and relying on the consultation of Member States experts.

COVID-19 impacts, and updated policy scenarios, building upon the scenarios developed for the 2030 Climate Target Plan. These scenarios were prepared with the help of a contract with E3M lab, National Technical University of Athens, and the detailed modelling results will be published alongside the legal proposals.

In addition, the Commission bases itself on the growing body of peer-reviewed empirical research on the EU ETS and makes use of several support contracts. Among the support contracts, Vivid Economics conducted a study to support the European Commission in the review of the MSR²⁰.

Concerning carbon leakage provisions, a supporting study carried out by Öko-Institut, Trinomics, Ricardo and Adelphi on “Assessment of potential carbon leakage in the third and fourth trading phase of EU Emissions Trading System” has been considered. Furthermore, Ricardo conducted a study on EU ETS for maritime transport and possible alternative options of combinations to reduce greenhouse gas emissions.

- **Impact assessment**

The proposed Directive is accompanied by an impact assessment, which builds on the findings of the comprehensive impact assessment for the 2030 Climate Target Plan²¹. This formed the analytical basis to set the objective of at least net 55% reduction in greenhouse gas emissions by 2030 compared to 1990. An executive summary and the positive opinion of the regulatory scrutiny board on the impact assessment will also be made publicly available. The impact assessment is based on integrated modelling scenarios that reflect the interaction of different policy instruments on economic operators, in order to ensure complementarity, coherence and effectiveness in achieving the 2030 climate ambition. This is complemented by available data and specific analytical tools for addressing specific policy design questions.

The impact assessment analyses three types of problems. First, those associated with the need to strengthen the existing EU ETS in a commensurate way with the increased net greenhouse gas emissions reduction target by 2030, compared to 1990, of at least -55%, while avoiding supply/demand imbalances. Second, the need to ensure certain sectors contribute sufficiently to the achievement the increased target. Finally, the need for increased investment and greater capacity to address the distribution of impacts of emission reduction measures, while funds remain limited.

Regarding strengthening the existing EU ETS to increase its ambition in line with the net at least -55% 2030 target, any of the option packages would be effective and efficient in achieving the 2030 objective. The impact assessment also concluded that a more targeted approach to free allocation is needed, where it still applies, in the form of strengthened benchmarks and conditionality on decarbonisation efforts in order to incentivise the uptake of low-carbon technologies.

²⁰ Vivid Economics, (2021) – “Review of the EU ETS’ Market Stability Reserve”, report prepared for DG CLIMA.

²¹ SWD(2020)176.

Regarding the MSR, the impact assessment amongst other showed that to maintain the good functioning of the EU ETS, the intake rate should be maintained at 24% until 2030, and adapted so as to remove undesired threshold effects when the total number of allowances in circulation (TNAC) is very close to the 833 million upper threshold.

To extend the climate policy framework to maritime transport, four main options and different geographical scopes were analysed. The preferred option would be the integration of the maritime transport sector in the existing EU ETS.

The impact assessment looked at establishing emissions trading for road transport and buildings or all fossil fuel combustion as a new self-standing emissions trading as a main option. Both options would provide additional economic incentives and via the cap ensure the delivery of the same relative reduction in emissions in the sectors concerned, of XX% by 2030 compared to 2005. Including only buildings and road transport in the scope of an additional emission trading system, as opposed to all fossil fuel-consuming sectors currently outside the ETS, has clear benefits in terms of economic efficiency, notably as it would avoid the creation of a new carbon leakage risk protection regime for those parts of small industry, who would be in need of such a regime, but would be subject to a burden likely disproportionate to its benefits.

- **Regulatory fitness and simplification**

The EU ETS legislation has consistently favoured approaches to minimise the regulatory burden for both economic operators and administrations. While the majority of installations under the EU ETS are in the energy-intensive industries with market structures characterised by large enterprises, the proposal also caters for small emitters, which may be owned by SMEs or micro enterprises. In particular, in addition to existing rules alleviating the administrative burden and costs of monitoring and reporting emissions, installations with low emissions benefit from the possibility for Member States to exclude them from the EU ETS if they are subject to national measures leading to an equivalent contribution to emission reductions.

In line with the Commission's commitment to Better Regulation, this proposal has been prepared inclusively, based on full transparency and continuous engagement with stakeholders, listening to external feedback and taking into account external scrutiny to ensure the proposal strikes the right balance (see also section on the collection and use of expertise).

The envisaged extension to maritime transport would build on existing monitoring, reporting and verification mechanisms that exempt small ships. The new EU ETS for other sectors would apply upstream, building on existing provisions regulating tax warehouses or fuel suppliers.

- **Fundamental rights**

The proposal respects the fundamental rights and observes the principles recognised in particular by the Charter of Fundamental Rights of the European Union. In particular, it contributes to the objective of a high level of environmental protection in accordance with the

principle of sustainable development as laid down in Article 37 of the Charter of Fundamental Rights of the European Union²².

4. BUDGETARY IMPLICATIONS

[To be reviewed with the financial statement and own resources proposal]

The EU ETS generates significant revenues. The proposal affects national budgets and administrations primarily because most of these auction revenues at present accrue to Member States. The secure operation of the Union registry is funded from the Union budget.

There are potentially significant positive impacts on national budgets from the extension of the EU ETS scope to maritime transport and the new EU ETS for road transport and buildings. The direct impact on national budgets will also depend on to which extent additional revenues will be directed to EU own resources. In line with the inter-institutional agreement on the budgetary matters²³, the Commission is proposing an own resource based on the EU ETS²⁴.[--]

Extending the EU ETS scope to maritime transport and the new EU ETS for road transport and buildings will require additional resources for the secure operation of the Union registry, as specified in the financial statement accompanying this proposal.

5. OTHER ELEMENTS

- **Implementation plans and monitoring, evaluation and reporting arrangements**

The Commission will continue to monitor and evaluate the functioning of the EU ETS in its annual Carbon Market Report, as provided under Article 10(5) of the ETS Directive. This covers also the impacts of the current revision of the EU ETS. The Commission's annual Carbon Market Report and Member States annual report shall also apply to the sectors to which emissions trading is extended. The monitoring, reporting and verification data obtained through the regulation of the new sectors will be a key source of information for the Commission to evaluate progress in the sectors concerned.

As for other sectors, monitoring, reporting and verification rules for shipping (currently contained in Regulation (EU) 2015/757 of the European Parliament and of the Council²⁵) will be brought within the ETS Directive. The outcome of the current co-decision process to amend Regulation (EU) 2015/757 should be taken into account in the legislative process, with revised rules for shipping being incorporated into the ETS revision as appropriate.

²² OJ C 326, 26.10.2012, p. 391.

²³ OJ L 433I, 22.12.2020, p. 28–46

²⁴ [---]

²⁵ Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport, and amending Directive 2009/16/EC (OJ L 123, 19.5.2015, p. 55–76).

Furthermore, evaluation of progress on the application of the ETS Directive is provided for in the current Article 21 of the Directive itself²⁶.

The initiative builds on the process based on integrated national energy and climate plans and the robust transparency framework for greenhouse gas emissions and other climate information that is contained in Regulation (EU) 2018/1999 of the European Parliament and of the Council²⁷. The Commission will use *inter alia* the information submitted and reported by Member States under the Governance Regulation as a basis for its regular assessment of progress.

Further details on monitoring and evaluation are provided in section 9 of the impact assessment accompanying this proposal.

- **Detailed explanation of the specific provisions of the proposal**

The main elements of the ETS Directive which are amended are the following:

Maritime Transport (Article 3, Articles 3g to 3l, and Article 16)

The proposal extends the scope of the EU's Emissions Trading System to cover maritime transport. To this end, the proposal amends the definition of "emissions" in Article 3(b) to include emissions from ships performing a maritime transport activity, expands Chapter II of the Directive to cover "aviation and maritime transport" and adds maritime transport as a new activity in Annex I. Further, it includes new definitions for "shipping company" and "administering authority in respect of shipping companies" in Article 3(v) and Article 3(w) respectively. To expand Chapter II to maritime transport, it inserts Articles 3g to 3n.

The extension of the EU ETS to maritime transport applies in respect of emissions from incoming voyages and emissions occurring at berth in an EU port, and the same rules on auctioning; the transfer, surrender and cancellation of allowances, penalties and registries apply to maritime transport as to the other sectors covered by the EU ETS (Article 16). The obligation to surrender allowances in the maritime transport sector is gradually phased-in over the period 2023 to 2025, with shipping companies having to surrender 100% of their verified emissions as of 2026 (Article 3h). In accordance with this phase-in, to the extent fewer allowances are surrendered in respect of verified emissions for maritime transport during these years, the amount of allowances not surrendered should be cancelled. The existing monitoring and reporting rules (Article 3i), as well as verification and accreditation rules (Article 3j) for emissions from maritime transport are to be incorporated in their entirety in

²⁶ This article requires Member States to submit to the Commission an annual report paying particular attention to issues including the allocation of allowances, operation of the Registry, application of monitoring and reporting, verification and accreditation and issues relating to compliance.

²⁷ Regulation (EU) 2018/1999 of the European Parliament and of the Council of 11 December 2018 on the Governance of the Energy Union and Climate Action, amending Regulations (EC) No 663/2009 and (EC) No 715/2009 of the European Parliament and of the Council, Directives 94/22/EC, 98/70/EC, 2009/31/EC, 2009/73/EC, 2010/31/EU, 2012/27/EU and 2013/30/EU of the European Parliament and of the Council, Council Directives 2009/119/EC and (EU) 2015/652 and repealing Regulation (EU) No 525/2013 of the European Parliament and of the Council (OJ L 328, 21.12.2018, p. 1–77).

the MRV system under the EU ETS. Where the MRV rules need to be adjusted to fit into the EU ETS context, they can be amended through implementing legislation. Once the EU maritime transport MRV system is integrated in the overall ETS Directive and its MRV framework, the maritime MRV Regulation ought to be repealed (Article 4 of this Directive). In addition to the general EU ETS rules on penalties, expulsion orders can be issued against ships under the responsibility of a shipping company that has failed to surrender allowances for two or more consecutive reporting periods, with the result that ships under its responsibility can be denied entry into an EU port (Article 16(11a)). Each shipping company falling within the scope of application of the EU ETS is attributed to a Member State – the administering authority – for its administration under the Directive. The administering authority is determined based on where the shipping company is registered and if the company is not registered in a Member State, on the number and origin of historical port calls in the EU. As of 2024, the Commission publishes and regularly updates a list of shipping companies covered by the Directive and their respective administering authority (Article 3k). A reporting and review clause is included (Article 3l) to monitor the implementation of this Chapter and to take account of relevant developments at the level of the IMO.

Linear reduction factor and one-off cap reduction (Art. 9)

The linear reduction factor is changed to [XX]% from the year following the entry into force of the Directive amending the ETS Directive. It ensures that the overall quantity of allowances ('cap') will decline at an increased annual pace resulting in an overall emission reduction of sectors under the EU ETS of [XX%] by 2030 compared to 2005. The increased linear reduction factor is combined with a one-off downward adjustment of the cap to reduce it to be in line with this level of annual reduction having been applicable from 2021. In addition, from the year following entry into force, the cap is to be increased by an amount of allowances corresponding to the maritime transport emissions to be included in the EU ETS and derived from data from the EU Maritime transport MRV system for the years 2018 and 2019.

Use of auction revenues (Article 10)

To address the increased needs in low-carbon investments, the provision on the use of auction revenues is amended so that Member States must use all the revenues for climate-related purposes, including to support low-income households' sustainable renovation.

Further, to address the distributional and social effects of the transition, the proposal provides for auctioning an additional 2% of the cap to fund the energy transition of the Member States with GDP per capita below [--]% of the EU average in 2016-2018, through the Modernisation Fund.

More stringent benchmark approach and establishing conditionality for free allocation (Article 10a(1))

To reduce the possibility of applying the cross-sectoral correction factor following the adjustment of the cap, the update of the benchmarks is proposed to follow closer the emission reductions in sectors and sub-sectors, by increasing the maximum update rate to 2.5% per

year as of 2026 instead of the current 1.6%. This approach is considered to deliver a fairer and more transparent distribution of free allocation than a potential higher cut for all sectors by the cross-sectoral correction factor.

In addition, free allocation is made conditional on decarbonisation efforts in order to incentivise the uptake of low-carbon technologies. Installations covered by the obligation to conduct an energy audit under Article 8(4) of the Energy Efficiency Directive ('EED') will be required to implement recommendations of the audit report, or to demonstrate the implementation of other measures which lead to greenhouse gas emission reductions equivalent to those recommended by the audit report. Otherwise, they would see their free allocation reduced. In accordance with Article 8(4) EED, SMEs are not subject to an energy audit. Further, under the conditions of Article 8(6) EED, enterprises that are not SMEs and that are implementing an energy or environmental management system are exempted from the energy audit requirement.

Carbon border adjustment measures (Article 10a(1))

A Carbon Border Adjustment Measure (CBAM) is an alternative measure to mitigate carbon leakage risks. Sectors and subsectors covered by that measure should therefore not receive free allocation.

Carbon contracts for difference (Article 10a(8))

Carbon contracts for difference (CCDs) are an important element to trigger emission reductions in industry. Project-based carbon contracts for difference offer the EU the opportunity to guarantee investors in innovative climate-friendly technologies a fixed price that rewards CO₂ emission reductions above the current price levels in the EU ETS. The scope of the Innovation Fund is extended to provide support to projects in the form of price-competitive tendering support such as CCDs.

Modernisation Fund (Article 10d)

This proposal aligns the Modernisation Fund with new climate objectives of the Union by requiring that investments are consistent with the objectives of the European Green Deal and the Climate Law and eliminating the support to investments related to any fossil fuels, instead of only solid fossil fuels. In addition, the proposal: increases the percentage of the fund that needs to be invested in priority investments; gives more prominence to renewable sources and energy efficiency investments in transport, buildings, waste and agriculture; targets energy efficiency as a priority area at the demand side, including industry explicitly as eligible sector; and includes the support of households to address energy poverty.

Carbon Capture and Utilisation (Articles 3 point (b) and Article 12(3b))

The increased climate ambition will encourage making use of all the technological solutions to reduce emissions, including carbon capture and utilisation. As a result, the proposal establishes that surrender obligations do not arise for emissions of CO₂ that end up

permanently chemically bound in a product so that they do not enter the atmosphere under normal use.

Removal of barriers for innovative low-carbon technologies by modifying the EU ETS scope and benchmarks (Article 2, Article 10a and Annex I)

The EU ETS free allocation rules are amended to better support decarbonisation of energy intensive industries by the deployment of break-through technologies.

Efficient technologies just below benchmark level receive more free allocation than they emit. This puts innovative technologies outside the EU ETS at a competitive disadvantage, so investments in those technologies may be discouraged. Innovative installations can fall out of the EU ETS because they change their production process or because their total rated thermal input of the combustion units of an installation decreases to less than 20 MW.

This disincentive is addressed by: (i) specifying that installations stay within the EU ETS if they reduce the total capacity of their combustions units to reduce greenhouse gas emissions (e.g. through electrification); (ii) making the definitions of activities technology neutral (removing references to fossil fuels or specific production processes); (iii) referring to production capacities instead of combustion capacities and (iv) reviewing the benchmark definitions to ensure equal treatment of installations independently of the technology used, including when using low- or zero-carbon technologies. Maintaining innovative installations in the EU ETS will also reduce benchmark values and thus encourage greater emissions reductions.

Introduction of emissions trading for buildings and road transport (Chapter IVa)

New emissions trading for buildings and road transport should be established as a separate self-standing system from 2025 (Chapter IVa). During the first year, the regulated entities will be required to hold a greenhouse gas emissions permit and to report their emissions for years 2024 and 2025 (Articles 30b and 30f). The issuance of allowances and compliance obligations for these entities will be applicable only from 2026, which will allow the new system to start functioning in an orderly and efficient manner (Articles 30c, 30d and 30e). As there is a substantially large number of small emitters in the sectors of buildings and road transport, and for reasons of technical feasibility and administrative efficiency, the point of regulation is established not with the emitters, but further upstream the supply chain (Article 30b and Annex III). Therefore, the release for consumption of fuels which are used for combustion in the sectors of buildings and road transport will be the activity regulated for the new system (Annex III). The scope of the sectors of buildings and road transport is defined on the basis of relevant sources of emissions included in [2006 IPCC Guidelines for National Greenhouse Gas Inventories \(Annex III\)](#). The regulated entities are defined in line with the system of excise duty of Council Directive (EU) 2020/262²⁸, since a robust monitoring and reporting mechanism for the quantities of fuels released for consumption already exists for tax purposes

²⁸ Council Directive (EU) 2020/262 of 19 December 2019 laying down the general arrangements for excise duty (recast) (OJ L 58, 27.2.2020, p. 4-42).

under that Directive. The monitoring, reporting and verification obligations in the sectors of buildings and road transport will be aligned to the extent possible with the well-functioning mechanisms established for stationary installations and aviation (Article 30(f)).

The emissions cap for the new emissions trading system will be set from 2026 based on data collected under the Effort Sharing Regulation and ambition level and decrease to reach emission reductions of XX% in 2030 compared to 2005 for the sectors of buildings and road transport (Article 30c and Annex IIIa). A corresponding linear reduction factor is defined. Once the monitoring and reporting of the new emissions trading is established, the total quantity of allowances for 2028 will be adjusted on the basis of the available MRV data for the period 2024 to 2026. The linear reduction factor will be revised only if the MRV data is significantly higher than the initial cap, and not due to small-scale differences with EU UNFCCC inventory data.

The allowances for the new emissions trading will be auctioned as no free allocation is foreseen (Article 30d). In order to ensure a smooth start of emissions trading in the new sectors, a certain amount of allowances will be front-loaded (first subparagraph of Article 30d(2)). In addition, to ensure market stability from the start a Market Stability Reserve will also operate in the sectors concerned based on specific rules (second subparagraph of Article 30d(2)). As the system is new, mitigation measures are foreseen in order to address the potential risk of excessive price volatility, which might be particularly high at the start of emissions trading in the new sectors (Article 30h).

In order to address some of the transitional and social challenges from the carbon pricing in the new sectors, as well as to ensure targeted support for innovation, emissions trading for road transport and buildings will also contribute to the already existing low-carbon funds. Thus, 150 million allowances issued under the new emissions trading system for road transport and buildings will be made available to the Innovation Fund to stimulate the green transition (Article 30d(4)).

The Commission will monitor the application of the rules of the new emissions trading and, if necessary, it will propose a review by 1 January 2028 to improve its effectiveness, administration and practical application (Article 30i).

The main elements of the MSR Decision amended through the proposal are the following:

Taking into account net demand from aviation (Article 1(4a))

The proposal amends the calculation of the total number of allowances in circulation so that it includes aviation emissions, and allowances issued in respect of aviation. Regulation (EU) 2017/2392 of the European Parliament and of the Council²⁹ amended Article 12(3) of the EU ETS Directive to allow all operators to use all allowances that are issued for their surrender obligations, including aviation allowances. The accuracy and the efficacy of the reserve as a

²⁹ [Regulation \(EU\) 2017/2392 of the European Parliament and of the Council of 13 December 2017 amending Directive 2003/87/EC to continue current limitations of scope for aviation activities and to prepare to implement a global market-based measure from 2021 \(OJ L 350, 29.12.2017, p. 7–14\).](#)

measure of the market's stability through its supply and demand will be improved by including aviation allowances in the calculation of the reserve, while preserving its environmental integrity. As such, aviation emissions and allowances are counted into the total number of allowances in circulation if they have occurred, or were issued, as of the year following the entry into force of this proposal. Although there are no separate maritime allowances, the text must be modified to include allowances and emissions in relation to the maritime sector in the calculation because the text currently refers exclusively to emissions and allowances for installations.

Intake rate (Article 1(5))

The intake rate is amended in order to address the 'threshold effect' that would take place when the total number of allowances in circulation (the TNAC) is very close to the upper threshold. In that case, one allowance more or less in the TNAC may trigger or not intakes, depending on whether the TNAC is above or below the threshold. This uncertainty may create price volatility on the market.

The proposal modifies the mechanism of the intake rate. It proposes a buffer MSR intake when the TNAC is between 833 million and 1096 million. In that case, the intake will be the difference between the TNAC and the 833 million threshold. As long as the TNAC is above 1096 million allowances, the normal intake rate would apply (24% until 2030).

The reason for choosing the figure of 1096 million allowances is that, at that amount, the 24% intake and the difference between the TNAC and the upper threshold are close to equal. This addresses the threshold effect, all the while maintaining an efficient MSR intake if the TNAC is higher.

Definition of the total number of allowances in circulation (Article 1(5))

When calculating the TNAC, the formula will specify that only allowances issued and not put in reserve are included in the supply of allowances, and the number of allowances in the reserve is no longer subtracted from the supply of allowances. This change makes the calculation of the total number of allowances in circulation clearer, and has no material impact on its result, including on the previous calculations of the indicator.

Invalidation mechanism (Article 1(5a))

As of 2023, allowances in the MSR above the level of auction volumes of the previous year are invalidated. However, the level of auction volumes of the previous year depends on various elements, such as the cap, and the operation of the MSR itself. In order to ensure that the level of allowances that remains in the reserve after the invalidation is more predictable, it is proposed to limit the number of allowances in the reserve at a level of 400 million allowances. This value also corresponds to the lower threshold for the value of the TNAC, below which allowances are released from the MSR.

MSR for the emissions trading for road transport and buildings (Article 1a)

To address the risk of an imbalance between the supply and demand, a Market Stability Reserve will also operate for the new emissions trading for road transport and buildings, with allowance intakes and releases based on the thresholds for the surplus of allowances in the respective market. Moreover, to allow that the MSR can operate as an effective tool to address imbalances on the market from the start of emissions trading in the two sectors, a number of allowances for the new sectors will be created in the reserve. In order to address the potential risk of excessive price volatility, measures are foreseen to allow for release of additional allowances from the MSR. However the triggering mechanism for this additional release will be based on the increase in the average allowance price and not on the surplus of allowances in the market.

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DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Directive 2003/87/EC and Decision (EU) 2015/1814 as regards the Union's increased climate ambition for 2030 to strengthen the EU Emissions Trading System and extend it

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 192(1) thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Economic and Social Committee³⁰,

Having regard to the opinion of the Committee of the Regions³¹,

Acting in accordance with the ordinary legislative procedure,

Whereas:

- (1) The Paris Agreement, adopted in December 2015 under the United Nations Framework Convention on Climate Change (UNFCCC) entered into force in November 2016 (“the Paris Agreement”)³². Its Parties have agreed to hold the increase in the global average temperature well below 2 °C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1,5 °C above pre-industrial levels.
- (2) Tackling climate and environmental-related challenges and reaching the objectives of the Paris Agreement are at the core of the Communication on “The European Green Deal”, adopted by the Commission on 11 December 2019³³. The necessity and value of the European Green Deal have only grown in light of the very severe effects of the COVID-19 pandemic on the health and economic well-being of the Union's citizens, which have shown that our society and our economy need to improve their resilience to external shocks and act early to prevent or mitigate them. European citizens continue to express strong views that this applies in particular to climate change.
- (3) The Union undertook to reduce the Union's economy-wide net greenhouse gas emissions by at least 55% by 2030 below 1990 levels in the updated nationally determined reduction commitment submitted to the UNFCCC Secretariat on 17 December 2020³⁴.

³⁰ OJ C [...], [...], p. [...].

³¹ OJ C [...], [...], p. [...].

³² Paris Agreement (OJ L 282, 19.10.2016, p. 4).

³³ COM(2019)640 final.

³⁴

https://www4.unfccc.int/sites/ndcstaging/PublishedDocuments/European%20Union%20First/EU_NDC_Submission_December%202020.pdf

- (4) The Union has enshrined into legislation the target of economy-wide climate neutrality in Union law in Regulation (EU) [...] of the European Parliament and of the Council³⁵. That Regulation also establishes a binding Union domestic reduction commitment of net greenhouse gas emissions (emissions after deduction of removals) of at least 55% below 1990 levels by 2030.
- (5) All sectors of the economy need to contribute to achieving those emission reductions. Therefore, the ambition of the EU Emissions Trading System (EU ETS), established by Directive 2003/87/EC of the European Parliament and of the Council³⁶ to promote reductions of greenhouse gas emissions in a cost-effective and economically efficient manner, should be increased in a manner commensurate with this economy-wide net greenhouse gas emissions reduction target for 2030.
- (6) The EU ETS should incentivise production from installations that partly or fully reduce greenhouse gas emissions. Therefore, the description of some categories of activities in Annex I of Directive 2003/87/EC should be amended to ensure an equal treatment of installations in the concerned sectors. In addition, free allocation for the production of a product should be independent of the nature of the production process. It is therefore necessary to modify the definition of the products and of the processes and emissions covered for some benchmarks to ensure a level playing field for new and existing technologies. It is also necessary to decouple the update of the benchmark values for refineries and for hydrogen to reflect the increasing production of hydrogen outside the refineries sector.
- (7) Council Directive 96/61/EC of 24 September 1996³⁷ was repealed by Directive 2010/75/EU of the European Parliament and of the Council³⁸. The references to Directive 96/61/EC in Article 2 and Annex IV should be updated accordingly. Given the need for urgent economy-wide emission reductions, Member States should be able to act to reduce greenhouse gas emissions that are under the scope of the ETS through other policies than emission limits adopted pursuant to Directive 2010/75/EU.
- (8) The definition of electricity generators was used to determine the maximum amount of free allocation to industry in the period from 2013 to 2020, but led to different treatment of cogeneration power plants compared to industrial installations. In order to incentivise the use of high efficiency cogeneration and to ensure equal treatment of all installations receiving free allocation for heat production and district heating, all references to electricity generators in the Directive should be deleted. In addition, Commission Delegated Regulation (EU) 2019/331³⁹ specifies the eligibility of all industrial processes for free allocation. Therefore, the provisions on carbon capture

³⁵ Regulation (EU) 2021/... of the European Parliament and of the Council (OJ L [...], [...], p. [...]).

³⁶ Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a system for greenhouse gas emission allowance trading within the Union and amending Council Directive 96/61/EC (OJ L 275, 25.10.2003, p. 32).

³⁷ OJ L 257, 10.10.1996, p. 26–40.

³⁸ [Directive 2010/75/EU of the European Parliament and of the Council of 24 November 2010 on industrial emissions \(integrated pollution prevention and control\) OJ L 334, 17.12.2010, p. 17–119.](#)

³⁹ Commission Delegated Regulation (EU) 2019/331 of 19 December 2018 determining transitional Union-wide rules for harmonised free allocation of emission allowances pursuant to Article 10a of Directive 2003/87/EC of the European Parliament and of the Council (C/2018/8664) (OJ L 59, 27.2.2019, p. 8–69).

and storage in Article 10a(3) of Directive 2003/87/EC are also no longer needed and can be deleted.

- (9) Greenhouse gases that are not directly released into the atmosphere should be considered emissions under EU ETS and allowances should be surrendered for those emissions unless they are stored in a storage site permitted under Directive 2009/31/EC of the European Parliament and of the Council⁴⁰, or they are permanently chemically bound in a product so that they do not enter the atmosphere under normal use. The Commission should be empowered to adopt implementing acts specifying the conditions where greenhouse gases are to be considered as permanently chemically bound in a product so that they do not enter the atmosphere under normal use, including obtaining a carbon removal certificate where appropriate in view of legislative developments on the regulatory framework for the certification of carbon removals.
- (10) International maritime transport activity, consisting of voyages between ports under the jurisdiction of two different Member States or between a port under the jurisdiction of a Member State and a port outside the jurisdiction of any Member State, has been the only means of transportation not included in the Union's past commitments to reduce greenhouse gas emissions. Emissions from fuel sold in the EU for journeys that depart in one Member State and arrive in a different Member State or a third country have grown by around 36% since 1990. Those emissions represent close to 90% of all EU navigation emissions as emissions from fuel sold in the EU for journeys departing and arriving in the same Member State have been reduced by 26% since 1990. In a business-as-usual scenario, emissions from international maritime transport activities are projected to grow by around 14% between 2015 and 2030 and 34% between 2015 and 2050. If the climate change impact of maritime transport activities grows as projected, it would significantly undermine reductions made by other sectors to combat climate change.
- (11) In 2013, the Commission adopted a strategy for progressively integrating maritime emissions into the Union's policy for reducing greenhouse gas emissions. As a first step of this stepwise approach, the Union established a system to monitor, report and verify emissions from maritime transport in Regulation (EU) 2015/757 of the European Parliament and of the Council⁴¹, to be followed by the definition of reduction targets for the maritime sector and the application of a market based measure. In line with the commitment of the co-legislators expressed in Directive (EU) 2018/410 of the European Parliament and of the Council⁴², action from the International Maritime Organization (IMO) or the Union should start from 2023, including preparatory work on adoption and implementation and due consideration being given by all stakeholders.

⁴⁰ Directive 2009/31/EC of the European Parliament and of the Council of 23 April 2009 on the geological storage of carbon dioxide and amending Council Directive 85/337/EEC, European Parliament and Council Directives 2000/60/EC, 2001/80/EC, 2004/35/EC, 2006/12/EC, 2008/1/EC and Regulation (EC) No 1013/2006 (OJ L 140, 5.6.2009, p. 114–135).

⁴¹ Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport, and amending Directive 2009/16/EC (OJ L 123, 19.5.2015, p. 55–76).

⁴² Directive (EU) 2018/410 of the European Parliament and of the Council of 14 March 2018 amending Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments, and Decision (EU) 2015/1814 (OJ L 76, 19.3.2018, p. 3–2).

- (12) Pursuant to Directive (EU) 2018/410, the Commission should report to the European Parliament and to the Council on the progress achieved in the IMO towards an ambitious emission reduction objective, and on accompanying measures to ensure that the maritime transport sector duly contributes to the efforts needed to achieve the objectives agreed under the Paris Agreement. Efforts to limit global maritime emissions through the IMO are under way and should be encouraged. However, while the recent progress achieved through the IMO is welcome, these measures will not be sufficient to achieve the objectives of the Paris Agreement.
- (13) In the European Green Deal⁴³, the Commission stated its intention to take additional measures to address greenhouse gas emissions from the maritime transport sector through a basket of measures to enable the Union to reach its emissions reduction targets. In this context, the amendment of Directive 2003/87/EC to include the maritime transport sector in the EU ETS is necessary to ensure this sector contributes to the increased EU climate objectives and the objectives of the Paris Agreement. The extension of the EU ETS to the maritime transport sector should include emissions from ships performing voyages arriving at a port under the jurisdiction of a Member State from a port outside the jurisdiction of a Member State, emissions from ships performing voyages arriving at a port under the jurisdiction of a Member State from a port under the jurisdiction of a Member State, and emissions at berth in a port under the jurisdiction of a Member State. To ensure a smooth inclusion of the sector in the EU ETS, the surrendering of allowances by shipping companies is gradually increased with respect to verified emissions reported for the period 2023 to 2025. To protect the environmental integrity of the system, to the extent fewer allowances are surrendered in respect of verified emissions for maritime transport during these years, once the difference between verified emissions and allowances surrendered has been established each year, a corresponding amount of allowances should be cancelled. As from 2026, shipping companies should surrender allowances for an amount equal to all of their verified emissions reported in the preceding year.
- (14) The provisions of Directive 2003/87/EC as regards maritime transport activities should be kept under review in light of international developments and efforts undertaken to achieve the objectives of the Paris Agreement, including the second global stocktake in 2028, and subsequent global stocktakes every five years thereafter, intended to inform successive NDCs. In particular, the Commission should report no later than by 30 September 2028 to the European Parliament and to the Council on progress in the IMO negotiations concerning a global market-based measure. In its report, the Commission should analyse the IMO instruments and, assess, as relevant, how to implement those instruments in Union law through a revision of Directive 2003/87/EC. In its report, the Commission should include proposals as appropriate.
- (15) The Commission should review the functioning of Directive 2003/87/EC in relation to maritime transport activities in the light of experience of its application and should then propose measures to ensure its effectiveness.
- (16) In order to reduce the administrative burden on shipping companies, one Member State should be responsible for each shipping company. The Commission should publish an initial list of shipping companies that performed a maritime activity falling within the scope of the EU ETS, which specifies the administering authority in respect of each shipping company. The list ought to be updated at least every two years to

⁴³ COM(2019)640 final.

reattribute shipping companies to another administering authority as relevant. For shipping companies registered in a Member State, the administering authority should be that Member State. For shipping companies registered in a third country, the administering authority should be the Member State in which the shipping company had the greatest estimated port calls from voyages falling within the scope of Directive 2003/87/EC in the last two monitoring years. For shipping companies registered in a third country and which did not perform any voyage falling within the scope of this Directive in the last two monitoring years, the administering authority should be the Member State from where the shipping company had terminated its first voyage falling within the scope of this Directive. The Commission should publish and update on a biennial basis a list of shipping companies falling within the scope of this Directive specifying the administering authority for each shipping company. In order to ensure equal treatment of shipping companies, Member States should follow harmonised rules for the administration of shipping companies for which they have responsibility, in accordance with specific guidelines to be developed by the Commission.

- (17) Member States should ensure that the shipping companies that they administer comply with the requirements of Directive 2003/87/EC. In the event that a shipping company fails to comply with those requirements and any enforcement measures taken by the administering authority have failed to ensure compliance, Member States should act in solidarity. As a last resort measure, the administering Member State should be able to decide on the imposition of an entry ban at Union level of the ships under the responsibility of the shipping company concerned.
- (18) Directive 2003/87/EC should ensure the monitoring, reporting and verification of emissions, fuel consumption and energy efficiency of ships performing voyages falling within the scope of Directive 2003/87/EC. Therefore, the rules laid down in Regulation (EU) 2015/757, as amended by Regulation (EU) [--]⁴⁴ should be incorporated into the monitoring, reporting and verification system of the EU ETS. That Regulation should be repealed with the entry into force of this Directive. In addition, the Commission should be empowered to adopt delegated acts to amend the current rules to ensure the reporting of emissions aggregated at shipping company level, amend the definition of shipping companies, amend the monitoring and reporting obligations in case of changes of companies, change the definition of the reporting parameters, including the reporting period, update the list of default emission factors, define harmonised rules for the approval of monitoring plans by administering authorities and amend the conditions for the accreditation and withdrawal of accreditation, for mutual recognition and peer evaluation of accreditation bodies. To ensure a smooth transition to the new legal framework for the monitoring, reporting and verification of emissions from maritime transport, the Commission delegated and implementing acts adopted pursuant to Regulation (EU) 2015/757 should remain in force until they are repealed by delegated acts adopted in accordance with Directive 2003/87/EC.
- (19) Based on experience from similar tasks related to environmental protection, the European Maritime Safety Agency (EMSA) or another relevant organisation should,

⁴⁴ Regulation (EU) [--] of the European Parliament and of the Council amending Regulation (EU) 2015/757 in order to take appropriate account of the global data collection system for ship fuel oil consumption data.

as appropriate and in accordance with its mandate, assist the Commission and the administering authorities in respect of the implementation of this Directive.

- (20) Regulation (EU) 2017/2392 of the European Parliament and of the Council⁴⁵ amended Article 12(3) of Directive 2003/87/EC to allow all operators to use all allowances that are issued. Permitting provisions in Article 6(2)(e) should be aligned with this amendment.
- (21) Achieving the Union's emissions reduction target for 2030 will require a reduction in the emissions of the sectors covered by the EU ETS of [XX%] compared to 2005. The Union-wide quantity of allowances of the EU ETS needs to be reduced to create the necessary long-term carbon price signal and drive for this degree of decarbonisation. To this end, the linear reduction factor should be increased, also taking into account emissions from maritime transport. The latter should be derived from quantity of emissions from maritime transport activities reported in accordance with the Regulation (EU) 2015/757 for 2018 and 2019 in the Union, adjusted by the linear reduction factor from 2021.
- (22) Bearing in mind that this proposal amends Directive 2003/87/EC in respect of a period of implementation that has already entered into force on 1 January 2021, for predictability, environmental effectiveness and simplicity, the steeper linear reduction pathway of the EU ETS should be a straight line from 2021 to 2030, such as to achieve emission reductions in the EU ETS of [XX]% by 2030, as the appropriate intermediate step towards economy-wide climate neutrality in 2050. As the increased linear reduction factor can only apply from the year following entry into force of this Directive, a one-off reduction of the quantity of allowances will reduce the total quantity of allowances so that it is in line with this level of annual reduction having been made from 2021.
- (23) Achieving the increased climate ambition will require channelling as many resources as possible to the climate transition. As a result, all auction revenues should be used for climate related purposes. Further, to address the distributional and social effects of the transition, an additional amount of 2% of the Union-wide quantity of allowances from [year entry into force of the Directive] to 2030 should be used to fund the energy transition of the Member States with a gross domestic product (GDP) per capita below [--] of the EU average in 2016-2018, through the Modernisation Fund.
- (24) Further incentives to reduce greenhouse gas emissions by using cost-efficient techniques should be provided. To that end, the free allocation of emission allowances to stationary installations from 2026 onwards should be conditional on investments in techniques to increase energy efficiency and reduce emissions. The relevant delegated acts should be adjusted accordingly.
- (25) The Carbon Border Adjustment Mechanism (CBAM) should be an alternative to free allocation to address carbon leakage risks. To the extent that sectors and subsectors are covered by that measure they should not receive free allocation. The relevant delegated acts on free allocation should be adjusted accordingly for the sectors and subsectors covered by the CBAM.

⁴⁵ [Regulation \(EU\) 2017/2392 of the European Parliament and of the Council of 13 December 2017 amending Directive 2003/87/EC to continue current limitations of scope for aviation activities and to prepare to implement a global market-based measure from 2021 \(OJ L 350, 29.12.2017, p. 7–14\).](#)

- (26) In order to better reflect technological progress and adjust the corresponding benchmark values to the relevant period of allocation while ensuring emission reduction incentives and properly rewarding innovation, the maximum adjustment of the benchmark values should be increased from 1,6% to 2,5% per year. For the period from 2026 to 2030, the benchmark values should thus be adjusted within the range of 4% to 50% compared to the value applicable in the period from 2013 to 2020.
- (27) The scope of the Innovation Fund should be extended to support innovation in low-carbon technologies and processes that concern the consumption of fuels in the sectors of buildings and road transport. In addition, investments to decarbonise the maritime transport sector should be supported by the Innovation Fund, which includes investments in sustainable alternative fuels, such as hydrogen and ammonia, that are produced from renewables, and of zero-emission propulsion technologies like wind technologies.
- (28) Pursuant to Commission Regulation (EU) No 389/2013⁴⁶, when aircraft operators no longer operate flights covered by the EU ETS their accounts are set to excluded status, and processes may no longer be initiated from those accounts. To preserve the environmental integrity of the system, allowances which are not issued to aircraft operators due to their closure should be used to cover any shortfall in surrenders by those operators, and any leftover allowances should be used to accelerate action to tackle climate change by being placed in the Innovation Fund.
- (29) Carbon Contracts for Difference (CCDs) are an important element to trigger emission reductions in industry. Project-based CCDs offer the opportunity to guarantee investors in innovative climate-friendly technologies a price that rewards CO₂ emission reductions above those induced by the current price levels in the EU ETS. The range of measures that the Innovation Fund can support should be extended to provide support to projects in the form of price-competitive tendering support such as carbon contracts for difference, and the Commission should be empowered to adopt delegated acts on the precise rules for this type of support.
- (30) Where an installation's activity is temporarily suspended, free allocation is adjusted to the activity levels which are mandatorily reported annually. In addition, competent authorities can suspend the issuance of emission allowances to installations that have suspended operations as long as there is no evidence that they will resume operations. Therefore, operators do no longer need to demonstrate to the competent authority that their installation will resume production within a specified and reasonable time in case of a temporary suspension of the activities.
- (31) Corrections of free allocation granted to stationary installations pursuant to Article 11(2) of Directive 2003/87/EC can require granting additional free allowances or transferring back surplus allowances. The allowances set aside for new entrants under Article 10a(7) of Directive 2003/87/EC should be used for those purposes.
- (32) The scope of the Modernisation Fund should be aligned with the most recent climate objectives of the Union by requiring that investments are consistent with the objectives of the European Green Deal and the Climate Law, and eliminating the support to any investments related to fossil fuels. In addition, the percentage of the Modernisation

⁴⁶ [Article 10 of Commission Regulation \(EU\) No 389/2013 of 2 May 2013 establishing a Union Registry pursuant to Directive 2003/87/EC of the European Parliament and of the Council, Decisions No 280/2004/EC and No 406/2009/EC of the European Parliament and of the Council and repealing Commission Regulations \(EU\) No 920/2010 and No 1193/2011 \(OJ L 122, 3.5.2013, p. 1–59\).](#)

Fund that needs to be devoted to priority investments should be increased to 80%, energy efficiency should be targeted as a priority area at the demand side, including industry explicitly as eligible sector, and support of households to address energy poverty should be included within the scope of the priority investments.

- (33) Implementing Regulation (EU) 2018/2066⁴⁷ lays down rules on the monitoring of emissions from biomass which are consistent with the rules on the use of biomass laid down in the legislation on renewable energy of the Union. As the legislation becomes more elaborate on the sustainability criteria for biomass with the latest rules established in Directive (EU) 2018/2001 of the European Parliament and of the Council⁴⁸, the empowerment in Article 14 should be explicitly extended to the adoption by the Commission of implementing acts laying down the necessary adjustments for the application in the EU ETS of sustainability criteria for biomass. In addition, the Commission should also be empowered to adopt implementing acts to specify how to account the storage of emissions from mixes of zero-rated biomass and biomass that is not zero-rated sources.
- (34) As carbon dioxide is also expected to be transported by means other than pipelines, such as by ship and by truck, the current coverage in Annex I for transport of greenhouse gases for the purpose of storage should be extended to all means of transport for equal treatment irrespective of if they are covered by the EU ETS. Where the emissions from the transport are also covered by another activity under this Directive, the emissions should be accounted under that other activity to prevent double counting.
- (35) The exclusion of installations using exclusively biomass from the ETS has led to situations where installations combusting a high share of biomass have obtained windfall profits by receiving free allowances greatly exceeding actual emissions. Therefore, a threshold value for zero-rated biomass combustion should be introduced above which installations are excluded from the ETS. The threshold value of 95% follows the uncertainty rule of Commission Delegated Regulation (EU) 2019/331⁴⁹.
- (36) The Communication of the Commission on Stepping up Europe's 2030 climate ambition⁵⁰, underlined the particular challenge to reduce the emissions in the sectors of road transport and buildings. Therefore, the Commission announced that a further expansion of emissions trading could include emissions from road transport and buildings. Emissions trading for these two new sectors would be established through separate but adjacent emissions trading. This would avoid any disturbance of the well-functioning emissions trading in the sectors of stationary installations and aviation. Previous experience has shown that the development of the new market requires setting up an efficient monitoring, reporting and verification system. In view of ensuring synergies and coherence with the existing Union infrastructure for EU

⁴⁷ Commission Implementing Regulation (EU) 2018/2066 of 19 December 2018 on the monitoring and reporting of greenhouse gas emissions pursuant to Directive 2003/87/EC of the European Parliament and of the Council and amending Commission Regulation (EU) No 601/2012 (C/2018/8588) (OJ L 334, 31.12.2018).

⁴⁸ Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources (OJ L 328, 21.12.2018, p. 82–209).

⁴⁹ Commission Delegated Regulation (EU) 2019/331 of 19 December 2018 determining transitional Union-wide rules for harmonised free allocation of emission allowances pursuant to Article 10a of Directive 2003/87/EC of the European Parliament and of the Council (C/2018/8664) (OJ L 59, 27.2.2019, p. 8–69).

⁵⁰ COM(2020)562 final.

emissions trading covering the emissions from stationary installations and aviation, it is appropriate that emissions trading for the two new sectors is set up via an amendment to Directive 2003/87/EC.

- (37) In order to establish the necessary implementation framework and to provide a reasonable timeframe for reaching the 2030 target, emissions trading in the two new sectors should start in 2025. During the first year the regulated entities will be required to hold a greenhouse gas emissions permit and to report their emissions for years 2024 and 2025. The issuance of allowances and compliance obligations for these entities will be applicable as from 2026. This sequencing will allow starting emissions trading in the sectors in an orderly and efficient manner.
- (38) Due to a substantially large number of small emitters in the sectors of buildings and road transport, it is not possible to establish the point of regulation at the level of entities directly emitting greenhouse gases, as it is the case for stationary installations and aviation. Therefore, for reasons of technical feasibility and administrative efficiency, it is more appropriate to establish the point of regulation further upstream in the supply chain. The act that triggers the compliance obligation under the new emissions trading should be the release for consumption of fuels which are used for combustion in the sectors of buildings and road transport, including for combustion in road transport of greenhouse gases for geological storage. To avoid double coverage, the release for consumption of fuels which are used in other activities under Annex I of Directive 2003/87/EC would not be covered.
- (39) The regulated entities in the two new sectors and the point of regulation should be defined in line with the system of excise duty of Council Directive (EU) 2020/262⁵¹, with the necessary adaptations, as this Directive has already set a robust control system for all quantities of fuels released for consumption for the purposes of paying excise duties. End-users of fuels in these sectors would not be subject to obligations under Directive 2003/87/EC.
- (40) The regulated entities falling within the scope of the emissions trading in the sectors of buildings and road transport must be subject to similar greenhouse gas emissions permit requirements as the operators of stationary installations. It is necessary to establish rules on the permit applications, the conditions for issuance and content, the review, and any changes related to the regulated entity. In order for the new system to start in an orderly manner, Member States must ensure that the regulated entities falling in the scope of the new emissions trading have a valid permit as of the start of the system in 2025.
- (41) The total quantity of allowances for the new emissions trading should follow a linear trajectory to reach the 2030 emission reduction target taking into account the cost-efficient contribution of buildings and road transport of XX% emission reductions by 2030 compared to 2005. The total quantity of allowances would be established for the first time in 2026, to follow a trajectory starting in 2024 from the value of the 2024 emissions limits (1 109 755 000 CO₂t), calculated as under Article 4(2) of Regulation (EU) 2018/842 on the basis of the reference emissions for these sectors for the years from 2016 to 2018. Accordingly, the linear reduction factor should be set at XX%. From 2028, the total quantity of allowances would be set on the basis of the average reported emissions for the years 2024, 2025 and 2026, and should decrease by the

⁵¹ Council Directive (EU) 2020/262 of 19 December 2019 laying down the general arrangements for excise duty (OJ L 058 27.2.2020, p. 4).

same absolute annual reduction as set from 2024, which corresponds to a XX% linear reduction factor compared to the comparable 2025 value of the above defined trajectory. If these emissions are significantly higher than this trajectory value and if this divergence is not due to small-scale differences in emission measurement methodologies, the linear reduction factor should be adjusted to reach the required emissions reduction in 2030.

- (42) The auctioning of allowances is the simplest and the most economically efficient method for allocating emission allowances, which also avoids windfall profits. Both the buildings and road transport sectors are under relatively small or non-existent competitive pressure from outside the Union and are not exposed to a risk of carbon leakage. Therefore, allowances for buildings and road transport should only be allocated via auctioning without any free allocation.
- (43) In order to ensure a smooth start of emissions trading in the new sectors and taking into account the need of the regulated entities to hedge or buy ahead allowances to mitigate their price and liquidity risk, a higher amount of allowances should be auctioned early on. In 2026, the auction volumes will therefore be [20%] higher than the total quantity of allowances for 2026. This amount would be sufficient to provide liquidity, both if emissions decrease in line with reduction needs, and in the event emission reductions only materialise progressively. The detailed rules for this front-loading of auction volume are to be established in a delegated act related to auctioning, adopted pursuant to Article 10(4) of Directive 2003/87/EC.
- (44) The distribution rules on auction shares are highly relevant for any auction revenues that would accrue to the Member States, especially in view of the need to strengthen the ability of the Member States to address the social impacts of a carbon price signal in the buildings and road transport sectors. Notwithstanding the fact that the two sectors have very different characteristics, it is appropriate to set a common distribution rule similar to the one applicable to stationary installations. The main part of allowances will be distributed among all Member States on the basis of the average distribution of the emissions in the covered sectors during the period from 2016 to 2018.
- (45) The conditions for the use of auction revenues under the new system should address challenges associated with the carbon price in the sectors covered. Because of the potentially significant social impact of the carbon price, Member States should be required to spend all of the auction revenues on the climate and energy-related purposes already specified for the existing emission trading, but also for measures added specifically to address related concerns for the new sectors of road transport and buildings. In addition, more targeted measures should be identified, whereby the Member States are required to use at least 50% of their auction revenues for low-income households.
- (46) Innovation and development of new low-carbon technologies in the sectors of buildings and road transport are crucial for ensuring the cost-efficient contribution of these sectors to the expected emission reductions. Therefore, 150 million allowances from emissions trading in the buildings and road transport sectors should be made available to the Innovation Fund to stimulate the cost-efficient emission reductions.
- (47) Regulated entities covered by the new emissions trading should surrender allowances for their verified emissions corresponding to the quantities of fuels they have released for consumption. They should surrender allowances for the first time for their verified emissions in 2026. In order to minimize administrative burden, a number of rules

applicable to the existing emissions trading system for stationary installations and aviation should be made applicable to emissions trading for buildings and road transport, with the necessary adaptations. This includes in particular rules on transfer, surrender and cancellation of allowances, as well as the rules on the validity of allowances, penalties, competent authorities and reporting obligations of Member States.

- (48) For emissions trading in the new sectors to be effective, it should be possible to monitor emissions with high certainty and at reasonable cost. Emissions will be attributed to regulated entities on the basis of fuel quantities released for consumption and combined with an emission factor. Regulated entities should be able to reliably and accurately identify and differentiate the sectors in which the fuels are released for consumption, as well as the final users of the fuels, in order to avoid undesirable effects, such as double burden. To have sufficient data to establish the total number of allowances for the period from 2028 to 2030, the regulated entities holding a permit at the start of the system in 2025 should report their associated historical emissions of 2024.
- (49) It is appropriate to introduce measures to address the potential risk of excessive price increases, which if particularly high at the start of the new emissions trading may undermine the readiness of households and individuals to invest in reducing their greenhouse gas emissions in addition to the safeguards provided by the Market Stability Reserve. While the market will continue to determine the carbon price, safeguard measures will be triggered by rules-based automatism, whereby allowances will be released from the Market Stability Reserve only if concrete triggering conditions based on the increase in the average allowance price are met. This additional mechanism should also be more reactive, in order to address excessive volatility due to factors other than changed market fundamentals. The measures should be adapted to different levels of excessive price increase, which will result in different degrees of the intervention. The triggering conditions would be monitored by the Commission and the measures would be adopted by an implementing act following a vote by the Climate Change Committee established in accordance with Article 44(1)(a) of Regulation (EU) 2018/1999 of the European Parliament and the Council⁵².
- (50) The application of emissions trading in the two new sectors should be monitored by the Commission and, if necessary, a review would be proposed to the Parliament and the Council to improve the effectiveness, administration and practical application of emissions trading for buildings and road transport on the basis of acquired knowledge. The first report of the Commission should be due on 1 January 2028.
- (51) A well-functioning, reformed EU ETS with an instrument to stabilise the market is a key means for the Union to reach its agreed target for 2030 and the commitments under the Paris Agreement. To address the imbalance between supply and demand of allowances in the market, the Market Stability Reserve was established under Decision (EU) 2015/1814 in 2018 and became operational in 2019. Article 3 of that Decision provides that the reserve must be reviewed three years after it became operational.

⁵² Regulation (EU) 2018/1999 of the European Parliament and of the Council of 11 December 2018 on the Governance of the Energy Union and Climate Action, amending Regulations (EC) No 663/2009 and (EC) No 715/2009 of the European Parliament and of the Council, Directives 94/22/EC, 98/70/EC, 2009/31/EC, 2009/73/EC, 2010/31/EU, 2012/27/EU and 2013/30/EU of the European Parliament and of the Council, Council Directives 2009/119/EC and (EU) 2015/652 and repealing Regulation (EU) No 525/2013 of the European Parliament and of the Council (OJ L 328, 21.12.2018, p. 1–77).

- (52) Considering the need to deliver a stronger investment signal to reduce emissions in a cost-efficient manner and with a view to strengthening the EU ETS, Decision (EU) 2015/1814 should be amended so as to increase the percentage rate for determining the number of allowances to be placed each year in the reserve. In addition, for lower levels of the total number of allowances in circulation (TNAC), the intake should be equal to the difference between the TNAC and the threshold that determines the intake of allowances. This would prevent the considerable uncertainty in the auction volumes that results when the TNAC is close to the threshold, but ensure that the surplus reaches the volume bandwidth within which the carbon market is deemed to operate in a balanced manner.
- (53) Furthermore, in order to ensure that the level of allowances that remains in the reserve after the invalidation is predictable, the invalidation of allowances in the reserve should no longer depend on the level of auction volumes of the previous year. The number of allowances in the reserve therefore should be fixed at a level of 400 million allowances, which corresponds to the lower threshold for the value of the TNAC.
- (54) The analysis of the impact assessment has also shown that net demand from aviation should be included in the total number of allowances in circulation. In addition, since aviation allowances can be used in the same way as general allowances, including aviation in the reserve would make it a more accurate, and thus a better tool to ensure the stability of the market. The calculation of the total number of allowances in circulation should include aviation emissions and allowances issued in respect of aviation as of the year following the adoption of this proposal.
- (55) To clarify the calculation of the TNAC, Decision (EU) 2015/1814 should specify that only allowances issued and not put in reserve are included in the supply of allowances. Moreover, the formula should no longer subtract the number of allowances in the reserve from the supply of allowances. This change would have no material impact on the result of the calculation of the TNAC, including on the previous calculations of the indicator or on the reserve.
- (56) In order to mitigate the risk of supply and demand imbalances associated with the start of emission trading for buildings and road transport sectors, as well as to render it more resistant to market shocks, the rule-based mechanism of the reserve established under Decision (EU) 2015/1814 should be applied to the new sectors. For the reserve to be operational from the start of the system, it should be established with an initial endowment of 600 million allowances for emissions trading in the road transport and buildings sectors. The initial lower and upper thresholds, which trigger the release or intake of allowances from the reserve, should be subject to a general review clause. Other elements such as the publication of the total number of allowances in circulation or the quantity of allowances released or placed in the reserve should follow the rules of the reserve for other sectors.
- (57) In order to ensure uniform conditions for the implementation of Articles 12(3b) and 14(1) of Directive 2003/87/EC, implementing powers should be conferred on the Commission. Those necessary implementing powers should be exercised in

accordance with Regulation (EU) No 182/2011 of the European Parliament and of the Council⁵³.

- (58) In order to adopt non-legislative acts of general application to supplement or amend certain non-essential elements of a legislative act, the power to adopt acts in accordance with Article 290 of the Treaty on the Functioning of the European Union should be delegated to the Commission in respect of Articles 3i, 3j and 10a(8) of Directive 2003/87/EC. Moreover, to ensure synergies with the existing regulatory framework, the delegation in Articles 10(4), 10a(8), 14(1) and 15 of Directive 2003/87/EC should be extended for the sectors of road transport and buildings. It is of particular importance that the Commission carry out appropriate consultations during its preparatory work, including at expert level, and that those consultations be conducted in accordance with the principles laid down in the Interinstitutional Agreement on Better Law-Making of 13 April 2016. In particular, to ensure equal participation in the preparation of delegated acts, the European Parliament and the Council receive all documents at the same time as Member States' experts, and their experts systematically have access to meetings of Commission expert groups dealing with the preparation of delegated acts.
- (59) In accordance with the Joint Political Declaration of 28 September 2011 of Member States and the Commission on explanatory documents⁵⁴, Member States have undertaken to accompany, in justified cases, the notification of their transposition measures with one or more documents explaining the relationship between the components of a directive and the corresponding parts of national transposition instruments. With regard to this Directive, the legislator considers the transmission of such documents to be justified.
- (60) Directive 2003/87/EC and Decision (EU) 2015/1814 should therefore be amended accordingly,

HAVE ADOPTED THIS DIRECTIVE:

Article 1

Amendments to Directive 2003/87/EC

Directive 2003/87/EC is amended as follows:

(1) **Article 2 is amended as follows:**

(a) **Paragraphs 1 and 2 are replaced by the following:**

“1. This Directive shall apply to the activities listed in Annexes I and III, and to the greenhouse gases listed in Annex II. Where an installation that is included in the scope of the ETS due to the operation of combustion units with a total rated thermal input exceeding 20 MW changes its production processes to reduce its greenhouse gas emissions and no longer meets this threshold, it shall remain in the scope of the ETS until the end of the relevant five year period referred to in Article 11(1) following the change to its production process.”;

⁵³ Regulation (EU) No 182/2011 of 16 February 2011 laying down the rules and general principles concerning mechanisms for control by the Member States of the Commission's exercise of implementing powers (OJ L 55, 28.02.2011, p. 13).

⁵⁴ OJ C 369, 17.12.2011, p. 14.

2. This Directive shall apply without prejudice to any requirements pursuant to Directive 2010/75/EU of the European Parliament and of the Council(*).

(*) Directive 2010/75/EU of the European Parliament and of the Council of 24 November 2010 on industrial emissions (integrated pollution prevention and control) OJ L 334, 17.12.2010, p. 17–119.”.

(2) **Article 3 is amended as follows:**

(a) **point (b) is replaced by the following:**

“(b) ‘emissions’ means the release of greenhouse gases from sources in an installation or the release from an aircraft performing an aviation activity listed in Annex I or from ships performing a maritime transport activity listed in Annex I of the gases specified in respect of that activity, or the release of greenhouse gases corresponding to the activity referred to in Annex III;”.

(b) **point (d) is replaced by the following:**

“(d) ‘greenhouse gas emissions permit’ means the permit issued in accordance with Articles 5, 6 and 30b;”;

(c) **point (u) is deleted;**

(d) **point (v) is inserted:**

“(u) ‘shipping company’ means the shipowner or any other organisation or person, such as the manager or the bareboat charterer, that has assumed the responsibility for the operation of the ship from the shipowner and that, on assuming such responsibility, has agreed to take over all the duties and responsibilities imposed by the International Management Code for the Safe Operation of Ships and for Pollution Prevention, set out in Annex I to Regulation (EC) No 336/2006 of the European Parliament and of the Council(*);

(*) Regulation (EC) No 336/2006 of the European Parliament and of the Council of 15 February 2006 on the implementation of the International Safety Management Code within the Community and repealing Council Regulation (EC) No 3051/95 (OJ L 64, 4.3.2006, p. 1).”;

(e) **point (w) is inserted:**

“(w) ‘administering authority in respect of a shipping company’ means the authority responsible for administering the EU ETS in respect of a shipping company in accordance with Article 3k;”;

(f) **point (x) is inserted:**

“(x) ‘regulated entity’ for the purposes of Chapter IVa shall mean any natural or legal person, except for any final consumer of the fuels, that engages in the activity referred to in Annex III and that falls in one of the following categories:

- a) where the fuel passes through a tax warehouse in the meaning of Article 3(11) of Council Directive (EU) 2020/262(*), the authorised warehouse keeper in the meaning of Article 3(1) of that Directive, liable to pay the

excise duty which has become chargeable pursuant to Article 7 of that Directive, or

- b) if point (a) is not applicable, any other person liable to pay the excise duty which has become chargeable pursuant to Article 7 of Council Directive (EU) 2020/262 in respect of the fuels covered by this Chapter, or
- c) if points (a) and (b) are not applicable, any person which has to be registered by the relevant national authorities of the Member State for the purpose of being liable to pay the excise duty, including any person exempt from paying the excise duty, as referred to in the fourth subparagraph of Article 21(5) of Council Directive 2003/96/EC, or
- d) if none of the above points is applicable, or if several persons are jointly and severally liable for payment of the same excise duty, any other relevant entity designated by a Member State in accordance with Article 30b.

(*) Council Directive (EU) 2020/262 of 19 December 2019 laying down the general arrangements for excise duty (OJ L 058 27.2.2020, p. 4).”;

(g) **point (y) is inserted:**

“(y) ‘fuel’ for the purposes of Chapter IVa shall mean any fuel listed in Table-A and Table-C of Annex I of Council Directive 2003/96/EC(*), as well as any other product offered for sale as motor fuel or heating fuel as specified in Article 2(3) of that Directive;”;

(*) Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity, OJ L 283 31.10.2003, p. 51.”;

(h) **point (z) is inserted:**

“(z) ‘release for consumption’ for the purposes of Chapter IVa shall mean the same as in Article 6 of Council Directive (EU) 2020/262.”.

(3) **the title of Chapter II is replaced by the following:**

“AVIATION AND MARITIME TRANSPORT”

(4) **Article 3a is replaced by the following:**

“Article 3a

Scope

Articles 3b to 3f shall apply to the allocation and issue of allowances in respect of the aviation activities listed in Annex I. Articles 3g to 3l shall apply in respect of the maritime transport activities listed in Annex I.”

(5) **Article 3f is replaced by the following:**

“Article 3f

Monitoring and reporting plans

The administering Member State shall ensure that each aircraft operator submits to the competent authority in that Member State a monitoring plan setting out measures to monitor and report emissions and tonne-kilometre data for the purpose of an application under Article 3e and that such plans are approved by the competent authority in accordance with the acts referred to in Article 14.”.

- (6) **Article 3g is replaced by the following:**

“Article 3g

Scope of application to maritime transport activities

1. The allocation of allowances and the application of surrender requirements in respect of maritime transport activities shall only apply in respect of emissions from ships performing voyages arriving at a port under the jurisdiction of a Member State and emissions from ships at berth in a port under the jurisdiction of a Member State.
2. Articles 9, 9a and 10 shall apply to maritime transport activities in the same manner as they apply to other activities covered by the EU ETS.”.

- (7) **The following Article 3h is inserted:**

“Article 3h

Phase-in of requirements for maritime transport

Shipping companies shall be liable to surrender allowances according to the following schedule:

- (a) 20% of verified emissions reported for 2023;
- (b) 45% of verified emissions reported for 2024;
- (c) 70% of verified emissions reported for 2025;
- (d) 100% of verified emissions reported for 2026 and each year thereafter.

To the extent that fewer allowances are surrendered compared to the verified emissions from maritime transport for the years 2023, 2024 and 2025, once the difference between verified emissions and allowances surrendered has been established in respect of each year, a corresponding quantity of allowances shall be cancelled rather than auctioned pursuant to Article 10.

- (8) **The following Article 3i is inserted:**

“Article 3i

Monitoring and reporting of emissions from maritime transport

1. Shipping companies shall determine their emissions in accordance with the delegated acts adopted pursuant to paragraph 2.
2. The Commission is empowered to adopt delegated acts in accordance with Article 23 to amend monitoring and reporting methods of emissions from maritime transport activities provided for in Regulation (EU) 2015/757 of the European Parliament and of the Council (*), Commission Implementing Regulation (EU) 2016/1927(**), Commission Implementing Regulation (EU) 2016/1928(***) and Commission Delegated Regulation (EU) 2016/2071(****). The Commission is empowered to adopt those delegated acts in accordance with Article 23 to set the rules for monitoring and reporting at company level, amend the definition of shipping

companies, amend the monitoring and reporting obligations in case of changes of companies, change the definition of the reporting parameters, including the reporting period, update the list of default emission factors and define harmonised rules for the approval of monitoring plans by administering authorities.

3. In respect of emissions from maritime transport activities listed in Annex I, shipping companies shall, for each ship under their responsibility, monitor and report the relevant parameters during a reporting period in line with those delegated acts.

(*) Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport, and amending Directive 2009/16/EC (OJ L 123, 19.5.2015, p. 55).

(**) Commission Implementing Regulation (EU) 2016/1927 of 4 November 2016 on templates for monitoring plans, emissions reports and documents of compliance pursuant to Regulation (EU) 2015/757 of the European Parliament and of the Council on monitoring, reporting and verification of carbon dioxide emissions from maritime transport (C/2016/6948) (OJ L 299, 5.11.2016, p. 1).

(***) Commission Implementing Regulation (EU) 2016/1928 of 4 November 2016 on determination of cargo carried for categories of ships other than passenger, ro-ro and container ships pursuant to Regulation (EU) 2015/757 of the European Parliament and of the Council on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport (C/2016/6951) (OJ L 299, 5.11.2016, p. 22).

(****) Commission Delegated Regulation (EU) 2016/2071 of 22 September 2016 amending Regulation (EU) 2015/757 of the European Parliament and of the Council as regards the methods for monitoring carbon dioxide emissions and the rules for monitoring other relevant information (C/2016/5900) (OJ L 320, 26.11.2016, p. 1).”.

(9) **The following Article 3j is inserted:**

“Article 3j

Verification and accreditation of emissions from maritime transport

Member States shall ensure that the reports submitted by shipping companies pursuant to Article 3i are verified in accordance with the criteria set out in the delegated acts adopted pursuant to the second paragraph, and that the competent authority is informed thereof.

The Commission is empowered to adopt delegated acts in accordance with Article 23 to amend reporting and verification methods of emissions from maritime transport activities provided for in Regulation (EU) 2015/757 and Commission Delegated Regulation (EU) 2016/2072(*). The Commission is empowered to adopt those delegated acts in accordance with Article 23 to amend the conditions for the accreditation and withdrawal of accreditation, for mutual recognition and peer evaluation of accreditation bodies.

(*) Commission Delegated Regulation (EU) 2016/2072 of 22 September 2016 on the verification activities and accreditation of verifiers pursuant to Regulation (EU) 2015/757 of the European Parliament and of the Council on the monitoring, reporting

and verification of carbon dioxide emissions from maritime transport (C/2016/5904) (OJ L 320, 26.11.2016, p. 5).”

(10) **The following Article 3k is inserted:**

“Article 3k

Administering authority in respect of a shipping company

1. The administering authority in respect of a shipping company shall be:

(a) in the case of a shipping company registered in a Member State, the Member State in which the shipping company is registered;

(b) in the case of a shipping company that is not registered in a Member State, the Member State with the greatest estimated number of port calls from voyages performed by that shipping company in the last two monitoring years and falling within the scope set out in Article 3g;

(c) in the case of a shipping company that is not registered in a Member State and that did not carry out any voyage falling within the scope set out in Article 3g in the preceding two monitoring years, the administering authority shall be the Member State from where the shipping company has terminated its first voyage falling within the scope set out in Article 3g.

Where appropriate, the responsible administering authority in respect of a shipping company shall be updated biennially.

2. Based on the best available information, the Commission shall:

(a) before 1 February 2024, publish a list of shipping companies which performed a maritime activity listed in Annex I that fell within the scope defined in Article 3g on or with effect from 1 January 2023, specifying the administering authority for each shipping company in accordance with paragraph 1; and

(b) at least every two years thereafter, update the list to reattribute shipping companies to another administering authority where appropriate or to include shipping companies which have subsequently performed a maritime activity listed in Annex I that fell within the scope defined in Article 3g.

3. The Commission may, in accordance with the examination procedure referred to in Article 22a(2), develop guidelines relating to the administration of shipping companies under this Directive by administering authorities.”.

(11) **The following Article 3l is inserted:**

“Article 3l

Reporting and review

1. The Commission shall consider possible amendments in relation to the adoption by the International Maritime Organisation of a global market-based measure to reduce greenhouse gas emissions from maritime transport. No later than 30 September 2028, the Commission shall present a report to the European Parliament and to the Council in which it shall examine any such measure. Where appropriate, the Commission may follow up to the report with a legislative proposal to the European Parliament and to the Council to amend this Directive as appropriate.

2. The Commission shall monitor the implementation of this Chapter and possible trends as regards companies seeking to avoid being bound by the requirements of this

Directive. If appropriate, the Commission shall propose measures to prevent such avoidance.”.

- (12) **Article 3h is replaced by the following:**

“Article 3m

Scope

The provisions of this Chapter shall apply to greenhouse gas emissions permits and the allocation and issue of allowances in respect of activities listed in Annex I other than aviation and maritime transport activities.”

- (13) **In Article 6(2), point (e) is replaced by the following:**

“(e) an obligation to surrender allowances equal to the total emissions of the installation in each calendar year, as verified in accordance with Article 15, within four months following the end of that year.”.

- (14) **In Article 9, the following paragraph is added:**

“In [the year following entry into force of this amendment], the Union-wide quantity of allowances shall be decreased by [-- million allowances]. In the same year, the Union-wide quantity of allowances shall be increased by [--] million allowances for maritime transport. Starting in [the year following entry into force of this amendment], the linear factor shall be [--]%. The Commission shall publish the Union-wide quantity of allowances within 3 months of [date of entry into force of the amendment to be inserted].”.

- (15) **Article 10 is amended as follows:**

- (a) **In paragraph 1, the third subparagraph is replaced by the following:**

2 % of the total quantity of allowances between 2021 and 2030 shall be auctioned to establish a fund to improve energy efficiency and modernise the energy systems of certain Member States (‘the beneficiary Member States’) as set out in Article 10d (‘the Modernisation Fund’). The beneficiary Member States for this amount of allowances shall be the Member States with a GDP per capita at market prices below 60 % of the Union average in 2013. The funds corresponding to this quantity of allowances will be distributed in accordance with Part A of Annex IIb.

In addition, 2 % of the total quantity of allowances between [year following the entry into force of the Directive] and 2030 shall be auctioned for the Modernisation Fund. The beneficiary Member States for this amount of allowances shall be the Member States with a GDP per capita at market prices below [--] of the Union average of the period 2016 to 2018. The funds corresponding to this quantity of allowances will be distributed in accordance with Part B of Annex IIb.

- (b) **In paragraph 3, the first and second sentence are replaced by the following:**

“Member States shall use all the revenues generated from the auctioning of allowances referred to in paragraph 2 for one or more of the following:”.

- (16) **Article 10a is amended as follows:**

- (a) **in paragraph 1:**

- (i) **the following two subparagraphs are inserted after the second subparagraph:**

“In the case of installations covered by the obligation to conduct an energy audit under Article 8(4) of Directive 2012/27/EU of the European Parliament and of the Council(*), free allocation shall only be granted fully if the recommendations of the audit report are implemented, to the extent that the pay-back time for the relevant investments does not exceed five years and that the costs of those investments is proportionate. Otherwise, the amount of free allocation shall be reduced by 25%. The amount of free allocation shall not be reduced if an operator demonstrates that it has implemented other measures which lead to greenhouse gas emission reductions equivalent to those recommended by the audit report. The measures referred to in the first subparagraph shall be adjusted accordingly.

No free allocation shall be given to installations in sectors or subsectors to the extent they are covered by other measures to address the risk of carbon leakage as established by Regulation xxx [reference to CBAM]. The measures referred to in the first subparagraph shall be adjusted accordingly.

(*) Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency, amending Directives 2009/125/EC and 2010/30/EU and repealing Directives 2004/8/EC and 2006/32/EC (OJ L 315, 14.11.2012, p. 1–56).”;

- (ii) **the following sentence is added at the end of the third subparagraph:**

“In order to provide further incentives for reducing greenhouse gas emissions and improving energy efficiency, the determined Union-wide *ex-ante* benchmarks shall be reviewed before the period from 2026 to 2030 in view of potentially modifying the definitions and system boundaries of existing product benchmarks.”;

- (b) **paragraph 2 is amended as follows:**

- (iii) **in the third subparagraph, point (c) is replaced by the following:**

“(c) For the period from 2026 to 2030, the benchmark values shall be determined in the same manner as set out in points (a) and (d) on the basis of information submitted pursuant to Article 11 for the years 2021 and 2022 and on the basis of applying the annual reduction rate in respect of each year between 2008 and 2028.”;

- (iv) **in the third subparagraph, the following point is added:**

“(d) Where the annual reduction rate exceeds 2,5 % or is below 0,2 %, the benchmark values for the period from 2026 to 2030 shall be the benchmark values applicable in the period from 2013 to 2020 reduced by whichever of those two percentage rates is relevant, in respect of each year between 2008 and 2028.”;

- (v) **the fourth subparagraph is replaced by the following:**

“By way of derogation regarding the benchmark values for aromatics and syngas, these benchmark values shall be adjusted by the same percentage as the refineries benchmarks in order to preserve a level playing field for producers of those products.”;

(c) **paragraphs 3 and 4 are deleted;**

(d) **in paragraph 6, the first sentence is replaced by the following:**

“Member States should adopt financial measures in accordance with the second and fourth subparagraphs in favour of sectors or subsectors which are exposed to a genuine risk of carbon leakage due to significant indirect costs that are actually incurred from greenhouse gas emission costs passed on in electricity prices, provided that such financial measures are in accordance with State aid rules, and in particular do not cause undue distortions of competition in the internal market, and do not address indirect costs linked to emissions covered by benchmarks established in accordance with paragraph 1.”;

(e) **in paragraph 7, the second subparagraph is replaced by the following:**

“From 2021, allowances that pursuant to paragraphs 19, 20 and 22 are not allocated to installations shall be added to the amount of allowances set aside in accordance with the first sentence of the first subparagraph of this paragraph.”;

(f) **paragraph 8 is amended as follows:**

(i) **the first subparagraph is replaced by the following:**

“8. 325 million allowances from the quantity which could otherwise be allocated for free pursuant to this Article, and 75 million allowances from the quantity which could otherwise be auctioned pursuant to Article 10, shall be made available to support innovation in low-carbon technologies and processes in sectors listed in Annex I and Annex III, including environmentally safe carbon capture and utilisation (“CCU”) that contributes substantially to mitigating climate change, as well as products substituting carbon intensive ones produced in sectors listed in Annex I, and to help stimulate the construction and operation of projects that aim at the environmentally safe capture and geological storage (“CCS”) of CO₂, as well as of innovative renewable energy and energy storage technologies; in geographically balanced locations within the territory of the Union (the “innovation fund”). Projects in all Member States, including small-scale projects, shall be eligible. These allowances may also be used to support break-through innovative technologies and infrastructure to decarbonise the maritime sector.”;

(ii) **in the second subparagraph the following paragraph is added:**

“Allowances not issued to aircraft operators due to the closure of aircraft operators and which are not necessary to cover any shortfall in surrenders by those operators, shall also be used for innovation support as referred to in the first subparagraph.”;

(iii) **in the third subparagraph the last two sentences are replaced by the following:**

“Technologies receiving support shall be innovative and not yet be commercially viable at similar scale without support but shall represent breakthrough solutions and be sufficiently mature for application at pre-commercial scale. Among others, support to projects can be provided in the form of grants, contribution to Union financial instruments, price-competitive tendering support such as carbon contracts for difference, and technical assistance. In the case of grants, up to 60% of the relevant costs of projects may be supported, out of which up to 40% need not be dependent on verified avoidance of greenhouse gas emissions, provided that pre-determined milestones, taking into account the technology deployed, are attained. In the case of price-competitive tendering support and in the case of technical assistance, up to 100% of the relevant costs of projects may be supported.”;

- (iv) **the fourth subparagraph is replaced by the following:**

“The Commission is empowered to adopt delegated acts in accordance with Article 23 to supplement this Directive concerning rules on the operation of the innovation fund, including the selection procedure and criteria, and the eligible sectors and technological requirements for the different types of support.”;

- (g) **The first sentence of paragraph 19 is replaced by the following:**

“No free allocation shall be given to an installation that has ceased operating.”;

- (h) **The following paragraph 22 is added:**

“22. Where corrections to free allocations granted pursuant to Article 11(2) are necessary, these shall be carried out with allowances from, or by adding allowances to, the amount of allowances set aside in accordance with paragraph 7 of this Article.”.

- (17) In Article 8, the words “of the European Parliament and of the Council⁽¹⁾” and footnote ⁽¹⁾ are deleted.

- (18) **In Article 10c, paragraph 7 is replaced by the following:**

“Member States shall require benefiting electricity generating installations and network operators to report, by 28 February of each year, on the implementation of their selected investments, including the balance of free allocation and investment expenditure incurred and the types of investments supported. Member States shall report on this to the Commission, and the Commission shall make such reports public.”.

- (19) **Article 10d is amended as follows:**

- (a) **In paragraph 1, the first subparagraph is replaced by the following:**

“1. A fund to support investments proposed by the beneficiary Member States, including the financing of small-scale investment projects, to modernise energy systems and improve energy efficiency shall be established for the period from 2021 to 2030 (the ‘Modernisation Fund’). The Modernisation Fund shall be financed through the auctioning of allowances as set out in Article 10, for the beneficiary Member States set out therein.

- (b) **the second subparagraph of paragraph 1 is replaced by the following:**

“The investments supported shall be consistent with the aims of this Directive, as well as the objectives of the Communication from the Commission of 11 December 2019 on The European Green Deal (*) and Regulation (EU) [--] of the European Parliament and the Council establishing the framework for achieving climate neutrality and amending Regulation (EU) 2018/1999 (European Climate Law)(**) and the long-term objectives as expressed in the Paris Agreement. No support from the Modernisation Fund shall be provided to energy generation facilities that use fossil fuels.”;

(*) COM(2019) 640 final.

(**) [insert the full title and the OJ reference].”;

(c) **paragraph 2 is replaced by the following:**

“2. At least 80% of the financial resources from the Modernisation Fund shall be used to support investments in:

- (a) the generation and use of electricity from renewable sources;
- (b) heating and cooling from renewable sources;
- (c) the improvement of demand side energy efficiency, including in transport, buildings, agriculture and waste;
- (d) energy storage and the modernisation of energy networks, including district heating pipelines, grids for electricity transmission and the increase of interconnections between Member States;
- (e) the support of households to address energy poverty concerns; and
- (f) a just transition in carbon-dependent regions in the beneficiary Member States, so as to support the redeployment, re-skilling and up-skilling of workers, education, job-seeking initiatives and start-ups, in dialogue with the social partners.

”.

(20) **Article 12 is amended as follows:**

(a) **paragraph 2 is replaced by the following:**

“2. Member States shall ensure that allowances issued by a competent authority of another Member State are recognised for the purpose of meeting an operator’s, an aircraft operator’s or a shipping company’s obligations under paragraph 3”;

(b) **paragraph 2a is deleted;**

(c) **paragraph 3 is replaced by the following:**

“3. The Member States, administering Member States and administering authorities in respect of a shipping company shall ensure that, by 30 April each year,

(a) the operator of each installation surrenders a number of allowances that is equal to the total emissions from that installation during the preceding calendar year as verified in accordance with Article 15;

(b) each aircraft operator surrenders a number of allowances that is equal to its total emissions during the preceding calendar year, as verified in accordance with Article 15;

(c) each shipping company surrenders a number of allowances equal to its total emissions during the preceding calendar year, as verified in accordance with Article 3j.

Member States, administering Member States and administering authorities in respect of a shipping company shall ensure that allowances surrendered in accordance with the first subparagraph are subsequently cancelled.”;

(d) in paragraph 3-a, the first sentence is replaced by the following:

“3-a. Where necessary, and for as long as is necessary, in order to protect the environmental integrity of the EU ETS, operators, aircraft operators, and shipping companies in the EU ETS shall be prohibited from using allowances that are issued by a Member State in respect of which there are obligations lapsing for aircraft operators, shipping companies and other operators.”;

(e) **the following paragraph is inserted after paragraph 3a:**

“3b. An obligation to surrender allowances shall not arise in respect of emissions of greenhouse gases which are considered to have been captured and utilised to become permanently chemically bound in a product so that they do not enter the atmosphere under normal use.

The Commission shall adopt implementing acts concerning the requirements to consider that greenhouse gases have become permanently chemically bound in a product so that they do not enter the atmosphere under normal use.

Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 22a(2).”.

(21) **In Article 14(1), the following sentence is added:**

“Those implementing acts shall apply the sustainability and greenhouse gas emission saving criteria for the use of biomass established by Directive (EU) 2018/2001 of the European Parliament and of the Council(*), with any necessary adjustments for application under this Directive, for this biomass to be zero-rated. They shall also specify how to account for storage of emissions from a mix of zero-rated sources and sources that are not zero-rated.”

(*) Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources (OJ L 328, 21.12.2018, p. 82–209).”.

(22) **The title of Chapter IV is replaced by the following:**

“PROVISIONS APPLYING TO AVIATION, MARITIME TRANSPORT, AND STATIONARY INSTALLATIONS”.

(23) **Article 16 is amended as follows:**

(a) **paragraph 2 is replaced by the following:**

“2. Member States shall ensure the publication of the names of operators, aircraft operators and shipping companies who are in breach of requirements to surrender sufficient allowances under this Directive.”;

(b) **paragraph 3 is replaced by the following:**

“3. Member States shall ensure that any operator, aircraft operator or shipping company that does not surrender sufficient allowances by 30 April of each year to cover its emissions during the preceding year shall be held liable for the payment of an excess emissions penalty. The excess emissions penalty shall be EUR 100 [*to be increased in accordance with the European index of consumer prices since 1 January 2013 as per para 4, if the penalty would restart at EUR 100 due to the amendment*] for each tonne of carbon dioxide equivalent emitted for which the operator, aircraft operator or shipping company has not surrendered allowances. Payment of the excess emissions penalty shall not release the operator, aircraft operator or shipping company from the obligation to surrender an amount of allowances equal to those excess emissions when surrendering allowances in relation to the following calendar year.”

(c) **the following paragraph 11a is inserted after paragraph 11:**

“11a. In the case of a shipping company that has failed to comply with the surrender requirements for two or more consecutive reporting periods and where other enforcement measures have failed to ensure compliance, the competent authority of the Member State of the port of entry may issue an expulsion order which shall be notified to the Commission, the European Maritime Safety Agency (EMSA), the other Member States and the flag State concerned. As a result of the issuing of such an expulsion order, every Member State shall refuse entry of the ships under the responsibility of the shipping company concerned into any of its ports until the company fulfils its surrender obligations in accordance with Article 12. This paragraph shall be without prejudice to international maritime rules applicable in the case of ships in distress.”.

(24) **Article 18b is replaced by the following:**

“Article 18b

Assistance from the European Maritime Safety Agency and other relevant organisations

For the purposes of carrying out its obligations under Articles 3c(4), 3f, 3i, 3j, 3k, 3l and 18a, the Commission and administering authorities may request the assistance of, the European Maritime Safety Agency or another relevant organisation and may conclude to that effect any appropriate agreements with those organisations.”.

(25) **In Article 23, the list of Articles “3d(3), 10(4), 10a(1) and (8), 10b(5), 19(3), Article 22, Articles 24(3), 24a(1), 25a(1) and Article 28c” in paragraphs 2, 3 and 6, is replaced by “3d(3), 3i, 3j, 10(4), 10a(1) and (8), 10b(5), 19(3), Article 22, Articles 24(3), 24a(1), 25a(1) and Article 28c”.**

(26) **The following Chapter IVa is inserted after Article 30:**

“CHAPTER IVa

EMISSIONS TRADING SYSTEM FOR BUILDINGS AND ROAD TRANSPORT

Article 30a

Scope

The provisions of this Chapter shall apply to emissions, greenhouse gas emission permits, issue and surrender of allowances, monitoring, reporting and verification in

respect of the activity referred to in Annex III. This Chapter shall not apply to any emissions covered by Chapters II, IIa and III.

Article 30b

Greenhouse emissions permits

1. Member States shall ensure that, from 1 January 2025, no regulated entity carries out the activity referred to in Annex III unless that regulated entity holds a permit issued by a competent authority in accordance with paragraphs 2 and 3.
2. An application to the competent authority by the regulated entity pursuant to paragraph 1 for a greenhouse gas emissions permit under this Chapter shall include, at least, a description of:
 - (a) the regulated entity;
 - (b) the type of fuels it releases for consumption and which are used for combustion in the buildings and road transport sectors as defined in Annex III and the means through which it releases these fuels for consumption;
 - (c) the end use(s) of the fuels released for consumption for the activity referred to in Annex III;
 - (d) the measures planned to monitor and report emissions, in accordance with the acts referred to in Articles 14 and 30f;
 - (e) a non-technical summary of the information under points (a) to (d).
3. The competent authority shall issue a greenhouse gas emissions permit granting authorisation to the regulated entity referred to in paragraph 1 for the activity referred to in Annex III, if it is satisfied that the entity is capable of monitoring and reporting emissions corresponding to the quantities of fuels released for consumption pursuant to Annex III.
4. Greenhouse gas emissions permits shall contain, at least, the following:
 - (a) the name and address of the regulated entity;
 - (b) a description of the means by which the regulated entity releases the fuels for consumption in the sectors covered by this Chapter;
 - (c) a list of the fuels the regulated entity releases for consumption in the sectors covered by this Chapter;
 - (d) a monitoring plan that fulfils the requirements established by the acts referred to in Article 14.;
 - (e) reporting requirements established by the acts referred to in Article 14;
 - (f) an obligation to surrender allowances, issued under this Chapter, equal to the total emissions in each calendar year, as verified in accordance with Article 15, within four months following the end of that year.
5. Member States may allow the regulated entities to update monitoring plans without changing the permit. Regulated entities shall submit any updated monitoring plans to the competent authority for approval.

6. The regulated entity shall inform the competent authority of any planned changes to the nature of its activity or to the fuels it releases for consumption, which may require updating the greenhouse gas emissions permit. Where appropriate, the competent authority shall update the permit in accordance with the acts referred to in Article 14. Where there is a change in the identity of the regulated entity covered by this Chapter, the competent authority shall update the permit to include the name and address of the new regulated entity.

Article 30c

Total quantity of allowances

1. The Union-wide quantity of allowances issued under this Chapter each year starting in 2026 shall decrease in a linear manner beginning in 2024. The 2024 value shall be defined as the 2024 emissions limits, calculated on the basis of the reference emissions under Article 4(2) of Regulation (EU) 2018/842 of the European Parliament and of the Council(*) for the sectors covered by this Chapter and applying the linear reduction trajectory for all emissions within the scope of that Regulation. The quantity shall decrease each year after 2024 by a linear reduction factor of XX%. By 1 January 2024, the Commission shall publish the Union-wide quantity of allowances for the year 2026.

2. The Union-wide quantity of allowances issued under this Chapter each year from 2028 shall decrease in a linear manner beginning from 2025 on the basis of the average emissions reported under this Chapter for the years 2024 to 2026. The quantity of allowances shall decrease by a linear reduction factor of XX%, except if the conditions of point 1 of Annex IIIa apply, in which case, the quantity shall decrease with a linear reduction factor adjusted in accordance with the rules set out in point 2 of Annex IIIa. By 30 June 2027, the Commission shall publish the Union-wide quantity of allowances for the year 2028 and, if required, the adjusted linear reduction factor.

(*) Regulation (EU) 2018/842 of the European Parliament and of the Council of 30 May 2018 on binding annual greenhouse gas emission reductions by Member States from 2021 to 2030 contributing to climate action to meet commitments under the Paris Agreement and amending Regulation (EU) No 525/2013 (OJ L 156, 19.6.2018, p. 26).

Article 30d

Auctioning of allowances for the activity referred to in Annex III

1. From 2026, allowances covered by this Chapter shall be auctioned, unless they are placed in the Market Stability Reserve established by Decision (EU) 2015/1814. The allowances covered by this Chapter shall be auctioned separately from the allowances covered by Chapters II, IIa and III.

2. The auctioning of the allowances under this Chapter shall start in 2026 with a volume corresponding to [120]% of the auction volumes for 2026 established on the basis of the Union-wide quantity of allowances for that year and the respective

auction shares and volumes pursuant to paragraph 3, 5 and 6. The additional volumes to be auctioned shall be deducted from the auction volumes for the period from 2028 to 2030. The conditions for these early auctions shall be set in accordance with paragraph 7 and Article 10(4).

In 2026, 600 million allowances covered by this Chapter are created as holdings in the Market Stability Reserve pursuant to Article 1a(3) of Decision (EU) 2015/1814.

3. 150 million allowances issued under this Chapter shall be auctioned for the innovation fund established under Article 10a(8). Article 10a(8) shall apply to the allowances referred to in this paragraph.

4. The total quantity of allowances covered by this Chapter after deducting the quantities set in paragraph 3 shall be auctioned by the Member States and distributed amongst them in shares that are identical to the share of reference emissions under Article 4(2) of Regulation (EU) 2018/842 for the sectors covered by this Chapter for the average of the period from 2016 to 2018, of the Member State concerned.

5. The revenues generated from the auctioning of allowances covered by this Chapter, or the equivalent in financial value of these revenues, shall be used for one or more of the activities referred to in Article 10(3) or for one or more of the following:

- (a) measures intended to contribute to the decarbonisation of heating and cooling of buildings or to the reduction of the energy needs of buildings, including the integration of renewable energies;
- (b) measures to provide financial support in order to address social aspects in low- and middle-income households and worst-performing buildings;
- (c) measures intended to accelerate the uptake of zero-emission vehicles or to provide financial support for the development of infrastructure for strategically located, smart and intelligent refilling and charging stations for zero-emission vehicles, whether urban or publicly available on highways, or measures to encourage a shift to public forms of transport, or to provide financial support in order to address social aspects in lower-income households.

Member States shall use at least 50% of their revenues generated in accordance with paragraph 5 from the auctioning of allowances under this Chapter for low-income households.

Member States shall be deemed to have fulfilled the provisions of this paragraph if they have in place and implement fiscal or financial support policies or regulatory policies, which leverage financial support, established for the purposes set out in the first subparagraph and which have a value equivalent to the revenues generated from the auctioning of allowances referred to in this Chapter.

Member States shall inform the Commission as to the use of revenues and the actions taken pursuant to this paragraph in their reports submitted under Regulation (EU) 2018/1999 of the European Parliament and of the Council (*).

6. Articles 10(4) and 10(5) shall apply to the allowances issued under this Chapter.

(*) Regulation (EU) 2018/1999 of the European Parliament and of the Council of 11 December 2018 on the Governance of the Energy Union and Climate Action,

amending Regulations (EC) No 663/2009 and (EC) No 715/2009 of the European Parliament and of the Council, Directives 94/22/EC, 98/70/EC, 2009/31/EC, 2009/73/EC, 2010/31/EU, 2012/27/EU and 2013/30/EU of the European Parliament and of the Council, Council Directives 2009/119/EC and (EU) 2015/652 and repealing Regulation (EU) No 525/2013 of the European Parliament and of the Council (OJ L 328, 21.12.2018, p. 1).

Article 30e

Transfer, surrender and cancellation of allowances

1. Article 12 shall apply to the emissions, regulated entities and allowances covered by this Chapter with the exception of Article 12, paragraphs (2a), (3), (3a), the third and the fourth sentence of paragraph (4) and paragraph (5). For this purpose:
 - (a) any reference to emissions shall be read as if it were a reference to the emissions covered by this Chapter;
 - (b) any reference to operators of installations shall be read as if it were a reference to the regulated entities covered by this Chapter;
 - (c) any reference to allowances shall be read as if it were a reference to the allowances covered by this Chapter.
2. From 1 January 2027, Member States shall ensure that, by 30 April each year, the regulated entity surrenders a number of allowances covered by this Chapter, that is equal to the total emissions, corresponding to the quantity of fuels released for consumption pursuant to Annex III, during the preceding calendar year as verified in accordance with Articles 15 and 30f, and that those allowances are subsequently cancelled.

Article 30f

Monitoring, reporting, verification of emissions and accreditation

1. Articles 14 and 15 shall apply to the emissions, regulated entities and allowances covered by this Chapter. For this purpose:
 - (a) any reference to emissions shall be read as if it were a reference to the emissions covered by this Chapter;
 - (b) any reference to activity listed in Annex I shall be read as if it were a reference to the activity referred to in Annex III;
 - (c) any reference to operators shall be read as if it were a reference to the regulated entities covered by this Chapter;
 - (d) any reference to allowances shall be read as if it were a reference to the allowances covered by this Chapter.
2. The Member States shall ensure that each regulated entity monitors for each calendar year as from 2025 the emissions corresponding to the quantities of fuels released for consumption pursuant to Annex III. They shall also ensure that each regulated entity reports these emissions to the competent authority in the following year, starting in 2026, in accordance with the acts referred to in Article 14(1).

3. The Member States shall ensure that each regulated entity holding a permit in accordance with Article 30b on 1 January 2025 report their historical emissions for year 2024 by 30 March 2025.
4. The Member States shall ensure that the regulated entities are able to identify and document reliably and accurately per type of fuel, the precise volumes of fuel released for consumption which are used for combustion in the buildings and road transport sectors as identified in Annex III, and the final use of the fuels released for consumption by the regulated entities. The Member States shall take appropriate measures to avoid any risk of double counting of emissions covered under this Chapter and the emissions under Chapters II, IIa and III. Detailed rules for avoiding double counting shall be adopted in accordance with Article 14(1).
5. The principles for monitoring and reporting of emissions covered by this Chapter are set out in Part C of Annex IV.
6. The criteria for the verification of emissions covered by this Chapter are set out in Part C of Annex V.

Article 30g

Administration

Articles 13, 15a, Article 16(1), (2), (3), (4) and (12), Articles 17, 18, 19, 20, 21, 22, 22a, 23 and 29 shall apply to the emissions, regulated entities and allowances covered by this Chapter. For this purpose:

- (a) any reference to emissions shall be read as if it were a reference to emissions covered by this Chapter;
- (b) any reference to operator shall be read as if it were a reference to regulated entities covered by this Chapter;
- (c) any reference to allowances shall be read as if it were a reference to the allowances covered by this Chapter.

Article 30h

Measures in the event of excessive price increase

1. If, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than twice the average price of allowance during the six preceding consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, in a timely manner, adopt an implementing act in accordance with the examination procedure referred to in Article 22a(2), to release 50 million allowances covered by this Chapter from the Market Stability Reserve in accordance with Article 1a(7) of Decision (EU) 2015/1814. For this purpose, the Commission shall immediately convene a meeting of the Committee referred to in Article 44(1), point (a), of Regulation (EU) 2018/1999.
2. If, for more than three consecutive months, the average price of allowance in the auctions carried out in accordance with the act adopted under Article 10(4) is more than three times the average price of allowance during the six preceding

consecutive months in the auctions for the allowances covered by this Chapter, the Commission shall, in a timely manner, adopt an implementing act in accordance with the examination procedure referred to in Article 22a(2), to release 150 million allowances covered by this Chapter from the Market Stability Reserve in accordance with Article 1a(7) of Decision (EU) 2015/1814. For this purpose, the Commission shall immediately convene a meeting of the Committee referred to in Article 44(1), point (a), of Regulation (EU) 2018/1999.

Article 30i

Review of this Chapter

By 1 January 2028, the Commission shall report to the European Parliament and to the Council on the implementation of the provisions of this Chapter with regard to their effectiveness, administration and practical application, including on the application of the rules under Decision (EU) 2015/1814 and use of allowances of this Chapter to meet compliance obligations of the compliance entities covered by Chapters II, IIa and III. Where appropriate, the Commission shall accompany this report with a proposal to the European Parliament and to the Council to amend this Chapter.;

- (27) **Annexes I, IIb, IV and V to Directive 2003/87/EC are amended in accordance with Annex I to this Directive, and Annexes III, IIIa and IIIb are inserted in Directive 2003/87/EC as set out in Annex I to this Directive.**

Article 2

Amendments to Decision (EU) 2015/1814

Decision (EU) 2015/1814 is amended as follows:

- (1) **Article 1 is amended as follows:**

- (a) **in paragraph 4, the second sentence is replaced by the following:**

‘The total number of allowances in circulation in a given year shall be the cumulative number of allowances issued and not put in reserve in the period since 1 January 2008, including the number that were issued pursuant to Article 13(2) of Directive 2003/87/EC as in force until 18 March 2018 in that period and entitlements to use international credits exercised by installations under the EU ETS in respect of emissions up to 31 December of that given year, minus the cumulative tonnes of verified emissions from installations under the EU ETS between 1 January 2008 and 31 December of that same given year, any allowances cancelled in accordance with Article 12(4) of Directive 2003/87/EC.’;

- (b) **paragraph 4a is inserted after paragraph 4:**

“4a. As from [the year following the entry into force of this Directive], the calculation of the total number of allowances in circulation shall include the number of allowances issued in respect of aviation and maritime transport

since the beginning of that year, and the number of allowances surrendered by aircraft operators and ship operators in respect of emissions for which allowances are the units which can be used in respect of EU ETS obligations.”.

(c) **paragraph 5 is replaced by the following:**

“5. In any given year, if the total number of allowances in circulation is between 833 million and 1 096 million, a number of allowances equal to the difference between the total number of allowances in circulation, as set out in the most recent publication as referred to in paragraph 4 of this Article, and 833 million, shall be deducted from the volume of allowances to be auctioned by the Member States under Article 10(2) of Directive 2003/87/EC and shall be placed in the reserve over a period of 12 months beginning on 1 September of that year. If the total number of allowances in circulation is above 1 096 million allowances, the number of allowances to be deducted from the volume of allowances to be auctioned by the Member States under Article 10(2) of Directive 2003/87/EC and to be placed in the reserve over a period of 12 months beginning on 1 September of that year shall be equal to 12% of the total number of allowances in circulation. By way of derogation from the last sentence, until 31 December 2030, the percentage shall be doubled.

Without prejudice to the total amount of allowances to be deducted pursuant to this paragraph, until 31 December 2030, allowances referred to in point (b) of the first subparagraph of Article 10(2) of Directive 2003/87/EC shall not be taken into account when determining Member States' shares contributing to that total amount.”.

(d) **paragraph 5a is replaced by the following:**

“5a. Unless otherwise decided in the first review carried out in accordance with Article 3, from 2023 allowances held in the reserve above 400 million allowances shall no longer be valid.”.

(2) **The following Article 1a is inserted after Article 1:**

“Article 1a

Operation of the Market Stability Reserve for the buildings and road transport sectors

1. Allowances covered by Chapter IVa of Directive 2003/87/EC, shall be placed in and released from a separate section of the reserve established pursuant to Article 1 of this Decision, in accordance with the rules set out in this Article.
2. The placing in the reserve under this Article shall operate from 1 September 2027. The allowances covered by Chapter IVa of Directive 2003/87/EC shall be placed in, held in, and released from the reserve separately from the allowances covered by Article 1 of this Decision.
3. In 2026, the section referred to in paragraph 1 shall be created in accordance with Article 30d(2), second subparagraph of Directive 2003/87/EC. By 1 January 2031, the allowances referred to in this paragraph that are not released from the reserve shall no longer be valid.
4. The Commission shall publish the total number of allowances in circulation covered by Chapter IVa of Directive 2003/87/EC each year, by 15 May of the subsequent year separately from the number of allowances in circulation under

Article 1(4). The total number of allowances in circulation under this Article in a given year shall be the cumulative number of allowances covered by Chapter IVa of Directive 2003/87/EC issued in the period since 1 January 2026, minus the cumulative tonnes of verified emissions covered by Chapter IVa of Directive 2003/87/EC for the period between 1 January 2026 and 31 December of that same given year and any allowances covered by Chapter IVa Directive 2003/87/EC cancelled in accordance with Article 12(4) of Directive 2003/87/EC. The first publication shall take place by 15 May 2027.

5. In any given year, if the total number of allowances in circulation, as set out in the most recent publication as referred to in paragraph 4 of this Article, is above 440 million allowances, 100 million allowances shall be deducted from the volume of allowances covered by Chapter IVa to be auctioned by the Member States under Article 30d of Directive 2003/87/EC and shall be placed in the reserve over a period of 12 months beginning on 1 September of that year.

6. In any year, if the total number of allowances in circulation is less than 210 million, 100 million allowances covered by Chapter IVa shall be released from the reserve and added to the volume of allowances covered by Chapter IVa to be auctioned by the Member States under Article 30d of Directive 2003/87/EC. Where fewer than 100 million allowances are in the reserve, all allowances in the reserve shall be released under this paragraph.

7. The volumes to be released from the reserve in accordance with Article 30h of Directive 2003/87/EC shall be added to the volume of allowances covered by Chapter IVa to be auctioned by the Member States under Article 30d of Directive 2003/87/EC within a period of three months from the entry into application of the measure adopted pursuant to Article 30h of Directive 2003/87/EC.

8. Article 1(8) and Article 3 shall apply to the allowances covered by Chapter IVa of Directive 2003/87/EC.”

Article 3

Transposition

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 31 December 2023 at the latest. They shall forthwith communicate to the Commission the text of those provisions.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 4

Repeal and transitional provisions

1. When complying with their obligation as set out in the first subparagraph of Article 3(1) of this Directive, Member States shall ensure that their national legislation transposing Articles 3(u), 10a(3), 10a(4) and 10c(7) and Annex I point 1 of Directive 2003/87/EC, as in force on [date of adoption of the Directive], continue to apply until 31 December 2025.

2. Regulation (EU) 2015/757 is repealed with effect from the entry into force of this Directive.
3. References to the repealed Regulation shall be construed as references to Directive 2003/87/EC and read in accordance with the correlation table in Annex [X] to that Directive.
4. Delegated and implementing acts adopted pursuant to Regulation (EU) 2015/757 shall remain in force until they are repealed by delegated acts adopted pursuant to Article 3i and Article 3j.

Article 5

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 6

Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament
The President

For the Council
The President

(1) **Annex I to Directive 2003/87/EC is amended as follows:**(a) **Point 1 is replaced by the following:**

“1. Installations or parts of installations used for research, development and testing of new products and processes, and installations where emissions from the combustion of biomass that complies with the criteria set out pursuant to Article 14 contribute to more than 95% of the total greenhouse gas emissions are not covered by this Directive.”

(b) **Point 2 is replaced by the following:**

“2. When the total rated thermal input of an installation is calculated in order to decide upon its inclusion in the EU ETS, the rated thermal inputs of all technical units which are part of it, in which fuels are combusted within the installation, are added together. These units could include all types of boilers, burners, turbines, heaters, furnaces, incinerators, calciners, kilns, ovens, dryers, engines, fuel cells, chemical looping combustion units, flares, and thermal or catalytic post-combustion units. Units with a rated thermal input under 3 MW shall not be taken into account for the purposes of this calculation.”

(c) **The second row of categories of activity is replaced by the following:**

Refining of oil, where combustion units with a total rated thermal input exceeding 20 MW are operated	Carbon dioxide
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(d) **The fifth row of categories of activity is replaced by the following:**

Production of iron or steel (primary or secondary fusion) including continuous casting, with a capacity exceeding 2,5 tonnes per hour	Carbon dioxide
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(e) **The seventh row of categories of activities is replaced by the following:**

Production of primary aluminium or alumina	Carbon dioxide
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(f) **The fifteenth row of categories of activities is replaced by the following:**

Drying or calcination of gypsum or production of plaster boards and other gypsum products, with a production capacity of calcined gypsum or dried secondary gypsum exceeding a total of 20 tonnes per day	Carbon dioxide
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(g) **The eighteenth row of categories of activities is replaced by the following:**

Production of carbon black involving the carbonisation of organic substances such as oils, tars, cracker and distillation residues with a production capacity exceeding 50 tonnes per day	Carbon dioxide
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(h) **The twenty-fourth row of categories of activities is replaced by the following:**

Production of hydrogen (H ₂) and synthesis gas with a production capacity exceeding 25 tonnes per day	Carbon dioxide
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- (i) **The twenty-seventh row of categories is replaced by the following:**

Transport of greenhouse gases for geological storage in a storage site permitted under Directive 2009/31/EC, with the exclusion of those emissions covered by another activity under this Directive	Carbon dioxide
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- (j) **the following row is added after the last new row, with a separation line in between:**

“Maritime transport Maritime transport activities of ships covered by Regulation (EU) 2015/757 of the European Parliament and of the Council performing voyages with the purpose of transporting passengers or cargo for commercial purposes	Greenhouse gases covered by Regulation (EU) 2015/757”;
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- (2) **Annex IIb to Directive 2003/87/EC is replaced by the following:**

“ANNEX IIb

**Part A - DISTRIBUTION OF FUNDS FROM THE MODERNISATION FUND
CORRESPONDING TO THE THIRD SUBPARAGRAPH OF ARTICLE 10(1)**

	Share
Bulgaria	5,84 %
Czechia	15,59 %
Estonia	2,78 %
Croatia	3,14 %
Latvia	1,44 %
Lithuania	2,57 %
Hungary	7,12 %
Poland	43,41 %
Romania	11,98 %
Slovakia	6,13 %

**Part B - DISTRIBUTION OF FUNDS FROM THE MODERNISATION FUND
CORRESPONDING TO THE FOURTH SUBPARAGRAPH OF ARTICLE
10(1)**

Share

%

%

%

%

%

%

%

%

%

%

(...)

- (3) **The following Annexes are inserted as Annex III, Annex IIIa and Annex IIIb to
Directive 2003/87/EC:**

“ANNEX III

ACTIVITY COVERED BY CHAPTER IVa

<p>Activity:</p> <p>1. Release for consumption of fuels which are used for combustion in the sectors of buildings and road transport.</p> <p>This activity shall not include:</p> <p>(a) the release for consumption of fuels used in the activities of Annex I of this Directive, except if used for combustion in the activities of transport of greenhouse gases for geological storage (activity row twenty seven);</p> <p>(b) the release for consumption of fuels for which the emission factor is zero.</p> <p>2. The sectors of buildings and road transport shall correspond to the following sources of emissions, defined in 2006 IPCC Guidelines for National Greenhouse Gas Inventories, with the necessary modifications to those definitions as follows:</p> <p>(a) Combined Heat and Power Generation (CHP) (source category code 1A1a ii) and Heat Plants (source category code 1A1a iii), insofar they produce heat for categories under (c) and (d), either directly or through district heating networks;</p> <p>(b) Road Transportation (source category code 1A3b), excluding the use of agricultural vehicles on paved roads;</p> <p>(c) Commercial / Institutional (source category code 1A4a);</p> <p>(d) Residential (source category code 1A4b).</p>	<p>Greenhouse gases</p> <p>Carbon dioxide (CO₂)</p>
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ANNEX IIIa

ADJUSTMENT OF LINEAR REDUCTION FACTOR IN ACCORDANCE WITH ARTICLE 30c(2)

1. If the average emissions reported under Chapter IVa for the years 2024 to 2026 are more than 2% higher compared to the value of the 2025 quantity defined in accordance with Article 30c(1), and if these differences are not due to the difference of less than 5% between the emissions reported under Chapter IVa and the inventory data of 2025 Union greenhouse gas emissions from UNFCCC source categories for the sectors covered under Chapter IVa, the linear reduction factor shall be calculated by adjusting the linear reduction factor referred to in Article 30c(1).

2. The adjusted linear reduction factor in accordance with point 1 shall be determined as follows:

$$[LRF_{adj} = 100\% * ((MRV_{[[2024][2025]-2026]} - (MRV_{[[2024][2025]-2026]} + ((ESR_{[2024]} - 6 * LRF_{[2024]} * ESR_{[2024]}) - MRV_{[[2024][2025]-2026]}) / 5)) / MRV_{[[2024][2025]-2026]}), \text{ where,}$$

LRF_{adj} is the adjusted linear reduction factor;

$MRV_{[[2024][2025]-2026]}$ is the average of verified emissions under Chapter IVa for the years [2024][2025] to 2026;

$ESR_{[2024]}$ is the value of 2024 emissions defined in accordance with Article 30c(1) for the sectors covered under Chapter IVa;

$LRF_{[2024]}$ is the linear reduction factor referred to in Article 30c(1).]

”

- (4) **Annex IV to Directive 2003/87/EC is amended as follows:**

The sentence “The emission factor for biomass shall be zero.” in Part A and Part B of Annex IV is replaced by the following:

‘The emission factor for biomass that complies with the sustainability criteria and greenhouse gas emission saving criteria for the use of biomass established by Directive (EU) 2018/2001(*), with any necessary adjustments for application under this Directive, as set out in the implementing acts referred to in Article 14 shall be zero.’

- (a) **In Part A, in the section “Calculation”, the sixth subparagraph is replaced by the following:**

“Default oxidation factors developed pursuant to Directive 2010/75/EU shall be used, unless the operator can demonstrate that activity-specific factors are more accurate.”;

- (b) **The following Part C is added after Part B:**

“PART C — Monitoring and reporting of emissions corresponding to the activity referred to in Annex III

Monitoring of emissions

Emissions shall be monitored by calculation.

Calculation

Emissions shall be calculated using the formula:

Fuel released for consumption × emission factor

Fuel released for consumption shall include the quantity of fuel released for consumption by the regulated entity.

Default IPCC emission factors, taken from the 2006 IPCC Inventory Guidelines or subsequent updates of these Guidelines, shall be used unless fuel-specific emission factors identified by independent accredited laboratories using accepted analytical methods are more accurate.

A separate calculation shall be made for each regulated entity, and for each fuel.

Reporting of emissions

Each regulated entity shall include the following information in its report:

A. Data identifying the regulated entity, including:

- Name of the regulated entity;
- Its address, including postcode and country;
- Type of the fuels it releases for consumption and its activities through which it releases the fuels for consumption, including the technology used;
- Address, telephone, fax and email details for a contact person; and
- Name of the owner of the regulated entity, and of any parent company.

B. For each type of fuel released for consumption and which are used for combustion in the buildings and road transport sectors as defined in Annex III, for which emissions are calculated:

- Quantity of fuel released for consumption;
- Emission factors;
- Total emissions;
- End use(s) of the fuel released for consumption; and
- Uncertainty.

Member States shall take measures to coordinate reporting requirements with any existing reporting requirements in order to minimise the reporting burden on businesses.”.]

(5) **Annex V to Directive 2003/87/EC is amended as follows:**

The following Part C is added after Part B:

“PART C — Verification of emissions corresponding to the activity referred to in Annex III

General Principles

1. Emissions corresponding to the activity referred to in Annex III shall be subject to verification.

2. The verification process shall include consideration of the report pursuant to Article 14(3) and of monitoring during the preceding year. It shall address the reliability, credibility and accuracy of monitoring systems and the reported data and information relating to emissions, in particular:

- (a) the reported fuels released for consumption and related calculations;
- (b) the choice and the employment of emission factors;
- (c) the calculations leading to the determination of the overall emissions.

3. Reported emissions may only be validated if reliable and credible data and information allow the emissions to be determined with a high degree of certainty. A high degree of certainty requires the regulated entity to show that:

- (a) the reported data is free of inconsistencies;
- (b) the collection of the data has been carried out in accordance with the applicable scientific standards; and
- (c) the relevant records of the regulated entity are complete and consistent.

4. The verifier shall be given access to all sites and information in relation to the subject of the verification.

5. The verifier shall take into account whether the regulated entity is registered under the Union eco-management and audit scheme (EMAS).

Methodology

Strategic analysis

6. The verification shall be based on a strategic analysis of all the quantities of fuels released for consumption by the regulated entity. This requires the verifier to have an overview of all the activities through which the regulated entity is releasing the fuels for consumption and their significance for emissions.

Process analysis

7. The verification of the information submitted shall, where appropriate, be carried out on the site of the regulated entity. The verifier shall use spot-checks to determine the reliability of the reported data and information.

Risk analysis

8. The verifier shall submit all the means through which the fuels are released for consumption by the regulated entity to an evaluation with regard to the reliability of the data on the overall emissions of the regulated entity.

9. On the basis of this analysis the verifier shall explicitly identify any element with a high risk of error and other aspects of the monitoring and reporting procedure which are likely to contribute to errors in the determination of the overall emissions. This especially involves the calculations necessary to determine the level of the emissions from individual sources. Particular attention shall be given to those elements with a high risk of error and the abovementioned aspects of the monitoring procedure.

10. The verifier shall take into consideration any effective risk control methods applied by the regulated entity with a view to minimising the degree of uncertainty.

Report

11. The verifier shall prepare a report on the validation process stating whether the report pursuant to Article 14(3) is satisfactory. This report shall specify all issues relevant to the work carried out. A statement that the report pursuant to Article 14(3) is satisfactory may be made if, in the opinion of the verifier, the total emissions are not materially misstated.

Minimum competency requirement for the verifier

12. The verifier shall be independent of the regulated entity, carry out his activities in a sound and objective professional manner, and understand:

- (a) the provisions of this Directive, as well as relevant standards and guidance adopted by the Commission pursuant to Article 14(1);
- (b) the legislative, regulatory, and administrative requirements relevant to the activities being verified; and
- (c) the generation of all information related to all the means through which the fuels are released for consumption by the regulated entity, in particular, relating to the collection, measurement, calculation and reporting of data.”.