



Council of the  
European Union

Brussels, 5 December 2014  
(OR. en)

16360/14

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**Interinstitutional File:  
2014/0011 (COD)**

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**CLIMA 114  
ENV 955  
MI 969  
IND 367  
ENER 495  
ECOFIN 1146  
TRANS 572  
COMPET 656  
CODEC 2414**

**NOTE**

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From: General Secretariat of the Council  
To: Delegations

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Subject: Proposal for a Decision of the European Parliament and of the Council concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and amending Directive 2003/87/EC

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-Information note from the Presidency on the state of play

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Delegations will find in the Annex an information note from the Presidency on the above-mentioned subject, which will be dealt with under "other business" at the Council (Environment) meeting on 17 December 2014.

**Proposal for a Decision of the European Parliament and of the Council concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and amending Directive 2003/87/EC**

**Information from the Presidency on the state of play**

**I. Background**

On 22 January 2014, alongside its Communication on a policy framework for climate and energy in the period from 2020 to 2030, the Commission issued a legislative proposal concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme<sup>1</sup>. The proposed market stability reserve (MSR) aims at addressing the current market imbalance in the EU Emission Trading System (ETS) and improving its resilience to future unexpected and sudden demand shocks. The Commission's impact assessment explains that at the start of phase 3, the EU ETS was characterised by a surplus of around 2 billion allowances<sup>2</sup>, and that the structural surplus is expected to remain in place up to and beyond the end of phase 3 of the ETS in 2020. In order to address the surplus of emission allowances that has built up in the ETS, it was decided earlier this year, as a short term measure, to postpone ("backload") the auctioning of 900 million allowances from the years 2014-2016 until 2019-2020, following the adoption of the necessary amendments to Directive 2003/87/EC (the "ETS-Directive")<sup>3</sup> and Commission Regulation No 1031/2010 (the "Auctioning Regulation")<sup>4</sup>. However, according to the explanatory memorandum to the MSR proposal, because the surplus is of a structural, long-lasting nature, further action to strengthen the ETS is necessary.

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<sup>1</sup> Docs. 5654/14 + ADD 1 + ADD 2 (COM(2014) 20 final).

<sup>2</sup> In the impact assessment accompanying the proposal (p. 8, footnote 8), surplus is defined *"as the difference between the cumulative amount of allowances available for compliance at the end of a given year, and the cumulative amount of allowances effectively used for compliance with the emissions up to that given year."*

<sup>3</sup> Decision No 1359/2013/EU of the European Parliament and of the Council of 17 December 2013 amending Directive 2003/87/EC clarifying provisions on the timing of auctions of greenhouse gas allowances, OJ L 343, 19.12.2013, p. 1.

<sup>4</sup> Commission Regulation (EU) No 176/2014 of 25 February 2014 amending Regulation (EU) No 1031/2010 in particular to determine the volumes of greenhouse gas emission allowances to be auctioned in 2013-20, OJ L 56, 26.2.2014, p. 11.

Furthermore, according to the Commission proposal, the increase in the annual linear reduction factor from 2021 onwards in line with the EU's new 2030 greenhouse gas emissions target will, by itself, not be sufficient to address the market imbalance nor will it protect the ETS against future shocks.

The proposed MSR would work by triggering adjustments to annual auction volumes whenever the total number of allowances in circulation is outside a predefined range. The main elements of the proposal are the following:

- In each year beginning in 2021 (phase 4 of the ETS), based on data published in May of the preceding year, 12% of the total number of allowances in circulation in year x-2 will be placed in the reserve if this amount is at least 100 million;
- If the total number of allowances in circulation in a given year is below 400 million, 100 million allowances will be released from the reserve;
- In order to mitigate the undue effects of end-of-period auction supply peaks, the additional auction supply is spread over the final year of a trading period and the first two years of the following period;
- The Commission proposes to review the functioning of the MSR by the end of 2026, with a particular focus on the percentage of allowances to be placed into the reserve and the thresholds.

## **II. State of play**

The Working Party on the Environment (WPE) examined the proposal and the accompanying impact assessment at four meetings during the Hellenic Presidency. In the context of a policy debate on the 2030 climate and energy policy framework at the Council (Environment) on 3 March 2014, Ministers broadly agreed on the need to strengthen the ETS and welcomed the Commission's proposal. During the Italian Presidency, a certain number of key issues were identified and discussed at five WPE meetings. On 16 July 2014, an exchange of views on the proposal took place at the informal meeting of environment ministers in Milan. The Presidency reported on the outcome of the discussion to the President of the European Council.

At its meeting on 23-24 October 2014, the European Council agreed on the 2030 climate and energy policy framework for the European Union and endorsed a binding EU target of an at least 40% domestic reduction in greenhouse gas emissions by 2030 compared to 1990<sup>5</sup>. As regards, the ETS, the European Council stated that a well-functioning, reformed Emissions Trading System with an instrument to stabilise the market in line with the Commission proposal will be the main European instrument to achieve this target, confirmed that the annual linear factor will be changed from 1.74% to 2.2% from 2021 onwards, and gave a number of further orientations, including on free allocation and the continuation of existing measures after 2020 to prevent the risk of carbon leakage.

Without prejudice to more detailed comments/positions expressed by individual delegations, the Presidency has identified the main issues set out below on which the positions can be summarised as follows:

- **The start of the implementation of the MSR and the treatment of backloaded allowances:**

On these two key political issues, at present delegations' positions fall into three groups of roughly equal size. Some delegations are of the view that the MSR should be implemented well before the year 2021, with concrete suggestions varying between 2017 and 2019. Those delegations also consider that the backloaded allowances should be transferred directly into the MSR instead of bringing them back onto the market from 2019; a small number of delegations in this group could also support their permanent cancellation. Other delegations support the implementation of the reserve from 2021, as proposed by the Commission. Of these delegations, most are opposed to the direct transfer of backloaded allowances into the MSR, but a small number of delegations support that idea, provided that the MSR is not implemented before 2021. The remaining delegations have not yet taken a position on the two issues.

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<sup>5</sup> Doc. EUCO 169/14.

- **Conditions for the removal of allowances into the reserve and their return to the market:**

A number of delegations consider the thresholds and conditions for triggering the MSR in the Commission proposal as broadly acceptable. However, some delegations have suggested adjustments to one or more of the parameters proposed by the Commission, and many delegations reserve their final position on the issue pending further analysis.

- **Response time of the MSR:**

A large number of delegations consider that the two-year time lag, or the response time between the moment the information on the market situation is available and the auctioning volumes are adjusted, should be reduced.

- **Frequency of review of the MSR:**

Some delegations agree with a review of the MSR taking place every five years, others consider that it should be reviewed more frequently, for example, every three years.

Although excluded from the scope of the present Commission's proposal, several delegations have stressed the need to take account of the risk of carbon leakage also in the period after 2020. The Commission has indicated that it will present a legislative proposal on the wider review of the ETS at a later stage.

In the European Parliament, Mr Ivo Belet (EPP) was nominated Rapporteur for the Committee on the Environment, Public Health and Food Safety (ENVI) on 10 July 2014. The vote in the ENVI committee is expected to take place on 24 February 2015.

On 13 February 2014, the Council decided to consult the Economic and Social Committee and the Committee of the Regions on the proposal. The Economic and Social Committee adopted its opinion on 4 June 2014<sup>6</sup>.

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<sup>6</sup> NAT/637 – EESC-2014-00800-00-00-AC-TRA (available on EESC website).

### **III. Next steps**

In view of the above, the Presidency considers that considerable progress has been made on the proposal through the identification and focused discussion on the key issues, which will serve as a sound basis for further work under the incoming Latvian Presidency. However, more work will be needed, particularly on the above-mentioned key issues, to enable the Council to establish its position on the proposal with a view to possible informal negotiations with the European Parliament.

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