IOGP position on the revision of the EU Emissions Trading System (EU ETS) Directive

The International Association of Oil & Gas Producers (IOGP) supports the goals of the Paris Agreement and the EU's ambition to reach climate neutrality by 2050. We recognize that there are many challenges on the road to meet this objective as the energy transition will require significant investments, new technologies, effective policies, and behavioural changes. To this end, IOGP supports carbon pricing as a primary tool to achieve emission reduction goals, as it incentivises the most cost-effective emission reductions.

IOGP welcomes the Commission's proposal to mandate Member States to use 100% of their EU ETS revenues for climate-related purposes and to further strengthen the Innovation Fund and the Modernisation Fund – crucial steps to scaling up low-carbon technologies needed for industrial decarbonisation and to enable necessary investments in the transformation process. The Commission should be commended for its proposals to account for all CO_2 transportation modes in the revised EU ETS Directive, to establish provisions for accounting of CO_2 within Carbon Capture and Utilisation (CCU) processes, and to introduce Carbon Contracts for Differences (CCfDs) to bridge the gap between the prevailing carbon price and the level needed to make Carbon Capture Utilisation and Storage (CCUS) deployment possible – which goes in line with recommendations laid out in the IOGP-coordinated Madrid Forum report on 'The potential for CCS and CCU in Europe'[1].

In view of the European Commission proposal for a revised EU ETS Directive we would like to make the following recommendations:

1) **Recognising the advantages and versatility of natural gas in the context of the Modernisation Fund**: Exclusion of natural gas projects from the scope of the Modernisation Fund would disregard the most cost-effective solution to support Member States on their respective transition pathways. In their NECPs, many Member States refer to natural gas as an important driver of transition, in particular in carbon intense regions[2]. In a 2050 perspective, investing in the production of natural gas and low-carbon gases, as well as in gradual technical adaptations of the EU gas infrastructure to carry hydrogen and other low-carbon gases, can contribute to climate neutrality while making use of existing infrastructure in a more cost-effective way. In this context, the EU should ensure that investments in natural gas and natural gas-based technologies are included in the scope of the Modernisation Fund. If the EU fails to take a technology neutral approach, the costs associated with Modernisation Fund projects risk becoming higher than necessary in relation to their GHG emission reduction potential, which could put an additional strain on beneficiary Member States. A comprehensive assessment should be carried out to determine if the proposed increase of the fund is proportionate to the tightening of the Linear Reduction Factor (LRF), and whether additional resources should be allocated to meet modernisation needs of beneficiary Member States.

[1] The potential for CCS and CCU in Europe, IOGP (2019): https://ec.europa.eu/info/sites/default/files/iogp_-_report_-_ccs_ccu.pdf
[2] See IOGP's NECP assessment.

2) **Need for increased and effective carbon leakage protection**: We welcome the increased EU climate ambition, however the associated price signals in the EU ETS resulting from the proposed increase of the LRF, the tightening of the Market Stability Reserve (MSR), as well as the gradual phase-out of free allowances will increase the need for an effective carbon leakage protection mechanism for the impacted EU ETS sectors to maintain a level playing field for EU producers when competing domestically and on export markets. Maintaining the current share of free allowances would enhance EU industries' ability to foster investments necessary for the decarbonisation and would not affect the climate targets set out by the Fit for 55 package. Additionally, compliant entities should not be penalised for preparing for breakthrough technologies rather than investing in incremental energy efficiency improvements – therefore, acting on the results of energy audits should not be made obligatory through the EU ETS to make up to 25% of free allocations conditional. This maintains R&D, employment and investment in the EU and safeguards the competitiveness of EU industry while avoiding carbon leakage.

3) **Longer term convergence to a uniform cost of carbon**: We support the near-term separation between the existing EU ETS and the new system covering road transport and buildings, given the different marginal abatement costs and market dynamics considerations. Longer term convergence to a uniform cost of carbon will enable emission reductions at lowest societal costs. However, considering the vulnerable character of households and the risk of mobility poverty as a result of proposed expansion of carbon pricing, we recommend the Commission to continuously assess the impact of proposed regulation on these sectors as well as adequacy of the proposed mitigation measures, and propose further mitigation measures if necessary.