

COGEN Europe contribution to the European Commission's Consultation on EU emissions trading system (ETS) – update of the free allocation rules

Brussels, 19 December 2023

COGEN Europe, the European Association for the Promotion of Cogeneration, supports the Commission's efforts to comply with the EU objectives of achieving the emissions reduction target of 55% by 2030 and climate neutrality by 2050.

At the same time, we strongly believe that the reviewed EU ETS Directive together with its implementing and delegated acts, should be based on what is technically and economically feasible, building on existing best practice through promoting the most efficient technologies currently available, while avoiding unbearable increases in costs, undermining the competitiveness of the European industry or discriminating between different European industries. COGEN Europe is supportive of the EU ETS process, aiming to establish a level playing field for all technologies, including high efficiency cogeneration, to deliver steady and cost-effective emission reductions in the EU.

Nevertheless, taking into account the broad revision of the EU ETS Directive and its implementing acts, we find it essential to provide guidance on the rules in relation to the conditionality of free allocation and climate-neutrality plans (CNPs) for installations with product-benchmarks and district heating operations, and the requirements CNPs must meet to ensure the free allocation to eligible installations.

Cogeneration (CHP) supplies low carbon heat and flexible electricity to key sectors and millions of consumers across the EU, from residential to public buildings, from the energy intensive industries (chemical, alumina refineries, food & drink, pulp & paper) to the tertiary sector (hospitality sector, bakeries, greenhouses, hospitals). Cogeneration produces today 12% of the total electricity and 16% of the heat in the EU. More than 60% of the heat supplied through district heating comes from local cogeneration plants. This ensures significant energy savings (>30 bcm) and CO₂ emission reductions (>150 million tons of CO₂ reduced yearly). EU level strategies must thus address the challenges and maximise opportunities for measures needed to achieve sectoral transformations and policies to respond in a comprehensive and inclusive manner, while maintaining energy security and competitiveness of EU industry.

To achieve this, COGEN Europe recommends that the free allocation rules revision addresses the following provisions:

- **Conditionality related to energy efficiency measures**

Since the Article 22a requires that the operator shall establish, implement, document and maintain a procedure for implementing recommendations, which lead to improving the installation's energy efficiency, it may be useful to harmonize the text proposed in the draft FAR regulation with the four-year period of the EED evaluation of the existing measures to achieve energy efficiency increase (Article 11). This will allow operators/companies to reduce administrative burden and ensure an implementation of this provision by introducing the same approach for the next allocation period. Moreover, establishing a coherent framework and avoiding double measures at the national level should remain the crucial and overarching goal.

- **Fallback benchmarks**

Currently, fallback benchmarks group all sectors together under one fallback benchmark value for fuel and heat, regardless of the differences in technologies and technological potential and/or challenges regarding changing the fuel that can be used in the sectors covered. This leads to inaccurate values and today the heat and fuel fallback benchmarks do not reflect the reality of some of the sectors that rely on these benchmarks for the allocation of free allowances to their installations, leading eventually to significant cost increases and a shrinking of the EU processing capacity (even for Critical Raw Materials). Therefore, it would be important to set new sector specific fallback benchmarks for sectors that are not treated fairly, due to technological consideration, under the current approach in implementing acts under Article 10a(2) of ETS Directive. The benchmarks methodology should ensure that the heat and fuel fallback benchmarks reflect the reality of the sectors covered. These benchmarks should be sector specific, to ensure that due consideration is given to sectorial and geographical differences.

For example, for one of our members in the case of alumina refineries and aluminium recycling provides a concrete example of this unscientific and unfair treatment: According to the revised ETS, fallback benchmarks will face a cut of 50% as they will be set by installations consuming biomass belonging to specific range of processes and industrial sectors. This leads to **artificially low thresholds** that cannot be reached by an alumina refinery or recycling plant, for which biomass does not form a feasible alternative as stipulated in multiple international studies; this leads to an unduly penalizing 50% reduction of free allocation, and consequential cost increase and closures to plants that are already struggling because of the higher energy costs since the energy crisis (between 2021 and 2022 the sector has lost respectively 1 million tons of EU alumina and primary aluminium production). It is also important to mention that both alumina and primary aluminium are globally priced commodities,

so European companies are therefore not able to pass on to consumers any extra regulatory costs imposed by the EU, which at the same time are not faced by other global competitors.

The [IEA report on the role of biomass](#), provides some additional argumentation regarding the high temperatures and the gaseous fuels needed for various industrial processes, which renders the use of biomass unviable for these processes.

- **Reduction milestones timeframe**

According to the implementing act, a detailed description of reduction milestone is planned for 2025 and for each 5-year period afterwards. This will be very difficult to achieve, as the IA enters into force towards the end of 2023. The operators of the installation simply have too little time to prepare for that, as investments in the energy sector take on average 5 years to complete. Therefore, *a detailed description of all measures planned during each five-year period in order to reach the milestones and targets described in order to reach climate neutrality by 2050*, should refer to **2030** and 5-year periods thereafter.

- **Ensure consistency between documents related to free allocation requirements**

According to the revised ETS Directive, operators applying for free allocation in May 2024 will need to establish a climate-neutrality plan for the installations for which they apply for additional free allocation. Those plans, among other things, include providing evidence that they have implemented energy efficiency measures with proportionate costs and with a payback of three years or less to avoid the 20% free allocation penalty. Although, in line with the provisions of the Energy Efficiency Directive energy audits must be prepared in every four-year. Therefore, timelines across different files concerning the energy efficiency conditionality should allow sufficient time to operators for implementing such recommendations. Furthermore, companies that have implemented a certified energy or environmental management system which requires continuous improvements should be considered fulfilling the ETS energy efficiency conditionality.

Moreover, for conditional free allocation for district heating, while the ETS Directive requires the establishment of the CNP by 1 May, the draft FAR requires submission of the CNP by 30 May (Article 22b), together with the Baseline Data Report, therefore there is not enough consistency between both documents when operators/DH company are planning to apply for FA.

- **Ensure the security of supply and system adequacy for EU industry**

It is key that EU and national legislation fully accounts for and rewards CHP energy savings and emission cuts for both electricity and heat. Currently, CHP covered by the ETS are competing with less efficient boilers not subject to a carbon price outside the ETS. Meanwhile, smaller CHPs that fall under

the Effort Sharing Regulation, reduce carbon emissions within the ETS (by self-generating lower carbon electricity and avoiding electricity purchase from the grid), but cannot be counted as carbon reducing under national emissions targets. The application of a carbon price to buildings could minimise and eventually get rid of the “internal carbon leakage” between heating installations covered by the ETS and those falling under Effort Sharing Regulation sectors. Yet, any such mechanism should be designed in such a way as to fully account for CHP efficiency and carbon reductions for both electricity and heat.

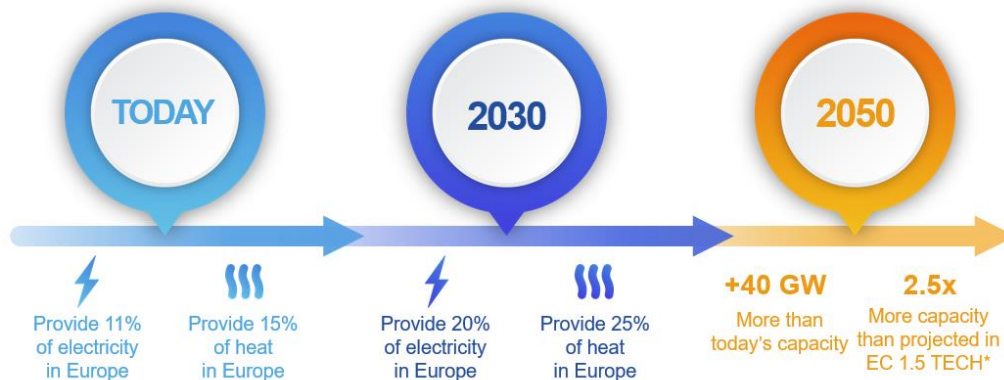
Ensure that the competent authorities take a comprehensive approach to assessing the potential for cogeneration in their territory, fully considering its benefits in terms of primary energy efficiency, energy systems integration and energy system flexibility. New gas-based CHP is mostly renewables ready, as it can run on different blends of renewable gases and hydrogen should these fuels become economically available in the future. Some technologies are fully flexible to run from 0 to 100% hydrogen, to match potential variability in availability.

Moreover, it is important that existing and new investments in cogeneration providing services on both the electricity and heat markets do not face barriers to delivering their primary purpose: supplying heat on an uninterruptible basis to many leading industries. To this end, it is crucial to **maintain priority dispatch** of electricity from cogeneration in industrial installations and reinforce compensation in case this electricity is curtailed¹.

Setting climate neutrality plans for installations under ETS for an ambitious, resilient and cost-effective pathway to net-zero by 2050

The cogeneration sector is committed to building the foundations to that: a resilient, decentralised and carbon-neutral European energy system by 2050, with cogeneration as its backbone. Already today, CHP is one of the most cost-effective and sustainable energy solutions for industry to meet its on-site demand of both high-grade heat and electricity, reducing in many cases up to 30% of CO₂ compared to any other combustion process. CHP is also RES-ready, with existing installations having the option to be converted to use zero carbon fuels (e.g., biomethane and hydrogen), when they become available. In carbon neutral 2050 scenarios, CHP can be cost-effective for a variety of applications and can reduce overall energy system costs by EUR 4-8 bn annually (see [Artelys study on CHP in 2050](#)).

¹ Priority dispatch helps ensure that efficient electricity is fed onto the grid in priority over less efficient and polluting sources, in line with articles 12 & 13 of EU Electricity Regulation and former article 15 of the Energy Efficiency Directive 2012/27/EU (EED).



About COGEN Europe

COGEN Europe, the European Association for the Promotion of Cogeneration, is the cross-sectoral voice of the cogeneration industry. We have over 60 members: 13 national associations and 50 organisations spanning the entire value chain from technology manufacturers and users to consultancies. The cogeneration sector is committed to the creation of a resilient, decentralised and carbon neutral European energy system by 2050 with cogeneration as its backbone, empowering European citizens and industry to generate their own efficient, reliable and affordable clean heat and power locally.

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