CONSULTATION RESPONSE

EFET
European Federation of Energy Traders

EFET response to the Commission consultation on the reporting obligations during the transitional period of the Carbon Border Adjustment Mechanism

Brussels, 11 July 2023

Key messages

1. Cost-efficiency and competition in the supply of decarbonised electricity would be enhanced by the UK and EU linking their ETSs, ensuring efficient cross-border trading rules and exempting each other from the application of CBAM.
2. It is essential for the Energy Community countries to meet the requirements for an exemption, as CBAM could slow down the pace of market integration and decarbonisation in the region.
3. The technical implementation rules for electricity imports need to reflect the features of cross-border electricity trading.

Detailed comments

The rationale for putting in place a Carbon Border Adjustment Mechanism (CBAM) is to ensure a level-playing field and environmental accountability, and to promote the adoption of carbon pricing mechanisms in third countries. However, the densely interconnected European electricity system translates into strong interdependence of countries within and outside of the EU. We hope that the application of CBAM with respect to electricity imports from the UK and from the Energy Community region is an occasion to deepen these links, rather than distance the EU system from that of its neighbours. We also wish to make sure that the technical implementation requirements duly take into account the specificities of the interconnected electricity system and the way electricity is traded across the borders of Europe at large.

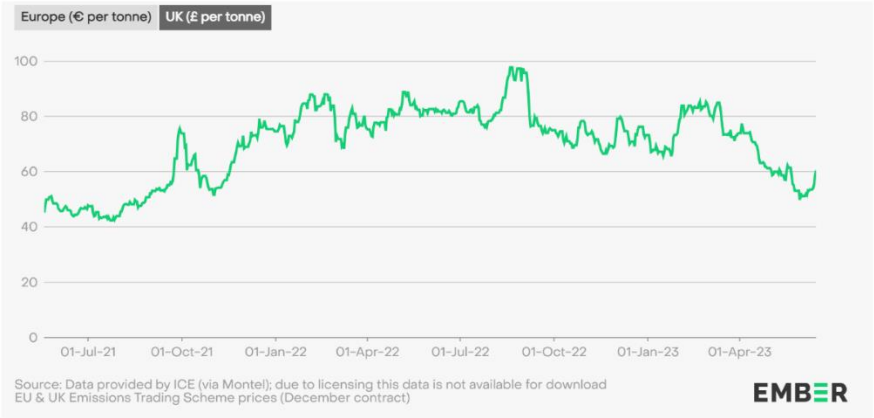
Enhancing cost-efficiency, competition and decarbonisation through linking the UK and EU ETSs

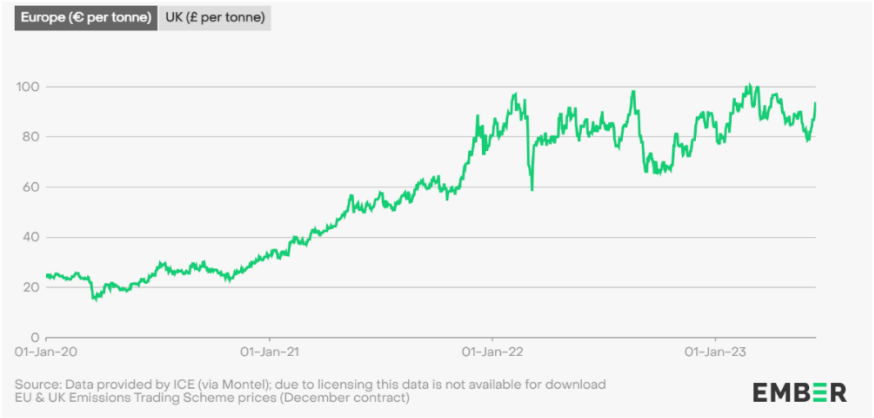
Political recognition that the UK and the EU are on a similar decarbonisation path, with a comparable level of ambition and targets is important. This will ensure greater cooperation, which would allow for more efficient cross-border exchanges and harnessing more effectively the enormous potential of offshore renewables. Greater cooperation will help us achieve our

decarbonisation targets faster and at a lower cost and will strengthen our security of supply.

The UK has decarbonisation commitments and energy, climate and environmental policies similar to those of the EU. It also has a comparable carbon pricing regime – the UK Emissions Trading System (UK ETS). The decarbonisation signal of the UK ETS is further enhanced by the UK Carbon Price Support (CPS).

Prior to Brexit, the UK was part of the EU ETS. The independent UK ETS established after Brexit is largely based on the EU ETS design. Furthermore, since the start of the UK ETS, the system has delivered a strong decarbonisation signal like the one of the EU ETS, as illustrated in the two price charts below.





We therefore urge EU and UK policymakers to cooperate and explore the following measures to ensure that the UK carbon pricing regime is recognised and taken into account and to reduce (or remove altogether in the case of an exemption) the administrative burden of CBAM with respect to electricity imports from the UK:

- Linking the UK ETS and the EU ETS: This would be a comprehensive solution, which would ensure an exemption for the UK from CBAM (Art. 2(6)

of CBAM) and would also benefit the functioning of the two carbon markets in terms of enhanced liquidity.

- Recoupling the Great Britain (GB) and EU electricity markets: This would open the possibility for an exemption from EU CBAM for electricity imports (Art. 2(7) of CBAM), which would remove the administrative burden and the implementation challenges outlined later on in the consultation response. In addition, price coupling would ensure that interconnectors between the EU and GB operate in the most efficient way possible, optimising cross-border exchanges and the dispatch of renewable energy.
- Enacting a bilateral agreement taking into account the UK carbon pricing regime: While such an agreement may resolve some technical implementation challenges, however, the reporting and verification requirements and related administrative costs are likely to remain.

Since reporting requirements under the EU CBAM will start applying as of October 2023 and full implementation will commence in 2026, work on securing a solution for electricity imports needs to start immediately and be completed within a rather ambitious timeframe. This is important for the following reasons:

- **To avoid paying twice for carbon emissions (or inappropriately taxing renewable/ low-carbon electricity).** If CBAM is applied in full to electricity imports from GB, a carbon price would be paid *twice* on at least some of the electricity imports. The reason for this is the following: electricity is often traded via anonymised exchanges, which is why establishing a paper trail between a producer and an importer is usually not possible. As a result, an importing party would not be able to present documentation on a carbon price having been paid on electricity production in GB in order to obtain a discount from CBAM. Imposing such additional costs on electricity imports from GB – on which a carbon price has been paid under the UK ETS (+CPS) – would be at odds with the spirit of CBAM.
- **To ensure efficient flows over the interconnectors and avoid undue costs to consumers.** Since imports may have to pay a carbon price twice, as described above, the efficiency of interconnector flows between the EU and GB may be affected, which would also translate into increased costs to consumers in neighbouring EU markets.
- **To enable the smooth expansion of offshore renewable energy projects and hybrid assets**, which would benefit consumers and contribute to the decarbonisation of both the EU and the UK. Such assets are expected to pick up considerably after 2025, and it would be important for cross-border trading arrangements to facilitate their growth, rather than create uncertainty for investors and project developers (e.g. due to the congestion rule for using actual emissions – consider the case of hybrid assets where an offshore renewable energy asset will be exporting to the EU through an interconnector that is also used by other exporters).

- **To avoid implementation challenges with respect to Northern Ireland and the Republic of Ireland.** Electricity generators in Northern Ireland are part of the Single Electricity Market on the Island of Ireland and also part of the EU ETS. It is difficult to work out how CBAM could be applied in a viable manner: a) one part of the UK cannot impose a CBAM fee on another in the case of Northern Ireland; b) the interconnectors with both Northern Ireland and the Republic of Ireland operate under an implicit allocation regime in Intraday.
- **To avoid implementation challenges with respect to electricity trading between the UK and Norway.** Currently, the NSL interconnector between the UK and Norway operates under an implicit capacity allocation regime in the day-ahead timeframe. Norway is exempt from CBAM and we are not clear as to whether EU CBAM legislation would also be applied in Norway. In both cases - if EU CBAM is extended to Norway and if it is not - the implications for trading over the NSL interconnector need to be considered - in the case of the former, because CBAM would have to apply under an implicit allocation regime, and in the latter case - to address the potential risk of circumvention.

Ensuring that the Energy Community region meets the requirements for a CBAM exemption

We urge the Commission, in cooperation with the Energy Community Secretariat, to continue working with the region's authorities to ensure that the whole Energy Community region further integrates its energy markets with that of the EU. This is essential to help Energy Community countries prepare to meet the requirements for a CBAM exemption and not to jeopardise progress on decarbonisation at a continental scale.

We are concerned that CBAM implementation would slow down the pace of market integration and decarbonisation in the Energy Community region. Electricity market coupling with EU neighbours would bring important benefits for consumers (more efficient cross-border flows and cost savings) and the environment (optimised dispatch of renewables across the coupled markets). Failure to make progress or backtracking on market integration due to CBAM implementation would be a missed opportunity to deliver these benefits.

In addition, the continued uncertainty whether CBAM would apply in the region and the potential unintended consequences of its application affects investment decisions already today and could impact decarbonisation efforts in the years to come. This uncertainty will persist at least until the end of 2025, if not longer, since even if a country has obtained an exemption, the exemption can be withdrawn at a later stage.

Close cooperation with the national authorities in the Energy Community region is needed to ensure that the ambitious timelines and extensive criteria for a CBAM exemption are met.

- Ambitious timelines:
  - The Energy Community countries would have to complete the process of market coupling by the summer of 2025. This timeline is tight, considering that they have not yet transposed the necessary legislation (required to be completed by the end of the year) and there has been very limited progress on technical implementation. In addition, there are questions whether the "market coupling" requirement for a CBAM exemption should cover only Day-Ahead or also the Intraday market coupling. This would make meeting the already challenging deadlines even more difficult to meet, if possible at all. **We therefore urge the Commission to clarify their position and confirm that day-ahead market coupling is sufficient to secure a CBAM exemption.**

  - The timeline for implementing an emissions trading scheme (regional or local – we would also appreciate clarity on this) with a price equivalent to the one of the EU Emission Allowances (EUAs) is also tight. There has been insufficient progress and clarity on concrete implementation plans from national authorities, which contributes to the uncertainty on the way forward.
    In addition, since the deadline for implementing an ETS is 2030, while market coupling needs to be implemented within the next two years, we are concerned about the impact of implementing market coupling without an effective carbon pricing mechanism in the region.

- The risk of moving at different speeds: If some countries obtain an exemption and others do not, this means that some will proceed with further market integration, while others most likely will not. This is likely to have a serious impact on trading and security of supply across the West Balkans. The situation is further complicated by the fact that the region has strong interconnections and is also used for transit by neighbouring EU Member States.

Taking into account the specificities of cross-border electricity trading

The following section includes comments on the draft rules for the transitional period, but also comments and concerns related to the full implementation of CBAM and the extent to which it takes into account the specificities of the electricity sector. One key issue arising from the way electricity is traded (e.g., on

anonymised exchanges) and the challenge that creates for establishing a paper trail was described in detail in an earlier section. Other key issues include:

- Unintended consequences for renewable energy producers: The requirement to prove that there was no congestion at the time of export in order to use actual emissions for the calculation of the carbon footprint of one's electricity imports into the EU means that a renewable energy producer would not have full visibility on costs in advance. This can impact discussions with lenders (e.g. banks) early on in the project development stage, because there is no way to prove in advance that the CBAM fee would not apply to the relevant renewable energy project/ production, considering that information on congestion is not available in advance. Lenders, who tend to be risk averse, may conclude that the project is not viable (as the project with a CBAM fee at the level of EUAs may not be profitable), or may increase the cost of capital to account for the CBAM risk.

  The congestion rule can also create challenges for existing projects, which would be put at a disadvantage. Information on congestion is not available in advance. Therefore, renewable electricity export is discouraged and/or disadvantaged in comparison to export from other production facilities where the costs would be known in advance.

  In addition, in the West Balkans region there are periods of the year with strong transit flows between EU Member States through non-EU countries (GR>NMK>RS>HU, for example, or BG>RS>HU, or IT>MNE>RS>HU/HR). Such transit flows, from countries that are EU members and with the EU ETS in place may be part of the reason for congestions at borders with non-EU countries. As a consequence, a renewable electricity producer in one of these third countries may have to pay a CBAM fee due to congestion that is fully or partially caused by such transit, which would not be fair.

  We are concerned that imposing the congestion rule may discourage further renewable investment, which would have the opposite effect of what CBAM intended to achieve – i.e. incentivising the energy transition in third countries.

  Effectively, with the congestion rule in place there is no level playing field between EU and non-EU renewables.

- Treatment of transit:

  Additional clarifications are needed with regard to the treatment of transit flows between EU Member States through non-EU countries. There is no specific guidance on how it would be declared/exempted. All the relevant data is available to the TSOs and it would be helpful if TSOs-issued documentation is considered eligible and sufficient for verification purposes.

  We note that Article 5(4) states the following: *"Imports are to be measured per border for time periods no longer than one hour and no deduction of export or*

transit in the same hour shall be possible." We would like to know whether this means that there would be no exceptions for transit.

Furthermore, Article 7 of the draft rules (Reporting of information regarding carbon price) sets several criteria for the reporting of the carbon price paid in the country of origin. It seems to us that this should not be necessary with regard to transit flows between EU Member States through non-EU countries. In our view, these requirements should be removed, or at least simplified in the case of such electricity, as the generated electricity would have been subject to the EU ETS.

- Verification requirements:
  The verification requirements should take into account what information is already available. This could help simplify the verification process where possible. TSO reports/confirmations and TSO license/ registration/ measurement data, for instance, are one such source of accurate and reliable information. In the case of the Energy Community region, for example:
  - The Western Balkan TSOs are members of ENTSO-E, having adopted and applying ENTSO-E rules and procedures (Ukraine and Moldova have a Connection Agreement, so they would be treated the same way in this case);
  - No production plant can inject energy into the grid without being approved, tested and checked by the relevant TSOs and DSOs;
  - TSOs have all the relevant data available (connection point of relevant power plant, measurement data, cross-border flows);
  - There are metering procedures in place and data available (in hourly and/or 15min resolution);
  - With RES power plants and/or any other power plant in the relevant TSO area, at the moment of its licensing and registration with the TSO, it is known what kind of a plant it is, how it produces energy, what its installed capacity is. The TSO and/or DSO are also aware of the quantity that is being produced in real time/at the very moment it produces energy.

- Verification requirement for using actual embedded emissions:
  We have noted that the draft rules for the transitional period do not include the requirement to verify whether the criteria for using actual emissions have been met. Annex IV, 5(e) of CBAM requires that "the fulfilment of the above criteria is certified by an accredited verifier, who shall receive at least monthly interim reports demonstrating how those criteria are fulfilled."

  At the same time, D2.4 of the Annex III to the Implementing Regulation does not include this requirement. We would appreciate a confirmation whether the omission is intentional or not.

- Methodology for calculating default values:

Considering that the emissions factor of imported electricity will be subject to specific default values applied by the Commission, we request more information on how the Commission would approach the process of defining these values. In particular, we refer to:
Annex III D.2.1: "*CO2 emission factors in the third country, group of third countries or region within a third country, shall be* ***based on data from the International Energy Agency (IEA)*** *provided by the Commission.*"

In addition, default values can be determined for a third country or region within a third country. It is important to define regions (or at least criteria for definition) already in this preparatory phase, since some third countries at the borders of the EU may have regions with a specific energy mix. This would enable electricity importers to prepare in a timely manner and plan their investments and trading activities.

- Annex III, D 2.3 clarification
  When calculating embedded emissions, the following timeline is applied: "for the five-year period, starting from year minus two." Would it not be more appropriate to simply apply a period of the last five years?

- Netting of electricity exports
  Netting should be allowed in the declaration of electricity exports. Indeed, if CBAM is applied to all nominated flows, this would result in CBAM costs being applied to electricity that does not physically enter the EU, which would not be appropriate. However, Article 5.4 of CBAM seems to go in the opposite direction. We would appreciate a clarification.

- Declarant in case of PTRs held by non-EU partner
  Article 5(4) of the CBAM Regulation states that the entity to which the physical transmission rights (PTRs) are allocated is considered to be the declarant. If there is a transaction on the border between a non-EU and an EU entity and the PTRs owner is the non-EU entity, who should declare? If we understand correctly, the EU entity which imports energy and does not have its own capacity but is using capacity provided by its non-EU partner is not obliged to report. Is this correct? On the other hand, the non-EU partner would not declare either, as it does not operate in the EU. A clarification would be helpful.

- Submission of reports
  We understand that the declarant shall have web access to the relevant Transitional CBAM Registry where the declarant should submit its reports. Are reports to be submitted on a *business entity* level or on a *country of delivery* level? For example, if there is an EU company, GR entity, and it is importing in the EU from Serbia to Hungary, from Bosnia to Croatia, from Albania to Greece, should it submit one report with the GR customs office for all the

locations where it has imported electricity or three separate reports to the customs authority of each country where it has imported electricity?

- Making available additional guidance and a Questions & Answer (Q&A) portal
  We understand that Guidance per sector is likely to be published. This is essential, given the challenges we have identified with the application of CBAM with respect to electricity imports. Indeed, some of the rules do not take into account sufficiently well the way electricity is traded across borders today.

  It would also be very useful if the Commission could open a portal or any other virtual place with a Q&A section where market participants could submit questions on an ongoing basis and where feedback is made public. We already have positive experience with such a Q&A portal set up by the Agency for the Cooperation of Energy Regulators (ACER) with respect to the implementation of the reporting requirements under the Regulation for Energy Market Integrity and Transparency (REMIT), for instance.

  Such Guidance and Q&A facility should be made available as a matter of priority, given the tight implementation timeline with the first reports due in six months.

- Penalties
  The penalties for incorrect reporting during the transitional period are significant. We are concerned that since there is insufficient detail and no guidance provided yet, incorrect reports may be submitted due to lack of proper understanding of the requirements. Article 9 allows for updates of submitted reports, especially for the first two reports, but if there is a misunderstanding on the declarant's side, and the declarant is not aware of that, that may result in a penalty.

  At the same time, there is no mechanism through which mistakes could be flagged for correction during the transitional period, which is meant to be a learning experience both for the Commission and the reporting parties - instead, penalties will apply directly.

  Therefore, we propose that during the transitional report no penalty should be imposed prior to the Commission flagging an issue and requesting an update to a report. Should, however, the Commission decide to proceed with the suggested penalties regime, we request that the level of the penalties is reduced substantially.

- Use of energy attribute certificates
  CBAM does not make a reference to energy attribute certificates such as guarantees of origin (GoOs) as a mechanism for demonstrating the origin of the imported electricity. In our view such instruments should be given further

consideration, as that could address some of the challenges with CBAM implementation. In addition, it could encourage the development of GoO schemes in neighbouring markets, which would be beneficial for the growth of renewable energy.