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How ITP Energised can help you prepare for ETS Phase 4

Free Allocation of Allowances



EU ETS Phase 4 Briefing Note

Introduction

The revised **EU ETS Directive (2018/410)** implements Phase 4 of the EU ETS, which runs from 2021-2030 and will drive EU target emissions reduction through a mix of interlinked measures.

Operators wishing to obtain an allocation of free allowances under Phase 4 must take urgent action to apply to the competent authority by **30th May 2019**.

The ITPenergised team have been involved with the ETS since the run-up to Phase 1 of the scheme and have supported operators and regulators with a wide range of issues covering numerous industries in the last two decades. We are well placed to support you with preparation of your application for free allowances under Phase 4 and any other ETS issues arising.

Phase 4 Free Allocation of Allowances

Under EU ETS Phase 4, operators of eligible installations can apply for an allocation of free allowances¹. There will be two rounds of free allowance allocation under Phase 4 of the EU ETS, each lasting five years (2021-2025 and 2026-2030). The free allocations for these periods will be based on operator's historical activity levels from the periods 2014-18 and 2019-2023 respectively.

The European Commission Regulation on "Transitional Union-wide rules for harmonised free allocation of emission allowances pursuant to Article 10a of the EU ETS Directive" (known as the Free Allocation Rules, or FAR) sets out the approach to coherent implementation of the allocation methodology for Phase 4 of the EU ETS. The FAR are currently in draft form but contain important directions for operators with installations qualifying under the ETS.

Application for Free Allowances

Unlike Phase 3 of the EU ETS, under Phase 4 the historical activity level data submitted must be verified by an independent 3rd party verifier. The application for free allowances must include the following:

- a baseline data report;
- a verification report (produced by the verifier); and
- the Monitoring Methodology Plan (MMP) used for the above reports, unless it has already been approved by the competent authority (CA).

¹ The only activities not eligible for free allowances are electricity generators and installations for the capture and pipelines for the transport of, or to storage sites for, carbon dioxide.

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The MMP should be approved by the CA; however, due to timing constraints for the application process, MMPs must be validated by an approved verifier before submission to check compliance with the FAR.

Details of the minimum content required for the baseline data report and the MMP are provided in Annex IV and Annex VI of the FAR respectively. The Commission has also provided templates for both documents.

Carbon Leakage List (CLL)

The CLL sets out which activities qualifying under the EU ETS are considered at risk of businesses transferring production to other countries with laxer emission constraints. Activities listed on the CLL receive 100% of the free allocation of allowances under Phase 4 in contrast to those not on the list, who start with 30% of their free allocation in 2021, reducing to 0% by 2030.

The number of activities identified as being at risk of carbon leakage has reduced in Phase 4. Crucially for the Oil and Gas sector, extraction of oil is on the new CLL but extraction of natural gas (including condensate) is not.

Under article 10(3) of the FAR, historical activity level data is required to be split out to align with qualifying activity (i.e. what energy is used for extraction of gas and what energy is used for extraction of oil) by NACE codes. This is a critical and potentially highly quantitative area to manage when applying for free allowances, but details of how to perform this split have not yet been provided by OPRED. Activities which can be undertaken to progress the application prior to guidance on this issue are listed below in the “What can Operators do?” section.

Deadline for Applications

According to the draft FAR, in order to receive free allocation, the operator must submit an application for free allocation by **30th May 2019**. There are twin challenges of completing the application materials and securing the third-party verification by this date.

Implications of missing the application deadline

If a satisfactorily verified application is not received by the deadline, the installation will not be entitled to receive a free allocation for the first period (2021-2025) of Phase 4. In this situation, all required allowances would have to be purchased on the free market. The cost of traded CO₂ in March 2019 was approximately €22/tonne.

What can Operators do?

Whilst some important aspects of the process for applying for free allocations under Phase 4 of the EU ETS are to be decided, with the deadline for applications rapidly approaching it is crucial for operators to get the process underway.

Key steps which can be undertaken whilst awaiting further guidance and final issue of the FAR include understanding the equipment which must be included in the historical activity level

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data for free allowances; developing your data collection process and identifying any potential data gaps; engaging a verifier; and starting work on the MMP.

Our Support to You

ITP Energised can provide support to your organisation on the EU ETS and your application for free allowances under Phase 4 of the scheme with:

- Data gathering
- Calculation of sub-installation split by NACE code, if required
- Completion of Baseline Data Templates
- Preparation of Monitoring Methodology Plans
- Administrative and technical support through the verification process
- Liaison with competent authorities on outstanding guidance

Selected ETS Experience

The ITP Energised team were involved in providing support to SEPA prior to Phase 1 of the scheme, including development of Monitoring, Reporting and Verification (MRV) reporting templates, and since that time have been involved in the full range of ETS activities, including:

- Preparing ETS permit applications
- Preparing applications for free allowances under the New Entrants Reserve process
- Managing permits on behalf of operators
 - preparation of notifications, and variations
 - preparing activity change assessments
 - dealing with improvement reports
 - preparing Significant Capacity Extension / Reduction applications
 - leading the verification process
 - cessation of operation / transfer of permit to new owner
- Representing operators in meetings with the CA

This support has been provided to a number of sectors including the following:

- Onshore and Offshore Oil and Gas Installations
- Food and Drink
- Power Generation
- Pharmaceutical
- UK Regulators

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