

EU ETS and shipping

The EU has published its update to the green deal, known as “Fit for 55” in reference to the 55% reduction in carbon emissions targeted for 2030. The proposals are intended to enable the acceleration of greenhouse gas emission reductions in the next decade and combine: application of emissions trading to new sectors and a tightening of the existing EU Emissions Trading System (ETS); increased use of renewable energy; greater energy efficiency; a faster roll-out of low emission transport modes and the infrastructure and fuels to support them; an alignment of taxation policies with the European Green Deal objectives; measures to prevent carbon leakage; and tools to preserve and grow our natural carbon sinks.

The “Fit for 55” proposals impact the shipping industry in a number of ways. For example, the FuelEU Maritime Initiative sets a limit of greenhouse gas emissions from ships calling at EU ports to promote the use of sustainable maritime fuels and zero-emission technologies. In addition, as expected, the proposals seek to extend the ambit of the EU ETS to include maritime transport.

What is the EU ETS?

Established in 2005, the EU ETS was the first emissions trading system in the world and remains the largest greenhouse gas emissions trading system across multiple countries and multiple sectors. It operates as a cap and trade system: a maximum amount of allowances is available in the scheme and these are allocated to participants either via free allowances or auctions, where participants purchase allowances. If the allowances which a particular participant has is insufficient to meet its needs, then it has a choice: to reduce carbon emissions to within its allowances or to purchase further allowances which are traded on a secondary market.

The availability of free allowances depends on the industry the participant is involved in: in the power sector, there are generally not any free allowances available, but in aviation, to aid the transition to a low carbon economy, the industry receive the majority of their allowances for free.

As the UK has now left the EU, the UK's participation in EU ETS has ended. Instead, the UK has introduced its own emissions trading scheme, the UK ETS, although at present this only covers the power and aviation industries. However, the Department for Transport have indicated that they are considering expanding the UK scheme to include shipping, although no firm decision has been taken on this.¹

Shipping and the EU ETS

Shipping has not, historically, been included in the EU ETS, but the draft legislation released on 14 July 2021 as part of the revised green deal changes that, including maritime emissions within the scheme. The current proposals are as follows:

- The industry will become incrementally subject to the EU ETS, with shipping companies being required to surrender allowances equivalent to the following amounts in relation to

ships above 5,000 GT which call at EU ports:

- 20 % of verified emissions reported for 2023;
- 45 % of verified emissions reported for 2024;
- 70 % of verified emissions reported for 2025; and
- 100 % of verified emissions reported for 2026 and each year thereafter.

- It is not just intra-EU voyages which are used to calculate the amount of verified emissions: 50% of emissions from voyages which start or end outside of the EU will be caught, as well as 100% of emissions from intra-EU voyages.
- The EU ETS will apply to ships calling at EU ports, regardless of the flag that they fly, or where the owner of that ship is incorporated. Member States will be responsible for administering the scheme for shipping companies incorporated in that jurisdiction. For shipping

¹ (Shipping being considered for UK emissions trading scheme, minister confirms :: Lloyd's List (informa.com))

companies caught under the EU ETS which are not incorporated in a Member State (a Non-EU Shipping Company), administration of the scheme will be the responsibility of the Member State that the Non-EU Shipping Company visits most frequently in a two year period, or the first port a Non-EU Shipping Company visits if it has not made any voyages within the EU in the previous two years.

- The ambit of the Innovation Fund (funded with proceeds of auctioned allowances) will be extended to support investments to decarbonise the maritime transport sector.
- A penalty for non-compliance with the EU ETS scheme, in the form of an expulsion order will be introduced. Where a shipping company has failed to surrender allowances for two or more consecutive reporting periods, an expulsion order can be issued against ships which it is responsible for. An expulsion order can lead to ships being detained by the Member State the ship is flagged in and denied entry into a port under the jurisdiction of a Member State (other than the flag state).

These proposals will need to be formally adopted before the amendments to the current EU ETS legislation take effect and so there could be further changes to the draft legislation. However, as the proposals envisage shipping being included within the EU ETS by 2023, this suggests that the EU does not intend to lose momentum on its decarbonisation strategy.

Who will pay?

The cost of including shipping in the EU ETS will be significant for industry: the price of CO₂ has risen sharply over the last few months, with prices expected to increase further. The ratcheting up of the amount of maritime emissions to be included in the scheme will mean that shipping will have a gradual introduction to the cost this will entail, but even from the outset of the scheme, these costs, plus the administrative costs of being involved with the scheme, may be onerous. How these costs will be allocated between ship owners, operators and consumers remains to be seen.

Decarbonisation

Potential inclusion of shipping in the EU ETS is a clear sign of the importance which the EU has placed on decarbonising the industry. Ship-owners will have to navigate involvement in the scheme over the coming years, and the associated requirements and costs placed upon them, as well as the other raft of sustainability provisions which are being introduced. Including the FuelEU Maritime Initiative, and at IMO level, initiatives such as the Energy Efficient Existing Ship Index (EEXI), which was adopted last month and is due to come into force in 2022, for further information on this and other aspects of sustainability in shipping, see: [Climate change and sustainability disputes: Transport sector perspectives | Global law firm | Norton Rose Fulbright](#).

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