Draft comments from the Confederation of Swedish Enterprise regarding the upcoming 2040 climate target and policy architecture

In February 2024, the European Commission published a communication on the EU's climate targets for 2040. Based on an impact assessment, the Commission has recommended a target of a 90 percent net reduction in GHG emissions by 2040 compared to 1990. According to the Commission, the communication opens a political debate on the way forward for EU and includes a recommendation for the next Commission to take forward as a legislative proposal to incorporate in the European Climate Law. Furthermore, the Commission President Ursula von der Leyen stated in the political guidelines for the Commission 2024 – 2029 that the 90% target for 2040 will be proposed by the Commission to be enshrined in the Climate Law. The Commission also recently published information about an upcoming call for evidence concerning a European Climate Law amendment scheduled to be proposed in Q1 2025.

The Confederation of Swedish Enterprise fully supports the ambition of climate neutrality by 2050 and the goal of net emission reductions of 55 percent by 2030 compared to 1990 level. We also welcome that the Commission initiates an early process to establish an additional ambitious and intermediate climate target for 2040, and firmly believe that the primary focus of 2040 climate policy should be to remove GHG emissions rather than an overreliance of compensating them. Swedish and European companies are well-placed to lead the transition efforts but also require the necessary conditions to accelerate their ambitions while preserving or enhancing competitiveness. While setting ambitious targets for 2040 is essential, they alone are insufficient. Enabling policy will be crucial to provide the European business with a strong and stable framework for competitive decarbonization.

Below, the Confederation of Enterprise lists the most essential policy areas and proposals that would contribute to creating a 2040 climate target architecture that will provide some of the necessary prerequisites for the business community to fully contribute to meeting the upcoming climate target.

Emission Targets and Carbon Pricing

The EU has, with the Fit for 55 package established a very ambitious climate policy. In order to achieve net zero by 2050 and to reach an ambitious interim target for 2040, the EU's climate policy need to continue to evolve and safeguard competitiveness for European businesses and a cost-efficient framework for carbon pricing also after 2030. Starting from the currently applicable EU legislation concerning EU climate targets and emissions pricing, the Confederation of Swedish Enterprise has arrived at several policy conclusions for EU emission targets and carbon pricing after 2030.

SUPPORT AMBITIOUS EU CLIMATE TARGET FOR 2040

The Confederation of Swedish Enterprise fully support the European climate ambitions to achieve climate neutrality by 2050, and the intermediate targets set up within Fit-for-55. The Confederation of Swedish Enterprise further supports a continued high ambition for the net greenhouse gas emissions target for 2040, and firmly believe that cost-efficient carbon pricing should continue to be a main feature of the EU's toolbox to reduce emissions.

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EMISSION REDUCTION FIRST PRINCIPLE

The primary focus of 2040 climate policy should be to remove GHG emissions as soon as possible, rather than an overreliance of compensating them in other ways. Complementary efforts such as increased natural and technical carbon sinks are small compared to the large fossil emissions in the union. Moreover, efforts to increase natural and technical carbon sinks may come with high direct and indirect costs.

DEVELOPMENT OF ETS 1 AND 2 TRAJECTORIES AFTER 2030 NEED TO BE ADAPTED TO UPCOMING 2040 TARGET

The EU ETS 1 and 2 will continue to be key policy instruments to reduce emissions and their future development and trajectory after 2030 needs to be clarified through political decisions during the 2024-2029 mandate. Several factors need to be considered when establishing the ETS 1 and ETS 2 development and trajectory after 2030. The electrification of e.g. the transport sector will likely allocate emissions from the ESR and ETS 2 sectors to ETS 1, putting more pressure on the ETS 1 sectors. Going forward, EU legislators need to take utmost consideration of the competitiveness of European business in general, and the EU energy intensive industry subjected to international competition in particular, when designing its ETS policies for 2030 and onwards. During the 2024-2029 political cycle, the EU ETS 1 and 2 development and trajectories between 2030 and 2040 need to be legally established and adapted to the trajectory of the upcoming 2040 climate target and the 2050 climate neutrality target. In addition, the EU Commission must already during the next mandate start the discussion on how remaining GHG emissions in hard-to-abate sectors should be handled and how the functioning of the emission trading system might be impacted when the allocation of new emission allowances eventually become too sparse to allow for a liquid allowance market.

ADAPTING THE ETS 2 AND ESR TARGET

After 2030, ETS 2 should ideally be developed to a fully functioning emissions trading scheme, without a price stability mechanism, thus removing the need for overlapping policy instruments at EU and at national level (such as e.g. taxes and reduction obligation). Each Member State have a responsibility to reach net-zero emissions and the 2040 ESR target should either be removed or based on increased convergence of Member States commitments to strengthen the EU's path to climate neutrality. Either way, emissions that are in the scope of the ETS should in a future policy framework not simultaneously be in the scope of the ESR target. It should be contemplated whether effort sharing among Member States in the transport, building and additional sectors after 2030 – sectors that are also covered by the ETS 2 between 2027-2030 – is better achieved through already established forms of dedicated funding such as e.g. the Social Climate Fund.

COMPREHENSIVE APPROACH TO INDUSTRIAL CARBON MANAGEMENT

The Confederation of Swedish Enterprise welcomes that the EU Commission in its recent communication acknowledges and strategically addresses the topic of industrial carbon management, which is an important building block in achieving the EU's net neutrality target and the upcoming intermediate target for 2040. Industrial carbon management is an important tool for several hard-to-abate sectors. However, the Confederation of Swedish Enterprise also advocates for a more comprehensive approach to the issues addressed in the Commission's communication on Industrial carbon management. Carbon atoms should not only be perceived as something negative that needs to be phased out. For industrial processes, carbon atoms are often an essential input that cannot be replaced, while emissions of CO_2 to the atmosphere of course needs to be avoided. Carbon atoms are a crucial component in several goods, such as plastics, textile, rubber and sustainable fuels.

DEVELOPMENT OF CBAM

Several uncertainties surround the CBAM, including its ability to achieve its stated objectives, the administrative burden it may impose on EU importers, challenges in accurately measuring emissions in third countries, and the potential for trade policy conflicts. Therefore, the EU must closely monitor the impacts and effectiveness of the CBAM to ensure its objectives are met without unintentionally incentivizing offshoring of production and undermining its climate goals. In addition, it is crucial to maintain the competitiveness of European products in third markets. The definition and eventual implementation of a WTO-compatible export support scheme is crucial to maintain the competitiveness of European companies exporting products in the ETS and CBAM scope to third markets. One such measure that could be explored is maintaining full free allocation for the part of the product which is destined for export to third markets.

Concerning the expansion of CBAM scope, the Confederation of Swedish Enterprise considers that the CBAM in principle should ideally be extended to all sectors where there is a price on carbon in the EU, with the potential exception of sectors where products are non-tradeable. Therefore, from the point of view of achieving the purpose of CBAM (avoiding carbon leakage) CBAM should correspond to ETS. Without such an expansion of CBAM, more advanced sectors of the economy will risk carbon leakage. However, there are technical and practical constraints in such an endeavor, as it is very hard to estimate the carbon emitted by advanced products with many components, such as e.g. vehicles and machinery. New technology, perhaps AI-enabled, and new data might alleviate the problem but with today's methodology this is nearly impossible. If the EU nonetheless proceeds, the Union risks introducing a system that might become very administratively burdensome and risks being protectionist, as we might charge CBAM fees above their factual corresponding ETS-costs. Therefore, the Union should proceed with caution analyzing potential market consequences, and carefully assess the cost-benefit ratio step by step.

Energy policy

The European Commission has as previously mentioned, stated in the communication regarding the 2040 climate target and its impact assessment that a technology neutral approach needs to be taken to power generation as all types of low carbon technologies will be needed to achieve a fully decarbonized power system by 2040 if 90 % emission reduction are to be achieved. This approach by the Commission is much welcomed and fully supported by the Confederation of Swedish Enterprises. In addition, the Confederation outlines below several principles and policies that should guide the EU's energy policy approach during the next policy cycle to enhance the possibilities of reaching an ambitious climate target for 2040:

PRINCIPLES OF COST-EFFICIENCY AND A SYSTEMIC APPROACH SHOULD GUIDE EU ENERGY POLICY

EU energy policy under the next political cycle move more towards a systemic approach where all types of prerequisites - power generation, the grid infrastructure, the need for dispatchable and flexible capacity and the need for interconnector build-out – affect each other. European energy policy should therefore move towards a more comprehensive and coherent policy that encompasses the overall need and cost for the energy system. One of the main focuses for EU energy policy going forward needs to be to contribute to building an electricity system where the total cost for the overall electricity system is internationally competitive.

TECHNOLOGY NEUTRAL APPROACH TO ELECTRICITY GENERATION

A European transition to increased and decarbonized electricity production is required for the EU to become climate neutral by 2050 and to be on track for the intermediate 2040 target. Policies for e.g. energy efficiency, nuclear technologies and renewable electricity must serve to facilitate this transition. Instead of setting targets for specific types of power sources, the objective of EU energy policy should be to, through a technology neutral approach, contribute to a significant increase in a reliable and resilient supply of decarbonized power generation at competitive costs. The EU should in this context strive for an indicative target of 100 % decarbonized electricity generation by 2040, instead of showing preference for specific renewable energy technologies.

A SINGLE MARKET FOR ELECTRICITY MAY REQUIRE STABILITY PACT

A prerequisite for a strengthened internal market for electricity going forward is that Member States respect the principle that each Member State has a responsibility to ensure a resilient and reliable electricity system. The ambition to strengthen the functioning of the European electricity system through interconnectors should therefore also include incentives for individual Member States to assume responsibility to build electricity systems that contribute to the provision of wider system benefits and stability for the European electricity market. Such incentives or requirements at national level could include areas such as ensuring sufficient dispatchable power generation in connected bidding-zones to meet expected demand and ensuring more optimal design of connected bidding-zones to minimize structural bottle necks.

ENSURE POLICY COHERENCE IN THE TRANSITION TO NET ZERO

While the EU's electricity generation is expected to increase substantially in order to meet net zero targets, the EU has in parallel established that Member States collectively shall ensure a reduction of final energy consumption of at least 11,7 % by 2030 compared to 2020. Going forward, the EU and its Member States need to ensure policy coherence and that energy efficiency targets do not hinder the investments in electrification necessary to reduce emissions and increase growth.

Permitting Policy

The permitting system is of considerable strategic importance to the EU, to be able to achieve the green transition competitively and address the challenges we face. The time it takes to obtain permits undermine a willingness to invest in Europe. Investors want to know that they will see a return on their investments, but unfortunately the current EU and Member State system is often too inefficient and unpredictable.

MORE EFFICIENT AND TRANSPARENT PERMITTING PROCESSES

More efficient and transparent permitting processes are crucial to reach the EU target for climate neutrality by 2050, and to ensure a stable investment framework that fosters competitiveness and delivers abundant and affordable fossil-free and/or low-carbon energy to EU industry and households. Unpredictable and overly complex processes with long lead times for obtaining permits are currently acting as obstacles to EU inward investment, which in turn is undermining the EU's ability to compete on the global stage.

POLICY COHERENCE NEEDED BETWEEN THE EU'S AND MEMBER STATES' PERMITTING PROVISIONS

To speed up permitting process for renewable energy projects, net zero technologies and raw materials the EU has introduced new rules and measures targeting specific technologies and types of projects (e.g. RED III, NZIA, CRMA etc.). During the next political cycle, the Commission should aim to improve the general requirements and procedures for permitting, rather than promote certain industries and technologies. Value-chains in the economy are almost always complex and dependent on many different suppliers of technologies and input goods, and only promoting a selection of those suppliers will inevitably lead supply chain inefficiencies and distortions of competition. The ambition should rather be to create better conditions for businesses in general to promote competitiveness within the EU. With the current fast-track and technology specific approach to permitting policy by the EU, the substantive rules of underlying directives for permit evaluation, such as e.g. the Industrial Emissions Directive (IED) and the Water Framework Directive (WFD) have at the same time become more prescriptive or remained unchanged. Such substantive rules for permitting, and the Member State harmonized implementation and enforcement of the rules, are however even more important in terms of providing an efficient and holistic permitting framework. A more systemic approach to streamline the permitting policy needs to be undertaken by the next Commission to ensure policy coherence between different legislations affecting the prerequisites for Member State's permitting processes with the aim to reduce overlap and cut red tape.

Financing and policy for a decarbonized economy

Competitive and technology neutral framework conditions for businesses are fundamental policy prerequisites to support innovation and to attract private capital and investment. The Confederation of Swedish Enterprise outlines below several principles and policies that should guide the EU's policy approach to financing and industrial policy for a net zero economy during the next policy cycle in order to enhance the possibilities of reaching an ambitious climate target for 2040:

LONG-TERM COMPETITIVENESS THROUGH GOOD FRAMEWORK CONDITIONS FOR BUSINESSES

The Confederation of Swedish Enterprise advocates for measures that promote businesses' competitiveness in general, rather than measures directed at specific market participants. As a point of departure, the state should not act as a venture capitalist but instead strive to create stable and favorable prerequisites for private investments.

Public measures may however be warranted in the case of market failures. There may be cases where companies are not fully incentivized to consider externalities, such as e.g. investments in research or climate measures. The same situation may occur in areas where the state has a particular responsibility to provide fundamental societal services such as e.g. infrastructure.

PUBLIC MEASURES FOR THE ENERGY SECTOR

The availability of a sufficient and reliable supply of energy at a competitive cost is a fundamental factor for the competitiveness of Swedish and European business in the long term, and a key enabler for the green transition. The state has a particular responsibility for investments in the grid infrastructure, just as it has in other types of infrastructure.

When it comes to the generation of electricity, the state should exercise the same caution as for other measures more specifically directed at individual market participants to avoid market distortions. The state should primarily focus on ensuring stable and favorable prerequisites for private investments. There may however occur market failures where particular qualities of the different types of electricity production are not valued appropriately by the market. Some power sources, such as hydropower and nuclear power, are dispatchable and provide the electricity system with positive externalities that other power sources cannot directly deliver. This could motivate public measures when necessary for additional investments to materialize.

PRIORITISE REALLOCTAING EXISTING FUNDS RATHER THAN SEEKING NEW MEMBER STATE FUNDING

For an extended period, the EU has advocated for harmonized strategies in financing, favoring collaborative funding mechanisms over national state aid, with the aim of mitigating the risk of economic disparities. However, in times of strained public finances and unallocated EU funding, Member States are reluctant to allocate new funds to additional funding schemes. Instead, the Commission should priorities and reallocate existing funding.

IF IMPLEMENTED – STATE AID OR EU FUNDING SHOULD BE MOBILIZED WITH CARE TO MITIGATE DISTORITIONS

The EU's ability to mobilize more private investments in necessary energy production capacity and essential infrastructure will be central to reaching the Net-Zero target. Measures that improve framework conditions for such private investments are fundamental and need to be the primary focus. Next to private finances, targeted public funding may be necessary to de-risk some of the investments needed to substantially increase capacities and infrastructures. An efficient energy system build-out could be required to be supported by state aid or EU funding. If state aid or EU funding measures are implemented, they should be mobilised with care to mitigate distortions of competition within the single market. State aid measures should be targeted, time-limited and only address market failures. EU funding should be time-limited, based on competition, excellence and ex-post evaluated.

Leading by example

The EU has emerged as a frontrunner in climate action, with initiatives like EU ETS, the Green Deal, Fitfor55, and RepowerEU. With a goal to become the first climate-neutral continent by 2050, the EU is committed to fostering a sustainable and resilient future. Maintaining its leadership role in climate policy is crucial for enhancing European competitiveness and making substantial contributions to the global fight against climate change. However, this leadership requires a strategic approach that prioritizes cost-effective measures and facilitates policies supporting education, skill development, research and development, as well as critical infrastructure such as electricity grids and digital networks.

CONTINUED EUROPEAN LEADERSHIP

The EU's steadfast commitment to spearheading climate policy is essential for nurturing both economic competitiveness and environmental sustainability. This leadership must hinge on political continuity in the transition to net zero, complemented by the implementation of cost-effective tools and measures, as well as ensuring social sustainability and legitimacy. Policies aimed at promoting education and capacity development, research and development, and robust infrastructure like electric grids and digital networks are pivotal components of a sustainable climate strategy. By harnessing these elements, the EU can cultivate a synergistic approach that not only benefits its Member States but also establishes a global standard for effective climate governance.

ADVOCATING INCREASED GLOBAL AMBITIONS

In addition to leading regionally, the EU must continue to actively champion heightened global ambitions in climate action. Acknowledging the interconnected nature of climate challenges, the EU should assume a pivotal role in urging nations worldwide to embrace more ambitious climate goals. As the world endeavors to achieve climate neutrality and adapts to the challenges posed by a changing climate, the EU's advocacy for broader global efforts becomes increasingly vital. By leveraging diplomatic channels and collaborative initiatives, the EU can cultivate a shared commitment to combating climate change on a global scale.

STRENGTHENING INTERNATIONAL CLIMATE FINANCING

Recognizing the reliance of many least developed countries on conditional Nationally Determined Contributions (NDCs) supported by promised financial aid, the EU should enhance existing financing mechanisms. It is crucial to promptly fulfill previously set climate financing targets, ensuring that financial commitments translate into tangible support for vulnerable nations. By strengthening financial arrangements, the EU can demonstrate its dedication to global solidarity in addressing challenges related to climate change.

ADVOCATING GLOBAL CO2 FINANCING

As part of its climate leadership, the EU should persist in promoting the widespread implementation of global carbon pricing. A harmonized global framework for CO2 pricing would create a level playing field for businesses, discouraging carbon-intensive practices, and encouraging sustainable alternatives. However, a global carbon price must be high enough to generate substantial change. Moreover, it should be complemented with a market stability reserve to achieve transparency and long-term stability to promote investments. Transitioning from substantial subsidy packages, such as the Inflation Reduction Act (IRA), towards a system of emission pricing will not only foster economic efficiency but also drive innovation and technological advancements in the quest for a carbon-neutral future.

Through partnerships and international cooperation, the EU leverages its influence to promote sustainable practices and the transition to clean energy on a global scale and is actively engaged in shaping global policies for greenhouse gas (GHG) pricing. The EU is a partner in the Global Carbon Pricing Challenge (GCPC), an international initiative aiming to cover 60% of global emissions with carbon pricing by 2030.

In conclusion, the EU's commitment to advancing climate policies is not only a regional necessity but a global imperative. By championing cost-effective measures, encouraging global cooperation, strengthening financial commitments, and promoting emissions pricing, the EU can lead the way towards a sustainable and resilient future for our planet. Achieving a carbon-neutral planet requires collaborative efforts, and the EU must continue to be at the forefront of this transformative endeavor.

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