

Financing REPowerEU: Alternatives to the MSR

The REPowerEU Plan contains important proposals to reduce dependency on Russian fossil fuels. We support the Czech Presidency in reaching an agreement on the REPowerEU-proposal as soon as possible. In order to do so without harming our climate ambitions, it is of the utmost importance to **preserve the integrity of the ETS Market Stability Reserve**.

Financing any part of the subsidies for REPowerEU from **auctioning allowances from the MSR undermines the hard-earned credibility of the EU Emission Trading System**, even at low volumes. The EU ETS is the cornerstone of EU climate policy. Using the MSR to finance budgetary deficits sets an **undesired precedent** of auctioning allowances that are otherwise cancelled. This **risks an increase of carbon emissions**, as allowances may well be used by the market prior to potential reabsorption into the MSR. In addition, auctioning through the MSR puts a downward pressure on the ETS price. This effect was also observed after the publication of this proposal and leads to a lower overall amount of funding available at EU and Member State level for the transition away from fossil fuels.

There have been in-depth discussions about **using allowances from the Innovation Fund to finance the RRF**. The benefits of financing through the Innovation Fund over auctioning MSR allowances is well outlined by the Danish non-paper. In case the Innovation Fund would be too small to achieve the policy objectives of the Fund, **the amount of subsidies could be lowered accordingly**, to a level that leaves sufficient funding in the Innovation Fund as well as finding means to finance REPowerEU objectives.

Frontloading of ETS auctioning through the auction calendar

Financing REPowerEU subsidies could also be done by **frontloading the auctioning of ETS allowances**. Frontloading allowances would lead to similar financial flows as through MSR auctioning, as it shifts auction volume over time, while avoiding an undesired precedent and the risk of increasing emissions. This proposal has three major advantages compared to auctioning through the MSR:

1. Allowances to be auctioned are sourced from within the ETS cap, leaving the integrity of the MSR and ETS intact.
2. No increase in emissions is to be expected as the cumulative available allowances is not changed.
3. The total amount of funding available for the transition away from fossil fuels is not lowered through price effects.

ETS allowances that are scheduled to be auctioned in the period 2027-2030 would instead be auctioned already in the period 2023-2026. The auction calendar would be adjusted accordingly. The figure below shows how the cap would evolve in the coming years, taking €10 billion in subsidies. This is generated through auctioning 125 million ETS allowances in 2023-2026, 50% of which come from frontloading general ETS allowances and 50% from the Innovation Fund. As illustrated, this would entail a limited increase of yearly allowance auctioning, which is compensated in later years.

