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10^ο ΔΙΕΘΝΕΣ ΣΥΝΕΔΡΙΟ ΝΑΥΤΙΚΟΥ ΔΙΚΑΙΟΥ

Η προστασία της ναυτιλιακής επιχείρησης

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The proposed extension of the EU-ETS to shipping - BIMCO´s ETS - allowances (ETSA) clause for time charter parties 2022 filling a legal gap

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1 Introduction

1.1 Background

On 14 July 2021 the Commission of the European Union (EU Commission) proposed to include shipping to the current European Union Emission Trading System (EU ETS). The inclusion will take place by amendments to the 2003 ETS-Directive (hereinafter EU ETS 2021 proposal),¹ as well as to the 2015 Regulation on monitoring, reporting and verification of carbon dioxide emissions from maritime transport, (hereinafter the MRV-regulation)² which are the two main legal instruments governing the inclusion of shipping to the EU-ETS.

On 8 February 2023 the Council and the Parliament reached an agreement on the final text for the extension of the EU-ETS through amendments to the 2003 EU ETS-directive, hereinafter the 2023 agreement.³

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1. Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation (EU) 2015/757. COM(2021) 551 final 2021/0211 (COD).
 2. Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from maritime transport, and amending Directive 2009/16/EC.
 3. The whole document (Interinstitutional Files 2021/0211 (COD) 2021/0202 (COD)) from the General Secretariat of the Council to the Delegations, 6210/23 is available on-line.)

Although embracing the idea of expanding the EU ETS to shipping, both the EU Parliament⁴ and the EU Council⁵ have proposed changes to the proposal, particularly related to the scope provision. Despite some discussion on the details, all three institutions agree that an extension of the EU ETS to shipping is a necessary step in order to fulfil the emission reduction target of the “Fit for 55” package.⁶ The reason is that shipping, due to its large dependence on fossil fuels, is considered a *major polluter*: Global shipping is estimated to be responsible for around 2-3 percent of total global greenhouse gas emissions. The situation is even worse at EU level where shipping accounts for 13% of emissions from transport.⁷ According to a study from the International Maritime Organisation (IMO); the Fourth IMO GHG Study 2020, emissions from shipping will continue to increase:⁸ Depending on the development in world markets related to the Covid19 pandemic, emissions are projected to increase from about 90% of 2008 emissions in 2018 to 90-130% of 2008 emissions by 2050.⁹ When the current EU ETS legislation was revised in 2018, it was predicted to deliver a 43% reduction of EU ETS emissions by 2030 compared to 2005. This would have been coherent with the previous target of at least 40% reduction by 2030 compared to 1990.¹⁰ However, according to the Commission, if the legislation would have remained unchanged the sectors covered by the EU ETS would achieve only a reduction of 51% compared with 2005, which is not satisfactory considering the new target of at least 55% reduction compared to 1990 levels. To reach the latter goal, the sectors covered by the EU ETS need an emission reduction of 61%.¹¹ If shipping was

4. Amendments adopted by the European Parliament on 22 June 2022 on the proposal for a directive of the European Parliament and of the Council amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union, Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and Regulation (EU) 2015/757 (COM(2021)0551 - C9-0318/2021 - 2021/0211(COD))(1)

5. See the proposed changes by the Council to the 2003 directive of 30 July 2022: Dossier interinstitutionnel: 2021/0211(COD) 10796/22 pdf (europa.eu) p. 13. (Accessed 15 November 2022).

6. COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS EMPTY ‘Fit for 55’: delivering the EU’s 2030 Climate Target on the way to climate neutrality. COM(2021) 550 final.

7. Ibid.

8. Smazzare, Reduction of GHG Emissions From Ships: Fourth IMO GHG Study 2020.

9. Ibid. at p. 6.

10. Ibid. p. 1.

11. Ibid.

left outside, this would be difficult to attain.¹² The EU ETS 2021 proposal accordingly contain the needed regulatory changes to include emissions from shipping to the system.

This Chapter outlines the *proposed* inclusion of shipping to the European Union's Emissions Trading System (EU-ETS) as of November 2022, as well as BIMCO's ETS – emission trading scheme allowance clause for Time Charter Parties 2022, which covers a legal gap on the very important question on who the *end payer* of the emission allowances under the proposed system will be.¹³ According to the present proposal, the *Shipping Company*, which is defined as the Shipowner or any other person that has assumed responsibility for the operation of the ship from the Shipowner, is responsible for compliance. However, according to the proposal and in line with the *polluter pays principle*, the Shipping Company could, by means of a contractual arrangement, hold the entity that is directly responsible for the decisions affecting the CO₂ emissions of the ship, normally the *Charterer*, accountable for the compliance costs. BIMCO's ETS-emission trading scheme allowance (ETSA) clause for Time Charter Parties 2022 offers such a contractual arrangement. The clause will be outlined below (3), following an introduction to the ETS system (1.2) and its extension to shipping (2).

1.2 The EU Emissions Trading System (ETS)

The EU Emissions Trading System (EU ETS) is defined as a cornerstone of the EU's policy to combat climate change and is considered a key tool for reducing greenhouse gas emissions cost-effectively.¹⁴ It is the world's first major carbon market and remains the biggest one. It currently covers around 40% of the EU's greenhouse gas emissions. The main legal instrument governing the EU ETS is the *ETS-Directive on establishing a system for greenhouse gas emission allowance trading within the Union* from 2003 with its multiple amendments

12. Ibid.

13. This chapter builds on previous works by the author, in particular: Eftestøl, E. J.: "Fit for 55" and the Polluter Pays Principle. Who Pays under the proposed EU ETS for shipping? *European Transport Law* 2022 p. 111-125. See also: Eftestøl, E. J. & Ylihøjjo, E.: Paving the way for a European Emissions Trading System for shipping: EU and IMO on different paths in Soyer, B. & Tettenborn, A. (eds.), *Disruptive Technologies, Climate Change and Shipping*, Abingdon: Routledge, 2022 p. 175-193 and Eftestøl, E. J. & Ylihøjjo, E.: International Shipping - Who levels the playing field? in Basu Bal, A., Rajput, T., Argüello, G. and Langlet, D. (eds.), *Regulating Risk in Trade, Maritime Transport and Marine Environment* Brill, 2022/23 (In press).

14. COM (2021) 550 final (n1), at 2.2.

(hereinafter the ETS-Directive).¹⁵ The ETS-Directive provides a scheme for greenhouse gas emission allowances within the community, with the aim to promote reduction of greenhouse gases in a cost-effective and economically effective manner.¹⁶ It is a “cap and trade” system. This means that a cap, a maximum, is set for the total amount of certain greenhouse gases that can be emitted by the entities covered by the system.¹⁷ This maximum is reduced over a period so that the total emissions fall. Within the set maximum, the participants covered by the system can buy or receive emission allowances which they can trade with one another as needed. The fact that the total number of allowances available is capped ensures that they have a value. For the EU ETS to work it is important that the emissions can be measured, reported and verified with a high level of accuracy.

It is obligatory for the sectors covered by the directive to participate in the system. The entities subject to the ETS-Directive are named *installations* and the persons in charge are *operators*. According to the ETS-Directive art. 4 the operator of an installation needs a *permit* issued by a competent authority to legally undertake activities covered by the directive. This means that any person who operates or controls¹⁸ a stationary technical unit where the activities listed in Annex I and the emissions listed in Annex II of the ETS Directive, are carried out, needs to have a permit to perform the activity.¹⁹ The permit gives the operator allowance to emit. However, the right to emit is coupled to an obligation to surrender allowances equal to the total emissions of the installation each calendar year, within four months following the end of that year.²⁰ This means that the deadline for paying the emissions for 2023 is 30 April 2024 as an example. By surrendering allowances, the participants

15. DIRECTIVE 2003/87/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 October 2003 establishing a system for greenhouse gas emission allowance trading within the Union and amending Council Directive 96/61/EC (Consolidated).

16. Ibid. art. 1.

17. Ibid. art. 3 (e).

18. Or, if provided for in national legislation, to whom decisive economic power of the technical functioning of the installation has been delegated, see ETS-directive (n13) art. 4.

19. The greenhouse gases and activities listed in Annex I and II to the ETS-directive include: *Nitrous oxide (N2O)* from production of nitric, adipic and glyoxylic acids, *glyoxal*; *perfluorocarbons (PFCs)* from production of aluminium and *carbon dioxide (CO2)* from electricity and heat generation, energy-intensive industry sectors including oil refineries, steel works, and production of iron, aluminium, metals, cement, lime, glass, ceramics, pulp, paper, cardboard, acids and bulk organic chemicals and commercial aviation within the European Economic Area.

20. ETS-directive (n13) art 6 (e).

compensate for their emissions from the previous year, concluding that year. It is a precondition for the system to work that the operator is capable of monitoring and reporting the emitted emissions. Guidelines for monitoring and reporting emissions is provided by the Commission and ensured by the Member States.²¹

An allowance means allowance to emit *one tonne of carbon dioxide equivalent* during a specified period, which shall be valid only for the purpose of meeting the requirements of the ETS-Directive and shall be *transferable*.²² The transferability provides a right to trade the allowances and is hence a precondition for the *cap-and-trade* system to work. The total amount of allowances, “the cap” under the ETS is set by the EU and divided between the Member States.²³ Allowances can thereafter be obtained through a mixture of free allowances and allowances acquired by auction. From 2021 onwards, 57% of the allowances are auctioned.²⁴ The Member States auction their allowances in accordance with the ETS Directive chapter II and the Auctioning Regulation.²⁵

According to the European Central Bank (ECB), the price on allowances has grown from 8 euro per tonne in 2018 to *around 40 euro per tonne in 2021* and is estimated to continue growing.²⁶ Auctions are held by auction platforms. One of the auction platforms is the European Energy Exchange AG (EEX), which serves as a joint auction platform for 25 Member States and separately as auction platforms for Germany and Poland respectively.²⁷ The highest carbon price during 2022 was on August 19, at 98.01 euros per metric ton.²⁸ The Member States are responsible for keeping a *registry* to ensure the accurate accounting of the issue, holding, transfer and cancellation of allowances.²⁹ It is important that the registers are *public*.³⁰ The Member State

21. Ibid. art. 14 and 15.

22. Ibid. art. 3 (a).

23. Ibid. art. 10.

24. Ibid. art. 10 nr. 1 second para.

25. COMMISSION REGULATION (EU) No 1031/2010 of 12 November 2010 on the timing, administration and other aspects of auctioning of greenhouse gas emission allowances pursuant to Directive 2003/87/EC of the European Parliament and of the Council establishing a system for greenhouse gas emission allowances trading within the Union.

26. https://www.ecb.europa.eu/pub/economic-bulletin/focus/2021/html/ecb.ebbox202106_05-ef8ce0bc70.en.html (Accessed 05.04.2022).

27. European Energy Exchange AG (EEX) (Accessed 14.11.2022).

28. EU-ETS carbon pricing 2022 | Statista (Accessed 12.03.2023)

29. ETS-directive (n12) art 19 nr. 1.

30. ETS-directive (n13) art 19 nr. 1.

shall every year by 30 June report to the Commission on the application of the ETS-Directive and the Commission shall evaluate the system.³¹ The results are published in an annual (technical) report from the Commission. The latest report: *Application of the European Union Emission Trading Directive. Analysis of national responses under Article 21 of the EU ETS Directive in 2020* was published 25 May 2021.³² It considers the reports from all countries that have implemented the EU ETS. For the reporting year 2019 these were the 28 EU Member States, as well as Norway, Iceland and Liechtenstein, together 31 countries. The total emissions reported were approximately 1,500 Mt CO₂ (eq), which is almost 11% lower than the year before. Emissions from the 611 participating aircraft operators, with total emissions of almost 70 Mt CO₂, was however 0.7% higher than in 2018.³³

In line with the ETS Directive article 16, all countries have some form of *penalties* in place for different types of infringements. Most penalties concern *fin*es with a defined financial minimum or maximum,³⁴ but also *jail sentence* is used as a penalty.³⁵ In addition some countries provide the option to impose *penalties other than fines and jail sentences*. This can e.g., be an option to *shut down an installation* for a period.³⁶ All countries have a defined penalty for infringements such as not having a permit or not complying with permit conditions, not submitting an emission report and not monitoring in line with the approved monitoring plan. The fines for these categories are usually also higher than for other types of infringements.³⁷

31. Ibid. art 21.

32. *Ouden*es, *Machtelt*, *Iersel*, *Sjors van*, *Bystricky*, *Eliska* and *Voogt*, *Monique*: Application of the European Union Emission Trading Directive. Analysis of national responses under Article 21 of the EU ETS Directive in 2020. European Publication, 2021.

33. Ibid. p. 9.

34. The variation in fines among countries is high. Considering only defined minimum or maximum numbers larger than zero, the minimum fines range from €63 (Hungary, per day) to €75,000 (France) per infringement and the maximum ranges from €102 plus the allowance price (Liechtenstein, per tonne CO₂) to €16 million (Estonia). In some countries the size of fines also differs between the 14 types of infringements reported under Article 21. Ibid. p. 86.

35. Cyprus, Denmark, Estonia (for some infringements), Ireland, Luxembourg, Norway and Sweden (for some infringements) provide for the possibility of a jail sentence of up to 120 months for some or all types of infringements. France is the only country that has indicated a minimum jail sentence: a period of 12 months for operating without a permit or failure to comply with the conditions of the permit. Ibid.

36. In Greece the authorities have an option to shut down installations for a period between 5 to 20 days. Ibid.

37. Ibid.

2 Expanding the system to shipping

2.1 Scope: Maritime activity with an EU connection

According to the EU ETS 2021 proposal, the EU ETS will include *maritime transport activities*³⁸ for vessels calling at EU ports. The extension of the EU ETS to shipping includes a duty to *surrender allowances* as described above in 1.2. The EU ETS will cover not only intra-EU carbon emissions, but also emissions that occur *outside* the EU. This extraterritorial extension of the system rises both political and legal concerns. From a legal perspective, the question of whether the EU has *competence* to include emissions from third country vessels entering EU territory as regards CO₂ gases emitted outside the EU, arises. According to the decision of the European Union Court of Justice (EUCJ) in the ATA case “*Air Transport Association of America and Others v Secretary of State for Energy and Climate Change*” (Case C-366/10), the EU has such competence under EU law. Despite the fact that the case directly concerned the external dimension of a Directive from 2008 on including aviation to the EU ETS, the problem is parallel for shipping.³⁹ It seems also that an inclusion of CO₂ gases emitted outside the EU into the EU ETS for vessels calling at EU ports, does not violate public international law.⁴⁰

Another challenge related to the extraterritorial effect of an extension of the EU ETS to extraterritorial shipping, has been to decide *on the guiding principles for the extension*. The north-south division has been a longstanding challenge in context of the United Nations Framework Convention on Climate Change, 1992 (UNFCCC) and must also be taken into concern when introducing a mandatory emission trading system to all vessels (within the scope of the

38. See the proposed change of Article 3: “(b) ‘emissions’ means the release of greenhouse gases from sources in an installation or the release from an aircraft performing an aviation activity listed in Annex I or from ships performing a maritime transport activity listed in Annex I of the gases specified in respect of that activity, or the release of greenhouse gases corresponding to the activity referred to in Annex III;”

39. See Directive 2008/101/EC of the European Parliament and of the Council of 19 November 2008 amending Directive 2003/87/EC so as to include aviation activities in the scheme for greenhouse gas emission allowance trading within the Community. For a thorough analysis, see *De Baere, Geert and Ryngaert, Cedric*, The ECJ’s Judgment in *Air Transport Association of America* and the International Legal Context of the EU’s Climate Change Policy in *European Foreign Affairs Review* Volume 18, Issue 3, 2013, pp. 389 - 409.

40. In this direction see: *Perez, Daniel*, The Inclusion of Shipping in the EU Emissions Trading Scheme: A Legal Analysis in the Light of Public International Law (October 30, 2012). *Revista Catalana de Dret Ambiental*, Vol. III, No. 2, pp. 1-55, 2012, Ch. 3. The article is available at SSRN: <https://ssrn.com/abstract=2210858>.

system) calling at EU ports. The UNFCCC follows the principle of *Common but Differentiated Responsibilities and Capabilities*. The International Maritime Organization (IMO), however, follows the principle of “*No More Favourable Treatment*”.⁴¹ In order to comply with the praxis of the CJEU and the raised concerns related to the extraterritorial effect of the extension of the EU ETS to shipping, the Commission has chosen to follow the same guidelines as the UNFCCC and proposed a limited extension of the system: Only 50% of the emissions from voyages between a port under the jurisdiction of a Member State and a port under the jurisdiction of a third country (or the other way around) shall be included in the EU-ETS. This solution gives the third country a possibility to decide on appropriate action in respect of the other share of emissions.⁴² The solution also opens for other countries, like the US and China, to adopt similar systems.

Furthermore, the chosen scope model has caused concerns regarding *evasive port calls and delocalisation of transshipment activities outside the Union*.⁴³ The latter has been a concern from several stakeholders. Among others, the World Shipping Council (WSC) argues in a position paper on the EU ETS, that reducing the scope to intra-EU voyages would reduce the risk of *carbon leakage* and *market distortions*, making the system a stronger basis for the EU to lead on adoption of global market-based measures (MBMs) for shipping.⁴⁴ In its response to the Commission’s EU ETS 2021 proposal, the EU Council recognizes the risks mentioned above.⁴⁵ To mitigate the risks, the Council proposes to exclude from the concept of *port of call* certain stops at nonUnion

41. See: *Saiful Karim and Md S Karim*, Prevention of pollution of the marine environment from vessels: The potential and limits of the International Maritime Organisation (Springer, New York 2015). p.34

42. See the proposed article 3g on Scope of application to maritime transport activities: 1. The allocation of allowances and the application of surrender requirements in respect of maritime transport activities under the jurisdiction of a Member State and arriving at a port outside the jurisdiction of a Member State, fifty percent (50 %) of the emissions from ships performing voyage departing from a port outside the jurisdiction of a Member State and arriving at a port under the jurisdiction of a Member State, one hundred percent (100 %) of emissions from ships performing voyages departing from a port under the jurisdiction of a Member State and arriving at a port under the jurisdiction of a Member State and one hundred percent (100 %) of emissions from ships at berth in a port under the jurisdiction of a Member State.

43. EU ETS 2021 proposal (n 34) preamble at (17).

44. See: <https://www.worldshipping.org/statements/wsc-position-paper-on-eu-ets> (Accessed 07.04.2022).

45. See the proposed changes by the Council to the 2003 directive of 30 July 2002: pdf (europa.eu) p. 13. (Accessed 30. October 2022).

ports. The exclusion is targeted to ports in the Union's vicinity where the risk of evasion is the largest. According to the Council, a limit of *300 nautical miles* constitutes a proportionate response to evasive behavior, balancing the additional burden and the risk of evasion. Furthermore, the exclusion from the concept of port of call only targets ports where transshipment of containers, measured in twenty-four equivalent unite, exceeds 65% of the container traffic of that port during the most recent 12 month period for the port. The Commission shall by 31 December establish a list of the ports.⁴⁶

2.2 Phased in from 2023/24?

To ease the burden on the shipping companies and to ensure a smooth inclusion of shipping in the EU ETS, the obligation to surrender allowances is proposed to be *gradually phased-in* over the period 2024 to 2026, with shipping companies having to surrender 100 % of their verified emissions as of 2026.⁴⁷ According to the proposed new article 3ga, shipping companies shall be liable to surrender allowances according to the following schedule:⁴⁸

- (a) 40 % of verified emissions reported for 2024;
- (b) 70 % of verified emissions reported for 2025;
- (c) 100 % of verified emissions reported for 2026 and each year thereafter.

To the extent that fewer allowances are surrendered compared to the verified emissions from maritime transport for the years 2024 and 2025, a corresponding quantity of allowances shall be cancelled rather than auctioned pursuant to Article 10, once the difference between verified emissions and allowances surrendered has been established in respect of each year. The allowances will in other words be capped *and* limited.

2.3 The obligation: to report and surrender emissions

It has been paramount to the Commission to make the inclusion as easy on the industry as possible. The EU ETS 2021 proposal is therefore based on emissions already monitored, reported and verified under the MRV shipping Regulation from 2015,⁴⁹ under which the first reporting period started in January

46. See the 2023 Agreement 3g 1a (Accessed 13.03.2023).

47. Ibid article 3ga.

48. Is not likely that the above-mentioned schedule will be kept. At least one year delay is expected.

49. Regulation (EU) 2015/757 of the European Parliament and of the Council of 29 April 2015 on the monitoring, reporting and verification of carbon dioxide emissions from

2018.⁵⁰ Both the Commission proposal as well as the MRV shipping regulation apply to commercial ships⁵¹ *above 5000 gross tonnage*.⁵² Smaller ships are exempted with reference to the cost efficiency principle.⁵³ In the 2023 agreement, the Council and Parliament agreed to extend the *physical scope* of both the MRV regulation and the EU ETS 2021 proposal. *Offshore vessels* of 5000 gross tonnage will be included in the MRV-system from 2025 and in the EU ETS from 2027. As regards smaller general cargo vessels and off-shore vessels, between 400-5 000 gross tonnage, they will be included in the MRV-system from 2025. This will prepare for an inclusion in the EU ETS, but no decision is made for such inclusion yet. According to the plan, the question will be reviewed in 2026, see the 2023 agreement, preamble 19(a).⁵⁴

Subject to the MRV shipping Regulation, GHG emissions from intra-EU voyages, incoming voyages from a non-Union port to a port within the Union, as well as outgoing voyages from a Union port to a non-Union port, must be monitored, verified and reported, irrespective of which flag the ships sail under.⁵⁵ The obligation applies when the ship stops to load or unload cargo or to embark or disembark passengers.⁵⁶ It includes information on CO emissions and

maritime transport, and amending Directive 2009/16/EC OJL 123/55 as amended by Commission Delegated Regulation (EU) 2016/2071 of 22 September 2016 amending Regulation (EU) 2015/757 of the European Parliament and of the Council as regards the methods for monitoring carbon dioxide emissions and the rules for monitoring other relevant information [2015] OJ L320/1 (MRV Shipping' (2015) 58 Official Journal of the European Union L123/55)

50. Ibid. art. 8.

51. Non-commercial ships, naval-auxiliaries, warships and fish-catching or -processing ships are excluded. Ibid. art 2.2.

52. Ibid. art. 2.

53. Ibid. The Exemption from the regulation can be extracted from art 2, which holds the scope of the regulation. According to art. 2.2 the Regulation does not apply to warships, naval auxiliaries, fish-catching or fish-processing ships, wooden ships of a primitive build (!), ships not propelled by mechanical means or government ships used for non-commercial purposes.

54. See also the 2023 Agreement Annex II (2021/0211 (COD)) - MRV p. 161. (Accessed 13. 03.2023)

55. Ibid. art. 2.1. "...from their last port of call to a port of call under the jurisdiction of a Member State and from a port of call under the jurisdiction of a Member State to their next port of call, as well as within ports of call under the jurisdiction of a Member State."

56. Ibid., art 3 (b); "[S]tops for the sole purposes of refuelling, obtaining supplies, relieving the crew, going into dry-dock or making repairs to the ship and/or its equipment, stops in port because the ship is in need of assistance or in distress, ship-to-ship transfers carried out outside ports, and stops for the sole purpose of taking shelter from adverse weather or rendered necessary by search and rescue activities are excluded."

other relevant information arising from the ships' voyages during a reporting period, which is normally one year.⁵⁷ Both the monitoring and the reporting must be complete and cover CO emissions from the combustion of fuels, while the ships are *at sea as well as at berth*. The aggregated emissions data should be submitted to the "administering authority" at company level and in line with Chapter II of the MRV shipping Regulation.⁵⁸

2.4 Information to be submitted to administrative authority

The emission report is to be submitted to the Commission and the authorities of the flag States involved by 30 April each year⁵⁹ in an electronic inspection database called THETIS.⁶⁰ THETIS is developed, maintained, and hosted by the European Maritime Safety Agency (EMSA). EMSA has developed a new module in THETIS, namely THETIS-MRV, enabling companies responsible for the operation of large ships using EU ports to report their CO₂ emissions under the MRV Shipping Regulation. THETIS-MRV includes a mandatory and a voluntary module. Through the mandatory module, companies will generate Emission Reports, which is assessed by Verifiers who issue an electronic *Document of Compliance* in the system.⁶¹

As of 2024 the Commission is to publish and regularly update *a list of shipping companies* covered by the Directive and their respective administering authority (Article 3gd). If the shipping company is registered in a Member State, the administering authority shall be the Member State.⁶² In other cases the Commission proposes that the Member State with the greatest estimated number of port calls from voyages performed by a shipping company not registered in a Member State in the last four monitoring years will be the administering authority, if falling within the scope set out in Article 3g.⁶³

Lastly, if the shipping company is *not registered in a Member State* and *did not carry out any voyage* falling within the scope set out in Article 3g in the preceding four monitoring years, the administering authority shall be the Member State from where the shipping company has started its first

57. Ibid. art. 9 and 11.

58. EU ETS 2021 proposal art 3gc.

59. MRV shipping regulation (n 49) art. 11(1).

60. See: <https://mrv.emsa.europa.eu/#public/eumrv> (Accessed 13.12.2021).

61. The system has been available from 7 August 2017 and can be reached at <https://mrv.emsa.europa.eu>.

62. Ibid. art 3gd 1 (a).

63. The 2023 agreement art3gd 1 (b).

voyage falling within the scope set out in Article 3g⁶⁴. Where appropriate, the responsible administering authority in respect of a shipping company shall be updated every fourth year. In order to ensure equal treatment of shipping companies, Member States should follow harmonised rules for the administration of shipping companies for which they have responsibility, in accordance with detailed rules to be established by the Commission. Member States should ensure that the shipping companies that they administer comply with the requirements of Directive 2003/87/EC.

2.5 Penalties for non-compliance

In the event that a shipping company *fails to comply* with the requirements, e.g. by missing the deadlines for surrendering emissions allowances, it runs the risk of triggering enforcement procedures according to the EU-ETS directive art. 16. The article sets out, as a starting point, that the *Member States* are responsible for laying down rules on penalties applicable to infringements of the national provisions adopted pursuant to the directive. The penalties must be effective, proportionate and dissuasive.⁶⁵

In addition to penalties decided on by the Member States, the directive imposes a penalty fee of 100 EUR on all responsible entities covered by the directive, including the *shipping company*, for each tonne of carbon dioxide equivalent emitted for which the responsible entity has not surrendered allowances.⁶⁶ This comes on top of the obligation to surrender an amount of allowances equal to those excess emissions when surrendering allowances in relation to the following calendar year.⁶⁷ Furthermore, the directive provides for a “*name-and-shame*” sanction. According to the proposed article 16 (2), “Member States shall ensure publication of the names of operators, aircraft operators and shipping companies who are in breach of requirements to surrender sufficient allowances under this Directive.”

As a last resort measure, the Commission proposes that the Member States should be able to *refuse entry* to the ships under the responsibility of the shipping company concerned, except for the Member State whose flag the ship is flying, which should be able to detain that ship.⁶⁸ A precondition in

64. Ibid. 3gd 1 (c).

65. Ibid. art. 16 (1).

66. Ibid. art 16 (3) which according to the EU ETS 2021 proposal art 16 (3)a also will apply to shipping companies.

67. Ibid.

68. Ibid.

both situations is that the shipping company has failed to comply with the surrender requirements for two or more consecutive reporting periods and other enforcement methods have failed. Also, the shipping company should be allowed to submit its observations before an expulsion order is issued or the ship is detained. When an exculpation order is issued, all Member States, except the Member State whose flag the ship is flying, shall deny the ship access to its ports, until the allowances are surrendered.⁶⁹ These rules, are however, overruled by international maritime rules applicable in the case of ships in distress.⁷⁰

3. The problem of allocating the costs

3.1 The proposal: The Shipping Company or Shipowner takes the cost

Both the MRV shipping regulation⁷¹ and the EU ETS shipping directive⁷² points out the “*shipping company*” as the entity responsible for monitoring and reporting the relevant parameters during the one-year reporting period. Until now this has been unproblematic, as there are no costs (to speak about) related to the registration process. This will of course change if (or when) shipping is included in the EU ETS and the obligation is not only to report the emissions, but also to surrender the allowances.

According to the proposed article 3 (v), the “shipping company” includes the “...shipowner or any other organisation or person, such as the manager or the bareboat charterer, that has assumed the responsibility for the operation of the ship from the Shipowner and that, on assuming such responsibility, has agreed to take over all the duties and responsibilities imposed by the International Management Code for the Safe Operation of Ships and for Pollution Prevention”, the so called ISM Code. The purpose of the ISM Code is to provide an international standard for the safe management and operation of ships and for pollution prevention⁷³ The ISM Code applies directly in the EU

69. Ibid. article 11a.

70. Ibid.

71. The MRV shipping regulation (n 49) article 3(d)

72. EU ETS 2021 proposal (n 34) article 3gb.

73. The ISM Code in its current form was adopted in 1993 by Resolution A.741(18) and was made mandatory with the entry into force, on 1 July 1998, of the 1994 amendments to the SOLAS Convention, which introduced a new chapter IX into the Convention. It has been amended several times thereafter.

through a regulation from 2006.⁷⁴ It requires that companies *establish safety objectives* as described in the Code and, in addition, *develop, implement and maintain a safety management system* which includes functional requirements as listed in the Code. The intention is that the ISM Code should support and encourage the development of a safety culture in shipping.⁷⁵

Normally the Shipowner allocates the responsibility for the ship to a Ship Management Company. This is done under a ship management agreement, such as SHIPMAN 2009, where the Ship Management Company assumes responsibility for the operation of the vessel.⁷⁶ Both the Shipowner as well as the Ship Management Company can in other words be considered as Responsible Shipping Company. The responsibility allocated to the Ship Management Company is however normally limited, leaving the commercial operation of the vessel to a third party, the Charterer, with the exemption of a bareboat charter party where the Charterer takes on both the technical and the commercial responsibility. Under a voyage or a time charter party, however, the Charterer oversees the commercial operation of the ship. Different charter parties provide the Charterer with different options and responsibilities. The time Charterer has quite wide authority and can use the vessel for almost any purpose and route. Under a voyage charter the authority of the Charterer is more limited as the voyage that the vessel will perform is agreed. In both situations, however, the Charterer will make all decisions on fuel, rout, speed and amount of cargo and/or passengers. This means that the person who decides on the parameters that influences on the amount and quality of fuels (and hence of emissions) spent by the vessel, and the person responsible for surrendering the allowances, will not always be the same. A solution that is not in line with the *polluter pays principle*. The Commission is aware of the problem and proposes that the issue is solved by contractual agreements.⁷⁷

74. Regulation (EC) No 336/2006 of the European Parliament and of the Council of 15 February 2006 on the implementation of the International Safety Management Code within the Community and repealing Council Regulation (EC) No 3051/05 (OJ L 64, 4.3.2006, p. 1).

75. See e.g. Resolution A.1118(30) Adopted on 6 December 2017 (Agenda item 9) REVISED GUIDELINES ON THE IMPLEMENTATION OF THE INTERNATIONAL SAFETY MANAGEMENT (ISM) CODE BY ADMINISTRATIONS at 1.1.

76. See SHIPMAN 2009 article 4 (b) where the ship manager undertakes to ensure compliance with the IMSCode.

77. See the EU ETS 2021 proposal, preamble at (20).

3.2 The Councils response

Also the EU Council agrees to this solution: (20a) and proposes, in line with the polluter pays principle, that “the shipping company should ... be entitled, under national law, to claim reimbursement for the costs arising from the surrender of allowances from the entity that is directly responsible for the decisions affecting the CO₂ emissions of the ship. While such a mechanism of reimbursement could be subject to a contractual arrangement, Member States should, to reduce administrative costs, not be obliged to ensure or control the existence of such contracts but should instead provide, in national law, a statutory entitlement for the shipping company to be reimbursed and the corresponding access to justice to enforce that entitlement. For the same reasons, this entitlement, including any possible conflict relating to the reimbursement between the shipping company and the entity operating the ship, should not affect the obligations of the shipping company vis-à-vis the administering authority nor the enforcement measures that might be necessary against such a company to ensure the full compliance with Directive 2003/87EC. This position was not changed in the 2023 agreement.

3.3. BIMCO’s contractual arrangement, the ETSA- Clause for Time Charter Parties

3.3.1 A duty to collaborate and share information

With its new ETS-Emission Trading Scheme Allowances (ETSA) Clause for Time Charter Parties 2022, BIMCO provides a contractual solution to the problems addressed above. The clause with comments can be found on BIMCO’s homepages.⁷⁸ According to BIMCO, the ETSA Clause follows the “*polluter-pays*” principle by ensuring the pass-through of ETS costs to the commercial operators of vessels - in this case, the time charterers. The fundamental principle behind the clause is that it requires both parties to the charter party to *cooperate and collaborate*.

This means that both the Owners and the Charterers agree to co-operate and *exchange all relevant data and information* necessary to facilitate compliance with “any applicable Emission Scheme”. An Emission Scheme is defined in the clause to include a “greenhouse gas emission trading scheme that regulate the issuance, allocation, trading or surrendering of emission allowances.” As stated in the clause, this obviously includes the EU-ETS. The data and

78. ETS - Emission Trading Scheme Allowances Clause for Time Charter Parties 2022 (bimco.org) (Accessed 21.10.2022)

information shared shall enable both the shipowners and the time charterer to calculate the amount of emission allowances to be surrendered to the relevant authorities in respect of the Vessel subject to the Charter Party. The Owners shall monitor and report the relevant greenhouse gas emissions of the vessel for verification by an independent verifier in accordance with the applicable emission scheme. For the EU-ETS this is stated in the MRV-regulation.⁷⁹ All information, including information on the aggregated emissions, shall be exchanged between the parties in a *timely manner* to facilitate compliance with the system.

As mentioned above, it is normally the shipowner who is responsible for surrendering allowances under the EU ETS. In line with the *polluter pays* principle, the ETSA-clause redirects this cost to the Charterer. According to the clause, the Shipowner must notify the Charterer, in writing and within the first seven days of each month of the quantity of Emission Allowances for the previous month.⁸⁰ The Owners' notifications shall include the relevant calculations and the data used to establish the quantities.

3.3.2 Charterers to pay for the allowances

Although it is the Shipowner who is responsible for monitoring, reporting and surrendering emissions under the MRV regulation, BIMCO's ETSA clause shifts the financial burden from the Shipowner to the Charterer. According to the clause C(i), "... the Charterers shall provide and pay for the Emission Allowances corresponding to the Vessel's emissions under the scope of the applicable Emission Scheme" throughout the Charter Party period. The money shall be transferred to an *account nominated by the Shipowners* within the seven days notification period mentioned above. If the estimated quantity is higher or lower than the actual quantity, any difference in Emission Allowances shall be transferred by the Charterers or returned by the Owners within 7 days of notification from the receiving party. Likewise, if the vessel is off-hire, the Charterers have the right to offset against any Emission Allowances that the Charterer otherwise would have been responsible for. The ETSA clause also gives the Charterers a right to claim the Owners to return already submitted Emission Allowances for the off-hire period.

If the Charterers fail to transfer allowances in accordance with the above (ETSA Clause c) the Owners have the right, according to clause d, after a 5 days' notice, to suspend the performance of any or all their obligations under

79. Above in 2.3 and 2.4.

80. ETSA-clause C (1).

the Charter Party, until the allowances are received in full by the Owners. The Vessel shall regardless of this be on hire and the Owners are exempted from any responsibility for the action taken. Furthermore, such action does not impact any other rights or claims that the Owners might have against the Charterer under the Charter Party.

4. Concluding remarks

Carbon dioxide certainly comes with a cost: Under the MRV regulation, the Shipowners are responsible for monitoring, reporting and verifying the emissions. With the proposed extension of the ETS-directive, they are also responsible for acquiring and surrendering allowances. The current price around 80 euros per emitted tonne CO₂ equivalents, indicates that this will be costly. Because it is the Charterers who make the operational decisions on a vessel and hence can impact the quantity of fuels consumed, the proposed solution is not in line with the *polluter pays principle*. The EU Council hence advises the parties to solve this unbalance by contractual solutions.

BIMCO's ETS – allowances (ETSA) clause for time charter parties fills the legal gap and provides a solution which shifts the financial burden off the cost of emissions to the Charterer. This is in line with the general rule for time charter parties that Charterers pay for the bunkers during the Charter Party period. Whether or not the solution also works as an incentive for the Shipowners to acquire climate smart vessels re-main to be seen.

And this is only the start: With the 2023 agreement the EU institutions decided to include non-CO₂ emissions (methane and N₂O) in the MRV regulation from 2024 and in the EU ETS from 2026. Yet, the 2023 agreement contains several modifications to consider geographical specificities. It proposes transitional measures for small islands, ice class ships and journeys relating to outermost regions and public service obligations. Certain member states with a relatively high number of shipping companies will in addition receive 3.5% of the ceiling of the auctioned allowances to be distributed among them, art. 3g(2).

However, there will be no free allowances for the shipping industry. Emissions allowances must be acquired by auction and surrendered to the national authorities from 2024. The revenues will be used for inter alia promotion of climate friendly transport and public transport in all sectors, see the preamble (17b) and art 10(3) of the 2023 agreement.

ISBN: 978-960-654-992-2



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