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Doubts growing over shipping's readiness for Europe's ETS carbon tax

Maersk and Hapag-Lloyd have outlined their ETS surcharges per container from the first quarter of next year. Photo credit: Hapag-Lloyd.

Greg Knowler, Senior Editor Europe | Oct 5, 2023, 10:57 AM EDT

The impact of Europe's emissions trading system (ETS) on the container shipping value chain is becoming apparent, with growing concerns that the industry is not prepared for the incoming carbon tax regime.

Shipping will be included in Europe's ETS on Jan. 1 when all emissions on voyages and port calls within the European Union and European Economic Area, and 50% of emissions on voyages into or out of the regions, will be subject to the carbon tax.

To comply with the ETS, ocean carriers will essentially need to become experts in carbon credit trading, on top of monitoring, verifying and reporting CO_2 emissions across regional fleets and their vessels operating in the region.

"Container shipping will bear the biggest cost of all segments, driven by its outstanding importance to global maritime transport and the higher speeds and consumption of the vessels employed," Albrecht Grell, managing director of Hamburg-based maritime data and technology firm OceanScore, told the *Journal of Commerce* Thursday.

"European shipping is better prepared than non-European players, and larger companies are better prepared than smaller ones — with quite a few of the small ones basically not yet prepared at all," Grell added.

All ship operators will be required to monitor and report their emissions and surrender allowances for every ton of CO_2 they emit. Shipping will be required to pay for allowances covering 40% of greenhouse gas emissions in 2024, rising to 70% in 2025 and 100% from 2026.

Carbon credits, known as EU allowances (EUAs), will be purchased at a fixed price in the primary market through auctions arranged several times a year by the European Energy Exchange (EEX) on behalf of the EU. They can also be bought and sold on the secondary market over the counter through brokers or online trading platforms.

Maersk and Hapag-Lloyd advised the market two weeks ago they will be collecting an emissions surcharge from customers from the first quarter of 2024, and CMA CGM today released estimates of €25/TEU from Asia to Europe and €20/TEU from Asia to the Mediterranean.

"The surcharge amount will be shared mid-November and may be reviewed on a quarterly basis, depending on the updated version of the EU ETS regulation and the market value of carbon allowances," CMA CGM said in a statement.

Potentially huge liabilities

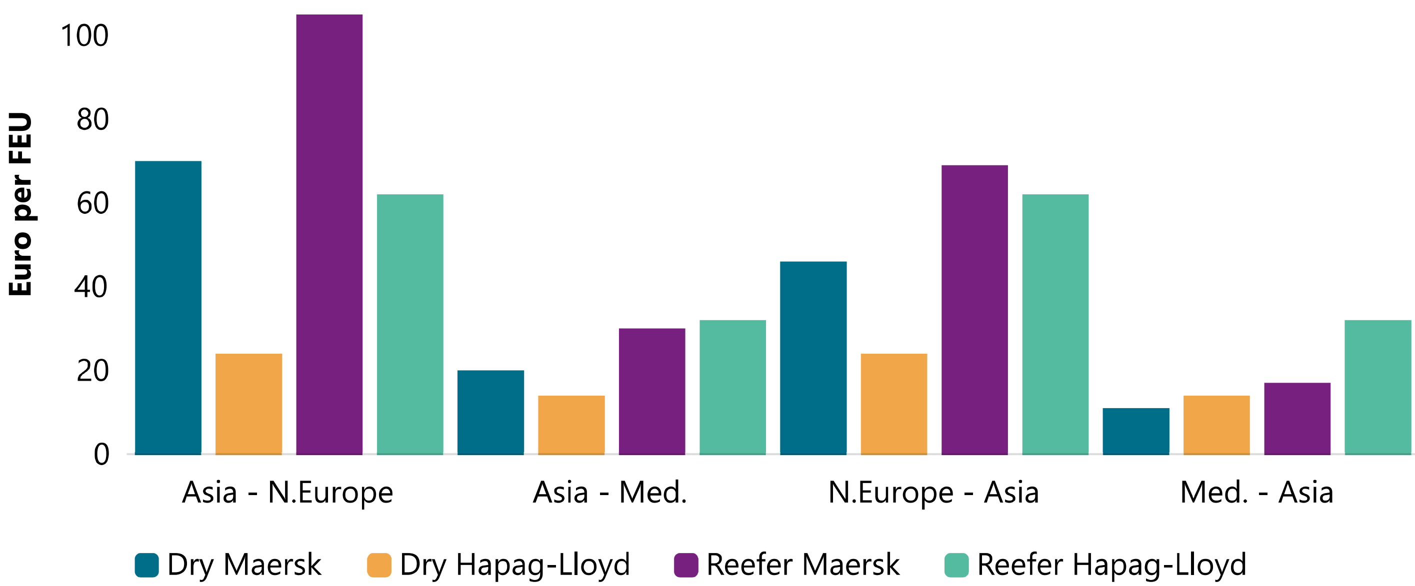
Significant penalties await for non-compliance, with carriers required to make up any shortfall of allowances with an inflation-linked fine of €100 per tonne of CO_2 equivalent for emissions the carriers have not covered by purchasing EUAs. Grell said a company also risks its entire fleet being expelled from trading in EU waters if the carrier fails to surrender sufficient allowances for a single vessel over two consecutive years or more.

However, Grell warned of wider financial implications for shipping companies, with the need to buy and sell EUAs introducing a new element of balance sheet risk with exposure to potentially huge liabilities. The total annual cost to shipping after 2026 when the three-year phase-in period ends is estimated to be up to €10 billion.

"This can translate into millions of euros in liabilities for the party responsible for buying and surrendering allowances, especially when managing or owning a large fleet," Grell said. "It may also be difficult to pass on these costs to the charterer as the 'polluter pays' principle dictates due to possible disputes over EUA volumes or pricing."

Maersk, Hapag-Lloyd ETS emissions surcharges on Asia-Europe trades

Estimated Emissions Trading System (ETS) surcharges in EUR per FEU from Q1 2024 on Asia to North Europe and Mediterranean



Source: Hecla Emissions Management

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Berlin CO2 management provider Zero44 released an ETS tool for trading in EUAs this week with software developed in partnership with MPC Container Ships, Harren Group and Zeaborn Ship Management. But the solutions provider said in a statement Wednesday that complying with the ETS presented significant challenges.

"Since January this year, we have been working intensively on our ETS solution and, together with our development partners, have examined the complexity of regulation from all perspectives," Friederike Hesse, co-founder and managing director of Zero44, said in the statement.

A key challenge was that ETS accounting was annual and retrospective, with data verification to take place on March 31 in the year following the assessment period, and the submission of EUAs to be made in the following September.

"This is a problem for the sector because charter contracts are structured differently in terms of timing," Zero44 noted in the statement, adding that to prevent major financial risks, settlement of the ETS needed to be close to the time of each completed voyage rather than at a specific time each year.

No clear view of responsibility

Another major challenge raised by Zero44 was the multitude of business models and stakeholders involved in European ocean shipping. It was an issue the *Journal of Commerce* highlighted in May when concerns were expressed over how the huge cost of meeting the regulation could be factored into contracts between several parties in the shipping value chain.

"Owners, charterers, international safety managers [ISMs], commercial managers and cargo owners are affected by the ETS and have to agree among themselves who is responsible for which measures within the ETS value chain and how often the settlement of allowance trading should take place," Zero44 noted.

"These agreements also influence each other. For example, an agreement between the owner and the charterer has an impact on the agreements between the owner and the ISM manager," it added. "Time charters, voyage charters, pools and parceling each bring their own challenges."

A third challenge involved Europe's Union Registry that is used to account for all industry EUAs but was not designed with the specificities and requirements of shipping in mind. Zero44 said links in the Union Registry between the EUAs and the ships, voyages, charterers and ship managers would have to be managed within a shipping company itself to allow the correct accounting of costs.

Despite the uncertainties, with less than three months before the ETS is implemented, waiting to see how the ruling plays out is no longer an option, warned Grell.

"Hope that 'we will manage somehow, as always' could be a risky proposition," he said. "Preparations concerning [the] assessment of EUA ... as per specific regulation, processes, contractual arrangements with charterers and owners, and responsibilities in the companies are generally far from where they should be."

Contact Greg Knowler at greg.knowler@spglobal.com.