



Contractual issues arising from EU ETS implementation explained

Splash

March 5, 2024



Helen Barden and Mark Smith from NorthStandard answer questions arising from the first months of Europe's Emissions Trading System being applied to shipping.

Several issues were left unanswered as the European Union's Emissions Trading System (EU ETS) was applied to shipping from the beginning of this year, but answers to those questions are becoming apparent.

The European Commission issued a set of EU ETS implementing regulations in October and November 2023, with a further implementing decision published in January 2024. However, they have not provided all the answers. Some owners and operators have planned and are better prepared for shipping's inclusion in the EU ETS. However, there remains confusion in some areas and NorthStandard has sought clarification on these to guide its members.

The Commission Implementing Regulation (EU) 2023/2599 has provided clarification on who is the "Shipping Company" under the EU ETS.

Without a written mandate (adhering to the requirements of the implementing legislation) between the shipowner and other entity, such as the bareboat charterer or management company, the ETS obligations will remain with the shipowner. But who is the shipowner? In the FAQs on the European Commission's website, it states that the shipowner is the registered owner of the ship.

In line with the European Commission NorthStandard interprets the implementing regulation to state that a shipowner could mandate its obligations to the ISM company and no one else.

Therefore, a bareboat charterer would need to be the ISM company and agree to be mandated to take on ETS obligations if a shipowner wanted to pass ETS obligations on to its bareboat charterer. If the ship manager is the ISM company as part of a chain with the registered owner and bareboat charterer and doesn't want to take on ETS obligations, these will stay with the registered owner.

It is, however, possible for a ship manager or bareboat charterer to help an owner with the operational side of compliance, even if they don't want to be the entity ultimately responsible for compliance with the EU ETS.

Thetis MRV, MOHAs and monitoring

A third party, such as a ship manager, could be given access to the Thetis MRV system and provide monitoring and reporting tasks on the shipping company's behalf.

In addition, a third party should be able to have access to a shipping company's maritime operator holding account (MOHA), although specific requirements should be checked with the relevant registry. Some shipping companies will already have opened their MOHA, and now more will be able to do so as Implementing Decision 2024/411 has been published listing each shipping company and its designated administering authority. It should be noted, however, that there may be shipping companies not on the list, but which will have to comply with the EU ETS. Indeed recital (6) of the Implementing Decision makes the point that because the inclusion of a shipping company into the EU ETS is dependent upon a vessel in its fleet undertaking a voyage caught by the EU ETS, a shipping company's obligation to comply with the EU ETS is not dependent upon its being included in the list.

The MRV data must be properly verified by 31 March of the following year and the required allowances surrendered by 30 September of that year. So, for 2024 data, the relevant dates will be 31 March 2025 and 30 September 2025 respectively.

Voyage of discovery

Contractual questions about the responsibility of EU ETS compliance between owners and charterers continue. Examples include the allocation of compliance costs passed on to charterers in a time and voyage charter party. Another is whether, in a voyage charter context, ballast and repositioning legs of the EU ETS voyage apply and who bears the cost?

A lot will depend on commercial negotiations between both parties. BIMCO has produced a time charter party clause to assist, as well as a suite of three voyage charter clauses to help with allocating the risks and costs of emission trading schemes. The BIMCO Emission Trading Scheme Allowances Clause for Voyage Charter Parties 2023 leaves it for the parties to determine whether to include ballast legs or not.

But beyond the question of commercial agreement, has NorthStandard seen conflicting opinions over what parts of voyages qualify for inclusion as chargeable to the EU ETS?

Generally, any confusion over which voyages are caught under the EU ETS is caused by differing interpretations of the regulations. NorthStandard has sought to educate its members on the scope of the EU ETS and which emissions will be included or not.

The EU ETS is route-based to cover 100% of CO₂ emissions from ships making voyages between ports of call under the jurisdiction of EU member states and while they are at berth or manoeuvring within ports in EU states. From 2026 methane and nitrous oxide emissions will be added.

The scheme also applies to 50% of emissions from ships performing voyages from an EU member state port of call to a port of call outside its jurisdiction and vice versa.

But what if ships call at ports for repairs or solely for bunkering, or are party to a ship to ship (STS) transfer outside a port?

A port of call is defined in the regulations as the port where a ship stops to load or unload cargo or to embark or disembark passengers or where an offshore vessel stops to relieve the crew. So, all the examples in the above paragraph are not "ports of call" and so are not relevant for the purpose of determining the scope of the voyage caught up by the EU ETS.

Neighbouring container transshipment port calls are also excluded from the definition of port of call and those determined to be such a neighbouring container transshipment port are included in Implementing Regulation 2023/2297.

Future costs

In a webinar hosted by NorthStandard, a case study of a 20,000 teu containership trading from Jebel Ali to Rotterdam via the Suez Canal was considered.

Its 6,330 nautical mile voyage at a speed of 16 knots would take 16.5 days roughly consuming 100 tonnes of very low sulphur fuel oil per day. Using a carbon factor of

3.114 would mean the emission of 311 tons of CO₂ per day that – multiplied by 16.5 days – yielded a total of 5,138 tonnes of CO₂.

Assuming potential carbon costs of \$100 per ton at the initial 40% reporting level for the first year of the ETS, the voyage would lead to a total cost of approximately \$1,092,000 – a 10.3% increase on the circa \$999,000 it would have cost before the EU ETS came into being.

When the EU ETS reporting rate rises to 70% in 2025 that would go up to an 18.2% increase and in 2026, at 100%, it would be 26% more.

If, in the case study example, the ship stops for repairs at Jeddah and solely to tranship containers at Tangier, the calculated totals would remain unchanged because Jeddah and Tangier would not fall within the definition of port of call.

Companies that fail to surrender allowances will be hit with an excess emissions penalty of €100 per ton of CO₂ equivalent, in addition to the cost of the emission allowances they should have paid. There is also a potential for non-compliance leading to ships being banned from EU ports.