AmCham EU's response to ETS post-2020 carbon leakage provisions

CONSULTATION RESPONSE

Executive summary

As part of the debate on the reform of the EU ETS post-2020, the American Chamber of Commerce to the European Union (AmCham EU) believes that European policy-makers need to take into account key issues around costs and competiveness for industries exposed to the risk of carbon leakage. These industries have so far received no clarity as to the rules for free allocation and compensation of the ETS indirect costs beyond 2020. Taking into account the elements of any future international agreement, the provisions for carbon leakage and compensation for indirect costs in the ETS Directive must be extended beyond 2020 when qualifying installations will be receiving far fewer allowances than they do today.

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AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled €2 trillion in 2013 and directly supports more than 4.3 million jobs in Europe.

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Introduction

The American Chamber of Commerce to the European Union (AmCham EU) has been a consistent supporter of a global carbon market as one of the principal means of combatting and mitigating climate change. AmCham EU has also regularly singled out the importance of a stable and strong EU Emissions Trading Scheme to support the EU's decarbonisaton strategy.

AmCham EU supports an EU ETS based on the following principles:

- A stable regulatory regime that is market-based and eschews arbitrary interventions;
- A predictable, long-term framework, giving clear policy signals to business and the investment community; and
- Avoiding damaging European competiveness, allocating CO_2 emissions as cost effectively as possible while ensuring carbon leakage protection for exposed industries in the absence of an international agreement.

The ambitious climate and energy targets put forward by the Commission for 2030 will have major implications for the carbon and energy costs of key parts of the manufacturing sector. AmCham EU, therefore, strongly welcomes the fact that, after their first debate on the 2030 package, EU leaders have asked the Commission to 'develop measures to prevent potential carbon leakage' and have called 'for long-term planning security for industrial investment in order to ensure the competitiveness of Europe's energy-intensive industries'.

AmCham EU fully endorses these requests because they are vital to support our members in their investment decisions for the period beyond 2020, which are already under consideration.

Competitiveness, carbon leakage and present free allocation rules

Business requires clarity on the ETS's future because it is the cornerstone of EU climate policy, and structural reform requires a longer-term vision.

For EU industry to continue to reduce its GHG emissions toward 2020 and beyond, it must remain globally competitive. AmCham EU believes that in the absence of an international agreement and comparable efforts by other countries in reducing GHG emissions, special measures to support EU industry covered by the ETS are a prerequisite to continue investing in innovation in EU industrial assets.

AmCham EU would like to stress that, when debating free allocation, it is important to remember that:

- Free permits do not exempt the industries that receive them from the obligation to reduce their carbon emissions according to ETS linear reduction factor;
- The allocation is based on best performers benchmarks, and as such none of the sectors at risk of carbon leakage receives the totality of its required carbon permits free of charge; and

- A 40% EU GHG target will translate into a tighter ETS reduction target after 2020 that, together with other tabled proposals such as the introduction of a market reserve mechanism, will result in higher carbon costs.

Free allocation is key to mitigating the impact of direct ETS carbon costs on industries at risk of carbon leakage. To effectively prevent investment leakage, free allocation provisions must provide for concrete carbon cost mitigation as well as long term predictability.

Free allocation alone is, however, not sufficient to protect energy-intensive sectors from loss of competitiveness from exposure to carbon costs passed through their energy consumption, the so-called indirect ETS costs. This is why the ETS Directive has foreseen the possibility for Member States to compensate a limited number of energy-intensive industries for their indirect ETS costs. However, this tool has been largely ineffective. While indirect ETS costs have a major impact on energy-intensive industries, their compensation depends on the will/ability of national governments to support their industries, and to date only four Member States have set up meaningful compensation mechanisms. This has resulted in an ineffective protection of exposed industries and competitive distortions across the EU.

Options for post-2020

Strategic choices

In light of the fact that the number of allowances will decline after 2020 as a result of the tightening of the ETS cap based on the EU 40% target, AmCham EU stresses the importance of preserving a share of the post-2020 allowances budget for carbon leakage and competitiveness measures. The number of free permits should be sufficient to guarantee full coverage for sectors deemed to be at risk of carbon leakage as well as free permits for ETS indirect compensation for a limited number of sectors exposed to carbon-costs pass-through in their electricity bill.

When considering specific support schemes for industrial innovation and the deployment of low carbon technologies, AmCham EU believes that it is important to bear in mind that different industry sectors have different innovation patterns and the scale of the required investments can vary immensely, e.g. for some sectors further meaningful greenhouse gas (GHG) emissions reductions can only be attained via breakthrough technologies. A support scheme for innovation in the ETS might not suffice to provide the required investment support, as has been the case for the NER 300 for carbon capture and storage (CCS) demonstration projects. Stepping up the innovation support via large-scale EU innovation projects and funding, such as Horizon 2020, might be a more effective approach.

Allocation modalities

AmCham EU regrets that industries at risk of carbon leakage have so far received no clarity as to the rules for free allocation and compensation of the ETS indirect costs beyond 2020. This is already impacting investment decisions. It is thus imperative to provide a clear vision of the level of protection from increased carbon and energy costs related to climate mitigation policies that EU manufacturing industries can rely upon after 2020. This implies that the two current categories for sectors in terms of exposure to the risk of carbon leakage should be retained, as well as the current thresholds, so as to not impede the visibility of companies operating within the framework.

Taking into account the relevant developments related to any future international agreement, the provisions for carbon leakage and compensation for indirect costs in the ETS Directive must be extended beyond 2020 when qualifying installations will be receiving far fewer allowances than they do today. Their duration should at least match that of phase IV of the ETS to ensure sufficient investment predictability.

AmCham EU believes that industries exposed to global competition and unable to pass on the additional carbon costs must continue to receive free of charge the totality of permits determined in accordance to the benchmarks. Furthermore, it is essential to ensure effective protection across the entire EU from EU carbon costs impacting energy prices, i.e. ETS indirect costs, through an EU-wide compensation mechanism.

When reviewing the rules used to determine the allocation due to each installation, it is key to ensure that the ETS does not put a brake to the EU economic recovery. In light of this, dynamic allocation based on actual production data should be further explored.

Innovation support

The goal of the EU ETS is to drive GHG emissions reduction in a cost-effective way. While it should help stimulating investments in cleaner process and technologies, the ETS is not an innovation fund to finance the low-carbon transition.