

Ecochem Materials Ltd.

Portview House
Thorncastle Street
Dublin 4,
Ireland.

Tel: +353 (0)1 678 1800

Fax: +353 (0)1 678 1816

Website: www.ecochem.ie

European Commission
Directorate-General Climate Action
Unit B.1 – Implementation of ETS
Avenue de Beaulieu, 24
B-1049 Bruxelles
Belgium

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ETS in crisis, the example of the cement sector

Dear Sir or Madam,

Thank you very much for this opportunity to comment on the future structural options for the ETS. Ecochem Materials Ltd is Europe's largest ground granulated blastfurnace slag (GGBS)¹ cement manufacturer with manufacturing plants in three Member States: Ireland, the Netherlands and France, and sales in an additional 5 EU countries. While our comments primarily focus on the cement sector we believe they have wider implications for the ETS as a whole.

1. Issues Facing the Cement Industry:

a. Over-allocation leading to low CO₂ price:

- i. This is an EU wide problem. The Commission itself estimates the over allocation will reach more than 2bn tCO₂ by 2020². There is an urgent need to find an EU solution. According to a recent report by Sandbag³ the 10 largest Germany polluting companies, which accounted for nearly half of Germany's emissions, will be 99.8% shielded from needing to buy CO₂ credits in Phase 3. This will continue even if the supply of allowances in the wider market is reduced, and the price of CO₂ increases. Therefore Sandbag concludes that the ETS is "failing to cap emissions below

¹ GGBS is made by taking a by-product of the steel industry, rapidly quenching it with water and grinding it. The resulting chemistry of GGBS and is similar to OPC (ordinary Portland cement).

² EU Commission Report "The state of the European carbon market in 2012" published Nov 2012.

³ "Der Klimagoldesel 2013: Carbon Fatcat Companies in Germany" Sandbag Report published Feb 2013
<http://www.sandbag.org.uk/reports/>

- business-as-usual levels, failing to provide clean companies with a competitive advantage, and failing to provide a clear investment signal”.
- ii. Consequences: no/low economic incentive to innovate with low carbon technologies; accumulation of surplus credits postpones the need to innovate far into the future, even if price rises. Consequently there is currently extensive underutilisation of clean cement technology in Europe: e.g. granulated slag and pulverised fuel ash.
 - iii. Over-allocation means no cost of CO₂ to pass on in increased cement prices – cement prices have not changed with the advent of the ETS. The buyer of cement has no price incentive to prefer green cements.
- b. Failure to include all significant suppliers in the cement sector leads to severe competitive distortions.
- i. Green cement producers, such as Ecocem, are excluded from ETS because their CO₂ emissions are too low. As a result Ecocem competes with the cement industry but has to play by different rules.
 - ii. Increased green cement sales reduce sales of polluting cement, therefore a reduction in CO₂ emissions occurs at the polluting cement plant. The reduction is due to the investment, efforts and risk-taking of the green cement producer. The ETS ensures that the economic advantage of this reduction goes to the polluting competitor without any action on his part.
 - iii. The competitive distortion is significant. In Phase 2, Ecocem estimates that for every tonne of polluting cement sold in Ireland the ETS subsidises the polluter by €12 a tonne of cement or 17% of the selling price.
- c. Failure to take account of the collapse of unprecedented and unsustainable booms in construction on cement demand leading to severe competitive distortions and incentives to increase CO₂ emissions.
- i. The EU cement industry is over-allocated, but certain national cement industries are hugely over-allocated due to the collapse of unsustainable construction booms from levels that will not return, even in the long term. Several countries in the EU are significantly below their Phase 2 and Phase 3 baseline production levels and are unlikely ever to recover fully.
 - ii. These structural over allocations generate windfall profits for polluting cement producers: the CO₂ reductions are the result of a permanent downwards adjustment of construction activity, and would have occurred even in the absence of the ETS. The windfall profits of the polluting cement sectors are a transfer from the national taxpayer for no environmental benefit.
 - iii. Cement plants in countries where cement demand has reduced to less than 50% of “boom” levels (Ireland, Spain and Greece) can still keep all their allocation by producing at 50% of clinker capacity. Profit optimisation means preferences for polluting technology (clinker over low carbon alternatives), with additional production exported to other markets (additional CO₂ emission from the transport/handling), and the production of “not-for-sale” (i.e. dumped) cement to qualify for full allocation. This is already a major driver of cement production in Spain and Ireland. The capture of the highest allocation is then an award for

production of CO₂-intensive cements, a subsidy to compete with the green cement sector and an incentive to emit more CO₂ in serving export markets.

- iv. Ecocem estimates that under Phase 2 the Irish cement sector received a windfall profit of €120m from over allocation. This will increase to €370m under Phase 3, assuming an average price of €30/tCO₂.

2. Consequences for the cement sector.

- a. Manufacture and supply of green cements in installations outside the ETS carries a severe financial penalty compared to installations with the ETS. The ETS installations capture the rewards from CO₂ reduction from increased use of green cement technology in non-ETS installations.
- b. Over-allocation, for whatever reasons, gives windfall profits to polluting cement manufacturers that makes their polluting cements significantly more competitive against green cements.
- c. Over-allocation defers action on use of low-carbon technologies by the incumbent installations. Higher CO₂ emissions result.
- d. ETS rules provide incentives to a significant part of the industry to optimise credit allocation by producing more CO₂ than necessary.

3. Necessary structural reforms.

- a. Eliminate free over-allocation, and in particular that due to past unsustainable construction booms.
- b. Manage credit allocation to target CO₂ price band.
- c. Revise rules that give perverse incentives to increase CO₂ emissions.
- d. Level the playing field for green cements from installations now outside the ETS, i.e. the same treatment for all installations using low carbon cement technology, not just for polluting incumbents.

Again thank you for giving us the opportunity to comment on the methods to improve the structure of the ETS and we would be happy to discuss these proposals in more detail,

Yours sincerely,



Donal O'Riain

Managing Director

Ecocem Materials Ltd.