

# Structural options to strengthen the EU ETS

Holcim contribution to the European Commission's public consultation

February 2013

---

## Holcim identification in the EU Transparency Register: N°626908810188-39

---

Holcim is one of the world's leading companies of cement and aggregates, and holds majority and minority interests in around 70 countries on all continents. In EU27, Holcim produced 19.6 Mt cement in 2010, representing more than 10% of cement produced in the area.

We believe that the current exceptional circumstances provide an opportunity to undertake a comprehensive reform of the system to ensure its long-term sustainability. For this reason, our comments go beyond the scope of the structural reform options presented in the Commission's 2012 carbon market report. We refer the European Commission to CEMBUREAU's contribution for the cement sector's comments on the six specific options presented in the 2012 Carbon market report.

Holcim has committed to reducing CO<sub>2</sub> emissions per ton of cement by 25% by 2015 compared to 1990 levels and a well-functioning EU policy and regulatory framework is needed to meet our objective sustainably. And whilst the overarching aim of the EU ETS is to incentivize the transition towards a low carbon economy, we are of the view that the system is not delivering on its objectives and a one-time revision of EU ETS is needed.

To improve the EU ETS, Holcim believes that any structural reform needs to reconsider the way free allowances are allocated, moving away from an allocation based on historic production and rather accounting for actual production and emissions (for example, in a system with free allowances the allocation could be based on actual production levels; in a system with full auctioning, importers could be subject to a carbon levy).

## **Multiple reforms are detrimental; a one-time comprehensive revision of the ETS is needed**

To reduce emissions and plan investments effectively, industry needs a simple, reliable and predictable legal framework that provides long term visibility. Such framework must be able to reward carbon efficiency while establishing a level playing field between domestic producers, importers and among sectors. The competitiveness of the European industry at large, not only the cement sector, relies on such conditions.

Holcim is of the view that the current ETS does not reward efficiency, and it does not provide the required long term visibility and stability. Besides the current uncertainties, EU ETS was developed under the assumption that an international trading scheme would be in place by 2020; hence, it does not foresee the need to allocate free allowances to carbon leakage exposed sectors beyond 2020. However, international negotiations are not sufficiently advanced, and protecting EU competitiveness requires amending the ETS Directive for the post-2020 period.

Multiple interventions (i.e. the proposed back-loading, followed by structural reforms that are the object of this consultation and then by post-2020 reforms) undermine the reliability and predictability of EU ETS, as such they have detrimental impacts on the ability to invest in Europe. For this reason, it is fundamental to avoid multiple structural reforms over a few years.

Therefore, we acknowledge that a one-time comprehensive review of EU ETS is needed to ensure its long term sustainability.

## **Address the root cause of the problem, not the consequence**

The sluggish economy combined with the fixed supply of allowances (the amount of which is determined by historical activity) has inevitably led to a build up of a substantial surplus of allowances, the consequence of which is the current low carbon price. The options proposed by the EC aim to adjust the supply and demand balance of allowances based on today's forecasts of the future, however these forecasts cannot account for unforeseen events that may materialize (e.g. economy restarts faster than expected or slows down more). And these events may require again intervening on the system.

To solve all obvious issues of EU ETS, if interventions and/or structural reforms are to be done at some point in time they must address the root cause of the problem and not just its symptoms (i.e. low price).

The root cause of the current problem is the fixed supply of allowances that is totally independent of economic developments (i.e. ex-ante system based on historical production levels). This fundamental weakness is exacerbated by other mechanisms such as the stepwise adjustment to the amount of free allowances depending on capacity utilization thresholds (50%, 25% and 10%). Such mechanisms amplify negative consequences of EU ETS, hindering assets rationalization and undermining EU ETS credibility.

## **Review the allowance allocation mechanism**

Currently, the underlying assumption of EU ETS is that the supply of allowances must match the cap of ETS on a yearly base. Holcim believes that the supply of allowances - through auctioning and free allocation - needs to be adjusted to economic developments, reflecting larger or smaller needs for compliance purposes. To this end, different mechanisms to establish flexible supply of allowances could be envisaged without the need to regularly intervene on the market.

In particular, Holcim believes that any structural reform needs to reconsider the way free allowances are allocated to avoid the pitfalls generated under the current rules. The cost of carbon to the regulated entity should not be linked to historic production levels, but rather to actual production level and emissions. For example, for carbon leakage exposed sectors, in a system with free allowances the allocation could be based on actual production levels; in a system with full auctioning, importers could be subject to a carbon levy.

\* \* \*