RESPONSE TO THE EUROPEAN COMMISSION PUBLIC CONSULTATION IN PREPARATION OF AN ANALYTICAL REPORT ON THE IMPACT OF THE INTERNATIONAL CLIMATE NEGOTIATIONS ON THE SITUATION OF ENERGY INTENSIVE SECTORS

Question 1: *In your opinion, how have key indicators of the risk of carbon leakage (such as exposure to international trade, carbon prices etc.) for the EU energy intensive industry changed since the adoption of the climate change and energy package implementing the EU's unilateral 20% emission reduction target at the end of 2008?"*

CIRFS response:

The man-made fibre industry is on the list because the criteria for intensity of trade with third countries as defined in the Directive were met. **The intensity of trade has in 2008 even further increased to 38%.**

Question 2: *Do you think that the outcome of Copenhagen, including the Copenhagen Accord and its pledges by relevant competitors of European energy-intensive industry, will translate into additional greenhouse gas emission reductions sufficient to review the list of sectors deemed to be exposed to a significant risk of carbon leakage? If so, how and why?*

Question 3: *In your view, what would be a compelling new general economic or other factor which would require a change of the level of free allocation to sectors deemed to be exposed to a significant risk of carbon leakage?*

CIRFS response to Question 2 and 3:

The outcome of Copenhagen, including the Copenhagen Accord, is very poor. No binding agreement has been reached, confirming that there is indeed a big difference in the efforts which will be made globally to reduce CO2 emission, and proving that in reality there is a serious risk of carbon leakage. **In this respect we see no reason at all to review the list of industries being exposed to carbon leakage, or to change the level of free allocation to sectors, unless it is an increase.**

Question 4: *Do you consider free allocation of allowances as sufficient measure to address the risk of carbon leakage, or do you see a need for alternative or additional measures?*

CIRFS response to Question 4:

We do not consider free allocation of allowances, as it is worked out now, as a sufficient measure to address the risk of carbon leakage. Our industry is disappointed that being on the list of industries exposed to serious risk of carbon leakage does not sufficiently deal with the dangers to competitiveness which arise for our industry, in relation to countries which have so far failed to agree quantified commitments on reduction of CO2 emissions.

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Free allocation is only meant for heat while electricity is an important part of the energy use. The compensation for heat is reduced by all kinds of correction factors and the compensation for electricity will eventually be given at national level. After all, it looks like the compensation will be very poor. **We think that free allocation is as such a sufficient measure, but it has to be a 100% compensation for the direct and indirect cost increases.** See also attachment

We recommend you;
- **not to review** the list of industries being exposed to carbon leakage, and
- **to go for a real and fair compensation of direct and indirect cost increases**.

Attachment

COMPENSATION UNDER ETS 2013 FOR INDUSTRIES AT RISK OF CARBON LEAKAGE: VIEWS OF THE EUROPEAN MAN-MADE FIBRES INDUSTRY

The European man-made fibres industry

The European man-made fibres industry is the second-largest producer of man-made fibres in the world, and a **global leader** in innovation, quality and sustainable production methods. It provides essential raw materials for a wide variety of uses, including textiles, transport, construction, housing, hygienic and medical applications and environmental protection projects. It has annual sales of over €11 billion, with production in almost every EU member state.

Part of the industry's **raw materials** is from renewable sources (sustainably managed forests), part is from oil, and a growing part uses recycled materials. **Energy usage** is steadily being reduced, air and water emissions are strictly controlled and being brought down every year, **water usage** is much lower than for most competing materials, and the light weight, **durability** and **performance** of man-made fibres save large amounts of energy during the lifetime of the products in which they are incorporated.

The man-made fibres industry in the Emissions Trading System

CIRFS: **European Man-made Fibres Association**, the industry representative association, shares the commitment of European industry as a whole to the need for reduction of CO2 emissions at both the European and global levels. Its member companies throughout Europe are steadily reducing their own emissions, but a certain amount of energy usage is an inescapable part of the production processes.

Man-made fibres are a sector where **global competition** is intense. The European industry is a major exporter, but also faces strong import competition, mainly from Asian countries and above all from China. This intense global competition means that industry profit margins are constantly under pressure, and the pattern of trade can be seriously affected (lower exports and/or higher imports) if conditions of competition change – for example, if European costs increase due to policies not implemented in similar ways in other regions of the world.

The risk of "carbon leakage" in the man-made fibres industry

It is clear that, given the strong competition from Asian countries and the low margins which result, inclusion of man-made fibres on normal terms in the Emissions Trading System due to take effect in 2013 would certainly lead to reduction of production in Europe, and a large rise in imports from Asia, and China in particular, unless these countries make commitments equivalent to those taken by the EU under the ETS. At Copenhagen, no such commitments were given by the main non-European man-made fibre producing countries. The carbon emissions per tonne of output (due to carbon intensive energy sources and lack of treatment of emissions) in most of these countries are substantially higher than in Europe. Full application of ETS to man-made fibres in Europe would thus lead both to an **increase in global carbon emissions** and to serious **industrial problems** in Europe for the man-made fibres industry and the industrial sectors which it supplies.

CIRFS therefore welcomes the recognition of man-made fibres as a sector at risk of "**carbon leakage**", in the light of its high level of trade intensity. Under the ETS Directive, this results in compensation (free allowances at the level of a benchmark) for heat production and possibly compensation for electricity costs via national regulations, which still have to be worked out.

Recognition of man-made fibres as at risk of "carbon leakage" does not solve all problems

Man-made fibres are not explicitly mentioned in Annex I of Directive 2009/29/EC, but are affected by ETS due to their combustion installations or additional heat/electricity costs.

However, as the details of the ETS trading scheme are now being worked out, there is a very serious risk that the **compensation provided to the European man-made fibres industry will be much too limited** to avoid the danger of a serious loss of industry competitiveness at the global level, after a whole range of correction factors have been applied. This is very unfair compared to the non-European players, who after the poor result of the Copenhagen Conference, will not face a similar cost burden.

Proposed arrangements for setting a benchmark for heat production are totally unrealistic and damaging in the context of man-made fibres

The man-made fibres industry has too few production units and too large a range of products and processes to be able to propose a product benchmark. The sector will consequently rely mainly on the **heat production benchmark.** Heat is in many cases supplied via Combined Heat Power (CHP) installations. The unanimous experience (of man-made fibre producers with their own CHP installations) is that the efficiency of a CHP is strongly dependent on variations in demand and on the electricity-heat ratio needed in practice. Man-made fibres are a cyclical industry, with strong seasonal variations in demand, and the initially set efficiency benchmark of 90% is not reachable under practical CHP conditions. **The proposal to further increase the efficiency benchmark to 93% is even more unrealistic.** Additionally, **CIRFS strongly opposes the proposal to apply a yearly correction factor** of 1.74% to the heat production benchmark and other (fallback) benchmarks. The allocation amount for the exposed sectors should remain stable for a more extended period, as the idea that companies can easily and quickly switch between technologies by new investment is unrealistic both from a timescale and economic point of view.

The arrangements proposed give rise to serious dangers of distortion of competition from different CHP ownership structures

Some man-made fibre producing companies are directly within ETS because they own and operate their own CHP installations, and will have some benefit (even if not sufficient, because of the benchmark correction factor proposals described above) from the status of the industry as at risk of "carbon leakage". However, many others are not directly within ETS, because they **buy heat from a central unit in an industrial park**, of which they may be part but not full owners – this is a consequence of industrial

restructuring in recent years. This different structure of CHP ownership makes compensation for being exposed to "carbon leakage" difficult and uncertain. In particular, there is no guarantee that no ETS costs will be passed through from the heat supplier to the man-made fibre producer. **CIRFS asks that a regulation should be prepared in order to avoid distortions of competition resulting from these different CHP ownership structures.**

Different national arrangements for compensation on electricity consumption will lead to huge distortions of competition

The major part of the cost increase from ETS for most man-made fibres will be due to their **electricity consumption**. CIRFS is convinced that a regulation must be worked out to adopt financial measures in a harmonised way across Europe. However, it is the individual Member States which will decide if compensation will be given or not. Needless to say, **this will result in huge distortions of competition across Europe**, if (as seems likely) different Member States adopt different policies**.**

The situation could be further confused by national energy taxes

At national level, CIRFS also sees a risk of proliferation of **energy taxes**, related or not to CO2, which may be introduced in the coming years. These in themselves would be damaging to industrial production in the EU, and would create distortions of competition between Member States. Added to the possibility of inadequate compensation under ETS, whose dangers we stress above, and the distortions of competition which may arise from ETS, this would make the **conditions of competition** in and outside Europe for the man-made fibres industry even more adverse.

Conclusion and CIRFS proposal

The man-made fibres industry has been recognized as exposed to carbon leakage, but fears it will obtain only very low compensation for the increased costs, because of unrealistic correction factors for heat production and electricity costs compensation at national level that may be very limited or even non-existent. This will result in very serious distortions of competition at a global level, against the interests of manufacturing in the EU, but also at a European level, between companies operating in different Member States.

CIRFS proposes the following actions:

- **Given the intense competition in man-made fibres and the risk of carbon leakage, which would result in a global increase of carbon emissions, full compensation for the costs resulting from ETS must be available to EU producers.**

- **Steps should be taken to avoid distortions of competition in EU due to different structures of ownership of CHP installations.**

- **Distortions of competition due to different Member State policies on compensation for electricity cost increases are not acceptable.**

- **New regulations should be introduced as soon as possible to make these arrangements legally binding, and consistent throughout the EU**