Final (V 8) - 13 February 2014

Input to Public Consultation 'Draft Guidelines on Environmental and Energy State aid for 2014-2020'

State Aid comments/draft Cefic positioning

For 2014 the European Commission (EC) is planning a revision of the state aid rules, reshaping the Environmental and Energy Aid Guidelines (EEAG).

I. Cefic' key points

1. **Cefic welcomes the EC approach towards competitive Renewable Energy Sources (RES). This is crucial to prevent increasing consumer electricity costs and distortions of the Internal Energy Market.**
2. **The cumulative effects of EU climate policy measures must be recognized for any exemptions granted on taxes and/or surcharges: Exemptions for industry from RES surcharges but also from other residual costs are necessary, must be fact-based and proportionate to the policy cost level to avert national disadvantages vis-à-vis global competitors.**
3. **We support the Commissions intention to reform and harmonize RES surcharges and similar support schemes. Surcharges and support schemes should be minimized, fully transparent in terms of costs and objectives, and should decline over time. In parallel, specific exemptions put in place by national governments to shield their energy intensive industries from such costs should remain as long as and proportionate to, the respective cost burdens.**
4. **A Minimum burden of 20% is arbitrary and not acceptable as it would deteriorate competitiveness and investment climate for EU energy-intensive industries.**
5. **Need for flexibility at Member State level, no 'one size fits all': As long as multiple RES support schemes persist, this must result in optional choices for individually designed exemptions for industries.**
6. **Existing and well-functioning legal frameworks must not be undermined or even removed by EEAG: Maintain confidence in existing measures based on valid EU legislation (Energy Taxation Directive, Energy Efficiency Directive).**
7. **No further dis-harmonisation of the European energy and electricity tax framework: Chapter 5.6 of the EEAG shall clearly state that any exercise of the options for reductions or exemptions granted to the Member States as set forth within the ETD as currently applicable will be considered as being justified cases of state aid. Thus, no further requirements shall be imposed upon the Member States to make use of such optional reductions or exemptions, even if those are – in accordance with the ETD – granted below minimum tax levels.**

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II. General comments

Cefic fully agrees with the European Commission's assessment that vast changes have taken place in the energy market in the past decade, specifically regarding:

- RES (Renewable Energy Sources) share in total energy mix having increased significantly, while many RES technologies become more competitive
- RES generation having a distortive impact on the wider electricity market
- RES having an effect on network stability and patterns of generation dispatch
- Consumers bearing the costs of sustainability and security of electricity supply in diverging proportions without always being able to compensate / pass on these costs
- The use of certain policy instruments producing counter-productive effects.

Ultimately, Cefic asks the Commission to include the following key starting point in its further analysis: Surcharges and support schemes should be minimized, fully transparent in terms of costs and objectives, and should decline over time. In parallel, specific exemptions put in place by national governments to shield their energy intensive industries from such costs should remain as long as and proportionate to, the respective cost burdens.

Cefic welcomes the European Commission's initiative to modernize state aid, especially as we are a global industry operating in an increasingly internationalized world. The EEAG must support the objective of delivering 20% of GDP from manufacturing industries by 2020, and link in with the upcoming 2030 framework to form a coherent package that will give industry the long-term confidence required to invest in Europe: Revising the State Aid Guidelines presents an opportunity to secure the future of energy-intensive industries in Europe, protecting them from uncompetitive energy prices caused by decarbonisation policies not borne by competitors in other regions of the world. In addition, the guidelines have to take into account the EU's global competitiveness and not be limited to achieving a level playing field within Europe. Furthermore, in the absence of a relevant harmonisation at European level, the Commission should leave enough scope to the Member States in the shaping of their regulating systems. This includes to consider non-state aid subsidies as what they are and not to try to subject systems which are so far viewed as not relevant to state aid.

Thus, the Commission should adequately take into account the principles stated below:

> ***State Aid definition**: Article 107(1) TFEU defines aid as being "granted by a Member State or through State resources in any form whatsoever". Measures that e.g. exempt energy intensive industries from decarbonisation costs that do not involve the transfer of state resources are clearly not state aid. This principle was reaffirmed by the Court in PreussenElektra AG v Schleswag AG.*
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> *In some Member States such practice exists and it is vital that this can continue. The Guidelines must not deviate from the Court ruling and should explicitly state that such measures fall outside the remit of state aid controls.*

However, Cefic welcomes the Commission's willingness to recognise the need for adequate exemption rules for energy-intensive industries from surcharges and taxes. But as pointed out in detail above, the level of these exemptions should be in line with the level of the various local forms of surcharges, thus likewise Member State specific.

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III.Chapter 5.6 Aid in form of reductions in or exemptions from environmental taxes

The most important harmonised environmental taxes are the taxes levied on energy products and electricity as governed by the Council Directive 2003/96/EC. The current Council Directive 2003/96/EC for the taxation of energy products and electricity (Energy Tax Directive - ETD) strives to integrate the aims of environmental protection and the objectives of the Kyoto Protocol, i.e. objectives of abate GHG emissions; see i.e. recitals (6), (7), (25).

However, recent discussions between the Member States, the Commission, DG TAXUD and other stakeholders raise concerns that any rigid position taken by the EEAG will create an obstacle for the Member States to set ambitious national levels of energy or electricity taxation: due to restrictive state aid provisions, Member States setting such ambitious national levels of energy or electricity taxation will either face a loss of competiveness of their domestic energy intensive industry or they will face severe state aid investigations by the Commission.

Accordingly, limitations set by the EEAG for the Member States regarding exemptions from energy or electricity taxation as foreseen by the ETD will give Member States rather an incentive for lowest possible levels of national energy or electricity taxation, while still causing uncertainty for investments. Moreover, any limitations set by the EEAG will lead to discussions between Member States and the Commission to change from optional reductions or exemptions towards optional taxation rights in the course of the on-going revision of the ETD. However, such an approach of optional taxing rights clearly leads away from a harmonization of the European energy and electricity tax framework. This observation equally applies to any exemption system – whether harmonized or not – and should be taken into account in chapter 5.7. EEAG draft too.

We welcome point (176) insofar as it relates to non-harmonised taxes designed to have a comparable effect to EU ETS on electricity prices and which are not implemented to satisfy Council Directive 2003/96/EC. However the exemptions or reductions from tax on electricity as set forth by the Council Directive 2003/96/EC do not distinguish whether the electricity tax is borne by the supplier and passed on to the electricity user as indirect tax cost or whether the electricity tax is directly borne by the electricity user (direct tax cost). In both cases, the electricity user is entitled to carry out exemptions or reductions from electricity tax, provided that the criteria as set forth by the Council Directive 2003/96/EC and the respective national laws on electricity tax are met.

To avoid further dis-harmonisation of the European energy and electricity tax framework, chapter 5.6 of the EEAG shall clearly state that any exercise of the options for reductions or exemptions granted to the Member States as set forth within the ETD as currently applicable not be considered state aid and thus outside of scope of the EEAG. Thus, no further requirements shall be imposed upon the Member States to make use of such optional reductions or exemptions, even if those are – in accordance with the ETD – granted below minimum tax levels.

As a consequence the current wording of point (175) is not appropriate: aid, allowed in accordance with the ETD, even below the minimum tax levels, should be considered as a harmonised environmental tax.

With regard to (176c) the EEAG should state that the aid may be paid to the beneficiary in the year in which the costs are incurred or in the following year, based on the respective production levels. If the aid is paid in the year in which the costs are incurred an ex post monitoring mechanism might be in place to ensure that any over-payment or under-payment of aid will be repaid.

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IV. Chapter 5.7 Aid in the form of reductions in funding support for electricity from renewable sources

In general, this section should be future proofed by broadening the scope to include all forms of renewable energy and not just renewable electricity. Hence, Cefic suggests changing the title above accordingly and replacing 'electricity' by 'energy'. Moreover, this chapter recognizes that RES surcharges aiming to improve environmental protection are likely at the same time to cause a significant increase in production costs for energy intensive companies, that cannot be passed on to customers without leading to significant loss of business activity and related employment, technological skills and innovative capability. Thus, exemptions from these surcharges or similar forms of costs are recognised by the Commission.

Cefic acknowledges the Commission's openness to allow for Member States compensation for additional costs caused by the specific national energy mix so as to facilitate the overall funding of support to energy from renewable sources and avoid carbon leakage. Member States introduced a variety of measures to meet the EU-obligated 20% Renewable target by 2020. These different national mechanisms lead to diverse cost burdens on energy consumers throughout the various EU Member States. In countries with high cost burdens, energy intensive industry is particularly vulnerable to carbon leakage. We therefore urge the European Commission to respect the Member States individual approaches to reach the 20% renewables target and allow for country specific mechanisms to ensure relevant safeguards are in place for vulnerable and energy intensive energy consumers in areas with a generally high cost approach. A unilateral 'one size fits all' assessment of proportionality may punish energy intensive industries located in countries with a high share of costly renewables energies. Safeguards in place for vulnerable and energy intensive consumers in areas with a generally high cost approach, should be maintained for as long as the relative cost disadvantage versus competitors and the risk of carbon leakage is likely to exist.

Hence, Cefic's main demand is the following: Due to a lack of harmonization of different support schemes for RES a large variety of different exemption rules and systems exist throughout the 28 Member States. When recognizing exemptions from RES-costs, the European Commission needs to take into account the difference in Member States' approaches to these exemptions schemes by allowing comparable flexibility in the respective criteria. Cefic therefore suggests that the EEAG should cover not only a sectoral approach as proposed in the EEAG draft but also alternative criteria as stated below (section a and b).

Furthermore if the Commission wants to harmonize the exemptions on the surcharges, first, the principle of involvement of the State must be controlled, and, secondly also a maximum level of surcharge should be defined in an harmonized way in order to ensure that harmonization in exemption effectively leads to a level playing field for consuming industry.

Finally, this type of aid should be explicitly permissible for all the costs of a Member State's decarbonisation policies, including the funding of investment in new nuclear and other non-renewable low carbon generating capacity and the costs of addressing the variability of wind generation through for example the introduction of a capacity market.

a. Sectoral approach as set forth in the EEAG draft

Criteria trade intensity and electricity intensity (184 and 176a): DG COMP proposes sector eligibility based on the cost increase incurred as a percentage of GVA and on trade intensity. These criteria stem from the Carbon Leakage (CL) list definition under the EU ETS Directive. Operators

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within a sector may then become eligible on a comparable basis to the sector as a whole (185). But, depending on economic developments companies/operators can fall in or out of eligibility under either criteria adding to investor uncertainty. Also, for state aid purposes, where minimising trade distortions in the internal market is the paramount concern, the trade intensity calculation should of course include intra-EU trade.

The trade intensity of a company/operator in the chemical sector may reflect neither the strong value chain character of the industry as a whole nor the costs or general challenges of transporting multiple base feedstocks. Rather, the energy cost intensity is illustrating the cost impact on a company, since evaluated over their total value chain up to end product level nearly all products are exposed to import substitution. Hence, many companies/operators might fall through the cracks of such a statistic, even though they make an important contribution to a trade intensive value chain. Furthermore, low trade intensity in a particular time period does not exclude exposure to international competition.

The definition is further not reflecting real cost burden on industry due to climate and energy policy. It does not take into account surcharges on electricity or higher energy costs due to energy mix steering. Consequently, criteria to evaluate the threat of carbon leakage based on trade intensity or energy intensity or a combination of both will tend to give only a snapshot evaluation as they rely on historical data and can at best provide a limited picture of the future impacts of a cost shock on the exchange of goods inside and outside Europe. Energy cost intensity should be taken as recognizing the impact of additional energy costs on an operator~~,~~ while trade intensity can be taken into account as an additional criterion.

The eligibility criteria should be therefore based on the cumulative effect of all de-carbonization and other environmental costs, including costs from environmental taxes, capacity payments, the cost effect of steering of the energy mix and the impact of EU ETS on power prices. It is the cumulative cost effect which is important for industry. Therefore, in order to ensure unintended competitiveness impacts are effectively mitigated, the cost impacts of Member States' multiple decarbonisation measures instruments within should be aggregated when assessing the impact of production costs against GVA thresholds.

The criteria should then be applied in analogy to the three combinations of the direct CL list, i.e. for highly electricity intensive sectors/subsectors, highly trade intensive sectors/subsectors or a combination of both with lower respective thresholds as already proposed in earlier drafts of the EEAG.

Proposal for Number 184 and 176b:

184 and 176b) In order to ensure that the aid has an environmental effect the aid should be targeted to avoid that without a reduction in the financing burden, certain sectors are at risk of relocating outside the EU. The aid should be limited to sectors that are exposed to a significant risk of carbon leakage due to the cost burden of energy and climate policy. Accordingly, the aid can only be granted if

(a) the sector intensity of trade (incl. intra EU trade) is above 10% AND the costs of climate and energy policies lead to a substantial increase in production costs calculated as a proportion of the gross value added amounting to at least 3%.
OR
(b) the costs of climate and energy policies lead to a particularly high increase in production costs calculated as a proportion of the gross value added amounting to at least 10%
OR

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(c) the sector intensity of trade (incl. intra EU trade) is particularly high and above 20%

If neither of the above mentioned alternative criteria is met the burden of proof is on the Member State to demonstrate that the beneficiaries cannot pass on the cost increase to customers without leading to important sales reductions (qualitative criterion)

In order to provide the predictability to encourage investments, exemptions from these added costs should be granted for as long as the causes for those additional costs exist, e.g. RES surcharges or taxes. The necessity to provide longer term assurances to address carbon leakage were also included in the EU Commission 2030 Climate and Energy communication from 22 January 2014.

b. Exemption schemes in accordance with criteria set forth in the ETD

As stated above, Member States implemented different exemptions schemes to sustain competitiveness of their energy intensive industries. Those systems – in case they constitute state aid – have to be granted by the European Commission as well. For this purpose, we suggest a new paragraph following the current (184) which takes into account the remarks below.

Cefic requests that similar possibilities foreseen under the ETD should be equally taken into account:

- Exemptions for energy intensive businesses (cfr. ETD definition) that have concluded an energy efficiency agreement or that fall under a tradable permit scheme
- Exemptions for all manufacturing businesses that have concluded an energy efficiency agreement or that fall under a tradable permit scheme
- Exemptions for Eligible processes: electrolysis, chemical reduction, metallurgical processes
- Exemptions for Electricity when it accounts for more than 50% of cost of a product

Such exemptions schemes must be granted that apply the respective criteria when defining energy intensive companies.

In fact the electricity cost intensity is illustrating the cost impact on a company. This is accurately reflected in Art. 17 (1) a of the ETD criteria which we suggest to use here:

- Energy intensive businesses:
  - the purchases of energy products and electricity amounts at least up to 3% of production value
  - Cost increase by 0,5% of GVA

V. Further remarks on chapter 5.6 and 5.7

Minimum burden (186b and 176 and 179)

In the current draft of the EEAG conditions put forward in the chapters 5.6 and 5.7 do not reflect the economic reality and the different exemptions systems in the following aspects: Energy generation installations and energy intensive manufacturing plants share the characteristic of being highly capital-intensive with long lifetimes of 20-30 years. Therefore, they rely on

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investment security over those periods. Hence, the guidelines proposals below are absolutely inadequate:

- A minimum financial burden of 15% (until 31.12.2017) and 20% (as of 2018) in para 186b
- Minimum indirect tax burden of 20% (176c)
- Minimum tax payment of 20% (179a)

Cefic believes that these criteria contradict the aim of avoiding competitive disadvantages and do not create additional environmental advantages. They also undermine the existence of well-functioning voluntary agreements in certain Member States. Manufacturing's cost disadvantages vis-à-vis competitors in other world regions can only be appropriately compensated if EU energy intensive companies are granted up to a full relief as long as RES cause additional costs due to levies etc.

The EEAG suggest that aid should be limited to sectors that are exposed to a significant risk of carbon leakage due to the funding of support to energy from renewable sources or environmental taxes. However, not only RES create surcharges, but all costs should be taken into account. The split of the total costs into different parts, each to fulfil certain criteria in order to receive aid, should be avoided. Indeed in Member States with multiple decarbonisation measures in place the cumulative impact of multiple 20% residual costs can of itself seriously damage industries competitiveness.Consequently, the minimum burden should be dropped.

Lump sum payment Number 186 a

(for the respective comment on Lump sum payment regarding 176c see above)

We refer to our general comments on Section IV on the Commission's mandate to regulate national aid in such detail.

Cefic asks for clarification regarding the payment as a lump sum amount. This cannot be the manner of granting exemptions. If, as suggested, any reduction should take the form of a lump sum payment this will create an unnecessary financial and administrative burden and push up additional pre-financing costs. It is rather complex for companies to determine the lump sum payment as a valuation needs in case of a certificate scheme. So basically it would pave way for an extra red tape. In any case, a tax credit approach does not ensure full protection against loss of competitiveness since there are no equal cost burdens in the different Member States.

Self-generation (proposed amendment for 181)

In number 181 the European Commission proposes that all energy consumers should bear the cost of RES funding. With regard to own electricity consumption which is generally made in efficient and ecologically advantageous CHP plants throughout the chemical industry, we suggest that own industrial electricity generation should not generally contribute to the financing of RES. In addition to the ecologically friendly technologies used, own electricity production contributes to grid stability and therefore to the security of supply.

In order to avoid these advantages, we propose an addition to RN 181 to clarify the meaning of "energy consumers": ***In principle, all final customers who externally purchase electricity from the public grid should bear the cost from such funding for that portion.***

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VI. Aid for CHP

a. Operative Aid

In note 150-152 of the latest EEAG draft the Commission considers operational aid for CHP only compatible with state aid under the same conditions applying to aid for deployed RES (for new CHP) and for existing biomass (existing CHP). The respective conditions can hardly be applied to industrial CHP which receives operative aid in a wide range of forms, e.g. tax reduction, FIT, exemptions from charges financing RES etc. All these different forms of exemptions/aid must be taken into account when defining conditions for promoting high efficient CHP.

Accordingly, conditions for the aid for CHP cannot be covered by the respective chapters for promoting RES. Intermittent and not intermittent technologies (such as CHP) have both a positive environmental impact. Aid for CHP however needs to be covered by a different chapter reflecting the remarks in the previous passage.

b. Investment Aid

The draft EEAG suggest to reduce investment aid for cogeneration to 65 % (small enterprise), 55 % (medium sized enterprise) 45 % (large enterprise) of the eligible costs. In the present environment State Aid guidelines the limitations are respectively 80%, 70% and 60%.

In Cefics opinion the suggested changes openly contradict one important aim of the new Energy Efficiency Directive (EED): the promotion of cogeneration (see hereafter some extracts from EED):

- ***The provisions*** *of Directive 2004/8/EC on promotion of cogeneration* ***should be strengthened*** *(recital 12),*
- *High-efficiency cogeneration has significant potential for saving primary energy which is largely untapped in the Union. Member state should carry out a comprehensive assessment of the potential for high-efficiency cogeneration. These assessments should be should be updated to provide investors with information concerning national development plans and contribute to* ***a stable and supportive investment environment****. (recital 35),*
- *To maximize energy savings and avoid energy saving opportunities being missed, the greatest attention should be paid to* ***the operating conditions of cogenerations units****. (recital 38)*

The propositions of the draft EEAG do not help promoting CHP – on the contrary they further worsen an already difficult investment situation: CHP becomes in many Member States less and less attractive for chemical companies even though they could help to improve energy efficiency. As gas prices in the EU remain high and due to an increased level of subsidized RES in the electricity market wholesale electricity prices alone do currently not allow a reasonable CHP profitability. We therefore recommend keeping the existing limitations (80%, 70% and 60%) for the investment aid for new CHP.

VII. Capacity mechanisms

With regard to capacity mechanisms the key driver of all actions must remain a well-functioning internal energy market across the EU delivering internationally competitive energy costs for industry. We welcome the guidelines in this respect as they foresee that all other measures must have been profoundly assessed so that capacity payment mechanisms remain a measure of last resort. Secure energy supplies are critical to the operation of many energy intensive manufacturing processes and the presence of larger numbers of intermittent, insecure generators leads to the need for generation adequacy measures in an attempt to maintain secure energy supplies. For energy-intensive industry capacity payment mechanisms mean basically another level of cost burden which adds to the existing cumulative charges in order to achieve respective the EU energy and climate policy targets. Most importantly, as the issue of reduced competitiveness of conventional generation is created by subsidies (for RES) in the first place, it is a mistake to try to resolve it with more subsidies. Rather RES should bear any cost associated with maintaining sufficient discretionary (read: conventional) back-up generation on-line.

In any case, if capacity mechanisms cannot be avoided after all, Cefic calls for exemptions from these additional surcharges for large industrial customers which are exposed to Carbon Leakage for the same reasons as described above with view to RES surcharges.

VIII. Aid for RES

Cefic welcomes the Commissions attempt to avoid windfall profits in the RES aid by setting limitations in time and implementing technology neutrality. However we remain concerned that there is no thorough assessment for RES aid regarding its alignment with the more general objective of the common interest.

Cefic agrees with the EC that RES should be developed as an integral part of the broader energy system, and therefore be exposed to the cost-saving effects of liberalised energy markets. Mature RES technologies should take on the same responsibilities as other power producers, not least as regards balancing obligations and grid connection costs. Subsidy schemes provided to both traditional and RES electricity sources should be phased out to ensure a level playing field and competitive costs to energy consumers. **Regrettably, the Commission proposes very firm criteria for industry exemptions from RES surcharges. On the other hand, the EC does not take the opportunity to provide a timeframe within which Member States should improve their inefficient and costly RES subsidy schemes; this is a disappointing omission and suggests the relative priority given to the importance of a maintaining a competitive manufacturing base in Europe.** We further encourage the Commission to urgently focus more on transparency for all energy sources and equally compare costs and benefits, in terms of competitiveness, security of supply <u>and</u> sustainability.

IX.Aid for CCS

CCS could become an economically viable solution if alternative lower cost alternatives have been exhausted and technology improved respectively. Ultimately, market conditions alone must determine the preferred technology to reduce carbon emissions most cost effectively.[1]

[1] For further information please find below the link to the Cefic position on CCS from June 2013: http://www.cefic.org/Documents/PolicyCentre/Cefic-answer-EC-consultation-on-CCS.pdf

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