Inquiry into EU Climate Change Policy

Sub-Committee D of the House of Lords' European Union Committee

Evidence submitted by the **Energy Intensive Users Group**

Note: The Energy Intensive Users Group (EIUG) represents the sectors of UK industry for which secure, internationally competitive energy supplies are a matter of commercial necessity. EIUG is the UK member of the International Federation of Industrial Energy Consumers (IFIEC) which represents these sectors at a European level.

1. The Commission this year is expected to review their programme on climate change.

    - Is the EU approach to climate change appropriate both for achieving its Kyoto targets and maintaining competitiveness?

    - Is the balance between Member State and EU action correct?

Many EU countries' Kyoto targets are so far removed from their current status that meeting them is unlikely to be achievable whilst maintaining competitiveness. The situation within the UK is unusual in that, unlike all the other EU states apart from Sweden, we are on track to meet our Kyoto commitments. The UK's competitive position would however be undermined if we become the only state in the EU to require emissions reductions beyond our Kyoto commitments, as recently proposed (until other states clarify their position, the extent of the resulting impact on competitiveness is difficult to quantify).

2. Given that the Commission recently warned that only the UK and Sweden are currently on course to meet their emissions reduction targets under the Kyoto Protocol, how can the EU live up to its commitments under the Protocol?

The EU can live up to its commitments by reducing emissions internally (e.g. substituting gas for coal generation, improving energy efficiency, etc.) and externally, by purchasing emissions credits (e.g. carbon trading with Russia, in the event that it ratifies the protocol, or by financing schemes outside the EU via Joint Implementation or Clean Development Mechanisms). Unfortunately, the scale of the emissions reductions required in some states means that the costs of compliance will be high, risking significant economic damage.

- What measures should be taken against those EU countries not on course to meet their targets under the Protocol?

It is difficult to see what can be done to force countries to meet their Kyoto targets, unless the extent of under-performance (and hence the cost of rectification) is trivial, in which case the threat of fines or other punitive action might be a realistic possibility. An example recently highlighted by PwC is the case of Spain, which is so far adrift from its target that the cost to business of complying with its commitment could be as much as 3.6 billion euro a year. The level of sanctions which would be required to force Spain into compliance could be so great that the member state is forced to conclude that they simply could not afford to comply.

- What impact might inaction by individual Members States have on the EU as a whole?

Inaction by individual member states will mean that the EU will fail to achieve its overall Kyoto target. However, it will also result in those states gaining a competitive advantage over others in the Union (such as the UK) who remain committed to meeting their targets, even if this means imposing increased costs on manufacturing industries, especially through high energy prices.

- How will the accession of ten new Member States affect the EU's climate change ambitions?

The short-term ambition of imposing an emissions trading regime would be made easier with the availability of 'hot air' – the spare emissions credits available in many accession countries (largely arising as a result of the post-Soviet economic collapse). It remains to be seen whether the accession countries will be as enthusiastic to constrain emissions (and economic growth) as the current EU member states in the longer term.

- The UK will hold the Presidency of the EU in the second half of 2005; what should be their priorities to achieve a sustainable policy on climate change?

A priority of achieving a sustainable policy on climate change would be most welcome. Current EU policies are unlikely to be economically sustainable, as those states furthest adrift from their Kyoto commitments are starting to realise. Promoting measures that pose a fundamental threat to the EU's long term industrial competitiveness is counterproductive. This is a particular concern for energy-intensive industries that depend on internationally competitive energy supplies. If production in these industries is forced offshore, there is a loss to the EU economy but no benefit in terms of global emissions.

The UK might wish to consider how the balance of emphasis on emissions control within the EU might shift from the current focus on industry (where emissions are already declining, and competitiveness is under threat) to the domestic and transport sectors.

3. How well understood is climate change amongst the general public at large?

    - Do many people know of its current and predicted effects? Do people know of its causes? Do people know what they can do to reduce greenhouse gas emissions and to mitigate the effects of climate change?

The means available to control industrial greenhouse gas emissions is well understood by those in manufacturing industry, where the associated emissions have been on a declining trend in absolute and relative terms for many years, and of course in the energy industries themselves. Willingness to take action appears to be comparatively low in the public, domestic, service and transport sectors, where the associated emissions continue to rise.

    - Is the EU effectively communicating the urgency of climate change?

There is a danger in exaggerating for effect when discussing the urgency of anticipated climate change and the extent to which human activity can influence it, as this may have the opposite effect to that intended.

Recent reports claiming that a third of animal and plant species could become extinct by 2050 as a result of climate change, and the comments by the UK's Chief Scientific Adviser trivialising the threat of international terrorism relative to that of climate change, are misleading. If people are to be persuaded that climate change is a serious issue, it needs to be discussed in ways that make it relevant to the general public, without resorting to inappropriate comparisons of risks.

4. Are EU policies regarding energy and renewable technologies compatible with climate change policy? Should there be more integration between these initiatives?

EU policy is inconsistent. Support for renewable electricity generation is largely ideological in origin rather than being based on sound science and economics. With the exception of large scale hydro electricity, renewable generation generally represents poor value for money in terms of the reductions in greenhouse gas emissions that it delivers. The current level of investment across Europe in expensive, subsidy-dependent intermittent wind generation fails to recognise that this form of generation still requires a permanent back up from

fossil fuel or nuclear sources. Additional investment to extend and modify electricity transmission and distribution systems to accommodate new renewable generation is often also required. Investment should be justified on the basis of value for money and where externalities associated with that investment have been internalised. There is no good justification for renewable generation be treated as if it is uniquely exempt from such requirements.

European climate policy aims are not assisted by national policies to phase out the use of nuclear power, the principal zero carbon source of electricity in Europe providing 75% of supplies in France, 47% in Sweden, 33% in Finland, 31% in Germany, 30% in Spain and 26% in the UK. Renewables cannot replace capacity on this scale in the timeframe required. In the absence of carbon sequestration, all the fossil fuel alternatives would necessarily raise emissions. Emissions cuts, such as those envisaged in the UK, are therefore impractical for the foreseeable future unless there is a continuing, possibly expanded role for nuclear generation.

5. The EU Emissions Trading Scheme will come into operation in 2005.

- How well are Member States progressing with the implementation of the scheme?

Many EU states appear to be struggling to implement the scheme in accordance with the prescribed timetable. Only one state (the UK) had even put the emissions trading directive into law by 31 December 2003, as required. Only a couple of states have so far published their draft national allocation plans, which themselves may or may not meet the approval of the Commission. Germany has announced that it may not publish its plan on schedule, citing that “thoroughness is more important than speed”. There are real fears that a significant number of states may be unready to participate in the scheme if it goes live on 1 January 2005, as intended.

It is interesting to note that the pioneering USA emissions trading scheme (for sulphur, rather than carbon emissions) needed two years for the details of allocation, caps, etc., to be agreed before trading could take place in a single national market, affecting around 250 industrial installations. Yet it is proposed that a much more ambitious process will be completed in the EU within a year, in a group of fifteen existing states and ten new ones, most of which have hundreds of affected installations (there are around 1,400 in the UK alone).

- Has it been well designed?

Further changes are still possible before the scheme goes live, but even at this stage there are concerns about potential issues of state aid and other internal distortions of trade which could arise as a result of the differing approaches

member states are taking to implementation. The most efficient design would place no artificial limits on the extent to which external trading can take place.

- Is there a role for other economic instruments to be used alongside emissions trading?

There is currently a plethora of measures (renewable supply obligations, guaranteed sales prices for renewable electricity, downstream energy taxes, etc.) that impact the European energy markets. Carbon trading is unlikely to achieve its potential to deliver emissions reductions at least cost whilst it is competing with this variety of other instruments some of which may well be incompatible.

6. The EU has played a significant role in international negotiations on climate change.

- What role should the EU play in shaping future international objectives after the 2008-12 commitment period laid down in Kyoto?

The EU might consider whether it is wise to continue pursuing a Kyoto-style approach to international negotiations on climate change. The increase in greenhouse gas emissions from developing countries in the decades ahead will far outstrip any reductions that EU and other developed countries can realistically hope to achieve. Emissions from China, for example, will soon be comparable with those from the USA (if current growth rates persist). A policy that ignores these realities will carry neither intellectual nor political credibility.

- How effective is the EU in international climate negotiations?

No one could criticise the EU for failing to put an effort into climate negotiations, but it is appropriate to question what this approach has actually achieved. A 'Kyoto-or-nothing' stance has not won converts in the USA or Australia (which have rejected the protocol) or in Russia (which may well do likewise). There is a very real possibility that the protocol may never come into effect. It is to be hoped that lessons will be learned from this experience for the future.

- How could it be more effective in encouraging those states yet to ratify the Protocol to re-engage in international discussions?

- How can the EU best exert pressure on developing countries to keep emissions under control whilst expanding their economies?

There is an implication in this question that it is a proper function for the EU to 'exert pressure on developing countries', presumably by threatening trade sanctions. Given that the EU is unlikely to achieve its own Kyoto targets, the key question remains whether the EU should "go it alone" in sticking with its Kyoto

commitment or seek to find an alternative approach which gains greater global commitment.

Historically, emissions reductions have largely come about for economic reasons – be they positive, from new technological opportunities (e.g. the 1990s 'dash for gas') or negative (e.g. the post-Soviet economic collapse in Eastern Europe). If the EU is serious about encouraging a global transition to low carbon technologies, it would be more productive to work with the economic grain, rather than against it. One does not need to 'exert pressure' on countries to adopt cheaper technologies (unless they are opposed to free markets). A more sensible approach would be to invest in research and development with the aim of rendering low carbon technologies cheaper and therefore more attractive in their own right. These might include carbon sequestration (recognising that fossil fuel generation will be a fact of life for the foreseeable future) as well as nuclear and renewable technologies, and the use of hydrogen or other energy storage media, especially for transport purposes.

It would seem sensible for the EU to accept that global emissions of greenhouse gases are set to rise during our lifetimes (and indeed those of our children) under all conceivable scenarios, even if every developed country in the world adopted the most ambitious reduction targets, such as those recommended by the Royal Commission on Environmental Pollution. The world will therefore have to adapt to any consequential climatic change, and incur the costs (or benefits) of adaptation. These facts should be borne in mind when considering what emission controls measures might prove applicable, on a cost-benefit basis, to developed and developing countries alike, but on a much more long term basis.