

HT 359 – Consultation on Community Guidelines on state Aid for Environmental Protection

Draft Guidelines on environmental and energy aid 2014 – 2020

Response from the Energy Intensive Users Group

Introduction

The UK's Energy Intensive Users Group (EIUG) represents manufacturing sectors including steel, chemicals, paper, mineral products, glass, ceramics and industrial gases that operate in global markets and depend on access to secure, internationally competitive energy supplies to remain in business. These industries employ 225,000 workers directly, providing indirect employment for over 800,000 workers, and contribute over £15 billion to UK GDP. EIUG is the UK member of IFIEC Europe (the International Federation of Industrial Energy Consumers) which represents these industries at a European level, and is also responding to this consultation.

Secure and competitive energy supplies are of fundamental importance to the Union's economic future.

Energy intensive industry (EII) also plays a vital role in the Union's economy. Many EIIs provide the foundation of large and valuable supply chains, whose competitiveness would suffer if those EIIs no longer existed in the Union. Others supply materials and products into the construction industry. The Union's economy would suffer immense strains if these materials and products had to be imported because it was no longer profitable to make them in Europe.

It is therefore of critical importance that, in addressing this new area of state aid guidance, the Commission promulgates rules that actively facilitate these two objectives: the development of secure and competitive energy supplies and the protection of EIIs' competitiveness.

Aid to energy from renewable energy sources

EIUG supports the Commission's objectives of reducing the costs of renewables support and reducing the distortion of trade in renewable energy caused by national subsidy regimes.

EIUG therefore welcomes the differentiation between "deployed" and "less deployed" technologies, with the requirement that aid to the former must be "granted in a genuinely competitive bidding process on the basis of clear, transparent and non-discriminatory criteria". This market response to the financing of renewables should be less costly and should minimise the risk of renewables operators being over-subsidised.

Paragraph 120 (c) requires that "aid is granted by way of a feed-in-premium or *equivalent measures involving the direct marketing of the electricity produced.*" EIUG assumes that the italicised equivalent measures would embrace the UK's

proposed contracts for difference (CfD). EIUG is not convinced that CfDs are the most cost-effective means of subsidising low carbon generation. Nevertheless given the current state of the UK's power market, it would be counter-productive to use the state aid rules to require the UK to re-think its energy strategy. EIUG would therefore welcome approval of the UK's CfD proposals under this clause, subject to a more rapid move to an auctioning system to establish the strike prices than currently proposed.

EIUG is however disappointed that section 5.2 of the draft refers only to renewables. It is the right of each Member State to determine their own energy mix, subject to the achievement of their 2020 targets. It would therefore be more appropriate for section 5.2 to apply to all forms of low carbon generation, including nuclear and the use of fossil fuels with carbon capture and storage.

Aid in the form of reductions in or exemptions from environmental taxes

EIUG welcomes the concept introduced in paragraph 176, which will enable the Commission to approve the UK's proposal to compensate certain EIs for the costs of its Carbon Price Floor tax.

We do however have grave concerns about the proposals regarding eligibility and proportionality, which are dealt with below, as the same proposals also occur in section 5.7.

Aid in the form of reductions in funding support for energy from renewable sources

EIUG also welcomes the Commission's recognition that EIs need protecting from the adverse impacts on their competitiveness of the costs of decarbonising the Union's energy supplies.

We do however reiterate that this type of aid should be explicitly permissible for all the costs of a Member State's decarbonisation programme, 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 and the cost of extra infrastructure grid and balancing charges.

More importantly, EIUG believes that the detail of the Commission's proposal needs substantial revision in two respects:

1. Eligibility

The Commission's proposal is seriously flawed. The Commission is proposing two arbitrary and inflexible thresholds which must both be met. However, with little experience of assessing this type of aid, the Commission may well be excluding from it undertakings that are at genuine risk of going out of business. These thresholds have been read across from the EU ETS Directive, which at least contained the safeguard of applying a qualitative assessment as well as a quantitative test.

EIUG recognises the importance of ensuring that eligibility is established as fairly as possible across all Member States paying this type of aid, but we believe it is far too early for the Commission to be setting hard and fast thresholds such as those being proposed. To exemplify our concerns, following are some of the failings we have identified:

- The GVA test discriminates against labour intensive sectors, which by definition have a higher GVA - and Gross Operating Surplus or EBITDA would be a fairer measure that does not discriminate against extra jobs.
- Under paragraph 176, the electricity intensity test would apparently be assessed at the level of “consumers” – i.e. at the level of the individual undertaking, as currently applied by the UK for its EU ETS compensation scheme and proposed for its Carbon Price Floor compensation scheme. The same test under 184 would apparently be applied at the sector level. The use of a rigid threshold can lead to distortions under both approaches. Under the first approach, undertakings operating within the same sector will be treated differently if one undertaking narrowly exceeds the threshold while another narrowly misses it. On the other hand, a simple sectoral approach can result in undertakings becoming eligible which are not genuinely electro-intensive. There needs to be some means of including companies making unique electro-intensive products / operating unique electro-intensive processes when measured in one country, whereas the sector as a whole at EU level might not qualify.
- The suggested 5% threshold is ten times greater than one of the criteria for energy (not electricity) intensity stipulated in the Energy Tax Directive¹. Differences of this magnitude demonstrate just how arbitrary a simple threshold test can be. We therefore propose that the threshold is, as previously, 0.5% if GVA has to be used.
- Historical trade intensity is not necessarily an adequate indicator of future trade exposure: for example, loss of cost competitiveness may result in increased levels of imports of products which, prior to this cost distortion, had not been significantly traded. Intra-EU and extra-EU trade intensity should be used as there has been transfer of electro-intensive businesses already between EU countries directly as a result of electricity price (e.g. from UK to France and Germany)

EIUG therefore urges the Commission to adopt a more flexible approach. Member States should be free to use alternative methodologies to determine eligibility. The Commission will then have the ability to check on a case by case basis that the proposed methodology does genuinely target only those undertakings that are in need of “competitiveness” aid as a result of incurring burdensome costs which they are unable to pass on, while at the same time avoiding intra-sectoral distortions.

Additionally, it is essential that the Guidelines explicitly allow for the cumulative effect of multiple decarbonisation measures. Eligibility must be assessed taking account of all measures that impact artificially on electricity prices, even when a Member State proposes to provide aid only for a selection of those measures. For example, the UK

¹ Council Directive 2003/96/EC

currently has four decarbonisation measures that increase industrial electricity prices², shortly to rise to six when its Electricity Market Reform proposals are implemented³. If eligibility were to be assessed on the basis of the each measure taken in isolation, many undertakings/sectors in genuine need of competitiveness aid would fail the test. Other Member States may have just one, large scheme to incentivise decarbonisation. Competing undertakings in these Member States would qualify more easily. Cumulative assessment must therefore be allowed in order to minimise competitive distortions.

Finally, some EII sectors may not meet a trade intensity test because they provide products only to other EII sectors who are trade exposed. They may be able to pass their costs on to their consumer sectors, but under the Commission's current proposals these additional costs would not be eligible for aid. The adoption of a more flexible approach would enable the Commission to authorise aid for such cases when its necessity can be clearly demonstrated.

² The EU ETS, the Carbon Price Floor, the Renewables Obligation and the Feed in Tariffs for small-scale renewables.

³ The Contracts for Difference for both renewables and nuclear and the proposed capacity market.

Proportionality

The draft Guidelines define “proportionality” as: “the aid amount is limited to the minimum needed to **incentivise the additional investment or activity in the area concerned**” (emphasis added).

In the case of competitiveness aid however, the purpose is not to incentivise additional investment or activity. The purpose is to protect EIs from the collateral damage they suffer from other policies. Aiding only a proportion of the costs serves no purpose whatsoever. It does not meet any policy objective. It does not incentivise any action to meet an objective of common interest⁴. It merely ensures that the affected EIs continue to suffer a proportion of collateral damage. Therefore, exceptionally in this instance, EIUG insists that aid intensity of up to 100% should be allowed.

Aid for generation adequacy

EIUG is not convinced that capacity mechanisms are necessary. In a properly functioning market, the market itself should be capable of ensuring that standby capacity is available.

Nevertheless, we recognise that Member States are increasingly resorting to capacity mechanisms, and it is therefore appropriate that the Commission develops guidelines to ensure that such mechanisms minimise both market distortions and the costs imposed on consumers.

In this context, EIUG reiterates that state aid should be allowed to compensate EIs for, or exempt them from, the additional costs of capacity mechanisms where these clearly arise as a direct result of environmental policy (e.g. to ensure the availability of additional dispatchable backup to compensate for the unreliable output of intermittent renewable power generation).

⁴ Energy efficiency improvements by EIs are already incentivised by a host of other measures that impact directly on them, including the EU ETS, energy taxes, energy efficiency agreements – plus of course the high price of energy in the EU even without decarbonisation policy measures.