

# CONTRIBUTION TO THE PUBLIC CONSULTATION ON THE

## REVISED CLIMATE, ENERGY AND ENVIRONMENTAL AID GUIDELINES (CEEAG)

### OUR KEY MESSAGES

#### Protection of energy intensive industries (EIIs) against undue energy costs

- Several elements of the draft proposal on the CEEAG on **reductions from electricity levies for energy-intensive users** and **reductions in environmental taxes** pose an excessive burden on the steel industry, increasing the risk of carbon leakage, and discourage the uptake of low carbon technologies that rely directly or indirectly on electricity.
- **State aid intensity for reductions**, which is limited at 75% in the draft CEEAG, must be **maintained at 85%** as in the current phase 2013-2020 (paragraph 359). Protection for the **most exposed undertakings** should be kept at the level of **0.5% GVA**, instead of the proposed 1.5% GVA (par. 360).
- The above reductions/exemptions shall apply analogously to **other charges that directly or indirectly fund the implementation of EU climate change policy objectives** set out in the European Green Deal and that result in **undue energy costs for EIIs**, such as those related to capacity mechanisms, network costs, and other similar charges (par. 354).
- The eligibility criteria do not include the option of 4% trade intensity and 20% electro-intensity that was present in the previous guidelines. Due to that, the list of eligible sectors **excludes the industrial gases (NACE code 2011) – e.g. hydrogen and oxygen - from the scope of application of the reductions**. These are an integral part of the steel value chain today, and will be even more crucial for the transition to low carbon technologies in the nearest future (par. 357 and related Annex I).
- **State aid should not be made conditional**. If now state aid is made conditional to additional measures to be taken by a company, de facto it is not anymore a (partial) reimbursement of incurred costs as it requires additional costs to the company. Moreover, related proposals do not reflect the specificities of different industrial sectors and of companies and might lead to different and disproportionate outcomes (paragraphs 356, 364 and 365).

#### Aid for the reduction and removal of greenhouse gas emissions including through support for renewable energy

- Recognise that carbon pricing policies (e.g. ETS) do not counter equally the problem of externalities for all sectors and thus allow carbon contracts for difference (CCfDs) to cover the **full abatement costs** of the new low-carbon processes for sectors most exposed to international competition (paragraphs 40, 78 and 103).
- Conversion to low carbon production processes in the EU will often occur in existing facilities (brownfield). The CEEAG should envisage also **aid for dismantling CO<sub>2</sub> intensive installations** (new proposal under section 4.1.2 scope and supported activities).

- Support for the **use of electricity made from renewable energy sources in energy-intensive production processes** by levelling the costs of long-term power purchase agreements (new proposal under section 4.1.2 scope and supported activities).
- The targeted and distinct approach on **harmonised and non-harmonised environmental taxes** should be maintained to ensure **fair environmental taxation** (section 4.7 Aid in the form of reductions in taxes or parafiscal levies, draft CEEAG).

## Introduction

The Commission Communication “The European Green Deal” set very ambitious targets on climate change policy for the EU and it now encourages a debate around the necessary legislative framework for a successful transformation of the EU economy towards climate neutrality.

The European steel industry is keen to start the transformation. Our ambition is – under the right conditions - **to reduce CO<sub>2</sub> emissions by 2030 by 30% compared to 2018 (which equates to 55% compared to 1990) and towards carbon neutrality by 2050**. The sector is able to significantly advance the EU’s climate objectives as CO<sub>2</sub> emissions are concentrated in a limited number of installations that cover about 25% of EU industrial and almost 6% of EU total CO<sub>2</sub> emissions. These could have the highest abatement potential in volume amongst all industrial sectors if our projects can be implemented successfully and low-carbon steel finds its way into the market.

However, companies cannot invest today in low-carbon technologies that will entail higher production costs as there is no market which would pay a premium accounting for the additional cost of low-carbon steel vis-à-vis conventional steel products with similar properties. This is particularly true for steel, a trade-intense material, exposed to a very high risk of carbon leakage and significant overcapacities in third countries.

The difficulty of investing stems from the fact that steel is characterised by high capital and operational costs and very long investment cycles, a situation aggravated by historically low profitability. Low-carbon technologies entail for example the use of new energy carriers and feedstocks such as renewable energy and hydrogen, which would substantially increase operational costs. Such investment needs to constitute a sustainable business case in order to be able to compete with conventional steel. In this context, **carbon contracts for difference (CCfDs)** could be a game-changer, kickstarting this transformation. If well designed under the revised CEEAG, these contracts could provide substantial financial resources and underpin a viable business model to help scale-up projects and produce low-carbon steel at a commercial scale in Europe.

While the European steel industry is embarking on this major transformation path, **our sector must remain competitive throughout this phase and beyond**. There are external factors not directly controlled by the sector (most importantly, access to competitive low carbon energy/electricity and feedstock), which will play a crucial role. The CEEAG should avoid placing an excessive burden on the steel industry, increasing the risk of carbon leakage and hindering the investment capacity of the steel companies at this critical turning point.

Importantly, the EU needs a **holistic, supportive regulatory framework and enabling policies** to empower the European steel industry to further contribute to the EU’s climate objectives and sustainable growth targets; an approach in terms of policy solutions is necessary, ranging from proposals to ensure free and fair international trade, to R&D support, financing solutions, climate and energy policy, circular economy and environmental policies<sup>1</sup>.

<sup>1</sup> <https://www.eurofer.eu/publications/position-papers/a-green-deal-on-steel-update/>

As a frontrunner, the EU has the opportunity to set ambitious benchmarks on low-carbon steel globally, driving the transition of other regions in the world that today lag behind. From a long-term perspective, the EU will benefit from greater market share, once the demand for low-carbon products takes up, provided that it supports the industry addressing the technological and financial risks.

### Protection of energy intensive sectors (EIS) against undue energy costs

Under the existing EEAG (section 3.7), EIS exposed to international competition are entitled to aid in the form of reductions in or exemptions from environmental taxes and funding support for electricity from renewable sources.

This underlying principle and objective of the provisions has been retained and thus recognised in the draft CEEAG. Especially the fundamental notion that without such reductions and exemptions EIS would be placed at such a competitive disadvantage that it would have not been feasible to introduce the support for renewables at all.

### Recommendations on state intensity (paragraph 359, draft CEEAG) and protection of most exposed undertakings (par. 360, draft CEEAG)

Although these reductions and exemptions ensure the competitiveness of EIS sectors - including the steel industry - and contribute to the overall environmental objectives as they support environmental ambition in the EU while avoiding carbon, investment, jobs leakage to third countries with less environmental ambition, the European Commission's proposals substantially weaken those provisions. **Lowering the allowed state intensity from 85% to 75%** (paragraph 359), narrowing the scope of permitted aid and reducing protection to the **most exposed undertakings** by increasing the threshold of mandatory contributions from **0.5% to 1.5% GVA** would dramatically increase the risk of carbon leakage of a sector that is subject to fierce international competition and must be avoided (par. 360).

The EU steel sector has reduced both capacity and production over the last decade, with the EU share in total global production decreasing from almost 15% in 2008 to around 9% in 2018. As a result of the combined effect of increasing imports and decreasing exports, the EU became net importer in terms of quantities in 2013 and in terms of value in 2015. In 2014, the EU imported 26,3 million tonnes of steel while, in 2019 the imports were already at the level of 34,7 million tonnes.

Steel is one of the most traded goods worldwide and, at the same time, the one where the large majority of anti-dumping investigations have been initiated by G20 countries. This is a clear sign of the fact that the sector is suffering from trade distortions at global level. We recall that the gap between global steel production and demand is approximately 650 million tonnes, which is almost three times the European production capacity of around 220 million tonnes.

The profitability of the steel sector has drastically fallen. As an example, we estimated the earnings before interest and taxes (EBIT) margins for the years 2014-2016 at between 1-2 percent<sup>2</sup>. With these Commission proposals, the steel industry and other EIS would face the imminent risk of losing market shares to competitors in third countries where no comparable climate protection measures are in place or where such exemptions are provided.

Furthermore, affordable and competitive electricity prices are essential to facilitate the transition to low carbon technologies which require even larger amounts of electricity. The European steel industry estimates that the sector will need, annually, about 400 TWh of CO<sub>2</sub>-free electricity from the grid by 2050. This 400 TWh corresponds to more than seven times the steel industry's current electricity purchase from the grid. Of this, around 230 TWh would be used for the production of about 5,5 million tonnes of hydrogen<sup>3</sup>. The contribution of the steel industry to the achievement of the EU Green Deal through transformation towards electro intensive processes will increase the

<sup>2</sup> [Characteristics of European Steelmaking in the Context of Indirect Emissions Costs, NERA Economic Consulting, April 2019](#)

<sup>3</sup> <https://www.eurofer.eu/assets/Uploads/EUROFER-Low-Carbon-Roadmap-Pathways-to-a-CO2-neutral-European-Steel-Industry.pdf>

exposure of the steel industry to renewable levies. This exposure will grow with the update of the new technologies. We thus urge the Commission to maintain the current provisions of the EEAG and support a **state aid intensity at 85%** (paragraph 359) and a level of **0.5% GVA** to better protect the **most exposed undertakings**, instead of the proposed 1.5% GVA (paragraph 360).

#### **Recommendations on other charges that directly or indirectly fund the implementation of EU climate change policy objectives (paragraph 354, draft CEEAG)**

Rising shares of renewables will most likely be accompanied with increased generation adequacy measures in the form of **capacity mechanisms**. In analogy to the situation with contributions to renewables, financing such costs would equally result in **undermining the competitiveness of the steel industry and other EIs**. Furthermore, EEs offer solutions in these fields as they contribute to the stability of the grid thanks to their specific consumers' profiles. Hence, they should be also shielded from an undue extent of these and similar regulatory costs, taking into account their overall contributions to taxes and levies. We thus call on the Commission to **lift the proposed restrictions in the draft CEEAG** (paragraph 354).

#### **Recommendations on the inclusion of the industrial gases sector (paragraph 357 and related Annex I, draft CEEAG)**

In addition to direct electricity consumption, the steel sector uses significant amounts of industrial gases (NACE code 2011) for unavoidable purposes such as oxygen which have an important electricity consumption embedded. On the basis of the data from the Best Available Techniques Reference document (BREF), the embedded electricity consumption is estimated at 24 kWh/t crude steel in the EAF route and 92 kWh/t in the BF/BOF route (which is around 20-25% of the total electricity consumption in BF/BOF route). The new combined eligibility criteria exclude the option of at least 20% of electro-intensity and at least 4% that was applied until 2020. Due to that, the list of eligible sectors **exclude the industrial gases – e.g. hydrogen and oxygen - from the scope of application of the reductions**. The **lack of compensation for the electricity consumption related to industrial gases would substantially expose the steel sector to carbon leakage risk**. These are an integral part of the steel value chain today, and will be even more crucial for the transition to low carbon technologies in the nearest future, as these will require large consumption of industrial gases like hydrogen. The industrial gases sector must remain eligible for compensation under the CEEAG and the proposed criteria should thus be revised accordingly and include again the option 20% electro-intensity and 4% trade intensity (paragraph 357 and related Annex I).

#### **Recommendations on conditionality criteria (paragraph 356 and paragraphs 364 and 365, draft CEEAG)**

State aid should not be made conditional on additional requirements. In fact, this kind of state aid aims at reimbursing partially the energy consuming sectors for the costs of the climate and energy policies passed on in the energy bill. If now state aid is made conditional to additional measures to be taken by the company (i.e. investments in energy efficiency or emission reductions and carbon free power purchase agreement,) de facto it is not anymore a (partial) reimbursement of incurred costs since it requires additional expenditure to the company. As the eligible sectors are acknowledged as being at risk of carbon leakage (on the basis of market characteristics, profit margins and abatement potential), the missed reimbursement would create the conditions for the materialisation of such risk, leading to an increase in global emissions.

Furthermore, the proposed conditionality requirements are actually linked to the implementation and enforcement of other pieces of legislation (notably the Energy Efficiency Directive and the Renewable Energy Directive). However, member states retain the possibility of adopting different instruments to promote energy efficiency and renewables in order to achieve the targets set in such legislation. Therefore, the conditionality requirements would overlap and possibly collide with different national measures.

Compensation should also not be made conditional to a minimum level of the levies. Due to the very large energy consumption and the partial nature of exemptions, energy intensive industries such as steel would have major competitive disadvantage compared to producers based in third countries that do not have comparable climate legislation and related regulatory costs. Provisions on minimum contribution levels already ensure that also energy intensive industries support the funding of renewable schemes in all member states.

## Aid for the reduction and removal of greenhouse gas emissions

### Recommendations on the possibility to grant state aid for the full abatement cost (paragraphs 40, 78 and 103, draft CEEAG)

Carbon Contracts for Difference need to cover the **full abatement costs of the new low-carbon processes**, as this is the only way to create a concrete business case ensuring that projects on low-carbon steel are implemented. An improper design could otherwise result in a CCfD that would fail to make low-carbon production process economically viable.

CCfD require also to factor in the **lack of a global-level playing field compared to third countries where steel production is not subject to similar CO<sub>2</sub> costs constraint** as production in the EU. This is particularly true for materials such as steel where the pass-through of unilateral regulatory costs is not possible due to fierce international competition, as also confirmed by the low profit margins registered by the European sector.

Therefore, an effective CCfD – one that makes low-carbon steel internationally competitive – necessitates **aid at the level of the full abatement costs in the EU, i.e. the “difference” should be calculated between production costs of low carbon technologies and production costs of conventional ones, without discounting the avoided ETS-related costs**. As an example, a project that delivers emissions reductions of 2 tonnes of CO<sub>2</sub> per tonne of steel while entailing total costs of €700 per tonne of steel (after deducting possible benefits) compared to production costs of €500 per tonne of steel for conventional production (without considering ETS costs) would be granted a CCfD of €100 per tonne of abated CO<sub>2</sub> (i.e. €200€ / 2 tonnes of CO<sub>2</sub>).

**A CCfD that compensates only for the difference with the EU ETS price would fail to provide sufficient incentives** in high-risk investment in low-carbon technologies since they would remain exposed to international competition not subject to any carbon constraints. The strike price in a CCfD should cover the full cost-difference of the transformation, including operational costs and the additional investment costs (i.e. financial services for interest and depreciation), if funds for the latter are not made available under different funding instruments. It must be ensured under State Aid law that different instruments can be combined.

Low-carbon steel produced with the support of CCfDs will co-exist with conventionally produced steel for decades to come as the transition of the European steel industry will be gradual. It is therefore necessary to complement measures to stimulate lead markets for low-carbon steel with effective measures against carbon leakage.

### Recommendations on aid for dismantling CO<sub>2</sub> intensive installations (new paragraph under section 4.1.2 scope and supported activities)

Conversion to low carbon production processes in the EU will often occur in existing facilities (brownfield). Current state aid rules under the EEAG do not envisage aid for dismantling of CO<sub>2</sub> intensive installations, while 100% aid intensity is possible for the remediation of contaminated sites. Granting of **aid for dismantling CO<sub>2</sub> intensive installations after transformation to low carbon production** should be allowed under the revised state aid rules, with a level of 100% aid intensity similarly to aid for remediation of contaminated sites.

## Recommendations on support for the use of electricity made from renewable energy sources in energy-intensive production processes (new paragraph under section 4.1.2 scope and supported activities)

The **costs associated with the active use of electricity from renewable energy sources**, which can be ensured via long-term power purchase agreements, for instance generated by wind farms, are **often higher than the costs at which electricity can be purchased on the market**. With a view to the necessity of keeping electricity prices low in international competition, incentives to use renewable energy sources, and hence to contribute to the goal of climate neutrality, can be created through **compensation of the cost difference via state support measures**. It should be thus possible to support the use of electricity made from renewable energy sources in energy-intensive production processes, such as electric arc steelmaking, by compensating the extra costs involved through public aid.

## Recommendations on the definition of state aid, in light of recent European Court of Justice cases (a chapter on the notion of aid could be included in the CEEAG, e.g. before the second chapter on scope and definition)

The draft CEEAG does not take into account very recent court cases on the definition and boundaries of state aid, and in particular when it comes to exemptions for energy intensive undertakings. These Guidelines only cover measures which fulfil all criteria provided for in Art. 107 (1) TFEU. Particularly, measures which do not involve State resources shall not constitute aid within the meaning of Art. 107 (1) TFEU and therefore shall not be covered by the State aid regime. This applies, inter alia, when the respective funds are not at the disposal of the state but controlled by private parties. The ECJ recently applied these criteria in a case where funds were generated by surcharges paid by private parties in accordance with national schemes<sup>4</sup>. These funds were exclusively earmarked to finance the respective scheme and the role of the State was limited to the monitoring of the private parties involved. In this case the ECJ explicitly held that these funds were not at the disposal of the state and therefore no State resources were involved. Given the lack of State resources, the exemptions for energy intensive undertakings did also not constitute State aid, given that the system was entirely financed by private players. As a result, such measures do not constitute State aid and do not fall under the scope of these Guidelines. Member States do not face any restrictions under State aid law when setting-up such schemes. The revised CEEAG should take into account these developments and clarify such conditions.

## Aid in the form of reductions in taxes

### Recommendations on a targeted and distinct approach on harmonised and not-harmonised environmental taxes (section 4.7 Aid in the form of reductions in taxes or parafiscal levies, draft CEEAG)

The draft CEEAG (section 4.7 Aid in the form of reductions in taxes or parafiscal levies) excludes the targeted and distinct approach on harmonised and not-harmonised environmental taxes, which is in place under the current EAAG 2014-2020. The Commission proposal would entail that certain category of beneficiaries will not be able to receive state aid related to harmonised environmental taxes - when above the Union minimum tax level set by the relevant applicable Directive - via a simplified approach to assess the necessity and proportionality of the aid. As a consequence, the restrictive criteria to assess the proportionality of aid (paragraphs 269 and 270 of the draft CEEAG) would apply to all beneficiaries and to all type of environmental taxes.

<sup>4</sup> (1) ECJ, C-405/16 P, Judgment of 28 March 2019, ECLI:EU:C:2019:268 - Germany v Commission; see also ECJ, C 556/19, Judgment of 21 October 2020, ECLI:EU:C:2020:844, paras. 25 et seqq. – Eco TLC; GC, T-98/16 and others, Judgment of 19 March 2019, ECLI:EU:T:2019:167, paras. 133 et seqq. – Italy v Commission.



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This proposal is against the principle of fair taxation, as it would pose a disproportionate burden on the European steel industry, would lead to an increased risk of carbon leakage and could undermine the intra EU level-playing field among EIs companies and sectors.

We call on the European Commission to reintroduce the differentiation between harmonised and non-harmonised taxes and the related targeted approach (paragraphs 172-175 EEAG 2014-2020).