COPACEL
Union Française des Industries des Cartons, Papiers et Celluloses

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Public consultation (Ref.: HT.582) on the "draft guidelines on state aids measures in EU ETS post 2021"

COPACEL is the French association representing the pulp (NACE code 17.11) and paper (NACE code 17.12) industry. In the frame of the public consultation, COPACEL makes several comments about on the draft Guidelines on certain State aid measures in the context of the system for greenhouse gas emission allowance trading post 2021.

Directive 2003/87/EC of the European Parliament and of the Council established a system for greenhouse gas emission allowance trading (ETS) within the European Union, in order to promote reductions of greenhouse gas emissions in a cost-effective and efficient manner. In the frame of this Directive, indirect costs can be compensated by Member States in order to address the carbon leakage risk, avoiding the relocation of industrial production outside the Union.

As a matter of fact, greenhouse gas emissions costs passed on electricity prices over the last few years severely impact the competitiveness of the pulp and paper industry, thus increasing the risk of carbon leakage, and leading to an increase of carbon footprint in Europe.

Compensation of indirect cost in the frame of EU- ETS phase IV shall be able to maintain the competitiveness of the European industry by promoting investment dedicated to energy transition and reducing as much as possible distortion of competition between Member states.

COPACEL makes the following comments on the draft guidelines on state aid measures:

- **both pulp (NACE 17.11) and paper (NACE 17.12)** been recognized among the sectors most at risk of carbon leakage have to **remain in the list of sectors eligible for carbon costs compensation** in electricity price;
- the proposed **new boundaries of the regional zones**, compared to the ones identified in the current state aid guideline **shall be questioned. The proxy proposed by the Commission,** "being the weighted average of the CO2 intensity of electricity produced from fossil fuels at national level"**, is very relevant only at regional level. As a consequence, all electricity markets coupled in the Central Western Europe (CWE) region shall share the same emission factor.**
- **The provisions on conditionality are unhelpful and potentially also counter-productive. There will be cases where the investment, even if proportionate, cannot be implemented due to national energy policies or national regulations**.

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1) Eligibility

COPACEL welcomes that both pulp (NACE 17.11) and paper (NACE 17.12) have been recognized among the sectors most at risk of carbon leakage.

Both our sectors are electro-intensive and compete at international level. It is therefore important to safeguard their competitiveness, while we pursue our efforts in both decarbonizing our operations and provide an ever-growing number of products and solutions to decarbonize other segments of the European economy.

Therefore**, both pulp (NACE 17.11) and paper (NACE 17.12) have to remain in the list of sectors to be compensated for carbon costs in electricity.**

2) Proportionality

As a matter of principle, compensation for indirect carbon costs, as well as for direct carbon costs, needs to ensure an effective protection against the risk of carbon leakage.
In this respect, it is still not possible to assess to what extent the draft guidelines would deliver the necessary level of protection. Many values in the formula are still missing: percentage reduction in the 'fall back electricity consumption efficiency benchmark', limit to the amount of indirect carbon costs paid by undertakers in certain sectors, CO_2 emission factors. These values will be crucial to calculate the final amount of aid granted to undertakings.
Among the key values missing, one special mention goes for the revised minimum regional CO_2 emission factors in different geographic areas (Annex III). **As a matter of principle, compensation for carbon costs in electricity prices should reflect the exposure to carbon cost passed into electricity prices. No distinction should be made between costs incurred and opportunity costs.**

In this respect, **we support the Commission decision to keep the definition of 'CO_2 emission factor'** as *"the weighted average of the CO2 intensity of electricity produced from fossil fuels in different geographic areas"*, as it is the case already in the current state aid guidelines valid until 2020.

At the same time, we have **concerns over the proposed new boundaries of the regional zones**, **compared to the ones identified in the current state aid guidelines**. The rationale, as explained in the report produced by the consultant, is that further market integration and market coupling, the price convergence has decreased. And, always according to the consultant, price convergence "*the only factor that reflects whether two neighbouring markets shared similar indirect carbon costs.*"

We disagree with the consultant's conclusions. The first element to be looked at is the correlation in price movements between interconnected markets. The price convergence, as acknowledged also by the consultant, can be the result of several factors. But that doesn't necessarily prove the lack of correlation between two zones in the price formation.

We invite Commission to refer to the Compass Lexecon[1] study, carried out in 2019, which concluded that **despite French very low carbon production mix (less than 0.05 t CO_2/MWh in 2018), the electricity market price in France incorporates a CO_2 component of around 0.76 tCO_2 / MWh almost equal to its neighboring countriesin CWE zone (Germany, Belgium and the Netherlands).**

[1] https://www.fticonsulting.com/fti-intelligence/energy/research/carbon/analysis-co2-power-emission-factor-indirect-compensation-related-eu-ets

The Compass Lexecon study also concluded that the **proxy proposed in the draft (i.e. "the weighted average of the CO_2 intensity of electricity produced from fossil fuels at national level") is very well adapted at regional level but absolutely not relevant at national level**.

The Commission proposal to set a national emission factor instead of a regional factor will lead to widely diverging national emission factors within the CWE area, while the industries located in the region incur the same indirect costs of EU ETS.

COPACEL also noted the new provision that gives the **possibility to Member States to limit the amount of the indirect costs to be paid by undertakers**, should the aid intensity of 75% be inadequate.
This provision mirrors the approach that has already been introduced in the state aid guidelines on energy and environmental protection (EEAG). Moreover, from what stated in the consultant's report, such provision could be beneficial in limiting the indirect costs for our industry.
While we welcome such possibility, we think the provision needs further clarifications, also in view that the two guidelines are different in nature: while the ETS guidelines retroactively compensate for a cost already incurred, the EEAG caps upfront the additional costs.

1. It should be clear that "undertaking" refers to "company" and not to "installations". If otherwise, the provision would raise major market distortions.[2]
2. It should be clarified that the possibility for Member States to cap indirect costs is an additional measure that comes on top of the provision to grant aid intensity of 75%, should the latter not suffice to protect against the risk of carbon leakage. In other words: no installation is compensated less than 75% of CO_2 cost.

3) Conditionality

Our sector is strongly committed to improve energy efficiency and reduce both our direct and indirect emissions. We are already periodically reporting on our investments in promoting energy efficiency and renewable energy sources in our installations.

The partial compensation and high electricity prices, coupled with internal and international market competition, are already sufficient drivers to push companies in implementing energy efficiency measures. Moreover, compensation for carbon costs passed into electricity prices is already partial and set at the level of benchmark setter. Meaning that even the best performer is subject to carbon costs due to partial compensation. The system has therefore already an embedded mechanism requiring undertakers to minimize the impact of carbon costs.

However, **we find the provisions on conditionality (paragraph 54) unhelpful and potentially also counter-productive. There will be cases where the investment, even if proportionate, cannot be implemented due to national energy policies or national regulation**. That could be the case, for instance, if no budget is available, or if market conditions require other strategies to remain competitive. Moreover, forcing investing in incremental efficiency measures could prevent investments in radical transformative measures, leading to stranded assets and/or drying up resources for projects with longer payback times.

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[2] For instance, two installations producing the same product using the same amount of electricity, would receive a different level of compensation just to the different nature of their legal entity. Examples in this direction include cases when GVA is calculated at the installation or at headquarters level, or whether other activities not related to the production process take place at the industrial site (conversion of products, R&D centres…) leading to higher GVA values.