

FORTUM POSITION

COMPETITION CONTRIBUTING TO THE EUROPEAN GREEN DEAL DOCUMENT

20 November 2020

The purpose of this letter is to provide Fortum contribution to the questions submitted by DG Competition in the Competition Contributing to the European Green Deal document aim of which is to gather ideas and proposals from everyone with a stake in this issue, including competition experts, academia, industry, environmental groups and consumer organizations which will help the Commission to update competition legislative.

The document contains a number of questions, grouped into three parts - each covering one of the three competition law instruments: antitrust, State aid control and merger control. Exercising the right to reply either to all or to only certain parts or questions Fortum's reply will focus on elaborating on State aid control issues.

Fortum welcomes the process of the State aid rules review, particularly with respect to environmental protection and energy issues in line with the European Green Deal, what aims to transform the EU into a fair and prosperous society, with a modern, resource-efficient and competitive economy. The goal of which is to make Europe the first climate neutral continent by 2050, where economic growth is decoupled from resource use.

In principle, Fortum shares the presented by the EU Competition Commissioner Margrethe Vestager on the launch of the results of an evaluation of state aid rules view that "there is no need to reinvent the wheel," when it comes to the forthcoming review of the state aid rules but that "in some areas, rules will need to be updated". Thus plans to review six sets of rules matching future of electricity market design with the state aid before the end of 2021: Regional aid Guidelines, IPCEI Communication, RDI Framework, Risk Finance Guidelines, Environmental and Energy Guidelines and relevant provisions of GBER of the relevant state aid guidelines to the end of 2021 are essential in Fortum opinion.

Referring to particular questions submitted in the State aid section:

1. What are the main changes you would like to see in the current State aid rulebook to make sure it fully supports the Green Deal? Where possible, please provide examples where you consider that current State aid rules do not sufficiently support the greening of the economy and/or where current State aid rules enable support that runs counter to environmental objectives.

In general, Fortum believes in open playing field market, nevertheless in Fortum's view state aid should remain necessary for R&D projects, innovations and first-of-kind technologies that are close to commercialisation, including synthetic gases, which will play an important role in replacing fossil gases. However, technology neutrality should be a guiding principle in any State aid rule.

In Fortum view, there is room for clarification of the current State aid guidelines' provisions relating to taxation, especially concerning situations where the same energy product – electricity, heating or cooling – is subject to different tax treatment because of different production technologies and thus provisions of the updated State aid guidelines should be more linked with the forthcoming reviewed

EU Energy Tax Directive addressing the role of taxation in support of energy transition. It is important to ensure that the provisions are clear and aligned in both legislative instruments.

Regarding aid in the form of tax exemptions or tax reductions, the revision of the State aid guidelines should reflect the overall aim to decarbonise all sectors, i.e. going beyond energy production such as heating and cooling, clean gas production etc., and the role of electrification in decarbonisation should be recognised. The electricity tax rate will have an important role in speeding up electrification and thereby in the decarbonisation of societies.

It is also necessary to ensure compatibility between the EU ETS, State aid and taxation. All CO₂ emitting production should be subject to ETS-driven carbon pricing or a (national) CO₂ tax, but not both. This principle should be clarified both in the state aid reviewed legislation and in the Energy Tax Directive. For example, in some countries, district heating production is covered by the EU ETS, but it is also subject to additional national CO₂ taxation, whereas the heating of individual buildings is not always subject to any CO₂ steering – not to ETS or to CO₂ taxation. This effectively distorts competition between different competing heating methods. Such overlapping policy steering on certain production technologies is, in practice, a hidden national subsidy to those production forms that are not subject to overlapping policy steering.

2. If you consider that lower levels of State aid, or fewer State aid measures, should be approved for activities with a negative environmental impact, what are your ideas for how that should be done?

a. For projects that have a negative environmental impact, what ways are there for Member States or the beneficiary to mitigate the negative effects? (For instance: if a broadband/railway investment could impact biodiversity, how could it be ensured that such biodiversity is preserved during the works; or if a hydro power plant would put fish populations at risk, how could fish be protected?)

The EU ETS should be the only instrument to steer fuel switching from fossil fuels to non-fossil, including biomass. State aid may be necessary only for R&D, innovations and first of-kind biomass projects that are close to commercialisation. As a whole, the use of biomass should be assessed from the system efficiency point of view, giving preference to using biomass for high-value bio-based materials and products and using the reject biomass as a transitional energy source for electricity and heat.

Secondly, an example of the heating sector that requires urgent and systemic decarbonisation, which constitutes development opportunities. Currently, only minor parts of the heating and cooling sectors are covered by the ETS (electrical heating and district heating and cooling), while some others remain outside (building-specific H&C solutions). The policy priority should be to include the whole heating sector in the EU ETS scope – this would ensure the most cost efficient transition towards decarbonised solutions. Addressing this requires systemic solutions to enable the transition to energy-efficient low-carbon heating. To support this process, the revised State aid rules should allow investment and operative aid to low-carbon, efficient and scalable heating solutions. Decarbonisation of heating, transport and industries through coupling with the renewable electricity market is expected to play an important role in climate mitigation. In the heating sector, this includes wider and swifter implementation of heat pumps, thermal storages, geothermal sources etc. as part of efficient district heating and cooling in urban areas and individual heating in rural areas. The revised State aid rules should allow effective promoting measures for the efficient individual heating solutions and DHC systems, both in terms of investment and temporary operational aid, or other effective, nationally determined measures, e.g. taxation.

Last but not least, since the approval of the existing State aid guidelines, carbon removal technologies have developed and CCS is no longer the only solution. Both CCU, direct capture of CO₂ from the air (DAC), and material substitutions based on carbon removals are becoming feasible and should be considered in the framework of the guidelines. Sufficiently strong market-based incentives are not yet in place for the development of CCS/CCU, new carbon sinks and material substitutions. In order to achieve the 1.5-degree target, the EU needs to develop a mechanism to reward these, including removal of CO₂ from flue gases or directly from the air. State aid can contribute to fostering the development of these technologies. State aid should be focused on CCS/CCU/DAC technology development and industrial-scale demonstration projects to make CCS/CCU/DAC financially sustainable without State aid in the long run.

All forms of CO₂ transportation should be in the scope of state aid rules. Under the current framework only transportation via pipelines is considered eligible for State aid. Other relevant transportation forms that can be monitored could be considered to be included in the system such as ships, trucks and trains.

3. If you consider that more State aid to support environmental objectives should be allowed, what are your ideas on how that should be done?

a. Should this take the form of allowing more aid (or aid on easier terms) for environmentally beneficial projects than for comparable projects which do not bring the same benefits (“green bonus”)? If so, how should this green bonus be defined?

b. Which criteria should inform the assessment of a green bonus? Could you give concrete examples where, in your view, a green bonus would be justified, compared to examples where it would not be justified? Please provide reasons explaining your choice.

Promotion of the transition to technologies with less negative environmental impact should be based on more efficient and flexible power markets and a strengthened carbon price instead of specific subsidies where relevant. RES technologies, such as wind and solar, have already reached cost-parity in some parts of Europe. Where subsidies are still deemed justified, their design should be as market-based as possible to expose producers to market prices; for example, during hours with negative market prices subsidies should not be paid. They should also be technology neutral and open for cross-border participation. Tenders have proved to be an essential way to bring down the cost of the new technologies. Retroactive changes in subsidies should not take place without compensation. However, in terms of retroactivity, a distinction should be made between direct financial subsidies and indirect subsidies in the form of exemptions from market obligations. It should be possible to abolish the latter kind of exemptions in order to reach a level playing field.

4. How should we define positive environmental benefits?

a. Should it be by reference to the EU taxonomy and, if yes, should it be by reference to all sustainability criteria of the EU taxonomy? Or would any kind of environmental benefit be sufficient?

Yes, there should be by a reference to the EU taxonomy. In Fortum view the taxonomy should provide a harmonised regulatory framework to transparently reflect the volume of taxonomy-aligned activities within a given company. Nevertheless, Fortum underlines the need for more balanced approach focusing on emissions performance containing the spilling over of taxonomy to also other legal documents, seeking taxonomy aligned status for hydro, nuclear and hydrogen and securing role for sustainable natural gas as a transition fuel. Fortum also vows to avoid the creation

of a specific brown taxonomy for 'harmful activities' in the context of the Sustainable Finance renewed action plan.