FEDIL

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FEEDBACK NOTE ABOUT EU ETS STATE AID GUIDELINES PUBLIC CONSULTATION

FEDIL – The Voice of Luxembourg's Industry represents over 600 companies from the industry sector as their major business federation. FEDIL welcomes the possibility to contribute in improving the EU Emissions Trading System's state aid guidelines through public consultation.

The revision of the ETS Directive (2018/410/EU) in preparation of Phase 4 of EU ETS is expected to send an even stronger price signal to incentivise emission reductions. It is expected to further raise the challenge of increased electricity costs arising from EU ETS. These costs, also referred to as indirect carbon costs, will affect both, (1) electricity intensive sectors and (2) sectors that drive their energy transition by electrifying processes that are currently running on fossil fuels. State aid grants that effectively support the efforts of both types of sectors will be crucial to prevent carbon leakage and to promote the energy transition.

The following elements need to be considered during the update of the state aid guidelines:

1 Eligibility

Phase 4 of EU ETS will contribute to further accelerate the decarbonisation of industrial processes in many sectors. It is safe to assume that decarbonisation efforts will also rely on the electrification of processes or on the switch to low-carbon e-fuels. Consequently, the consumption of electricity will increase, and it will do so across a large spectrum of sectors, surpassing the ones identified today as electricity intensive.

The list of eligible sectors must thus allow the possibility to be extended dynamically to new sectors using quantitative thresholds as they run through the process of the energy transition towards a higher electricity intensity. The economic rationale of these sectors will change over time: Companies with a high trade intensity which are currently hardly exposed to indirect ETS costs, will be affected in the future. These company's global competitive position will then deteriorate. Therefore, reviewing the eligibility list regularly will be necessary to include new sectors as they increase their exposure to indirect costs of ETS.

2 Energy Efficiency Efforts as a condition

For companies exposed to indirect costs of EU ETS, continuous energy efficiency optimisation efforts represent a prerequisite to maintain global competitiveness. Indirect cost compensation must be considered a protection to level-off the additional indirect costs by EU ETS certificates included in the power market prices invoiced to final customers. It will by no means prevent companies from continuing to invest in energy efficiency measures. Only once the additional indirect ETS costs are compensated, companies will start competing on equal footing with global competition. Energy efficiency must, therefore, not necessarily be a prerequisite for the eligibility of indirect cost compensation.

3 Level of Compensation

In Phase 4 of EU ETS, rising CO_2 prices will increasingly incentivise the industry to convert CO_2 emitting processes into using electricity. In other words, the energy transition will increase the industry's dependence on affordable electricity in the future. It is thus essential that affordable electricity represents a viable alternative source of energy to support the industry's efforts to substitute CO_2 emitting processes.

An adequate level of compensation, that can be adapted via *the aid intensity*, represents a powerful factor to preserve electricity as that alternative source of energy. This is especially true when considering that it is hard to predict the evolution of the CO_2 price and that electricity will represent an increasing cost factor for the industry.

It is thus important that the aid intensity preserves a level of flexibility, with (1) no predefined upper limit and (2) no regressive factor over time. Both elements would harm the European industry's global competitiveness, hamper the energy transition and prevent the possibility to effectively adapt the level of compensation in case of increasing carbon leakage risks. The factor should rather be kept stable over the period 2021-2030 at a minimum factor equal to today's 75% with the possibility to be increased if necessary.

The level of compensation is also influenced by *the product specific electricity consumption efficiency benchmarks* and *the baseline output*. The calculation methods of these two factors need to be reviewed with the aim to increase their level of accuracy in terms of reflecting business reality.

4 Scope

The electricity expenses of the industry are not directly influenced by the amount of renewable energy it consumes from the energy mix acquired on the market, since the electricity price on the market is indexed to the marginal price. This price is set by the most expensive power generation source according to the merit order. Today this source is often based on fossil fuels, a situation that might not change in the foreseeable future. The scope of the level of support should thus consider all electricity consumed by the eligible installation.

5 EU-intra Level Playing Field

State aid schemes must consider the wide differences between Member States' economic structures and policies and acknowledge that current decarbonisation levels of EU's industry are still widespread. To preserve, however, the integrity of the internal market, which is at the very core of the EU project, differences in the application of state aid schemes across the EU, including different upper limits per Member States, must be worked out to converge towards harmonised state aid rules across the entire EU in the long

term. In the meantime, the differences in current Member State approaches with regards to the EU ETS state aid grants should not be a reason to limit the financial compensation in Phase 4.