

Outcome of the Round Table on Climate change on 27 May 2008

Introduction

The round table gave business, politicians and other stakeholders the possibility to discuss how to exploit the opportunities and minimize the costs of combating climate change and to what extent there is a need for public support. See, in particular, the opening speech from *Neelie Kroes*, Commissioner for Competition.

Below is a more detailed summary of the proceedings of the round table. Please note the views and statements referred to in this summary were made by speakers and participants in the round table. They *do not necessarily reflect the position of the European Commission* on any of the issues concerned. For further details, please consult the presentations from the speakers.

The need to transform society

Many participants underlined that combating climate change requires a complete transformation of society. In this context, business and financial industry see vast opportunities (technological innovation and profitable investments in emission reduction). Markets will provide most of the solutions because they will be profitable. In particular investments in energy efficiency and renewable energy sources can work as a growth engine. Someone's cost is someone else's income – the question is how we end up in the 'income side' of that equation.

One vision was that there will be a third industrial revolution. All great economic revolutions occurred when new energy regimes converged with new communication regimes. The information technology revolution in the 1990's is now converging with a new energy distribution regime and the new revolution will be based on four pillars:

1. a new industrial regime founded on a reconfiguration of the transport, construction, and electricity sectors. By committing itself to use 20% of renewable energy by 2020, the EU is a leader in this industrial revolution;
2. a new way to design buildings, so that they become power plants able to collect renewable energies;
3. new storage technologies using hydrogen which is a storage medium for renewable energies;
4. the development of technologies, similar to the ones that created Internet, to put together all the regions of the world so that they can share the surplus of energy.

The third industrial revolution will create millions of new jobs and pave the way to a new partnership between all the regions in the world.

For more information see, in particular, the presentations made by *Caio Koch-Weser*, Vice Chairman, Deutsche Bank Group, Dr *Žiga Turk*, Development and Minister, Republic of Slovenia and *Jeremy Rifkin*, President, Foundation on Economic Trends.

Seizing the opportunities and minimizing the costs – the right framework

Higher energy efficiency will be crucial. One of the cheapest and fastest ways to reduce emissions is through energy savings in buildings. The payback time for energy saving investments is around two years due to the high oil price. Such investments do not deteriorate the competitiveness and thus do not lead to carbon leakage. Europe can become leaders in energy saving technologies through a big competitive "home" market. Thus, it is essential to have a framework ensuring competition.

It was also discussed to what extent consumers would support market based solutions. Some observed that consumers were increasingly conscious in their choice of products and this would boost the markets for environmentally friendly production and products. Others thought that consumers focus only on price and thus demand would not increase unless Member States use subsidies to ensure competitive prices.

There was agreement that markets only work well if there is an enabling long term framework which requires courage and leadership by politicians and business. A number of suggestions and comments were made in this context:

The following was suggested:

- Preserve the Clean Development Mechanism (CDM) and Joint Implementation (JI) under the Kyoto Protocol and consider to combine the two;
- Focus on key greenhouse gas emitting sectors and develop common methodologies to inter-governmental agreements. Make global agreement to drive all energy intensive users towards low carbon.
- Countries like China and Japan copy to some extent EU regulation (e.g., REACH), thus it is important that EU sets the scene.
- Technology leapfrogging: support establishment of mechanisms to leverage private finance in particular, support R&D and demonstration projects in the field of Carbon Capture & Storage.
- Full auctioning and the inclusion of all sectors under the EU Emission Trading System (EU ETS). Industry must share their environmentally friendly technologies. Intellectual property rights are a key driver of innovation, thus sharing should be based on the purchase of intellectual property rights.
- Maintain a vigorous competition policy to improve the functioning of the market. Ensure fair competition and elimination of market barriers rather than harmonisation. Need active competition and internal market policy in order to tackle non-price barriers to trade. Higher market-based prices and same price for all on carbon are necessary to reduce emissions sufficiently.

- To get the necessary investments in renewable energy the preconditions are investment security, a clear legal and political framework ensuring well functioning markets, national deployment programmes, market access, grid access enforcement and ownership unbundling. Politicians must show courage to put in the place the right legislation even if it jeopardises re-election and progressive companies should speak with one voice
- Furthermore, Member States should learn from experience and resort to the more efficient feed-in tariff instrument rather than the less successful tradable green certificates.
- Work with governments to facilitate international market based mechanisms, apply consistent use of financial/tax incentives adapted to each sector and finance to avoid deforestation.
- Shape the values of consumers. Public authorities should set an example – including reprioritize the EU budget and use of green public procurement.
- Higher compulsory minimum standards for energy efficiency performance and focus on carbon-free buildings.
- Massive communication and training. There is a great awareness about climate change but there is a lack of information on how to reduce emissions. Furthermore, it must be clearly visible, which products are green.
- Common metrics e.g. for carbon accounting standards and systematic, periodical evaluation of progress as well as visible and harmonised benchmarking.
- Create (finance) the necessary infrastructure, e.g. for the distribution of energy from renewable sources.
- It must be obvious that "you need to be green to grow".

For more information see, in particular, the presentations from *Jean-Pascal Tricoire*, CEO, Schneider-Electric and *Lars G. Josefsson*, CEO, Vattenfall.

When is State aid necessary?

Markets will provide many solutions but in some cases State aid is will be appropriate. If the Polluter Pays Principle was fully implemented everywhere there would not be a market failure and thus no need for State aid. The debate showed that there is a need to have an integrated approach to policy development taking into account other policy objectives. The following comments were made:

- It was not always desirable to implement Polluter Pays Principle either for practical, social or competitiveness reasons. These other objectives may prevail.

- State aid should be allowed when it is not too distortive but the Commission should take a tougher line if there are significant distortions, in particular if the obstacle to apply Polluter Pays Principle is political.
- Aid should be allowed to remedy self-imposed distortions caused by e.g. relatively high standards or taxes.
- The new Environmental aid guidelines allow Member State sufficient flexibility to provide State aid. In particular, it was welcomed that it was possible to cover the full difference between production costs and market price related to production of renewable energy as well as all extra costs for aid which is granted on the basis of bidding process.
- The Commission is being vigilant regarding competition but it is only the tip of the iceberg. The energy market itself is not working. Annual subsidies for fossil fuel are in the range of US\$ 100-200 billion. Highly concentrated markets, trust, cartels, grid access manipulation obstruct investments in renewable energy and there are large windfall profits in the energy sector.
- In the future General Block Exemption it should be considered to allow even higher intensities for consultancy services for SMEs and to abandon a request for SMEs to have a certified cost calculation.

For more information see, in particular, presentations from *Andrea Benassi*, Secretary-General, UEAPME, *Graham Branton*, Director State aid, BERR and *Dörthe Fouquet*, European Renewables Energy Federation.

Ensuring success of the reform of EU ETS

Some underlined that EU in the past failed to adopt sufficiently high harmonised energy taxes and a proper functioning EU ETS. Also, it was mentioned that a global agreement is the preferable solution and that no decisions should be taken before it is clear what other global players will do while at the same time it is crucial that the EU shows leadership.

As regards the reform of EU ETS, the following suggestions were made:

- The reform of the EU ETS must not give in to lobbyism, which had neutralised the intended effect of the current ETS. There is support in principle to full auctioning after the third period. The new EU ETS must be based on full auctioning with only one or two exemptions.
- There is a need to recognize the competitive situation of certain sectors and the need to ensure that the interests of SMEs as well as security of supply are taken into account.
- Carbon leakage/competitiveness must be defined and dealt with in a transparent way. The term "carbon leakage" should not be misused to cover situations where displacement of production does not lead to less environmentally friendly production. Some found that the focus should be on loss of competitiveness rather than carbon leakage.

- Substitution away from carbon intensive products is a desirable effect of the ETS. If the carbon price is correct, alternative and less carbon intensive products will be used/developed instead of high carbon intensive products. This would partly lead to a desirable substitution away from the former. Thus exemptions should not be made to keep carbon intensive products in the market.
- We must thoroughly and objectively identify the few sectors that are really exposed to international competition. The assessment must be made independently i.e., not made by industry itself.
- Each business is in a unique competitive position and that must be taken into account. Exposure to international competition should be looked at installation level, not sector level.
- A solid database is required and an analysis of profitability must be made under strict confidentiality in line with the practice in DG Competition.
- Competition policy has an important role to play in the assessment. In highly concentrated markets companies can pass on the costs to consumers – the Commission should protect consumers from being harmed.
- There is no reason to make any exemptions for the production of steel and aluminium. Furthermore, the presence of large price differences within the EU shows that the cement sector is unlikely to be exposed to international competition. Others mentioned that transport of cement would lead to CO₂ emissions and thus this could justify exemptions to avoid transport related emissions.
- Companies will not move out of Europe because of ETS alone but because of a combination of regulatory burden, price of raw materials etc – but EU should not accelerate this process via ETS.
- ETS should be simple, predictable and transparent.
- There must be clear guidance on where the income from the auctioning should be spent e.g. earmarking of revenues to investment in low carbon technologies and carbon capture storage. Even if ETS works well, the carbon price will not trigger the development of Carbon Capture & Storage. Thus public support will be necessary in the development phase.
- In areas where significant R&D efforts are needed or where estimating and monitoring emissions is too difficult and costly, other targeted policy interventions may be more appropriate.
- Need to push for international agreements e.g. in the cement sector as a complementary instrument.

For more information see, in particular presentations from *Rod Christie*, President, Central & Eastern Europe, GE Energy and *Sanjeev Kumar*, WWF European Policy Office.

Concluding remarks

To combat climate change we must change fundamentally. We must make markets work better and put in place regulation, taxes and aid where the market fails. The best starting point are open and functioning markets and thus a vigorous competition policy is essential. A rigid application of Polluter Pays Principle is not feasible, but State aid should only be used as an alternative if it is necessary, proportional and transitional. The necessity and proportionality must be strictly applied and analysed sector by sector. The exemptions should not be so high that prices on carbon do not rise. Public assistance to Carbon Capture & Storage could be inevitable – but it should be support for a real project not for sector agreements.

The debate confirmed the need to an integrated approach in policy development and to take into account that it is a dynamic process depending on what other actors are doing. Furthermore, the debate also showed a need not just to involve business and policy but also consumers.

It is important to constant monitor progress and therefore, in a couple of years it would be a good idea to follow-up on the progress made in this field.