

## COMMISSION DECISION

of 29 April 2011

### **concerning the national allocation plan for the allocation of greenhouse gas emission allowances notified by Estonia in accordance with Directive 2003/87/EC of the European Parliament and of the Council**

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the functioning of the European Union,

Having regard to Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC<sup>1</sup>, and in particular Article 9(3) thereof,

Whereas:

- (1) The national allocation plan of Estonia for the period 2008-2012, developed under Article 9(1) of Directive 2003/87/EC<sup>2</sup> (hereinafter "the Directive"), was notified to the Commission by letter dated 7 July 2006 and registered by the Commission on 12 July 2006. Estonia submitted additional information in order to complete the notified plan by letter dated 7 November 2006, registered on 9 November 2006, in reply to questions from the Commission, and by letter of 6 February 2007, registered on 15 February 2007.
- (2) On 4 May 2007, the Commission adopted the Decision C(2007)1978 final rejecting the national allocation plan. Estonia has then amended its national allocation plan in conformity with Decision C(2007)1978 final. Estonia implemented the amended national allocation plan according to Article 11(2) of the Directive. Pursuant to Regulation 2216/2004/EC<sup>3</sup>, the Estonian national allocation plan table has been entered into the Community independent transaction log (CITL) and the allowances were allocated to individual installations for 2008 and 2009.
- (3) In parallel, Estonia brought an action for annulment against Decision C(2007)1978 (Case T-263/07). On 23 September 2009, the Court of First Instance (First Chamber) rendered a judgment annulling that decision. As a result of the annulment of the

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<sup>1</sup> Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC, OJ L 275, 25.10.2003, p. 32, as amended by Directive 2004/101/EC of the European Parliament and of the Council of 27 October 2004, amending Directive 2003/87/EC establishing a scheme for greenhouse gas emission allowance trading within the Community, in respect of the Kyoto Protocol's project mechanisms, OJ L 338, 13.11.2004, p. 18.

<sup>2</sup> OJ L 275, 25.10.2003, p.32

<sup>3</sup> OJ L 386, 29.12.2004, p.1

Decision C(2007)1978 and in line with the Court of First Instance's judgement, the Commission has reassessed the national allocation plan and rejected it on 11 December 2009.

- (4) By letter dated 8 February 2011, registered on 10 February 2011, Estonia notified to the Commission a revised national allocation plan for the period 2008-2012. Estonia submitted additional information needed for the assessment of the notified plan by letter dated 1 April 2011, registered on 4 April 2011, in reply to questions from the Commission sent by letter dated 18 March 2011.
- (5) The Climate Change Committee<sup>4</sup> considered on 14 April 2011 the national allocation plan and asked the Commission to assess the plan as all previous allocation plans for the second trading period, taking into account verified emissions data and macro-economic developments, in order to ensure equal treatment of all Member States. The Climate Change Committee also asked the Commission to consider in its assessment the importance of preserving the integrity of the internal energy market and avoiding undue distortions of competition. It furthermore underlined the importance of avoiding possible distortions of competition in the power market resulting from allocation of additional allowances to the Estonian power sector to underpin power exports from Estonia to neighbouring Member States.
- (6) The national allocation plan contravenes criteria 1, 2 and 3 of Annex III to the Directive because the total quantity of allowances intended to be allocated is more than would be consistent with assessments of actual and projected progress made pursuant to Decision 280/2004/EC and more than would be consistent with the potential, including the technological potential, of activities covered by the EU Emissions Trading Scheme (hereinafter "EU ETS") to reduce emissions. Criteria 2 and 3 provide for a methodology comparing Estonia's proposed figures to the most representative emissions figures, taking into account economic growth and carbon intensity improvements. Pursuant to criterion 1, the total quantity of allowances to be allocated shall not be more than is likely to be needed for the strict application of the criteria of Annex III.
- (7) With respect to criterion 2, the actual greenhouse gas emissions of the sectors covered by the EU ETS in Estonia are reported as being 13.540891 million tonnes in 2008 and as being 10.322884 million tonnes in 2009. The actual verified greenhouse gas emissions of the sectors covered by the EU ETS in Estonia in 2010 are reported as being 14.421275 million tonnes, compared to a proposed allocation in the EU ETS for that year of 14.845333 million tonnes. This means that based on actual verified emissions Estonia's emissions amount on average for the period 2008-2010 to 12.761683 million tonnes per year. The submitted NAP, however, provides for an average annual allocation for the period 2008 to 2012 of 14.329495 million tonnes. Compared to verified emissions in 2010, this leads on average to an annual allocation of 16.681213 million tonnes for the years 2011 and 2012, corresponding to a total annual increase of the average annual allocation over emissions in 2010 of 2.259938 million tonnes for the years 2011 and 2012. The emission figures for 2008 to 2010 are

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<sup>4</sup> Decision 280/2004/EC of the European Parliament and of the Council of 11 February 2004 concerning a mechanism for monitoring Community greenhouse gas emissions and for implementing the Kyoto Protocol, OJ L 49, 19.02.2004, p. 1, established under Article 9 thereof.

the most reliable and accurate emissions figures for the Commission to compare with Estonia's proposed figures for the assessment under criteria 2 and 3 because they have been reported by individual installations in Estonia falling under the EU ETS and have been independently verified pursuant to Article 15 of the Directive.

- (8) The above mentioned verified emission figures, in particular the fact that for three years of the five-year period covered by the national allocation plan actual verified emissions have by far been lower on average than what is proposed in the national allocation plan, challenges the reliability of the methodology of the national allocation plan and its emission projections for the years 2011 and 2012. These figures rather underpin the results of the Commission's assessment as expressed in Decision C(2007)1978 final of 4 May 2007.
- (9) In reply to questions from the Commission, Estonia put forward that its projections of greenhouse gas emissions in 2010 as submitted by 15 March 2011 were 20.4 million tonnes, with the ETS sectors contributing to 66% of these emissions. The Commission notes that, whereas this is coherent with 2010 verified emission figures, this by itself does not support the overall quantity proposed in the plan. The most exact and thus the most up-to-date information, on which the Commission has to base its assessment at the time of taking a decision on the plan, however, suggests that on average emissions in the period 2008 to 2010 were in fact much lower than the proposed average of 14.329495 million tonnes.
- (10) With respect to criterion 3, the Commission notes that for a national allocation plan to be consistent with the potential, including the technological potential, of activities covered by the scheme to reduce emissions requires assessment of total allocations in accordance, in particular, with projections of economic growth and improvements in carbon intensity<sup>5</sup>. The Commission has assessed the figures at its disposal, including those in the public domain, with a view to comparing these to Estonia's projected emissions.
- (11) The Commission notes that the estimate of future annual emissions in the EU ETS is on average 2.259938 million tonnes higher for the years 2011 and 2012 than the reported verified emissions of Estonia in 2010. The methodology used in the Estonian national allocation plan assumes an increase of electricity exports to neighbouring countries over the second trading period due to the restructuring of the Baltic electricity market. The Commission observes that, without further evidence of Estonian electricity producers indeed facing a higher demand until the end of the trading period, the level of the electricity exports in 2010, 2011 and 2012 is insufficiently substantiated in the national allocation plan. In particular, a different emission coefficient, being CO<sub>2</sub> emissions per GWh electricity produced domestically using shale oil, has been applied in 2009 (1.10 Kton/GWh electricity produced) compared to the period 2010 to 2012 (1.16 Kton CO<sub>2</sub>/GWh). This implies that the need for allowances in the power sector is substantially overestimated, or, at least, without this variation being explained, not sufficiently substantiated.
- (12) Moreover, consideration of recent gross domestic product (hereinafter "GDP") data indicates that in Estonia GDP in 2012 is expected to be approximately 10% higher

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<sup>5</sup> See in particular point 11 of COM(2005) 703 final.

than in 2009, after having dropped by 13,9% in 2009 compared to 2008<sup>6</sup>. The growth in allocation to industrial installations covered by the EU ETS from 2009 to 2012 as proposed in the national allocation plan is, however, significantly higher than these recent GDP growth estimates would suggest. In the absence of more substantive information, this suggests that the need for allowances is also overestimated in the industrial sector.

- (13) The Commission also considers that the methodology used for calculating the proposed size of the new entrants' reserve, leaving aside verified emissions in 2010 for installations covered by the reserve, where relevant, contravenes criteria 1 and 3 of Annex III to the Directive and Article 10 thereof. Moreover, the interplay between the allocation from this reserve to installations of the power sector and the forecast of emissions from the power production provided by Annex III of the national allocation plan is not clear. For example, the plan is silent on whether industrial installations covered by the new entrants' reserve produce electricity, and if so, how this has been taken into account when allocating to electricity producers covered by Annex III to the plan. Due to this lack of clarity, the Commission cannot exclude that emissions are double counted for the purpose of determining the allocation.
- (14) Accordingly, the Commission finds that the Estonian proposed average allocation of 14.329495 million tonnes for each of the years 2008-2012 contravenes criteria 1, 2 and 3 of Annex III to the Directive.
- (15) Furthermore, the national allocation plan contravenes criteria 4 and 5 of Annex III to the Directive. Pursuant to criterion 4 of Annex III of the Directive, the Commission has examined whether the national allocation plan is consistent with other EU legislative and policy instruments. According to the plan, allocations mainly rely on growth projections relating to power exports. It states that the largest factor influencing Estonian emissions and therefore the proposed allocation is the projected increase in electricity exports after the restructuring of the Baltic electricity market. It takes account of increased exports to Latvia and Lithuania following the closure of the Ignalina Nuclear Power Plant, but also of increased electricity exports to Finland due to the delay in the construction of a new Finnish nuclear power plant until 2013. The methodology by which Estonia intends to allocate allowances to the power generating sector is based on the impact of these structural changes, allegedly leading to higher exports. However, on the basis of the information received, the approach chosen may not avoid allocation to the power sector beyond expected needs. The allocation claimed as necessary for electricity production is insufficiently substantiated in the plan. The estimates depend on many subjective assumptions which are difficult to verify in an objective manner, namely without more information on the volumes covered by actual export contracts. It appears to the Commission that the data has not been critically and systematically reviewed in the light of e.g. capacity utilisation and capacity limits, import and export trends and macro-economic developments and policy decisions. Electricity exports in 2011 and 2012 will, in particular, depend on the competitive situation of the Estonian power sector in relation to electricity suppliers

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<sup>6</sup> The GDP growth assumptions are based on the Commission's Economic and Financial Affairs Directorate-General's forecasts of November 2010 published on the website: [http://ec.europa.eu/economy\\_finance/eu/forecasts/2010\\_autumn\\_forecast\\_en.htm](http://ec.europa.eu/economy_finance/eu/forecasts/2010_autumn_forecast_en.htm) and on data of the International Monetary Fund, World Economic Outlook Database, April 2011.

from other countries in the region. It can therefore not be excluded that the proposed allocation impacts on the provisions on third party access of Directive 2003/54/EC of the European Parliament and the Council of 26 June 2003 concerning common rules for the internal market in electricity<sup>7</sup>.

- (16) Pursuant to criterion 5 of Annex III to the Directive, the Commission has examined compliance of the national allocation plan with the provisions of the Treaty, and in particular Articles 107 and 108 thereof. The Commission considers that the allocation of allowances free of charge to certain activities confers a selective economic advantage to undertakings which has the potential to distort competition and affect intra Union trade. The allocation of allowances for free appears to be imputable to the Member State and to entail the use of State resources to the extent that more than 90% of allowances are given for free. In addition, the aspects of imputability and State resources are further strengthened in the second trading period as the participation as of 2008 in international emissions trading and in the other flexible mechanisms of the Kyoto Protocol, the Joint Implementation and the Clean Development Mechanism, enables the Member States to take further discretionary decisions influencing their budgets and the number of EU allowances granted to ETS installations. The Commission therefore at this stage considers that the plan could potentially imply State aid pursuant to Article 107(1) of the Treaty. On the basis of information provided by Estonia, the Commission at this stage cannot consider with certainty that any potential aid granted under the national allocation plan is consistent with and is necessary to achieve the overall environmental objective of the Directive. Non-compliance with criteria 1 and 2 fundamentally jeopardises the overall environmental objective of the emission trading scheme. The Commission considers that in such a case the environmental benefit of any aid included in the allowances may not be sufficient to outweigh the distortion of competition referred to above. The Commission notes, in particular, that with a total quantity of allowances based on projections of the increase in exports in the power sector, and these being insufficiently substantiated, and considering the lack of clarity with regard to new entrants' allocations, the national allocation plan has the potential to distort the competition in the electricity market. The Commission at this stage therefore cannot exclude that any aid involved would be found incompatible with the common market should it be assessed in accordance with Articles 107 and 108 of the Treaty.
- (17) Therefore the Commission concludes that the national allocation plan contravenes criteria 1, 2, 3, 4 and 5 of Annex III to the Directive and must therefore be rejected.
- (18) In order to bring the national allocation plan in conformity with the criteria listed in Annex III to the Directive, Estonia should amend the plan. The Commission should be notified of the amendments made to the plan in accordance with this Decision by Estonia as soon as possible, taking into account the time-scale necessary to carry out the national procedures without undue delay.
- (19) Pursuant to Article 9(3), second sentence, of the Directive, the Member State shall only take a decision under Article 11(2) of the Directive if the new national allocation plan is accepted by the Commission.

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<sup>7</sup> OJ L 176, 15.07.2003, p.37

HAS ADOPTED THIS DECISION:

*Article 1*

The Commission rejects the national allocation plan of Estonia for the first five-year period mentioned in Article 11(2) of the Directive.

*Article 2*

This Decision is addressed to the Republic of Estonia.

Done at Brussels, 29 April 2011

*For the Commission*  
*Connie HEDEGAARD*  
*Member of the Commission*