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COMBINED EVALUATION ROADMAP / INCEPTION IMPACT ASSESSMENT

This combined evaluation roadmap / Inception Impact Assessment aims to inform citizens and stakeholders about the Commission's work in order to allow them to provide feedback on the intended initiative and to participate effectively in future consultation activities. Citizens and stakeholders are, in particular, invited to provide views on the Commission's understanding of the current situation, problem and possible solutions and to make available any relevant information that they may have, including on possible impacts of the different options.

TITLE OF THE INITIATIVE	Revision of the Guidelines on certain State aid measures in the context of the greenhouse gas emission allowance trading system post-2020
LEAD DG – RESPONSIBLE UNIT	DG COMP, Unit B3
LIKELY TYPE OF INITIATIVE	Revision of State aid Guidelines
INDICATIVE PLANNING	Q3 2020

This combined roadmap/Inception Impact Assessment is provided for information purposes only. It does not prejudge the final decision of the Commission on whether this initiative will be pursued or on its final content. All elements of the initiative described by this document, including its timing, are subject to change.

A. Context, evaluation, problem definition and subsidiarity check

Context

The EU Emission Trading System (ETS) is a cornerstone of the EU's policy to combat climate change and its key tool for reducing greenhouse gas emissions cost-effectively. The ETS creates a carbon price signal for businesses to reduce emissions that contribute to climate change. There are two ways this affects companies covered by the ETS. On the one hand, these companies have to buy CO_2 certificates corresponding to their own industrial emissions (so-called direct ETS costs). Companies also pay more for the electricity which they consume (so-called indirect ETS costs). Indirect ETS costs stem from the fact that electricity producers pass the carbon price to consumers via the electricity price.

EU law foresees compensation for both types of costs. Direct ETS costs are compensated via the granting of free allowances directly under the ETS Directive. Indirect ETS costs can be compensated by Member States as long as this is in accordance with the Guidelines on State aid measures in the context of the EU greenhouse gas emission trading system (Guidelines). It is these Guidelines which the Commission is now updating.

The aim of compensation is to avoid that the EU ETS results in CO_2 intensive industries moving outside the EU because of the EU ETS with increased emissions of CO_2 in countries with less ambitious climate policies and thus contribute to an increase of global emissions. This potential phenomenon is referred to as “carbon leakage”.

Member States are free to decide whether to compensate companies for indirect ETS costs and currently 17 out of 28 do not. As a result, different practices across the EU may give rise to competition distortions across economic actors in different Member States. Excessive compensation can also undermine the incentives towards reducing CO_2 emissions as well as result in overcompensation. The Guidelines offer to Member States the possibility to limit these possible effects by specifying for which economic sectors compensation is possible and how much compensation can be given.

The current Guidelines date from 2012 and will expire on 31 December 2020. They therefore have to be revised for the next period starting on 1 January 2021. The legislative framework of the EU ETS has also been recently revised for its next trading period 2021-2030 with the adoption of the new ETS Directive.

The revision of the guidelines needs to take into account the rules of the revised ETS Directive (2018/410/EU) as regards the revised provisions on indirect emissions compensation (Article 10a(6)).

Evaluation

The evaluation will be performed in parallel with the impact assessment and will feed directly into the latter.

The evaluation criteria applied are effectiveness, efficiency, relevance, coherence and EU added value of the Guidelines.

The Commission has already performed a comprehensive evaluation for the revision of the ETS Directive in 2015, which also covered the impact of indirect ETS costs on the carbon leakage risk. That evaluation concluded that there is no evidence that carbon leakage has occurred in the first phases of the application of the ETS but that this result does not necessarily mean that carbon leakage might not happen in the future. As regards the compensation of indirect ETS costs, the evaluation pointed to a lack of evidence about carbon leakage having occurred due to indirect ETS costs. 11 Member States provide for compensation of indirect ETS costs, and 17 Member States do not. The evaluation identified a risk of carbon leakage occurring in the future and considered that compensation for indirect ETS costs is relevant only to the extent that industries are exposed to a significant risk of carbon leakage, and where their competitiveness cannot be protected by free allocation. It also noted that the Guidelines have helped to limit the potential competition distortions.

The present evaluation will build on and update this previous evaluation performed in the context of the revision of the ETS Directive in 2015, by collecting evidence after that date. It will also complement it with an analysis of the application of the Guidelines as regards individual Member States after the entry into force of the Guidelines in 2012. This analysis will focus on the measures which Member States have introduced in application of these Guidelines since 2012 and which the Commission has approved under State aid rules.

Problem the initiative aims to tackle

The main problem which this initiative addresses is the potential risk of carbon leakage due to indirect ETS costs.

The initiative will also aim to strike a balance considering that excessive compensation can be an obstacle for cost-effective decarbonisation of the economy pursued through the 2030 climate and energy framework which set in particular an objective of at least -40% cuts in greenhouse gas emissions by 2030 (below 1990 levels as well as coherence with the transition to a low-carbon economy).

Finally, this initiative will address the risk of competition distortions and how to preserve the integrity of the internal market. Although, the revised ETS Directive considers the implementation of indirect costs compensation measures in accordance with State aid rules, Member States are not obliged to give compensation. This leads to a situation where only some companies in a given eligible sector receive compensation from their national government. The fact that not all Member States implement this compensation may impact the level playing field within a sector.

Basis for EU intervention (legal basis and subsidiarity check)

The proposal falls under the exclusive competence of the Union. In particular, the Commission has exclusive competence to assess compatibility of a State aid measure under Article 107(3)(c) of the TFEU.

B. Objectives and policy options

The revision of the Guidelines will need to balance several objectives: (i) to address the risk of carbon leakage due to indirect ETS costs. This will be done by providing for compensation for the sectors most exposed to this risk of carbon leakage; (ii) to preserve the incentives of the EU ETS for a cost-effective decarbonisation of the economy, in particular by incentivising energy-efficiency measures; and (iii) to minimise competition distortions in the internal market.

Several options could be considered:

In the baseline option the current rules for granting compensation are prolonged. This would mean that compensation would be granted to undertakings in 13 sectors and 7 subsectors, as selected in 2012. Member States would be able to compensate for indirect ETS costs at the current rate. To calculate the amount of indirect ETS costs for each MegaWatt hour (MWh) of electricity consumed, Member States would continue to be grouped together based on whether their electricity market is coupled with that of their neighbours.

1. In term of undertakings/sectors

There are a number of alternative options for deciding which economic sectors should be eligible for compensation. One option would be to align eligibility for compensation of indirect costs with the eligibility for free allowances, which is determined by the so-called Carbon Leakage list established by the European Commission as a delegated act. This would lead to a much longer list of eligible sectors than under the current Guidelines. Alternatively, a more targeted list of eligible sectors specifically for the purposes of the Guidelines could be established. Such a more targeted list would have to be established based on the economic situation of the relevant sectors, for example as regards their exposure to international commercial activity and their exposure to indirect ETS costs.

2. In term of amount of compensation

There are also a number of options as regards the amount of compensation that can be paid. The key question in this respect is what percentage of the indirect ETS costs should be compensated. The possibilities range from partial compensation of indirect costs as it is in the current Guidelines, to lower or higher percentages of cost compensation. It would also be possible to introduce specific rules for sectors that are particularly exposed to a carbon leakage risk. The percentage of indirect cost which is compensated can either remain stable over the entire trading period or could be reduced overtime as was the case in the current Guidelines.

In order to determine how much indirect ETS cost each MWh of electricity consumed in a given Member State contains, it is also necessary to determine the role which carbon based electricity generation plays in this Member State. In an electricity market that is based heavily on renewable energy, electricity consumers will be exposed to lower indirect ETS costs. The current Guidelines have for this purpose established regional CO_2 factors, which reflected the electricity mix in a given region. Regions were defined based on whether market coupling between different national markets was in place. The options in this respect range from a uniform CO_2 factor at EU level, to amended regional CO_2 factors, or to the introduction of specific national CO_2 factors.

The initiative will also examine whether the compensation should be made conditional upon energy efficiency investments, such as the participation in an effective national energy management system. The usefulness of an upper limit on the total compensation which can be granted by a given Member State will also be considered.

The above-mentioned policy options may be combined in packages.

C. Preliminary assessment of expected impacts

Likely economic impacts

The guidelines will have significant economic impacts both for sectors eligible for compensation and for other sectors, which may compete with eligible sectors in certain product markets.

Should the Guidelines be excessively strict as regards which sectors are eligible for compensation or as regards the maximum compensation amounts, this could result in carbon leakage (e.g. via the relocation of economic activity outside the scope of the EU ETS).

Conversely, a very generous compensation system could lead to very significant economic consequences in terms of distortion of competition in the internal market. In any eligible sector, companies that do not receive compensation compete with companies that benefit from it as Member States are not obliged to grant compensation. Companies that produce sustainable alternative products to those which receive compensation would also be disadvantaged. This distortive effect can be reduced by only including sectors which are exposed to an actual carbon leakage risk and by limiting the compensation to the necessary minimum.

Likely social impacts

The Guidelines will have a significant social impact. One of the main objectives of the Guidelines is the avoidance of carbon leakage that would lead to losses of jobs inside the EU.

To avoid the significant social and employment impacts of carbon leakage, it is important to cover sectors genuinely exposed to carbon leakage due to indirect ETS costs and to provide an adequate compensation amount to address the carbon leakage risk while avoiding overcompensation.

Likely environmental impacts

The ETS Guidelines will contribute to reaching EU environmental objectives, in particular fighting climate change. The Guidelines will ensure that compensation of indirect ETS costs remains limited to the minimum necessary to prevent risk of carbon leakage that would undermine the effectiveness of the ETS.

Likely impacts on fundamental rights

The initiative has no impact on fundamental rights.

Likely impacts on simplification and/or administrative burden

The initiative does not create additional burdens in terms of administrative procedures, as the granting of State aid requires a Commission assessment under Article 107 TFEU.

The revision and update of the compatibility criteria in the Guidelines would have a positive impact on the clarity of the State aid requirements for the compatibility of future aid schemes in the next trading period and would make them coherent with the new ETS directive. The revised Guidelines will take into account the impact of the various options on administrative burdens.

D. Evidence base, data collection and better regulation instruments

Impact assessment

An impact assessment is being prepared to support the preparation of this initiative and to inform the Commission's decision.

Evidence base and data collection

This initiative will build upon the information already available and gather new evidence and quantitative data, including through stakeholders consultations, as well as on the Commission's experience with the application of the Guidelines.

Consultation of citizens and stakeholders

The aim of the consultation is to draw upon existing evidence (decisions of the Commission on schemes implemented by Member States to compensate indirect ETS costs, and publicly available literature on the ETS and carbon leakage in particular) to deliver a high quality impact assessment by allowing interested parties to provide their feedback and experiences of (i) implementing the State aid rules related to ETS and (ii) as regards the potential policy options. The consultation will foresee backward looking questions that address existing performance and forward looking questions on the design of the new Guidelines. The main stakeholders identified are the Member States, businesses exposed to a risk of carbon leakage or those which compete with such businesses, and civil society:

- National and regional competent authorities involved in the granting of aid (high interest)
- Businesses and SMEs, in particular industries exposed to ETS indirect emission costs such as the sectors included in the Carbon Leakage List (high interest)
- Trade associations representing businesses (high interest)
- Interest groups who professionally deal with adaptation to climate change, e.g. academia, think tanks, green NGOs (high interest)

The planned consultation activities are:

- Four week consultation to provide feedback on the inception impact assessment
- Public consultation (12 weeks) on the basis of a questionnaire available on the European Commission's public consultation portal: Have your say.
- Targeted consultation (8 weeks) to any interested stakeholder who may be willing to make a claim that a specific sector should be eligible for the compensation or not, on the basis of a sector specific questionnaire. The questionnaire will be available on DG Competition's consultation website: http://ec.europa.eu/competition/consultations/open.html
- Targeted consultation (8 weeks) to national and regional competent authorities involved in the granting of aid, to gather information relating to the implementation of State aid scheme compensating for indirect CO_2 emission costs. The questionnaire will be officially sent to all Member States through the Permanent Representations.
- Possible interviews with stakeholders who replied to the sector specific questionnaire, in case there is need to explain the information and data gathered in the context of that targeted consultation. Based on the replies received during the targeted consultation, the Commission will contact the stakeholders to invite them for an interview.
- Targeted consultation (8 weeks) to any interested stakeholder on the draft revised Guidelines. Stakeholders will be informed of the consultation on DG Competition's consultation website: http://ec.europa.eu/competition/consultations/open.html
- Meeting with the Member States to take place in Autumn 2019, and in particular with national and regional competent authorities involved in the granting of aid, to gather feedback on the draft revised Guidelines. An invitation to the meeting will be officially sent to all Member States through the Permanent Representations.

The questionnaire for the public consultation will be available in English, French and German. Replies can be submitted in any of the 24 official EU languages.

A 10-page synopsis report will be developed bringing together the results of all consultation activities. A summary of the public consultation will also be published.

Will an Implementation plan be established?

An implementation plan is not required. If a Member State plans to adopt a State aid scheme on the basis of the Guidelines it will need to follow the notification procedure that is specific to EU State aid law.