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COMMISSION STAFF WORKING DOCUMENT

Document accompanying the

**Commission Decision determining a list of sectors and subsectors which are deemed to
be exposed to a significant risk of carbon leakage pursuant to Article 10a (13) of
Directive 2003/87/EC**

Executive summary of the impact assessment

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EXECUTIVE SUMMARY

The amended ETS Directive was formally adopted on 23 April 2009. It provides that full auctioning should be the rule from 2013 onwards for the power sector. For other sectors, a transitional system should be put in place for which free allocation in 2013 would be 80 % of a relevant benchmark and to be reduced to 30% in 2020.

To address the risk of carbon leakage, the Directive foresees that sectors exposed to a significant risk of carbon leakage should receive free allowances at 100 % of the benchmark. The list of those sectors should be determined based on specific criteria outlined in the Directive. By the end of 2009 the Commission shall, by Comitology procedure, adopt a Decision determining those sectors. That Decision is the subject of this impact assessment.

It is important to underline that certain important assumptions are already stated in the Directive, and thus not subject to this impact assessment. The main such item is the price of the allowances that will be used when estimating the costs for the affected sectors. Article 10a (14) of the Directive states the assessment should be based on an average carbon price according to the Commission's impact assessment accompanying the package. This price was 30 Euro per ton CO₂, and will thus be used in the all calculations related to this issue.

Another important element to stress is that it is not the intention of this impact assessment to assess how the list of sectors affects Member States' auctioning revenues. The impact on their auctioning revenues will depend on a large number of factors, including the total ETS cap, the number of sectors exposed to carbon leakage, the setting of the benchmarks etc, and is therefore not possible to estimate at this stage.

However, it can already be stated that the distribution of auctioning revenues between Member States will not be affected by the list of carbon leakage, since the distribution is already determined and will be based on historic emissions and redistribution factors outlined in Annex IIa of Directive 2009/29/EC. In any case, as is shown in this impact assessment, the impact of the choices at the Commission's disposal will have very small impact on the number of sectors on the list, and thus on the total auctioning revenues from the ETS.

The Commission Decision, with a list of sectors, is thus an obligation deriving from the Directive. Therefore no diverting policy options could be developed. This impact assessment therefore focuses on the methodological choices the Commission has to make. These choices concern the level of disaggregation of sectors; the cost baseline when estimating the direct costs for sectors due to the implementation the Directive; the use of emission factors for the electricity production; and the selection of sectors for additional qualitative analyses.

For the level of disaggregation the main choice was between NACE 3 level and NACE 4 level. The analysis shows that NACE 4 level is the appropriate one, since it is the most detailed level for which official emissions and trade data is provided. It therefore provides a

more targeted approach than NACE 3. It is also proposed to accept more detailed disaggregation at the level of subsectors when they belong to non-exposed NACE 4 sectors and if their specificities lead to a very different impact on carbon leakage than for the NACE 4 sector they are part of.

A key criterion in the Directive for determining the list of sectors is the costs due to the implementation of the Directive. For this a baseline is needed. Different assumptions are outlined in this analysis, from 100% auctioning as the baseline, to 24% auctioning. The assumption of 75% auctioning is the preferred option as the proportionate impact assessment shows that this option is the most likely to correspond to the actual situation with stringent benchmarks.

The analysis also shows that the use of 100% auctioning instead of 75% auctioning would not lead to any modification of the list of sectors. The assumption of 24% auctioning would have a greater impact but does not take into account that the benchmarks will have an effect of increasing the auctioning level, although this is very likely to happen.

To estimate the impact on electricity prices (so called indirect costs), assumption on the CO₂ intensity of electricity production has to be made. Average CO₂ intensity or marginal CO₂ intensity have been assessed as options. The analysis shows that there is only little difference in the results between the two options, but the use of average values for the emission factors reflects the real emissions linked to the electricity production in the European Union and is therefore the proposed option. The use of marginal CO₂ costs would overestimate the real costs for most industries covered by the ETS.

The Directive requires the use of qualitative assessments to add sectors to the list. The choice has been to analyse sectors close to the quantitative thresholds, and certain subsectors with specific situations. A more comprehensive analysis covering all sectors not qualifying through the quantitative criteria would lead to significant additional administrative costs and time. The proposed option was the only one feasible given the time constraints. Sectors and subsectors can however be added next year, with no loss of free allowances for such sectors. Thus the economic impact of this limited approach is nil.

In summary, the overall economic, social and environmental impacts of the above mentioned methodological choices have been identified as negligible due to the high stability of the list of sectors.

In accordance with the Article 10a (6) of the ETS Directive Member States may also adopt financial measures in favour of sectors or sub-sectors determined to be exposed to a significant risk of carbon leakage due to costs relating to greenhouse gas emissions passed on in electricity prices, in order to compensate for those costs and where this is in accordance with state aid rules applicable and to be adopted in this area. The carbon leakage list covered by this impact assessment only has an impact on the free allocation of allowances for direct emissions. Therefore, defining a list of sectors eligible for compensation payments due to indirect emissions is not subject to the current document or the Commission's decision on carbon leakage.

In this context it can be noted that the calculation of the cost to determine the list of sectors is composed of the sum of direct and indirect costs. However the possible financial compensation (Art. 10a.6) only addresses indirect costs (due to carbon costs of electricity generation). Since free allowances cannot cover more than the full direct costs, and the financial compensation cannot cover more than the full indirect costs, overcompensation is not possible.