EU hands industry €24 billion in pollution windfall

- *European Union policy - meant to cut pollution not pay for it – provides industry with bumper payout*
- *Report undermines 'carbon leakage' claims & adds to momentum for urgent overhaul of crucial policy currently not 'fit for purpose'.*

Brussels, 15 March 2016: New analysis shows how industry across Europe has earned a €24 billion windfall from 2008 to 2014, under the EU Emissions Trading Scheme (EU ETS). This is the main policy used across the EU to "cost-effectively"[i] reduce CO_2 emissions across industry. The findings in a report '*Calculation of additional profits of sectors and firms from the EU ETS*', from independent environmental analysts CE Delft, adds momentum to calls from MEPs and campaigners for an overhaul of the policy ahead of the negotiations to revisit the ETS rules this year at EU level.

The sectors profiting most from pollution payouts have been iron and steel, cement, refineries and petrochemicals. The sum netted by industry over the period is more than 10 times the amount the EU has spent on innovation under the EU ETS[ii]. With highly profitable companies such as ArcelorMittal and Lafarge benefiting from the windfall, the report adds to existing criticism of the scheme.

The report identified three ways industry has secured windfall profits through the scheme:
- Companies were awarded too many free emissions allowances that they could sell for a profit in the market;
- Companies bought cheaper international offsets to comply with their targets, and were able to sell remaining free allowances for a profit on the market.
- Companies made their consumers pay for non-existent carbon costs (by passing through the "costs" of freely obtained emission allowances).

However, given that the analysis – commissioned by Carbon Market Watch – was limited to 19 of the EU's 28 Member States[iii], the actual figure of subsidy awarded is likely to be significantly higher across the region as a whole. The research also underscores the importance of ongoing negotiations to change the current rules, highlighting how outcomes must prevent further exploitation of the EU ETS at the expense of European taxpayers.

Femke de Jong, EU Policy Director at Carbon Market Watch explains: *"Instead of making the polluter pay, energy-intensive companies are allowed to pollute for free under the EU ETS. Even worse, they are able to profit from their pollution to the tune of billions. It's European taxpayers that are picking up this bill as governments forego scarce public money."*

Findings also highlight that 'carbon leakage' claims by polluters, often used as means to justify special treatment for various industrial sectors – and allocation of the free permits – are unsubstantiated. Carbon leakage refers to a hypothetical situation where companies transfer production to countries with weaker climate change policies to lower their production costs. However, the report demonstrates that the EU ETS has been a profit, rather a cost, for industry.

The report moreover shows that most of the industrial sectors pass on at least part of the 'cost' of free allowances in product prices in which case they are at lower to no risk of carbon leakage according to the ETS directive.

"*If costs are passed through, free allocation is not a good instrument to combat eventual carbon leakage*" says **Sander de Bruyn, Senior Economist at CE Delft**.

So far, no evidence has been found for production displacement due to the EU ETS[iv]. Energy intensive companies themselves have also reported to their shareholders that competitiveness risks of the EU ETS are not an issue for them[v].

Femke de Jong, adds: "*Today's findings bust open the industry myth of carbon leakage. There has never been evidence to back-up the relocation threats made by industry. In light of the Paris Agreement that helps to level the playing field to cover over 95% of global emissions, the concept of overgenerous allocation of free pollution permits in the EU ETS can no longer be entertained by decision makers*".

Having given out 11 billion free pollution permits over the 7 years in question, Member States missed out on at least €137 billion in auctioning revenues[vi]. Giving away free emission allowances also reduces the incentive of companies to produce more efficiently or to invest in breakthrough technologies that reduce CO_2.

"*The EU ETS reform must help achieve the decarbonisation objectives of the European economy whilst allowing a "just transition" for all workers without undermining quality of life or generating windfall profit. The EU must adopt a real low-carbon industrial policy and take appropriate measures to ensure the EU ETS effectively contributes to a socially fair transition to a low-carbon economy*" comments **Montserrat Mir, ETUC Confederal Secretary** in charge of climate and energy issues.

In the coming months, European policymakers are revisiting the rules under which industrial sectors are able to receive free pollution permits.

MEP Jytte Guteland, the S&D spokesperson on the EU ETS revision commented: *"Europe can no longer afford the windfall profits that have occurred during the current system. The overall ambition of the ETS must be to gradually move towards ever increasing auctioning, as this is the underpinning logic of the system and a fair solution for market actors."*

MEP Bas Eickhout, the Greens/EFA spokesperson on the EU ETS added: "*Environmental and health related costs induced by industrial activities should not be borne by society, but by the ones that cause them. This is not at all the case under the current EU ETS. On the contrary, companies make huge profits out of the pollution permits which they received for free. There is only one solution: the handing out of free emission allowances has to be phased out rapidly."*

The launch of the report is accompanied by an event RE-PLUMBING THE EU ETS: low-carbon innovation and carbon leakage in a post-Paris world - Tuesday 15th March, 15:00 - 17:00 European Parliament - Room 5G1 (live webstream available here).

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Notes to editor:

- Report, Calculation of additional profits of sectors and firms from the EU ETS - March 2016
- Policy brief, Industry windfall profits from Europe's carbon market - March 2016
- The national myth busters: United Kingdom – France – Germany – Netherlands – Sweden – Luxembourg
- The ArcelorMittal and Lafarge infographics

What is the EU ETS

The EU Emissions Trading System covers the EU's greenhouse gas emissions (GHG) from the industry and power sector which amount to just over 40% of the EU's total GHG emissions. After each year, companies participating in the system must surrender enough allowances to cover all of their emissions.

Carbon Leakage

Carbon leakage refers to a hypothetical situation where companies transfer production to countries with weaker climate change policies to lower their production costs. Under the current EU ETS rules industrial companies deemed at risk of carbon leakage are awarded free pollution permits. Giving free emission allowances to industry reduces the amount of allowances that governments can auction, and reduces the auctioning revenues that could be mobilised by governments. Consequently, free allocation means that less money is available for investments in the low-carbon transition of the European economy.

Windfall profits

The current EU ETS rules hand out free emission allowances to industrial companies deemed at risk of "carbon leakage". The emission allowances that are given away for free represent subsidies, since governments forego income and lose out on revenues from auctioning these pollution permits. Windfall profits occur when industrial companies are over-subsidised for their pollution.

Table 1 shows sectors that have profited most from the EU ETS in the period 2008-2014

Sector	Windfall profits from surplus	Windfall profits from offsets	Windfall profits from min. cost-pass through	Total windfall profits
Iron and steel	€1,044 million	€235 million	€7,995 million	**€8.0 billion**
Cement	€2,649 million	€146 million	€1,915 million	**€4.7 billion**
Refineries	€170 million	€83 million	€4,178 million	**€4.4 billion**
Petrochemicals	€780 million	€41 million	€815 million	**€1.6 billion**

Table 2 shows the total windfall profits for all 19 European countries in CE Delft study

Member State	Windfall profits from surplus	Windfall profits from offsets	Windfall profits from min. cost-pass through	Total windfall profits
Austria	-€226 million	€14 million	€641 million	**€429 million**
Belgium	€698 million	€23 million	€711 million	**€1,432 million**
Czech Republic	€194 million	€15 million	€463 million	**€673 million**
Denmark	€110 million	€3 million	€124 million	**€237 million**
Finland	€114 million	€7 million	€360 million	**€481 million**
France	€818 million	€112 million	€1,780 million	**€2,710 million**
Germany	€1,121 million	€187 million	€3,191 million	**€4,500 million**
Greece	€359 million	€20 million	€300 million	**€679 million**
Hungary	€54 million	€4 million	€151 million	**€210 million**
Ireland	€163 million	€1 million	€48 million	**€212 million**
Italy	€519 million	€53 million	€1,743 million	**€2,315 million**
Netherlands	€236 million	€27 million	€819 million	**€1,082 million**
Poland	€266 million	€20 million	€738 million	**€1,025 million**
Portugal	€227 million	€7 million	€211 million	**€446 million**
Slovakia	€341 million	€13 million	€468 million	**€823 million**
Slovenia	€15 million	€1 million	€22 million	**€38 million**
Spain	€1,672 million	€49 million	€1,167 million	**€2,888 million**
Sweden	€388 million	€15 million	€326 million	**€729 million**
United Kingdom	€1,010 million	€58 million	€2,035 million	**€3,104 million**

<u>Unsubstantiated industry claims on carbon leakage</u>

In the past years, industry lobbyists have made several unsubstantiated claims about the impact of the EU ETS on their competitiveness. Certain corporations have made profits worth hundreds of millions of euros from the EU's climate policies, while still claiming that the EU ETS is impacting their competitiveness.

Claim by ArcelorMittal: "*EU energy and climate policy is punishing the steel sector and other energy-intensive industries, which is having a profound impact on our competitiveness*" (2014)[vii].

Fact: The steel company has made **more than €400 million** from the EU ETS in the last 5 years according to its own annual reports.

Claim by Lafarge: "*Unequal carbon pricing place[s] the EU manufacturing sector in general – and the cement sector in particular – at risk of carbon leakage*" (2013)[viii].

Fact: The cement company has made **€485 million** from the EU ETS in the years 2010 to 2014 according to its own annual reports.

<u>Carbon Market Watch policy recommendations for the EU ETS revision:</u>

- Phase out the free allocation of pollution permits by gradually increasing the share of allowances to be auctioned from the current 57% to 100% in the future.
- Introduce a tiered "carbon leakage" approach and target free allowances only to those that really need it. The left-over free allowances should be cancelled or auctioned for innovation support.
- Annually reduce the amount of free allowances that an installation receives (the *benchmark*) in line with the overall decarbonisation pathway of the EU ETS.
- Invest more auctioning revenues in climate friendly innovation and support the frontrunners that want to invest in breakthrough technologies.

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[i] http://ec.europa.eu/clima/policies/ets/index_en.htm
[ii] SWD (2015) 135, p. 123 http://ec.europa.eu/clima/policies/ets/revision/docs/impact_assessment_en.pdf
[iii] Austria, Belgium, Czech Republic, Germany, Denmark, Spain, Finland, France, United Kingdom, Greece, Hungary, Ireland, Italy, Netherlands, Poland, Portugal, Sweden, Slovenia and Slovakia.
[iv] Ecorys (2013), Carbon leakage evidence project, see here
[v] See letter to Barroso here, 2014
[vi] Based on information provided by CE Delft (2016), using average annual carbon prices.
[vii] FT (20 Jan 2014), "Rewrite energy policy and re-industrialise Europe"
[viii] Lafarge answer to the public consultation on the 2030 climate and energy framework (2013), see here