The EU Emissions Trading System

"Carbon leakage" and industry ambition in a post-Paris world

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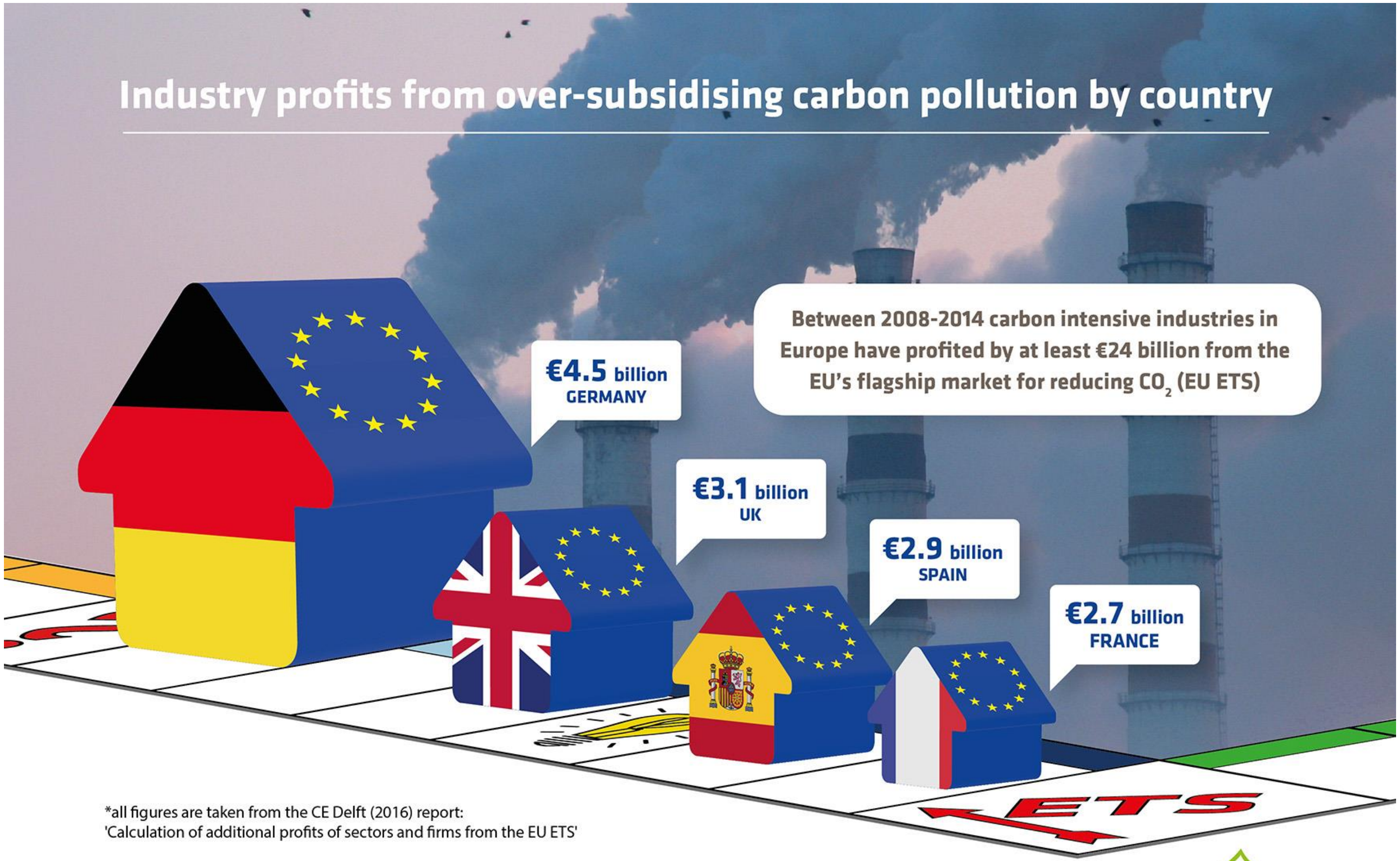
Launch of new CE Delft report: industry earned a €24 billion pollution windfall under the EU ETS



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Five problems related to the current system of free allocation of pollution permits

1. **No evidence for "carbon leakage"** or production displacement due to the EU ETS.
2. **Current EU ETS rules over-subsidise industry pollution**. Free allocation has resulted in significant profits for corporations.
3. **European taxpayers are picking up the bill** as governments forego scarce public money.
4. Without an urgent change of the rules, **emission reductions of industry will stall over the next 15 years**.
5. **The Paris agreement will help level the playing field** across the global economy as it covers over 95% of global emissions.

1. No evidence for production displacement due to the EU ETS

Carbon leakage = the hypothetical situation where companies transfer production to countries with weaker climate policies to lower their production costs.

- **The new CE Delft study demonstrates that the EU ETS has been a profit, rather than a cost, for industry**.
- **Ecorys study for the Commission (2013) found no carbon leakage evidence**:

"We found no evidence for any carbon leakage – according to the ETS Directive, defined as production relocation due to the ETS - in the past two ETS periods"

- **Industry confirms lack of "carbon leakage" risks:**

Energy intensive companies have reported to their shareowners that the competitiveness risks of the EU ETS are not an issue for them (see letter to Barroso here, 2014).

- **OECD rejects carbon leakage arguments:**

"There may be reasons for being concerned about competitiveness in Europe, but environmental stringency isn't one of them" (chief economist Catherine Mann, see here)

2. Current ETS rules over-subsidise industry pollution

Current "*carbon leakage*" rules do not only allow EU industries to pollute for free, it has even enabled them to profit from their pollution, in three ways*:

1. Companies were awarded too many free emission allowances that they could sell for a profit in the market: **€8 billion profits**.
2. Companies bought cheaper international offsets to comply with their targets, and were able to sell remaining free allowances for a profit in the market: **€0.6 billion profits**.
3. Companies made their consumers pay for non-existent carbon costs (by passing through the "costs" of freely obtained emission allowances): **€15.3 billion profits**.

In total, **energy-intensive companies** in 19 EU countries **profited over €24 billion from pollution payouts under the EU ETS.**

The sum netted by industry over the 2008-2014 period is more than 10 times the amount the EU has spent on innovation under the EU ETS.

*CE Delft (2016), *Calculation of additional profits of sectors and firms from the EU ETS*

Industries have made profits from the EU ETS, while claiming otherwise

Claim by ArcelorMittal:
"EU energy and climate policy is punishing the steel sector.."

Fact:
ArcelorMittal has made over **€400 million** from the EU ETS over the last 5 years [according to its own annual reports]

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3. European taxpayers are picking up the bill

- Free allocation means that **governments forego scarce public funds** as it reduces the auctioning revenues that could be mobilized.
- Between 2008-2014, **EU governments lost out on at least €137 billion in auctioning revenues** by given free allowances to industry + power sectors.

Figure 1 Value of free allowances vs auctioning revenues (2008-2014)

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4. Current “carbon leakage” rules stall emission reductions over the next 15 years

- Giving away free allowances **reduces the incentive** of companies to produce more efficiently or to invest in breakthrough technologies that reduce CO_2.

- Consequently, without an urgent change of the rules, the European Environment Agency (EEA, 2015) projects that **industry’s emission reductions will stall over the next 15 years**.

- This is not in line with the EU’s decarbonisation objective to 95% emission reductions by 2050 in order to keep climate change well below 2°C.

5. The Paris agreement helps to level the global playing field

- The Paris agreement helps to level the global playing field as it covers over 95% of global emissions. There are no carbon leakage risks when other countries take comparable climate measures.

- The efforts by other countries also need to be recognized in the EU ETS carbon leakage rules to avoid unjust pollution subsidies.

- The Paris Agreement should hence result in less pollution permits given for free after 2020.

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Despite these problems, the EU ETS revision hands out free allowances to all industrial sectors

- The EU ETS revision proposes to continue with many of the existing “carbon leakage” rules, including the hand-out of **6.3 billion** **free emission allowances** in the post-2020 period.

- This represents a pollution subsidy of **€160 billion** to heavy emitters, at the expense of taxpayers.

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The EU ETS revision will result in windfall profits for heavy industry

The Commission's impact assessment shows that the steel, cement, refineries and chemicals sectors are able to pass through all their compliance costs to their customers and make **€19 billion from the EU ETS** in the 2021-2030 period.

Table 24 Overview table on estimated compliance cost per sector, taking into account cost pass-through rates

		With lowest cost pass through rates	
		compliance cost (million €)	% of turnover
Steel	Baseline B	-1.300	-0,8%
	Simple	-1.400	-0,9%
	Limited changes	-1.990	-1,2%
	Targeted	-1.930	-1,2%
Cement	Baseline B	-310	-1,9%
	Simple	-240	-1,4%
	Limited changes	270	1,6%
	Targeted	-230	-1,4%
Refineries	Baseline B	-190	0,0%
	Simple	-320	-0,1%
	Limited changes	-140	0,0%
	Targeted	-110	0,0%
Chemicals	Baseline B	-100	-0,1%
	Simple	-190	-0,1%
	Limited changes	-70	0,0%
	Targeted	-50	0,0%

€13 billion profits in 2021-2030 period

€3.1 billion profits in 2021-2030 period

€1.9 billion profits in 2021-2030 period

€1 billion profits in 2021-2030 period

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Key question in the EU ETS revision: subsidising pollution vs. supporting low-carbon solutions

"Governments should stop working on the assumption that tighter regulations will hurt their export share and focus on the edge they can get from innovation."***

Supporting industry innovation:
450 million allowances,
± €11 billion

Subsidising industry pollution:
6.3 billion allowances,
± €160 billion

*OECD Chief Economist Catherine Mann, see [here]

Key recommendations

Transform EU's main climate instrument from subsidizing industry's pollution to supporting the solutions that help decarbonize Europe's industrial sectors:

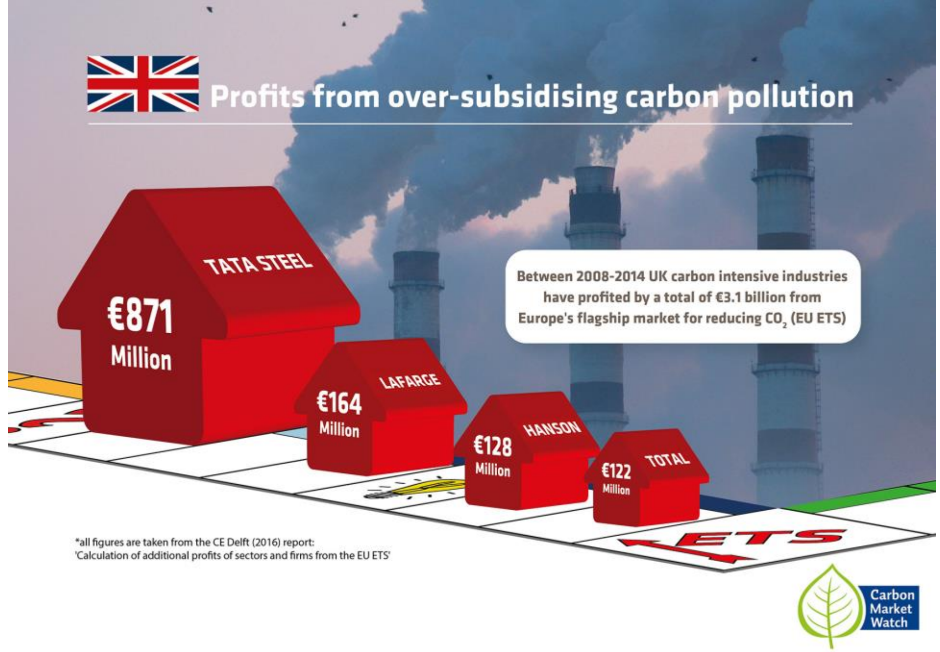
- **Phase out the free allocation of pollution permits** by gradually increasing the share of allowances to be auctioned from the current 57% to 100% in the future.
- **Do not give free allowances to those that do not need it** by introducing a targeted, tiered "carbon leakage" approach. The left-over allowances should be cancelled.
- **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 low-carbon innovation** and support the frontrunners that want to invest in breakthrough technologies.

Read more:

Carbon leakage factsheets:

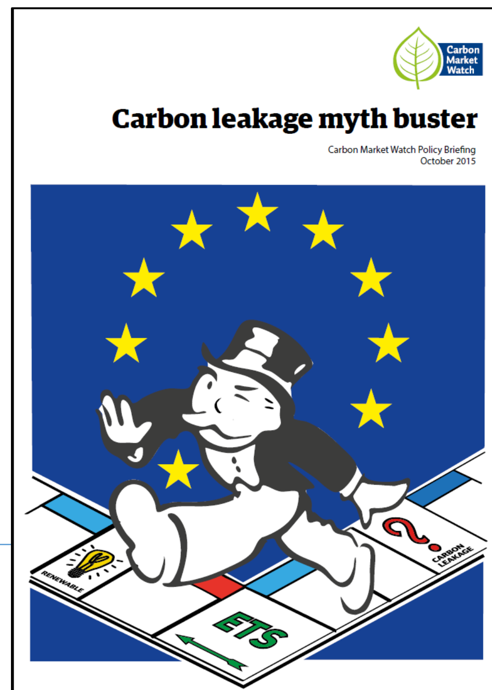
- Germany
- France
- The UK
- The Netherlands
- Sweden

www.carbonmarketwatch.org



On industry windfall profits here

On our carbon leakage recommendations here



On increasing the environmental integrity of the EU ETS here