

06.11.15**Decision**
of the Bundesrat

Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments**COM(2015) 337 final**

In its 938th session on 6th November 2015 the Bundesrat adopted the following Opinion pursuant to §§ 3 and 5, Act on Cooperation between the Federation and the Federal States in European Union Affairs (EUZBLG):

1. The Bundesrat welcomes the fact that the Commission has tabled a proposal on amending directive 2003/87/EC long before the beginning of the fourth trading period for the European emissions trading system (2021 to 2030 period). This makes it possible to establish clarity at an early stage about the general framework provisions for installations included within the European emissions trading system.

Furthermore, the Bundesrat also welcomes the draft proposal; it sets the course in a number of important respects for further reform of the EU emissions trading system for the fourth trading period from 2021. This should create the vital preconditions to ensure that the EU's 2030 climate and energy objectives can be attained.

The Bundesrat also welcomes the fact that this draft proposal foresees implementation at an early stage of the EU's objectives of reducing greenhouse gas emissions by 2030.

In addition, the Bundesrat also welcomes in principle the objective set by the Commission's proposal of introducing amendments to Directive 2003/87/EU to

ensure that in the forthcoming trading period the EU emissions trading system once again becomes an effective instrument for mitigating climate change.

2. The Bundesrat also welcomes the ambitious goals for reductions in greenhouse gas emissions by 2030.

In this context the European emissions trading system (ETS) constitutes the central component of European Union climate change policy. The Bundesrat supports the ETS as a market-based system that aims to create long-term incentives for cost-efficient reductions in emissions.

3. Reliable framework conditions for the ETS are crucial to the functioning of this system. The Bundesrat therefore requests the Federal Government during the further course of negotiations to advocate inter alia that transparent and readily comprehensible provisions and clear price signals for cost-efficient climate change mitigation be adopted at an early stage in order to create fair framework conditions and long-term planning security for investments in climate-conscious forms of energy and low-carbon technologies.
4. The Bundesrat notes that the European emissions trading system is the most effective instrument to reduce greenhouse gas emissions in Europe. The Commission's measures to reinforce the allocation effect of the European emissions trading system therefore deserve general support.
5. The Bundesrat considers that there is a risk that in the absence of an international agreement on climate change mitigation European companies bear a unilateral burden that impairs their international competitiveness. The Bundesrat has already repeatedly drawn attention to the need to avoid relocation of production to non-EU countries with less ambitious climate change mitigation goals – most recently in its Opinion of 8th May 2015 (BR-Official Document 72/15 (Decision), Point 6). Relocation of energy-intensive industries leads to job losses in the EU but does not make any contribution to climate change mitigation. For that reason the results of the Climate Change Conference in Paris (COP 21) must be taken into account in further deliberations on the draft proposal.

6. In drafting the recast of the ETS, attention must be paid to international competitiveness and the considerable associated risk of carbon leakage from the most energy-intensive industries and from industries highly dependent on foreign trade. Only by taking this into account will it be possible to ensure that the industrial value-added chains that characterise Germany, and on which millions of jobs depend, can be secured on a sustainable and enduring basis.

The Bundesrat welcomes the continuation of credits for companies at risk of carbon leakage that compete in the international arena with companies which are not required to comply with comparable climate change mitigation requirements.

Relocations of investments or an exodus of companies to non-EU states would also be damaging to the economy and to consumers in Germany and across the EU.

7. The Bundesrat welcomes the instruments of "backloading" and "MSR", but draws attention to the need to avoid short-term interventions in the ETS to ensure that this recast of the provisions creates a long-term robust system from the fourth trading period on.
8. Alongside planning security, the global climate change mitigation perspective is of vital importance. The goal of reducing the concentration of greenhouse gases in the atmosphere to 450ppm in order to attain the 2-degrees goal can only be achieved through a coordinated, legally binding, global approach. In this respect the World Climate Change Conference in Paris at the end of 2015 plays a decisive role. The Bundesrat welcomes the active and responsible role assumed by the Federal Government and the EU in this context. The results of this conference should be incorporated into the European legislative process.
9. The Bundesrat therefore welcomes activities undertaken in the run-up to the Climate Change Conference in Paris to convince as many states as possible to adopt legally binding reduction commitments.
10. The overall objective should be to encourage emissions reductions outside the EU too, thus simultaneously creating global markets for low-carbon technologies.

11. The Bundesrat supports the conclusions of the European Council of 24th October 2014 (EUCO 169/14) and calls on the Federal Government to advocate in negotiations that the principles agreed at that meeting are also reflected in the legislative act. This applies above all to the following points:

- Steps must be taken to prevent the risk of carbon leakage as a result of climate change mitigation policy until such a time as other leading economies undertake comparable efforts;
- Adequate support must be provided to sectors that are at risk of erosion of their international competitiveness;
- The benchmarks must be in keeping with technical progress;
- To preserve international competitiveness, inappropriate CO₂-related costs should not arise for the most efficient installations in these sectors.

12. As mentioned in the EUCO 169/14 conclusions, the benchmarks for allocation of free certificates should be in line with technological progress. The Bundesrat welcomes this approach. Taking technological progress into account also implies taking the limits of technological possibilities into account. The Bundesrat therefore advocates taking technical, thermodynamic and physical maximum thresholds into account and incorporating these into the legislation. The BREF documents (Best Available Techniques Reference Document) could serve as a point of reference. Benchmarks that are impossible to comply with in technical terms should certainly be excluded. In this context, it is important to stipulate overall thresholds for benchmarks for all the requisite technical processes and sub-installations within a process.

The system of deploying attainable benchmarks for allocation of free certificates runs counter to the idea of making the 1 per cent per annum benchmark more stringent across the board. Instead the proposed "reality check" should be used to set a realistic benchmark.

The Bundesrat requests the Federal Government to take steps to ensure that the wording in Article 1, Sub-section 5, Letter b is adapted to stipulate that there shall be no further flat-rate reduction of free allocation installations which are remain among the top ten per cent of best-performing installations in Europe in the fourth trading period too, on the basis of the benchmark figures calculated.

A flat-rate reduction would not take sufficient account of the limits of technical feasibility and would disadvantage highly efficient installations. This applies in particular for process-related emissions that cannot be reduced due to the stoichiometry underlying the process in question.

13. The Bundesrat does however see an urgent need to act concerning the establishment of sector-specific ex-ante benchmarks for free allocation of emissions certificates within the context of the European emissions trading system, in order to ensure that important processes and technologies with specific unique features are no longer disadvantaged and to ensure that the undertakings in question can be treated appropriately. On the basis of the currently valid provisions in Article 10a, Directive 2003/87/EC, it is only possible to establish an ex-ante benchmark if sufficient data is available to determine the top ten percent of the most efficient installations in a sector or sub-sector. This provision does not allow for appropriate treatment of undertakings that only have a single installation in Europe or a very limited number of installations in the relevant sector. This also holds true for undertakings that work with production processes in which solid, liquid or gaseous waste and/or residual materials are produced as an intrinsic part of the process, and must be fed back into the process as a combustible to comply statutory obligations. In this respect the undertakings in question have to date not been treated appropriately.

14. The Bundesrat therefore requests the Federal Government to advocate at the European level that a corresponding amendment of Article 10a of Directive 2003/87/EC be introduced. In particular the Bundesrat requests the Federal Government to take steps to ensure that
 - in cases in which there are fewer than ten installations in a sector or sub-sector within the scope of Directive 2003/87/EC, the average performance of these installations, adjusted by an efficiency factor if necessary, should be taken as the point of departure in establishing the basis for the ex-ante benchmarks;
 - in establishing the EU-wide ex-ante benchmarks, it is vital to take account of existing obligations under legislation on waste relating to solid, liquid or gaseous waste and/or residual materials produced as an intrinsic part of a process and used for energy recovery.

15. As certificate prices rise, attenuation of and compensation for electricity price effects will become considerably more important in order to ensure that electricity-intensive production processes remain internationally competitive. The Commission's guidelines on state aid already significantly limit the level of compensation that may be paid at present. Further reduction would mean that compensation, which would be only partial, would have no impact at all in terms of carbon leakage protection. The Bundesrat therefore considers that it is important to ensure that the provisions on electricity price compensation are not made less advantageous than in the trading periods to date. It must be possible to provide compensation for all indirect costs. Sub-sub-section 1 of Article 10a Sub-section 6 of the directive should therefore be amended accordingly.

16. The Bundesrat supports the approach of cost-efficient reduction of greenhouse gas emissions. This should be based on the various CO₂-avoidance costs in the various sectors.

In this context the avoidance costs in particular of process-determined emissions that do not stem from a combustion step should be taken into account. These emissions arise from the material use of an energy source. Specific provisions should be introduced for these emissions. In this context the Bundesrat advocates a consistent European policy and correspondingly also alignment with the Energy Efficiency Directive (Directive 2012/27/EU). In that legislation non-energy-related forms of utilisation are not added to the figures for the target parameter of primary energy consumption.

17. In order to secure the international competitiveness of energy-intensive industries and to take the considerable risk of carbon leakage into account, realistic and attainable benchmarks on the basis of the top ten per cent of the most efficient installations is urgently needed. The benchmarks must also fully reflect emissions due to electricity generation from residue gases too – as is already envisaged in the Emissions Trading System Directive, but not put into practice by the Commission.

18. With a view to ensuring timely and reliable planning, the Bundesrat calls on the Federal Government to advocate vis-à-vis the Commission that the revised carbon leakage list should already be tabled in 2017.

It is vital in the new methodology for drawing up the carbon leakage list to ensure that all sectors and sub-sectors with a risk of carbon leakage are covered by the provisions. The Federal Government should ensure that this is done by reviewing and correspondingly taking into account exceptions for heterogeneous activity categories and inputs, as well as by setting the level of the threshold value at 0.18 for the qualitative assessment.

19. The Bundesrat furthermore also calls on the Federal Government to ensure that production of inputs for energy-intensive industries that form an integral component of the value-added chain of an activity at risk of carbon leakage are incorporated into the provisions on avoidance of direct and indirect carbon leakage.
20. Parallel to carbon leakage, there is also the risk of investment leakage. Physical relocation of production installations (carbon leakage) is often the final step; however a shortfall in investments is a clear sign that developments are moving in this direction. There is currently a clear lack of investment in the EU. This point should therefore play a greater role in considerations and in the legislation. To that end there is a need to devise specific criteria to encompass these economic effects. The Federal Government should call on the Commission to develop criteria along these lines and to broaden the thrust of the directive accordingly.
21. The Bundesrat takes note of the maintenance of the mechanisms for solidarity and growth in Member States with below-average gross domestic product and the introduction of the new Modernisation Fund. In this context the Bundesrat takes a critical stance in respect of further extending the option free allocation to also include the power generation sector in certain Member States. This option must not lead to a competitive advantage in intra-EU competition for emission-intensive power installations in the Member States that enjoy such preferential treatment. This does not reflect the spirit of an integrated Single Market for energy and does not serve the interests of climate change mitigation. A review clause for Article 10c should therefore be added. In addition, the impact should be monitored and in particular the consequences for cross-border electricity trade should be analysed.

22. Furthermore, a clear and legally binding commitment to long-term reduction and to phasing out of these exceptional provisions is needed. In added, there is need to develop a cross-trading-periods approach that does not envisage a further extension of free allocation for the energy industry in individual Member States as for the transition from the third to fourth trading period on the basis of the proposal submitted by the Commission.

23. The Bundesrat supports extension of the Innovation Fund NER 300, which will become NER 450. In this context the Bundesrat welcomes both the increased provision of funding as well as the extension of the scope of application to industrial process innovations. In designing this scheme, it is important to ensure that all Member States have access to the Innovation Fund on an equal footing, thus making a clear distinction between this fund and the Innovation and Modernisation Fund. Technological innovations are the only way to attain the goal of competitive low-carbon production in the medium term.

The Bundesrat considers that the Innovation Fund to be introduced is in principle a viable instrument. The Bundesrat advocates stipulating that the funding made available may only be used for projects that reflect the EU's long-term goals for climate change mitigation and environmental protection.

24. The Bundesrat is in favour of the Commission's proposal of greater flexibility to take growth of existing installations into account and for new installations. The ETS must not serve as a brake on innovation and growth. This greater flexibility should also apply to lower-level growth of industrial output in growth phases. The Bundesrat therefore welcomes the reinforcement of the NER and its linkage to the MSR.

The Bundesrat also welcomes the stated intention to make allocation of certificates more dynamic. The principle of "Dynamic Allocation" should however be used more clearly.

25. The Bundesrat recognises the Commission's efforts in its proposal to find a way to enable adjustment of allocation quantities to changing levels of production. The division into two allocation phases constitutes an important initial step in this direction. In the Bundesrat's view the allocation should however be based

on current production levels. This enables industrial growth and avoids discussions on adjustments in the case of unforeseen developments. In addition, a system of this kind would be better suited to extending the emissions trading system to the international context.

26. The Bundesrat points out that one cause for the current surplus of certificates, which has led to de facto failure of the market, is the large quantity of so-called CDM certificates that are on offer.
27. The Bundesrat advocates an integrated European Energy and Climate Change Mitigation concept. Developments on energy markets should also be taken into account in this context. The Bundesrat emphasises the need for additional flexibility options in the European electricity market. In this context load management also plays an important role. The Bundesrat points out that operating at partial-load efficiency generally reduces efficiency rates and hence leads to increases of specific emissions.
28. In the interest of planning and investment security, the Bundesrat furthermore advocates that all the central provisions should be stipulated at an early stage directly in the directive. Central elements, such as for example adjustments of benchmarks, should not be regulated or adjusted subsequently through delegated acts. If any other approach were adopted, the Bundesrat considers that this would entail a risk of a shift in the allocation of competences, and insufficient democratic control.