POSITION PAPER

27 February 2014

BUSINESSEUROPE reaction to the EU climate and energy package

KEY MESSAGES

1 The package includes some openings to ensure that competitiveness, security of supply and climate objectives are better balanced than in the past. However, it still lacks concrete actions to tackle the challenge of excessively high energy prices and safeguard the international competitiveness of European businesses.

2 The proposal to focus on a single greenhouse gas (GHG) reduction target post-2020 is positive and needs to be confirmed by the Spring European Council. It will incentivise renewable sources and energy efficiency in a more cost-effective way. The proposed set of competitiveness- and security-related indicators is a step in the right direction.

3 Europe must set a 2030 GHG reduction target in line with the actions of other developed and emerging countries. Therefore, it must establish a clear conditionality between the 40% GHG domestic reduction target and the completion of an international climate agreement in 2015 in Paris involving all major economies in a comparable way.

4 A genuine reform of the EU ETS with an improved carbon leakage support must take place post-2020, not the proposed piecemeal approach. The Market Stability Reserve proposal should be discussed, in conjunction with compensation measures for direct and indirect costs, in light of the outcome of the 2015 Climate Conference in Paris. The current carbon leakage list must remain unchanged.

5 The Commission rightly pushes for the completion of the internal energy market, effective competition between suppliers and the further deployment of cross-border infrastructures. Information exchange on major national energy decisions with possible impact on other Member States must be strengthened.

6 The non-prohibitive approach on shale gas is positive. It illustrates Europe’s determination to explore and exploit, in a sustainable manner, potentially highly advantageous unconventional energy resources.

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BUSINESSEUROPE REACTION TO THE EU CLIMATE AND ENERGY PACKAGE

In June 2013, BUSINESSEUROPE published its vision on how to transform the EU's energy and climate policies into true industrial growth drivers. Looking at the experience gained from the current framework, we outlined four main challenges that need to be addressed: high energy prices, the lack of coherence in climate policies; the fragmentation of the EU internal energy market and the lack of progress on a global climate agreement. This analysis led to the definition of seven concrete policy recommendations with the ultimate aim of reaching a true integration of EU's industrial, energy and climate objectives.

The European Council adopted important orientations on energy policy in May 2013, in particular on the completion of the internal energy market and the importance of stronger coordination of national energy policies, diversification of Europe's energy supply and the need to address the impact of high energy prices. The 2014 Spring European Council is an important *rendez-vous* for further decisions, including on the post-2020 energy and climate policy.

On 22 January 2014, the European Commission published an initiative for an industrial renaissance, together with an energy prices and costs analysis, a proposal for a 2030 framework for climate and energy, a legislative initiative on the EU ETS and recommendations on the production of unconventional energy resources. It is also currently consulting on the state aid guidelines for energy and environment.

The energy and climate package provides a number of positive messages on the cost-effectiveness of meeting the growth and competitiveness objectives. The package notably demonstrates openness to ensuring that competitiveness, security of supply and climate objectives are better balanced than in the past. However, it still lacks the right level of ambition and concrete actions to address the challenge of high energy prices.

Prices have risen to unprecedented levels in Europe at a time when our main competitor, the United States, is benefitting from increasingly lower energy prices. These price variations are affecting industrial competitiveness and leading to "investment leakage" with new investments in manufacturing sectors progressively moving outside Europe. International developments should also be better reflected. No doubt that climate policy will remain a driver of EU's energy strategy with the development of renewable energy sources and energy efficiency. However it is questionable whether Europe can continue at the same pace without undermining its competitiveness.

The following sections outline BUSINESSEUROPE's reactions to some of the main proposals and the conditions that we believe are important to strengthen competitiveness and to enable the re-industrialisation of Europe.

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1. A single GHG target must be complemented with an architecture to improve competitiveness

The proposal to focus on a single greenhouse gas (GHG) emissions reduction target post-2020 is positive and needs to be confirmed by the Spring European Council. The single GHG target will provide a long-term perspective to business and investors and increase the predictability and consistency of the regulatory framework. EU targets for energy efficiency and renewable energy sources should not be continued after 2020 as they are not economically efficient. However, should an EU level renewable target be agreed, it must not be translated into a binding burden sharing at national level.

Renewable energy sources should continue to be encouraged in a smarter, less distortive and cost-effective way and support schemes must be gradually integrated into regular markets in order to ensure a cost-effective energy transition. R&D policies and funding should support the least mature technologies.

The public consultation on a 2030 energy efficiency policy framework recently launched by the European Commission will provide the platform for reviewing implementation of the energy efficiency directive and for designing the right post-2020 policy framework for further improving energy efficiency across the EU's economy. A single 2030 GHG target and EU ETS will allow Member States to adopt differentiated measures driven by the market. This will unlock the energy efficient potential of diverse sectors in a cost effective way, such as the promotion of energy efficiency in high potential areas such as buildings and cities, which should be prioritised.

Europe needs more ambition for competitiveness and security of supply objectives. Europe will only be successful in designing a post-2020 energy and climate policy if it sets a framework in which cost-competitiveness, security of supply and climate objectives are placed on equal footing.

The European Commission proposal to establish and to monitor a set of competitiveness- and security-related indicators (e.g. energy price differentials between the EU and major trading partners, deployment of smart grids and interconnections, etc.) is a step in the right direction, but much more ambition is needed. It should be clearly linked to early political commitment and actions to improve Europe's competitiveness.

The methodology and data collection for the indicators will have to be organised in close cooperation with stakeholders, particularly impacted industries.

2. Set EU's 2030 GHG reduction target in line with the actions of other developed and emerging countries

Europe must establish a clear conditionality between the 40% GHG domestic emission reduction and the completion of an international climate agreement in 2015 in Paris. BUSINESSEUROPE strongly supports global efforts to reduce emissions and urges all parties to pledge commitments in the first quarter of 2015 as decided at the UNFCCC COP-19/CMP-9 in Warsaw. Whatever the outcome on the international negotiations in 2015, the EU should set a binding 2030 GHG emissions reduction target.

At a time when the EU's share of global emissions is decreasing and countries like Japan, Australia and Canada have significantly scaled back their national climate actions, the Commission is proposing to further raise the EU's level of ambition with a 40% domestic target. We must be careful in preventing the EU from being once again a lone frontrunner without followers. Therefore BUSINESSEUROPE thinks that the proposed level of ambition (40%) can only be seen as realistic if a binding international climate agreement with comparable and measureable contributions by our main global competitors can be concluded in 2015.

3. Consolidate the future of the EU ETS and international competitiveness

A genuine reform of the EU ETS with an improved carbon leakage support must take place post-2020, not the proposed piecemeal approach. The package reflects on the importance of the EU ETS post-2020, which should be the main instrument to reduce emissions for industry and other covered sectors and to promote investments in low carbon technologies.

The proposed Market Stability Reserve (MSR) under the EU ETS opens the debate on possible measures to tackle the volatility of EU emission Allowances prices post-2020. However, this proposal is an initiative which exclusively aims at tackling this particular challenge. To make the EU ETS 'fit-for-purpose' from 2020, more fundamental structural reforms are required.

In particular, as long as no global level playing field is achieved, stronger measures will have to be taken at EU level to safeguard industrial competitiveness and avoid investment leakage:

- For sectors at risk of carbon leakage, full compensation through free allocation based on benchmarks must allow the most efficient companies to be globally competitive without being penalised by direct carbon costs. Real/recent production levels – combined with realistic benchmarks – should be considered as an option for the allocation of free allowances in order to avoid problems deriving from over or under allocation.

- In addition, energy intensive sectors at risk of carbon leakage should be compensated for carbon cost impacts on electricity prices. A stronger convergence of compensation levels for indirect carbon costs across Member States is needed. Rules should be developed at EU level through common sectoral approaches (e.g. use of auctioning revenues, additional free allocation, etc.) rather than through state aid rules.

Therefore, in order to take decisions in the right order, BUSINESSEUROPE believes the MSR proposal should be discussed, in conjunction with new compensation measures for direct and indirect costs, in light of the outcome of the 2015 Climate

Conference in Paris. At this point, Europe will be able to make the final decision on the level of ambition for the 2030 GHG emissions reduction target and consequently for the ETS and particularly non-ETS sectors where further improvements will need to be achieved

The Spring European Council must approve and reaffirm the Commission proposal to keep the current carbon leakage list unchanged. For legal certainty purposes, the current criteria and existing assumptions for the carbon leakage list must be preserved. The carbon leakage list links, directly and legally, the EU GHG reduction target with critical measures that are designed to protect the competitiveness of EU industry, such as compensation for indirect costs or state aid guidelines.

Europe needs an overarching strategy to safeguard the international competitiveness of businesses. The cost impact of EU's climate policies goes beyond the CO_2 price. Taxes and shortcomings in the EU and national energy polices have contributed to a 21% increase of energy bills for industrial consumers in four years. In a more than ever competitive world, the high cost of non-mature renewable energy technologies cannot be borne by European business exposed to international competition. Europe needs a coherent strategy to safeguard the international competitiveness of businesses facing higher energy costs than their competitors elsewhere. As a first step, this has to be properly reflected in the EU energy and environmental aid guidelines, which must allow for protection of energy-intensive industries. Without such a strategy, Europe will not reach its target for an increased industrial activity.

4. Completion of the internal energy market and coordination of national energy policies

The European Commission rightly pushes for the completion of the internal energy market, effective competition between suppliers and the further deployment of cross-border infrastructures. The completion of the internal energy market, the implementation of the third energy package and the development of needed infrastructures to achieve effective markets integration should be an absolute priority. Existing power capacities and demand side management should be used to contribute to the security of supply. When a capacity mechanism is put in place it should be non-discriminatory, technology-neutral and be available both to new and existing capacities.

The proposed new governance for the 2030 framework would establish an iterative process of consultation by Member States with neighbouring countries in the preparation of national energy and climate plans. It mirrors work by the European Council to strengthen information exchange on major national energy decisions with possible impact on other Member States and the Union as a whole. These are important initiatives which should be further strengthened to avoid the fragmentation of the EU internal energy market.

5. Working towards a diversification of EU's energy supplies

BUSINESSEUROPE believes the Commission non-prohibitive approach on shale gas goes in the right direction. It illustrates Europe's determination to explore and exploit, in a sustainable manner, potentially highly advantageous unconventional energy resources such as shale gas. However clarifications are needed on how the Commission intends to proceed with Best Available Techniques and it is questionable whether the proposed 18 month period for reviewing the implementation of recommendations will be sufficient to make an informed assessment.

BUSINESSEUROPE looks forward to working constructively with the European institutions to build on these comments to improve the EU energy and climate framework towards 2030 and to establish the right conditions for supporting investments in Europe and to ensure that industrial competitiveness and growth become a policy imperative for the incoming EU political cycle.

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