



EUROPEAN CARBON AND GRAPHITE ASSOCIATION

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Emission trading scheme for NO_x and SO₂

European industry is committed to an overall continuous improvement of its environmental performance. The undersigned sectors support the existing Directive concerning Integrated Pollution Prevention and Control (IPPC) (Directive 96/61/EC) as the better tool to regulate industrial emissions. In particular, the integrated approach of dealing with different environmental emissions is beneficial to the overall environmental performance of industrial installations. The targeting of individual emissions with commercial incentives as drivers risks jeopardising the holistic approach and might yield higher emissions in other areas without a real need or justification by shifting the attention of concerned industries to those specific emissions. The usefulness of BREF notes therefore becomes very questionable. In addition, the IPPC Directive takes into account environmental objectives, local conditions and economic aspects in an integrated manner and drives continuous environmental improvement through the regularly updated BREF notes.

Executive Summary

The undersigned sectors oppose an emission trading scheme (ETS) for NO_x and SO₂ and would like to highlight that:

- **An ETS is a tool to further regulate already highly regulated sources:**
 - NO_x and SO₂ emissions are already regulated by several Directives, national taxes, fees and international agreements
 - It is likely that monitoring and administration costs, both for participating companies and national administrations will increase
 - Any future market-based instrument is unlikely to involve sectors other than industry
 - The legal stability might be lost and the complexity will be increased when industry is being regulated by two(or more) legal instruments
 - An ETS for NO_x and SO₂ will not lead to technological change
- **Environmental and health impacts need to be addressed:**
 - NO_x and SO₂ are local and regional pollutants
 - The integrated approach of IPPC will be compromised
- **Sectoral impact assessments are needed:**
 - The important and likely effect of an ETS for NO_x and SO₂ on power prices, impacting all parts of society and, in particular, the competitiveness of the undersigned sectors
 - The lack of room for trading in the undersigned sectors
 - The likely distortion of competition – within countries/sectors, and outside the European Union (EU)
 - The unlikely possibility to account and reward industry for early actions

For these reasons, the undersigned sectors prefer the certainty and the balance of the existing system under the IPPC Directive. In this existing system, costs can be measured and planned, a quality essential in industries that require high capital investments, a long-term view and certainty, which is the case in the undersigned industries.

Detailed outline of concerns regarding emission trading NO_x and SO₂

An ETS for NO_x and SO₂ is currently being discussed and investigated in several contexts, for example in the revisions of the IPPC Directive and the National Emission Ceilings (NEC) Directive (Directive 2001/81/EC). So far, no detailed proposal has been presented. The undersigned sectors nevertheless like to express their concern about the possible consequences of an ETS for NO_x and SO₂.

ETS is a tool to further regulate already highly regulated sources

The promotion of market-based instruments should only be considered if it can be clearly demonstrated that these alternative instruments can deliver the required environmental objective at less cost and without damage to the competitiveness of European industry (the Lisbon agenda). The recent experience that can be drawn from the ETS for CO₂ is not encouraging. No cost-benefit analysis has shown that market-based instruments such as an ETS would deliver positive results.

In general, an ETS for NO_x and SO₂ does not make sense if existing regulatory limits or taxes imposed on these pollutants are maintained. Such a scheme would only make sense if it were to provide an alternative to meeting the environmental objectives in respect of those pollutants at a lower cost. The undersigned sectors reject the idea of an ETS for NO_x and SO₂ due to the following:

1. NO_x and SO₂ emissions are already regulated by several Directives, national taxes, fees and international agreements

NO_x and SO₂ emissions are already regulated by several Directives, such as the IPPC, NEC and Large Combustion Plants (LCP) (Directive 2001/81/EC). In addition to EU environmental legislation, industry has to comply with national environmental measures such as taxes and fees, and often takes part in voluntary agreements. Industry thereby contributes significantly to the reduction of these pollutants. If this fact is not sufficiently recognised, as was the case in the development of the ETS for CO₂, industry faces double regulation and has to bear twice the burden on its cost base, namely the cost of existing local instruments (such as taxation of energy products or fulfilment of voluntary agreements) and the cost of purchasing allowances.

2. It is likely that monitoring and administration costs, both for participating companies and national administrations will increase

The experiences in the USA¹ with ETS for SO₂ and in the EU with the ETS for CO₂ show that both systems are characterised by high administrative burdens and costs. Monitoring, verification, reporting, controls, developing and maintaining registries, accounting treatment of allowances, and trading itself generate burdens, costs and also a lot of uncertainty (see for example the accounting treatment of CO₂ allowances in the current ETS for CO₂), as some of these are difficult to identify and assess at the outset.

This is particularly the case for Small and Medium Enterprises (SMEs) that face specific problems with an ETS - for example the lack of resources to follow up the market price.

3. Any future market-based instrument is unlikely to involve sectors other than industry

Any future additional market-based instrument at national or at EU level will most likely only include industrial sectors (as for CO₂) to the detriment of those sectors that cannot directly pass on the additional costs to their customers (global EU players will be less competitive), such as the undersigned sectors. Measures should be fair, proportionate and cost-effective. Thus, the regulation of industry's NO_x and SO₂ emissions, which have already been significantly reduced in the past, should be accompanied by appropriate measures to tackle emissions from other sources. Significant other sources of NO_x and SO₂ emissions - for example, emissions from transports and households - should also carry their share and contribute to the reduction of NO_x and SO₂ emissions.

4. The legal stability might be lost and the complexity will be increased when industry is being regulated by two(or more) legal instruments

¹ <http://www.epa.gov/airmarkets/arp/index.html>

The full implementation and application of the IPPC Directive is an ongoing process that will deliver its complete achievements in the coming years (compliance by 30th October 2007). Rather than the development of market-based instruments, the dynamic and harmonised application of the IPPC Directive is clearly the best tool to ensure the continuous improvement of environmental performance and create the conditions of a level playing field between European installations at the same time as providing medium and long-term certainty in terms of predictability of the legal framework and of costs, as well as in terms of time for investments.

5. An ETS for NO_x and SO₂ will not lead to technological change

One of the main problems associated with trading schemes linked to operating permits is their lack of long-term certainty. This is particularly serious for manufacturing industries that require heavy capital investment, and which therefore need long-term certainty and predictability. The long-term price of tradable emissions allowances is too uncertain to be a driver of systematic technological change in industries whose capacity investments must be planned over 30-year periods.

In permit schemes, because the supply of permits is stable, small changes in demand can lead to large changes in price. In a NO_x trading scheme in Los Angeles, prices rose from 13 cents to \$37 within 2 years. In an SO₂ trading scheme, prices had a monthly volatility of 10%.² The same phenomenon is also to be found in the ETS for CO₂ in the EU.

Economists³ conclude that this lack of a long-term framework for innovation and investment is the biggest failing of emission trading schemes. A stable regulatory framework with “command & control” rules, however tough, is often preferable for industry.

Environmental and health impacts need to be addressed

The only experience we have at European level with an ETS is with the one for CO₂. The nature of the impacts of NO_x and SO₂ emissions on the environment and on the human health is fundamentally different from that of CO₂ emissions. Therefore, we need to tackle their abatement and the prevention of harmful effects, while keeping the following in mind:

1. NO_x and SO₂ emissions are local and regional pollutants

Due to the local and regional environmental and health effects of NO_x and SO₂ emissions, there is a need to ensure a minimum level of protection. This means that local air quality limit values have to be respected, and that trading would come on top of this. It needs to be recognised that the need to respect local air quality limit values significantly reduces the room for trading.

2. The integrated approach of IPPC will be compromised

Applying an ETS to only some of the pollutants covered by the IPPC Directive would disrupt the integrated approach, as it would disregard cross-media effects and effects on other pollutants. For example, a certain technique to reduce NO_x may NOT be considered as a Best Available Technique (BAT) due to unacceptable cross-media effects. Under an ETS, however, such effects will not be duly taken into account, and installing the technique may even result in a financial benefit!

Sectoral impact assessments are needed

The impact assessments that have been carried out so far are insufficient. In particular, the study “*Assessment of options to streamline legislation on industrial emissions and analysis of the interaction between the IPPC Directive and possible emissions trading schemes for NO_x and SO₂*”⁴ carried out in the framework of the IPPC revision focused only on the power sector and based the assessment on assumptions that are not valid for the industry as a whole. Before any scheme is set up, there is a

² “A rough guide to carbon trading” (http://www.prospect-magazine.co.uk/article_details.php?id=8220)>

³ E.g. Mr. Dieter Helm of Oxford University

⁴ ENTEC, Contract 070402/2005/420336/MAR/C4: Assessment of options to streamline legislation on industrial emissions and analysis of the interaction between the IPPC Directive and possible emissions trading schemes for NO_x and SO₂, (draft final report December 2006)

need to carry out sectoral impact assessments taking into account the specificities of each sector and for the undersigned sectors in particular, the following:

1. The important and likely effect of an ETS for NO_x and SO₂ on power prices, impacting all parts of society and, in particular, the competitiveness of the undersigned sectors

As power prices are set on the basis of marginal costs, which are normally determined by production using fossil fuels (with considerable emissions of both NO_x and SO₂), the market price will include the cost of allowances. As power prices will be the same for all means of generation (including for those with no emissions of NO_x and SO₂), windfall profits will be generated. The opportunity cost calculation implies that the price of allowances (including those that are received for free) will be added to the marginal cost. This situation is even more worrying as identified by the Energy inquiry of DG Competition⁵: the electricity markets are distorted and dominated by large incumbents, which can impose prices on consumers. Market-based instruments do not work, and should not be applied, when the markets are not functioning. If this happens, the undersigned sectors (characterised by being energy-intensive) – whether or not covered by the ETS – will see their competitiveness seriously impaired.

Furthermore, emissions from the power industry largely depend on the fuel used, which can be switched to a less polluting source in a way that is not possible for the raw materials in the undersigned sectors.

2. The lack of room for trading in the undersigned sectors

The undersigned sectors are already operating today under conditions based on BAT. It is therefore difficult to understand how a trading system would work: who would sell and, more relevantly, who would buy, unless the idea would be to trade beyond BAT, an unacceptable proposition.

3. The likely distortion of competition – within countries/sectors, and outside the European Union (EU)

The undersigned sectors are operating and marketing their products on the worldwide market. Prices are set by worldwide competition, and there is therefore no possibility for the undersigned sectors to pass on costs of allowances to the customers.

A scheme operating within an individual sector would also be problematic. As some industries (for example the ceramics, lime, dolomite, magnesite and cement sectors) have no option in the choice of their raw material and its chemical composition. Therefore, emissions of certain pollutants for example SO₂ can vary widely between different regions, even in the same Member State. This is duly recognised in the ceramics BREF⁶ with different BAT-AELs for different raw materials. A trading system would be environmentally unsound as it would financially stimulate the transport of raw materials.

4. The unlikely possibility to take into account and reward industry for early actions

The undersigned sectors do not believe that it would be possible to reward front runners through an ETS, as the recent ETS for CO₂ shows. As each incumbent to the scheme cannot be granted an allocation greater than what is strictly needed, it is virtually impossible to be rewarded for early action.

In the case of an ETS for NO_x and SO₂ that would operate under a Cap and Trade system, it might even unnecessarily hamper efficient installations from expanding in cases where operators actually could be in a position to win new market shares!

Conclusion

The undersigned sectors are opposed to any emission trading scheme for SO₂ and NO_x because we do not believe it will provide the best possible environmental protection, given that the BAT concept is being undermined, the impacts are not sufficiently assessed, and because it will further jeopardise the competitiveness of the European industry, in particular of SMEs across the EU.

⁵ http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/energy/

⁶ <http://eippcb.jrc.es/pages/FActivities.htm>

**CEFIC – European Chemical Industry Council**

Since 1972, Cefic is the voice of the European chemical industry in the European Union and in the world. Cefic represents 27.000 large, medium and small chemical companies in Europe producing 30 % of the world chemicals and employing 1.3 million employees.

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**CEPI aisbl - The Confederation of European Paper Industries**

The European paper industry is one of the most competitive and sustainable in Europe producing 100 Mtonnes of paper and board and 40 Mtonnes of pulp annually. It provides directly 230,000 jobs and has a turnover of 74 billion €. Along the forest and paper chain there are 2,950,000 jobs.

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**Cérame-Unie – Liaison Office of the European Ceramic Industry**

Cérame-Unie represents more than 2000 companies across Europe. The turnover is estimated at 27 billion € and the industry employs 230.000 people.

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**CPV - The European Glass Federation**

CPV represents more than 1.000 companies and ca. 196.000 workers. The size of the glass companies range from small furnaces (SMEs) to big multinationals present in several countries. In 2005, the total EU 25 glass production reached a volume of 37 Mtonnes. The production value amounted to some 37 billion €.

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**EUROFER – European Confederation of Iron and Steel Industries**

The European Steel Industry (EU-25) has a total annual production of a little more than 190 Mtonnes, and has a turnover of just under 100 billion €. The industry provides direct employment for 380,000 EU citizens; over 22 million people are employed in the steel processing, using and recycling industries.

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**EUROMETAUX - European Association of Non-Ferrous Metals Industries**

The European Non-Ferrous Metals industry, represents several thousand companies of all sizes, is present in every Member State, employs over one million people and adds 50 billion € of value by transforming simple ores and minerals into high value added metals and semi-fabricated products.

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**Euromines - The European Association of Mining Industries,**

Metal Ores & Industrial Minerals, it covers 42 different metals and minerals and represents a variety of mineral processing facilities that would be concerned by this proposal. Euromines represents more than 350,000 jobs in Europe.

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