

REVISING THE ENVIRONMENTAL AND ENERGY STATE AID GUIDE- LINES TO REDUCE THE FINAN- CIAL BURDEN ON PRIVATE CON- SUMERS

Position of the Federation of German Consumer Organisations on the revision of the Environmental and Energy State Aid Guidelines 2014-2020 of the European Commission

11. Januar 2021

Impressum

Verbraucherzentrale

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INHALT

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ABOUT THE FEDERATION OF GERMAN CONSUMER ORGANISATIONS

The Federation of German Consumer Organisations (Verbraucherzentrale Bundesverband e.V. – vzbv; www.vzbv.de) is the umbrella organisation for more than 40 consumer organisations throughout Germany and represents the interests of German consumers vis-à-vis policymakers, the private sector and in public.

SUMMARY

The European Commission is reviewing its “Environmental and Energy State Aid Guidelines (EEAG)”¹. These guidelines have an impact on environmental and energy policies of the Member States and on the fair distribution of costs for these policies. Thereby they also impact on consumer welfare and energy costs of households. Today, consumers often bear the costs of energy and environmental policies, while the industrial sector receives state aid to maintain competitiveness and prevent carbon leakage. Households incur further costs due to exemptions of industrial stakeholders from contributing to the financing of public goods, such as a healthy climate.

In this position paper, vzbv argues that the European Commission should focus on a fairer distribution of costs when it revises the EEAG. The European Commission should ensure that all stakeholder groups (industry, companies and private consumers) contribute to safeguarding and financing public goods. When revising the EEAG, the European Commission has a chance to promote public acceptance of energy and environmental policies by reducing exemptions for industrial stakeholders and phasing out direct and indirect fossil fuel subsidies. The new EEAG should entail stronger conditionality for state aid to industrial beneficiaries with regard to their decarbonisation efforts. The criteria for state aid should be strengthened to reduce the number of beneficiaries to those really in need of public funds. The European Commission should pay special attention to emerging technological trends such as a hydrogen economy and heed the lessons learned from traditional networked industries such as gas and electricity where unbundling and the “user pays”-principle are firmly established. With regard to special purpose financing models, such as a “cost-averaging system” to promote renewables or combined heat and power installations, the European Commission should develop new tools to ensure that such financing systems are appropriately controlled by the public.

I. INTRODUCTION

vzbv is convinced that the energy transition could be a driver to increase consumer welfare if it is implemented in a socially just and fair way and if it distributes the costs among all stakeholders. However, the current implementation of the European energy transition raises concerns as the financing of the transition has become more and more problematic from a consumer perspective. On the one hand, safeguarding public goods such as a clean environment and a healthy climate has increasingly become a task for which households shoulder most of the financial burden. On the other hand, public policy measures that support industrial stakeholders have neither created the necessary

¹ [https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0628\(01\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0628(01)&from=EN)

incentives to decarbonise production, nor have they proven adequate to ensure a fair distribution of energy costs between households and industry.

The Environmental and Energy State Aid Guidelines (EEAG)² of the European Commission are due to be revised by the end of 2021. Due to their impact on energy prices and the financing of energy and environmental policies, the revision is essential for consumers.

vzbv believes that the current EEAG harm consumer welfare by placing the costs for the energy transition disproportionately on the shoulders of consumers. While it remains necessary to apply the polluter-pays principle and thus give greenhouse gases emissions and environmental degradation an appropriate price, consumer acceptance fades if the costs are not distributed transparently and fairly among all market participants. In addition, consumers are largely dependent on choices offered by the market and cannot change the way manufacturers produce with their purchasing decision alone.

The EEAG revision should put private consumers' interests centre stage. A stronger focus on private consumers is a prerequisite to address issues of social justice and public acceptance when it comes to a fair distribution of costs for the energy transition.

II. EEAG AS A DRIVER FOR A FAIRER DISTRIBUTION OF COSTS

1. PHASE-OUT OF FOSSIL FUEL SUBSIDIES AND EXEMPTIONS FOR INDUSTRY

State aid needs to be an enabler of the energy transition. The revised EEAG should more strongly support the political targets for climate and energy sustainability enshrined in the "European Green Deal". According to the Social Sustainability Barometer for the German Energiewende³, consumers consistently support⁴ the transition towards a renewable-based energy supply in which coal and nuclear power plants are phased-out⁵.

However, the current EEAG are focused too much on the notion of "preserving industrial competitiveness", while neglecting the fair distribution of costs associated with the energy transition. An example of an unfair distribution of costs is the deployment of renewable energy sources (RES) in Germany for which households and small enterprises pay disproportionally more than energy intensive users (EUI). The EEAG include state aid in the form of reductions or exemptions from environmental taxes, but also provide for reductions in electricity surcharges to EIUs. In addition to exemptions, parts of the industrial and transport sectors in Germany benefit from both direct and indirect fossil fuel subsidies⁶. According to a study by the Overseas Development Institute, Germany

² [https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0628\(01\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0628(01)&from=EN)

³ IASS – Sustainability Barometer for the German Energiewende, 2017: <https://www.iass-potsdam.de/en/news/social-sustainability-barometer-energiewende-shows-broad-support-along-doubts-about>

⁴ 88 percent of the population across all education, income and age groups – and in both rural and urban areas

⁵ 63 percent of the population support a coal phaseout. 68 percent support a nuclear phaseout

⁶ Example: state aid for capacity mechanisms, which include coal-fired power plants, is allowed until 2025. Cf. OECD, 2019, p.3: <https://www.oecd.org/fossil-fuels/publication/OECD-IEA-G20-Fossil-Fuel-Subsidies-Reform-Update-2019.pdf>, 13/10/2020

alone provided fiscal support worth 33 billion euros per year in support of combustion engine vehicles, a capacity mechanism including coal-fired power plants, aviation, shipping, petrol and diesel⁷. The number also includes tax and RES levy exemptions for the industrial sector, which constitute implicit subsidies and lead to a disproportionate burden on consumers who have to fill any arising gaps in the financing of public goods. This undermines both the climate objectives and the fair distribution of costs in society.

There is a risk that, lacking harmonised EU energy taxation, Member States introduce reductions or exemptions in different ways. This in turn can lead to discrimination between different types of consumers and distorts competition in the internal market if only a certain part of the energy users – private households – bears the costs. The magnitude of exemptions is jeopardising public support for the energy transition. 75 percent of the German population regard the energy transition as a joint task, to which everyone in society must contribute. They complain about an unfair distribution of costs and misplaced subsidies for energy-intensive industries.⁸ About two-thirds of private consumers would accept even higher RES levies if the industry's exemptions were abolished⁹, indicating that consumers are willing to pay for a public good if the costs are shared equally.

❖ Therefore, policy-makers should abolish all direct fossil fuel subsidies as well as exemptions for industry, including the tax exemptions for kerosene in the aviation sector. Such an approach would distribute the costs of saving the climate and preserving the environment more equally and consumers would be more willing to accept higher costs¹⁰.

2. REVAMP PUBLIC POLICY REGARDING INDUSTRIAL COMPETITIVENESS

Relying too much on a decrease of energy costs to sustain competitiveness undermines the polluter pays principle and puts at risk the funding for the energy transition. Moreover, it starts a race to the bottom with third countries which spills over into taxation, wages, environmental and consumer protection. Such a race cannot be won by the European Union without fundamentally harming the public interest. It also opens up the EU to critique from less developed countries, who argue that only rich countries can afford to pursue ambitious climate policies while safeguarding their industrial bases through state aid measures.

Appropriate tools to deal with unfair competition exist, such as trade defence instruments, high environmental and consumer protection standards and funding for research, education and skills training. vzbv believes that the upcoming European Commission proposal on a carbon border adjustment mechanism could also provide a useful tool to safeguard European industrial competitiveness while ensuring that carbon pricing policies develop the desired steering effects towards more sustainable and de-

⁷ ODI, 2020, Phase-out 2020: monitoring Europe's fossil fuel subsidies, p.2: <https://www.odi.org/sites/odi.org.uk/files/resource-documents/11778.pdf>, 13/10/2020

⁸ IASS – Sustainability Barometer for the German Energiewende, 2017: <https://www.iass-potsdam.de/en/news/social-sustainability-barometer-energiewende-shows-broad-support-along-doubts-about>

⁹ RWI – Equity and the willingness to pay for green electricity in Germany, Nature Energy, 2018: <https://www.nature.com/articles/s41560-018-0233-x>

¹⁰ vzbv, 2019: <https://www.vzbv.de/pressemitteilung/verbraucher-sehen-chance-im-klimaschutz>, 13/10/2020

carbonised production methods. Introducing such a carbon border adjustment mechanism should lead to a revision of the state aid guidelines with a view to abolishing industry exemptions from taxes, RES levies and free allocation of ETS certificates.

- ❖ The European Commission should take a holistic view and consider alternative instruments to safeguard industrial competitiveness and protect European companies from unfair competition. The European Commission should aim at phasing out all direct and indirect fossil fuel subsidies and fully include EUs into the funding base for energy transition projects such as deploying renewable energy sources.

3. STRENGTHEN CURRENT STATE AID CRITERIA UNTIL NEW INSTRUMENTS ARE IN PLACE

Until a more comprehensive and socially just toolbox for safeguarding industrial competitiveness is created, the European Commission should try to minimise the current burden on households and re-examine the current criteria for state aid approval - exposure to trade and electro-intensity. On the one hand, the level at which the intensities were set are too simple. Not every company that currently benefits from exemptions is likely to move to a third country if exemptions are withdrawn or reduced. On the other hand, not every current beneficiary is threatened to be priced-out of the market if energy prices increase. They might stay competitive despite higher energy prices because they offer high product quality, a renowned brand, high productivity through well-trained workers, benefit from a market with high price elasticity of demand, provide products to niche markets for which a high degree of specialisation is required, or hold exclusive patents.

- ❖ The European Commission should reduce the number of sectors benefiting from exemptions in line with its original proposal on the ETS state aid guidelines.¹¹
- ❖ The European Commission should consider strengthening the conditionality surrounding possible state aid for energy intensive industry. These could include:
 - More stringent requirements on energy audits, including compliance with the recommendations resulting from an audit and an updated requirement to implement audit recommendations even if pay back times exceed a certain amount of years.
 - Requirement to reduce the carbon footprint of electricity consumption, for example through installing an on-site renewable energy generation facility.
 - Requirement to invest a significant share of at least 80 percent of the aid amount in projects that lead to substantial reductions of the installation's greenhouse gas emissions.
- ❖ The European Commission should consider strengthening the current criteria for industry exemptions, including higher trade and electro-intensities.
- ❖ The European Commission should develop further criteria to take into account the plausibility of companies being priced-out or moving to third countries in order to better target subsidies. Such criteria could include a market analysis that looks at price elasticity or an "easiness to relocate" indicator, as it might be easier for some

¹¹ https://ec.europa.eu/competition/consultations/2020_ets_stateaid_guidelines/draft_ets_guidelines_en.pdf

industries to “leak their carbon” than it is for others, where significant stranded investments would be left behind or significant up front investments would be required to relocate to another country.

III. REPORTING AND MONITORING

vzbv insists that monitoring and reporting is a crucial part of the state aid system. Without solid data, it is impossible to verify the effectiveness of state aid measures. Member States should systematically gather and report data on beneficiaries of state aid who shut down production sites and move their business outside the EU despite receiving subsidies. As carbon leakage is the underlying reason for state aid, it is necessary to monitor such leakages.

- ❖ The European Commission should conduct a rigorous qualitative and quantitative assessment of the incentivising effect that exemptions have on a company's decision on where to locate.

IV. TACKLING COST AVERAGING SUPPORT SCHEMES

In Germany, a nation-wide ‘cost averaging support scheme’ was set up for the promotion of renewable energy sources. Under such a scheme, the sum of the subsidies for RES deployment is averaged across every consumed kWh. Every electricity user pays a levy per kWh (renewable energy sources levy – RES levy). That means that if one type of user is exempt from paying the RES levy, other users need to compensate the funding gap. To support the competitiveness of certain industrial sectors, the German government introduced the ‘special equalisation scheme’, which exempts EIU from paying the RES levy. The methodology of the special equalisation scheme derives from the current EEAG's chapter on industry exemptions.

In 2019, the special equalisation scheme was worth 4.9 billion euro/year, benefitting 2098 companies while burdening private consumers with an extra 1.57 cent/kWh¹². This has to be seen together with a wide-ranging insulation of the energy-intensive industry from all costs associated with the energy transition. Benefits range from exemptions from concession levies (e.g. 3.6 billion euro/year), network charges (700 million euro/year), co-generation support levies (200 million euro/year), offshore-wind liability charges (100 million euro/year) to the free allocation of CO₂ emission certificates¹³. The financial burden on consumers is further aggravated as they do not only have to make up for this financing gap of roughly 10 billion euro/year, but they also have to pay another two billion euros in Value-Added-Tax¹⁴ on it.

However, the German financing mechanism provides a second benefit to industrial actors. The renewable energy that is paid for in large parts by households and small companies decreases the wholesale price of electricity that industry has to pay. Thus, industry is not only largely exempt from paying the RES levy, but also benefits from lower electricity prices through renewable energy funded by households. German households

¹² Bafa, 2020: file:///C:/Users/tbobi/AppData/Local/Temp/bar_hintergrundinformationen.pdf

¹³ FÖS – Brief expertise, 2017: <http://www.foes.de/pdf/2017-04-FOES-Kurzanalyse-Industrierausnahmen-2005-2016.pdf>

¹⁴ 19 percent in Germany from 1.1.2021 onwards

and small companies basically pay for the energy transition and subsidise the market price of electricity for industry. In addition, the RES levy is a market premium. That means it is the difference between the market price and the price that a RES producer has been guaranteed by the RES support scheme. The lower the wholesale market price, the higher the RES levy. German consumers are stuck in a vicious circle of price increases that have made the German retail electricity price one of the highest in the world.¹⁵

Unfortunately, the CJEU ruled in ‘Germany versus Commission’¹⁶ that the German Law on Renewable Energy from 2012 does not constitute state aid, thus removing it from the European Commission’s state aid purview. However, that decision only applies to the 2012 version of the law. Since 2012, the German Law on Renewable Energy has undergone repeated revisions, such as in 2017 and is currently being revised again. German lawmakers currently consider legislation that would use the revenue generated from Germany’s national emissions trading scheme to reduce the RES levy. The European Commission should use these revisions to examine if the “element of state control”, which the CJEU found missing, is now established and whether the law could be once again assessed under EU state aid competence.

In Germany, cost averaging systems are also being used to subsidise combined heat and power, applying a similar mechanism as for the financing of renewable energy. Further cost averaging systems are discussed with regard to the financing of hydrogen installations. In each case, industrial players benefit from exemptions to contribute to this public policy objective. Even though these exemptions might not technically constitute state aid, they do develop a distortionary impact on competition in the internal market. Consider the following example: two EU Member States (A, B) establish a financing mechanism for RES. Member State A finances it through the budget, Member State B through a cost averaging system. Member State A can only provide limited exemptions to EIU because state aid rules apply, while Member State B could potentially fully exempt its industry. In theory, there is an incentive for companies to move from A to B. Such a race for the lowest contributions to the financing of a public good cannot be in the interest of the European Union as it undermines the incentive to decarbonise production and distorts the level-playing-field of the internal market. Hence, special precaution need to be taken with regard to cost-averaging financing systems.

- ❖ The European Commission should develop policies and legal tools to ensure the control over and conditionality for cost averaging support schemes.
- ❖ The European Commission should strengthen the principle of a fair distribution of costs between industry, companies and private consumers by developing neutral indicators to determine a risk to the overall solidarity of financing the public good. Such indicators could be derived from a best practice analysis of how Member States implement Article 21 (3) (b) of the Renewable Energy Directive¹⁷ where the

¹⁵ Eurostat, May 2020: <https://ec.europa.eu/eurostat/documents/2995521/10826603/8-07052020-AP-EN.pdf/2c418ef5-7307-5217-43a6-4bd063bf7f44> 26/10/2020

¹⁶ CJEU, 2019, C-405/16 P: <https://curia.europa.eu/jcms/upload/docs/application/pdf/2019-03/cp190044en.pdf>

¹⁷ Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources. Article 20 (3) (b) allows Member States to introduce charges on RES prosumers “if it is demonstrated, by means of a cost-benefit analysis performed by the national regulatory authority of that Member State, which is conducted by way of an open, transparent and participatory process, that the provision laid down in point (a)(ii) of paragraph 2 either results in a significant disproportionate burden on the long-term financial sustainability of the electric system”. https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uris-erv:OJ.L_.2018.328.01.0082.01.ENG&toc=OJ:L:2018:328:TOC ; 23/10/2020

concept of a “significant disproportionate burden on the long-term financial sustainability of the electric system” is introduced in EU legislation.

- ❖ In case a risk to the overall solidarity of financing a public good like the energy transition is determined, Member States should be required to reduce exemptions or finance them from their national budgets.

V. STATE AID FOR HYDROGEN

Hydrogen has enjoyed a great deal of attention by public policy makers in recent months. Even though hydrogen plays only a marginal role in today's energy systems, there is a certain potential for its use, e.g. in the aircraft industry or in the decarbonisation of certain industrial processes, e.g. the steel sector.

However, vzbv does not see hydrogen applications to play a role for households in the short or medium term. The reasons are diverse: first of all, hydrogen should be clean, i.e. produced with renewable energy, but renewable energy is still scarce and should better be used to electrify heating and transport than to produce hydrogen which entails a high degree of energy loss when produced.

With regard to state aid for hydrogen production, transport, storage and usage:

- ❖ vzbv points to the aforementioned risks to a fair distribution of costs if cost averaging support schemes pay for setting up and operating hydrogen value chains.
- ❖ vzbv also points to the user pays principle, which means that those industrial actors who wish to use hydrogen should carry the costs for the production and for the infrastructure necessary to transport and store hydrogen. Those costs should not be dumped on households.
- ❖ State aid should not be allowed if it is intended to finance fossil-fuel based hydrogen production. Using fossil-fuel based hydrogen would create lock-in effects with regard to long-term investments and promote market inefficiencies which could undermine the transition towards renewable energy production.
- ❖ Drawing from lessons learned from comparable networked industries (gas, electricity) vzbv demands the complete unbundling of electrolyzers and hydrogen network operators and potential hydrogen service providers (such as hydrogen refuelling stations).
- ❖ The European Commission should pay special attention to the financing of hydrogen networks (such as dedicated pipelines or industry-centric distribution networks) through general grid charges borne by households. The general grid charges are meant to finance gas and electricity distribution systems. The Commission should prevent cross-subsidisation of a hydrogen infrastructure that is not used by households. In addition, existing gas networks, which have been paid for by consumers through the general network charges should not be misappropriated and transformed into hydrogen networks.
- ❖ When the European Commission considers the impact of a state aid mechanism for hydrogen, it should require the Member State to explain why direct electrification would not be a more efficient and resource-appropriate way forward.