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Euromines Position with regards to the allocation rules for Phase 4 of the EU Emission Trading System (ETS)

Background information about the European mining Industry

The European mining industry plays a crucial role in the ability of the European Union (EU) to nurture a sustainable growth including access to and supply of raw materials. Linked to all industries across all supply chain stages, raw materials are essential to numerous industrial sectors including over 30 million jobs and playing a key role in the development of modern environmentally friendly technologies[1].

The European mining industry competes at all levels, local, national and international mainly on costs. Cost increases cannot be passed to consumers precisely because the mining companies compete at global level and must maintain cost structures comparable to the ones of their international competitors. In this context, a strong industrial base, securing a reliable fair international competition, a level playing field and unhindered access to raw materials is of key importance for Europe's prosperity and growth.

Euromines welcomes the European Union commitment to reduce greenhouse gas emissions by at least 40% domestically by 2030 (the sectors covered by the ETS to reduce their emissions by 43% compared to 2005), but would like to underline the list of elements essential for the extractive industry in achieving this objective, such as:

- The whole design of the EU ETS should not undermine the competitiveness of industry, in particular the energy-intensive sectors that are most vulnerable to unilateral carbon and energy cost increases;
- Free allocation at European level should continue to be the key tool for sectors exposed to carbon leakage alongside with financial compensation for CO2 costs and electricity prices (electricity represents a substantial share of the mining industry operating expenses), as long as a global commitment to price carbon is not reached;
- The post 2020 rules on free allocation and financial compensation for indirect costs should be clear, predictable and effective to ensure the competitiveness of the European industry;
- Alternative measures such as separate policy regimes for industrial and power generation sectors and the inclusion of imports in EU ETS should be analysed and further explored;
- Post 2020 legislation implementing the 2030 package should avoid overlapping with other legislation in particular in the field of renewables and energy efficiency.

[1] The Raw Materials Initiative, http://ec.europa.eu/growth/sectors/raw-materials/policy-strategy/index_en.htm

Given all of the above, Euromines would like to make the following comments and recommendations with regards to the allocation rules for Phase 4 of the EU Emission Trading System (ETS):

1. Free allocation and carbon leakage provisions (Art. 10a and 10b)

1.1Benchmarks for the determination of the free allocation to industry

Under the current proposal for phase 4, product benchmarks will be cut based on the level of verified efficiency improvement achieved. In a central case, this would result in an average 17.5% reduction from the current product benchmarks over 2021–2030.

Euromines position and recommendation:

Euromines believes that a revision of benchmarks should take place only once in the trading period so that it allows legal certainty and limits the administrative burden, in particular for sectors with a high number of installations.

The benchmark level should be better tailored to meet the individual circumstances of each sector and comply with the technological progress.

Benchmarks should be recalculated based on updated data provided by the industry in Europe in order to reflect the actual evolution of emission performance and should not result from an annual linear reduction as this is arbitrary and contradicts the principle of technical feasibility.

Historic levels should not be taken into consideration when calculating the benchmark because they tell little about future developments and could well result in effectively placing a ceiling on investment in new industrial activities.

1.2Carbon Leakage (CL) Factor

Under the current proposal, the CL factor in phase 4 of the EU ETS will be 100% for those sectors and subsectors considered to be at significant risk of CL (i.e. on the CL list) and 30% for the others. In this context, the CL status is vital to maximising the number of free allowances granted and minimising direct carbon costs.

Euromines position and recommendation:

Free allocation for carbon leakage sectors should be dynamic, taking into account recent production levels. It should allow industrial growth and extended production in the sense of backward integration. The current system based on historical activity levels deters any incentive for growth in times of economic recovery.

The qualitative threshold for carbon leakage assessment should be more flexible and take into consideration both sub-sectors and exposure to indirect costs.

1.3The Cross-Sectoral Correction Factor

No other linear correction factor should be applied as it will additionally cut the free allocation below economically and technologically feasible levels.

1.4Process emissions

Process emissions are particularly significant for the mining industry most of the times accounting for over 50% of direct emissions. Within subsectors and installations, discrepancy of share of process emissions is very high, depending on raw material and technology, making difficult for the industry to improve its emissions intensity to match the rate of decline of free allowances anticipated in phase 4 of the EU ETS.

The EC has already acknowledged the difficulty in reducing process emissions: where the fall-back approach for process emissions is used, the number of free allowances provided is equivalent to 97% of the process emissions.

Euromines position and recommendation:

Process emissions should either be excluded or granted full free allocation due to the inability to reduce them as they are linked to the chemical properties of locally available raw materials.

A possible route to supporting industries with a significant share of process emissions would be to create a separate pot for free allocation to industries at risk of CL, with a high share of process emissions.

Another suggestion would be to apply a lower cross-sectoral correction factor for sectors with a high share of process emissions.

2. Indirect carbon costs (Art. 10a(6))

A key factor to the net indirect carbon cost is the level of financial compensation which is provided by Member States.

For several mining sectors (iron ore, mined potash, nonferrous metals ores), the indirect emissions intensities are higher than the direct emissions ones. However, as free allocation only offsets part of the direct carbon cost and State Aid is currently not provided to compensate for the indirect carbon costs of the surveyed installations, the total net carbon cost is significant.

At the same time, the current system for indirect cost compensation encourages installations to prefer direct emissions over indirect emissions. This hinders greater electrification of the production process, thereby slowing down an essential step in the transition to a low carbon economy.

Euromines position and recommendation:

Euromines supports the introduction of state aid and compensation for indirect carbon cost across all Member States. Where such a system is already efficiently implemented, its status quo should be recognised and conserved. The existing levels of compensation in the countries, where compensation systems exist, should remain unchanged.

3. Sector specific recommendations

3.1Magnesia

Process emissions are particularly significant for the magnesia sector accounting for over 66% of direct emissions. This result indicates that it will be difficult for this sector to improve their emissions intensity to match the rate of decline of free allowances anticipated in phase 4 of the EU ETS, leading to exposure to a greater risk of CL.

Magnesite is considered critical raw material for the EU policies due to its economic importance. The strategic uses are numerous in industrial sectors and agriculture (food chain supply). The European production fulfils all the environmental and safety regulations for all applications.

Considering the best case scenario where State Aid for indirect cost compensation is provided by all Member States, this aid would cover about 65% of the indirect carbon cost. The resulting total net carbon cost of magnesia under this best case is estimated to be 8€/t. In the mid and worst case scenarios, where indirect

carbon costs are not offset by support measures, the net carbon cost will be approximately 9€/t and 35€/t, respectively. This cost increase in European production of magnesia leaves the sector outside the world market.

Euromines position and recommendation:

Process emissions (decarbonisation MgCO3 --- MgO+CO2) should either be excluded or granted full free allocation due to the inability to reduce them as they are linked to the chemical properties of locally available raw materials.

A possible route to supporting industries with a significant share of process emissions would be to create a separate pot to guarantee 100% of allocations relating directly with annual production.

3.2Iron ore

In the best and mid case scenarios, the level of free allocation to the sector will cover 75% of the direct carbon costs. The reduction compared to the current level of free allocation is due to the anticipated cut in the cross sectoral correction factor (CSCF) and benchmark. Under the worst case scenario, which would see the iron ore sector fall off the CL list, free allocation covers only 25% of the direct carbon cost.

Euromines position and recommendations:

The best and mid case scenarios are dependent upon the availability of the EU aggregated Gross Value Added (GVA) data for the iron ore mining sector which is required to calculate emissions intensity. This data is currently not available via Eurostat. The EU should accept verified third-party data in order to ensure that sectors deemed to be at 'high risk' of carbon leakage receive the collect free allocation under Phase IV of ETS.

It is important that compensation schemes for indirect carbon costs are implemented in all EU Member States in order to provide financial predictability for EU mining sectors and to streamline industrial competitiveness between Member States. This scheme should be mandatory and based upon a common EU-wide formula. Where such a system is already efficiently implemented, its status quo should be recognised and conserved.

The proposed Innovation Fund is essential to promote the shift to technologies that can facilitate the transition towards low carbon mining with a maximum reduction of emissions.

3.3Non-ferrous metal ores

As non-ferrous metal ore mining does not face direct carbon costs, and non-ferrous metal ore mining is not eligible for State Aid, the entire net carbon cost is attributed to indirect carbon costs. The future indirect carbon cost is expected to increase by approximately a factor of four, due to the higher carbon prices anticipated post-2020.

Considering the best case scenario where State Aid for indirect cost compensation is provided by all Member States, this aid would cover about 60% of the indirect carbon cost. Therefore, CL will remain an issue for the non-ferrous metals sector in phase 4 of the EU ETS. Even under a best-case scenario which provides financial compensation for indirect carbon costs, the net carbon cost still are between 8–13% of current energy costs in Phase 4 of the EU ETS.

Euromines position and recommendations:

Euromines recommends a mandatory compensation instrument in all EU Member States. In such a system, all eligible installations in the EU ETS would receive support for their indirect costs based on a harmonised EU-wide formula.

4. Funding and financial compensation measures

Euromines believes that financial compensation measures are of utmost importance to prevent carbon leakage.

Energy intensive industries acting in the mining sector constantly have to improve their energy efficiency as they struggle to reduce a major cost via more efficient processes. The European mining and minerals industry is among (if not) the lowest CO2 generating extractive industry in the world. A number of companies have made over the last few years major efforts to further reduce their emissions in accordance with best available techniques (BAT) prescribed at EU level and increase their energy efficiency up to the level that technology and physics allow.

Additional expenses would lead not only to a carbon but also an investment leakage, less jobs, less production and less innovation.

Euromines position and recommendation:

Euromines advocate for R&D support for technologies which can deliver emission intensity or electricity intensity improvements, following a more structured review of opportunities.

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About Euromines

Euromines, the European Association of Mining Industries, Metal Ores & Industrial Minerals, represents large and small companies and subsidiaries in Europe and in other parts of the world which provide jobs to more than 350,000 people. Through the activities and operations of these members, more than 42 different metals and minerals are produced. Their sustainable exploitation can increase Europe's supply of mineral resources, help ease imports from third countries usually applying lower environmental, corporate and social standards and foster the socio-economic growth of Europe's Regions.