



Ms Marianne Wenning  
Head of Unit  
European Commission  
DG Environment  
Avenue de Beaulieu 5  
1160 Brussels

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Dear Ms Wenning,

BUSINESSEUROPE has examined different policy approaches for dealing with NO<sub>x</sub> and SO<sub>2</sub> emissions. It has led us to the conclusion that an EU-wide trading scheme cannot be the way forward, given the strong objections prompted by the putative environmental and economic benefits. A central point is that industrial emissions of these gases are already effectively regulated by several international agreements, European legislations and national measures such as site-specific permit conditions or taxation. An EU-wide trading scheme would bring double regulation and unnecessary costs.

BUSINESSEUROPE recognises the importance of a broad and integrated debate on how to continue improving air quality in the EU while pursuing economic growth. However, on NO<sub>x</sub> and SO<sub>2</sub> emissions, DG Environment should not limit the debate on possible solutions to an emission trading scheme. It is indispensable to address a number of key points at the very outset of the discussion, starting with a clear identification of the nature and extent of the problems, and with a review of policies and initiatives already in place at national, European and international level.

With an open mind but strong reservations on the direction taken by DG Environment work, BUSINESSEUROPE and the main industrial sectors took part in the first study of the ENTEC consultancy "*Assessment of the possible development of an EU-wide NO<sub>x</sub> and SO<sub>2</sub> trading scheme for IPPC installations*" and provided a significant amount of data.

i) *Comments on the final draft report of the first DG Environment study*

As a follow-up to the stakeholders meeting organised on 10 February, BUSINESSEUROPE would like to pass on to you the following general comment.

Our view is that the draft final report does not make a convincing case and does not provide clear and satisfactory responses on a number of pivotal elements (e.g. risk of double regulation, costs for industry or effective benefit-sharing, workability of the emission trading scheme for NO<sub>x</sub> and SO<sub>2</sub>, etc.).



In addition, we believe that the report contains significant inaccuracies and methodological approximations (regarding policy baselines, modelling approaches and data representativeness, etc.), which raise serious questions about the robustness of the conclusions presented.

You will find at annex a comprehensive list of key concerns on the draft report. Many of them have already been mentioned by industry at the stakeholders meeting on 10 February and remain valid.

The additional meetings which were organised on 22 February with several European industry associations with a view to clarifying how sectoral data have been used by ENTEC have not managed to allay key concerns. Further uncertainties have arisen for a number of industry sectors and in some cases apparent mistakes have been uncovered.

ii) *Comments on the second DG Environment study*

I would like to share with you also a number of comments on the second study "*Economic analysis to support an impact assessment of the possible establishment of EU-wide emissions trading of NO<sub>x</sub> and SO<sub>2</sub>*".

You will understand our astonishment to learn that work on the second study has started even though the first has yet to be finalised. The meeting on 10 February showed that many questions remain for all the stakeholders involved. It would seem more coherent and effective not to have started the second study until the first has been concluded and the identified flaws properly addressed. The common ground identified between all stakeholders could then have formed a clear and solid base to start work on the second study.

Moreover, allow me to underline that all representatives of industry were very surprised to see that what was announced as the first workshop on the second study was compressed into no more than thirty minutes of presentations/discussions at the end of the day. We do not think that it can be regarded as a first stakeholder consultation meeting for the second study.

On the substance, it is essential that this second study does not base itself exclusively on an equilibrium model, since the calculations on CO<sub>2</sub> leakage have shown that this does not make it possible to analyse competitiveness issues correctly. Furthermore, the methodology must draw inspiration from work by DG Enterprise and Industry and the sectors concerned on CO<sub>2</sub> leakage.

Lastly, it is crucial that indirect impacts on energy prices are taken into account in the second study in the same way as they have been addressed in the CO<sub>2</sub> leakage assessments for the directive on Emission Trading Scheme for greenhouse gases.



To conclude, BUSINESSEUROPE and the industrial sectors maintain their reservations regarding the process and the end product that will result, but welcome the recognition that a competitiveness study is needed. They are prepared to contribute to it. To this end, the points set out above are essential to establish a good basis for the work.

I thank you for the attention you may give to these matters and remain at your disposal for any further discussions on this important subject.

Yours sincerely,

Marco Mensink  
Chairman of the BUSINESSEUROPE NO<sub>x</sub>/SO<sub>2</sub> Trading Task Force

*Cc: Andreas Menidiatis, DG Enterprise and Industry  
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**ANNEX: list of industry key concerns on the final draft report “Assessment of the possible development of an EU-wide NO<sub>x</sub> and SO<sub>2</sub> trading scheme for IPPC installations” (8 March 2010)**

According to BUSINESSEUROPE, the draft final report does not provide clear and satisfactory responses on a number of pivotal elements (e.g. risk of double regulation, costs for industry, workability of the emission trading scheme, etc.) and contains a number of inaccuracies and methodological approximations (regarding policy baselines, modelling approaches, sensitivity analysis, etc.).

Industry’s main concerns are summarised below:

1) RISK OF DOUBLE REGULATION

- It is acknowledged in the draft report that air quality limits set by the Air Quality Directive will need to be respected and therefore may require imposition of emission limit values (ELVs). Although the modelling indicates that ELVs would be lifted, industry does not see this to be a likely scenario in the Member States. There is no assessment of the impact of setting ELVs for NO<sub>x</sub> and SO<sub>2</sub> on top of an emission trading scheme (ETS), which is the likely situation. The Dutch experience shows that ELVs and a trading scheme for NO<sub>x</sub> do not work together as market liquidity is very low.

2) COSTS FOR INDUSTRY ARE NOT PROPERLY ADDRESSED

- The way that costs are presented in the draft report brings confusion in the perception of the relation between costs and benefits between sectors and Member States. For example, the costs for industry have been mixed with the environmental benefits and costs for society as a whole. In addition, the costs for industry are presented as savings compared to a reference scenario. In fact, they remain costs for industry. In order to ensure well-informed decisions, the final report should be improved on these aspects in order to provide clarity on who bears which costs and who receives the benefits.
- For companies applying IPPC-permit conditions, an ETS would bring additional costs whatever the allowance allocation system is. The situation for companies already operating at a Best Available Techniques (BAT) level would even be more unfair, as an ETS would bring additional costs in the absence of full free allocation. In any case, the administrative costs would come on top of this:
  - The estimation of costs presented in the draft report does not take into consideration the huge administrative work associated with the organisation of an ETS as the experience with the ETS for CO<sub>2</sub> shows. All the adjustments which are required to avoid pollution-leakage and economic downturn, such as benchmarking, auctioning organisation or national registries have not been taken into consideration.



- The total of €35 million per year regarding monitoring, reporting and verification (MRV) costs of ETS for NO<sub>x</sub> and SO<sub>2</sub> seems to underestimate the reality. The draft report fails to recognise the many technical challenges associated with measurement and/or estimation of NO<sub>x</sub> and SO<sub>2</sub> emissions under actual industrial conditions. Where such challenges are encountered (e.g. no suitable location for installation of a continuous emission monitoring system in an existing facility), investment costs and engineering time required to establish adequate monitoring and reporting systems will escalate far above the optimistic numbers assumed in the report.
  - The draft report provides no assessment of the indirect costs to energy-intensive industries due to the effect of an ETS on power prices. These effects need to be assessed at a national level. On 10 February, DG Environment mentioned that the indirect costs will be taken into consideration into the second study. Therefore, it must be clearly stated in the final report of the first study that it has not addressed the indirect impacts on power prices and therefore cost impacts are limited in scope.
- 3) LACK OF GUARANTEES ON THE WORKABILITY OF ETS FOR NO<sub>x</sub> AND SO<sub>2</sub>
- The draft report provides no assessment of the liquidity of the market under the different ETS scenarios. The fact that new installations should in practice have little room to trade is an example of key elements which should be carefully assessed. The draft also lacks of a sensitivity analysis of the capacity to maintain an ETS in the long term, which is the basic condition to influence market operators' behaviours.
  - Experience shows that the perfect market conditions assumed in the report in fact do not exist. This is clearly illustrated by the ETS for CO<sub>2</sub> and it has a significant impact. For example:
    - In the case of auctioning, "Benefits" of trading are immediately reduced if the system moves away from total revenue recycling, which is ignored as a possible outcome of the legislative process.
    - CO<sub>2</sub> and NO<sub>x</sub> emissions are often coupled (CO<sub>2</sub> lowering will increase NO<sub>x</sub>). The overlap and interference between ETS for CO<sub>2</sub> and ETS for NO<sub>x</sub> is not properly addressed in the report and remain a "gray area" with potential far-reaching negative impacts on industry.
  - Key drivers of the price in the ETS for CO<sub>2</sub> are oil price impacts, organisation of auctioning, sector caps, etc. The report assumes the lowest cost technical options will set the price, which in fact is by no means the case in ETS for CO<sub>2</sub>.



#### 4) ENVIRONMENTAL AND HEALTH IMPACTS

- The jumps in NO<sub>x</sub> and SO<sub>2</sub> emission reductions presented in the report seem to be triggered by the basic assumptions such as the application or not of national emissions ceilings (NEC) or the setting of caps based on upper, intermediate or lower Best Available Techniques Associated Emissions Levels (BATAELs). It shows that ETS does not have a huge impact in terms of emission reductions and that environmental and health objectives can be achieved by implementing existing laws. Therefore, the ratio between additional efforts (see section 2 on costs) and environmental and health impacts is unbalanced.
- The draft report favours an EU-wide trading scheme. This does not make sense from an environmental and health point of view since it has the potential to amplify or create new air quality hotspots. In addition, it would clash fundamentally with the well-established approach under the NEC Directive in which emission reductions across Europe are optimised at a national level.
- The report does not properly address the issue of cross-media effects. The ETS and the integrated approach defined by the IPPC system seem hardly compatible in practice at a local level. It is most likely that cross-media effects will appear as soon as an ETS for NO<sub>x</sub> and SO<sub>2</sub> is applied, resulting in likely undesirable effects on other pollutants and disproportionate costs.
- The analysis of environmental impacts is brought from the available 50x50 km grid to 10x10 km grid thanks to simplified assumptions. Moreover, even this assumption could be insufficient as local impacts can only be studied on the basis of a 1x1 km grid.

#### 5) INACCURACIES AND METHODOLOGICAL APPROXIMATIONS

##### a) Policy baseline

- The report attempts to second-guess the legislative outcome of two of three key air quality laws: the Industrial Emissions Directive (IED) and the National Emissions Ceilings (NEC) Directive, neither of which is finalised.
- There are significant differences for many Member States between this first study and the methodology used for the NEC Directive (GAINS approach developed by the International Institute for Applied Systems Analysis - IIASA). It is of concern that significantly different views of activity are being used for the development of air quality policy and legislation in the Industrial Emissions Directive (IED) and NEC Directive contexts. Until these differences are resolved the robustness of the policy baseline is questionable.



b) Database of industrial installations

- The distributions of emissions between Member States estimated by IIASA and ENTEC are clearly different. Therefore, there is a risk that the ENTEC data base is not adequate in terms of its composition of plants per Member States.
- It is questionable whether the database gains a sufficient degree of representativeness of the actual situation of plants, for example regarding the uptake of abatement techniques.

c) Modelling approaches

- The basis of the study for 2020 projections in NO<sub>x</sub> and SO<sub>2</sub> emissions is an out-of-date set of energy projections from the 2007 PRIMES model which do not adequately account for the effects of the economic crisis. In 2007, PRIMES estimations of Gross Value Added growth for the period 2005-2020 was + 35% whereas it has fallen to 22% according to recent figures derived from latest PRIMES estimations in 2009 (*source: Presentation of baseline 2009 scenario with PRIMES to the European Commission Climate Policy Working Group 2, January 2010*).
- The conclusions of the study are based on a very complex modelling process which contains significant uncertainties throughout. For example, the 'business as usual' scenarios shows enormous growth in sector emissions compared to the European Pollutant Emission Register (EPER) 2004 data.
- The draft report fails to provide a complete view of the costs/benefits ratio between sectors and between Member States. To this extent, a presentation of absolute figures instead of relative differences compared with a reference scenario would be useful.
- There is little or no sensitivity analysis of the data used in the scenarios, which fails to point out how the results are related to the existence of "perfect" conditions and what effects could arise if there is a slight move away from these conditions. A more careful assessment and quantification of the impact of the uncertainties on the policy-relevant conclusions is desirable since after months of discussions on GAINS modelling for example, there are still large differences (> 50%) in interpretations.