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The European Steel Association

DIRECTOR GENERAL

Brussels, 3 July 2015

Mr. Miguel Arias Cañete
Commissioner for Climate Action & Energy
European Commission
Rue de la Loi, 200
B-1049 Bruxelles/Brussel

Dear Commissioner Arias Cañete,

I am writing to you to seek your support and commitment with regard to the draft Commission proposal on the EU Emissions Trading Scheme (ETS) review that became public on 1 July 2015.

The draft proposal unfortunately does not take account of the clear concerns expressed by over 60 CEOs from the steel industry in a letter sent to the Commission on 24 June 2015 (attached).

Nor does the draft follow the guidelines on carbon and investment leakage as set out by the European Council on 24 October 2014 and supported by both the European Parliament and the Commission in their recent agreement on the Market Stability Reserve:

- The mandate "*to prevent the risk of carbon leakage*" and "*the most efficient installations in these sectors should not face undue carbon costs*" is not met because the shortage in free allowances for the EU steel industry will be as high as with the current rules making the most efficient steel plants in Europe structurally short due to unachievable benchmarks and the correction factor. Furthermore, there are no provisions that would ensure the offsetting of indirect costs. The correction factor is still part of the draft although the mandate implies deletion.

- The mandate that "*the benchmarks for free allocations will be periodically reviewed in line with technological progress*" is not met. In contrary, a second correction factor has been introduced with the automatic reduction of the benchmarks by 0.5% to 1.5% per year regardless of whether this is "in line with technological progress". The mandate is that benchmarks need to be updated periodically at the level of the most efficient installations and not artificially reduced below that value.

- The mandate that "*both direct and indirect carbon costs will be taken into account … to ensure a level-playing field*" is not met. A level playing field is not given if even the most efficient plant in Europe has costs not faced by its global competitors. In fact, nothing at all has changed for indirect costs as the modification of the word '*may*' into "'*should*' *compensate*" is merely stylistic. Instead, the Market Stability Reserve will significantly increase industrial energy prices in the EU compared to global competitors.

- The mandate "*incentives for industry to innovate will be fully preserved*" is not met for the steel industry as about half of our Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) may be wiped out by the costs of the EU ETS.

In addition to the above, the draft unexpectedly contains a new element that compounds the negative impact of the existing proposals. It defines the preservation of a fixed amount of auction volumes (i.e. 57% of the total ETS cap) as the primary objective of the reviewed ETS Directive, while the overall goal until now was the cost-efficient reduction of CO2 emissions taking into account also industrial competitiveness.

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Article 1 paragraph 5 of the draft states, "*In order to respect the auctioning shares set out in article 10, the sum of free allocations is necessarily limited.*" This means that auctioning stands above global competitiveness, growth, jobs and investment in Europe.

Accordingly, the draft places itself at odds with the professed key priorities of the Juncker Commission.

We are not aware that any member state has ever requested the above arrangement. The European Council Conclusions clearly set out the prevention of carbon and investment leakage as a priority (paragraph 2.4) over the auctioning of allowances.

This is also the opinion of several lawyers. Only the final paragraph (paragraph 2.9) of the Conclusions states that "*the rest of allowances will be distributed among all Member States on the basis of verified emissions, without reducing the share of allowances to be auctioned*"

Finally, I remind you of the Conclusions of the European Council of 20/21 March 2014 which stated, "*Europe needs a strong and competitive industrial base, in terms of both production and investment, as a key driver for economic growth and jobs. … A strong, resource-efficient and competitive European industrial base must be seen in relation to a coherent European climate and energy policy, including through addressing the issue of high energy costs, in particular for energy-intensive industries.*"

One of the principles set out in the March 2014 Conclusions is to "*ensure security of energy supply for households and businesses at affordable and competitive prices*". The EU ETS is probably the most powerful lever available to the Commission to act on the economy. It would be an irreversible miscalculation should it, as a policy tool, be turned into a hindrance to industrial competitiveness and economic sustainability.

As we have stated on several occasions previously, the ETS review needs to offset direct and indirect costs at the level of best performers in our sector, since the EU steel industry has been repeatedly recognised as being at a very high risk of carbon leakage.

Our industry is effectively on the precipice of viability in Europe, not at least because of significant extra-EU competition. There is significant global overcapacity and a substantial degree of protectionism in a number of large producers outside the EU, which undermines our continent's steel industry. A tool to strengthen environmental performance should not be used to further hammer the industry.

We hope that above considerations will find your support in the final discussions on the Commission proposal.

Yours sincerely,

Axel Eggert

CC: College of Commissioners