

November 18th, 2022

Open letter: ETS revision and CBAM should not discourage circularity

Dear Executive Vice-President Frans Timmermans

Dear Commissioner Paolo Gentiloni

Dear MEP Peter Liese

Dear MEP Mohammed Chahim

Dear Ambassador Jaroslav Zajíček

Dear Ambassador Edita Hrdá

We are writing to you on behalf of more than 5,500 industries, to express our strong concerns regarding the legislative texts on the revision of the Emissions Trading Scheme (ETS) and the Carbon Border Adjustment Mechanism (CBAM), presented by the European Commission, Council and Parliament as part of the dialogue.

The Commission, Council, and Parliament have proposed to extend the regime of free allocation until well into the next phase of the EU ETS, in the 2030s. We believe that the proposals perpetuate competitive distortions which are damaging to the EU's competitiveness, its self-sufficiency, its resilience to inflation and its ability to adapt to a lower-carbon world.

This is because:

- The allocation system of emission allowances, based on benchmarks, grants more permits to polluting production processes than to less polluting ones, thereby subsidising pollution.
- Plans to revise the ETS benchmarks (currently scheduled for implementation in 2026) will not fully address this problem because the installations covered by the scheme produce mostly intermediary products rather than finished ones (e.g., “clinker”, as opposed to “houses”). These changes will therefore fail to incentivise low-carbon activities.
- An amendment proposed by the Council even exempts the “hot metal” steel benchmark until 2030 from any change in annual reduction rate despite the forthcoming benchmark reform.
- Some products, such as steel, are to be covered by the CBAM but not the upstream products (called “precursors” in Annex III of the CBAM regulation) that are used to manufacture them, such as coking coal, sintered ore and ferro-alloys. As a result, the EU-based manufacture of precursors will keep receiving free allowances, and the embedded emissions of **precursors of imported steel will not be covered by the CBAM**, for obvious WTO compliance reasons.
- While the emissions from upstream products of the blast furnace route (coking coal and sintered ore) will likely be exempted of CBAM charges, this is not the case for a key upstream product

of the electric arc furnace (EAF) route: direct reduced iron will be covered by the CBAM under all proposals¹. The blast furnace and the EAF route are therefore not treated equally.

- It is sometimes assumed that the reform will see more installations covered by the ETS, which will then become eligible for free permits. However, this will also fail to reduce competitive distortions, as only larger plants can realistically join the ETS due to bureaucracy costs. The free allocation system, which grants emission permits in proportion to production output, is designed to incentivise high levels of production activity, to the detriment of resource-saving. The Russian war in Ukraine and ensuing critical need to save resources has shown the limits of this approach.
- The 4th phase of the EU ETS planned for 2021-2030 has gaps that put recycled materials at a disadvantage compared to primary raw materials (ores, coal, etc.). The disadvantage arises because ecological burdens from steel production from ores are not fully taken into account, as hard coal, iron ore and other non-ferrous metal ore mining are not subject to the EU ETS as they are not listed under Annex I of the Directive. The ecological burdens from ore extraction in Europe thus have no impact on the costs of steel production and are not internalized as external costs for the environment and society. When recycled steel material is used, these external costs are not incurred. Incentives to recycle are absent from the price mechanism and the steering effect of the EU ETS.

While the proposed extension of free allocation was thought to be protective of industry generally, it only protects *some* industry players.

The companies hereby represented would suffer from unfair competition if the above support measures were continued, as currently proposed. A late phase out of free allocation of allowances and a slow implementation of the CBAM would create an obstacle to otherwise profitable production practices, as the installations covered by the EU ETS do not need to price carbon costs into their products.

Our industries are labour-intensive and capital-intensive, but they are not resource-intensive. They have the potential of saving large amounts of resources, including Russian imports, including expensive fossil fuels.

Policymakers should not listen to just a handful of large stakeholders. European industrial policy should support the continent's SMEs, especially those that are essential in securing a front seat in the development of technologies and processes which will enable faster decline in Europe's greenhouse gas emissions and reduce dependence on Russian imports.

That is why, ahead of the trilogue negotiations about to start, we urge you to support the following positions:

1. **Hard coal, iron ore and other non-ferrous metal ore mining sectors as well as the production of pellets and DRI pellets, should be included** in Annex I of the Directive to cover greenhouse gas emissions from these sectors as well. The hard coal, iron ore and other non-ferrous metal ore mining sectors are counted as energy-intensive industries under Art. 10 b, (COMMISSION DELEGATED DECISION (EU) 2019/708 of 15/02/2019) without being subject to the EU ETS. This shows that the Commission has recognized these sectors as emitters of GHG emissions. Then they should also be covered by the EU ETS.
2. **The free allocation of emission allowances should be phased out as soon as possible.** Amendments 676 (Recital 30) and 678 (Article 10a (1a (2))) proposed by the Parliament

¹ Under Comext code 7203: "Ferrous products obtained by direct reduction of iron ore and other spongy ferrous products, in lumps, pellets or similar forms; iron having a minimum purity by weight of 99,94%, in lumps, pellets or similar forms"

gradually remove free allocation for CBAM sectors by 2032. That date is already too late, and should by no means be postponed, as suggested by the Commission and Council.

3. For products covered by the CBAM, **all corresponding upstream products ('precursors') falling under the ETS should also be covered by the CBAM** systematically. For the case of steel, this includes, but is not limited to, sinter, coke, ferro-alloys and hydrogen.
4. **Reject the European Council's Amendment 12(c(ii))** of Article 10a, exempting hot metal from the benchmarks' reduction rate update.
5. While free allocation is still in place, **equivalent incentives should be set up to reward demand-reduction measures for primary steel**, for example through the substitution of iron and alloying elements by steel scrap to internalize the well-documented climate benefits of using recycled materials instead of extracted ones².

We hope that you will take these points into consideration during your discussions at the trilogue and we remain at your disposal to further information or questions.

Yours sincerely,

Signatories



About EuRIC

The European Recycling Industries' Confederation (EuRIC) represents the recycling industry at a European level. Gathering the vast majority of national recycling federations from EU/EEA Member States, the Confederation represents about 5.500+ recycling companies – from market leaders to SMEs – generating an aggregated annual turnover of about 95 billion € by treating various waste streams such as household or industrial & commercial waste including ferrous and non-ferrous metals, end-of-life vehicles (ELVs), electronic waste (WEEE), packaging (paper and plastics), end-of-life tyres or textiles.

About Sandbag

Sandbag is a non-profit climate change think tank which uses data analysis to build evidence-based climate policy. We focus on EU policies such as the EU Emissions Trading Scheme and climate governance, and emissions reductions in industrial sectors.

We believe in Europe's ability to lead climate action, by example and using its large market and technological momentum as an incentive for others to follow. But we're also aware of the risk that Europe's might fail to deliver on its own pledges, which is why we want to get EU policy right.

² Compared to primary raw materials, the use of steel scrap in steel production processes saves 58% of CO₂ and saves 72% of energy, see [EuRIC \(2019\) Metal Recycling Factsheet](#); also read Sandbag's report on [the key role of circular steel in achieving climate goals](#).