



Legal Considerations Surrounding the Introduction of an Emissions Performance Standard at EU Level

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INTRODUCTION

This paper is produced by ClientEarth, in conjunction with WWF European Policy Office, in order to consider the appropriate legal framework for the introduction of an Emissions Performance Standard (EPS) into EU law. An EPS sets a maximum of carbon dioxide (CO₂) emissions, or CO₂ equivalent, per unit of output from energy generating power plants. The paper considers what components are essential to an EPS and how those components would interact with existing EU law, especially the potential inclusion of an EPS into the following three existing legislative instruments:

- the Greenhouse Gas Emissions Allowance Trading Scheme (ETS) Directive¹
- the Carbon Capture and Storage (CCS) Directive² and
- the Industrial Emissions Directive (IED)³

This paper is divided into three sections. The first will set out the competence of the EU to enact an EPS, the second will discuss the essential legal components of an EU EPS and the third section will conclude with an analysis of the possibility of including an EPS into the three listed Directives.

¹ Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC, as amended

² Directive 2009/31/EC of the European Parliament and of the Council of 23 April 2009 on the geological storage of carbon dioxide and amending Council Directive 85/337/EEC, European Parliament and Council Directives 2000/60/EC, 2001/80/EC, 2004/35/EC, 2006/12/EC, 2008/1/EC and Regulation (EC) No 1013/2006

³ Directive of the European Parliament and of the Council 2010/75/EU of November 24, 2010 on the industrial emissions (integrated pollution prevention and control) (transformed version) Official Journal of the EU L 334 of December 17, 2010 p. 17-119

1. COMPETENCE OF THE EU TO SET AN EPS

This section considers whether the EU has the power to enact an EPS. EU law is based on the premise that the EU can only act where the Member States have given the EU the right to act under the principle of 'conferral'. Where rights to act have not been given to the EU by inclusion in the EU Treaties, those competences remain with the Member States.⁴ Whenever the EU is to enact a new policy, the question of whether it has the competence to do so must be considered. The section below will consider whether the EU has the competence to enact an EPS, whether such an action would be compatible with the principles of proportionality and subsidiarity, what legal basis could be used for such a measure, what legal form such a measure should take and finally what powers the European Parliament has to encourage the development of an EPS.

1.1 Competence of the EU

The Treaty on the Functioning of the European Union (the “TFEU”) defines the competences of the EU. The Treaties delineate the competences of the EU thematically. An EU measure enacting an EPS would best fall under either the environment or energy competences. EU competences may be exclusive, shared or supporting, however, both environment and energy are areas of shared competence, which means that legislation and policy are formulated jointly by the EU and the Member States. Article 2 of the TFEU defines shared competence:

“The Member States shall exercise their competence to the extent that the Union has not exercised its competence. The Member States shall again exercise their competence to the extent that the Union has decided to cease exercising its competence.”

This means that while legislation and policy in areas of shared competence are formulated jointly by the EU and the Member States, Member States can only legislate or act only where the EU has not exercised its powers or has decided to stop exercising them. The EU has already exercised its powers to regulate greenhouse gas (GHG) emissions from power plants (i.e. through the ETS) and therefore the EU has competence in this area.

Although Member States only have residual competence left in areas of shared competence, Protocol 25 to the Lisbon Treaty on the exercise of shared competence, further explains that *“when the Union has taken action in a certain area, the scope of this exercise of competence only covers those elements governed by the Union act in question and therefore does not cover the whole area.”* This essentially means that just because the Union has legislated on a particular issue within a broader field, not all elements of the

⁴ See Seyad, SM (2012). “A Critical evaluation of the revised and enlarged European stability and growth pact,” *Journal of International Banking Law and Regulation*, Vol 27(5), pp 202-211 at p 210; and Armstrong, K (2013). “The new governance of EU fiscal discipline,” *European Law Review*, Vol 38(5), pp 601-617 at p 613.

broader field are automatically also subject to Union competence in areas of shared competence. In this sense, only areas where there is an express provision for the EU to act, or where the EU has achieved complete harmonisation provide the EU with exclusive competence.⁵

In the current case, GHG reduction commitments for power plants have been undertaken at EU level pursuant to climate change objectives (in Article 191(1) TFEU) and so reduction of GHGs from EU power plants is a field where it can be considered that the EU has competence to enact an EPS while also leaving residual competence to the Member States to enact an EPS nationally, as the UK has done. In conclusion, there is no legal doubt that the EU has competence to adopt an EPS.

1.2 Subsidiarity

The EU may only act where action of individual Member States will prove insufficient:

*"Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level."*⁶

The Treaty of Amsterdam provided some guidelines on when the Community can take action without breaching the subsidiarity principle:

"(a) The issue under consideration has transnational aspects which cannot be satisfactorily regulated by action by Member States.

(b) Action by Member States alone or lack of Community action would conflict with the requirements of the Treaty (such as the need to correct distortion of competition or avoid disguised restrictions on trade, or strengthen economic and social cohesion) or would otherwise seriously damage Member States' interests.

*(c) Action at community level would produce clear benefits by reason of its scale or effects compared with action at the level of the Member States."*⁷

All three of these guidelines are relevant to any measure enacted at EU level. Most importantly, as energy policy is an important area of the internal market it is clear that without coordinated EU action, there could be distortions of competition. While Member States enacting a national EPS can achieve a certain amount of emissions reductions, an EPS at EU level would provide the scale for such efforts that would be more in line with what is necessary to

⁵ See Case C-266/03 Commission v Luxembourg [2006] ECR I-4805 at paras 40 – 45, particularly para 45, and also paras 49 -52

⁶ TEU Article 5(3)

⁷ Treaty establishing the European Community (consolidated version) - Protocols annexed to the Treaty establishing the European Community - Protocol (No 30) on the application of the principles of subsidiarity and proportionality (1997), OJ C 321 E, 29/12/2006, P. 308 at para 5 and current Protocol 2 to the TFEU

combat climate change. In addition, as the number of allowances under the ETS is fixed, a reduction in the use of those allowances in one country will simply shift the use of those allowances to another country under the overall cap and/or reduce the price of the allowances. Thus the enactment of an EPS at community level rather than national level would provide clear benefits and thereby not fall foul of the EU subsidiarity principle.

1.3 Proportionality

Article 5(4) of the Treaty on the European Union (the “TEU”) lays down the principle of proportionality: *“the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties.”* This raises the question of whether an EPS at EU level is necessary to achieve the objectives of the Treaties. Considering the objectives of the Treaties include the protection of the environment, the promotion of energy efficiency and energy saving, and the development of new and renewable forms of energy this should not be difficult to prove.

In addition to the specific Treaty articles on the environment and energy, the EU Treaties contain a number of other references to the protection of the environment, for example, Article 3(3) TEU calls on the EU to promote “a high level of protection and improvement of the quality of the environment” and Article 11 TFEU directs that environmental protection requirements *“must be integrated into the definition and implementation of the Union’s policies and activities, in particular with a view to promoting sustainable development.”*

In assessing proportionality, the Court of Justice of the European Union (CJEU) will test whether a measure is “manifestly inappropriate having regard to the objective which the competent institution is seeking to pursue.”⁸ Thus the proportionality of any measure will be judged by the content therein, however as long as the EU EPS is designed so that it is not unnecessarily intrusive upon the Member States, this should not pose a real challenge to the measure as it would be manifestly in line with the objectives of the Treaties listed above.

1.4 Legal Basis

Under EU law, any legislative act should be expressly based on an article of the Treaties giving the EU competence. The choice article of the Treaties will specify which legislative procedure will then be used for adoption.

The legal basis is defined according to the purpose of the measure. The CJEU has stated in several rulings⁹ that the choice of legal basis for an EU measure has to be based on objective criteria, in particular the stated objective and the content of the measure. The EU has competence to enact a legislative measure regulating GHG emissions from power plants based on Article 192(1) TFEU as

⁸ Case C-331/88 R v Minister of Agriculture, Fisheries and Food, ex parte Fedesa [1990] ECR I-4023

⁹ Commission v Council (C-300/89): (1991) E.C.R. I-2867; Commission v Council (C-155/91): (1993) E.C.R. I-939; European Parliament v Council (C-187/93): (1994) E.C.R. I-2857; European Parliament v Council (C-164 & 165/97): (1999) E.C.R. I-1139

it can be considered a measure on environmental policy or under Article 194(a) TFEU as an energy policy measure.

According to the TFEU, EU measures on environment or energy policies can be adopted by 'the ordinary legislative procedure' involving jointly the European Parliament and the Council acting by qualified majority; however the 'special legislative procedure' with unanimity voting in the Council would be required for the adoption of measures primarily of fiscal nature or measures that affect the national energy mix of the Member States.¹⁰ The question of what measures are deemed to 'affect' the national energy mix has not been delineated, however, it can be argued that an EU EPS would not as of necessity affect a Member State's energy mix as long as the EPS was technology neutral i.e. that it set a level of CO₂ intensity that would apply to all energy producing plants and not mandate any particular technology, such as CCS, to comply. Where an EPS mandates specific technologies it would be difficult to argue that a Member State's energy mix was not affected and thus the unanimity voting procedure would almost certainly have to be used if the measure wanted to avoid legal challenge from a Member State.

Either of these articles would provide a specific legal base for EU action to enact an EPS. A specific legal base precludes the possibility of using a more general legal base.¹¹ Between them, Article 192(1) TFEU is to be preferred. Though any measure to reduce GHG emissions from power plants is an energy measure, it would be regulating those power plants due to their environmental impact rather than their inherent quality as energy sources. This is important as the CJEU has held in the past that the legal basis for a legislative act, "must rest on objective factors amenable to judicial review, which include in particular the aim and the content of the measure."¹² The CJEU has stated that, "if the examination of a Community measure reveals that it pursues a twofold purpose or that it has a twofold component and if one of these is identifiable as the main or predominant purpose or component whereas the other is merely incidental, the act must be based on a single legal basis, namely that required by the main or predominant purpose or component."¹³ This clearly indicates that as the EU would be regulating based on environmental concerns, Article 192(1) TFEU should be the legal base. It is also important to note that the legal base for the ETS and CCS Directives is the old Article 175(1) TEC, which corresponds to current Article 192(1) TFEU and the IED has its legal base in the current environment chapter of the Treaties (192) as well.

¹⁰ For a detailed discussion of the divisions between the environment and energy competences and the required voting procedures under each see, ClientEarth, Legal Framework Governing EU Law & Policy Making for 2030 Climate & Energy Process, available at: <http://www.clientearth.org/climate-energy/climate-energy-publications/legal-framework-governing-eu-law-a-policy-making-for-2030-climate-a-energy-process-2648>

¹¹ Case 45/86 Commission v Council [1987] ECR 1493 at para 13

¹² Case C-211/01 Commission v Council [2003] ECR I-0000 at para 38

¹³ Case C-155/91 Commission v Council [1993] ECR I-030 at para 19 and 21; Case C-36/98 Spain v Council [2001] ECR I-779 at para 59

1.5 European Parliament Competence

There are various types of own initiative reports the Parliament can draw up, including a legislative own-initiative report wherein the Parliament can request the Commission to issue a legislative proposal. Article 225 TFEU allows the European Parliament to request the Commission to submit any appropriate proposal on matters on which it considers that legislation is required.¹⁴ Such a request requires the signature of a majority of the MEPs to be valid. However, such a request from the Parliament does not bind the Commission to issue a proposal, rather the Commission must consider the request and give the Parliament reasons if it decides not to issue the relevant proposal. Where the Commission considers the request of the Parliament but fails to give adequate reasons for not bringing forward the relevant legislative proposal, the Parliament could potentially issue a motion of censure via Article 234 TFEU, however this can be seen as an extreme measure and unlikely to be utilised in practice without total disregard of the Parliament's request by the Commission.

In summary, a request from the Parliament to the Commission to issue a proposal for an EPS at EU level would certainly be of important normative force as a political instrument but the Commission must only consider such a request and can decline it.

1.6 Legislative Form

The best option to facilitate good design and long term certainty for an EPS is to enact the EPS via the legislative vehicle of a Directive, with further shaping of the design of the EPS in comitology¹⁵ as necessary. A Directive is a legislative instrument which the Member States must enact into their national legislation. This means that each Member State can adapt as necessary e.g. set appropriate agencies for the oversight of the EPS rules - which could be those that are already in use for the oversight of the ETS, as the UK has done. However, this does not leave the Member States with free rein; each Member State must meet certain standards for the implementation of the Directive in its national territory, and by a certain date.

In addition, Directives are intended to be minimum harmonisation measures only, i.e. Member States have the possibility to enact further or more stringent measures in addition to the legislation in the Directive. This is especially so with regard to the environment measures where the right of Member States of "maintaining or introducing more stringent protective measures" for the environment is explicitly retained in Article 193 TFEU. However, it must be noted that there are certain conditions attached to enacting policies under Article 193:

¹⁴ The Treaty article has been elaborated by the Decision of the Conference of Presidents of 12 December 2002, available at: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+RULES-EP+20130701+ANN-18+DOC+XML+V0//EN&language=EN&navigationBar=YES#def1>

¹⁵ Comitology is the process whereby the Commission is delegated executive competences in order to give effect to EU legislation. This practice implies that a committee is set up to scrutinize the implementing proposals made by the Commission. The committee is composed of representatives of Member States and represents the authority of the Council and the Parliament. After hearing the Commission, the committee is to adopt a formal opinion before the Commission proceeds.

1. The additional measures must actually result in a level of protection of the environment that is higher than the one pursued by the EU measure
2. It must fall within the field of application of the EU measure by following the same objectives
3. It must not frustrate the secondary objectives of the EU measure
4. Where such an additional measure would affect other EU provisions, it must not violate the principle of proportionality
5. And it must be notified to the European Commission¹⁶

Once these conditions are met, any Member State can introduce measures that go beyond those in any EU EPS Directive to ensure better environmental protection.

¹⁶ For further detail on these conditions see Chapter 2 of Peeters, Stallworthy and Cendra de Larragán, *Climate Law in EU Member States* (Edward Elgar, 2012)

2 THE LEGAL COMPONENTS OF AN EU EPS

This section looks at the legal components that would be required to enact an EU EPS via an examination of the main characteristics of EPS that exist in the USA, Canada and the UK.

2.1 The USA

The U.S. Environmental Protection Agency (EPA) will issue new GHG rules for new, modified and existing power plants in summer 2015.¹⁷ These rules require new electric utility generating units to comply with the following emission limits: (1) new coal-fired units would be limited to 1,100 pounds of CO₂ per megawatt-hour of electricity generated (1,100 lbs/MwH or 499g CO₂/kWh); and (2) new gas-fired units would be limited to either 1,000 lbs/MwH (454g CO₂/kWh); or 1,100 lbs/MwH (499 g CO₂/kWh), depending on their size.

Prior to the announcement of a federal level EPS, many States had enacted their own EPS rules. The most important ones being in California, Washington, Oregon and New York.¹⁸ The rules of the State level EPS are very similar and mainly inspired by the EPS applied in California since 2007.

The limiting standard for most of these rules is an emission rate of 1,100 lbs CO₂/MWh (499 g CO₂/kWh),¹⁹ the same as the proposed federal EPS and the same as the emission rate of a combined-cycle gas turbine (CCGT) power plant. The limits are triggered by the creation of new power generation plants, significant upgrades of a pre-existing plant, or new purchase contracts. It is noteworthy that the EPS runs in parallel with cap-and-trade schemes in California and New York.²⁰

The role of an EU EPS would be to ease the phasing away from high-carbon power production across the Union. In this respect, the initial EPS legislation could firstly apply the EPS to new power plants. The staged introduction of the EPS for existing power plants could then follow, with those plants either retrofitting CCS or via the controlled closure and/or replacement of capacity. However, it is also possible to enact an EPS that applies to all plants immediately without the need for a phased process. In this respect it should be noted that the Californian EPS had such an application, resulting in the immediate closure of the most polluting plants without adverse effect on the State's power supply.²¹

¹⁷ See Section 111(b) of the U.S. Clean Air Act

¹⁸ There are also EPS rules in the States of Montana, New Mexico and Illinois, however this paper will not analyse these EPSs as they are less influential and not technology neutral.

¹⁹ Approximately 500 gCO₂/kWh

²⁰ Simpson (August 2010) for the Regulatory Assistance Project, Emissions Performance Standards In Selected States, available at: RAP_ResearchBrief_Simpson_EPS_Updated_2010_08_12(2).pdf

²¹ Cowart R, (November 2014) for the Regulatory Assistance Project, Emission Performance Standards: Global Practice and Options for Europe (Presentation given to the European Parliament), available at: www.raonline.org/document/download/id/7433

The majority of the US EPS rules incentivise the use of CCS technology by allowing operators to use the technology as a means of meeting the CO₂ standard (the exception is Oregon where the use of CCS technology will not be taken into account²²).

Though the state-wide measures are operated by the individual States, they are federally managed and thus come under the 'anti-leakage' rule of the Clean Air Act. This means that States with an EPS cannot purchase power from other States with a CO₂ intensity higher than the level set in the EPS. This has implications for the EU. The UK has a national level EPS but at the same time has electricity interconnections with other European countries. In order for the UK EPS level not to be violated, the UK should implement such an anti-leakage rule itself, however, such a rule at EU level would raise questions of compatibility with EU internal market rules. A basic principle of EU law is that once goods or services are part of the internal market those goods or services should be able to move freely and without restriction between Member States. The UK has no jurisdiction to impose its EPS on other Member States and so the only possibility to ensure that energy entering onto the UK market was produced to the same emissions standard as the UK EPS, would be to create a rule that would selectively allow such energy into its territory depending on its environmental integrity (or impose a penalty where that energy was not of the correct standard). One of the fundamental freedoms of EU law is that goods and services should be able to move freely within the internal market. If the UK were to impose a restriction on energy entering its market, it could be seen as having the equivalent effect to a customs duty and violate EU law. There are exceptions to this general rule which allow such restrictions on the freedom of the internal market, including on the basis of protecting the environment, however it is impossible to say whether such an exception would be granted without seeing the exact regulation. However, it is to be noted that the CJEU is notoriously strict in its interpretation of the internal market rules. This adds to the reasoning as to why an EU level EPS would be preferable to national level EPS.

2.2 Canada

In Canada, coal-fired generation of power is subject to the *Reduction of Carbon Dioxide Emissions from Coal-fired Generation of Electricity Regulations*²³ (the Canadian Regulations), which established an EPS on the first of January, 2015. The EPS does not apply to gas-fired plants. The Canadian Regulations provide for an 'emission limit' of 420 tonnes of CO₂ per gigawatt hour (420g CO₂/kWh) of electricity produced for new coal-fired electricity generation units (plants that start producing electricity on or after July 1, 2015). The Canadian regulations also apply to 'old' plants, which are those units that have reached the end of their useful life - essentially when a unit has reached 50 years of operation. These plants must also comply with the EPS if they want to keep operating. The importance of applying the EPS to old plants can be seen through the fitting of the first commercial scale CCS project to the Boundary Dam plant which was stated by the owners to be

²² Oregon Senate Bill 101

²³ P.C. 2012-1060 August 30, 2012, available at: <http://www.gazette.gc.ca/rp-pr/p2/2012/2012-09-12/html/sor-dors167-eng.html>

explicitly to ensure the plant is able to continue to operate after the implementation of the Canadian Regulations.²⁴

The limit set in the Canadian Regulations was been chosen as it was considered roughly equivalent to the emissions rate of a combined-cycle gas turbine (CCGT) electricity generation plant.²⁵ This is a different level to that in the US, though both levels are set on the basis of CCGT equivalent emissions. A technical assessment of how the two countries came to levels for their EPS is beyond the scope of this paper, however it should be noted that setting the level of the EPS is a technical exercise. It is possible that EU policy makers would want to consider the signals sent by an EPS to investors, including a clear signal on CCGT investment when setting the level of the EPS. However, as the setting of the level of the EPS is a technical exercise there are essentially no legal constraints - the level could be set so high as to allow business as usual or set at a steeply declining trajectory so that power generation becomes less CO₂ intensive quite quickly over time. The legal basis for an EPS trajectory would be its grounding in the Treaties (e.g. the environment or energy chapters as discussed in the previous section), thereby allowing any trajectory to be designed, no matter how steep, as long as that trajectory could be justified on environmental or energy grounds. Similarly, the question of the scope covered by an EPS is a political rather than legal one. Whether a new legal instrument is proposed or an existing instrument is amended to introduce an EPS into EU law, the question needs to be addressed as to which installations the new instrument should apply. This is a question of whether only new plants would be included or whether existing plants would be included, as well and the scale of the plants to cover - only the largest plants or all but the smallest plants? This is essentially a technical question that will be decided in the political arena.

The Canadian Regulations also incentivise the use of CCS technology by granting an exemption from the EPS until 31 December 2024 to plants that have regulatory approvals for the capture element of a CCS system by 1 January 2022. In addition, the Canadian Regulations allow exemptions from the EPS in exceptional circumstances when the electricity supply is or might be disrupted (e.g. a lack of capacity).

2.3 The UK

The UK Energy Act 2013²⁶ established a national EPS. Section 57 sets a 'limit duty' on the amount of carbon dioxide new coal and gas plants may emit each year until 2044. There is a 450g/kWh 'emission limit' for generators larger than 50MW, but calculated as an annual limit, based on plants either running as a 'baseload' or for 85% of the year.²⁷ This permits higher-emitting plants to continue to run, but for fewer hours. Though the Act generally applies only to new build power plants, schedule 4 to the Act sets out other circumstances

²⁴ See details of the CCS project here: <http://saskpowerccs.com/ccs-projects/boundary-dam-carbon-capture-project/>

²⁵ Regulating Carbon in Canada: The impact of the federal government's proposed electricity coal performance standards, the International Institute for Sustainable Development, available at: http://www.iisd.org/pdf/2012/regulating_carbon_canada_electricity.pdf

²⁶ UK Energy Act 2013: <http://www.legislation.gov.uk/ukpga/2013/32/contents/enacted/data.htm>

²⁷ Cowart R, (November 2014) for the Regulatory Assistance Project, Emission Performance Standards: Global Practice and Options for Europe (Presentation given to the European Parliament), available at: www.raonline.org/document/download/id/7433

under which an EPS limit may be triggered, e.g. where plants are retrofitted or improved so that their life is extended. Similar to the Canadian example above, the UK Secretary of State has the power to suspend or modify the EPS in exceptional circumstances to ensure security of supply. However, there is currently overcapacity existing at EU level²⁸ and as such the use of such exemptions should be strictly limited and only used where absolutely necessary for the functioning of the EU energy market to ensure legal certainty in the operation of the EU EPS for installations and investors.

The UK EPS incentivises the utilisation of CCS technology by exempting fossil fuel generation plants equipped with CCS projects for three years from the date the CCS technology is operational, or 31 December 2027, whichever is the earlier. In addition it is important to note, as with the Californian EPS, the UK EPS illustrates that an EPS and emissions trading system can operate to complement each other. The UK EPS makes provision for the Secretary of State to promulgate additional regulations by reference to emissions under the ETS (section 57(7)(g))²⁹ to ensure compatibility between the implementation of the ETS Directive in the UK and the national EPS. It is not specified exactly what can be covered by these regulations but it may be supposed that it would generally be used to ensure the smooth functioning of the two measures e.g. the use of the same reporting and sanctioning arrangements. The legal compatibility between an EPS and carbon trading systems does not exclude the possibility of environmental or economic compatibility issues that would need to be addressed (discussed further in section 3.1).

²⁸ There has been a recent decline in demand for electricity, attributed to overcapacity and the rise in the amount of renewable energy. This has resulted in legacy utilities earnings falling. See, Greenpeace, 7 Charts Explaining Why Europe's Top Utilities Have Underinvested In Renewables, available at: <http://www.greenpeace.org.uk/newsdesk/energy/data/7-charts-explaining-why-europe%E2%80%99s-top-utilities-have-underinvested-renewables>; IDDRI, Getting out of the perfect storm: towards coherence between electricity market policies and EU climate and energy goals, September 2014, available at: http://www.iddri.org/Publications/Collections/Idées-pour-le-debat/WP1214_AR%20et%20a_EU%20electricity%20market.pdf, and Reuters, Downturn in Europe's energy markets sharpest since 2008 crisis, available at: <http://www.reuters.com/article/2014/06/06/energy-europe-power-gas-coal-idUSL6N0ON2DB20140606> See also Trilemma UK, Assessing the balance of risks associated with coal plant closure, available at: http://www.e3g.org/docs/Assessing_the_balance_of_risks_associated_with_coal_plant_closure.pdf which specifically looks at UK capacity in the event an EPS forces a closure of coal plants there in 2023.

²⁹ Section 57(7) states that "Regulations under subsection (6)(a) may, in particular, make provision— ... (g) specifying any category of emissions by reference to provision made, or that may from time to time be made, by or under regulations implementing the ETS Directive." And section 57(6)(a) states: " The Secretary of State may by regulations— ... (a) make provision about the interpretation of the duty imposed by subsection (1) ("the emissions limit duty")"

3 ANALYSIS OF THE INCLUSION OF AN EPS INTO EXISTING DIRECTIVES

This chapter introduces the ETS Directive, the IED, and the CCS Directive in consideration of whether the inclusion of an EPS therein would be appropriate considering the main purpose and provisions of the mentioned Directives.

3.1 The ETS Directive

The purpose of the ETS Directive is to establish a 'Community scheme' for greenhouse gas emission allowance trading. The objectives of the Directive are:

1. the establishment of a greenhouse gas trading scheme within the EU to reduce such emissions in a “cost-effective and economically efficient manner”³⁰;
2. the reduction of greenhouse gas emissions *to be increased* so as to contribute to levels of reductions that are *considered scientifically necessary* to avoid dangerous climate change [emphasis added]; and
3. going beyond a reduction of 20% greenhouse gases by 2020 where there is an international agreement approved by the EU which requires this.

These three stated aims have been examined by the CJEU in the cases of *Germany v Commission*,³¹ *Arcelor*³² and *Poland v Commission*.³³ It was stated that the protection of the environment by reducing GHGs is the ETS's principal, overarching objective and the non-environmental objectives (cost-effectiveness and economic efficiency) are accordingly sub-objectives. The main purpose of an EPS at EU-level would be to reduce GHGs. It should not pose a problem to design the EPS to be cost-effective and economically efficient as well, thereby meeting the overarching objective and sub-objectives of the ETS as well.

In the case of *Poland v Commission* the purpose of the ETS was elaborated further, "the purpose of the trading scheme was to fix a price for greenhouse gas emissions and leave the operators to choose between paying the price and reducing their emissions."³⁴ Whereas an EPS sets a limit for all power plants which in principle it should not be possible to 'buy' out of. This distinction in rationale between the ETS and the EPS is one that provides a rationale for placing an EU EPS into a new and separate legislative instrument, though it does not necessarily exclude the inclusion of an EPS in the ETS Directive.

³⁰ Article 1 of the ETS Directive

³¹ Case T-374/04 *Germany v Commission* [2007] ECR II-4431

³² Case C-127/07 *Arcelor* [2008] I-09895

³³ Case T-183/07 *Poland v Commission* [2009] ECR II-03395

³⁴ The judgement of 7 March 2013 in the case T-370/11, *Republic of Poland v European Commission*, point 90. *Op. Cit.*

Alternatively, an EPS could be seen as the vehicle by which the energy installations which are allowed to participate in the carbon market are selected (e.g. the most GHG intensive would be removed from the market entirely by virtue of the EPS limit).

There is no legal conflict between an EPS and the operation of the ETS. As outlined above, the simultaneous use of price and non-price measures is utilised in California³⁵ and the UK where an EPS currently exists alongside emissions markets. In addition, the analysis above has demonstrated that the EU has the competency to enact an EPS. It would be important to ensure that both measures are designed to be complimentary (e.g. so that there are no conflicting requirements on reporting or penalties i.e. as has been ensured in the UK EPS) so that no legal conflict of operation would arise. However, that is not to say that there might not be a question as to the effectiveness in economic or environmental terms of an EPS where it operates without adjustment to the ETS cap. The enactment of an EU wide EPS would presumably reduce GHG emissions but unless the ETS cap is reduced by an appropriate amount to take this into account, those GHG emissions will simply shift to a different sector or contribute to the build up of a further oversupply of ETS allowances. This is also an issue to be considered when individual Member States enact national level EPS.

A way to avoid such a scenario would be to have the ETS cap adjusted to remove an equivalent number of allowances to those saved by the EPS (EU or national). This would require amendment of the ETS Directive. This could be a politically difficult process as illustrated by the recent experience of 'backloading'³⁶ ETS allowances. Another scenario would be for willing Member States to retire the equivalent number of ETS allowances themselves. However, this second scenario potentially conflicts with the ETS Directive and could face challenge. Article 10.1 of the ETS Directive states that from 2013 Member States *shall* auction all allowances that are not allocated free of charge to installations. On its face this article grants Member States no discretion to cancel allowances not already allocated to specific installations. It does leave the Member States with the option of purchasing those allowances (which essentially would be cost neutral as the monies received from the purchasing would go back to the Member States themselves, though there would be some transaction costs). The question with this option then arises whether Member States are classes of persons eligible to purchase allowances under the ETS Directive. The persons eligible to apply for permission to bid in allowance auctions is laid down in Regulation No. 1031/2010 (Auctions Regulation). Article 18.1(e) thereof states that public bodies are eligible to participate in ETS auctions but only when they control installations that are covered by the ETS. However, Article 18.5 prohibits persons who are in a position to exercise significant influence over the management of the auction from participating. This leaves Member States as potentially able to direct their public bodies who operate ETS installations to buy excess allowances but they must ensure there is no appearance of

³⁵ While California is obviously not in the EU and has a different legal system, it is still illustrative for the operation of a price and non-price measures simultaneously as it is a common law jurisdiction, operating under a federal system.

³⁶ Decision No 1359/2013/EU of the European Parliament and of the Council of 17 December 2013 amending Directive 2003/87/EC clarifying provisions on the timing of auctions of greenhouse gas allowances

influence on the auction. However, the question of how the 'exercise of significant influence over the management of the auction' would be interpreted could leave such an action open to challenge, as it would be difficult to argue that the government or public body was not in a position of influence over that Member State's own auction.

The sanctions approach in the ETS could provide useful monitoring information and a model for sanctions upon which an EPS could be built. As stated above, the UK has used this option. In September 2014, the UK Department of Energy and Climate Change (DECC) issued new proposals for monitoring compliance with the UK EPS. The proposal is to borrow monitoring arrangements from the transposition of the ETS Directive. It also proposed sanctions that may be applied in the event of a breach of the EPS to be linked to the economic benefit associated with any emissions above the EPS limit.³⁷ The use of the same data processing arrangements as those in the ETS Directive were an EPS to be introduced at EU level would ease the administrative burden for Member States in implementation of the EPS. The inclusion of the EPS in a separate piece of legislation from the ETS does not preclude the use of ETS data in administering the EPS.

The use of the ETS administration for an EPS raises the question of whether the scope of the two would be the same. Ideally if an EPS was to be included in the ETS Directive the energy installations covered by the two Directives would be the same, otherwise duplicative but overlapping administrative measures would have to be established. In addition when considering the different scope of the ETS against an EPS, the inclusion of solely energy installations in the EPS, but the much broader scope of the ETS, raises the question of whether the inclusion would be appropriate. The ETS does not include only the power sector but also heavy industry (e.g. steel and aluminium producers) while an EPS would apply only to energy generating plants. However, it could be argued that as an EPS would reduce the requirement for allowances in the power sector, it would thereby redistribute the price signal impact on the covered sectors (e.g. all covered sectors pay less). Essentially this argument is that it would be economically more efficient to ensure the most polluting fossil fuel power plants are not currently being built so that there will be a lower economy wide carbon price signal in future and thereby benefit all the sectors covered by the ETS, not just the energy sector. Which in turn raises the question of whether a lower price signal would incentivise the necessary reductions of emissions in other sectors of the economy, but the decision is a political and not a legal one.

The European Commission has signalled that it will propose a revision to the ETS Directive in 2015 to implement the 2030 climate and energy framework. The revision could be used as an opportunity to revise the ETS with EPS incorporation in mind (including adjusting the ETS cap to take account of the EPS).

³⁷ DECC (Sept. 2014), Implementing the Emissions Performance Standard: Further Interpretation and Monitoring and Enforcement, UK (Consultation Document), available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/357217/implementing_emissions_performance_standard.pdf

3.2 The CCS Directive

The purpose of the CCS Directive is to establish a legal framework for the development of environmentally safe technologies for the capture, transport and geological storage of carbon dioxide (CO₂). The purpose of environmentally safe geological storage of CO₂ is the permanent containment of this gas in a way that prevents and, where this is not feasible, eliminates as far as possible the negative effects such gas might cause to the environment and human health if it remained in the atmosphere.

Pursuant to Article 4 of the Directive, Member States which intend to allow geological storage of CO₂ in their territory have to undertake an assessment of the storage capacity available in parts or in the whole of their territory, including by allowing exploration. The suitability of a geological formation for use as a storage site should be determined through a characterisation and assessment of the potential storage complex and surrounding area pursuant to the criteria specified in Annex I of this Directive.

One of the goals of enacting an EPS could be to incentivise power plants to equip with CCS technology. However, an EPS should be technology neutral and not *mandate* the use of CCS technology, as otherwise the measure could be claimed to affect the national energy mix of the Member States with consequences for the legislative procedure required for enactment (section 1.4). While CCS is a pollution control technology, not directly forcing Member States to change their national energy mix to use the technology; it can be argued that mandating its use would make the use of certain types of energy more expensive and thus indirectly affect the energy mix. The CJEU has not yet issued a full interpretation of what does or does not affect national energy mix. To avoid this question entirely it would be more appropriate to steer clear of mandating specific technology. For this reason it is not advisable to introduce an EPS into the CCS Directive. Such incorporation could lead to the interpretation that the sole purpose of the EPS is to support the spread of CCS technology.

Linking an EPS to the CCS Directive could also prove problematic as it is still uncertain when CCS will be in widespread use and fully commercially operational. Linking (or creating the idea that the two technologies are linked) could therefore raise questions over whether an EPS trajectory should be drawn up in line with CCS, potentially hindering the implementation of EPS requirements. In addition the purpose and aim of the CCS Directive is to harmonise technical health and safety requirements for the safe storage of CO₂ pursuant to CCS technology, rather than having the reduction of pollution as its main aim, and an EPS would have such an aim at its heart.

The European Commission is in the process of evaluating the impact of the CCS Directive to date. The main report of this evaluation was produced by a consortium of consultants who did not recommend the reopening of the CCS Directive.³⁸ However, they recognised that the "lack of comprehensive climate policies that place a significant market value on avoided emissions is the

³⁸ <http://www.ccs-directive-evaluation.eu/final-report/>

single biggest challenge facing CCS deployment." The report also recognises the potential importance of an EPS to incentivise the use of CCS technology. Indeed, the CCS Directive itself recognises the potential importance of an EPS to incentivise the use of CCS technology in Article 38.3 where it is stated that a review of the CCS Directive shall consider if "it is needed and practicable" to introduce an EPS when CCS projects have been sufficiently demonstrated.

In conclusion the introduction of an EPS into the CCS Directive would not be optimal for the enactment of a technology neutral EPS. Rather the link between an EPS and the use of CCS technology should be one of incentive but with the instruments separated in different legislative measures.

3.3 The IED

The IED is a legal act integrating and modifying seven other directives, in particular Directive 2008/1/EC (concerning integrated pollution prevention and control)³⁹ and Directive 2001/80/EC (on the limitation of emissions of certain pollutants into the air from large combustion plants).⁴⁰

The IED applies an integrated pollution prevention and control framework for industrial activities in the EU. The objectives of this Directive are stated in article 2 and 44 and include ensuring a high level of environmental protection and the improvement of environmental quality by the prevention of pollution from industrial activities and, as far as possible the reduction of such pollution in line with the principles of 'polluter pays' and of pollution prevention.

The IED significantly tightens the emission standards that existed for SO₂, NO_x and dust emissions and introduces an obligation of ongoing measurement of the concentration of such pollution for power sources greater than 50MW and an obligation to measure the total emissions of mercury in coal-fuelled sources. Industrial installations encompassed by the scope of the IED have to comply with very strict environmental protection standards; the Member States have to ensure that such installations do not cause any significant pollution and the best available techniques (BATs) are applied.

Emissions of greenhouse gases covered by the ETS Directive are in principle excluded from the scope of conditions determined in the permit granted under the IED (Article 9.1). The IED regulates gases on the basis of their effect on air quality rather than their climatic effects. However, some of these gases have climatic effects (e.g. SO_x and NO_x) and so the reduction of these gases to improve air quality also has a significant indirect climatic effect. The inclusion of a limit for CO₂ in the IED would thus amplify the effects the Directive already has on EU GHG emissions.

Of the Directives consider in this paper, the IED is the Directive with the closest purpose to that of an EPS. To prevent pollution which results from industrial activities and, as far as possible, to reduce such pollution in line

³⁹ Directive of the European Parliament and of the Council 2008/1/EC of January 15, 2008 concerning integrated pollution prevention and control, Official Journal L 24 of 29.1.2008, p. 8-29

⁴⁰ Directive of the European Parliament and of the Council 2001/80/EC of October 23, 2001 on the limitation of emissions of certain pollutants into the air from large combustion plants Official Journal L 309 of 27.11.2001, p. 1

with the principles of 'polluter pays' and of pollution prevention, would be a goal for an EU EPS though with a focus on GHGs rather than air pollutants. Specifically, the IED presents the operators of power installations with four options for the achievements of the Directive's requirements. The first option given by the Directive is the adjustment of emissions from such sources to permissible emission limit values by January 1, 2016⁴¹ (second paragraph of Article 30.2). This could provide a legitimate building block for an amendment introducing an EU EPS in the IED.

The IED is a 'recast'⁴² Directive, i.e. the merging of several pre-existing Directives into one. During the recast, amendments proposing the inclusion of an EPS for CO₂ at EU level were debated. There was a question at that time about whether the inclusion of an EPS for CO₂ might violate the recast rules, however, ClientEarth took the opportunity to clarify at that time that the incorporation in the IED of provisions setting up an EU EPS was neither inconsistent with EU policy nor did it violate the recasting rule.⁴³

As stated, Article 9 of the IED states that the permit issued to a power plant under the IED shall not include a limit on GHGs, where that power plant is included in the ETS:

"Where emissions of a greenhouse gas from an installation are specified in Annex I to Directive 2003/87/EC [the ETS Directive] in relation to an activity carried out in that installation, the permit shall not include an emission limit value for direct emissions of that gas, unless necessary to ensure that no significant local pollution is caused."

It is unlikely that an EU EPS would be enforced through the use of the permit system enacted by the IED as this is prohibited in Article 9. It could be argued though that this article should have a wider meaning i.e. that there should be no regulation of GHGs from any installation covered by the IED. However this would require a stretch of legal interpretation as the article is plain on its face that what it is prohibiting is the *use of the permit for GHG regulation* rather than GHG regulation *per se*.

This is further reinforced by the preamble (Recital 10) to the Directive. This clarifies the meaning of this Article by stating that this provision is to avoid regulatory duplication, however, it also specifically acknowledges Article 193 TFEU which restates the competence of the Member States to maintain or introduce more stringent policies than those included in EU law:

"In accordance with Article 193 of the Treaty on the Functioning of the European Union (TFEU), this Directive does not prevent Member States from maintaining or introducing more stringent protective measures, for example greenhouse gas emission requirements, provided that such

⁴¹ However for an EPS the date would have to be later in order to accommodate sufficient time for the legislative process to run its course

⁴² Website of the European Commission, definition of the term recasting, available at: http://ec.europa.eu/dgs/legal_service/recasting_en.htm.

⁴³ <http://www.clientearth.org/related-links/related-links/amendments-to-introduce-a-co2-emissions-limit-value-in-the-ied-ipcc-directive-related-link-113>

measures are compatible with the Treaties and the Commission has been notified."

A practical use of this Treaty Article can be seen in the implementation of an EPS by the UK. Thus the clarification in the preamble to the IED and the introduction of a national EPS by the UK without creating an EU law conflict confirms that Article 9 of the IED is not a barrier to the implementation of an EPS at national level. Article 9 has no effect upon EU competence as that stems from the EU Treaties and cannot be altered in a Directive

Thus Article 9 can be interpreted as a provision simply governing the use of the IED permit system. Were an EPS to use the IED permit system for administration purposes, Article 9 would need to be amended. This should not pose a problem; if the intention is to amend the IED to include an EPS, Article 9 would just be one in a series of amendments to ensure appropriate implementation of the EPS into the IED. Thus, Article 9 is not a significant barrier to the inclusion of an EPS in the IED.

The main reason to exclude an EPS from the IED is the more general point that CO₂ from power plants is already regulated by the ETS Directive. Including the EPS into the IED would thus spread the regulation of CO₂ from power plants across two Directives. As discussed above (section 3.1), an EPS can be included in the ETS Directive but as the main purpose of the ETS is to put a price on carbon, whereas in principle it should not be possible to 'buy' out of the EPS, it is better to have the two measures in separate legal instruments. However, in general, spreading regulations of the same aim across multiple legal instruments is to be avoided, preventing regulatory confusion and the EU aims to consolidate and recast legislation where possible to avoid this (e.g. the IED is a recast Directive itself).⁴⁴ The question of the size of the power plants which should be subject to an EPS is in major part a political and economic decision. Nevertheless, aligning the size of the EPS plants with the size of the plants already regulated by the Directive to include the EPS creates a more accessible and transparent regulatory framework. The IED regulates power plants whose thermal output is 50MW or greater, while there is also a proposed regulation for medium power plants regulating plants with output between 1 and 50MW.⁴⁵ The Environment Committee of the European Parliament proposed an EPS for very large plants (those above 300MW).⁴⁶ If an EPS was to be imposed on power plants producing output above 300MW, only some of the power plants in the IED would be subject to the EPS, creating two-tier regulation within the same Directive. This leads to the conclusion that, unless an EPS was to be placed on all plants of the same size as those regulated in the IED, ideally an EPS would be introduced in an entirely new and separate legal instrument. The introduction of an EPS in a separate legal instrument would also ensure maximum flexibility in setting the size of the power plants which would be the subject of the EPS.

⁴⁴ See the EU Legal Service, Helping to improve the quality of drafting of EU legislation, available at: http://ec.europa.eu/dgs/legal_service/legal_reviser_en.htm

⁴⁵ COM(2013) 919 final, available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52013PC0919&from=EN>

⁴⁶ See, the amendments put forward by the ENVI Committee to the European Parliament Plenary here: <http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&mode=XML&reference=A6-2008-414&language=EN>

4 CONCLUSION

This paper has analysed the various legal considerations surrounding enacting an EPS at EU level and has demonstrated that:

- There is no legal doubt that the EU has the competence to enact an EU EPS.
- Nor would the adoption of an EU EPS conflict with the EU principles of subsidiarity or proportionality.
- An appropriate legal basis for the introduction of an EPS could be found in either the energy or environment chapters of the Treaties, however, the environment chapter is to be preferred as an EPS would be primarily an environmental measure.
- The European Parliament has the competence to request the Commission to issue a proposal for an EU EPS, however, this is a political instrument and the Commission will not be bound by such a request.

FOR FURTHER INFORMATION

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About WWF

WWF is one of the world's largest and most respected independent conservation organizations, with over 5 million supporters and a global network active in over 100 countries. WWF's mission is to stop the degradation of the Earth's natural environment and to build a future in which humans live in harmony with nature, by conserving the world's biological diversity, ensuring that the use of renewable natural resources is sustainable, and promoting the reduction of pollution and wasteful consumption.

About ClientEarth

ClientEarth is a non-profit environmental law organisation based in London, Brussels and Warsaw. We are activist lawyers working at the interface of law, science and policy. Using the power of the law, we develop legal strategies and tools to address major environmental issues.

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