

# Institute for Market Economics (IME)

---

## Green Paper "A 2030 framework for climate and energy policies" [COM(2013) 169]

---

### Statement

#### 4.1. General

*- Which lessons from the 2020 framework and the present state of the EU energy system are most important when designing policies for 2030?*

**In general, the 2020 framework:**

- ✎ The 2020 framework fails to see that consumption of energy is beneficial for European citizens.
- ✎ The 2020 framework places too much emphasis on entrepreneurial possibilities and job creation related to efforts to increase energy efficiency.
- ✎ The proposals to use public procurement to promote the adoption of energy efficient products and practices ignore the relatively high cost to the public finances, and the limited benefits of such measures.
- ✎ The idea to use taxation and pricing to encourage behavioural changes ignore the cost of such measures on consumers, especially the less affluent ones.
- ✎ The 2020 framework does not take into the account the high prices of automotive fuel in the EU and the effects it has had on energy efficiency and behavioural changes in the transport sector. Further increases in both may be cost-inefficient and unnecessarily encroaching upon personal liberties.

#### Some examples

##### The 2020 framework overplays the role of energy efficiency

The assumption that increased energy demand can be met by increasing efficiency is not entirely sound. Increasing energy consumption represents the consumer demand driven by an increasing standard of living whereas increased efficiency represents technological change. In order for the “decoupling” to occur, technology must develop at a faster rate than the rate of increase in the standard of living. Therefore if we assume that “efficiency” is used in its primary sense, e.g. using more energy efficient appliances rather than consumers simply foregoing some activities or products, the notion of “decoupling” – as expressed by the Energy 2020 strategy – ignores the technological limitations and constraints.

### **The 2020 puts too much emphasis on effectiveness of government intervention in steering consumer behaviour (including promotion of energy efficiency through public procurement)**

The strategy advocates using public funds to steer changes in both consumer behaviour and the behaviour of producers of products that use energy, e.g. by advocating that public procurement should support energy efficient outcomes. Public funds already suffer from misallocation, improper use, lack of transparency and other problems. It is difficult enough to organize public procurement even with the simplest criterion of the lowest price. If public procurement were to be tied with energy efficiency there is a probability that the allocation of public funds would worsen further.

Products touted as more energy-efficient are usually more expensive<sup>i</sup>; typically the individual buyer weighs the extra initial cost against presumed benefits throughout the lifetime of the product, and makes a decision based on these calculations. If a blanket regulation to make available only goods of certain levels of efficiency is imposed, it risks increasing the initial expenditure without the correspondingly adequate savings. Therefore, if we strive for energy efficiency by imposing standards related to energy efficiency (obviously higher than current practices), this has the potential to increase government spending.

### **Taxation of energy inefficient products and / or subsidies to energy efficient products hurt the poorest the most**

Taxation of less energy efficient products usually harms the less wealthy parts of society, because the poorer tend to use the older and less energy efficient products. In the case of automobiles, an older vehicle fleet generates more emissions than a younger one<sup>ii</sup>. Imposing extra costs may hamper the purchases of expensive energy efficient items and create a problem of affordability, which would then have to be alleviated by providing a need-based subsidy.

Giving tax breaks for energy efficient practices or products also has its defects. In general (as described before), newer products (automobiles, appliances etc.) are more energy efficient (mostly due to simply being newer) and are more expensive. Therefore, giving tax breaks to such products is tantamount to subsidizing the more affluent members of society using taxpayers' money. Moreover, such tax breaks might stimulate purchases of additional products (as opposed to replacing the current ones), thus increasing the demand for energy<sup>iii</sup>.

There is no work-around to this problem. The adjustment of tax in whichever form—tax breaks for efficient products or increased taxation for less efficient products – creates problems and does not guarantee energy savings

## **4.2. Targets**

*- Which targets for 2030 would be most effective in driving the objectives of climate and energy policy? At what level should they apply (EU, Member States, or sectoral), and to what extent should they be legally binding?*

30% renewable resource share and 40% reduction in GHG by 2030 are overly optimistic. The EU should not expect a constant rate of increase in renewable energy and of reduction of the GHG to be kept over a time frame of more than 30 years, rather it should expect a diminishing rate. Targets should not be legally binding. A better option is to have an incentives based system, rather than a penalizing one. Targets should apply to the EU as a whole with each Member State determining its contribution to the overall objective. Targeting a specific sector could have unforeseen effects and consequences.

*- Have there been inconsistencies in the current 2020 targets and if so how can the coherence of potential 2030 targets be better ensured?*

To begin with the approach of 20% decrease in CO<sub>2</sub> emissions, 20% target of share of renewables, and 20% increase in energy efficiency is superfluous. If the goal is to reduce CO<sub>2</sub> emissions, then just one objective would suffice. There is no need to try and to match the goals of climate policy with the goals of energy policy because the two sets of goals are fundamentally incompatible. The goals of climate policy seek to restrict human activity and consumption of energy. The goals of energy policy seek to supply energy for the consumers and to maximize their satisfaction. We should recognize this fundamental mismatch and move from there with either climate or energy policy. Consequently while setting goals for 2030, Europe should decide on one core objective.

*- Are targets for sub-sectors such as transport, agriculture, industry appropriate and, if so, which ones? For example, is a renewables target necessary for transport, given the targets for CO<sub>2</sub> reductions for passenger cars and light commercial vehicles?*

There is no sound reason to have targets for specific sectors. If the overall goal is the reduction of CO<sub>2</sub> emissions, it should not matter what sector accomplishes it. Even more, the goals for certain sectors are harmful because there is a possibility that the sector will be over-achieving the goal in a cost-ineffective manner compared to possible savings in other sectors. Finally there is absolutely no sound justification to have specific (or tougher) targets for certain means of transportation (e.g. personal automobiles). In fact any mentions of especially tougher standards on certain technologies of consumer goods are a clear indication of political, social or technological bias.

*- How can targets reflect better the economic viability and the changing degree of maturity of technologies in the 2030 framework?*

The 2030 framework should get rid of any targets related to the use of certain technology or source of energy. If the reduction of CO<sub>2</sub> emissions is the key objective, there is no need to impose technology-specific or energy source – specific objectives. The emphasis should be put on economic viability, and reaching the goal of reducing CO<sub>2</sub> emissions at lowest cost to consumers. Renewable energy sources should compete among themselves and with conventional sources of energy which meet the goals of CO<sub>2</sub> reduction (e.g. nuclear, fossil fuels combined with CO<sub>2</sub> sequestration and many others).

*- How should progress be assessed for other aspects of EU energy policy, such as security of supply, which may not be captured by the headline targets?*

Security of supply has certain tangible indicators, e.g. number of interruptions of supply, duration of interruptions in supply etc. Measuring security of supply should not be mixed or confused with production of energy inside the country (domestic production), producing energy from indigenous sources, or producing energy from renewable sources.

#### **4.3. Instruments**

*- Are changes necessary to other policy instruments and how they interact with one another, including between the EU and national levels?*

*- How should specific measures at the EU and national level best be defined to optimise cost-efficiency of meeting climate and energy objectives?*

Feed-in tariffs for renewable energy combined with obligations for consumers (or companies) to purchase renewable energy allows producers of renewable energy to profit from the consumers and drive the energy prices higher. With interest of consumer in mind EU should advocate for the schemes where producers of renewable energy are made to compete with each other (e.g. more efficient producers of wind power with less efficient ones, electricity production from photovoltaic with electricity from biomass etc.) So that even if state financial support for renewables remains (even though we would advocate against it), only the most efficient technologies or energy sources are supported.

*- How can fragmentation of the internal energy market best be avoided particularly in relation to the need to encourage and mobilise investment?*

*- Which measures could be envisaged to make further energy savings most cost effectively?*

First, cutting of all subsidies to energy producers. Any subsidies, either for conventional energy or renewable energy forces the price of energy down. Because high market prices are a best driver for consumers to adopt relevant and justified changes in energy use, cutting of subsidies is justified.

Second, cutting or changes of social schemes where, in certain countries poor households receive handouts to cover all or some of their energy bill. If cutting of support schemes altogether seems to drastic, governments should move to support schemes where poor households receive support based on their income and wealth (or lack thereof), not on how much energy they use.

*- How can EU research and innovation policies best support the achievement of the 2030 framework?*

Any form of subsidy, be it for production, R&D, or marketing is harmful to the energy market. Yes, it might drive the costs of renewable energy down, thus helping the achievement of the 2030 goal for renewable resource share, but it also has negative spillover effects and unforeseen consequences, as we have seen in the current planning period.

#### **4.4. Competitiveness and security of supply**

*- Which elements of the framework for climate and energy policies could be strengthened to better promote job creation, growth and competitiveness?*

Promotion of expensive energy sources, and / or taxing cheaper sources of energy for consumers (households and businesses) cannot promote job creation, growth, or competitiveness. Moreover new “green jobs” (e.g. in production of equipment for production of renewable energy) inevitably destroy regular jobs, which are affected by higher energy prices (which in turn are a result of taxation of energy). The only way to promote job creation, growth and competitiveness via energy policy is to halt all taxation on energy. That would have an enormous benefit to consumers, business and competitiveness.

In regards to what would happen to renewable energy, in different countries different renewable energy will become competitive due to advances in technology and / or because of the developments in the market for conventional fuels. For example heat from biomass is

becoming competitive in Northern and Baltic countries because of the price of natural gas (esp. in the Baltics)

*- What evidence is there for carbon leakage under the current framework and can this be quantified? How could this problem be addressed in the 2030 framework?*

Main evidence of that is relocation (or closing and opening) of industrial companies from Europe to USA or other countries where energy prices are lower. Europe has some of the highest prices of energy not mainly because of the developments in the market, but more because of its energy policy (e.g. foregoing coal, which is an abundant resource in Europe).

*- What are the specific drivers in observed trends in energy costs and to what extent can the EU influence them?*

Taxation is a very specific driver. It directly influences the end-price for consumers. EU can easily influence it simply by reducing taxation on energy.

*- How should uncertainty about efforts and the level of commitments that other developed countries and economically important developing nations will make in the on-going international negotiations be taken into account?*

Uncertainty and risk are very important and should not be ignored. Europe would be committing a fatal mistake if it chose to pursue its climate policies unilaterally, disregarding what other industrialized nations do. Therefore if other countries do not commit themselves to costly and binding targets, neither should the EU.

*- How to increase regulatory certainty for business while building in flexibility to adapt to changing circumstances (e.g. progress in international climate negotiations and changes in energy markets)?*

A clear assurance of maximum commitment above which EU would never go could be a start. Given that the EU commitments to reduce CO<sub>2</sub> emissions already exceeds similar commitments made by other industrialized countries EU could announce a moratorium on further initiatives for reduction of CO<sub>2</sub> emissions in Europe. That would give European businesses a much needed breathing space to deal with competitors in other countries or regions.

*- How can the EU increase the innovation capacity of manufacturing industry? Is there a role for the revenues from the auctioning of allowances?*

*- How can the EU best exploit the development of indigenous conventional and unconventional energy sources within the EU to contribute to reduced energy prices and import dependency?*

EU should lift nearly all bans or restrictions on production of energy inside the EU. This should include rolling back legislation that restricts entry of new producers of economically viable energy into the market: renewable energy (e.g. limitations on dams), extraction and use of traditional hydrocarbons, unconventional hydrocarbons (e.g. shale gas) and any other economically viable sources of energy (e.g. nuclear). Lifting entry barriers for new companies in the energy market stimulates competition and naturally drives companies to innovate. This is a far better solution, than tax-payer subsidies.

*- How can the EU best improve security of energy supply internally by ensuring the full and effective functioning of the internal energy market (e.g. through the development necessary interconnections), and externally by diversifying energy supply routes?*

**Internal market.** In terms of internal market one should not forget the harm that various taxes, levies, and state aid have on trade in energy. Therefore EU should aim to eliminate taxes, levies and state aid in the energy sector as much as possible. If EU aims for a common market in energy the least it could do is to make national governments act by the rules of internal market. No special restrictions (implicit or explicit) on trade in energy should be tolerated.

**Infrastructure.** In terms of infrastructure one has to recognize that government regulation plays a large role in hampering investment. Existing legislation can be used to block any investment in the energy sector. Therefore improvement and streamlining of procedures would be a correct step. At the same time, this has to be extended to the entire sector, not just to renewables or projects of European interest. The whole energy sector would benefit from cutting the red tape.

Private capital is capable of financing infrastructure, including cross-border infrastructure if it can be guaranteed regulatory stability. In the cases where private investors express a wish to co-finance, various forms of cooperation between private and public capital should be pursued. At the same time, governments should take notice if private financiers do not want to invest in a given project. This can be an indication that the conditions for investment (e.g. rate of return) are inadequate, or that the whole project is of no commercial viability. This indication should be taken seriously, rather than be seen as a deficiency of private capital or an opportunity for public finance. Transnational dimension should not create the illusion that only public capital or nationally-owned companies are capable of dealing with financing the construction and overseeing the operations interconnections between countries.

Also it should be recognized that recent increases in stress on existing electricity grids comes from the need to accommodate many new intermittent producers of electricity such as wind energy. And it should also be recognized that such stress is a direct result of government subsidies and favourable treatment of renewable energy.

**External suppliers.** EU should foster favourable relations and climate of investment with its external partners. EU should resist any initiatives to limit, curtail or tax energy imports regardless of the reasons such initiatives are raised: "levelling playing field for producers of energy", "improving energy security" or others. As discussed earlier, consumers and businesses need cheap sources of energy, it would be harmful to deprive them of such sources.

#### 4.5. Capacity and distributional aspects

*- How should the new framework ensure an equitable distribution of effort among Member States? What concrete steps can be taken to reflect their different abilities to implement climate and energy measures?*

*- What mechanisms can be envisaged to promote cooperation and a fair effort sharing between Member States whilst seeking the most cost-effective delivery of new climate and energy objectives?*

First, EU should recognize that relatively poorer countries cannot shoulder the same burden of adopting CO<sub>2</sub> reduction and expand expensive renewable energy sources compared to wealthier countries. Second, EU should admit that it is the new-member states who achieved the highest reductions in CO<sub>2</sub> emissions in terms of the Kyoto framework (with 1990 as a base year). Third, EU should recognize that in term of energy per person used, people in new member states use clearly less energy than the average European. Having all this in mind it is fair, that if

EU wants to increase or maintain its obligations for reduction of CO<sub>2</sub> emissions it is the old member-states who should shoulder the burden.

---

<sup>i</sup> *Consumers: Buying Green?* // Euractiv, 2010. <<http://www.euractiv.com/en/food/consumers-buying-green-links dossier-497318>>.

<sup>ii</sup> *Average age of the vehicle fleet*, European Environment Agency, 2005. p. 3.

<sup>iii</sup> *Kosonen, Nicodeme, The Role of Fiscal Instruments in Environmental Policy. Taxation Papers*, 2009, p.12.