7 JUNE 2021

Climate Action Network (CAN) Europe is Europe's leading NGO coalition fighting dangerous climate change. With over 170 member organisations from 38 European countries, representing over 1.500 NGOs and more than 47 million citizens, CAN Europe promotes sustainable climate, energy and development policies throughout Europe.

CAN Europe contribution to State aid SA.53625 (2020/N) Germany

Compensation of RWE and LEAG for lignite phase-out

CAN Europe welcomes the Commission's decision to start a formal investigation into Germany's promised compensations to the lignite operators RWE and LEAG for closing their power plants. We are in the opinion that the amount of compensations and the foreseen date of closures do not reflect reality, and an approval of these unrealistic measures risk setting a bad example for other EU Member States' ongoing coal phase out discussions, potentially resulting in closure dates that are not compatible with the Paris climate agreement and European Green Deal objectives. The decision by the Commission on the German lignite case will send a clear message either in favour of climate protection or in favour of the fossil fuel industry. At the end of 2020, DG Competition kicked off a process to align competition rules with the European Green Deal. We believe that this should concern the whole State aid practice and rules, including case-by-case assesments of aid for coal closure.

Here below are the main points we would like to bring the Commission's attention to when investigating the case. These points are followed by more technical and detailed background with additional comments.

1. **No state aid should incentivise business as usual.**

   No subsidies should be paid to fossil fuel companies for operating; and nothing more than what is minimum required by EU State aid law for closing the plants. The coal industry is making losses faster than expected and any State aid would only compensate for lignite power plant operators' bad business decisions to keep relying on coal.

   A direct impact of the current EU ETS price[1] is that it almost halves the profitability of modern lignite-fired power plants in Germany beyond 2024[2], leading to almost half of the country's lignite fleet losing cash based on current expectations. The proposed revision of the EU Emissions Trading System in response to the EU's new emissions reduction target might lead to a "possible price of €130 per ton of CO2 in 2030[3]" which could be sufficient for the market dynamics to shutter the coal plants.

2. **A coal phase-out by 2030 without further compensation.**

   The phase-out date of 2038 is not in line with the EU's commitments under the Paris Agreement, which require a coal phase-out by 2030. According to the contract with lignite operators, the phase-out can only be accelerated without further compensation under strict conditions and until 2035, otherwise operators have the right to renegotiate the contract. This is a major hurdle for the ambitious policy needed in the face of the global climate crisis, and contradicts with the EU 2030 climate target and 2050 climate neutrality objective.

   A recent decision by the German Constitutional Court supported the need for an earlier coal phase out date by ruling that the country must make deeper emission cuts in the next decade in order not to 'shift the climate burden of making painful reductions to future generations'[4]. This means a 2038 coal phase out date for Germany is too late, as the energy and industry sectors generate the highest amount of CO2 emissions. German legislators are obliged by the Court to revise the Federal Climate Change Act by the end of 2022, in order to make deeper emission cuts which will directly impact plans for coal phase out.

3. **Adherence to the polluter pays principle.**

   The Commission must assess whether Germany has enforced the polluter pays principle before agreeing on any amount of compensation, in particular for the recultivation of lignite mines and recovering water pollution costs (e.g. sulphates pollution). Moreover, the German government must implement the strict levels of the Best Available Techniques Conclusions on Large Combustion Plants, including binding energy efficiency performance. This is reinforced by the Hinkley Point C ruling[5] requiring that the Commission checks compliance of activities with environmental law and principles as a condition for approving State aid.

---

[1] 50 Euros/ton in the week of 4 May 2021

[2] https://www.argusmedia.com/en/news/2195015-modern-german-lignite-plant-margins-halve-from-2024?utm_campaign=Oktopost-free-news-coal&utm_content=Oktopost-twitter&utm_medium=social&utm_source=twitter&utm_term=coal

[3] https://www.sciencedirect.com/science/article/pii/S0306261921003962

[4] https://www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/DE/2021/03/rs20210324_1bvr265618.html;jsessionid=77DB9650A66A447904AC49A056A4A56C.1_cid386

[5] https://www.clientearth.org/latest/press-office/press/ngos-win-right-to-take-eu-commission-to-court-over-environment-harming-subsidies/

4. **Meaningful allocation of money and just transition.**

   Financial resources must be allocated to more sustainable uses that are meaningful in the European Green Deal framework – this includes ensuring that the affected communities in coal regions are supported for a just transition to low-carbon local economies. Germany could have decided that the communities were first to be compensated for all the pollution, displacement and other external impacts of coal plants and mines, as well as for their just transition, before compensating the utilities.

5. **Transparency.**

   According to the government, the compensation sums are made up of lost profits, recultivation costs, and a legal disputes waiver - though it remains unclear which amount is paid for which item and whether the result is based on a formula. A financial study[6] commissioned by the German government on the recultivation costs was only disclosed several months after the Bundestag voted on the law. The study shows that the sums are not proportionate to the recultivation costs particularly regarding the operator LEAG.

6. **Commitment to the European Green Deal.**

   The climate neutrality, zero pollution and just transition objectives of the Green Deal and of the EU Climate Law must play a significant role in State aid decisions - as an integral element of the sustainable functioning of the internal market.

[6] https://www.bet-energie.de/fileadmin/redaktion/PDF/Studien_und_Gutachten/Gutachten_Folgekosten/Gutachten_Folgekosten_Braunkohleausstieg_Abschlussbericht.pdf

Background with additional comments

In 2019, Germany notified the Commission[7] of its plan to compensate its main producers of lignite-fired electricity, RWE and LEAG, with €4.35 billion (€2.6 billion for RWE and €1.75 billion for LEAG) for (i) foregone profits, as they cannot continue to sell electricity on the market, (ii) additional mine rehabilitation costs allegedly resulting from the anticipated closure, and (iii) a clause to waive rights in particular relating to the Energy Charter Treaty.

Following the green light for compensations for the closure of Dutch Hemweg 8[8] coal plant and German hard coal[9] power plant operators, German lignite operators, as well as other coal plant and mine operators in Central and Eastern European countries, are in line for restructuring or closure compensations. The planned compensations for German lignite operators are particularly problematic because the phase-out date of 2038 is far too late, the payments are astronomical, and it is still deeply unclear how the amounts were determined. Unlike the Dutch scheme, which introduced regulatory measures (binding energy efficiency levels aligned to BAT) which led to taxpayers' more cost effective closures, the German state aid system wants to maintain pollution levels of its operators to status quo level up to the phase out date and even "compensate" them.

The Commission expressed doubts about the proportionality of the proposed compensation payments and announced that it is starting an in-depth investigation.

Pre-conditionality to adhere to Union standards is a must. The Commission should ensure that the German government requires full implementation of Union standards such as Best Available Techniques for Large Combustion Plants, including energy efficiency performance (as in the Dutch case operators eligible for state aid where required to comply with binding energy efficiency levels). Currently the German Government fails to use its discretionary power to drive out lignite combustion through stricter pollution controls.

This decision will be formative in the EU. Given that many EU countries such as Poland, Romania, Czech Republic, Slovenia and Bulgaria have not yet determined how to phase out coal and are predisposed to diverting lavish amounts of taxpayers' money into State aid for coal companies, the next steps in this process will be key, as the German case can serve as an example for others. DG Competition must assess all compensation fossil fuel utilities demand for their coal with particular scrutiny and avoid compensating polluting companies for wrong business decisions investing into unprofitable coal, looking through the narrow lens of competition safeguarding.

In order to help fulfil the EU's Paris Agreement commitments and the Union's decarbonisation and zero pollution targets for 2030 and 2050, all EU countries must stop the use of coal for power generation by 2030. Power production from coal has become extremely unprofitable[10], to a level that should compel utilities to free themselves from their coal assets as soon as possible - well before 2030 in fact. German lignite plants have been making losses for some years now[11].

Besides dealing with the issue of using taxpayers' money to compensate polluting companies' bad business decisions, the new State aid regime must be coherent with the European Green Deal

[7] https://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_53625
[8] https://ec.europa.eu/commission/presscorner/detail/en/ip_20_863
[9] https://www.cleanenergywire.org/news/european-commisison-greenlights-german-hard-coal-exit-tenders
[10] https://ember-climate.org/commentary/2020/12/08/german-hard-coal/
[11] https://ember-climate.org/project/the-lignite-cash-cow/

objectives. **At the end of 2020, DG Competition started a stakeholder consultation to align competition policy with the European Green Deal which was followed by a conference[12] in February 2021.** If the Commission is serious about this intention, then climate neutrality, zero pollution and just transition objectives of the Green Deal must play a significant role in State aid decisions - and become an integral element of the functioning of the internal market. In the case of the German approach, the external costs due to other air pollutants or water pollution impacts are not even subtracted. **The German government could achieve lignite closures much earlier (by August 2021) and with a more cost-effective manner to the German taxpayers, if the government were to enforce rigorously the new EU Large Combustion Plants standards.**

The amount of compensation granted to lignite operators to phase out their lignite power plants in Germany showcases an absolute lack of transparency. The concept of non-transparent, flat-rate compensation for the majority of the lignite-fired power plant units to be finally decommissioned by 31 December 2029 (as pursued in Germany's coal phase-out legislation) does not seem appropriate[13]. In fact, this is perceived as delaying unprofitable lignite plants' exit from the market. Recent analysis demonstrates that German government's key assumptions behind the calculation of the compensations lead to a systematic overestimate of the state aid under question[14].

Despite the initiative to align the new State aid regime with the European Green Deal, the Commission has so far only expressed concerns about the amount of compensation rather than seriously questioning whether these payments are needed in the first place. The steep decline of profitability of lignite leads to the clear conclusion that for many units, any amount of aid would already be disproportionate. It is also unclear at this stage how the Commission assessed if Germany enforced the polluter pays principle before agreeing on the amount of compensation.

Lignite operations come at a high cost for people and ecosystems. In terms of air pollution only, the largest operational 18 lignite plants in Germany cause a damage cost of €7.4 billion per year[15]. The German lignite industry also consumes, pollutes and displaces millions of cubic metres of water for free or at drastically reduced prices, despite EU laws requiring water users to pay a fair price and polluters to pay for the environmental damage they inflict[16]. Germany could claim back €18.2 million per year as a compensation for lignite mines water abstraction costs only[17].

Potential link with the Energy Charter Treaty

The contracts with lignite operators that secure this compensation have a built-in clause that is supposed to protect the German government from being sued over a change in closure schedule via the Energy Charter Treaty - however, experts including ClientEarth, identified a possible loophole[18]. This means foreign investors with shares in the lignite companies could, in principle, initiate ISDS proceedings against Germany[19].

---

[12] https://ec.europa.eu/commission/commissioners/2019-2024/vestager/announcements/competition-policy-and-green-deal_en

[13] https://www.oeko.de/fileadmin/oekodoc/Assessment-of-the-planned-compensation-payments.pdf

[14] https://ember-climate.org/wp-content/uploads/2021/05/Assumption-of-German-Ministry-of-Economics.pdf

[15] If they were required to apply the EU Best Available Technique (BAT) pollution standards, due to apply latest by August 2021, the health damage burden of continued lignite operation could be reduced to €1.8 billion a year, meaning society would save €5.6 billion a year in terms of health and other air pollution-related costs.

[16] https://eeb.org/library/mind-the-gap-report/

[17] Conservative estimates, assuming North Rhine-Westphalia's rate were applied to every German lignite mine.

[18] https://www.de.clientearth.org/der-kohleausstieg-konnte-wegen-schlupflochern-noch-teurer-werden/

[19] https://www.documents.clientearth.org/wp-content/uploads/library/2020-09-04-the-german-lignite-phase-out-contract-and-investment-arbitration-isds-ce-en.pdf