Money for nothing? Commission set to release first findings on golden handshake to German lignite

Media advisory
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What is happening? As part of its coal phase-out, Germany promised multi-billion Euro payouts to lignite operators for closing their plants. On 2 March 2021, the Commission announced that it would open a formal investigation procedure into those promised compensations based on doubts about their compatibility with EU State aid rules. The opening decision is expected to be published in the coming weeks, and followed by a one-month public consultation. The Commission will then have up to 18 months to complete its assessment - though cases are generally solved sooner.

Why is it important? As the EU tries to reach its climate and environmental goals, the Commission must make sure that it is not giving the green light to subsidies that drive the bloc in the opposite direction. In Germany's case, it is fundamental not to use taxpayers' money to pay for mistakes made by companies or governments - like investing in clearly stranding fossil fuel infrastructures, overcompensating an unambitious phase-out, or making up for failure to enforce the polluter pays principle - and in fact cleaning up after the companies. Lignite operations come at a high cost for people and ecosystems, and State aid decisions must take this into account. The decision to compensate Germany's lignite plant closure will set an example for other coal phase out plans in Member States, as current ETS prices (43 euros/ton CO2 in March 2021) make it increasingly costly for coal plants to operate.

What is the legal context? The Commission is merely expected to look into whether this compensation package aligns with internal market rules only - this was mentioned in the announcement of the investigation, and would be in line with DG Competition's general approach to State aid cases historically. Until now, and even though the EU Treaties arguably oblige it to do so, the Commission has not strictly assessed State aid cases in the broader context of environmental and climate policies. At the end of 2020, DG Competition kicked off a process to align competition rules with the European Green Deal; this should concern the entire State aid practice and rules. To date, there have been no specific State aid guidelines on coal plant closure compensation but the Commission has started to handle them case by case. 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 industry.

What do we want?

- ***No State aid to incentivise business as usual.*** No subsidies should be paid to fossil fuel companies for operating; and nothing more than what is strictly 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 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.

- ***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. sulphate 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 requiring that the Commission checks compliance of activities with environmental law and principles as a condition for approving State aid.
- ***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.
- ***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 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.
- ***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.

Quote us:

“The EU competition policy should reinforce the European Green Deal and its climate, zero pollution and just transition objectives, and not secure yet another stream of subsidies to the coal industry. Under no circumstances can citizens’ money finance bad business decisions which aim to prolong the use of coal or other fossil fuels,” **said Elif Gündüzyeli, Senior Energy Policy Coordinator at CAN Europe.**

“The coal era is over and operators have known it for years, but they chose not to adapt. Instead of subsidising polluters with public money to compensate for their outdated business choices, the German government should claim back their air pollution, water and carbon debt, and hold polluters accountable for the damage they inflict to people and nature," **said Christian Schaible, Policy Manager for Industrial Production at the European Environmental Bureau.**

BACKGROUND

The European Commission (DG Competition) is expected to disclose the text of its in-depth legal investigation around the generous amounts of money that the German state intends to pay to lignite operators for closing earlier than foreseen. The recommendation for compensating the utilities to phase out coal by 2030 comes from the German Coal Commission who, in 2019, agreed on a national coal phase out date - of 2038.

In 2019, Germany notified the Commission 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 coal plant and German hard coal power plant operators, German lignite operators (as well as Romanian and Polish ones) 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, notably on mercury and nitrogen dioxide)

The outcome of this investigation will be used as a basis for the Commission’s final decision on the case. If the compensations are found to be proportionate (not overcompensating the operators), they could be allowed. On the contrary if the Commission finds that they amount to State aid incompatible with the internal market, they would not be allowed to be paid; in this case, the reservation clause in the contracts would be triggered, or Germany would need to amend the scheme, for example by reducing the amounts of compensations, to make it acceptable to the Commission.

This decision will be formative in the EU. Given that many EU countries such as Poland, Romania 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, to a level that should compel utilities to get rid of their coal assets as soon as possible - well before 2030 in fact. German lignite plants have been making losses for some years now.

Additionally, 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, leading to almost half of the country's lignite fleet losing cash based on current expectations. **Do the lignite operators in Germany really need State aid to phase out coal earlier than 2038, while it is clear that lignite business does not make economic sense anymore?**

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 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 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 more cost-effective manner to the German taxpayers, if the government were to enforce rigorously the new EU Large Combustion Plants standards.** The national rules implementing those standards have recently been blocked by the Bundesrat, due to lack of ambition to prevent mercury and nitrogen dioxide emissions from lignite combustion. Germany voted against those standards so to prevent costly retrofits to its operators, at the expense of public health and environmental protection.

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. In fact, this is perceived as delaying unprofitable lignite plants' exit from the market.

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[2]. 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

[1] 42 Euros/ton in the week of 12 March

[2] 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. https://eeb.org/library/lifting-europes-dark-cloud-how-cutting-coal-saves-lives/

polluters to pay for the environmental damage they inflict. **Germany could claim back €18.2 million per year as a compensation for lignite mines water abstraction costs only[3].**

The carbon cost the German government should recover from lignite operators can be estimated at €8.9 billion per year (based on data from 2019)[4].

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. This means foreign investors with shares in the lignite companies could, in principle, initiate ISDS proceedings against Germany.

USEFUL SOURCES

[1] *No money for old lignite. Is compensation for German lignite operators legally possible?* (2019) ClientEarth

[2] *The cash cow has stopped giving: Are Germany's lignite plants now worthless?* (2019) Sandbag/Ember

[3] Letter to the Commission by CAN Europe, Greenpeace, EEB: *German State aid for coal phase out*, (2020)

[4] Background paper E*conomic disadvantages for Greenpeace Energy due to compensation payments for coal-fired power plants operators,* Greenpeace Energy,

[5] *Assessment of the planned compensation payments for decommissioning German lignite power plants in the context of current developments* (2020) Öko-Institut e.V.

[6] *Coal phase-out compensation for LEAG. Non-compliance with State aid law and the EU's 2019 Electricity Market Regulation* (2020) ClientEarth

[7] *Disarm fossil fuel firms* (2020) CAN Europe

[8] *Vestager To Allow More State Aid To Boost Green Projects* (2020)

[9] *State of the Union: Questions & Answers on the 2030 Climate Target Plan* (2020) European Commission

[10] *Global and regional coal phase-out requirements of the Paris Agreement: Insights from the IPCC Special Report on 1.5°C* (2019) Climate Analytics

[11] Briefing The German lignite phase-out contract and investment arbitration (2020) ClientEarth

[12] *Mind the Gap: Mapping hidden subsidies for the coal and lignite industry* (2020) EEB

[13] *Lifting Europe's Dark Cloud: How Cutting Coal Saves Lives* (2017)

[14] *Competition policy supporting the Green Deal: our call for a sustainable competition policy*, ClientEarth (2020)

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

[4] Assuming a carbon cost shadow price of 100€ per tonne of CO2, whilst the current EAU price is 25€. In 2019 German lignite plants emitted 119 million tonnes of CO2.