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Unit B.3 – State aid Energy and Environment
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To the attention of:

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Ref: SA.53625(2019/EO) - Deutschland – Kohleausstieg

Dear ██████████,

In addition to our previous submissions in this matter¹, ClientEarth hereby submits supplementary analysis that we hope will be useful for the compatibility assessment of the planned **compensations to lignite plants operators** under the German coal phase out law ("KVBG") adopted on 3 July 2020.² The draft contract between the lignite plants operators, opencast mines operators and the Federal Republic of Germany has been published on 23 June 2020, containing the rights and obligations of the parties in implementation of the KVBG ("the contract").³ This contract has not been signed yet, as it still requires parliamentary consent. However, we currently do not expect substantial changes to occur as it reflects the result of a long negotiation process.

¹ ClientEarth report of October 2019, available at: <https://www.documents.clientearth.org/library/download-info/clientearth-analysis-no-money-for-old-lignite-is-german-coal-compensation-legal/>.

ClientEarth report of May 2020, DG COMP Registration: 2020/061587, available at: <https://www.documents.clientearth.org/library/download-info/coal-phase-out-compensation-for-leag-legalty-assessment/>.

ClientEarth email of 7 May 2020, DG COMP Registration: 2020/082701

² Available at: <http://dipbt.bundestag.de/dip21/brd/2020/0392-20.pdf>

³ Version of 23 June 2020, available at: https://www.bmwi.de/Redaktion/DE/Downloads/M-O/oeffentlich-rechtlicher-vertrag-zur-reduzierung-und-beendigung-der-braunkohleverstromung-entwurf.pdf?__blob=publicationFile&v=4



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The present letter focusses on the following:

1. Economic and legal analysis confirm that the amounts of compensations planned in the KVBG and implementing contract largely exceed the minimum required to incentivise early closure of the lignite plants and rather overcompensate their operators by almost €2 billion.
2. Analysis that the compensation that LEAG is entitled to receive under the law (€1.75 billion) will actually, as per the draft contract, benefit other undertakings than the lignite plant operator and cover the costs of recultivation of opencast mines that should in principle fall under the operators' liabilities, in breach of the polluter pays principle and paragraphs 7 and 44 EEAG.

1 Proportionality of the aid: still a severe risk of overcompensation of lignite plant operators

1. In our reports of October 2019 and May 2020, we expressed serious doubts as to whether the amounts of compensations planned for the closure of lignite plants under the draft KVBG would not lead to overcompensations. We criticised the lack of transparency of the calculation method since the draft law was not disclosing any formula. We advised that the German authorities should be careful as to include factors enabling the formula to adjust to the actual losses and other variables incurred by the lignite plants due to their earlier closure.

Not only those doubts remain, they are exacerbated by the KVBG adopted on 3 July 2020 due to the following aspects in particular.

Lack of a transparent formula taking into account the relevant variables

2. The KVBG and the draft contract with the operators still do not contain the formula for calculating the amount of compensations so that doubts as to the proportionality of the contemplated aid fully remain.
3. In a supplementary analysis of 29 June 2020 (**Annexes 1 and 1bis**⁴, see section 4.3 for the results), Öko-Institut evaluated, by a formula proposed at pages 21-22, that the lump amount of €1.75 billion promised to LEAG is overcompensating it by about €1 billion⁵; and the lump amount of €2.6 billion promised to RWE is overcompensating it by about €0.9 billion if the conversion costs for RWE's opencast mines are in the order of €1 billion.⁶

⁴ Also available in German at: <https://www.oeko.de/publikationen/p-details/einordnung-der-geplanten-entschaedigungszahlungen-fuer-die-stilllegungen-deutscher-braunkohlekraftwerke-im-kontext-aktueller-entwicklungen>

⁵ Öko-Institut appears to assume (p. 28 last para.) that units Jänschwalde A and B will receive contractual compensation in addition to the aid under the strategic reserve. This is in principle not the case, those units being eligible only to the strategic reserve payments according to the relevant legal provisions in the Energy Markets Act (EnWG). This makes Öko-Institut's conclusion that LEAG is very largely overcompensated even stronger since only four units are to be compensated by the overestimated lump sum of €1.75 billion.

⁶ Öko-Institut precises that the compensation amount for RWE could be justified in the order of €2.6 billion if the conversion costs of the opencast mines are in the order of €2 billion. The exact amount still needs to be established by the operators and the German authorities.

Absent any publicly available formula for calculating those compensations, Öko-Institut draws its conclusions from the most credible variables based on the evolution of climate policies and regulations at EU and national levels as well as market factors: *"Almost all lignite power plants have shown clear downward production trends since autumn 2019. In the months since March 2020, special effects from the Covid-19 pandemic have played an important role (particularly in terms of the decline in power consumption) but on closer examination, however, higher CO₂ prices, lower gas prices and the high feed-in of electricity from renewable energy plants are also important explanatory factors. With the exception of low gas prices (which can only be reliably estimated for short forecast periods), the three remaining explanatory factors (energy consumption, renewable power generation and the residual load requirement resulting from this, plus CO₂ prices) probably reflect a situation that will occur to an increasing degree and with ever greater strength going towards 2030."* (p. 13)

4. Moreover, lump sums, as currently planned in section 44(1) KVBG, cannot be accepted without reservation since other variables such as the date of closure of the plants shall also be taken into account.

Compensations are not adjusted as per the actual closure dates

5. Section 44(3) KVBG and section 10(4) of the draft contract provide that RWE and LEAG will receive the same amount of compensations if they close pursuant to the deadlines in Annex 2 KVBG or if they close earlier pursuant to their own reasons.⁷ In this sense, section 44(3) KVBG is an additional reward for the lignite operators. The provision reads:

DE:

„Werden eine oder mehrere Braunkohleanlagen vor den in Anlage 2 für die jeweilige Braunkohleanlage genannten Stilllegungszeitpunkten stillgelegt, verbleibt es bei der Entschädigung nach Absatz 1.“

EN (free translation):

"If one or more lignite installations are shut down before the closure dates specified in Appendix 2 for the lignite installation concerned, the compensation referred to in paragraph 1 shall apply."

The justification for this provision seems to be that there is a risk that the operators tactically delay closure of their lignite-powered units to benefit from (higher) compensations - which would undermine the stated objective that is reducing greenhouse gas emissions.

Rewarding earlier closure of the plants in principle contributes to the objective of reducing greenhouse gas emissions faster.

But section 44(3) KVBG raises the following doubts as to the design of the measure:

- This provision is a recognition that the closure schedule set in Annex 2 KVBG is not ambitious and too laxist in comparison with the lignite operators' expected behaviour absent the aid scheme – since it is anticipated that they may close earlier. This **questions**

⁷ The KVBG provides that the scheduled closure dates can also be brought forward statutorily. **This can trigger additional aid but the amounts are not evaluated in the law or contract yet.** See section 47 KVBG and section 21(1 a) of the draft contract.

whether the schedule in Annex 2 KVBG is appropriate to meet the objective of reducing greenhouse gas emissions.⁸

- Granting the same amount of compensations regardless of the date of closure of the plants raises serious doubts as to the **proportionality** of the compensations set out in section 44(1) KVBG. Assuming that the objective of the law is an ambitious reduction of greenhouse gas emissions, one would expect the amount of aid to be higher for plants closing earlier than for plants closing later, in order to incentivise them to do so.⁹ To this end, section 44(1) and (3) could be providing for **degressive aid intensities or amounts** overtime.¹⁰
- Whilst we assume that only closure pursuant to lawful behaviours and based on the undertaking's decision to contribute to the objectives of the KVBG make the plants eligible to section 44(3) KVBG, the contract should clarify whether closures pursuant to unlawful behaviours (e.g. violation of permit conditions) are also in the scope of this section and if so, how there can be a need for aid and an incentive effect to it.

2 Compensations to LEAG to be used for covering recultivation costs of opencast mines can violate the polluter pays principle

6. In paragraphs 14 and 30-31 of our report of May 2020, we analysed that the aid of €1.75 billion planned for LEAG included costs of recultivation of opencast lignite mines in Lusatia.¹¹ In light of the polluter pays principle and legal obligations of mine operators, we analysed that this would clearly not be an eligible, or 'net extra', cost since German mining law provides for a legal obligation on the mines operators to fund such recultivation; these costs would be faced regardless of the precise date of the coal phase-out.

Our analysis remains valid with the draft contract of 23 June 2020. It confirms that the intention of the German authorities is to relieve mines operators from the financial burden of their environmental liabilities although the law provides otherwise.

⁸ Section 2(1) KVBG provides that the objective of the law is to reduce the use of coal and emissions in a gradual and steady manner. This can be considered consistent with the Paris Agreement and EU's decarbonisation objectives as well as Germany's national objectives only if the schedule is ambitious enough so as to effectively achieve reduction of emissions by 2030. **However, the law allows lignite plants to operate longer than the climate emergency allows.**

⁹ Adjustments as per the actual loss of profits, saved costs and avoided losses etc. shall also be taken into account in the final award of the aid to individual plants and shall be factored in the (unpublished) formula.

¹⁰ This would not undermine the reservation in section 2 KVBG that the coal exit path should be gradual in order to ensure security of supply since Germany is not in a situation of insecurity of supply and the primary alleged objective of the law shall be reached.

¹¹ Former Section 42 (2) No. 3 of the draft KVBG: "A compensation for the permanent closure of lignite plants under Annex 2 with a net nominal capacity of more than 150 megawatts before 2030, amounting to [...] EUR 1.75 billion for lignite plants in Lusatia - the compensation compensates for economic disadvantages resulting from the early withdrawal of lignite **in terms of mining obligations**, necessary conversions, personnel restructuring and electricity marketing." (our emphasis)

7. Section 44(1) KVBG as adopted on 3 July 2020 no longer stipulates that the aid to LEAG shall cover costs of recultivation of mines as the compensations are paid for closures of lignite **plants**. However, the contract contradictorily provides:

- At section 7(1) and (2): the mines operators' liabilities under mining laws are not affected by the contract. Mines operators shall "*continue to bear the costs for the reconditioning of the opencast mines, the costs for mining damage and - as far as the responsibility of the mine operator for this arises from legal regulations, plans and permits - the cost of recultivation, for dewatering and for any aftercare as well all other costs incurred according to legal regulations (...)*" (free translation¹²); **but**
- At section 14: the compensation shall be used to cover the recultivation costs of opencast mines; the operator and special purpose vehicles set up by LEAG¹³ shall ensure that they will have sufficient financial resources to cover those costs when they become due¹⁴ – by, we deduct, saving part of the closure aid that is paid to them for this purpose.
- Sections 15 and 16 detail how opencast mines' recultivations costs are to be covered.

If these provisions in the contract remain, despite the absence of explicit wording in section 44(1) KVBG, this would raise serious concerns as to:

- the **use of the compensations** by the operators in conformity with the KVBG: the compensations are in principle designed for compensating the closure of lignite *plants*, which are undertakings independent from mine operator undertakings;
 - A potential **indirect aid** to LE-B and the special purpose vehicles operating the mines, which end up being payees of an aid that was in principle meant for LEAG power plants;
 - the compatibility of the payment of the aid to the mines with the **polluter pays principle**.
8. In respect of the polluter pays principle, paragraph 44 EEAG provides that aid for remedying contaminated sites can be granted only when the polluter is not identified or cannot be held legally liable for financing the remediation in accordance with the polluter pays principle. This is not the case of the opencast mines operators: not only are they well-identified and are

¹² Section 7(2) in German (original version) reads: "(...) Insbesondere tragen die Tagebaubetreiber unverändert die Kosten für die Wiedernutzbarmachung der Tagebaue, die Kosten für Bergschäden sowie – soweit sich die Verantwortung der Tagebaubetreiber hierfür aus den rechtlichen Vorschriften, Plänen und Genehmigungen ergibt – die Kosten für die Rekultivierung, für die Wasserhaltung und für eine etwaige Nachsorge sowie sämtliche sonstige Kosten, die die Tagebaubetreiber nach rechtlichen Regelungen tragen müssen (...)"

¹³ Lausitz Energie Bergbau AG (LE-B) operates the Welzow-Süd and Jänschwalde opencast lignite mines in Brandenburg and the Nochten and Reichwalde opencast lignite mines in Saxony. Some assets of LE-B (relating to pensions mainly) have been transferred to two special purpose entities: Lausitz Energie Vorsorge- und Entwicklungsgesellschaft Brandenburg GmbH & Co KG and Lausitz Energie Vorsorge- und Entwicklungsgesellschaft Sachsen GmbH & Co KG. According to the Federal Mining Act, the follow-up costs of coal mining must be borne by the mining operators, i.e. LE-B.

¹⁴ Section 14 of the contracts in German reads: "Es besteht Einigkeit zwischen den Vertragsparteien, dass die Entschädigung dafür genutzt wird, die Tagebaufolgekosten rechtzeitig abzudecken. Die Tagebaubetreiber sowie die Zweckgesellschaften werden daher dafür Sorge tragen, dass im Zeitpunkt der jeweiligen Fälligkeit der Tagebaufolgekosten ausreichende Finanzmittel zur Verfügung stehen, um diese Kosten zu begleichen."

parties to the contract, but section 7(1) and (2) recall their liabilities under German mining law – that include remediation and recultivation of the sites.

9. Moreover, the closure of the lignite plants should only have a marginal, if any, impact on the recultivation costs of the mines since those costs are legally due in any case when the mines themselves (not the plants they supply) cease to operate. In this respect, since the KVBG does not order the closure of mines – which are, on the contrary, seen as necessary for ensuring security of supply¹⁵ – the KVBG and the contract should not create new, additional recultivation cost on the mines operators to the ones generally due under mining law. In principle, mining law obliges the operators to **provision adequate sums** for this purpose.

On this basis, **there should not be any market failure**, in the sense of the mine operators risking not to face the full costs of their pollution¹⁶, created by the KVBG that could justify a State aid for financing mines recultivation costs.

10. This being said, in reality it appears that the **relevant permits have not required sufficient provisions** for recultivation of the opencast mines.¹⁷ Furthermore, an access to information request with a regional mining authority showed that an independent assessment of the actual cost of recultivation (without the coal phase-out) has not been carried out (**Annex 2**, last sentence). Sections 14 to 16 of the contract rather lead to think that allowing the mines operators to use the compensations (in principle due for the closure of plants) for the purpose of recultivation of mines makes up for the fact that they will not be in a position to comply with their mining law and environmental law obligations once they cease to operate the mines. This concern is further substantiated by the law that allows compensations payments to the LEAG's special purpose entities before actual closures of the opencast mines happen – which enables them to increase their provisions.¹⁸

Since paragraphs 7 and 44 EEAG require that Member States first ensure compliance with environmental legislation, a State aid could not be justified to remedy on the one hand, the undertakings' failure to comply with their mining law obligations and, on the other hand, the Member State's failure to enforce mining laws by requiring the operators to make adequate provisions for, and pay, their recultivation costs, whereas the operators are identified and legally responsible for them.

11. Thirdly, even if the aid could be used for covering costs relating to the opencast mines without there being an **indirect aid to the mine operators** – which again, is doubtful – it seems to confirm that the amount of compensation (€2.6 billion for RWE and €1.75 billion for LEAG) **has been calculated from the beginning for including costs** relating directly to the lignite plants and to the opencast mines – which could be an explanation for their excessive amount.

¹⁵ Preamble of the draft contract : in German :

In English (free translation): "On the basis of the information provided by the plant operators, the Federal Republic of Germany assumes that, subject to the reviews in the years 2022, 2026, 2029 and 2032, the mining concepts adapted to the decommissioning path and the use of the other opencast mines provided for therein are also necessary from the point of view of energy security." Note: "Other opencast mines" in this context means "other than Garzweiler II" operated by RWE, as the law contains a special provision for this mine to be mined as planned and without any reduction in coal extraction.

¹⁶ EEAG, para. 35(a)

¹⁷ ClientEarth and organisation BUND Landesverband Brandenburg e.V. challenge the mining permit for LEAG's mine Welzow-Süd for this reason.

¹⁸ See Section 45(3) KVBG.

Again, this is not the stated purpose of the law which is organising the closure of lignite plants and not of mines. The absence of published formula for the compensations does not enable us to draw firm conclusions on this and we can only encourage the Commission to be extremely vigilant.

Conclusion

Consequently, the Commission should conduct an extremely careful assessment of the compatibility of sections 14-16 of the contract with the polluter pays principle. One needs to ensure both that the compensation is calculated without reference to recultivation costs that would anyway be applicable (by applying a strict comparison between recultivation costs with and without the agreed phase-out), and that any compensation granted is actually used for the specified purposes relating directly to the closure of the lignite plants: when that it not the case, it should not be paid.

The level of details that still seem necessary to collect on the transactions and use of the aid, as well as its amount, call for the opening of a formal investigation. This would not only enable the Commission to collect information from interested third parties but also be able to request information directly from the operators pursuant to Article 7 of Council Regulation (EU) 2015/1589.

Kind regards,

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