Case C-126/20

Summary of the request for a preliminary ruling pursuant to Article 98(1) of the Rules of Procedure of the Court of Justice

Date lodged:

6 March 2020

Referring court:

Verwaltungsgericht Berlin (Germany)

Date of the decision to refer:

24 February 2020

Applicant:

ExxonMobil Production Deutschland GmbH

Defendant:

Bundesrepublik Deutschland, represented by the Umweltbundesamt, Deutsche Emissionshandelsstelle

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Subject matter of the main proceedings

(Challenge to an allocation decision by the Deutsche Emissionshandelsstelle (German Emissions Trading Authority, 'the DEHSt') — Concept of 'heat benchmark sub-installation' — Concept of 'process emissions sub-installation' — Request for clarification of the relationship between an allocation on the basis of heat benchmark and an allocation based on process emissions)

Subject matter and legal basis of the reference

Interpretation of EU law, specifically Decision 2011/278/EU; legal basis: Article 267 TFEU

Questions referred

1. Does the CO_2 released into the atmosphere as part of the processing of natural gas (in the form of sour gas) in the 'Claus process', by means of the CO_2 inherent

in natural gas being separated from the gas mixture, constitute an emission which, for the purposes of the first sentence of Article 3(h) of Commission Decision 2011/278/EU, occurs as a result of the process referred to in Article 3(h)(v)?

2. For the purposes of the first sentence of Article 3(h) of Commission Decision 2011/278/EU, can CO_2 emissions occur 'as a result of' a process in which the CO_2 inherent in the raw material is released into the atmosphere, even though the process taking place does not give rise to additional CO_2, or does that provision make it mandatory for the CO_2 released into the atmosphere to occur for the first time as a result of that process?

3. Is a carbon-containing raw material 'used' within the meaning of Article 3(h)(v) of Commission Decision 2011/278/EU where, in the 'Claus process', the naturally occurring natural gas is used to produce sulphur and, in the course of that procedure, the CO_2 inherent in the natural gas is released into the atmosphere, even though the CO_2 inherent in the natural gas does not play a part in the chemical reaction taking place in that process, or does the term 'use' make it mandatory for the carbon to play a part in, or indeed be essential to, the chemical reaction taking place?

4. If Questions 1 to 3 are answered in the affirmative:

On the basis of which benchmark is the allocation of free emission allowances to be carried out where an installation subject to the emission trading scheme satisfies both the defining conditions of a heat benchmark sub-installation and the defining conditions of a process emissions sub-installation? Does entitlement to an allocation on the basis of the heat benchmark take priority over entitlement to an allocation for process emissions or does entitlement to an allocation for process emissions take precedence over the heat benchmark and the fuel benchmark because it is more specific to the case in question?

5. If Questions 1 to 4 are answered in the affirmative:

Can entitlements to a further free allocation of emission allowances for the third trading period be met after the end of the third trading period with allowances of the fourth trading period where the existence of the allowance entitlement is established by a court only after expiry of the third trading period, or do allowance entitlements that have not yet been met lapse on expiry of the third trading period?

Provisions of EU law cited

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 (OJ 2003 L 275, p. 32), as amended by Directive 2009/29/EC of the European Parliament and of the Council of 11 March 2009 (OJ 2009 L 87, p. 109), and as last amended by Decision (EU) 2015/1814 of the European Parliament and of the

Council of 6 October 2015 (OJ 2015 L 264, p. 1): Article 2, Article 10a(1) and (4), Article 13 and Annex I

Commission Decision 2011/278/EU of 27 April 2011 determining transitional Union-wide rules for harmonised free allocation of emission allowances pursuant to Article 10a of Directive 2003/87/EC of the European Parliament and of the Council (OJ 2011 L 130, p. 1), as amended: Article 3(c) and (h)(v)

Decision (EU) 2015/1814 of the European Parliament and of the Council of 6 October 2015 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading scheme and amending Directive 2003/87/EC (OJ 2015 L 264, p. 1): recital 7

- Commission guidance documents on emission trading

Guidance Document No 8 on the harmonised free allocation methodology for the EU-ETS post 2012 — Waste gases and process emissions sub-installation

Case-law of the Court of Justice cited

Judgment of 8 September 2016, *Borealis and Others* (C-180/15, EU:C:2016:647, in particular paragraphs 62 and 69)

Judgment of 20 June 2019, *ExxonMobil Production Deutschland* (C-682/17, EU:C:2019:518)

Provisions of national law cited

Gesetz über den Handel mit Berechtigungen zur Emission von Treibhausgasen (Law on greenhouse gas emission allowance trading, 'the TEHG 2011') of 27 July 2011: Paragraph 9(1) and (6), Annex I, Part 2, point 1
Verordnung über die Zuteilung von Treibhausgas-Emissionsberechtigungen in der Handelsperiode 2013 bis 2020 (Regulation on the allocation of greenhouse gas emissions allowances in the 2013 to 2020 trading period, 'the ZuV 2020') as amended on 26 September 2011: Paragraph 2(29) (process emissions sub-installation), subparagraphs (b)(dd) and (ee) and (c), and Paragraph 2(30) (heat benchmark sub-installation); Paragraph 3(1) (formation of sub-installations)

Verordnung über die Zuteilung von Treibhausgas-Emissionsberechtigungen in der Handelsperiode 2013 bis 2020 (Regulation on the allocation of greenhouse gas emissions allowances in the 2013 to 2020 trading period, 'the ZuV 2020'), as amended on 26 September 2011: Paragraph 2(29) (process emissions sub-installation), subparagraphs (a), (b) and (c), and Paragraph 2(30) (heat benchmark sub-installation); Paragraph 3(1)

Brief summary of the facts and procedure

1 The **applicant**, which was also the applicant in Case C-682/17, operates a natural gas processing installation in Grossenkneten (Lower Saxony) in which sulphur is recovered. The sulphur recovery facility uses the 'Claus process'. The installation in question is used to process natural gas recovered from natural sources (raw gas) which, due its high concentration of hydrogen sulphide, is also referred to as sour gas. Carbon dioxide is naturally present in the natural gas that occurs in the subsoil. The carbon dioxide and other natural components of the raw gas must be partially removed before the natural gas is delivered to the transmission network, in order to maintain the quality prescribed by the network operator. Sulphur components and the carbon dioxide are removed from the natural gas recovered, and elemental sulphur is recovered, in the applicant's natural gas processing installation. The natural gas processing installation consists, in particular, of a sulphur recovery facility (comprising Claus-process facilities, a steam superheater, a steam boiler and a gas engine facility), natural gas desulphurisation (purification) and dehydration facilities, waste gas purification facilities and emergency flaring facilities. The Claus-process facilities are the main source of CO_2 emissions.

2 By decision of 17 February 2014, the DEHSt allocated to the applicant free of charge a total of 4 216 048 emission allowances for the allocation period running from 2013 to 2020 (third trading period). The allocation was based in part on the application of a heat benchmark and in part on the application of a fuel benchmark. The allowances which the applicant also applied for in respect of process emissions were refused on the ground that the carbon dioxide is already contained in the raw material for natural gas processing; it is not emitted as a result of the natural gas processing process ('Claus process'), meaning that the emissions are passed on through the facility due solely to the process.

3 By decision of 7 October 2019, the DEHSt dismissed the objection to the allocation decision lodged by the applicant on 12 March 2014. The reasons given were essentially that an allocation for process emissions in accordance with Paragraph 2(29)(b)(ee) of the ZuV 2020 could not be granted; that the 'Claus process' consists of an exothermic chemical reaction by which hydrogen sulphide is converted into sulphur; that the heat produced during that process is captured in the installation by recovery boilers before being used at the installation itself; that the allowance for the use of the heat produced in the 'Claus-process' facilities in the heat benchmark sub-installation had been allocated lawfully; that the processing of natural gas from raw gas involves the conversion of the hydrogen sulphide into sulphur in an exothermic chemical reaction; that the carbon dioxide does not play a part in, and is not necessary for, the 'Claus reaction'; that the carbon dioxide cannot be regarded as anything more than an associated gas of the fuel that is deployed; that only the hydrogen sulphide, which does not contain carbon, is used within the meaning of the relevant provision of the ZuV 2020; that no further carbon dioxide occurs as a result of the Claus reaction; and that the

carbon dioxide, which is later emitted into the atmosphere through a chimney, does not therefore occur as a result of the Claus process.

4 By the action which it brought on 8 November 2019, the applicant is pursuing its claim.

Principal arguments of the parties in the main proceedings

5 The **applicant** contends in substance: that the feed gas has to have a high hydrogen sulphide content for the Claus process; that the exothermic conversion of the hydrogen sulphide to sulphur in the Claus process takes place in two steps: a first thermal step, in which approximately one-third of the hydrogen sulphide is burnt in the Claus furnace to produce sulphur dioxide, and a second step, in which additional sulphur is recovered during an exothermic reaction in two or three consecutive catalytic steps; that, in addition to nitrogen, water vapour and carbon dioxide, the Claus gas still contains traces of sulphur compounds after the final catalytic step which are removed in the downstream waste gas purification facility; that the CO_2 naturally occurring in the sour gas and fed into the Claus-process facility from the gas scrubber, the processing of which is contested here, does not play a part in the Claus process taking place, but is fed to the waste gas purification facility with the Claus gas that contains hydrogen sulphide, and is emitted into the atmosphere through the chimney; that the main source of the CO_2 emissions is the inherent CO_2 already present in the sour gas; that this is released into the atmosphere as part of the recovery of sulphur through the Claus process; and that, according to judgment of the Court of Justice of the European Union of 20 June 2019, the release of inherent carbon dioxide is subject to the emission trading scheme.

6 The applicant takes the view that it is entitled to the free allocation of an allowance for a process emissions sub-installation in accordance with Paragraph 2(29)(b)(ee) of the ZuV 2020 and Article 3(h)(v) of Commission Decision 2011/278/EU; that the carbon dioxide emissions at issue result from the use of a carbon-containing raw material; that the sour gas used for the recovery of sulphur is extracted from natural deposits in underground reservoirs and contains a mixture of hydrogen sulphide, water vapour, methane and carbon dioxide; and that carbon dioxide contains carbon.

7 The applicant submits that, contrary to the view expressed by the defendant, carbon dioxide is not to be regarded as nothing more than an associated gas. The applicant's further contentions reflect those made in the main proceedings in Case C-682/17.

8 It contends that, contrary to the view expressed by the defendant, carbon dioxide is also not simply passed on in the process at issue. The applicant's further contentions on this point too essentially reflect those made in the main proceedings in Case C-682/17.

9 The applicant contends that the wording of the definition of the term 'process emissions sub-installation' presupposes that the raw material used contains carbon; that the wording of the relevant provisions does not require that carbon also play a part in the chemical reaction taking place; that, as also follows from the different language versions of Article 3(h)(v) of Decision 2011/278, use simply presupposes that something is used for a particular purpose; and that, contrary to the provision, Article 3(h)(v), of relevance here, the wording explicitly requires for processes in accordance with Article 3(h)(iv), for example, that the carbon-bearing material must participate in the reaction.

10 Further arguments, based on systemic and teleological considerations, that the criterion for process emissions should be the simple causal relationship between the process concerned and the production of CO_2 emissions, not whether the carbon participates in the Claus reaction, reflect those made in the main proceedings in Case C-682/17.

11 Lastly, the applicant notes that the uniform EU allocation rules were not intended to limit installations for the manufacture of sulphur to allocations on the basis of the heat benchmark; that limitation to the heat benchmark would be unequal treatment, for which there is no justification, in relation to the numerous other chemical products for which product benchmarks are expressly provided for in Annex I to Decision 2011/278; and that the fact that the quantities of carbon dioxide produced from the subsoil are not covered by any other sub-installation should be taken into account.

12 The arguments made by the **defendant** essentially reflect those made by it in the main proceedings in Case C-682/17.

Brief summary of the basis for the reference

13 The referring court notes that this dispute differs from the dispute adjudicated upon by the Court in Case C-682/17, in that the applicant's power station at the installation did not connect to the network until 2014 and did not start delivering electricity to the public grid until the summer of 2014, therefore after the start of the third trading period and after the allocation decision was adopted.

14 Questions 1 to 3, seeking clarification as to whether and, if so, by what benchmark, an entitlement to a free allocation of emission allowances exists for the 'Claus process' taking place in the installation in question, affect the applicant's entire allowance entitlement.

15 Question 4 is based on the reasons given by the Court in its judgment of 8 September 2016 in *Borealis and Others*, specifically on paragraphs 62 and 69 of that judgment.

16 The referring court is of the opinion that it follows from those reasons that the question of the hierarchy of the three 'fallback' approaches to the allocation

should not arise. If the definitions are mutually exclusive in every conceivable case, then allocation is in any case possible only on the basis of one of the three benchmarks. The defendant argues in several other proceedings pending before the chamber that there is a hierarchy between the three 'fallback' approaches and assumes that the heat benchmark takes precedence over the allocation of allowances on the basis of the process emissions benchmark.

17 Subject to the answer given to Questions 1 to 3, it seems possible in this case that the emissions from the 'Claus process' can meet the definition both of the heat benchmark and of process emissions. Due to the differentiation between measurable heat and non-measurable heat, the distinction between the heat benchmark and the fuel benchmark is clear. The referring court is of the opinion, subject to the answer given to Questions 1 to 3, that the relationship between an allocation on the basis of the heat benchmark and an allocation based on process emissions appears to require clarification in this case. For, if the Claus process uses a carbon-containing raw material within the meaning of Article 3(h)(v) of Decision 2011/278, the heat generated by the exothermic Claus process may be eligible for an allocation both on the basis of the heat benchmark, pursuant to Article 3(c) of Decision 2011/278, and on the basis of the benchmark for process emissions, pursuant to Article 3(h)(v) of Decision 2011/278.

In the opinion of the chamber, if a final decision cannot be adopted in these proceedings before the end of the third trading period, an answer to Question 5 will be relevant for its judgment.

18 The third trading period ends on 31 December 2020. According to the case-law of the German courts, when the first and second trading periods ended, allowance entitlements outstanding until 30 April of the year following the end of the trading period could no longer be met and, as there was no explicit transitional arrangement in national law, they lapsed. Nor does national law include a transitional arrangement in the third trading period for outstanding allowance entitlements still pending before the courts. The reason given for this lack of national transitional arrangements is that the rules for the free allocation of allowances in the trading period running from 2021 to 2030 are laid down conclusively in the EU Allocation Regulation and it is only permitted to balance allocation entitlements across periods if so provided for in the EU Allocation Regulation for the fourth trading period (which was still being drafted when the Federal Government lodged its defence).

19 The referring court would welcome a uniform decision in EU law on outstanding allocation entitlements. It notes that neither Directive 2003/87 nor Decision 2011/278 expressly regulates this matter. Nor does Commission Delegated Regulation (EU) 2019/331 of 19 December 2018 (OJ 2019 L 59, p. 8) (EU Allocation Regulation), enacted in the meantime, have a rule governing the balancing of allocation entitlements across periods, for example in the form of a case-law reserve.

20 The rule in Article 13 of Directive 2003/87 on the validity of allowances makes no reference to the question of allowances that have still not been allocated at the end of the third trading period. According to recital 7 of Decision (EU) 2015/1814 of the European Parliament and of the Council of 6 October 2015, allowances not allocated to installations pursuant to Article 10a(7) of Directive 2003/87 and allowances not allocated to installations because of the application of Article 10a(19) and (20) of the directive ('unallocated allowances'), should be placed in the reserve in 2020. In the opinion of the referring court, recital 7 suggests that the transition from the third to the fourth trading periods does not cause the additional allocation entitlements not met at that point to lapse. However, there is no unequivocal rule on what happens to additional allocation entitlements not met by the end of the third trading period.

21 This question has arisen in several actions that are pending before the chamber and before the national courts at other instances. As it will not be possible to deliver final judgment by the end of the trading period in all the proceedings and the case-law of the German courts to date gives installation operators cause to fear that allocation entitlements will lapse, urgent proceedings have already been initiated before the chamber to protect their legal rights. The chamber cannot anticipate in such urgent proceedings to protect legal rights the ruling of the Court needed on this question.

22 The referring court therefore asks the Court to clarify the question what effect the end of the third trading period will have on the allowance entitlements not met by then, even independently of a ruling on the other questions referred, as this is a fundamental question that has arisen in all proceedings still pending in the European Union for an additional allocation of emission allowances and urgently needs to be clarified to ensure legal certainty and the uniform application of EU emissions trading law.