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**Emissions Trading Before the European Court of Justice:
Market Making in Luxembourg**
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EMISSIONS TRADING BEFORE THE EUROPEAN COURT OF JUSTICE: MARKET MAKING IN LUXEMBOURG

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Abstract: The litigation faced by the EU ETS is of significance not only for that mechanism – the world’s largest carbon market – but also for emerging carbon markets around the world and thus the enterprise of tackling global climate change by way of market mechanisms. This working paper analyses the entire EU ETS docket of the Community Courts (the ECJ and CFI) to date and seeks to categorise those cases. Themes familiar to EC lawyers prevail – especially in relation to questions of standing and admissibility – that in the light of the recently agreed Phase III EU ETS look less like narrow technical rulings than the Courts’ constraining commercial and political actors from sundering legal responses to climate change.

Keywords: Climate change, climate change litigation, EU ETS, carbon markets, Community Courts, UNFCCC, Kyoto Protocol, energy

Emissions Trading Before the European Court of Justice: Market Making in Luxembourg*

1. Introduction

Anyone with even a nodding familiarity of global carbon markets recognises the current primacy of the EU Emissions Trading Scheme¹ within them. With a trading volume of at least €28bn in 2007, the EU ETS represents approximately 70% of global traded volumes in carbon products² and 62% of physical volumes.³ It is variously described as “the main driving force of the global carbon market”, “the main driver for emissions reductions, both at home and in developing countries”,⁴ “the engine, perhaps even the laboratory, of the global carbon market”.⁵ The EU ETS’s trading volumes dwarf those of its rivals - the voluntary Chicago Climate Exchange, the New South Wales ETS, the New Zealand ETS and the fledgling Japanese scheme - none of which has a volume equal

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¹ 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 L275/32. Hereinafter ‘EU ETS’, ‘the Directive’ or ‘the Scheme’. See JH Jans & HHB Vedder, European Environmental Law (3rd edn Europa Law Publishing, Groningen 2008) 385-388 for a pithy conspectus.

² Point Carbon, K Roine et al, Carbon 2008 - Post-2012 Is Now (Oslo, 2008). The World Bank’s estimate is €37bn, representing trades of more than 2bn EUAs. See World Bank, State and Trends of the Carbon Market 2008 (Washington DC, 2008).

³ World Bank, *ibid.*

⁴ Point Carbon, *ibid.*

⁵ World Bank, State and Trends of the Carbon Market 2008 (Washington DC, 2008).

to even 1% of the EU ETS.⁶ The Scheme's position of primacy will remain unchallenged unless and until a federal US scheme⁷ is established.

Within its own territory the Scheme is a significant policy instrument, with 40% of the EU's total GHG emissions within its regulatory ambit, representing approximately 11,000 of the EU's largest emitting installations. For the period 2008-2012 alone it is estimated to generate emissions reductions of 3.3% (139 MtCO₂ p.a.) from the base year of 1990 in the EU-15.⁸ Whilst the European Climate Change Programme⁹ extends to issues of fuel efficiency and quality, vehicular emissions, biofuels, renewables, and carbon capture and storage, it is no exaggeration to describe the EU ETS as the keystone in the architecture of the European response to global climate change.

For these reasons an understanding of the topography of EU ETS litigation is significant in and of itself. The legal challenges that the EU ETS, and decisions taken under it, face before the highest courts of the EU inform the manner in which the Scheme is interpreted and operates. Moreover, with two thirds of the 11,000 regulated entities involved in or planning to abate as a consequence of the scheme, its susceptibility to litigation is intimately linked to relevant investment decisions and the cost of capital.¹⁰ Outwith the EU, despite the failure of the US Congressional Lieberman-Warner Bill in 2008, the aftermath of the US General Election has seen the prospect of a US federal emissions trading scheme edge closer, creating the potential for comparative analysis and

⁶ Ibid 7.

⁷ WL Andreen, "Federal Climate Change Legislation and Preemption" (2008) *Environmental & Energy Law & Policy Journal*, Vol. 3, p. 261.

⁸ European Environment Agency, [Greenhouse Gas Emission Trends and Projects in Europe 2008: Tracking Progress Towards Kyoto Targets](#), EEA Report 5/2008, 7.

⁹ European Commission, ECCP, <<http://ec.europa.eu/environment/climat/eccp.htm>> accessed 1 February 2009.

¹⁰ Point Carbon, (n2). K Miles, "International Investment Law and Climate Change: Issues in the Transition to a Low Carbon World" *Society of International Economic Law*, Online Proceedings Working Paper No.27/08, available at <http://www.ssrn.com/link/SIEL-Inaugural-Conference.html> > accessed 1 December 2008.

raising future issues of interoperability. At the level of international policymaking, the legal robustness of the Scheme is a key determinant for future iterations of carbon markets and cognate mechanisms. From the perspective of the EU, commitment to the scheme is not in question - the EU's post-2012 strategy firmly sees an emissions trading scheme at its heart, as do many Member States and their sub-units. The precise nature of these architectural arrangements continues to evolve.¹¹

The concern of this chapter is the discrete matter of challenges to the EU ETS brought before the European Court of Justice (ECJ) and the Court of First Instance (CFI) – the 'Community Courts'.¹² This chapter commences with a brief account of the prehistory of the EU ETS (Part 2), followed by its legal form and operation (Part 3) before addressing the Court's case law concerning Directive 2003/87/EC (Part 4). It should be noted that the focus herein on the Community Courts' case law is not to suggest a priority in importance over litigation that takes place purely at the domestic level. Rather, space precludes consideration of disputes before the Courts of all 27 Member States and so national law will only be discussed herein tangentially.

2. Prehistory of the EU ETS

Given the EU's historical hostility to market mechanisms as solutions to pollution as recently as at the Kyoto Protocol negotiations, the Scheme's global centrality is a turnaround of some moment.¹³

Since that time however, the EU has sought to position itself as a global leader in this policy area

¹¹ In particular, see Part 3 below for details of Phase III EU ETS, agreed by the European Council on 12 December and by the European Parliament on 17 December – COM (2008) 0016.

¹² For an introduction to the judicial branch of the EU's, its legal basis, role and jurisdiction, see Part 4 below.

¹³ See C Damro, I Hardie, and D MacKenzie, "The EU and Climate Change Policy: Law, Politics and Prominence at Different Levels" (2008) 4 *Journal of Contemporary European Research* 185-189

with market mechanisms as its primary tool.¹⁴ The EU's warm embrace of market solutions to environmental problems is emblematic of its changing policy toolkit over the past decade.¹⁵ For present purposes it suffices to note that prior to and continuing into the 1990s, the EU adopted a policy approach of "regulatory environmentalism", premised on the assumption that reliance on free-market solutions would misallocate natural resources and produce inadequate incentives to prevent environmental degradation.¹⁶ There also existed a secondary and emerging strain in EU policy that, as early as 1993 in the form of the Community's Fifth Environmental Action Programme, acknowledged the limitations of command-and-control regulation and the utility of market mechanisms to "internal[ise] external environmental costs".¹⁷ This approach cohered somewhat better with the well-detailed preference of the US for environmental markets, which were deployed with success in the SO_x/NO_x contexts.¹⁸ Also familiar is the influence that these American domestic policy successes had in the negotiations at Kyoto, the architecture of the Kyoto Protocol and in particular the flexibility mechanisms contained in its Articles 6, 12 and 17.¹⁹

It is notable that having 'lost' the battle of ideas over the optimal means by which to tackle climate change, the EU subsequently embraced the new settlement with gusto.²⁰ The Kyoto Protocol committed the EU to an 8% GHG reduction by the end of 2012. Reductions were to be re-assigned

¹⁴ See S Oberthür and CR Kelly, "EU Leadership in International Climate Policy: Achievements and Challenges" 43(3) *The International Spectator* (2008) 35-50. At the time of writing, the EU's latest published approach to the Copenhagen COP in December 2009 is contained in COM (2009) 39/3.

¹⁵ See n.11.

¹⁶ J Golub, (ed), *New Instruments for Environmental Policy in the EU* (Routledge, London 1998) 8.

¹⁷ "A European Community programme of policy and action in relation to the environment and sustainable development", Official Journal C 138, 17/05/1993, p.5.

¹⁸ See C Streck and MW Gehring, "Emissions Trading: Lessons From SO_x and NO_x Emissions Allowance and Credit Systems Legal Nature, Title, Transfer, and Taxation of Emission Allowances and Credits", 4 *Environmental Law Reporter* (2005)

¹⁹ NS Ghaleigh, *The Environment and Anti-Americanism* in B O'Connor (ed) *Anti-Americanism: History, Causes, Themes* (Greenwood Press, Vol 1, Oxford 2007) 139.

²⁰ The EC, as well as its Member States, is a party to the Kyoto Protocol – Decision 2002/358, OJ 2002 L 130/1.

to Member States pursuant to its own 'Burden Sharing Agreement',²¹ facilitated by one of the EU's few negotiating successes at Kyoto, Article 4(1).²² Foremost amongst the jointly implemented responses of the EU is the Emission Trading Directive.²³ The Directive followed Commission consultations, studies and finally a "Green Paper on Greenhouse Gas Emissions Trading within the European Union"²⁴ which acknowledged the EU's Kyoto obligations as well as the necessity that that process did not represent the outer limit of the EU's relevant ambitions. Accordingly the proposal was for a scheme whose industry sector coverage was substantially repeated in the final Directive,²⁵ though with a threshold of 50MW rated thermal input. In terms of quantum of allowances and distribution, the Green Paper saw a role for the Commission only for purposes of determining Member States' internal allocations where the risk of national discrimination arose. The setting of total quantities of allowances was for the Member States themselves. The question of free allocation (by grandfathering or benchmarking) or auctioning was left open whilst the need to avoid discrimination against new entrants was given consideration.

The response to the Green Paper from EU institutions, industry and NGOs²⁶ was unusually uniform and positive facilitating, indeed requiring, swift legislative action. Introduced in October 2001 under the co-decision procedure,²⁷ the legislative proposal progressed quickly such that by December 2002 the Council had agreed a common position and textual agreement was found

²¹ Ibid, recital 10.

²² "Any Parties included in Annex I that have reached an agreement [may] fulfill their commitments under Article 3 *jointly...*" Italics added.

²³ Ibid. For an account of the Scheme's details, on which this section borrows, see J Robinson et al, Climate Change Law: Emissions Trading in the EU and the UK (Cameron May, London 2007) Part I.

²⁴ COM (2000) 87 Final.

²⁵ see Part 3 'Legal Form' below.

²⁶ See in particular Council Conclusions (Environment) 22 June 2000, European Parliament Resolution on the Commission Green Paper on GHG Emissions Trading A5-0271/2000 OJ C 197, 12.7.2001, p.400.

²⁷ The name given to the legislative process whereby measures are proposed by the Commission and jointly agreed by the Council and the European Parliament, pursuant to EC Treaty art 175(1).

between the Council and the Parliament in the second reading.²⁸ Such (relative) speed is accounted for by the widespread national support for the measure and perhaps the EU's desire to send a signal to the Marrakech UNFCCC Conference of the Parties, asserting its leadership role.

In terms of the substance of the process, it is notable that questions of industry sector coverage and thresholds attracted minimal contention.²⁹ Further, the task of setting total quantities of allowances to be allocated and the task of distributing those allowances, which were envisaged as separate in the Green Paper were combined in what were to become National Allocation Plans ('NAPs'). This created the risk that the "level of ambition under the scheme risk[ed] being diluted as a result of industry lobbying over their allocations...rather than ensuring that negotiation over the distribution [between and within Member States was] a zero sum game with no impact on the environmental integrity of the scheme."³⁰

3. Legal Form

The EU ETS is in its basic structure a conventional cap-and-trade scheme.³¹ At its heart a fixed number of allowances are issued which are divided into a quantity of pollutant which is emitted over commitment periods or phases. The level of resultant emissions is thus set to be equal to the established cap on emissions. Allowances are allocated to operators who are then obligated to monitor and report their emissions, and to surrender at the end each period an equal number of

²⁸ This is an unusual event for a measure with such broad and deep implications. Where such a consensus is not reached - the norm - a conciliation committee of both institutions is convened to negotiate a compromise.

²⁹ J Robinson et al, Climate Change Law: Emissions Trading in the EU and the UK (Cameron May, London 2007), p.63.

³⁰ Ibid, 65.

³¹ The economic rationale for such mechanisms is the claim that they minimise the marginal abatement cost of arriving at a particular level of pollution - the locus classicus for which is JH Dales, Pollution, Property and Prices: an essay in policy-making and economics (Toronto UP, Toronto, 1970), drawing, *inter alia*, on the Nobel prize winning insights of Ronald Coase's The Problem of Social Cost, 3 *Journal of Law and Economics* (1960), pp. 1-26.

allowances to the units of pollution emitted. Penalties are attached to non-compliance. The scheme also provides for the buying and selling of allowances between parties, whether regulated entities with obligations under the Scheme or mere third parties.

To this generic schema, the EU ETS's specific approaches to coverage and allowance should be noted. The Directive's coverage of activities, detailed in its Annex I, excludes aviation,³² shipping and most contentiously the aluminium and chemical sectors while including energy, ferrous metals, minerals, and pulp and paper. The Commission's Explanatory Memorandum to its original proposal justified the chemical exemption on the basis of its limited contribution to the EU's total CO₂ emissions (approx. 1% of the total) and that the large number of installations (approximately 34,000) would create significant administrative complexity to the Scheme.³³ The Memorandum remains silent on the exclusion of the aluminium sector. These choices have generated much subsequent controversy, not least before Community Courts.

Allowances, as we shall see, have been a source of at least equal controversy. Defined by Article 3(a) as the right to emit one tonne CO₂e during a specified period,³⁴ allowances are allocated and issued to installations by way of a two stage process. Stage one requires Member States to develop National Allocation Plans "stating the total quantity of allowances that it intends to allocate for that period and how it proposes to allocate them...based on objective and transparent

³² Amendments to scope of the Directive to include aviation post-2012 have recently been adopted – see Directive 2008/101/EC of the European Parliament and of the Council of 19 November 2008 amending Directive 2003/87/EC so as to include aviation activities in the scheme for greenhouse gas emission allowance trading within the Community. OJ L 8, 13.1.2009, p. 3–21.

³³ COM (2001) 581 Final, OJ C 75E, 26.3.2002, 33 at Part 11.

³⁴ "‘Allowance’ means an allowance to emit one tonne of carbon dioxide equivalent during a specified period, which shall be valid only for the purposes of meeting the requirements of this Directive and shall be transferable in accordance with the provisions of this Directive"

criteria, including those listed in Annex III.”³⁵ Such NAPs are subject to Commission approval, only after which may Member States definitively determine the total quantity of allowances and the allocation of the same amongst installations.³⁶ As with the question of sectoral scope, the details of such matters have greatly exercised the ECJ and are discussed below.

The EU ETS has been implemented in phases - 2005 to 2007 and 2008 to 2012 - which coordinate with the Kyoto Protocol compliance period, with Phase III to run from 2013 to 2020. Phase I is commonly described as a learning-by-doing phase, allowing Member States to get acquainted with a novel system, to make progress towards their Kyoto Protocol commitments and towards meeting their particular CO₂ goals pursuant to the Burden Sharing Agreement.³⁷ It has been decided that the Scheme will be extended to other greenhouse gases and installations in its Phase III.³⁸

As is well known, the ‘trial period’ of Phase I was characterised by a price collapse in late April 2006 after the publication of the verified emissions data by Member State after Member State revealed that emissions were significantly below their allocations to installations. Early 2006 pre-announcement over the counter prices were slightly over €30/ton, by mid-May had fallen to approx. €15/ton and then to near zero from early 2007 until the end of Phase I. In a sense it is inaccurate to characterize this as a market failure – it might be argued that the market reacted precisely as it ought to have by adjusting when information that changes expectations was made

³⁵ Directive art 9(1).

³⁶ Ibid art 9(3).

³⁷ Council Decision 2002/358/EC concerning the approval, on behalf of the European Community, of the Kyoto Protocol to the UN Framework Convention on Climate Change, and the joint fulfillment of commitments thereunder, OJ L 130, 15.05.2002, p1.

³⁸ Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/87/EC so as to improve and extend the greenhouse gas emission allowance trading system of the Community, COM (2008) 16 Final.

available. Once aggregate emissions, and the resulting demand for allowances were known, the fact of over-allocation had its predictable price consequences.³⁹ Thereafter, Phase II forward contracts dominated the markets' attention, with December 2008 EU Allowances (EUAs) ranging between €12-25 per tonne, remaining within the €20-24 band for the majority of 2007. Upon the commencement of Phase II, such prices remained durable (at around €20-25 for most of 2007), revealing the price of emitting GHG in the EU but also sending a strong signal to CDM and JI project developers that emission reductions generated through projects which generate carbon credits would find a robust market in the EU ETS.⁴⁰

A consequence of the Phase I price collapse was its impact on the design of Phase II. The Commission's approach to the Phase II caps has been described as "unquestionably tough",⁴¹ being much tighter than in Phase I in an overt attempt to create demand for emission reductions, whether generated within the EU or in non-Annex I countries. The Phase II cap for EU 27 is 2,098 Mt/yr, cutting Member States' suggested allocations in NAPs by 245 Mt/yr (10.4%). The largest absolute cuts were in Poland (76Mt), Germany (29Mt), Bulgaria (25Mt) and the largest relative cuts in Baltic states (ave. 37%).⁴² These figures represent a cut of 130MtCO₂ (6.0%) below 2005 verified emissions and 160MtCO₂ (7.1%) below 2007 verified emissions.

Whilst the cuts in MSs allowances are deep, the pain has been considerably eased by Phase II's 'credit limits' (the maximum CDM/JI volumes that can be purchased for compliance purposes)

³⁹ In the view of the Commission, the "swiftly corrected market price of allowances demonstrat[es] convincingly that the carbon market is working." Ibid at p 2. There is however also a strong argument that over-allocation was accompanied by over-abatement – AD Ellerman & BK Buchner, "Over-Allocation or Abatement" A Preliminary Analysis of the EU ETS Based on the 2005-06 Emissions Data" 41 Environmental Resource Economics (2008), 267-287, at 270.

⁴⁰ See World Bank, n.2 at 7.

⁴¹ Ibid.

⁴² See Point Carbon, n.2 at p. 28, Table 1.

which vary according to Member States from 10% in most cases, up to 22% for Germany.⁴³

Coupled with tightness of allocations, this creates the possibility for sizable offset/credit imports.⁴⁴

Nonetheless it remains the case that the EU ETS is projected to reduce EU-15 emissions by 139MtCO₂ p.a. during 2008-12 (a 3.3% reduction from the 1990 baseline). The ongoing impact of such measures is demonstrated by the fact that whilst the 2006 emissions of only 4 of the EU 15 were lower than their Kyoto target (France, Germany, Sweden and the UK), that figure is expected to rise to 12 of 15 by 2010 (Denmark, Italy and Spain being the miscreants).⁴⁵ Such is the strength of these projections that the operation of Phase II in much of 2008 saw relatively strong prices between €19-29/ton. Since the onset of the global recession and as at February 2009, that price had halved.

EU ETS Phase III has recently taken concrete form following approval by European Council and European Parliament in December 2008.⁴⁶ Unlike its predecessors, Phase III will run for an 8 year period commencing 1 January 2013 in contrast with the 5 year durations of Phases I and II. The emissions cap will be set by the Commission and features a steady trajectory towards 2020, aiming to reduce emissions by 21% overall,⁴⁷ based on annual reductions of 1.74%, but the figures are

⁴³ Facilitated by the 'Linking Directive' EC 2004/101, OJ 2004 L 228/18.

⁴⁴ Although outwith the scope of this paper, large scale credit imports create at least two concerns. Firstly, reliance on emissions reductions made in CDM/JI projects whose ability to achieve *actual* emissions reductions continues to be questioned – see M Wara & DG Victor, 'A Realistic Policy on International Carbon Offsets', Stanford Program on Energy and Sustainable Development Working Paper # 74, April 2008 – raises questions of effectiveness and thereby market and public confidence. Perhaps more importantly, the EU's policy of engagement at Copenhagen with developing economies involves the offer of unilateral emissions reductions of 20%, or 30% if matched by those parties. If EU MSs are able to count credit imports as 'domestic', the threshold is raised to a near impossible level for developing economies, who face the prospect of having to reduce their own emissions by 30% plus the quantity of emission reductions imported into the EU.

⁴⁵ European Environment Agency, "GHG Emission Trends and Projections in Europe", 2008.

⁴⁶ COM (2008) 0016 Final.

⁴⁷ Commission 'Question and Answers on the revised EU Emissions Trading Scheme' MEMO/08/796 Q5. Note the 21% reduction reflects the proportionately higher percentage contribution by EU ETS sectors to the EU's 20% emissions reduction target than other sectors and is expressed against a baseline of 2005, MEMO/08/796.

subject to modification by the Commission during the detailed implementation phase, in order to meet the overall target of 20% by 2020 against a 1990 baseline.⁴⁸ The cap is then divided among Member States according to emission levels under the ETS and subject to redistribution mechanisms. Emission allowances will increasingly be allocated by auction, in contrast to Phase II where free allocation has been the norm.⁴⁹ It is estimated in aggregate that 50% of allowances will be auctioned from 2013.⁵⁰

Phase III exhibits a higher degree of harmonisation, partly in response to criticism of Phases I and II. This is evident in the EU wide cap being determined by the Commission and harmonised rules for transitional free allocation. Although these measures benefit EU ETS participants by creating a more level playing field, these are achieved by the Commission exercising a higher degree of control in implementing the scheme.

4. The Community Courts' Case Law

In its relatively short life a notable feature of the EU ETS Directive is the sheer number of legal challenges to which it, and Commission Decisions taken under it, has been submitted. By way of (admittedly unscientific) comparison the EU's Regulation (EC) No 2037/2000 on Substances that Deplete the Ozone Layer has generated 25 actions before the Community Courts, the Air Quality Framework Directive (96/62/EC) 17. By comparison the EU ETS Directive has (as at the end of

⁴⁸ MEMO/08/796 Q9

⁴⁹ The limited practice of auctioning is evident from the analysis of past and present auction activity in the EU ETS reported by DG Environment at http://ec.europa.eu/environment/climat/emission/auctioning_en.htm visited 18 March 09 and see also MEMO/08/796 at Q5 which states less than 4% of allowances have been auctioned in Phase II.

⁵⁰ MEMO/08/796 at Q13

2008) resulted in 40 proceedings before the Courts.⁵¹ That number includes procedural actions as well as full judgments and a good number which remain pending. The analysis that comprises the remainder of this chapter organises the caselaw into the following categories: challenges to the validity of the Directive; Article 226 infringement proceedings; Article 230 challenges to Commission decisions on the NAPs in Phase I and Phase II infringement proceedings; and a category of miscellaneous cases.

As to the Community Courts themselves, it should be recalled that the uniform application of Community law requires a Community court system. The European Court of Justice and its inferior court, the Court of First Instance, consist of judges from Member States. The former is the highest judicial authority in the matter of Community law and is, pursuant to Article 220 EC, tasked to “ensure that in the interpretation of [the] Treaty the law is observed.” This entails *inter alia* monitoring the application of Community law both by Community institutions when implementing the Treaties and by Member States and individuals in relation to their obligations under Community law.⁵²

In the environmental context, one issue that has consistently arisen is that of access to the courts for individuals complaining that their ‘environmental’ rights have been infringed and whether adequate ‘judicial protection’ is afforded. This is a particularly pressing issue for individuals’ (including enterprises) actions against decisions of the Commission and whether they are admissible in Article 230 proceedings – a ‘judicial review’ procedure which imposes an

⁵¹ These figures are arrived at by searching the Court’s official case database - <http://curia.europa.eu/jurisp/cgi-bin/form.pl?lang=en> - for the precise citation of the legal instrument. As at 31/12/2008 “2003/87/EC” returned 84 hits, which when ‘cleaned’ to avoid double counting of procedural steps in a single action, arrives at 40 actual actions.

⁵² P Craig and G de Burca, *EU Law: Text, Cases and Materials* (4th Edn OUP, Oxford 2008), 66-76 and EC Treaty art 220, 226-245 and Treaty on European Union art 46.

admissibility test of 'direct and individual concern'. In the environmental context, where the *public* interest, rather than *specific* or *private* interests, commonly dominates the test can be difficult to satisfy.⁵³

4.1. Article 234 Preliminary References Challenging the Validity of the Directive

A critical set of questions arose in the litigation initiated in the French Conseil d'État⁵⁴ which then sought a reference for a preliminary ruling under Article 234 EC in *Société Arcelor Atlantique*.⁵⁵

The applicant is the world's largest volume producer of steel and as such its primary argument is the predictable one that the Directive is discriminatory in its scope of application in that it excludes sectors in direct competition with steel producers such as installations producing aluminium and plastics. They also raised before the Conseil d'État secondary objections, arguing on proportionality grounds that there were limited technical opportunities to reduce emissions beyond those achieved in steel sector since 1990, that their Article 43 EC freedom of establishment rights⁵⁶ were infringed by the Directive, likewise their fundamental property rights and that the Directive imposed obligations with unforeseeable financial implications and as such were inconsistent with legal certainty.

In its ruling the ECJ adopted a narrow interpretive approach, adhering closely to the specific reference question asked of it by the national court, namely whether the Directive was compatible

⁵³ See Jans and Vedder, chapter 5.3.

⁵⁴ 8.02.2007 *Société ARCELOR Atlantique et Lorraine* No. 287110, p.55. For a discussion of the national law implications of this case - which have attracted much comment in France - see J-M Sauve, "Judging the Administration in France: Changes Ahead?", Public Law (2008) 531-545

⁵⁵ Case C-127/07 *Société Arcelor Atlantique et Lorraine and Others v. Commission*.

⁵⁶ One of the 'four fundamental freedoms' of the European Community – along with free movement of goods, persons and services – it comprises the entitlement for economic operators (whether persons or enterprises) to carry on an economic activity in a stable and continuous way in one or more Member States.

with the principle of equal treatment.⁵⁷ This question was answered in the affirmative with reference to the exclusion of the plastics and aluminium sectors with respect to the included steel sector.

In determining the question of equality of treatment the Court first considered the comparability of the situations. This is to be assessed in light of the subject matter and purpose of the Directive and the Court noted that “the possible existence of competition between those sectors cannot constitute a decisive criterion.”⁵⁸ Given the Directive’s subject matter and purpose, differing sources of CO2 emissions are comparable. Sectors of the economy that emit such pollution can therefore contribute to the functioning of the Community trading scheme and so in the instant circumstances (steel versus aluminium and plastics) are in a comparable situation and, in principle therefore must be treated equally. Having established comparability, differential treatment on the part of included sectors is established by virtue of the disadvantages associated with compliance with the Scheme.

At the heart of the judgment lies the debate over justification of this differential treatment. Mindful that comparable situations may be differently treated by virtue of objective and reasonable criteria (proportionate and compatible with the aim of the legislation), the burden is on the Community institutions to (1) demonstrate the existence of a justification and (2) furnish the Court with information enabling it to verify the justification.

⁵⁷ The Court’s approach is certainly defensible in that they addressed the question that was asked of them by the national court, and only that question. However, the Court in such rulings has certainly been known to take a broader approach. There seems to be no consistency in where the Court does not deal with questions put by the litigants in domestic disputes because the national court did not ask the specific question and where it does. Craig and de Burca n. 52.

⁵⁸ Ibid para 36.

To this end the Community institutions submitting observations pointed to the novelty and complexity of the Trading Scheme and the provision for subsequent legislative review in support of its decision to limit the initial scheme to CO₂ and sectors making the most significant contribution to the overall emissions of that pollutant. The Court conducted its review on the basis of these considerations and the evidence set out by the Community institutions in support of its decision in which context, the ECJ reiterated its established general principles of judicial review that: (1) the EC legislator enjoys broad discretion in respect of political, economic and social choices; (2) where the latter choices involve complex assessments and evaluations, the EC legislator may favour a 'step-by-step' approach to regulation; (3) the EC legislator must take into account all the facts and technical/scientific data available at the time in reaching its decisions.⁵⁹ As applied to the Directive, the ECJ thus found that the preferred 'step-by step' approach was within the limits of the legislator's discretion but that the legislator's preferred incremental approach to Emission Trading does not release it from the demands of the principle of equal treatment (i.e. in deciding the order of inclusion in the Scheme etc).

The ECJ then examined the contested sectors individually, examining whether their initial exclusion was in fact justified in accordance with the above principles. In respect of chemicals the ECJ accepted that exclusion could be objectively justified and in particular that the relatively diffuse nature of the sector would impose a significant administrative burden were it to be included, and that the advantages to the scheme of including this sector from the outset may not have outweighed the difficulties. Exclusion from the Scheme was thus justified on the basis of 'administrative feasibility'. The ECJ also accepted that exclusion could be objectively justified for the aluminium sector and that the legitimacy of 'administrative feasibility' again meant that the

⁵⁹ See paras 57-59 *ibid* for authorities cited.

legislator was not required to base its decisions solely on a threshold for emissions. However, the Court's reasoning here differs from that underpinning its appraisal of the chemical sector. The justification for the exclusion of the aluminium sector is not considered in isolation. It is not simply a review of a cost-benefit analysis as in the former case. The Court refers to the respective total emissions of both the aluminium and the steel sector:

The difference in the levels of direct emissions between the two sectors concerned is so substantial that the different treatment of those sectors may... be regarded as justified.⁶⁰

The distinction in the Court's approach is of course very subtle. In effect, the ECJ's appraisal of the exclusion of aluminium sector also comes down to a cost-benefit analysis. However, the question is why is the ECJ 'comparing' the two sectors in its reasoning if competition considerations are excluded?⁶¹ It is unclear why this is not irrelevant for the assessment of whether or not the exclusion of that particular sector could be considered objective justified within the bounds of the legislator's discretion. It appears that the Court cannot shake off 'competition concerns' absolutely.

4.2. Article 230 Challenges to Commission Decisions on the National Allocation Plans

In terms of volume, it will be no surprise that challenges to Commission decisions on NAPs form that largest part of the Courts' EU ETS docket. Such annulment actions are addressed by phase in the below analysis, and chronologically within phase.

⁶⁰ Ibid para 72.

⁶¹ Ibid para 36.

4.2.1. Phase I Challenges

The first of these actions issued from the UK in late 2005, with the United Kingdom raising an action for annulment of the Commission's refusal in a letter to consider amendments to the UK's original NAP to increase its allowance.⁶² The UK maintained that its original NAP was merely 'provisional' while the Commission adopted a Decision in respect of the original NAP and rejected the UK's amendments. The core question was whether the Commission was entitled to reject as inadmissible amendments to allocations submitted by a Member State after publishing a Decision on the NAP?

The Court of First Instance held that Commission may not restrict a Member State's right to propose amendments to its NAP prior to that Member State issuing a definite decision on its allowances and allocations under Art 11(1) (By implication this applies to Phase II and beyond under Art 11(2) of Directive). Any amendments to a NAP made by a Member State must be notified and accepted by the Commission before they may form the basis for the Member State's final decision under Art 11(1) of the Directive. The contested Decision was thereby annulled. The CFI's decision is supplemented by a series of important comments on the respective roles and powers of the Commission and the Member States under the Directive, in particular that the Commission's review under Art 9(3) is strictly limited to an assessment of NAP against the criteria articulated in Art 10 and Annex III of the Directive - there is "no other ground for rejection."⁶³ The Commission is not entitled to restrict amendments to a NAP to those necessary to overcome incompatibilities it identified in its Decision on that NAP - Article 9(3) does not set out any such

⁶² Case T-143/05 United Kingdom v. Commission (joined with T-178/05), Case T-178/05 United Kingdom v. Commission. (CFI 23 November 2005).

⁶³ But note comments of CFI in the subsequent ruling in Case T-374/04 Germany v. Commission (below) in which the Court stated that Member States may base their NAPs on criteria other than Annex III where such are transparent and objective. It is then for the Commission to demonstrate that such infringe the Directive and/or EC law.

limits to the permissible amendments Member States may make to their NAP. Particular attention is drawn to the public consultation process in Article 11, which would be rendered meaningless if amendments were limited to correcting incompatibilities identified by the Commission in its Decision. Member States may propose amendments after expiry of the Commission's 3 month review period and any such amendments are still subject to the Commission's (limited) review and, in any case, must be made before the Art 11(1) decision is taken. The ruling appears to 'clip the wings' of the Commission which perhaps sought to carve out a more dynamic role for itself in the NAP process. The CFI rejected its arguments on economic stability as 'unsubstantiated' and 'at the very least, exaggerated.' The Commission is not entitled to constrain Member States in the exercise of their rights and as such is limited to reviewing only NAPs and amendments against Art 10 and Annex III.

The CFI's ruling in *EnBW Energie Baden Württemberg v. Commission*⁶⁴ has had an even greater direct impact on Courts' jurisprudence in this area. The case arose from the disgruntled German power station operator's challenge to one of the specific 'ex post' transfer rules in the German NAP under which an operator decommissioning an old power plant and replacing it with a (cleaner) new one may continue to enjoy the (larger) allowance it had in respect of the older plant for 4 years. The applicant argued that transfer rule constituted illegal State Aid and that its principle rival, RWE, would acquire, free of charge, excessive allowances under the transfer rule owing to its replacement of conventional installations. These allowances it may sell on the market, conferring an unjustified competitive advantage on that operator. With several nuclear installations to decommission, the applicant operator would not benefit in a like manner. Its additional allowance was thereby capped.

⁶⁴ Case T-387/04, (CFI 30 April 2007).

The Commission's response – as might have been anticipated - was to raise a plea of inadmissibility,⁶⁵ with Germany intervening to support this plea. This is the first case to rule on the admissibility of Art 230 EC actions by individuals against Commission Decisions on NAPs pursuant to Art 9(3) of the Directive. The CFI found the application inadmissible for want of locus standi. According to established case law, Article 230 EC requires that annulment of Decision would itself confer an advantage on the applicant, i.e. would result in contested NAP/transfer rules no longer enjoying authorisation, but the CFI found that the Commission does not enjoy a general power of authorisation under Art 9(3) of the Directive - the NAP is presumed lawful, subject to Commission's review against Art 10/Annex III. The CFI stated that the purpose of Commission review procedure is to provide legal certainty for the Member States, resolve disputes quickly and to ensure that, during the relevant trading period, the NAP doesn't risk being challenged by the Commission under Art 226 EC. It is the decision of the Member State itself, pursuant to Art 11(1) of the DIR, that affects the legal status of the individuals concerned. With no need for general authorisation by Commission and its contested Decision not affecting the rights of the applicant, the applicant does not have locus standi, leading to a finding of inadmissibility.

This concept of 'direct concern' for the purposes of Art 230(4) EC as articulated in *EnBW Energie Baden Württemberg v. Commission* is very much the orthodox position of the Court, though this is not to say that it is uncontroversial. The ECJ had recently affirming this very restrictive interpretation of 'direct concern' in *Union de Pequenos Agricultores v. Council*.⁶⁶ In so doing, the ECJ rejected Advocate General Jacobs' attempt to broaden standing and in the subsequent case

⁶⁵ For the established case law on this question, see Jans and Vedder, n.1 at 209-214.

⁶⁶ Case C-50/00 [2002] ECR I-6677.

of *Jego-Quere*⁶⁷ the ECJ also, implicitly, overruled the CFI's more cautious attempt to loosen the test. This remains a controversial area in general, with serious concerns over the adequacy of the Community system of legal protection.⁶⁸

EnBW Energie Baden Wurttemberg v. Commission casts a long shadow over the EU ETS case law. In *Drax Power and Others v. Commission*⁶⁹ the operators of the UK power station sought an annulment of Commission's revised (post T-178/05) Decision on the UK NAP, alleging the Commission's Decision contradicted the CFI's ruling in Case T-178/05, that the Commission wrongly concluded that 30th Sept. 2004 was cut-off point for amendments to NAP by Member States (that is, 3 months before the deadline in Art 11(1) for final decision by Member States based on NAP). The Commission again raised a plea of inadmissibility and the CFI again reiterated its conclusions in *EnBW Energie Baden Wurttemberg* - that it is the decision of the Member State under Art 11(1) of the DIR that 'directly effects' the legal situation of the applicants. Inadmissibility again followed. Similarly in *U. S. Steel Košice v. Commission*,⁷⁰ where the monopoly steel producer contested the Commission Decision on the Slovakian NAP. The primary objection is that Commission abused its powers of review under Art 9(3) of the DIR. Following the submission of the NAP, the Commission and the Slovakian Government entered into bi-lateral negotiations, with Commission pushing for reduction in the total allowance submitted. Slovakian representative then accepted a reduction (in a letter), which brought its total within its Kyoto Protocol commitments. The Commission raised plea of inadmissibility for want of locus standi, reasoning as above in *EnBW Energie Baden Wurttemberg*. The CFI stated that there was nothing in the Directive in principle to

⁶⁷ Case C-263/02, on appeal from the CFI.

⁶⁸ See generally Craig and de Burca, 509-528.

⁶⁹ Case T-130/06 (25 June 2007).

⁷⁰ Case T-489/04 (1 October 2007).

prevent bilateral negotiations between the Commission and Member States after NAP submitted and prior to Commission Decision. Also, even if it did affect the legal status of applicant directly, CFI held the Commission's Decision was not of direct and individual concern to the applicant. Again, the decision granting rights to individual installations is made by the Member State under Art 11 of the DIR. The only remedy for the applicant, where appropriate, is before national courts under national law.

A rather different set of issues arose in *Germany v. Commission*.⁷¹ The focus here is specifically on the provision in the German NAP for 'ex post allocation adjustments' which may be made in certain defined cases to correct intervening over-allocations (i.e. where an operator winds-up an installation). The Commission Decision declared these provisions of the NAP incompatible inter alia with point 10 of Annex III of the Directive.⁷² It was argued that allocations to individual installations must be determined in advance and may not be subsequently reallocated after a Member State makes its final decision under Art 11(1) of the Directive. The Commission also declared that the provisions on ex post adjustment for new entrants were discriminatory, favouring this group, contrary to criterion 5 of Annex III.⁷³

The CFI started from the position that, as a Directive, 2003/87 EC leaves to the Member State the choice of form/method to achieve the binding result it prescribes (see Article 249). Contested 'ex post adjustments' are not covered by the Directive and so in principle, it falls within Member State competence to provide such, subject to Commission demonstrating that they infringe the

⁷¹ Case T-374/04 (7 November 2007).

⁷² The Directive, Criterion 10 of Annex III: "the [NAP] shall contain a list of the installations covered by this Directive with the quantities of allowances intended to be allocated to each".

⁷³ The Directive, Criterion 5 of Annex III: "The [NAP] shall not discriminate between companies or sectors in such a way as to unduly favour certain undertakings or activities in accordance with the requirements of the Treaty, in particular Articles 87 and 88 thereof."

Directive/EC law. The CFI examined literal, historical, contextual and teleological interpretations of the criterion, finding that Art 11(1) does not expressly exclude such adjustments and that Art 9(3) also permits Member States to base NAP decisions on criteria other than Annex III where such are transparent and objective. Commission guidelines on Annex III also do not expressly exclude possibility of ex post adjustments. The Court's central focus was on teleological interpretation - whether the Directive's objectives and sub-objectives preclude the possibility of 'ex post adjustment' mechanism. The CFI found that, in principle, ex post adjustments linked to relatively small reductions in production output may frustrate the Directive's objective, as such deter installations from reducing production, but that Commission has not submitted evidence to this effect. With respect to the Commission's finding of discrimination contrary to criterion 5 of Annex III for the 'new entrants' rule, the CFI repeats the principle of non-discrimination (that comparable situations must not be treated differently...) and found that Commission has made only general statements and not shown that installations concerned are comparable or different. Finally, CFI confirmed the fundamental nature of the duty to support Decisions with adequate reasoning in Art 253 EC, which it views as finding specific expression in Art 9(3) of DIR 2003/87 EC. Accordingly the CFI found an infringement and was generally highly critical of the lack of evidence advanced by the Commission in support of its objections. The Commission Decision was annulled.

Other cases relating to Phase I were, at the time of writing still pending. Both *Romania v. Commission*⁷⁴ and *Bulgaria v. Commission*⁷⁵ are applications for annulment of Commission Decision on NAPs, for the year 2007. Both applicants argue that the Commission infringed Arts. 9(1), (3) and 11(2) by determining unilaterally, and in accordance with its own method, the total

⁷⁴ Case T-484/07.

⁷⁵ Case T-500/07.

allocation for Romania and Bulgaria respectively. This is the key objection which finds repeated expression in pending references (see the applications which follow below).⁷⁶ A single Phase I case was removed from the Register - *Associazione Italiana Tecnico Economica del Cemento and Others v. Commission*⁷⁷ in which the applicants contested Commission Decision on the Italian NAP for the first trading period, claiming it sanctioned State Aid contrary to Art 87 EC (also point 5 of Annex III).

4.2.2. Phase II Challenges

The spectre of admissibility and challenges to NAPs feature even more strongly in Phase II than I. Given the Court's long standing caselaw on such matters, the reasons for such actions are not transparent, although suggestions are made in the conclusion below.

The formula that 'Commission Decision do not affect the legal situation of the applicant for the purposes of Art 230 EC' is repeated with some regularity in the Phase II caselaw, starting with *Fels-Werke GmbH and Others v. Commission*⁷⁸ in which the applicant sought an annulment of part of Commission Decision on German NAP declaring its provisions on 'allocation guarantees' incompatible with Annex III. The applicant argued that the Commission misapplied Annex III and that the guarantees do not constitute State Aid. The Commission's plea of inadmissibility was granted by the CFI on the 'usual terms', and was upheld in the applicants appeal to the ECJ in *Saint-Gorbain Glass Deutschland GmbH and Others (FelsWerke...) v. Commission*.⁷⁹

⁷⁶ The Bulgarian cases also raises the following objections pertaining to the infringed duty of loyal cooperation (EC Treaty art 10), the Decision being delivered after expiry of 3 month deadline, and that the Decision is insufficiently reasoned.

⁷⁷ Case T-371/05.

⁷⁸ Case T-28/07 (11 September 2007).

⁷⁹ Case C-503/07 (8 April 2008).

In *U. S. Steel Košice v. Commission*⁸⁰ the monopoly steel producer sought an annulment of Commission Decision on Slovakian NAP arguing, as above, that the Commission exceeded its authority under Art 9(3), conducting its own assessment to determine the total emission allowance for that Member State. The applicant claimed the Commission's misuse of its powers was motivated by a desire to achieve a scarcity of resources to increase the market price of tradable allowances.⁸¹ Specific to the position of the Slovak Rep, the applicant contested the Commission's interpretation of the conditions for the provision of State Aid to the applicant pursuant to Title 4 point 2(a) of Annex to Accession Treaty. This provision sanctions State Aid to the applicant until end of fiscal year 2009 up to a maximum of \$500m and is conditional on production limits. The Commission argued that the production limits continued to apply irrespective of whether or not the maximum aid amount is reached before the end of the fiscal year 2009. As well as granting the Commission's plea of inadmissibility on the usual terms, the CFI also rejected the argument that the Decision constituted a reviewable Decision on the application of the Treaty provisions on State Aid. The Commission's review under Art 9(3) was held to be only a provisional assessment and not a Decision for the purposes of Art 87 EC.⁸² Near identical claims were made, and rejected on near identical grounds in the cases of *CEMEX UK Cement v. Commission*.⁸³ Further, a set of actions seeking the annulment of the Commission Decision on the Polish NAP all raise similar arguments and while they have not been joined formally, they were

⁸⁰ Case T-27/07.

⁸¹ A similar argument is made by P Street, *Environmental Law Review* (2007) 268-9, noting the political pressure exerted by the Commission, particularly in respect of the Commission's Phase II NAP review, in his critical assessment of the EU ETS.

⁸² The appeal to the ECJ against Case T-27/07 (19 June 2008), *U.S. Steel Košice v. Commission* Case C-6/08P, was dismissed on the basis that it is only when the Member State adopts a definite decision under Art 11 that an operator is legally granted a specific quantity of rights. Therefore the Commission's Decision does not affect the legal situation of the applicant for the purposes of Art 230 EC.

⁸³ Case T-13/07 (7 November 2007). The sought annulment by the cement producer to the Commission's Decision on the UK's phase II NAP alleged that Commission did not object to (i.e. approved) an under-allocation by the UK to the applicant in respect of one its plants, thereby discriminating in favour of cement manufacturers in competition with the applicant and constituting illegal State Aid. As a consequence, *CEMEX UK Cement v. Commission* Case T-313/07 was removed from the Court's register.

heard on the same date and dismissed as inadmissible, on the usual terms, by Order of the CFI on 23rd September 2008.⁸⁴

The application by multiple Polish energy companies (and supported by more of them) in *BOT Elektro Belchatow and Others v. Commission*⁸⁵ was dismissed as inadmissible. Following earlier rulings post *T-387/04 EnBW Energie Baden Wurttemberg*, the Court reiterated that it is the decision of the Member State pursuant to Art 11(2) of the DIR that affects directly the legal situation of the applicant. The fact that the latter – national – authority must comply with the Commission Decision on the NAP does not alter this fact.⁸⁶ This is a rather formalistic mode of reasoning. The Court's remarks at Para 49 are entertaining in this context:

The fear expressed by the applicants that the size of the reduction, as approved by the contested Decision, in the total quantity of allowances would necessarily lead to a proportional reduction in their individual allowances refers to an entirely hypothetical event.

The Court further examines the second criterion of Art 230(4) - the requirement that the measure leaves the addressee no discretion in its implementation. Here the CFI held that Member States do retain a margin of appreciation in that they can submit amendments to the Commission and remain free to impose stricter limits than those approved by the Commission (citing Art 175-6 EC as authority for the latter)!

⁸⁴ *Gorażdże Cement v. Commission* Case T-193/07 (23 September 2008). The argument was that Commission infringed Arts. 9(3) and 11(2) and inter alia the principle of cooperation by applying its own method to determine Poland's total allocation and imposing this on Poland. In effect, this restricted Poland's total allowance to a level markedly lower than that notified, which had been consistent with that Member State's Kyoto obligations. The other dismissed cases were Case T-195/07 *Lafarge Cement v. Commission*, Case T-196/07 *Dyckerhoff Polska v. Commission*, Case T-197/07 *Grupy Ożarów v. Commission*, Case T-198/07 *Cementownia "Warta" v. Commission*, Case T-199/07 *Cementownia "Odra" v. Commission*, Case T-203/07 *CEMEX Polska v. Commission*.

⁸⁵ Case T-208/07, (20 October 2008).

⁸⁶ *Ibid* paras 33-35.

The following Phase II annulment actions remained pending as of January 2009 - Czech Rep v. Commission,⁸⁷ Hungary v. Commission,⁸⁸ Estonia v. Commission,⁸⁹ Latvia v. Commission,⁹⁰ Lithuania v. Commission,⁹¹ Romania v. Commission,⁹² Buzzi Unichem v. Commission,⁹³ and Poland v. Commission.⁹⁴

⁸⁷ Case T-194/07. Annulment sought of Commission Decision on its NAP on the basis that the Commission had exceeded its authority and infringed Arts 9(3) and 11(2) by applying its own method for fixing the maximum quantity of allowances for that member state.

⁸⁸ T-221/07. Annulment sought of Commission Decision on its NAP on the basis that Arts 9(3) and 11(2) of DIR do not empower Commission to determine unilaterally the total quantity of emissions member state may allocate

⁸⁹ T-263/07. Annulment sought of Commission Decision on its NAP on the basis the Commission had infringed Arts 9(3) and 11(2) by making manifest errors of assessment, relied on false assumptions and did not verify its data.

⁹⁰ T-369/07. Annulment sought of Commission Decision on its NAP on the basis the Commission had failed to publish its Decision within 3 month time limit infringing Art 9(3), that Commission's expansive interpretation of Art 9(3) has encroached on its right to determine unilaterally its domestic energy policy, contrary to Art 175(2)(c) EC, that the Decision infringes criterion 1 of Annex III (not taking into account Latvia's Kyoto obligations) and finally, infringement of non-discrimination on nationality (from the perspective of member states) in that the Commission's methods disadvantage member states with low emissions.

⁹¹ T-368/07. Annulment sought of Commission Decision on its NAP on the basis that Commission had been delivered after the 3 month period, infringing Art 9(3), the Commission had exceeded its review power by overlooking NAP + Kyoto and unilaterally determining total allowance in line with its own methods.

⁹² Annulment sought of Commission Decision on its NAP on the basis the Commission infringed Arts. 9(1),(3) and 11(2) by determining, in accordance with its own method, the total allocation for Romania

⁹³ T-241/07. Annulment sought of Commission Decision on the Italian NAP contesting the Commission's objection to the provision for ex-post allocation adjustments in the NAP, according to which installations may retain allowances in respect of plant closures due to product rationalisation, i.e. transferring rights to remaining installations.

⁹⁴ T-183/07. Annulment sought of Commission Decision on its NAP on the basis that the contested Decision reduces the total CO2 limit proposed by Poland in its NAP by 26.7%, infringing the procedural demands of Art 9(3) as its Decision was taken after the expiry of the 3 month period, that Commission substituted its own facts for those submitted in the NAP obtained by an inconsistent application of its own preferred economic model, that the Commission also failed to take into account the binding Kyoto Protocol in reaching its Decision, contrary to criteria 1, 2 and 12 of Annex III, that the Commission exceeded its powers in limiting the transfer of rights from Phase I to Phase II, that the Commission's failure to consult with it and not take its energy concerns into account affects Poland's energy security. The application for interim measures was rejected by the CFI for want of urgency (T-183/07 R) and the applicant subsequently sought suspension of measures in respect of Commission's Decision, rejecting its NAP. Judgment on merits still pending the ECJ.

4.3. Miscellaneous Cases

For the sake of completeness⁹⁵ two further categories of cases require brief consideration, although neither has implications for the operation of the EU ETS as such.

The first category comprises *Abraham and Others v. Region Wallonne and Others*⁹⁶ and *Evropaiki Dynamiki v. Commission*.⁹⁷ The former concerns Directive 85/337 EEC on environmental impacts assessments for infrastructure projects and cites *United Kingdom v Commission*⁹⁸ in the context of public participation affecting project decisions; the latter's applicant sought an annulment of the Commission's decision to award the contract to another tenderer following the rejection of its tender for support services for the system of registries established under Directive.

4.4 Infringement Proceedings

The second set of marginal cases concern infringement proceedings, both successfully brought by the Commission under Article 226 EC, seeking declaration that Member States have failed to fulfill their obligations under Directives. The Court made such declarations against Finland and Italy owing to the non/incomplete transposition of the Directive within deadline prescribed in Article 31.⁹⁹

⁹⁵ See the methodology outlined in n.41.

⁹⁶ Case C-2/07.

⁹⁷ Case T-406/06. Dismissed by the CFI.

⁹⁸ Case T-178/05, see n.43.

⁹⁹ Case C-107/05 *Commission v. Finland* and Case C-122/05 *Commission v. Italy*

5. Conclusions

There has been a veritable “explosion of climate change litigation in subnational, national and supranational tribunals under a wide range of substantive legal approaches”¹⁰⁰ in recent years. For lawyers and legal scholars this has generated temporal challenges as past and present emissions result in future impacts, as well as geographical and jurisdictional complexities. It has manifested itself in a great variety of claims including attempts to protect the skiing industry of New England,¹⁰¹ the Inuit culture,¹⁰² the Californian coastal natural heritage¹⁰³ and most famously perhaps whether CO₂ is indeed an air pollutant for the purposes of the US Clean Air Act and how this determination ought to be made.¹⁰⁴ The implications of this litigation for national and international law is gaining increasing systematic attention,¹⁰⁵ and its spillover effects into international negotiations.¹⁰⁶

Such litigation stands in marked contrast to the rather technical foregoing analysis of the Community Courts’ EU ETS docket. This is explained in part by the fact that much climate change litigation is “impacts” oriented and as such claimants are casting around for established legal tools (international human rights law, torts, administrative judicial review, takings and expropriation etc.) that might be deemed to be applicable for the novel nature of claim they are making. The EU ETS litigation is not concerned with the impacts of climate change (declining snow packs, costs of

¹⁰⁰ HM Osofsky, “Climate Change Litigation as Pluralist Legal Dialogue?” 43 *Stanford Journal of International Law* (2007), 181 at 184.

¹⁰¹ *Connecticut v. American Electric Power Co.*, 406 F. Supp. 2d 265 (S.D.N.Y. 2005)

¹⁰² An Inuit Petition to the Inter-American Commission on Human Rights for Dangerous Impacts of Climate Change (2004), available at http://www.ciel.org/Publications/COP10_Handout_EJCIEL.pdf

¹⁰³ *California v. General Motors Corporation.*, 2007 WL 2726871 (N.D. Cal. Sept. 17. 2007).

¹⁰⁴ *Massachusetts v. EPA*, 127 S. Ct. at 1462.

¹⁰⁵ See inter alia Osofsky supra; WCG Burns, “Potential Causes of Action for Climate Change Damages in International Fora: The Law of the Sea Convention”, 1(2) *Journal of Sustainable Development Law & Policy* (2006), 27-51.

¹⁰⁶ DB Hunter, “The Implications of Climate Change Litigation for International Environmental Law Making” *American University Washington College of Law Research Paper No. 2008-14*.

adaptation to sea level rises etc) but rather the finessing of a new market mechanism from the perspective of key market actors within the established confines of EU law. Accordingly, traditional doctrines of non-discrimination, equal treatment, locus standi and legal certainty have come to the fore. What is less traditional is the sheer volume of litigation that the Directive has attracted in its short life. This might be explained as a classical ‘interest group theory of politics’¹⁰⁷ scenario, whereby a small number of well resourced actors affected by a regulatory change can be anticipated to organize themselves to respond to and challenge that change. Such an approach may explain the Arcelor litigation but it does not explain the slew of actions post-EnBW Energie.¹⁰⁸ Having been established that the Court’s conventional, restrictive, approach to standing in judicial review actions applied equally to challenges to Commission Decisions on NAPs, it would be clear that any subsequent challenges on this basis would similarly fail. However, the challenges continued despite their near-zero prospects of success and the ‘interest group theory of politics’ provides no clues as to why. When looking at the Member State source of challenges and the deepest of Phase II cuts, a certain degree of overlap emerges with Poland, Germany, Bulgaria and the Baltic states all featuring in both categories. Accepting the possibility that market actors in the energy, minerals and ferrous metals industries have been ‘encouraged’ by their national governments to challenge decisions, there is perhaps an element of both playing to national audiences (against ‘Brussels’ and ‘Europe’) and seeking to pressurize the Commission’s decision making processes – the latter strategy at least seems to have been singularly unsuccessful.

¹⁰⁷ See M Olson, The Logic of Collective Action (Harvard University Press, Cambridge MA, 1965). An alternative approach might be to view the challenges as instances of ‘voice’ on the part of actors who have no possibility of ‘exit’ from the EU (given their sunk costs) and regardless of their ‘loyalty’ – see AO Hirschman, Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States (Harvard University Press, Cambridge MA, 1970).

¹⁰⁸ Case T-387/04.

The changes to the Scheme brought about by Phase III amendments play interestingly into these questions. It is clear that there is a significant relationship between the case law findings and the challenges of EU enlargement. A disproportionate volume of the above challenges issue from the ‘new’ EU Member States (the ‘EU-10’) which in many cases have struggled to adapt their ageing industrial stock to the requirements of the EU’s ambitious energy and climate change policies. To this end, Phase III’s scheme for the auctioning of allowances makes provision for ‘redistribution mechanisms’ by which 10% of allowances are to be redistributed to low per capita income Member States as a solidarity mechanism.¹⁰⁹ It is not fanciful to infer that such a concession is a response to the EU-10 grievances expressed in part by the EU ETS case law.

In addition to those powers noted above, Phase III allocates even broader powers to the Commission, notably in the context of the new auctioning provisions. Auctioning will be introduced in stages, beginning with the electricity generation sector which will be subject to 100% auctioning from 2013. Optional and temporary derogations will exist for certain Member States,¹¹⁰ allowing for auctioning to build up from a minimum of 30% to 100% during Phase III and conditional upon modernising generation plant and infrastructure¹¹¹ which also bleeds into the ‘enlargement question’. For other sectors auctioning is to begin at 20% in 2013, reaching 70% in 2020 and 100% by 2027.¹¹² The Commission will develop and adopt harmonised rules for

¹⁰⁹ MEMO/08/796 Q7. A further 2% of allowances are redistributed to those Member States which had achieved early progress against Kyoto Protocol reduction targets and proceeds of auctioning 300m allowances are to be set aside to subsidise the development of carbon capture and storage demonstration plant, or other innovative renewable energy technologies. This is possibly the first EU revenue raising mechanism of any sort and a notable example of fiscal hypothecation.

¹¹⁰ The derogation is determined upon criteria including the interconnectivity of electricity grids, share of fossil fuels on generation mix and GDP/capita, from MEMO/08/796 Q7

¹¹¹ MEMO/08/796 Q15

¹¹² MEMO/08/796 Q7, Q15

transitional free allocation by comitology by 31 December 2010.¹¹³ Exceptions for sectors at risk of carbon leakage are to be assessed and determined by the Commission¹¹⁴ with these sectors to receive 100% free allowances. The Commission will review these provisions (and level of free allowances) following any international agreement reached at COP15 to determine their impact e.g. of sectoral agreements.¹¹⁵ In all these areas the Phase III arrangements have granted to the Commission a raft of new decision making powers in critical areas of policy – environmental, economic and industrial.

At the time of writing – less than three months after the agreement of Phase III – the consensus contained therein is already unravelling. Whilst Phase III was adopted as part of wider energy and climate package which emphasised issues of energy security and the EU's wider strategic external relationships, the deepening global recession has generated stronger budgetary pressure on Member States and weakened the political compact which existed in December 2008.¹¹⁶ How this manifests itself is inevitably a matter of conjecture but candidates might include Member States' (1) pressure on the financing elements of the package (e.g. subsidies for renewable energy, CCS and investment in large scale strategic infrastructure projects), (2) demands for wider definitions of sectors at risk of competitiveness issues and carbon leakage and (3) limits on the EU's level of ambition for the UNFCCC negotiations.

¹¹³ MEMO/08/796 Q14. These will rely on benchmarks for process technologies, favouring carbon efficient technologies.

¹¹⁴ MEMO/08/796 Q15

¹¹⁵ MEMO/08/796 Q15

¹¹⁶ See conclusions from the Environment Ministers' and EcoFin meetings (respectively http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/envir/106429.pdf and http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/106572.pdf) in February/March 2009 and the Spring Council, 19-20 March 2009.

In the face of such pressures the restrictive interpretation of the ECJ, particularly in respect of the admissibility issue, takes on a different light. What might have appeared to be a highly formalist Court, adhering to sometimes obscure procedural rules might instead be characterised as one committed to holding Member States to their political compacts. For the purposes of creating a stable market, such an approach generates a substantial certainty dividend. Attempts to dilute or resile from these commitments in Community Courts – whether raised by Member States or enterprises in their territories – will not be encouraged by the Courts' 'bullet proofing' of the Commission and its decisions. The extension of the Commission's powers by Phase III thus creates a position of some certainty in a market (like many others, perhaps) where there has been precious little.