

30 May 2019

FICIL's Position Paper on Energy Sector and Waste Management Policy

1. Executive Summary

Energy is in transition, when competing for international investment attraction to Latvia, national targets, clear framework, consistency and predictability will be of high importance. Across all industries policies, laws and regulations of a state need to be consistent, predictable and oriented towards the development and prosperity of a state. The presence of the above described values and principles in Latvia is one of the core concerns of the Foreign Investors Council in Latvia (FICIL), when preparing this position paper. Unfortunately, several events relating to the energy sector, which took place during the last year, and their consequential developments have risen concerns about the stability, predictability and quality of the policies, laws and regulations being implemented in Latvia, and about the monolithic nature of the rule of law in Latvia.

FICIL continues to stress that statistics, as well as comprehensiveness, reliability and public availability of statistical data in a user-friendly format continue to be an area of general concern in energy and waste management sectors, as well as in other areas of the economy. FICIL urges the government to make considerably wider use of big data and artificial intelligence solutions. This would help bringing policy making closer to the real-life situation. State policy would become more consistent, predictable and qualitative.

The quality and level of development of the National Energy and Climate Plan 2021 – 2030 (Plan) rises considerable concerns. Several of the activities listed into the Annex 4 to the Plan are not transparently analysed in the main text of the Plan. Due to this it is not clear whether these activities are considered into the calculations and forecasts of the plan. Also, some of the suggested activities, like, liberalisation of the heating system and shift to the use of renewable energy sources and electric power for the heating purposes, require discussion and coordination in the implementation with the revision of the mandatory procurement of electric power (MP system).

In the previous year, FICIL urged for consistency and predictability in decisions when considering MP system reform. Unfortunately, this was not the case. In fact, January 10, 2019 resolution of Saeima urging for abolition of the MP system as of March 31, 2019 negatively affected the investment environment of Latvia. FICIL urges for the qualitative in-depth revision of the MP system. During this process the interests of the state, end consumers, industries (especially energy intensive industries) and energy sector should be well balanced and safeguarded to the extent reasonably possible. In addition, this process should be harmonised with the suggested liberalisation of the heating system.

When it comes to the waste management sector, FICIL raises concerns with the Waste Management Plan for the coming 7 years, which has to be currently elaborated. EU has recently published its Early

Warning Report, in which Latvia is identified among those Member States, which are on the list not to achieve mandatory targets on the municipal waste management. It is important that Latvia finally selects and introduces sufficient and qualitative legal framework for the implementation of the single-use plastics related policies. There are several binding EU targets to be met. The waste collection and recycling systems, which could lead to the attainment of these targets, still require time for planning, putting into operation. Therefore, it is urgent for the government to make the necessary decisions and introduce legal framework to solve this issue.

FICIL urges government to refuse from as heavy dependence on the subsidies (especially in the energy sector) as it has been in Latvia so far. Transition to the business reasonably based in the core market principles, and self-sustainability of businesses should be put as the goal for the closest five years. This stems both from the general principles of fiscal discipline, as well as from the maturity level reached by the state, legal framework and market.

2. Recommendations

1. Modernisation of Statistics used in planning policies in energy and waste management sector.

There is a need for improvement of data reporting and processing. Proper use of the big data and artificial intelligence solutions could help identifying and analysing data gaps and overlaps, reduce administrative burden currently held by each state or municipal institution, as well as help avoiding overlapping in the information to be submitted by the private sector to state and municipal institutions. Reductions in the reporting in combination with the ease of the reporting tools could increase the aggregate amount of data actually reported.

2. Thorough reassessment of the National Energy and Climate Plan 2021-2030

Being a long-term policy document, the Plan should be meaningful with clear goals in line with EU requirements. It must take proper account of the diverse and dynamic sectoral developments, lessons learned so far, and various targets lying ahead. Incorporation of the main waste management issues into the Plan is strongly advised to allow for more reasoned, circular economy-based approach in projections and forecasts of the energy and climate sector. Both of them are inextricably dependent on the waste management policies and instruments. FICIL recommends that the main text of the Plan is substance wise improved to demonstrate expressly the place, sequence in performance and the potential value-added to be provided by all actions listed in the appendices of the Plan. It is important, that cross factors, pros and cons, as well as overlaps and contradictory effects of the planned activities are properly admitted, calculated and included into the forecasts of the Plan. Furthermore, FICIL recommends that the Plan is being publicly discussed in detail with the stakeholders following receipt of the EU Commission recommendations thereto.

3. In-depth revision of the MP system and potential further support for renewable sources of energy

Irrespective of the future result (full or partial abolition or transformation of the MP system), these types of actions need to be carried out in a transparent and predictive manner, as to not negatively affect the investment environment of Latvia. To achieve and maintain a stable and transparent investment climate, the underlying principles of the investment protection, legal stability and predictability require that resolutions of this scale and potential consequence are well-prepared and counter-balanced.

4. Implementation of the deposit system and Single-use Plastics Directive

FICIL represents various companies from food and drink industry that will be affected by the Single-use Plastics Directive (SUPD). FICIL believes that Ministry of Environmental protection and Regional Development (VARAM) has to proactively engage with the food and drink industry

in order to effectively implement the SUPD to meet the set targets and avoid a negative effect on the industry. ALL relevant policies should be carried out considering the existing costs of producer responsibility schemes, and connected to the industry's contribution via financing and public awareness initiatives.

5. Turning waste into resource by promoting material and energy recovery

Using residual waste flows as fuel is in the long term a facilitator to recovery, enabling efficiency and better recycling economy. As mentioned in the previous position paper on the energy sector, FICIL recommends focusing on the following for promotion of material and energy recovery:

- Decisively and actively close the possibility to landfill materials that can be recycled or re-used;
- Accessible and transparent RDF (refuse-derived fuel) market, with an open market and qualitative market for waste management services;

6. Advance sustainable financing models

FICIL contributes to the promotion of the opinion, that financial resources of the state budget should no longer be the first at hand resource to stimulate development and operation of the private sector businesses, especially in the energy and waste management area. It is important that wider use is made of the different financial instruments, for instance, structured instruments, project bonds, pension funds. Sustainable finance principles, which in essence are close to the main principles of the fiscal discipline, shall be advertised and used. This calls for the need to continue improving the legal framework to allow for the stable, long-lasting and predictable framework for this type of financing.

3. Rationale for recommendations

Statistics

FICIL continues to stress that statistics in energy and waste management areas, as well as comprehensiveness, reliability and public availability of statistical data in a user-friendly format continue to be an area of general concern. FICIL urges the government to make considerably wider use of the big data and artificial intelligence solutions. Statistical data on energy and waste management related issues as well as in other areas, which are at the disposal of the Central Statistical Bureau of Latvia should be substantially improved.

First, all market participants should be urged to timely and regularly submit the required data. This is an essential form, in which private sector can provide a valuable input into the policymaking. Second, to the extent possible the enormous amount of data being at the disposal of the state and municipal institutions should be timely and regularly transferred to the Central Statistical Bureau of Latvia. This would help increasing the comprehensiveness of the data. Third, government should regularly use statistical data both to plan and structure new policies, and to update or revise on a regular basis the existing policies. This would bring policymaking closer to the real-life situation and contribute to the more consistent, predictable and qualitative policymaking.

National Energy and Climate Plan 2021 – 2030

In its previous position paper, FICIL encouraged Ministry of Economics to timely involve stakeholders in the engineering of the National Energy and Climate Plan (Plan). Well-structured dialogue with the stakeholders is a key to develop a viable long-term policy document. With regret FICIL must admit, that this was not the case. For instance, a widely attended conference was organised, when practically all places of the Plan to contain the future actions and policies were empty or marked yellow. This could not have served as a reasonably sufficient basis for meaningful

discussions and informed decisions at the conference. Shortly after the conference, the draft was filed with the European Commission.

As stated in section 1.1.1 of the Plan (page 6), the year 2016 is taken as the base year for the Plan. For the overarching reasons described above in paragraph 1, FICIL urges to revise the Plan, calculations and forecasts included therein to ensure that they reflect as up-to-date situation as possible. For instance, massive revision of the mandatory procurement of electric power (MP) is being implemented since the year 2017. From the current wording of the Plan, it is not unambiguously clear, whether reductions stemming from the said acts are covered by the calculations and forecasts included into the Plan. This may have impact not only on the calculations and forecasts, but also on the identification of the most realistic goals, and selection of the most appropriate policy instruments for their attainment.

The use of RES and electric power for the heating purposes is directly linked to the heatedly debated revision of MP. Also, liberalisation of the heating system is a topical issue directly related to the awaited dismantling of the MP. This should lead to the discontinuation of the currently existing cross subsidy between the income of electric power sale under the MP system and the heat supply tariffs. A timely and well-prepared solution should be established for the further discontinuation of the currently existing cross-subsidy between the heating tariffs and sale of electric power under the mandatory procurement. Therefore, it is highly recommended that all of these interrelated issues are being dealt with in a consistent and harmonised manner to ensure that negative effect on the end-consumers and energy-intensive industries is avoided to the maximum extent possible.

FICIL continues to uphold the opinion that the most important components of the Plan are:

- the principles “polluter pays” and “CO₂ emissions carry costs” should dominate;
- fossil fuels should be taxed to promote renewables;
- market mechanisms should prevail over subsidies to avoid effects distorting market principles, which are based in the competition. Responsible and sustainable financing options outside the state budget and other types of subsidies should be widely promoted;
- the best projects are born in competition. Auctions should be used to select projects requiring the lowest, if any, and shortest in time subsidies;
- electrification of the transport sector should be encouraged more;
- legislation should be developed in a more harmonised manner to reduce currently existing barriers for the development of the large-scale wind parks;

MP system and renewable energy

On January 10, 2019 Saeima passed a resolution urging the Ministry of Economics to abolish the MP system as of March 31, 2019. Currently the deadline is shifted to May 31, 2019 and this work is still in progress. FICIL therefore is expecting well-considered and balanced proposals for further action from the Ministry of Economics for a joint discussion.

Before selecting the most suitable solution for the revision of the MP system, FICIL encourages to make honest, clear, and transparent conclusions gained from the previous experience. Governance and monitoring of the system require substantial improvement and strengthening. Interests of the energy-intensive companies and of end-consumers should be weighed and safeguarded in this process.

It is important, that a road map for further operation and development of the electric power and heat power production sector is available timely in advance to any critical changes. This road map should be harmonised with the planned liberalisation of the heat power sector and transition to electric power as the source of heat (see Section 3 above). Finally, it is of utmost importance that in the elaboration of this road map due attention is paid not only to the rule of law, but also to the fair competition, balanced state aid and consumer protection.

Waste management policy

In the 'Early Warning report' (http://ec.europa.eu/environment/eir/pdf/report_lv_en.pdf), the EU has warned Latvia that it is among the countries being at risk of not attaining the 2020 municipal waste recycling target, since Latvia is landfilling 64% of municipal waste, compared to EU average of 24%. Consequently, it is important that the Ministry of Environmental Protection and Regional Development (VARAM) takes these issues seriously and develops its next Waste management plan for next 7 years to achieve the set targets.

Single-use Plastics Directive sets certain plastic collection goals to be achieved in the next 5 - 10 years. Also, the Directive implies that the industry must cover the cost of the litter clean-up. However, the litter does not consist of only the beverage packaging. Hence, responsibility of producers must be established in transparent agreements among the concerned sectors. The SUPD also introduces bans for certain plastic products as of Q2 2021 and provisions for consumption reduction for other products containing plastic. Considering the provisions made by the Directive, it is important how the litter clean-up costs for the industry are calculated locally. As there is some flexibility for the Member States for implementing such fees, the industry's contribution is necessary to establish a preferred local model in cooperation with VARAM.

While implementing SUPD and waste management solutions in general, VARAM must avoid significant reduction in the already so scarce competition in the waste management sector. Failure to act so has a high risk to result in substantial rises in the respective participation prices for producers, far above what could be actually driven by the growing waste management standards.

The inability to meet the EU targets, but also several other big waste management scandals (for instance, waste fire in Jurmala, and big piles of waste tires at several places in Latvia), are leading to the conclusion that there is a strong need to strengthen the State Environmental Service. Especially, its acts and decision-making should be made more transparent and less independent from the industry.

Sustainable financing

In order to improve the quality of life, public services and infrastructure in Latvia, there is a need for an enormous amount of financing. From the sectoral and industry perspective, substantial investments would be required for the water supply and drainage systems, road, industrial and freight railway infrastructure, industrial parks and innovation incubators, as well as the special purpose properties: hospitals, schools, depots, prisons, stations, concert and art halls, multi-purpose centers.

Since Latvia is subject to the Maastricht criteria, and for several years already cannot resume having a non-deficit state budget, it is important that more active and wider use is made of the sustainable financing frameworks, for instance, public – private partnerships (PPP), energy service companies (ESCO), energy performance contracts (EPC) and similar.

Latvia has reached that level of state, legal and market maturity, in which the sources of financing alternative to the state budget, EU financing, subsidies and loans from the credit institutions should be promoted and widely used.

Finally, sustainable finance should be considered as one of the alternatives for the revision of the MP system (see Section on the mandatory procurement for electric power and potential further support for renewable sources of energy). In several situations this financing could be used to further finance those electric power production or CHP stations, which ability to operate and value created for the market is considered worth retaining in effect.