WELCOME TO A CHEMSEC WEBINAR

THE POWER OF CARROTS
WELCOME TO THE CHEMSEC WEBINAR:
HOW CHEMICAL LEGISLATION CAN MOVE THE INDUSTRY WITH THE HELP OF ECONOMIC INCENTIVES

The slides and recording will be available after the webinar.

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CHEMSEC INTRO

• Environmental NGO focusing on chemicals
• Constructive dialogues with business, investors and policy makers
• Highlighting good examples
• Developing online tools to help companies switch to safer chemicals
• Funding from charity funds and governments
THE AIMS OF THE CHEMICAL STRATEGY

• Substitution has not taken place at the expected pace under REACH

• Regulatory tools to drive and reward the production of safe and sustainable chemicals are needed

• Incentive industry to priorities innovation for substituting substances of concern

• Frontrunners encounter major economic barriers
Unlock the market

Economic incentives for alternatives to hazardous chemicals

Thea Sletten
22nd February 2022
Objective and scope

Objective
Understand the economic incentives and disincentives for substitution created by different regulatory measures, and why these are important

Topics covered
Key principles under REACH
Economic principles and policy instruments
Case study – REACH authorisation
Key principles of REACH

1. **Substitution Principle**
   - A hazardous chemical substance should be substituted if suitable alternatives exist
     ➢ Substitution is an objective within itself

2. **Polluter Pays Principle**
   - The polluters bear the costs of managing or preventing the damage from the pollution
     ➢ There should be economic incentives for not using hazardous chemicals

3. **Precautionary Principle**

4. **Right to Know Principle**
What can we learn from economics?

- Private actors tends to maximise their own benefits rather than others’
- This behaviour may lead to unintended consequences
- Interventions are often necessary to get the actors to consider these unintended consequences

- Example of market interventions:
  - Regulatory, e.g. bans, obligations
  - Economic, e.g. tax, subsidies
  - Information, e.g. labelling, information campaigns
  - Agreements, e.g. voluntary agreements, industry pledges
Why do we need economic incentives for substitution?

• Transitioning to alternatives can be
  - Challenging
  - Time-consuming
  - Costly
  - A risk to business continuity

• Companies are unlikely to take on this risk unless there is a potential reward on the other side
Unlock the market

Incentives mechanisms within policy instruments

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<tr>
<th>Type of policy instrument</th>
<th>Examples of incentives mechanisms</th>
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| Restrictions and other bans                                   | • Time-limited vs. permanent derogations  
|                                                               | • Length of the transition period(s)  
|                                                               | • Additional conditions (e.g. reporting, labelling)                                             |
| Exposure limit values and mandatory technology                 | • Risk management measures (RMMs)  
|                                                               | • Best available technology (BAT)  
|                                                               | • Hierarchy of controls                                                                       |
| Taxes, subsidies and fees                                      | • Size of tax, fee or subsidy  
|                                                               | • What is taxed or subsidised                                                                 |
| Information-related measures                                  | • Customer and investor pressure  
|                                                               | • Cost of information dissemination (e.g. labelling, downstream user communication)          |

Economic incentives may change based on regulatory decision-making
REACH authorisation – economic incentives for substitution

• Direct costs, e.g. application fees, cost of preparing an AfA, responding to regulators, costs of compliance with conditions imposed.

• Risk to business continuity if authorisation is not granted or from receiving a short review period, e.g. cease of production, customer and investor confidence

• Other risks to business continuity, e.g. customer pressure, reputational effects, retaining key workers

• Business opportunities from early transition to alternatives, e.g. technological lead and potential patents, capturing new customers

• Effectiveness relies on consistent regulatory decision-making
  - Easy to acquire an authorisation → less incentives to substitute early
  - Difficult to acquire an authorisation → stronger incentives to substitute early
Case study – DCC Maastricht court case

• In 2016, Sweden took to court an authorisation for lead chromate pigments was taken to court, on the basis that alternatives existed for the uses applied for.

• Sweden won (including appeal) and the authorisation was annulled.

• The EU court ruling (re)established some key principles to be upheld:
  i. The burden of proof lies solely with the applicant (‘Polluter pays principle’);
  ii. Uncertainty regarding the availability of alternatives should result in a refusal of the application not a shortened review period; and
  iii. Proportionality is irrelevant where the conditions for the granting of an authorisation are not met (‘Substitution principle’).

• Implications for future decisions on application for authorisation and the strength of the economic incentives.
What happened to the carrot?

• The suppliers of alternatives to lead chromate pigments lost a potentially large market due to the DCC Maastricht application being granted

• Using information from the public DCC Maastricht AfA it was found that the loss could be in the range of €200 million – €4.4 billion over the review periods granted.

• The DCC Maastricht authorisation only comprise 0.3% of the total volume of SVHCs applied for since 2013

• Thought experiment: If 5% of the total volume applied for has wrongfully received an authorisation, the loss to alternative providers could be in the order magnitude of €1 billion – €10 billion per year.
Why does it matter who receives the benefits?

• The losses are not net costs to society but distributional effects.

• If the benefits outweigh the costs, do we need to consider distributional effects?
  - The cost-benefit ratio may be different if you look at systemic changes, i.e. all applications and over an extended time-period.
  - Diminishing costs of substitution may improve cost-benefit ratio over time (but it usually starts out high).

• If the system favours alternative providers more companies will choose to attempt substitution earlier in time.

• Progressive substitution may be incentivised by ensuring that the polluter pays and the frontrunner is rewarded.
What can be gained?

- Only 35% of companies start the substitution process at the candidate list stage or before.
- If the potential financial gain from substituting early is considered more likely, more companies would start their substitution process earlier.

Source: Adopted based on: Socio-economic impacts of REACH authorisations, ECHA (2021)
Key messages

• Economic incentives can be powerful tools to accelerate the transition to alternatives

• Regulatory decisions may increase or decrease the economic incentives within a policy instrument

• Distributional effects are important to consider. ‘Carrot and stick’.

• It should be a race to the finish line!
Thank you

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HOW TO MAKE IT RIGHT

• Apply key principles for changing to alternatives

• Massive market potential

• Investing for the transition takes predictability

• It is possible
CHEMSEC policy asks

• Apply the Polluter pay principle in full - Impacts on society. The companies that use hazardous chemicals should bear the costs.

• Use economic incentives to drive the transition - REACH Review incorporate economic incentives. Fee for using SVHCs.

• Support the ones driving the transition - Being a frontrunner must pay off in financial terms and regulation must ensure this.

• Lack of action should never pay off - ensure that unintended ‘perverse’ incentives are avoided.
CHEMSEC CONCLUDES

• Make a profit
• Regulation needed
• Call it what you like, but make it work
• Stick to the Chemical Strategy
• Unlock the market for alternatives
LET'S DIVE INTO THE QUESTIONS!
LINKS & CHANNELS

• “Unlock the market” report
• Website: chemsec.org
• LinkedIn: @chemsec
• Twitter: @chemsec
• Facebook: @chemsecsweden
• Instagram: @chemsecsweden