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*R (on the application of Cemex UK Cement Ltd) v Department for Environment Food and Rural Affairs and others

QUEEN'S BENCH DIVISION (ADMINISTRATIVE COURT)

[2006] EWHC 3207 (Admin), [2006] All ER (D) 181 (Dec), (Approved judgment)

HEARING-DATES: 13 DECEMBER 2006

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CATCHWORDS:

European Community - Environment - Emissions Trading Scheme - Allocation of allowances - Carbon dioxide emissions - Claimant challenging allocation of emission allowances to cement plant - Whether allocation infringed EC principle of equality or non-discrimination - Parliament and Council Directive (EC) 2003/87.

HEADNOTE:

This case digest has been summarised by LexisNexis UK editors.

The claimant company, a global producer of cement, operated under strict allowances to its carbon dioxide emissions of its cement plants. The allocation of those allowances was governed by the UK National Allocation Plan which was made by the defendant Department for Environment Food and Rural Affairs, pursuant to the EU Emissions Trading Scheme, established by Council Directive (EC) 2003/87. Following a consultation exercise, the defendant as part of its allocation methodology, introduced a 'first year of operations rule' in Phase II of the plan, replacing a 'commissioning rule' in Phase I. That resulted in a reduced allocation to the cement plant in question. The claimant applied for judicial review. Its application for permission was heard together with the substantive hearing. The defendant adduced evidence that a new rule could have been formulated to treat all relevant sectors consistently, and that a special rule would not be needed, particularly as the commissioning rule applied only to three installations.

The claimant submitted, inter alia, that the allocation infringed the EC principle of equality or non-discrimination. In accordance with that principle, the claimant contended that like situations were not to be treated differently or different situations treated in the same way, unless that treatment was objectively justified. The defendant submitted that it had been entitled to replace the commissioning rule even though it had little material to objectively justify that decision.

The court ruled:

Provided a rule was capable of applying to all installations in a particular sector which justified different treatment it would not matter that only a limited number of installations would benefit from that rule. The desire to simplify, to treat all sectors consistently, and to retain only essential rules, provided no justification for a rule which treated two unlike sectors in the same way. The desire for 'administrative tidiness' provided no justification for discrimination. However, where a rule treating two sectors differently had been adopted for a pilot phase of a scheme upon the basis of very limited material by way of objective justification, the revocation of that rule would require commensurately little by way of objective justification ([48], [54]).

In the circumstances of the case, the introduction of a new allocation rule had not infringed the EC principle of equality or non-discrimination. The material that the defendant had relied upon as justification for not continuing the commissioning rule in Phase II although not extensive, had been more substantial than the material which persuaded the defendant that the adoption of the rule in Phase I was justified ([60]).

Permission to apply for judicial review would be granted, however, the substantive application would be dismissed ([74]).

INTRODUCTION:

This is the first approved version handed down by the court. An edited official transcript or report will follow.

COUNSEL:

Stephen Tromans and Colin Thomann for the claimant; Mark Hoskins and Maya Lester for the defendant and the first interested party; Aidan Robertson for the second interested party.

PANEL: SULLIVAN J

JUDGMENT: APPROVED BY THE COURT FOR HANDING DOWN (SUBJECT TO EDITORIAL CORRECTIONS)

JUDGMENTBY-1: MR JUSTICE SULLIVAN

JUDGMENT-1:

MR JUSTICE SULLIVAN:

1. Introduction

In this "rolled up" application for permission to apply for Judicial Review with the substantive hearing to follow if permission is granted, the Claimant challenges the allocation of carbon dioxide emission allowances to its cement plant at Rugby under the UK National Allocation Plan 2008 - 2012 dated 21st August 2006 ("the Plan") made pursuant to the EU Emissions Trading Scheme (EUETS). The Defendant, working with the DTI, is the government department responsible for the preparation of the Plan.

2. Background

The background to the preparation of the Plan is not in issue between the parties and a brief summary will suffice for the purposes of this judgment. The Introduction to the Plan is the most convenient starting point:

1. "This document sets out the UK's National Allocation Plan (NAP) for participation in the European Union Emissions Trading Scheme (the "EUETS" or the "Scheme") for the period 2008 to 2012 (Phase II).

2. The EU ETS is a Community-wide scheme established by Directive 2003/87/EC ("the Directive") for trading allowances to cover the emissions of greenhouse gases from permitted installations set out in Annex 1 of the Directive. Phase I began on 1 January 2005 and Phase II runs from 1 January 2008 to 31 December 2012.

3. Each member State must develop a NAP for the second phase stating:

. the total quantity of allowances that the Member State intends to issue during that phase; and

. how it proposes to distribute those allowances among the installations which are subject to the Scheme.

4. These Plans must be based on objective and transparent criteria, including those listed in Annex III of the Directive. Annex III consists of both mandatory and optional criteria and is reproduced for convenience at Appendix A. The European Commission published guidance on Phase II NAPs in December 2005. This aims to reduce many of the disparities resulting from the implementation of Phase I across the EU and, by requesting more detailed and consistent information, will allow a more transparent and robust assessment of Member States' NAPs and detail of how they will meet their Kyoto targets.

5. National Allocation Plans must be published and notified to the European Commission. The Commission will then consider each NAP and may reject any aspect of any Plan, giving reasons, on the basis that it is incompatible with the Directive. Member States may propose appropriate amendments.

6. Once accepted by the Commission, the NAP will form the basis for the final decision made by each Member State under Article 11 of the Directive on the total quantity of allowances to be issued and their distribution to installations subject to the Scheme. For Phase II (2008 to 2012), these final allocation decisions must be made by 31 December 2006".

3. The Directive

It is unnecessary to rehearse the provisions of the Directive, as to which there is no dispute. Recital (27) states that the Directive respects the fundamental rights and observes the principles recognised in particular by the Charter of

Fundamental Rights of the European Union. It is common ground that these include the principle of equality, or non-discrimination. Annex I to the Directive lists the activities to which it applies. These include:

"Installations for the production of cement clinker in rotary kilns with a production capacity exceeding 500 tonnes per day or lime in rotary kilns with a production capacity exceeding 50 tonnes per day or in other furnaces with a production capacity exceeding 50 tonnes per day".

4. Paragraph 5 in Annex III states that:

"The plan 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".

The Directive is implemented into Domestic Law by The Greenhouse Gas Emissions Trading Scheme Regulations 2005 (as amended in 2005 and 2006). For present purposes nothing turns on these regulations.

5. The allocation process

There is a summary of the process on pages 7 and 8 of the Plan. There are three stages. First a total figure of allowances for the UK is set: 246,175,995 allowances per annum in Phase II, equating to 1,230,879,990 allowances over the period 2008 - 2012. Second, that total is allocated between 19 sectors. The sectors are set out in Table 2.1 and include Large Electricity Producers (LEP), Refineries, Iron and Steel, Cement, Chemicals etc. Table 2.2 sets out the amount of allowances to be allocated to each sector. Each sector makes a contribution to a New Entrant Reserve (NER), for installations starting or extending operations between 2008 - 2012. After deduction of that contribution the allocation to existing installations in the cement sector is 10,993,592 per annum. By far the largest allocation, 99,892,660 per annum goes to Large Electricity Producers. Thirdly, the sectors' allowances are allocated to the existing installations within those sectors. The Summary explains:

"Allocations at installation level will be made on the basis of each installation's share of "relevant emissions". Relevant emissions are generally the average dropping the lowest year of emissions during the baseline period (2000 - 2003). Allocation Methodology Rules are available for calculating relevant emissions of

. Installations where changes have taken place during or after the baseline period;

. Installations where rationalisation of production has taken place during or after the baseline period;

. Installations that have undergone temporary closure during the baseline period;

. Installations that had the first year of operation during the baseline period.

A benchmarking methodology will be used for the LEP sector".

6. In these proceedings the Claimant does not challenge the first and second stages of the allocation process. Its concern is solely with the third stage of the process: how much of the cement sector's allowances should be allocated to its Rugby plant.

7. In order to understand the Claimant's concerns it is necessary to outline the history of the Rugby plant, and to examine in some detail how the allowances to individual installations within the cement sector were allocated in Phase I, and how they were allocated in Phase II, of the NAP.

8. The Rugby Plant

Cement has been manufactured at the site of the Rugby plant since the mid 19th Century. The new plant was a major investment. A new kiln replaced seven, older, more polluting kilns. The plant is connected by way of an underground pipeline, through which chalk slurry is pumped, to large chalk reserves in Dunstable Quarry in Bedford-shire, 55 miles away. The new plant was commissioned over a three year period, between February 2000 and February 2003.

9. Phase I NAP

Phase I started on 1st January 2005 and will run until 31st December 2007. In a Witness Statement dated 17th November 2006, Mr Cottam, a senior policy adviser at the DTI explains that the NAP for Phase I had to be developed within a tight timetable: the Directive came into force on 25th October 2003, Member States were required to implement it into domestic legislation by 31st December 2003, and to publish and notify their proposed Phase I NAP to the Commission by 31st March 2004, having first consulted on and taken account of public comments.

10. Consultation began in August 2003. For present purposes the following steps in the development of the Phase I NAP are relevant. A Consultation Draft NAP was published in January 2004. It explained how it was proposed to allocate allowances at installation level:

"3.2 The activity level allocations are divided between installations according to each installation's average share of annual emissions over the period 1998 - 2002. To calculate each installation's allocation, we have taken an average of the historic data provided, excluding the lowest year's emissions for each installation. Therefore, for an installation that has provided five year's data, the average of the four maximum years for that installation has been used. Similarly, for an installation that has provided four year's data (i.e. their first year of operation is 1999), we have used the average of three maximum years and so on. Where an installation has provided only a single year's data, that data has been used without adjustment.

3.3 A historic measure has been chosen to allocate at the installation level due to the complexity of projecting installation level emissions consistently and accurately. The use of an historic average also provides some compensation to potentially stranded assets. The exclusion of the lowest year's emission is intended to minimise the impact of an anomalous year with unusually low emissions on an installation's allocation.

3.4 There are a small number of installations that began operations during 2003. These installations are considered 'existing installations' for the purposes of the NAP, although historic data for the period 1998-2002 is not available. As a result the methodology described above is not appropriate. It is proposed that allocation will be calculated from actual 2003 emissions. These installations have therefore been asked to provide actual emissions data for 2003. Where an installation was only operational for part of 2003, the time period to which the data applies can be taken into account.

3.5 Installations that have commenced operations after 31 December 2003 will be allocated allowances from the new entrant reserve. The treatment of these installations is described in more detail in section 5.2 below".

11. Over 200 written responses to the consultation were received. The NAP was revised in the light of these responses and notified to the Commission on 30th April 2004. That version of the NAP and a consultation document on outstanding issues was published on 6th May 2004. Section 7 of that document explained:

"7.1 In the draft NAP, installation-level allocations were derived by calculating the installation's share of emissions during the baseline period, and applying this proportion to the draft NAP sector total to which that installation belongs.

7.2 The baseline period chosen was five years in length, running from 1998 to 2002. This baseline period was chosen to take as much account as possible of early action while recognising that few installations have accurate records going back before 1998. The period was extended until 2002 so that the allocation methodology would also reflect likely need of the installation as closely as possible. 2003 was not included because it was not clear at the time whether 2003 data would be available in time for inclusion in the NAP.

7.3 It was decided to take an average of the baseline period, rather than just choosing one year, as this was more likely to smooth out any anomalous variations and give an accurate representation of the historic emissions. It was decided not to use one maximum year as it is more likely that maximum years are also anomalous and therefore not truly representative of an installation's share of emissions.

7.4 In recognition of the fact that many operators expressed concern at the inclusion of a particularly low emissions year in the baseline period, Government decided to exclude the year with the lowest emissions and take an average of the remaining years.

7.5 In the NAP, the same basic principle for allocating to installations is maintained, namely distributing the sector total on the basis of historic emissions in the baseline period. However, the consultation on the draft NAP helped Government identify some concerns held by industry stakeholders about the way in which the allocation to installations takes place. The following sections describe the proposed approach with dealing with these problems.

7.16 Following responses to consultation and further consideration, Government has decided that the allocation methodology for installations that started operations in 2002 or 2003 should be altered from that set out in the draft NAP, since Government feels that the approach set out in the draft NAP was not sufficiently equitable. The previous approach unduly penalised those installations that happened not to have a full year's emissions data. In addition, one of the principles of the NAP is to apply consistent treatment to installations wherever possible. This is particularly the case for phases of commissioning. Section 7.32 deals with the issue of the treatment of commissioning phases in the baseline period....

Commissioning

Issue

7.32 Whether the proposed allocation methodology in the draft NAP takes sufficient account of periods of commissioning.

Background

7.33 "Commissioning" refers to any period of testing and trial running of a new or refurbished installation (or part of an installation) prior to the commencement of normal operations. During commissioning, emissions are usually significantly lower than the emissions during periods of normal operation. Therefore, an installation which was commissioning during the baseline period might receive a lower share of the sector total than would be the case if its share were determined on the basis of its normal operation.

7.34 In the draft NAP, commissioning was not taken into account explicitly, although by dropping the year with the lowest emissions from the 5 year baseline period the effect would have been to exclude a commissioning period for some installations.

7.35 However, some stakeholders have expressed concerns that this does not solve the problem where commissioning may have been carried out over a period of more than one year. These concerns have been expressed by the power stations sector, as well as other industrial sectors such as cement, steel and chemicals. The concerns are particularly acute for plant that started commissioning towards the end of the baseline period. In the case of the power stations sector, a substantial volume of new gas fired generating capacity started commissioning in or around 2000.

Options

7.36 Options to address this issue include:

. Option 1 - "do nothing". Assume that the methodology set out in the draft NAP will exclude most commissioning phases from the baseline period. Accept that there will be some cases not covered by this.

. Option 2 - Exclude emissions during commissioning phases, and then apply the same methodology as before (i.e. exclude data from year with lowest emissions and take an average of the remaining years). This option is only feasible if clear definitions of commissioning can be established.

. Option 3 - Drop data from the two years with the lowest emissions and take an average of the remaining years. Accept that there will be some cases not covered, but fewer than under Option 1.

. Option 4 - Exclude emissions during commissioning phases, and then apply the same methodology as option 3 (i.e. exclude data from two years with the lowest emissions and take an average of the remaining years).

Decision

7.37 Government recognises that commissioning over an extended phase during the baseline period can in some cases lead to low allocations that are not representative of normal operation. We have therefore decided that option 1 is not appropriate and that the allocation methodology needs to be adapted to fully take into account all commissioning phases in the baseline period.

Proposed Approach

7.38 Option 2 - As stated in paragraph 3.8 of the NAP, we are proposing that any emissions data relating to commissioning should be excluded from the calculation of relevant emissions. However, as noted above, this approach is dependent on establishing clear definitions of commissioning for all sectors.

7.39 Where there is a gap between the end of commissioning and the start of normal operations, then only data from the date on which normal operations commenced would be used.

7.40 The reason for taking this approach is one of equity. It is important that the NAP is fair and equitable across sectors and within sectors. Government recognises that it would not be practical to make adjustments for all the wide range of factors which cause historic emissions to be less than fully representative of future emissions for individual installations. However, we consider that the distortion to historic emissions data caused by the inclusion of commissioning data is significant as it could result in a significant proportion of installations receiving significantly less allowances than they require.

7.41 We favoured option 2 over options 3 and 4, because:

(a) options 3 and 4 do not specifically target the commissioning problem and in particular, do not take account of the fact that periods of commissioning vary between sectors; and

(b) excluding two year's data results in the allocation being based on fewer years data overall. Consequently there is a higher chance that the allocation is unrepresentative of periods of normal operation".

12. Consultees' views were sought as to the best approach to the definition of commissioning. The British Cement Association ("BCA") responded at a meeting with the DTI's consultants on 13th May 2004. The BCA's response included the following:

"The cement sector allocation has been disproportionately affected by commissioning in the baseline period. As such Defra should take note of the definitions provided by BCA in ANNEX I of this response."

13. In answer to the question:

"Do you believe that the approach proposed in section 7.38 is a fair and equitable way of treating installations which have carried out commissioning phases during the baseline period? If not, please give reasons."

The BCA answered:

"The approach taken in section 7.38 appears that the allocation to installations who had carried out commissioning during the base period are subject to a definition of commissioning being agreed appears fair."

In answer to the question:

"Do you consider that it is appropriate to have a single definition of commissioning common to all sectors or do you agree that that sector specific definitions are required? Please give reasons."

The BCA answered:

"It is imperative that sector specific definitions of commissioning are adopted. Otherwise significant inter sectoral discrepancies will occur in the allocation. This could potentially create an advantageous allocation for one sector over another in competing markets i.e. construction materials."

14. In Annex I the BCA suggested the following definition of commissioning for an installation that commissioned in the baseline period:

"The commissioning period ends (full normal operation commences) when the installation has achieved an average of greater than 85% of its nameplate (or guarantee) output over 90 days of operation".

15. On 26th July 2004 the Government published its final decisions on allocation methodology. Section H of that document dealt with "Treatment of Commissioning during the baseline period".

"38. An installation's share of allowances of the total sector allowance is calculated using that installation's 'relevant emissions' figure. The general methodology for calculating an installation's relevant emissions is to take the baseline data, drop the year with the lowest emissions, and then take an average of the remaining years.

39. The purpose of dropping the lowest year was to acknowledge that emissions in a particular year might be unusually low, for a number of reasons, including low emissions during commissioning and only having a partial year's data (due to operations starting during a calendar year rather than at the start).

40. The consultation on the draft NAP, highlighted that there were still some situations where dropping the lowest year was not sufficient to account for commissioning. This was specifically where the commissioning period took place across more than one calendar year. This was more likely in sectors where commissioning can often be a significant and protracted event.

41. Government therefore proposed in the NAP to further investigate the possibility of taking commissioning into account more specifically.

Decision:

. Commissioning will be specifically accommodated for in the power station and cement sectors and the 'Commissioning rule' will only therefore apply to them. It is recognised that commissioning will have taken place in other sectors, but that it was rarely a significant and protracted event.

. The Commissioning rule is that (a) data for any year prior to the year in which normal operations commenced is excluded from the calculation of relevant emissions; and (b) for the year in which normal operations commenced, the data used for calculating that installation's relevant emissions would include the commissioning data.

. For all other sectors, all data from date of first emissions will be used, including any part year or commissioning data.

. The normal baseline allocation methodology will then be applied (drop lowest year and take average).

Implementation

. The Government has, in consultation with industry, devised definitions of the date on which normal operations would generally be considered to have commenced for the power station and cement sectors. These dates of commencement of normal operations are defined as:

. Power stations - the later of (a) the date when the installation/technical units started paying full business rates or (b) the date when the handover of plant from builder to operator took place.

. Cement - as the date on which 90 days operation at an average load factor above 80% began.

. If any installation was 'commissioning' as defined above on 31 December of any of the baseline years, the calculation of its relevant emission will exclude those years. In the calendar year in which it starts normal operation, all data for that calendar year will be included in the calculation of its relevant emissions. The relevant emissions will then be calculated using the normal methodology i.e. take the average of remaining years data after dropping the lowest year. For example, an installation in the power stations sector started commissioning in March 1999 with normal operations starting in March 2000. Because normal operations does not start throughout 1999, up to an including 31 December, the data from this year is excluded. Because normal operations does start in 2000, then the commissioning data from this year is included.

. The normal baseline allocation methodology will then be applied. In the example above, this means that the lowest year of 2000, 2001, 2002 and 2003 is dropped. The average is taken of the remaining years.

. Operators of an installation affected by commissioning will need to provide evidence (this evidence would need to be verified) to Defra. Defra will consult the devolved administrations, DTI and the regulators as necessary to verify whether commissioning has taken place.

Rationale

. It is considered that where sufficient historic data is available, allocations to incumbent installations should based on historic emissions data. The original baseline allocation methodology in the draft NAP (published January) was to drop the year with lowest emissions from the baseline and then take the average. The rationale behind dropping the lowest year was to take account of operator's concerns that emissions in some years were lower than "normal" due to a number of reasons, one of which could be commissioning.

. A number of responses to the consultation on the draft NAP expressed concern that this would not be enough to address some periods of significant commissioning. In particular, it was raised by the cement sector and the power station sector, for both of whom commissioning could be significant events, over a long period of time, with emissions significantly lower than normal operations.

. It was therefore proposed in the consultation document that accompanied the NAP that went to the Commission that we could take these kind of major commissioning events more explicitly into account by excluding data from the commissioning period. Any such kind of new rule would require data resubmission from operators.

. We have considered this issue further and consider that any additional rule would be required to deal with commissioning in sectors where commissioning takes place over an extended period (i.e. the power station and cement sectors). It is considered that for all other sectors, the existing methodology takes account of years where emissions are low due to, among other things, commissioning. Data from such installations will be used from the date of first emissions.

. However, to ensure that installations commissioning over an extended period are not disadvantaged, data from the years where the installation was only commissioning would be excluded from the calculation of relevant emissions. The year in which the installation begins normal operations (including the commissioning data from that year) will be used in the calculation of the relevant emissions. This means that installations from the power station and cement

sectors will, so far as possible, be treated in the same way as installations from other sectors.

. It was decided not to exclude the commissioning data and the remaining partial year's data before calculating the relevant emissions for the following reasons:

o It will increase the number of installations that have fewer years data to use, thus making them more vulnerable to any remaining emissions anomalies.

o It will increase the number of incumbent installations that have to use the new entrants benchmarking methodology. However, Government's view is that where sufficient data could be available then allocations to incumbents should be based on historic emissions, as with most other installations.

o Excluding the partial year will disadvantage some operators, where their partial year has higher emissions than later years.

o Even if an operator is left with a partial year that has very low emissions, then this year can nonetheless be dropped using the 'drop 1 year' provision, which had always been the intention".

15. A "Revised list of installations and allocations" was published in February 2005. The Claimant's Rugby plant is one of 15 plants listed in the cement sector. Its annual allocation of allowances during Phase I is 1,291,669, based on benchmarking. Operators were given a three week period for their comments on the revised list. The final, approved version of the Phase I NAP was published in May 2005. Paragraphs 3.6 - 3.8 explained:

"3.6 An allocation methodology based on historic emissions has been chosen to allocate at the installation level due to the complexity of projecting installation level emissions consistently and accurately across installations in all sectors. The use of an historic average provides some compensation to potentially stranded assets. Emissions data from 1998 onwards were chosen on the basis that they are more accurate, available and able to be verified than data before that date. The exclusion of the lowest year's emissions is intended to minimise the impact where an installation has had an anomalous year with unusually low emissions.

3.7. However, it became clear during consultation on the draft NAP that there are situations in which the general approach for calculating relevant emissions is not appropriate. The following represents a summary of the approach to dealing with these cases. Further detail on the rules and rationale can be found in Appendix F.

(1) Commissioning

3.8. Firstly, installations in the power stations and cement sectors which underwent prolonged periods of commissioning during the baseline period will be disadvantaged if commissioning was carried out in more than one calendar year. For such installations, any emissions data relating to commissioning should be excluded from the calculation of relevant emissions i.e. the installation will only be treated as being in operation for the purpose of paragraph 3.3 above once commissioning has been completed. The application of this rule relies on an installation fulfilling the criteria set out in Appendix F. Furthermore, the rule on commissioning will only apply to installations classified in the power generation or cement sectors, in either of the lists notified to the Commission on 14 February 2005 and 14 June 2004)".

16. So far as relevant, Appendix F states:

"F. Treatment of commissioning during the baseline period

15. An installation's share of allowances of the total sector allowance is calculated using that installation's 'relevant emissions' figure. The general methodology for calculating an installation's relevant emissions is to take the baseline data, drop the year with the lowest emissions, and then take an average of the remaining years.

16. The purpose of dropping the lowest year acknowledges that emissions in a particular year might be unusually low, for a number of reasons, including low emissions during commissioning and only having a partial year's data (due to operations starting during a calendar year rather than at the start).

17. The consultation on the draft NAP, highlighted that there were still some situations where dropping the lowest year was not sufficient to account for commissioning. This was specifically where the commissioning period took place across more than one calendar year. This was more likely in sectors where commissioning can often be a significant and protracted event.

18. Government therefore proposed in the provisional NAP to further investigate the possibility of taking

commissioning into account more specifically.

Decision:

. Commissioning will be specifically accommodated for in the power station and cement sectors and the 'Commissioning rule' will only therefore apply to installations in these sectors (or those installations classified in these sectors in either of the lists of installation - level allocations notified to the European Commission on 14 February 2005 and 14 June 2004). It is recognised that commissioning will have taken place in other sectors, but that it was rarely a significant and protracted event.

. The Commissioning rule is that (a) data for any year prior to the year in which normal operations commenced is excluded from the calculation of relevant emissions; and (b) for the year in which normal operations commenced, the data used for calculating that installation's relevant emissions would include the commissioning data.

. For all other sectors, all data from date of first emissions will be used, including any part year or commissioning data.

. The normal baseline allocation methodology will then be applied (drop lowest year and take average).

Implementation:

. The Government has, in consultation with industry, devised definitions of the date on which normal operations would generally be considered to have commenced for the power station and cement sectors. These dates of commencement of normal operations are defined as:

o Power stations - the later of (a) the date when the installation/technical units started paying full business rates or (b) the date when the handover of plant from builder to operator took place.

o Cement - as the date on which 90 days operation at an average load factor above 80% began.

. If any installation was 'commissioning' as defined above on 31 December of any of the baseline years, the calculation of its relevant emission will exclude those years. In the calendar year in which it starts normal operation, all data for that calendar year will be included in the calculation of its relevant emissions. The relevant emissions will then be calculated using the normal methodology....."

17. Phase II NAP

Consultation on Phase II NAP began on 31st March 2005, before publication of the final approved version of Phase I, with a paper outlining the "UK Government approach to EUETS Phase II". The paper described Phase I as the pilot phase of the scheme and said that in Phase II there would be an opportunity "to build on experience from Phase I". It also said that:

"One of the main objectives for Phase II is to develop an allocation methodology which is straightforward to apply, well understood, is feasible within the timetable, transparent, can be utilised in future phases and does not create a disincentive for emissions reductions during Phase I".

18. On 19th July 2005 the first formal consultation document was published. That again described Phase I as the pilot phase of the scheme and stated that its implementation "provided a steep learning curve, and Government has already learned many lessons from the process". The Government's intention was "to improve and simplify the current rules of the scheme rather than make it more complex" (paragraph 2.2.4). Paragraph 12.0.2. stated that:

"12.0.2 The UK Government is planning to have a more focused consultation for the allocation methodology issues for Phase II in the form of sector specific meetings during the consultation period. The aim is to send out a sector specific document to each sector prior to the meeting. Stakeholders would then have until the end of this consultation period to feed in their views. The focused consultation will explore each of the questions below in more detail".

19. The document explained why it had been concluded that it was "not feasible to develop robust benchmarks for all installations and all sectors in time for Phase II".

"12.7.7 The Government therefore intends to give further consideration to developing benchmarks only where it is considered most feasible - for the electricity generators and combined heat and power plants, where measures of capacity are clear and outputs are not differentiated.

12.7.8 Unless there is a strong case put forward, the Government is not minded to pursue the development of

benchmarks for other incumbents in Phase II but will actively take this forward as a longer-term objective at a UK and EU level".

20. In August 2005 the various sectors were invited to comment on a more detailed paper on "Allocation Methodology". Paragraph 31 of the paper said:

"31. For Phase I, a number of rules were introduced to deal with baseline changes, commissioning and rationalisation. These rules were set out in the final UK NAP. Consideration is still being given to how these rules will apply for Phase II and stakeholders will be informed as soon as possible".

21. Template Response Forms were issued asking consultees (inter alia) "which allocation methodology would be appropriate to your sector". The methodologies listed included historic emissions and benchmarking. The BCA's response to this question was:

"A choice regarding a preferred allocation method will always be installation specific...."

In its response the Claimant contended that benchmarks should be used:

"The current methodology for allocation to the (benchmarked) installations should be used as the allocation methodology for them in Phase 2. The methodology should also be applied to original incumbent new entrants (those that were determined to be commissioning during the baseline period i.e. did not have sufficient representative historic data in the period 1998-2003 and were allocated using the same new entrant methodology".

22. On 24th November 2005 some interim decisions on Phase II methodology were published by the Defendant, consideration having been given to the consultation responses, of which there were over 300. Under the heading "Allocation Methodology Rules" the document said:

"In Phase I, rules were applied to tackle anomalies in emissions during the historic baseline period:

. Baseline changes and temporary closure rules were used to account for significant changes such as additions or closures within an installation.

. Rationalisation rules applied where an operator closed one or more installations and shifted production to another installation. It allowed data from the following year only to be taken into account.

. The Commissioning rule applied only to the cement and electricity generating sector and allowed data prior to the year of normal operations to be dropped.

The most significant proposed change is to replace the Commissioning rule with a "first year of operation" rule so that it can apply to all sectors and will allow the data from the start up year to be dropped. Other amendments have been considered, including a rule to tackle administrative receivership and partial rationalisation but the complexity of their application outweighs the evidence of the need for such rules.

It is proposed that the rules will apply to those installations that had the rules applied in Phase I (except for commissioning) and all other installations will be invited to apply for application of the rules before finalisation of the draft NAP".

23. The interim decisions document was accompanied by a paper containing a series of questions and answers. The answer to the question "Why had the Commissioning rule been dropped?" was:

"The Government reviewed the Phase I allocation methodology rules and has amended them for Phase II. It was considered preferable that a rule could be applied to all sectors - the First Year of Operation Rule has been introduced partly to replace the Commissioning rule".

24. The Claimant expressed its serious concerns at a meeting with the Defendant on 8th December and followed this up with a letter dated 13th December 2005. The letter said, inter alia:

"Having absorbed the recent Defra announcement on decisions on Allocation Methodologies for Phase 2 of EU ETS (published 24th November 2005) we are seriously concerned with the implications of the decision on the potential resulting allocation for our Rugby installation.

The installation of Rugby is our premier installation that accounts for over 50% of our production and 10% of total UK cement production. The installation utilises world-class state of the art benchmark standard technology, which was built to replace 7 older cement kilns.

We believe the methodology proposed (if our interpretation is correct) will lead to this plant being severely and inequitably under allocated compared to similar plants in the UK and will place our company at a major competitive disadvantage compared to the rest of the UK Cement Sector.

The actual emissions at our Rugby plant for 2003 and 2004 are particularly low compared to the design capability of the plant, firstly because the 2003-year was a commissioning period and secondly because 2004 was a low output year for a number of operational reasons.

The plant is currently on route to achieve outputs in the period 2005 to 2007 that will result in C02 emissions that will absorb the Phase I allocation and result in a deficit over the period.

If the allocation to our Rugby plant is based on the low output years of 2003/4 we have estimated, by simple comparisons to the known Phase I shares of each installation/company, that the Rugby % share of the Phase 2 Sector Cap will be reduced by an inequitable and severe amount.

We believe that if only 2003/4 data is taken into account the potential allocation starting point for our Rugby installation will result in this state of the art plant being under allocated and carrying an inequitable burden or share of the Sector Cap ".

The letter suggested alternative methods of allocation based upon, or incorporating an element of, benchmarking.

25. The letter from the DTI in reply dated 23rd January 2006 failed to address any of these concerns. It is difficult to avoid the conclusion that the letter was deliberately unhelpful, since it merely recited the proposed methodology, of which the Claimant was obviously very well aware, and studiously avoided giving any answer to the concerns expressed by the Claimant. The letter did, however, state that the position of the Rugby works had been considered in the decision making for the NAP, and offered to arrange a meeting once further details of the allocation methodology were released.

26. A meeting took place on 8th February 2006 at which the Claimant repeated its concerns to the Defendant, and suggested that a benchmark should be used for the Rugby plant. In a paper presented at the meeting, and sent to the Defendant on 10th February, the Claimant said that:

"The new state of the art Rugby plant was brought on stream in 2000. Severe problems were experienced with the operation of the plant leading to very low outputs from the installation compared to its design capacity. These problems were experienced in the period 2000 to 2003".

The paper explained that the final Phase I NAP allocation to the plant (after contribution to NER) was 1,163,632. That figure was contrasted with the much lower figures for emissions in the years 2000-2003, which were set out in a table.

27. In March 2006 the Defendant published a "Detailed Guide to Phase II Allocation Methodology". It said in paragraph 6:

"In Phase I, Allocation Methodology (AM) rules (previously known as Baseline changes, Commissioning and Rationalisation (BCR) rules) were applied to tackle certain anomalies in emissions during the historic baseline period. The Government has now reviewed the Phase I AM rules, and has decided that most of them will be retained in Phase II, with some amendments. In particular, the Government has decided to revoke the Commissioning rule that applied only to the cement and power stations sectors (it allowed for all data prior to the first year of normal operations to be excluded from the baseline data used in the calculation of relevant emissions). The Government considers it more appropriate to offer a rule that can apply to all sectors. Therefore, the First Year of Operation rule has been introduced, partly to replace the Commissioning rule".

Paragraphs 7.1 - 7.3 stated:

"7.1 The Commissioning rule has been revoked and partly replaced in Phase II by the First Year of Operation rule that will be applicable to all sectors.

Calculation of Allocations and Data Requirements

7.2 The standard allocation methodology will be used for all installations that successfully applied for the Commissioning rule in Phase I - i.e. using verified baseline data for the entire installation, including periods of commissioning, to calculate relevant emissions.

7.3 All operators of installations classified in sectors to which the Commissioning rule applied in Phase I and will continue to use historic data (rather than benchmark data) must submit historic emissions data for the installation or unit(s) for any years out of 2000 to 2003 that were dropped from their baseline emissions in Phase I. They are eligible to apply for all other AM rules in Phase II".

28. On 28th March 2006 a draft Phase II NAP was published for consultation. The relevant emissions for installations that commenced operation in 2003 were the highest annual emissions in 2003 and 2004 (paragraph 3.12). Paragraph 3.30 said:

"The Commissioning rule used in Phase I will not be applied in Phase II. The commissioning rule has been replaced with a "first year of operation rule" that will apply to all sectors. More details of all of the rules to be used for Phase II are set out below and in Appendix C".

29. The First Year of Operation (FYO) rule was explained in part G of Appendix C:

"31. This rule may be used to account for entire installations that began operations (i.e. first began emitting carbon dioxide, including periods of testing and commissioning) during the baseline period (i.e. 2000-2003).

33. If this rule is applied to an installation or unit, only the years following (i.e. excluding) the first year of operation for the installation or unit concerned are used to calculate relevant emissions for that installation...."

30. Having excluded the first year of operation under the FYO rule, the calculation of relevant emissions for Phase II also excludes the year with the lowest annual emissions from the remaining years in accordance with the normal methodology: see paragraph 3.12.

31. The Claimant repeated its concerns in a presentation to the Defendant on 21st April 2006, again contending that "benchmarking could address the under allocation" for the Rugby plant. When responding to a request for Allocation Plan Data, the Claimant said in its Verification Opinion Statement dated 3rd May 2006, that the commissioning of the Rugby plant "took place over several years due to severe operational and technical problems associated with the plant".

32. On 8th May 2006 the Defendant had received a memorandum from its consultants, Entec, summarising "the potential for commissioning and ramp-up periods" in various sectors in relation to the new entrant rules. The memorandum stated that:

"There is no clear definition for commissioning as this will vary sector to sector and between different processes in the same sector. The point may be where the testing and approvals have been completed, or may signify the start of commercial production or even perhaps achieving the design capacity.

What follows is a table summarising some of the main opinions regarding commissioning. It is worth noting that Entec currently do not hold historical data that could be used to estimate definitive answers. Only in a couple of cases do we have explicit information from operators regarding commissioning and in all cases this is either comments related to the periods or unverified statements".

33. The table then set out, sector by sector, the information gathered by the consultants under a number of headings. For the cement sector that information was as follows:

"Understanding of Commissioning.

(Is there a reasonable definition?)

The BCA identifies the end of the commissioning period as the hand-over point when contracted levels are reached.

Expert Judgement on what period may be.

The commissioning period can take several months to a year or more depending on whether this is the first production of product or achieving design capacity.

What is the evidence? Can this be supported by data? Does the data exist? Is it readily available? Are there example plant?

Further data has already been sent to DTI. This information does not provide definitive data.

Opinion of whether commissioning is likely to have a major impact?

Due to the long time periods involved there is likely to be an impact upon the emissions.

Is commissioning accounted for in the proposed phase II methodology?

Yes. Ramp up period of 100 days, with 50% load during this period".

The commissioning periods in the other sectors varied from a few days to up to 6 months. In only one other case (Iron and Steel) was it up to a year.

34. The Claimant responded to the March consultation draft on 19th May 2006. Its response included the following points:

"CEMEX UK Cement does not agree with the Government's decision to completely revoke the Commissioning rule that applied to the Cement Sector in Phase I and replace it with the First Year of Operation (FYO) rule.

We are of the opinion that this change will lead to a severe reduction of our Rugby Works installation share of the Phase 2 Sector cap, compared to its share in Phase I resulting in our cement interests in the UK being put at a serious competitive disadvantage.

We urge Government to reconsider the current eligibility criteria for application of the FYO rule to allow all installations to be treated equitably and not place a minority of installations which experienced protracted commissioning difficulties, and hence have unrepresentative baseline emission data, at a disadvantage.

We propose that the eligibility criteria as stated in the Consultation Draft NAP Appendix C Section G 31 for FYO should be modified by providing that in the case of an entire installation which completed commissioning (as defined in the Phase I NAP) after the date it first began emitting CO2, the First Year of Operation should be taken as the year it completed commissioning. Obviously this would be subject to full verification by the operator.

This slightly revised definition of FYO would allow all installations to be treated equitably and would not place a minority of installations who experienced commissioning difficulties at a serious competitive disadvantage".

35. On 2nd June 2006 the Claimant applied for 2003 to be treated as the Rugby plant's first year of operation under the FYO rule. In an email dated 5th June it explained that the application was justified on the basis that the Rugby plant "suffered a difficult and protracted commissioning period". That application was refused by the Defendant and an appeal by the Claimant resulted in the Appeal Officer, David Hart QC deciding on 18th September 2006 that the Rugby plant's first year of operation for the purpose of the FYO rule was 2000.

36. The deadline for publication of the Phase II NAP and notification to the European Commission was 1st July 2006. Slightly late, on 21st August 2006, the Phase II NAP was sent to the Commission. It was received a few days later.

37. The Judicial Review Proceedings

On 22nd September 2006 the Claimant's Solicitors sent a letter before claim to the Defendant and Interested Parties. They also made representations on behalf of the Claimant to the European Commission. The Claim Form was filed on 24th October 2006. On 29th November 2006 the Commission adopted a decision in respect of the Phase II NAP. The only (minor) aspect of the NAP which was found to be incompatible with the Directive is irrelevant for present purposes. The deadline for submission of the final Phase II NAP is 31st December 2006. It is, therefore, essential that a decision is reached in these proceedings as soon as possible. On 15th November the Court ordered that there should be an expedited hearing. That hearing took place on 6th and 7th December.

38. The Claimant's Grounds

The Claim Form challenged the allocation to the Rugby plant in the Phase II NAP on five grounds. It was said that the allocation:

(1) Infringed the EC Principle of Equality or Non-Discrimination;

(2) Infringed the Right of Establishment of Cemex Espana SA (the Claimant's parent company) under Article 43 EC;

(3) Infringed Article 87 EC on state aids;

(4) Breached the domestic law principles of good administration; and

(5) Breached Article 14 of the European Convention on Human Rights.

Although numerous authorities were cited, and some 50 authorities were included in a two volume Joint Bundle of Authorities, there was very little disagreement between the parties as to the relevant legal principles. I will refer to the limited areas of disagreement below. Moreover, on reading the parties' Skeleton Arguments it was apparent that there was a considerable degree of overlap between the five grounds and that, in reality, they were to a large extent five different ways of formulating the same underlying complaint.

39. On behalf of the Claimant Mr Tromans accepted that Grounds 4 and 5 were "effectively domestic versions of Ground 1". In his Joint Skeleton Argument on behalf of the Defendant and the DTI, Mr Hoskins accepted that the Phase II NAP rules for the allocation of allowances to individual installations had to comply with the EC principle of equality; and that under that principle like situations should not be treated differently or different situations treated in the same way, unless such treatment was objectively justified.

40. In these circumstances Mr Tromans realistically accepted that, if he could establish Ground 1, Grounds 4 and 5 would add nothing of substance; and conversely, if he could not establish Ground 1, then he would be unlikely to be able to make out a case on Grounds 4 and 5. The position was similar in respect of Ground 3. He accepted that in view of the commonality of features between Grounds 1 and 3 it was likely that failure on Ground 1 would also result in failure on Ground 3. Mr Tromans accepted that Ground 2 overlapped with Ground 1 to the extent that it depended on there being discrimination between recent market entrants, but contended that, to the extent that Ground 2 did not rely on discrimination, it would not necessarily fail if Ground 1 failed. However, he accepted that the Claimant in its representations to the Commission, had argued that those aspects of the Phase II NAP which it challenges in these proceedings were in breach of EC Law for the reasons set out in Grounds 1 - 3. In its decision on 29th November 2006 the Commission did not mention these criticisms. Mr Tromans, while not abandoning Grounds 2 and 3, was content not to pursue those grounds in his oral submissions, and reserved the written submissions in his Skeleton Argument in respect of those grounds as possible grounds of appeal and/or a reference to the European Court. I turn therefore, to consider Ground 1 which is determinative of these proceedings.

41. Discrimination/Objective Justification

The Defendant was under an obligation to ensure that Phase I NAP did not discriminate between companies or sectors: see paragraph 5 in Annex III to the Directive (paragraph 4 above). On its face, the decision to apply the Commissioning rule to the power station and cement sectors treated those sectors differently from all the other sectors. Such a difference in treatment required objective justification. There can be no doubt as to what constituted that justification in the Defendant's view. As a result of consultations on the draft NAP the Defendant was satisfied that, while dropping the lowest year of emissions was sufficient to account for commissioning in all other sectors, where commissioning was "rarely a significant and protracted event", it considered that dropping the lowest year of emissions was not sufficient to account for commissioning in the power station and cement sectors because the commissioning period was more likely to take place across more than one calendar year in those sectors "where commissioning can often be a significant and protracted event": see the consultation document published on 6th May 2004, section H of the July 2004 Allocation Methodologies document, and Appendix F to the May 2005 Approved NAP (paragraphs 13, 14 and 16 above).

42. While the Commissioning rule benefited the Rugby plant, and the Defendant would have been aware that the Rugby plant was the only installation in the relatively small cement sector that would benefit from the rule, the particular circumstances of the Rugby plant were not the justification for the rule.

43. Mr Cottam explains in his witness statement why the allocation methodology was not, and could not have been, based on an examination of the particular circumstances of each individual installation. Apart from the number of installations involved (1062 in Phase I and 1069 in Phase II), and the huge variations in size between them, considering each installation individually would have compromised certainty and transparency for all participants, since they would not have been able to calculate, in advance, their likely allocation. Moreover, considering the particular circumstances at each installation could have led to allegations of discrimination by the Defendant in favour of, or against, certain operators. Mr Cottam points out that:

"... there is an enormous range of factors that can cause individual installations to have lower emissions in one year than another. To some extent, as I have said, it is inherent in a historic approach to calculating emissions that past years' data will not always be an accurate reflection of emissions in future years, and some installations will be adversely affected by this. For example, there might be a fire or a strike at a particular plant. Market conditions, poor administration or management, or maintenance problems can also all potentially have this effect. It would be impractical and unworkable, given the sheer size of this scheme, for the Government to have to take decisions as to when each

installation is operating "normally" (whatever that may mean), on which each installation would no doubt make submissions that would have to be tested and assessed."

44. While the lengthy period of commissioning at the Rugby plant was part of the overall picture in the cement sector, there was, and still is, no explanation as to why "severe problems" were experienced there, leading to "protracted commissioning difficulties". The rationale for the adoption of the "Commissioning rule" was the Defendant's acceptance of the views expressed in the Phase I consultation exercise that protracted (in excess of one year) commissioning periods were an inherent characteristic of the power station and cement sectors as a whole, and that a "significant proportion of installations" would receive less allowances than they required if the rule was not introduced for those sectors: see para. 7.40 of the 6th May 2004 consultation document (paragraph 11 above).

45. Since this was believed by the Defendant to be the justification for a rule which treated the power station and cement sectors differently from all other sectors, it follows that if, in the light of the experience and information gained in Phase I, the Defendant (a) was no longer satisfied that commissioning in the cement sector was "so significant and protracted" as to justify different treatment for that sector; and (b) was satisfied that adopting the FYO rule coupled with the exclusion of the lowest year of emissions "would deal with most periods of commissioning in all sectors", there would be no proper basis for retaining the rule (whatever other arguments there might have been for revoking it) given that the rule was no longer required for the power station sector (renamed the LEP sector) since it was to be dealt with by benchmarking. In these circumstances retaining a different rule for the cement sector alone would have been discriminatory, since there would, in the Defendant's view, have been no justification for the difference in treatment between sectors.

46. Mr Cottam explained in paragraphs 58-64 of his witness statement why the Defendant decided to replace the Commissioning rule with the FYO rule in Phase II:

"58. First, we were concerned that our treatment of commissioning in Phase I had advantaged the cement and electricity generating sectors above other sectors. That concern was underlined by the threatened judicial review proceedings I mentioned above, in which an installation claimed that it was inequitable for the Commissioning rule to be applied to just two sectors. We considered it preferable, and more consistent with our obligations under the Directive, to treat all sectors consistently in this respect.

59. Second, the Commission Guidance had advised us to simplify our rules in the interests of transparency and certainty and only to retain essential rules. Our own principles required the Phase II NAP to be straightforward to apply, well understood, and feasible within the timetable. We did not consider that it was appropriate to retain a special rule for the cement and electricity generating sectors because of information we had gathered in the course of Phase I which revealed that the commissioning periods even in those sectors were generally not as long and protracted as we had expected. Furthermore, as the electricity generating sector (called the Large Electricity Producers sector in Phase II) was being allocated via a benchmark in Phase II, the Commissioning rule would no longer be relevant to that sector (since historic emissions would not be used). Any Commissioning rule would therefore have applied to the cement sector alone.

60. We found no clear evidence of average commissioning periods being significantly longer in the cement or electricity generating sectors, nor of particularly long commissioning periods in other sectors. We had specific evidence of two cement plants being commissioned within a year (Buxton Lime Industries commissioned its Tunstead plant in 7 months in 2004, and Castle Cements its Padeswood Kiln, which uses alternative fuels, in one month). The consultants examining this issue in relation to the new entrant rules (Entec) concluded that the commissioning period in the cement sector was "several months to a year or more depending on whether this is the first production of product or achieving design capacity", however they indicated that this view was not based on definitive data. [Reference is then made to information subsequently obtained by the Defendant. The interpretation of that information is disputed by the Claimant.]

61. Obviously there will be examples in all sectors of individual installations that have particularly long periods of commissioning, and the absence of a special Commissioning rule for those installations will result in a lower emissions allocation for those operators. But for the reasons I have set out above, it would not have been possible or appropriate to find a solution that would require a consideration of the individual factual circumstances of each installation that might have led it to have a particularly difficult year.

62. Even in the two sectors to which the rule had previously been applied (cement and electricity generating), there were only three installations to which it could still have been relevant in Phase II (Cernex's Rugby plant being one of

them, the second being in the Other Electricity Producers Sector, and the third in the Combined Heat & Power Sector). As I have already explained, the Large Electricity Producers were now being benchmarked as a sector. If we had applied a special rule to only three installations we would have been in danger of violating our obligation not to favour one installation or sector over another. If we had agreed to consider submissions from all installations on the reasons why they had experienced particularly low emissions in baseline years, the scheme (involving well over 1,000 installations) would have been unworkable, difficult to apply, complicated, and the criteria would not have been transparent or consistent.

63. Third, our experience in Phase I confirmed the difficulties of trying to define "commissioning" in a way that would apply to all sectors. Our consultants looked into this question and concluded that "there is no definition of commissioning as this will vary sector to sector and between different processes in the same sector". Commissioning might be said to end "where the testing and approvals have been completed, or may signify the start of commercial production or even perhaps achieving the design capacity".

64. Fourth, we had devised a new rule which we felt dealt adequately (even if not absolutely) with the problem of low emissions due to commissioning periods. The "first year of operations" (FYO) rule for Phase II states that for any installation or unit that began operations during the baseline period, the data for the year in which it first omitted CO2 would not be used in calculations of allocations. If an installation is successful in its application for this rule to apply, the FYO rule operates in addition to the general allocation methodology that allows installations to exclude their lowest baseline year of emissions. We considered that excluding the first year and the lowest year of emissions would deal with most periods of commissioning in all sectors. That rule is consistent with the general allocation methodology for incumbents, which is based on historic emissions, and treats commissioning problems consistently with other factors that can cause unusually low emissions."

47. There was no application to cross-examine Mr Cottam, and the Claimant does not suggest that his witness statement does not accurately, if belatedly, set out the reasons for the Defendant's decision. It is clear from paragraphs 60 and 64 of Mr Cottam's witness statement that the Defendant was no longer satisfied that commissioning in the cement sector was (in the words used in Phase I) such a "significant and protracted event" as to justify different treatment from other sectors, and was satisfied that the FYO rule, since it would be applied in conjunction with the exclusion of the lowest year of emissions, would be adequate to deal "with most periods of commissioning in all sectors", including the cement sector.

48. If the Defendant was legally entitled to reach these conclusions, they are sufficient to remove the perceived justification for the different treatment accorded to the cement sector in Phase I. Conversely, if the Defendant had still been satisfied that commissioning did present particular problems in the cement sector, and that commissioning in that particular sector was so protracted that it could not normally be dealt with by excluding the first year and the lowest year of emissions, then the other reasons given by Mr Cottam: a desire to treat all sectors consistently, to simplify the rules in the interests of transparency and certainty and to retain only essential rules, and not to have a special rule which would apply to only three installations, would not have been capable of justifying the abolition of the Commissioning rule. Provided a rule is capable of applying to all installations in a particular sector which justifies different treatment it does not matter that only a limited number of installations will benefit from the rule. A desire to simplify, to treat all sectors consistently, and to retain only essential rules, could not justify a rule which treated two unlike sectors in the same way. A desire for "administrative tidiness" could not justify discrimination. It is, therefore, unnecessary to examine the other reasons given by Mr Cottam for the abolition of the Commissioning rule. They are either unnecessary (if the reasons given in paragraphs 60 and 64 of his witness statement stand up to scrutiny) or insufficient (if they do not) to justify the Defendant's decision.

49. I have used the expression "stand up to scrutiny" because Mr Tromans submitted that this was not a case where he had to surmount the high threshold of Wednesbury irrationality. The policies in Phase I having been adopted and applied on the basis of objective justification, it was for the Defendant to justify the change. In EC cases

"The Court will test the solution arrived at and will pass it only if substantial factual considerations are put forward in its justification: considerations which are relevant, reasonable and proportionate to the aim in view".

Per Laws J (as he then was) in R v Ministry of Agriculture, Fisheries and Food ex p. First City Trading Ltd [1997] 1 CMLR 250, paragraph 69.

50. Mr Tromans also referred to Joined Cases 117/76 and 16/77 Ruckdeschel [1977] ECR 1753. In those cases, two products, Starch and Quellmehl, had been treated in the same way for the purpose of production grants for many years.

The rules were changed so that the former, but not the latter product was entitled to a production grant. The ECJ said:

"While the Council and the Commission have given detailed information on the manufacture and sale of the products in question, they have produced no new technical or economic data which appreciably change the previous assessment of the position.

It has not therefore been established that, so far as the community system of production refunds is concerned, Quellmehl and Starch are no longer in comparable situations.

Consequently, these products must be treated in the same manner unless differentiation is objectively justified".

51. Mr Tromans submitted that the Defendant had not produced, or relied upon any "new technical or economic data" which changed the assessment made in Phase I: that a commissioning rule was required for the cement sector.

52. Whether there is "objective justification" for a change in policy will depend on the facts of the particular case. More will be required by way of justification if there is a change to a long standing policy (as in Ruckdeschel) and/or a change to a policy that was based upon detailed or extensive technical or economic data.

53. In the present case, Phase I of the NAP was a "pilot phase" (paragraphs 17 and 18 above). To this extent, all of the rules, including the Commissioning rule, were "on trial" for a relatively short period, and the Defendant described the implementation of Phase I as a "steep learning curve". (paragraph 17 above). The Commissioning rule was adopted by the Defendant as a response to the consultation process. The material elicited from consultees which persuaded the Defendant to adopt the rule is fairly described by Mr Cottam as "largely anecdotal", but it must be remembered that the NAP for Phase I had to be developed within a very tight timetable (paragraph 9 above). The consultation process had to be very brief if the proposed Phase I NAP was to be notified to the Commission by 31st March 2004 (in the event it was notified a month later, see paragraph 11 above).

54. In these circumstances, where a new rule treating two sectors differently has been adopted for a pilot phase of a scheme upon the basis of very limited material by way of objective justification, its revocation will require commensurately little by way of objective justification. Although the Claimant contends that the Defendant misunderstood the position at Castle Cement's Padeswood Kiln, there is no evidence (apart from that relating to the Rugby plant itself) to gainsay the Defendant's view that dropping the first year and the lowest year of emissions will deal with most periods of commissioning in all sectors, including the cement sector. The information obtained by Entec was limited (paragraphs 32 and 33 above), but their memorandum to the Defendant was structured and, putting the matter at its lowest, less jejune than the bare assertions in the Phase I consultations. While the report found that commissioning in the cement sector could take longer than in other sectors, the period was not so long that it could not be accommodated by the FYO rule, together with dropping the lowest year of emissions if commissioning spilled over into a second year. The Tunstead Plant referred to by Mr Cottam fits into this pattern.

55. The evidence of Mr Boarder, the Energy Manager for Castle Cement Limited, dealing with the commissioning of the Padeswood Kiln is also consistent with the overall picture painted by the Entec report:

"In the case of Kiln 4 at Padeswood, it commenced operation in July 2005 following lengthy delays in the consenting process. The kiln equipment itself performed well and after three months the plant operatives could operate the plant at about 80% of the design capacity. There were however design faults in the feed equipment to the new kiln relating to the raw material handling and preparation equipment, rather than the kiln itself. This caused a problem of intermittent operation which took about a year to resolve. The length of the commissioning period of this kiln, therefore, is understandably not quite as precise as paragraph 60 of Rob Cottam's witness statement would appear to suggest".

56. Indeed, the Claimant's own evidence tends to confirm the Defendant's view that the three year commissioning period for the Rugby plant was a "one off", and was not representative of average commissioning periods in the cement sector as a whole. I have set out the Claimant's representations in the Phase II consultation above (paragraphs 24, 26, 31, 34 and 35). They all emphasise "the protracted commissioning difficulties" suffered by the Rugby plant.

57. In a second witness statement in response to Mr Cottam's evidence, Dr Evans, the Claimant's Sustainability Director, refers to the particular characteristics of the Rugby plant, which employs crusher drier technology, using chalk slurry, in a semi-wet process, and states that "a commissioning period for any plant like this would be expected to be longer than a year". He also says that:

"A longer than average commissioning period is not unique to CUCL's Rugby Plant. There are several plants across the world which have also had long and protracted commissioning periods; for example, the Ketton plant in the 1980's

took several years to reach capacity; Quinn plant in Ireland took two years; and Ruddersdorf and Rochester plants in the CEMEX Group also each took several years to reach capacity".

58. The proposition that the Rugby plant suffered a longer than average commissioning period in the cement sector is consistent with the way in which the Claimant was putting its case to the Defendant throughout the Phase II consultation process. Mr Tromans submitted that the Commissioning rule was not concerned with the "average commissioning period" in the cement sector. That ignores both the contrast drawn in the July 2004 allocation methodology document (paragraph 15 above) between the power station and cement sectors where commissioning "can often be a significant and protracted event", and other sectors where it was "rarely a significant and protracted event", and the concern expressed in the May 2004 document that if a Commissioning rule was not adopted "a significant proportion of installations" could receive significantly less allowances than they required (paragraph 11 above).

59. Phase I attempted to deal fairly with what the Defendant, on the limited information then available, considered were differences between the sectors' commissioning periods. It was never intended to, and did not, deal with "one off" cases within sectors, whether that sector was the cement, or any other sector.

60. For these reasons, the complaint underlying Ground 1 is not well founded: the material relied upon by the Defendant as a justification for not continuing the Commissioning rule in Phase II is not extensive, but it is less insubstantial than the material which persuaded the Defendant that the adoption of the rule in Phase I was justified.

61. Procedural Unfairness

Having seen Mr Cottam's explanation of the Defendant's reasons for abolishing the Commissioning rule Mr Tromans applied for permission to add a sixth ground of challenge: procedural unfairness. He submitted that insofar as the Defendant's decision was based on its view that there was "no clear evidence of average commissioning periods being significantly longer in the cement or electricity generating sectors", the decision making process was procedurally unfair because this view was never expressed by the Defendant during the Phase II consultation process, so the Claimant was deprived of an opportunity to answer the point.

62. It is trite law that any consultation process must be fair, and that if the process is to be fair those consulted must be given a sufficient explanation of the reasons for the proposal to enable them to give an intelligent and informed response. Mr Hoskins did not oppose the application. He submitted that what procedural fairness required in any one case would depend upon the particular circumstances of that case. In the present case, the Phase II consultation process was complex, covering a number of topics involving a large number of consultees: 232 written responses in the July 2005 consultation and a further 82 written responses in the March 2006 consultation. Since it was not possible to devise a Phase II NAP which required an examination of the particular circumstances of each installation individually it was not incumbent on the Defendant to consult on every factual issue that might be relevant to the Phase II NAP.

63. I found these aspects of the Defendant's response to the challenge on this ground wholly unconvincing. The consultation process for Phase II was to be more focussed, with sector specific meetings (paragraph 18 above). The abolition of the Commissioning rule was identified as "the most significant proposed change" (paragraph 22 above). It affected only the cement sector, since the power station sector (renamed the LEP sector) was to be dealt with by benchmarking. Moreover, the Defendant and/or its consultants had time to meet with the Claimant on a number of occasions: on 8th December 2005 (paragraph 24 above), 8th February 2006 (paragraph 26 above) and 21st April 2006 (paragraph 31 above). There would appear to be no reason, and certainly none was advanced by Mr Hoskins, why the Defendant could not have told the Claimant at any one, or more, of those meetings that it thought that there was no evidence of average commissioning periods in the cement sector being significantly longer than in other sectors. I have mentioned the letter dated 23rd January 2006 (paragraph 25 above). It must have taken some time, and considerable care on the Defendant's part, to draft such an unhelpful letter, disclosing nothing whatsoever about the Defendant's reasons for proposing to replace the Commissioning rule with the FYO rule. It would have taken no longer to give the true reasons. Plain speaking need be no more time consuming than obfuscation.

64. It is most regrettable that although the Claimant was repeatedly expressing its concerns in meetings and in correspondence with the Defendant over a period of months, it received no proper explanation of the reasons for the abolition of the Commissioning rule until Mr Cottam's witness statement was filed on 17th November 2006, when for the first time the "average commissioning period" point was mentioned. The only explanation given in the extensive documentation was that it was considered "more appropriate to offer a rule [the FYO rule] that can apply to all sectors" (paragraph 27 above) and that it was "preferable that a rule could be applied to all sectors" (paragraph 23 above). The lack of any reasoned explanation accords with Dr Evans' unchallenged recollection of the Defendant's

response at the meeting on 8th February 2006 that the "rules had to be simple" and that there "would always be winners and losers".

65. Although this lack of explanation reflects no credit whatsoever on the Defendant, does it mean that the decision to abolish the Commissioning rule was unlawful because the consultation process was procedurally unfair? In my view, the answer to this question is 'No'. In a further witness statement on behalf of the Claimant, Mr Lewis, the Claimant's Energy Compliance Manager has stated that:

"Had we understood that DEFRA considered that there was no clear evidence of long commissioning periods in the cement industry and that this was why they were dropping the Commissioning rule, then the Claimant would have addressed the point by instructing external expert consultants".

66. The Claimant has very considerable expertise and experience in the cement sector. It is the third largest cement manufacturer in the U.K. It is, in my view, significant that the Claimant has not felt able, on the basis of its own experience, to gainsay the Defendant's proposition that dropping the first year and the lowest year of emissions would deal with most periods of commissioning in the cement, as in all other sectors. Specifically, the Claimant accepts that the Rugby plant had a "longer than average commissioning period".

67. Moreover, I accept Mr Hoskins' submission that the Claimant's representations during the Phase II consultation period were not directed to the retention of the Commissioning rule. They were emphasising the very particular circumstances of Rugby, and advocating a tailor made response to those circumstances by way of benchmarking. They were doing so because, unless the rules were further adapted to respond to Rugby's particular circumstances, retention of the Commissioning rule would not, by itself, have achieved the desired result from the Claimant's point of view.

68. If the Commissioning rule had been applied, the Rugby plant commenced operating in 2003. For installations that commenced operation in 2003 the March 2006 Consultation Document proposed that the "relevant emissions" should be the highest annual emissions in 2003 and 2004 (paragraph 3.12(d)). That position is maintained in paragraph 3.8(d) of the Phase II NAP sent to the Commission on 21st August 2006. The figures contained in the Claimant's Verification Opinion Statement showed that the Rugby plant's highest annual emissions were in 2003. In a letter dated 23rd November 2006 to the Claimant's Solicitors the Defendant stated that, by comparison with the agreed figure of 1,163,632 allowances for Phase I, an allocation in Phase II applying the Commissioning rule, and taking 2003 as the highest annual emissions, would have resulted in a figure of 1,005,756 allowances. Applying the FYO rule in Phase II it is common ground that Rugby is allocated 932,784 allowances. The figure of 1,005,756 allowances applying the Commissioning rule with no benchmarking is not agreed, but I am satisfied that it tallies with the Claimant's own figures for emissions, and demonstrates why the Claimant was not advocating the retention of the Commissioning rule, but the application of some form of benchmarking in order to reflect the unique circumstances at its Rugby plant. This approach was reflected in the Claim Form which challenged the allocation of allowances by reference to historical emissions "rather than by reference to a benchmark".

69. It is clear that, apart from the LEP sector, the Defendant had decided not to adopt benchmarking for those installations which had commenced operations in 2003. Mr Cottam explains that, among the reasons why it was concluded that benchmarking was not feasible (other than in the LEP sector) was the fact that:

"Feedback during consultation on Phase II suggested that the benchmarks were unduly generous where plant should be expected to be more efficient and require fewer allowances. Following review and revision the Government does not consider that the Phase I benchmarks are suitable for future phases".

70. In summary, whatever information was provided about average commissioning periods in the cement, as opposed to other, sectors generally, it would not have materially assisted the Claimant's case for benchmarking to deal with Rugby's atypical problems. It follows that the challenge on Ground 6 must also fail.

71. Proportionality

For the sake of completeness I have considered whether the revocation of the Commissioning rule, while objectively justified by the change in the Department's view as to the significance of commissioning in the cement sector by comparison with other sectors, was nevertheless a disproportionate response, bearing in mind the impact of its revocation on the allocation of allowances for the Rugby plant. Although proportionality was referred to in the context of Ground I (see the dicta of Laws J in the First City Trading case cited in paragraph 49 above), it was not raised as a discrete issue.

72. For the reasons set out above, the rules in the NAP could not be tailored to the circumstances of any particular

installation. There is, inevitably, an element of "rough justice" in rules such as the Commissioning rule, the FYO rule and the lowest year of emissions rule. An installation commissioning, or commencing operations early in the year may gain more from the rules than an installation that is commissioned, or commences operations later in the year. An installation that is able to drop one, very bad, year may receive a greater allocation than an installation that has two bad years, with one being only marginally worse than the other, etc. Such examples could be multiplied many times bearing in mind the many and various reasons why taking an average of a number of previous years' emissions may not be truly representative of an installation's present capacity. Why should unusually protracted commissioning difficulties at an individual installation be treated any differently from other difficulties, such as unusually protracted marketing conditions, labour, management or maintenance problems at particular installations? Commissioning difficulties in particular cases may be due, at least in part, to other difficulties such as, e.g. management or maintenance problems.

73. The figures for the Rugby plant's allowances in Phases I and II are set out in paragraph 68 above. The Defendant's letter dated 23rd November points out that if the allocation to the Rugby plant was increased as a result of applying the Commissioning rule, such an increase would result in a corresponding decrease in allocations to other installations within the cement sector, including other plants owned by the Claimant. The Defendant contends that, in net terms, the difference between applying the Commissioning rule in Phase II to the Rugby plant and its actual Phase II allocation is 66,842 allowances per year. This figure is not agreed, but it is clear that in reality, it is the move from benchmarking in Phase I to the use of historic emissions data in Phase II, rather than the replacement of the Commissioning rule by the FYO rule, that causes the greater reduction. Any move from benchmarking to historic data has the potential to advantage, or disadvantage an individual installation. The more generous the Phase I benchmarks were, the greater the potential for disadvantage. While the reduction in the allowances allocated to the Rugby plant is still substantial, and will have significant (although not as great as alleged in the Claim Form) financial implications for the Claimant over the period 2008-2012 covered by the Phase II NAP, it could not be said that the change in the rules has such a disproportionate effect upon the Claimant that it is unlawful, if otherwise objectively justified.

74. Conclusion

Having considered the arguments at some length it would not be appropriate to refuse permission to apply for judicial review. I therefore grant permission but dismiss the substantive application.

75. I would like to express my gratitude to all Counsel for their very helpful submissions.

SOLICITORS:

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