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**EIUG Response to the Consultation on the Strategy and Policy Statement for Energy Policy in Great Britain**

**Introduction**

1. The Energy Intensive Users Group (EIUG) is an umbrella organisation that represents the interests of energy intensive industrial (EII) consumers. Its objective is to achieve fair and competitive energy prices for British industry. It represents manufacturers of steel, chemicals, fertilisers, paper, glass, cement, lime, ceramics, and industrial gases. EIUG members produce materials which are essential inputs to UK manufacturing supply chains, including materials that support climate solutions in the energy, transport, construction, agriculture, and household sectors. They add an annual contribution of £29bn GVA to the UK economy and support 210,000 jobs directly and 800,000 jobs indirectly around the country.
2. These industries are both energy and trade intensive – remaining located & continuing to invest in the UK and competing globally requires secure, internationally competitive energy supplies and freedom to export without tariff barriers. However, inward investment, growth and competitiveness have been hampered for years by UK energy costs higher than those of international competitors.

***Does the strategy and policy statement identify the most important strategic priorities and policy outcomes for government in formulating policy for the energy sector in Great Britain? If not, please provide details of the priorities that you think should be included.***

1. It does not. The draft strategy and policy statement does not include the important strategic priority and policy outcome relating to the mitigation of the risk of carbon leakage.
2. The strategies and papers the statement refers to recognise the importance of addressing the risk of carbon leakage to ensure that UK industry has the confidence needed to fully decarbonise in the UK. However, this objective is not reflected in the relevant section of the government’s strategic priorities although this is even more important since the Energy Bill includes an amendment to the existing duties of the Gas and Electricity Markets Authority referencing the net zero targets in the Climate Change Act 2008.
3. The abstracts from the various government strategies and papers below show that mitigating to risk of carbon leakage should also be one of the strategic priorities to be included in the strategy and policy statement and for Ofgem to have regard to.
4. **Net Zero Growth Plan** – “*We are determined that our efforts to decarbonise industry and reduce emissions are not undermined by carbon leakage. The consultation Addressing Carbon Leakage Risk to Support Decarbonisation, published alongside this plan, is a significant step forward in setting a new framework to mitigate this risk and considers a range of domestic policy options to protect against carbon leakage, including both a carbon border adjustment mechanism (CBAM) and mandatory product standards*” (p.49).
5. **British Energy Security Strategy** – “*The Government recognises that* *UK industrial electricity prices are higher than those of other countries and will act to address this. We will extend the Energy Intensive Industries (EII) Compensation Scheme for a further three years and intend to increase the aid intensity to up to 100% (1.5% of GVA). […] We will also consider other measures to support business including increasing the renewable obligation exemption to 100%”* (p.10)*.* The recent response to the review of the schemes to partially exempt certain energy intensive industries from the cost of the renewable financing policies has confirmed that government will implement full exemptions for these industries.
6. **Net Zero Strategy** – “*We recognise the importance of addressing the risk of carbon leakage so policy interventions do not lead to increased emissions elsewhere, and to ensure that UK industry has the confidence needed to fully decarbonise. The [Industrial Decarbonisation Strategy] and the Net Zero Review set out the potential options available to address this, including regulatory standards and Carbon Border Adjustment Mechanisms (CBAMs), as well as the ongoing review of our current carbon leakage mitigation policy of free allowances under the UK ETS. Government will continue to explore options to mitigate carbon leakage, with emphasis on an international, multilateral effort to tackle carbon leakage at source through global action on industrial decarbonisation and climate regulation, with continued monitoring of related global policy developments*” (p.122).
7. “*The transition to net zero can stimulate innovation that increases domestic competitiveness and global comparative advantage for some UK industries, providing potential export opportunities. Updated internal analysis based on the Energy Innovation Needs Assessment estimates that just over half of the £60 billion GVA potential from sectoral decarbonisation in 2050 comes from export related opportunities. However, there will also be risks to sectors and industries susceptible to competitiveness impacts, particularly those that are trade exposed and/or carbon intensive. Where UK firms lose market share to international firms with lower environmental standards, there is a risk of carbon leakage. There is little empirical evidence of this occurring in the UK to date, but risks could increase as further policy is implemented*” (p.329).
8. “*The magnitude of competitiveness effects in international markets is dependent on global climate ambition as well as domestic policy. If other countries, particularly the UK’s trading partners, increase their industrial decarbonisation ambition in line with the UK’s, and face similar transition impacts, then competitiveness effects will be smaller. Similarly, where the UK’s path to net zero creates export opportunities for UK businesses, the size of these will depend on the actions of the rest of the world. High global climate ambition will result in a large market for decarbonisation technologies and services but may also result in more global competition in those markets*” (.329)
9. **Industrial Decarbonisation Strategy** – “*Decarbonisation also creates challenges for industry. Many essential low carbon technologies are in earlier stages of development, and not yet deployed regularly at a commercial level. Low carbon manufacturing will also be more expensive for some sectors, leading to an increase in their costs, and therefore risking a reduction in their competitiveness. This creates a risk of “carbon leakage” (Chapter 2), which could impact both our domestic and global climate goals. We need to work with industry to overcome these barriers in the coming decades. Any action taken will need to be consistent with our international obligations, both under the Paris Agreement and wider international trade rules*” (p. 18).
10. “*Where decarbonisation leads to significant costs that creates carbon leakage risk, it should be supported by targeted intervention to mitigate this risk”(*p. 19).
11. **HMT Net Zero Review** – “*2.20 Climate rules and policies designed to reduce emissions in a given country can increase the costs of production of its businesses (including indirectly because of the impact on the price of inputs, such as energy) relative to international competitors if those competitors are subject to weaker climate change mitigation policies. 2.21 If such rules and policies (such as carbon pricing, or other emissions reduction policies), are not implemented in an equivalent way across jurisdictions, this can result in production and the associated greenhouse gas (GHG) emissions being displaced, undermining the original environmental objective of climate mitigation policies - this displacement of GHG emissions is known as carbon leakage*”.
12. Government has recognised the risk of carbon leakage and that UK industrial electricity prices are higher than those of other countries and has therefore taken measures to mitigate this risk by reducing industrial electricity prices in particular by providing compensation for the indirect emission cost due to the UK ETS and carbon price support mechanism, full exemptions from the indirect cost due to its renewable financing policies, reduction in the climate change levy in return for climate change agreements, exemption from the indirect cost of the capacity market levy and (part) compensation for network charges.
13. However, Ofgem has not taken the risk of carbon leakage into account in its regulatory decision-making and network charges (£/MWh) are higher for energy intensive industries in the GB relative to network charges in other European countries (see [CEPA](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1095296/CEPA_BEISNetworkChargesAllocation_FinalReport_20190322.pdf) (2019) *Allocation of Electricity Network Charges to Different Consumer Groups in Selected Countries*).
14. To avoid (further) misalignment between Government and Ofgem, the strategy and policy statement should include the mitigation of the risk of carbon leakage in its priorities listed and for Ofgem to have regard to mitigating the risk of carbon leakage.

***Does the strategy and policy statement effectively set out the role of Ofgem in supporting government to deliver its priorities? If not, please identify where these expectations could be made clearer.***

1. The draft strategy and policy statement does not effectively set the role of Ofgem in supporting government to deliver its priorities.
2. As stated above, the statement does not set the government’s strategic priorities in relation to mitigating the risk of carbon leakage. The section above gives the relevant abstracts of the various government strategies and papers.
3. The EIUG suggests that the role of Ofgem in supporting the government to deliver on its priority to mitigate the risk of carbon leakage should include the following:

* Assess the redistributive impact of its regulatory decisions on different consumer groups, including energy intensive industries, and avoid that certain groups structurally face a higher price increases relative to others due to its decision-making;
* Work with government so it has up to date and forward-looking retail energy price data, in particular around the impact of network charging.
* Support the administrator that will administer the [network charging compensation scheme](https://www.gov.uk/government/publications/energy-security-bill-factsheets/energy-security-bill-factsheet-network-charging-compensation-scheme-for-energy-intensive-industries#:~:text=The%20NCC%20Scheme%20is%20to,and%20to%20appoint%20an%20administrator.) for energy intensive industries, following royal assent of the Energy Bill;
* Take a more whole-system approach to network charging and include other variables, such as investment cost and congestion, as allowed under the legislative framework instead of pure cost-reflectivity (ie cost / consumption).
* Work with ACER to align its interpretation of cost-reflectivity more with its counterparts in Europe, in particular in relation to energy intensive industries.

1. As the figure below from the final CEPA report *Allocation of Electricity Network Charges to Different Consumer Groups in Selected Countries* for BEIS from 2019 shows, variety of use of system charges in European countries vary significantly because energy regulators have different interpretations of cost-reflectivity.



1. Ofgem’s interpretation of cost-reflectivity means that network charges for electricity intensive industries in the GB are generally higher than in other countries. This puts certain energy intensive industries at a competitive disadvantage and increase the risk of carbon leakage.
2. The Government has recognised this issue in relation to policy cost on industrial electricity prices and has implemented various measures to reduce these cost via compensation and exemptions.

***Given the Future System Operator does not exist yet but will need to have regard to the strategy and policy statement once it does, do you consider that we have effectively reflected the Future System Operator’s role in this document? If not, please identify where these expectations could be made clearer.***

1. The statement reflects the role of the Future System Operator reasonably well.

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