Budget 2014: submission from the **Energy Intensive Users Group**

Compensation Package for Energy Intensive Industries

The Energy Intensive Users Group (EIUG) represents manufacturing sectors including steel, chemicals, paper, mineral products, glass, ceramics and industrial gases that operate in global markets and depend on access to secure, internationally competitive energy supplies to remain in business. Energy Intensive Industries (EIIs) employ 225,000 workers directly, providing indirect employment for over 800,000 workers, and contribute over £15 billion to UK GDP.

EIUG welcomed the announcement in Autumn Statement 2011 of a £250m compensation fund to mitigate the indirect impact of the EU Emissions Trading Scheme and the UK-only Carbon Price Floor (CPF) on electricity prices to trade-exposed electro-intensive industries, recognising that funding would need to be developed in terms of scale, scope and duration in due course. We similarly welcomed the joint announcement by the Secretaries of State at BIS and DECC that certain energy intensive industries were to be partially exempted from the additional costs of Contract for Difference feed in tariffs (CFDs) for low carbon electricity generation, and the confirmation in Budget 2013 that compensation for the indirect impact of CPF would be extended until 2016.

However, not all electro-intensive UK manufacturing companies will necessarily receive compensation, and those that do qualify will only be partially compensated for the impact of those elements of climate policy currently covered by the package, whilst being left fully exposed to the impact of others (such as existing renewable subsidies) that are not yet covered. We therefore believe that the threat to these companies' international competitiveness must be mitigated by widening the scale, scope and budget of the compensation package.

EIUG has four specific areas of concern, which we urge Treasury to consider ahead of Budget 2014:

Duration of the compensation package

EIIs require confidence in the duration of compensation measures in order to continue investing in the UK (a situation analogous to that for low carbon power generation). It is essential therefore to give a clear signal about the intention to maintain compensation so long as equivalent climate policy costs do not apply to EIIs in competitor economies within the EU, or indeed elsewhere. We appreciate there is a limit to the extent to which any government can commit itself to future funding (or more accurately, in this instance, to forgo future revenue) but believe it would be both practical and desirable to make a public commitment to maintaining the compensation package until 2020.

Compensation for the impact of Renewable Subsidies

In contrast with established practice elsewhere in the EU, no compensation or exemption has yet been proposed for the mounting impact of the Renewables Obligation and the Feed in Tariff for small scale renewables on UK EIIs. Existing renewable subsidies account for around half of the uplift in UK industrial electricity prices attributable to climate policies and DECC forecasts confirm that their impact is set to carry on growing until at least 2017, with major legacy costs running well into the next decade and possibly beyond. We believe the EII compensation package should be extended to cover these costs, to the maximum extent permissible under EU state aid rules across all EII sectors, in line with practice in other Member States.

Trajectory of the Carbon Price Floor

The longer term competitiveness of EIIs will remain at risk if the CPF escalates in line with the trajectory as initially proposed. Whatever the theoretical benefits of the CPF at the time it was initially proposed, it is now abundantly clear that no other country in Europe – or indeed the world – is prepared to consider placing a similar burden on its power generators, and hence ultimately on its electricity users. It is also clear that the CPF will have no material effect on low carbon investment in the UK power sector (which will be largely supported by CFDs), nor can it reduce power sector carbon emissions overall, since these are subject to an EU-wide cap. Its principal consequence therefore is to increase the proportion of EU power sector decarbonisation costs that are to be borne by UK electricity users. All EIIs are set to be exposed to the escalating impact of the CPF on electricity prices, even if they are fortunate enough to qualify for partial compensation or exemption (EU state aid guidelines appear to require at least 20% exposure). The impact on EIIs that narrowly miss out on compensation (eligibility may be denied as a result of unduly restrictive EU guidelines) will remain wholly exposed, as will other less intensive manufacturing industries, some of which are also suppliers and customers of EIIs. We recognise that it could be impractical to alter declared CPF levels for the immediate future, but we believe the trajectory from 2015-16 and into the next decade must be modified (e.g. by freezing, or linking to CPI) if the CPF is to be rendered economically sustainable. This is a measure that would benefit all energy intensive companies.

Trajectory of the Levy Control Framework

We would welcome any opportunity to adjust the trajectory of the Levy Control Framework to reduce the future cumulative impact of climate policy measures on electricity prices. A revised longer term trajectory, allowing the market to deliver more internationally competitive electricity prices, would benefit all companies in our membership. An earlier than expected move to auctioning for developed technologies such as biomass and onshore wind would appear to provide such an opportunity.

We trust that explicit reference will be made to these concerns (provisionally, if need be) either in the Budget statement itself, or in additional material published at the same time.