

PARLIAMENTARY DEBATES

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OFFICIAL REPORT

Tenth Delegated Legislation Committee

DRAFT RENEWABLES OBLIGATION
(AMENDMENT) (ENERGY INTENSIVE
INDUSTRIES) ORDER 2017

Thursday 23 November 2017

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The Committee consisted of the following Members:

Chair: SIOBHAIN McDONAGH

† Bacon, Mr Richard (*South Norfolk*) (Con)
 † Cadbury, Ruth (*Brentford and Isleworth*) (Lab)
 † Courts, Robert (*Witney*) (Con)
 † Double, Steve (*St Austell and Newquay*) (Con)
 Ellman, Mrs Louise (*Liverpool, Riverside*) (Lab/
 Co-op)
 † Fletcher, Colleen (*Coventry North East*) (Lab)
 † Grogan, John (*Keighley*) (Lab)
 † Harris, Rebecca (*Castle Point*) (Con)
 † Metcalfe, Stephen (*South Basildon and East
 Thurrock*) (Con)

† Onwurah, Chi (*Newcastle upon Tyne Central*) (Lab)
 † Perry, Claire (*Minister for Climate Change and
 Industry*)
 † Pidcock, Laura (*North West Durham*) (Lab)
 † Pursglove, Tom (*Corby*) (Con)
 † Sturdy, Julian (*York Outer*) (Con)
 † Sunak, Rishi (*Richmond (Yorks)*) (Con)
 † Twist, Liz (*Blaydon*) (Lab)

Peter Stam, *Committee Clerk*

† **attended the Committee**

Tenth Delegated Legislation Committee

Thursday 23 November 2017

[SIOBHAIN McDONAGH *in the Chair*]

Draft Renewables Obligation (Amendment) (Energy Intensive Industries) Order 2017

11.30 am

The Chair: Before I call the Minister to move the motion, I wish Colleen Fletcher, the Opposition Whip, a very happy birthday. I hope that your day gets better from here.

The Minister for Climate Change and Industry (Claire Perry): I beg to move,

That the Committee has considered the draft Renewables Obligation (Amendment) (Energy Intensive Industries) Order 2017.

It is a pleasure to serve under your chairmanship, Ms McDonagh. May I join you in wishing enormous felicitations to the Opposition Whip, the hon. Member for Coventry North East, on her birthday?

The order will amend the Renewables Obligation Order 2015, which provides the legislative framework for the operation of the renewables obligation scheme in England and Wales. The draft order makes provision for indirectly exempting eligible energy-intensive industries from up to 85% of the policy costs of funding the renewables obligation scheme. It aims to avoid putting such industries at a significant competitive disadvantage and, as a second-order effect, to improve the cash flow and management of the scheme.

I will turn to the importance of the energy-intensive industries, or EIIs as they are often called. The transition to a low-carbon economy and the securing of our energy supplies must be done in a way that minimises the cost to business and domestic consumers. Our industrial gas prices are internationally competitive, but our industrial electricity prices have moved out of line with other European countries. As is set out in the clean growth strategy, which was published a couple of months ago, the UK's industrial electricity prices for large consumers were the highest after Italy's in 2016. That places our electricity-intensive manufacturing industries at a competitive disadvantage and increases the risk of international carbon leakage, where businesses relocate because of costs related to climate policies. That means that jobs and productivity are offshored, too.

To meet our legally-binding climate change and renewable energy targets, we have implemented a number of policies designed to incentivise the generation of electricity from renewable resources. The costs of those policies—or the investment—are recovered through obligations and levies on suppliers, which pass the additional costs on to their customers. The renewables obligation scheme is such a policy. Since 2002, it has been the main financial mechanism to deploy renewable electricity generation in the UK. We all know and should celebrate the enormous success we have seen in moving away from dirty fossil fuel

power generation to renewable sources. In 2002, 2.9% of our electricity was created from renewable sources. Last year, the figure had gone up to 25%.

The RO scheme is funded through an annual obligation on UK suppliers to present a certain number of renewables obligation certificates to Ofgem, which is the administrator of the scheme, in respect of each megawatt-hour of electricity supplied. Suppliers pass the costs of meeting their obligation on to electricity consumers. The impact of those policy costs on the bills of energy-intensive industries can reduce the attractiveness of the UK and increase the burden on what can be important strategic industries. If the Committee is interested, I am happy to provide a full list of all the industries that currently qualify for the exemptions. It is things such as steel, petroleum products and ceramics—things that we all value and want to keep working in the UK.

We have been compensating eligible EIIs for the indirect cost of the renewables obligation since December 2015. That year, we announced that the Government would move from a compensation scheme to an exemption scheme to ensure that eligible industries have long-term certainty and remain competitive. As I said, there is a second-order effect in terms of making the cash-flow management for these companies even more effective.

On 30 October, the Electricity Supplier Obligations (Amendment and Excluded Electricity) (Amendment) Regulations 2017 were made, providing an exemption for EIIs from up to 85% of the costs of the contracts for difference scheme. The order aims to do exactly the same thing for the same group of industries and companies exposed to additional costs arising from the renewables obligation, and exempts them from up to 85% of the cost. The exemption scheme, unlike the compensation scheme, allows real-time changes in energy use to be taken into account and provides greater certainty to businesses. It means that businesses do not have to go through the fairly tortuous process of paying the bill and then applying for compensation, and seems to me a far more cost-effective way of delivering the scheme.

The administration of the RO exemption, including the application and certification process, will be carried out through processes that are already in place in respect of the CfD exemption. Of course, this comes at a cost. We recognise that the EII exemption will redistribute the costs of the RO to other electricity consumers. We estimate that that will increase average annual household electricity bills by about £2.30 in the period to 2027-28.

However, as I set out clearly in the clean growth strategy, although we have seen some increase in the costs of energy, related to the various policy decisions that we have all taken to invest in renewables and our clean future, the average energy consumption in a household has gone down, primarily because of far greater energy efficiency in the home, which includes the redistribution effect of schemes such as the energy company obligation that have directly targeted energy efficiency. That means that average household energy bills fell by £14 between 2012 and 2016. Colleagues will know that we have published a draft Bill that would require Ofgem to impose a price cap on standard variable tariffs. We believe that it is time to bring to an end the unjustifiably high prices paid by many of the most loyal customers of the energy suppliers.

Colleagues will also have seen that we asked Professor Dieter Helm to do an all-singing, all-dancing, super-deluxe review of the cost of energy and particularly business energy costs. We are taking the time to assess his proposals carefully and have launched a call for evidence to open up the debate. I encourage all colleagues to submit evidence.

As I also set out in the clean growth strategy, the pool of carbon emissions emitted by industry and businesses is now the largest in the UK. That is what we need to target, and we have the aim of improving energy efficiency by at least 20% by 2030. Of course, that will not only cut emissions, but reduce the costs that industries pay for their overall energy. We are working with the most energy-intensive sectors to implement the joint action plans that we have developed with them on industrial decarbonisation and energy efficiency.

The order makes a number of amendments to the Renewables Obligation Order 2015 to provide the legislative basis to exempt eligible EIIs from up to 85% of the indirect costs of the RO scheme. In particular, it makes changes to the methodology for calculating the size of the annual supplier obligation, referred to as the obligation level, to reflect the fact that it will be applied to a narrower consumption base, as up to 85% of electricity supplied to eligible EIIs will be exempt. That will result in a proportionately higher obligation in respect of electricity supplied to non-eligible consumers.

The order also changes the scope of the obligation to exclude electricity supplied to eligible EIIs. That means that the obligation level for electricity supplied in England and Wales will be applied to 100% of electricity supplied to non-eligible consumers and at least 15% of the electricity supplied by licensed electricity suppliers to eligible EIIs. The order imposes additional requirements on electricity suppliers to provide information to Ofgem and the Department for Business, Energy and Industrial Strategy about the supply of electricity to eligible EIIs for the RO's end-of-year supplier compliance process.

The order sets out a process for introducing the exemption, which will entail calculating and publishing a revised version of the 2018-19 obligation level to take into account the new methodology. That process has been carefully designed to provide some lead-in time for suppliers and eligible industries to ensure that processes are in place to administer the exemption smoothly and that suppliers, especially smaller independent companies, have a chance to adapt their systems.

The Government intended the exemption to be introduced in January 2018. However, the timings for achieving that start date have passed, so, subject to parliamentary approval, we expect the process to be implemented from 1 April 2018 and to publish a revised 2018-19 obligation shortly.

It is worth reminding the Committee that the territorial extent of the order is England and Wales. We intend the exemption to apply right across Great Britain. The Scottish Government have devolved responsibility for administering the RO in Scotland, and they have approved an equivalent provision for delivery of the RO exemption through the draft Renewables Obligation (Scotland) Amendment Order 2017, so we have cut off the possible risk of carbon leakage. The exemption will not be introduced in Northern Ireland at this stage, but could be extended to Northern Ireland in the future. As a

devolved policy matter, it will be up to the restored Northern Ireland Executive to take it forward if they so decide.

The House of Lords Secondary Legislation Scrutiny Committee raised a number of points following its scrutiny of the draft order. The main ones were why we had decided on the change so soon after the compensation was introduced and whether we were seeking state aid clearance to extend the renewals obligation to direct competitors, by which I mean companies that, given the threshold test for participation in the scheme, are in the same industry but will not be eligible for the help.

I will summarise the main points. With regard to the changes in the exemption, the compensation schemes were introduced in January 2016 following their announcement in the 2014 Budget. The autumn statement announced that we would move towards that exemption basis. As I said, we think that moving to an exemption scheme provides additional benefits to EIIs—namely, increased certainty, real-time support and a far more streamlined administrative process than a compensation scheme.

The point about direct competitors is very valid. We have submitted a state aid notification to the European Commission. The Commission does not think our proposal is compatible with relevant state aid guidelines, but I am very keen to explore alternative options that we could bring forward within the scope of the guidelines to preserve parity within industry groups.

The draft order will make the necessary changes to the Renewables Obligation Order 2015 to allow us to exempt eligible EIIs from up to 85% of the indirect costs of funding the RO scheme. It provides companies in many of our most crucial and strategic sectors with greater long-term certainty. The measures set out in the order reduce the price differential between our extremely important domestic industries and their international competitors, removing the opportunity for a competitive disadvantage and the temptation to offshore what we know are incredibly valuable industries and jobs right across the UK. I commend the order to the Committee.

11.42 am

Chi Onwurah (Newcastle upon Tyne Central) (Lab): It is a great pleasure to serve under your chairmanship, Ms McDonagh. I start by thanking the Minister for bringing the draft order forward, and the Government for devoting attention to this important area—though not in as timely, transparent or logical a fashion as we would have desired.

For the benefit of the Whips and those Members with pressing engagements, I shall start by saying that the Labour party does not oppose this statutory instrument. We support the ends: the aim of lowering the cost of electricity for industries that use electricity intensively, where that cost is increased by green and social obligations. However, we have serious concerns about the means that the statutory instrument uses to lower those costs and regret that the Government are incapable of providing the support that energy-intensive industries merit.

Although energy costs account for 3% of UK business expenditure on average, there are sectors where that figure reaches 10%, including steel, cement, paper, ceramics, glass, chemical industries and others. They are referred to, as the Minister set out, as energy-intensive industries.

[*Chi Onwurah*]

Those industries play a crucial role in our economy, contributing more than £52 billion to our GDP and supporting 600,000 high-quality, skilled jobs. That is an important point, because our economy lacks high-quality, skilled, well-paid jobs.

Steel in particular has been crying out for support. It produces an economic output of £1.2 billion and employs 31,000 people, contributing 0.1% of the UK economy and 0.7% of manufacturing output. Let me emphasise again that those are high-quality, highly skilled jobs, which we wish to see retained and expanded in a productive economy.

The value that those industries bring to the UK economy in terms of jobs and economic output is therefore considerable. They are an important part of our manufacturing base and have a crucial role to play as part of any successful future industrial strategy. Energy-intensive industries are frequently foundation industries, producing materials that are an important part of supply chains for other industries in the UK. In an increasingly volatile world, we need strong foundation industries in Britain to ensure security in the supply of the materials on which our economy depends.

However, as we work towards a greener future and fulfil our international obligations to reduce carbon emissions, we need to develop manufacturing methods that are sustainable, including in their use of energy. That was what the renewables obligation, which was brought in by the last Labour Government in 2002, sought to achieve, by providing support drawn from energy bills for the development of renewable energy, and thus contributing to meeting the UK's EU target to produce 15% of our energy from renewable sources by 2020 and our low-carbon goals. As the Minister set out, that system was superseded by a combination of the feed-in tariff for small-scale generators and contracts for difference for large-scale generators, but existing projects benefited from the renewables obligation and will continue to do so for a number of years.

This policy necessarily exposes companies in energy-intensive industries to higher electricity bills, to which they are more vulnerable than other electricity consumers. The costs are significant. For a business using 10 GW of electricity a year, we are talking about £215,000. As most energy-intensive industries operate in international markets, those costs place them at a competitive disadvantage, and increase the risk of investment leakage through businesses choosing instead to make investments in countries with less ambitious climate policies.

That would be disastrous for UK industry and for the security of our supply of foundation materials, as I have indicated. As the Minister hinted, it would also effectively export our carbon emissions: we would continue to use the same or greater amounts of steel, ceramics and other materials, but would have to import them from countries where environmental regulations are weaker. It is worth noting that even before the effect of the renewables levies, UK energy prices are high by global standards. UK prices were equal to industrialised country averages in 2010, but 40% higher than the average by 2015.

The order intends to address the continuing cost of the renewables obligation on energy-intensive industries. As the Minister set out, it will set up a regime whereby

energy-intensive industries are exempt from 85% of the cost that would otherwise accrue to them as a consequence of the renewables obligation regime. It replaces a scheme set up in 2015 that provided for a rebate to go to companies operating in energy-intensive industries. That scheme was suspended in the summer of this year for reasons that the Government have still, even after the Minister's speech, not made entirely clear. I would appreciate it if the Minister provided some more clarity on that point.

The new regime that will be established by the statutory instrument differs substantially from the scheme that was previously in operation, chiefly in so far as it exempts energy-intensive industries from renewables obligation costs, and places the cost of exemption on to other non-exempted energy users. It is quite literally robbing Peter to pay Paul.

Claire Perry: I want to clarify that, because I raised exactly the same question at the briefing. As I understand it, right now the funding for this obligation and for contracts for difference is basically paid for by taxpayers. It comes out of the BEIS budget. Taxpayers are also energy consumers, so this is simply a question of whether we take the money out of our taxes or directly from the companies. It seems to me that it is probably a much more efficient scheme to—

Chi Onwurah *indicated dissent.*

Claire Perry: The hon. Lady shakes her head, but she and I both know that getting money out of the Government is complicated. If we want to help these industries, which she and I violently agree are critical to Britain, given the jobs within them, it seems to me far more streamlined and beneficial for them to work directly with their suppliers, rather than having to apply to BEIS and get money out of taxpayers, which is essentially coming out of our pockets.

Chi Onwurah: I thank the Minister for that intervention—it is always good to have a debate—but I disagree with her strongly. It should be difficult to get money out of the Government; that could be called accountability. The reason we have a Government is that they take decisions on behalf of the population—the citizens as a whole—that support the Government's values and objectives. The Department for Business, Energy and Industrial Strategy should set out those objectives, including greater renewable energy and support for our foundation industries, in its industrial strategy, and be prepared to support them financially. Perhaps that is a key difference between my, and Labour's, vision of Government and that of the hon. Lady. We believe that the Government and the public sector can make positive interventions in an entrepreneurial and innovative way to fulfil the ambitions and the potential of our industries and citizens.

Claire Perry: The hon. Lady is very smart; she really is one of the few intellectual thinkers. The Government do not have their own money. Government money comes from the same people who are paying the electricity bills. It is other people's money. It comes in as taxes and we also pay our energy bills. She and I, and everybody in this room, contribute to Government funds. I am sorry, but this is a very important point. As a Government—

The Chair: I am glad that there is a heated debate; that is all to the good. However, the Minister will get an opportunity to sum up, and I suggest to her that her interventions are becoming speeches.

Claire Perry: I apologise profusely.

Chi Onwurah: Thank you, Ms McDonagh. I am glad to have inspired such passion in the Minister. You must allow me a brief response on the difference between taxation and energy bills. Taxation is decided by the Government, comes generally from the people—hopefully in a progressive way, where the greatest shoulders bear the greatest burden; not as it is under this Government—and is then redistributed. When it comes to energy bills, however, the people who are the poorest and coldest may bear the greatest burden. Ms McDonagh is looking at me as if I may be exhausting her patience, so let me move swiftly on.

The explanatory memorandum suggests that the legislation will cause real problems, specifically for small and medium-sized companies, which will see their bills increase substantially. The Minister made reference to consumers, and the increase that they will see. According to the explanatory memorandum, for small business energy users the increase is likely to be £160 per year, but for a medium-sized business energy user it is likely to be about £6,700 per year. To put that in context, the Business Energy monitor sets out that the average small business spends just over £2,000 per year on electricity, and the average medium-sized business spends £3,146 per year on electricity. The increase necessitated by the statutory instrument is huge—seemingly a tripling of electricity bills for medium-sized businesses. I hope that the Minister will say what the actual impact on businesses will be in percentage terms, and what discussions she has had with the Federation of Small Businesses, for example, to assess that impact. From a party that styles itself as the party of enterprise and the entrepreneur, this is alarming to say the least.

How did the Government arrive at such a drastically unfair solution to what should have been a reasonably simple exercise of updating or replacing the rebate system? In spring 2016, the Department for Business, Innovation and Skills consulted on a new scheme to replace the rebate scheme. The consultation ran for eight weeks and looked in detail at the plans to implement an exemption scheme, receiving 69 responses. I am unclear as to how, after consulting on the proposals, the Government arrived at this solution, which will hit the bills of ordinary energy customers, and particularly small and medium-sized enterprises. Are the Government happy that this exemption scheme will put costs up for small businesses—the backbone of our economy? Have they considered any other methods of ensuring that non-exempted customers do not have to bear the costs of the scheme in the way that has been set out?

It is worth noting that the effect of the statutory instrument is to replace an energy-intensive industries compensation scheme for the effects of the renewables obligation with an exemption scheme. That means that the Government will save the money that previously went out in compensation and require the equivalent of what they have saved to go on to customers' bills instead. The additional costs on bills undoubtedly will need to be shown. Is it the Government's intention simply to lump them in with green and social costs, or

to account for them separately? Will the Minister also say how, where and whether the money that has been saved—as she set out—from the BEIS budget is being spent, or whether it is returning to the Exchequer?

The Minister mentioned that the timing of the new scheme is falling behind. The explanatory note published with the order states a firm intention that the exemptions should come in on 1 January. The Minister set out that that date will now be missed, with a four-month delay until 1 April, as I understand it. Why has that delay been allowed to happen, and what effect will that have on the finances of energy-intensive industries? It gets worse, because the Government intend to make the changes set out in the instrument alongside another statutory instrument, the Electricity Supplier Obligations (Amendment and Excluded Electricity) (Amendment) Regulations 2017.

The Chair: Thank goodness that is not what we are discussing today.

Chi Onwurah: Absolutely.

Mr Richard Bacon (South Norfolk) (Con): Can you say that again?

Chi Onwurah: I could, but I will not. That legislation was laid in draft in March 2017 and was subject to a continuation motion in June, but I understand that it has not yet been formally debated and agreed. That statutory instrument contains a number of amendments to the 2015 legislation, in addition to those proposed in the order we are discussing. In particular, it includes a schedule specifying which industries are to be exempt, which the Minister mentioned.

It looks, on the face of it, as though the regime that is due to come into place as a result of the order will be uncertain in its extent, and hence difficult for companies to plan for, since there will remain unfinished business in terms of definition and other matters. Does the Minister accept that and does she think that that will affect the timetable for implementation further, with a possible delay beyond 1 April? Why were the draft regulations not laid simultaneously with the order we are debating, so that we could have enjoyed debating them both and so that the uncertainty could have been cleared up straightaway?

Yesterday's Budget has thrown up a new flaw in the Government's policy in this area, which I would argue demonstrates the lack of seriousness with which they are treating the task in hand of supporting our energy-intensive and foundation industries. In the updated levy control framework that was released yesterday, the Government committed to

"no new low carbon electricity levies until 2025."

If I am not wrong, this statutory instrument seeks to implement just that—a new low carbon electricity levy. Will the Minister confirm that this is yet another example of the Government tying themselves in knots and U-turning on a policy before it is even brought into law?

In conclusion, our party does not support this system for the long term. If a Labour Government had been elected in June, we would not have done it in this way. We call on the Government to review the system with a view to returning to a rebate system, provided that we establish continuity of rebate and a stable environment

[Chi Onwurah]

for energy-intensive industries to work in. However, we recognise the urgent need to reinstate some form of cost-reduction scheme for the renewables obligation costs of energy-intensive industries. As such, although we have put on the record strongly and at some length our disagreement with several aspects of the statutory instrument, we will not oppose it.

12 noon

Claire Perry: I will endeavour to be brief and less passionate. I thank the hon. Lady for her thoughtful response. I am delighted that we are in violent agreement about the need to support these incredibly valuable industries and the thousands of high-skilled, productive jobs for the people they employ across the UK.

I will clarify a couple of points. The current scheme has not been suspended—I am not quite sure where that came from. It continues until the exemption is introduced, which will now be in April, so the normal rules will apply.

The hon. Lady asked a sensible question about the impact of the order on small businesses. SMEs can apply as well; it is not a size test, but a measure of what percentage of a company's gross value added is spent on energy.

Chi Onwurah: I thank the Minister for that clarification; it is an important point. SMEs can apply for the exemption but they would need to be in energy-intensive industries, as set out in the schedules to the 2015 order, which I understand will be updated. They may not know, as yet, whether they can apply for it. They may have a large bill without necessarily being in an energy-intensive industry.

Claire Perry: I am happy to clarify again. First, because the schedule of energy-intensive industries is already known—businesses already know if they are classified as in that sector—the test is whether they are energy-intensive users, regardless of their turnover. The measure is based on energy as a percentage of profits and labour costs. Businesses of all sizes can apply. Because the order effectively aligns the RO measures with the CfD measures, it is the same certification

process. Based on the legislation that we introduced recently, businesses will already know and will be able to say, “We have the certification and we will take that to our suppliers.” There should be certainty out there among businesses as to whether they can apply. The hon. Lady and I have the same thinking: what happens if energy bills fluctuate wildly? My understanding is that when a business is certified as eligible, that certification lasts for five years, so that gives businesses a sense of certainty for their future cost planning.

On the hon. Lady's point about additional costs, the overall impact is assessed at something like 0.5% of energy costs. I will write to her with the exact number. She is right that we want to ensure that there is no enormous uplift for businesses. As I tried to point out, one way of thinking about it is that businesses already pay a number of obligations to the state, such as corporate taxes and business rates. In effect, some of that money was coming back to them in the form of exemptions, but it was not coming back to all businesses. I think the fact that businesses that were not getting the money back will now see a bit going on their energy bills provides a more transparent system, as she said.

This is not a new levy; it is an application of the old scheme. The hon. Lady understands about business and she knows that it can be difficult for someone trying to manage their cash flow to have to apply to Government and wait for money that could take several months to come through. Simply having that money taken off their bills before they pay them has to be a better way for a small business owner or a financial manager to operate.

I am delighted that we have the Opposition's support on this. It is an important measure to support some of our most strategic industries. I thank Committee members for their patience and support. We want to try to safeguard the competitiveness of these industries. I therefore commend the draft order to the Committee.

Question put and agreed to.

Resolved,

That the Committee has considered the draft Renewables Obligation (Amendment) (Energy Intensive Industries) Order 2017.

12.5 pm

Committee rose.