Debate hots up over green breaks for big energy users

The government’s attempts to shield energy intensive industries (EIIs) from higher energy costs bought on by environmental legislation are coming under attack from all sides.

Last week, at the end of a consultation period, MPs said a proposed £250m compensation package for EIIs - designed to offset costs from the Emissions Trading System (ETS) and carbon price floor - must be altered as it fails to account of profits made from emission permit over-allocations. And more seriously perhaps, the European Union is considering an investigation into whether EII exemptions from the cost of green energy development – resulting from renewable price guarantees - break EU rules on state aid to business, which could threaten UK EII exemption plans before they’ve even left the drawing board.

The EU’s move was precipitated by complaints from smaller energy users in Germany, where such exemptions have been in place for many years. Commenting on the possibility of a similar move from small businesses in the UK, a spokesperson for the Department of Energy and Climate Change (DECC) told Utility Week: “We will be consulting on the scope of the [EII] exemption, including who will be eligible, early this year, so we can’t say at the moment who might be exempt and how [UK] small businesses may view this.”

As far as smaller UK users are concerned, John Walker, National Chairman, Federation of Small Businesses, told Utility Week: “The cost of energy is becoming a make or break issue for small firms and any policies that are likely to further increase small firms’ energy bills is obviously unwelcome news. The FSB will monitor with interest the scope of DECC’s proposals for the exemptions for energy intensive industries to see how small firms could be impacted. We believe reform of the electricity market and investment in low carbon energy generation should not unfairly penalise our members and needs to go hand in hand with real changes to the retail energy markets to ensure small firms get the fair deal they deserve at the hands of the big six energy companies.”

The DECC spokesperson acknowledged that exempting EIIs would indeed, “result in a slight increase in electricity costs for other users, compared to not exempting EIIs.” However, she added: “Overall the reforms we are proposing for the electricity market could mean [all] consumers benefit from lower electricity bills by the end of the 2020s, compared to what they would have been otherwise.” DECC added that the full impact on consumers will be determined by the scope of EII exemptions, and that providing the consultation over this proceeds to schedule in 2013, exemptions are expected to take effect when the Electricity Market Reform is implemented in Autumn 2014.

The spokesperson insisted DECC was working closely with the European Commission, “to ensure that our policies and any exemptions are compliant with state aid rules”. The UK government has said it is opposed to any European interference, claiming important energy intensive industries would simply relocate to other countries if exemptions were not made. Under the exemption system, private households and small businesses pay for the bulk of the above-market costs of renewable energy, while large-scale users such as steel, cement and paper producers do not.

The UK government’s green plans include long term market related contracts for difference (CfDs), which will be signed with developers of new green power capacity, providing “a stable rate of return designed to give certainty and support technologies that are further from the market”, according to DECC. The costs will be levied on energy suppliers, who are expected to pass these on to consumers. Exempting EIIs from these costs will help British industry compete internationally say DECC, while supporting global emissions reductions.

Germany’s Bund der Energieverbraucher (BdE), (Association of Energy Consumers) placed two complaints with the EU last autumn, claiming German EII exemptions mean its members are unfairly having to foot the whole bill for green capacity expansion. If the EU finds in favour of the German association, it will be an awkward decision for the UK, which has to abide by the same European anti-trust laws, and whose proposed exemption policy is very similar to the long-standing German one.

Europe’s powers include the ability to force national governments to change the law and claim back money from the companies that benefited. However, the EU has not yet committed to a formal investigation, stating that at this stage it is simply assessing the implications in terms of state aid, in particular for electricity repurchasing tariffs and for the exemptions of large-scale energy users, while discussing the issue with German authorities.

While the exemption plan has implications for the price of energy to other consumers, the £250 million compensation package criticised last week does not. Here the primary aim is to use government money to compensate EIIs for additional costs from the ETS and CPF, produced as generators burn fossil fuels. From 2013, the UK will impose a minimum price of about £16 per tonne of carbon dioxide, well above the current price in the ETS of €6.70.

With consultation now complete, parliament’s Environmental Audit Committee (EAC) insists the plan is altered to avoid compensating EIIs, when the same companies are making windfall profits from over-allocation of emissions allowances. If the criticism is accepted, any compensation must first take into account each company’s surplus carbon allowances and resulting profits, before awarding additional funds.

Joan Walley, chair of the cross-party committee that produced the new report, told reporters last week: "I welcome the government helping energy-intensive companies cope with additional carbon price rises to stop them moving jobs abroad. But it shouldn't throw good money after bad by giving compensation to those already making windfall profits from the emissions trading system when allowances were allocated free of charge."

None of the proposed EII compensation extends to the price difference between natural gas and other fuel types in Europe and competing economies such as the US – where natural gas is about a quarter of the European price. Faced with such large fuel price differentials, EIIs are already under pressure to move overseas, even without additional costs from green development. As many competitor economies currently show no serious commitment to decarbonise, the UK and other EU EIIs will be at an even greater disadvantage if they press ahead without exemptions.

If enough big users shut up shop and move to locations with cheaper energy, utilities could see demand for power fall in a UK market already struggling as a result of weak economic growth and Europe’s financial crisis. Although the criticism of EII exemptions is widespread, even most environmentalists agree that EIUs must be encouraged to remain as they provide the industrial capacity needed to support and develop a low carbon economy.

As the bills for green development across Europe continue to grow - Germany expected to spend more than €18 billion in green energy subsidies in 2013 – the debate over who pays is likely to get even livelier.