Widening the Exemption for Energy Intensive Industries from the Indirect Costs of the Renewables Obligation (Scotland):

Consultation Response Analysis

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Scottish Government
Riaghaltas na h-Alba
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Consultation Response Analysis

1. Background

The Renewables Obligation (RO) is one of the main support mechanisms for renewable electricity projects in the UK. The RO came into effect in 2002, placing an obligation on UK electricity suppliers to source an increasing proportion of the electricity they supply from renewable sources. A parallel mechanism, The Renewables Obligation (Scotland), exists for Scotland.

In 2017, the Scottish Government and UK Government delivered legislative changes to create a scheme that exempts Energy Intensive Industries (EII) from a proportion of the indirect cost of the Renewable Obligation.

To be eligible for exemption, businesses must pass a sector test and a 20% electrical intensity threshold[1]. In response to criticism that these rules create competitive distortions - by disadvantaging those who are not eligible but who operate in the same sectors as those who are – the UK Government committed to consult on widening eligibility.

Given our devolved responsibility for the Renewables Obligation (Scotland) (ROS), and historical advice to maintain parity with the management of the UK scheme, the Scottish Government published a consultation in parallel.

2. The Consultation

The purpose of this consultation was to gather views from interested parties on a proposal to widen the eligibility of EII for exemption from the indirect policy costs of the ROS.

The consultation, sought views on the same proposals for widening eligibility put forward by the Department for Business, Energy and Industrial Strategy (BEIS) who have oversight of the UK Renewables Obligation.

The consultation opened on 21 June 2018 and closed on 14 September 2018. The following questions were asked:

Consultation Questions

No.	Question	Responses
1a	**Does the current eligibility threshold (20% electricity intensity) create any competitive distortions?**	3
1b	**If so, which set of options would best address such options?**	3

[1] Electricity costs must be at 20% or higher of a business's Gross Value Added (GVA) which is defined as earnings before interest, taxes, depreciation, amortisation and staff costs including employers' pension and national insurance contributions

1c	**Should Scottish Government consider amending the ROS to deliver similar, or the same, changes?**	3
2a	**Are there alternative options to operate ROS exemption in Scotland?**	3
2b	**If so, what form could these alternatives take?**	1
2c	**What impact would divergent eligibility rules create in Scotland for Energy Intensive Industries, non-exempt businesses and consumers?**	2

3. Consultation Responses

A total of 3 responses were received from interested parties. During the consultation we arranged meetings with some interested stakeholders to discuss the topic. These meetings helped to informed our thinking on the way forward.

2 respondents gave permission for their responses to be made public. Published responses are available to see on the Scottish Government's consultation website at https://consult.gov.scot/energy-and-climate-change-directorate/widening-the-exemption/consultation/published_select_respondent.

Responses were received from the following type of organisations:

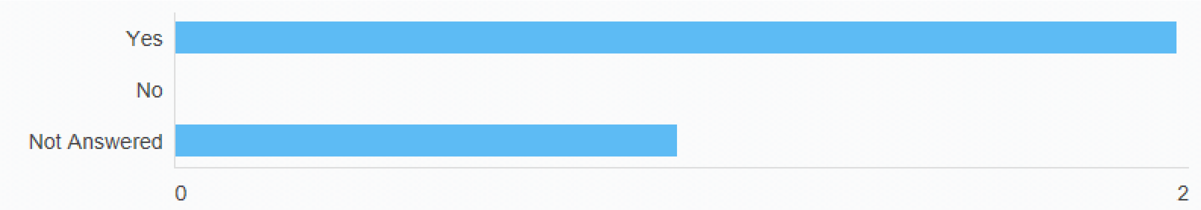
Organisations	
Trade Association	1
Energy Intensive Businesses	1
Energy Suppliers	1

A number of issues were addressed by respondents which are outlined below:

Issue Raised	
Current rules risks "eligibility movement" – where a company's GVA increases, separate to energy usage, and makes the company ineligible	2
Competition with EU countries who already have a lower exemption threshold	1
Charging bill payers as opposed to tax payers	1
The impact of widening exemption of other bill payers	1
Increased burden on administrators if eligibility is widened	1
Divergence in Scotland creates market distortions for companies operating across the UK	3
Administrative burden of divergent schemes	1
The need for consistency for consumers	2

4. Consultation Questions

1a Does the current eligibility threshold (20% electricity intensity) create any competitive distortions?



2 responses suggested that the current eligibility threshold for EII exemption does create competitive distortions. Whilst a third respondent did not answer question 1a directly, further reasoning was provided in the "please provide evidence/explanation for your answer" section. This asserted that an eligibility threshold would create some level of competitive disadvantage, regardless of where the threshold is set.

Key points raised:

- GVA can increase with profitability, and this can impact on whether a company is exempt or not, regardless of if they, the same levels of electricity as their competitors

- Other EU countries implement a lower exemption threshold, and some UK companies also have to compete with this

- The mechanism of levies on energy bills will create competitive distortions. This should be replaced with a general taxation system, proportionate to earnings

- By reducing the level of exposure to a proportion of customers, the exposure of non-eligible customers will always increase

Whilst responses provided some insight, none provided strong evidence that competitive distortions do exist.

1b If so, which options set out by BEIS would best address such distortions

3 responses were given to question 1b. In expressing support for lowering the threshold in line with the options proposed by BEIS, 2 responses showed preference for option 2 (15% electricity intensity threshold) and option 3 (10% electricity threshold). A third response provided no direct preference for any of the 3 options.

Key points raised:

- A low threshold of 10% would provide the maximum mitigation of falling out of eligibility from an eligible business perspective

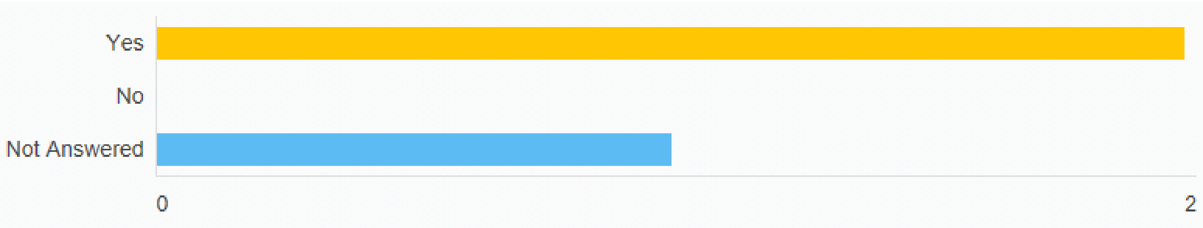
- To reduce the impact on other electricity consumers, a 15% threshold could be chosen

- If a decision is made to widen eligibility, this should only be extended to those who can sufficiently evidence the existence of competitive disadvantage

- There is an increased burden on administrators to provide exemptions to newly exempted businesses

- The uncertainty about the volume of exempt electricity limits an energy supplier's ability to accurately forecast costs for customers

1c Should the Scottish Government consider amending the ROS to deliver similar (or the same) changes?



Of the 3 responses, support for the Scottish Government making similar, or the same changes proposed in the BEIS consultation, was unanimous. Whilst 1 respondent did not answer this question directly, further reasoning was provided in the "please provide evidence/explanation for your answer" section.

Key Points:

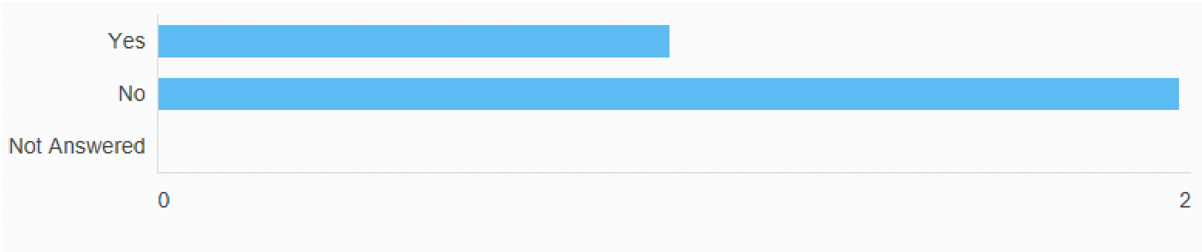
- Different changes in Scotland will create market distortions for businesses competing across the UK

- From an administrative perspective of eligible businesses who operate in both Scotland and England, rules should be the same across the UK

- All consumers will benefit from consistency across the two schemes

- Should SG decide to take a different approach, attention should be given to clear guidelines to reduce the risk of increased administrative burdens

2a Are there alternative options to operate the RO(S) exemption eligibility in Scotland?



1 response suggested that an alternative option for managing the exemption of EII from ROS costs. The remaining 2 responses did not think alternative options existed.

2b If so, what forms could these alternatives take?

Respondents who answered “No” to question 2a did not provide any response to question 2b. 1 response presented an alternative option for managing exemption of EII.

Key points:

- The Renewables Obligation policies should be funded progressively, through general taxation, not levies on energy bills.
- Where a general taxation approach is taken, it should be applied GB-wide.

2c What impact would divergent eligibility rules in Scotland create for Energy Intensive Industries, non-exempt businesses and consumers?

2 responses were given for this question. Both signalled opposition to a divergent approach across Scotland and the rest of the UK.

Key Points:

- A commercial disadvantage would arise if different rules exist. Where the market for goods is UK-wide, the same rules should be applied
- A divergent approach is likely to increase confusion amongst eligible and ineligible consumers.

Overall Findings

The consultation received a limited number of responses which were polarised in their opinion of extending or maintaining the existing electricity intensity threshold. Responses were however unanimous in emphasising the need for maintaining parity with the Renewables Obligation for England and Wales.

Next Steps

The Scottish Government would like to thank all respondents for taking the time reply to this consultation. We will publish a response in due course.

Scottish Government
Energy Industries Division
Industrial Decarbonisation Team

October 2019

Annex A

List of Respondents (who gave permission to have responses published)

SSE Business Energy

Scottish Government
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