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**EIUG Response to the Consultation on a Capacity Market Exemption**

**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 EIIs, including 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 foundation 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. In some cases, investment, economic activity & jobs have relocated abroad, leading to a subsequent increase in imports.

**Capacity Market Charge Exemption**

1. The EIUG strongly supports the proposal to exempt certain EIIs from the cost of the capacity market. An exemption from its cost will reduce the industrial electricity price differential with other countries, as shown by BEIS in its review of EII renewable exemption schemes[[1]](#footnote-1) in summer last year. Figure 3 of the review gives the breakdown of electricity prices into levies and charges and the wholesale price component in the first half of 2021 for extra-large industrial consumers in various European countries, and it shows that the UK is an outlier with levies and charges much higher than in other countries. The resulting price differential causes a market distortion that puts UK EIIs at a competitive disadvantage internationally.



Source: BEIS (2022), Review of the scheme to provide relief to energy intensive industries for a proportion of the indirect costs of funding renewable electricity policies, London: BEIS

1. The EIUG also would like to highlight that the capacity market supplier charge is likely to increase in the next years. The latest T-4 2026/27 capacity market auction result cleared at a record clearing price of £63/kW/year. This is more than double the price of any other T-4 auction to date. The graph below shows the capacity market supplier charge trajectory over the past years.



Source: LCPDelta

1. One of the key drivers of the higher clearing price is a higher assumed peak demand leading to a higher capacity requirement. With increasing electrification, peak demands are likely to increase further in the future.

**Capacity Market Exemption Process**

*Do you have views on whether the proposed process will deliver on the intent of the policy?*

1. The EIUG is of the view that the proposed mechanism to exempt eligible EIIs indirectly from the cost of the capacity market supplier charge will reduce industrial electricity prices. The EIUG agrees with the intention to exclude electricity demand from eligible EIIs from the charge, similar to the mechanism used in the EII renewable exemption schemes.

*Do you have views on creating a Capacity Market exemption which uses a similar structure as appropriate to the existing EII exemption scheme?*

1. The proposed intent is to base the capacity market exemption process on the design of the existing EII Exemption Schemes. The administrative processes to reduce the indirect cost of the various renewable deployment schemes for EIIs have worked well, and the EIUG does therefore not see any reason why basing the capacity market exemption on the same process would not deliver on the intent of the policy. Furthermore, both EIIs and electricity suppliers are familiar with the EII exemption schemes. However, DBT needs to include the Electricity Settlement Company in its governance arrangement to deliver the proposal.
2. The EIUG also support the intention to also exempt eligible EIIs from the portion of their bills that fund the operational costs of ESC.

*Are there aspects of the existing EII exemption scheme that you consider are not appropriate for the proposed Capacity Market exemption?*

1. Many EIIs in eligible sectors fall outside the existing EII exemption schemes due to the business-level test, particularly in the ceramics sector. This business-level test is leading to intra-sectoral distortions and acts to limit eligibility of EIIs in eligible sectors. The EIUG will make the case for removal of the test again when the Government intends to conduct a review of the analysis that underpins the eligibility criteria for the EII exemption schemes.

*Do you perceive these proposals to cause any unintended consequences to the running of the Capacity Market?*

1. As the capacity market payments, auctions and supplier charge are relatively separate from each other, the EIUG does not envisage any unintended consequences to the capacity mechanism.

*Do you have views on the impact on supplier credit cover requirements and how these will change as a result of the policy?*

1. The EIUG will leave it to licenced electricity suppliers to answer this question.

**Energy Efficiency**

1. The consultation poses a question of whether EIIs will be disincentivised to reduce electricity usage following implementation of the proposed exemption, given the associated saving and consequent capability to increase output.
2. The capacity market supplier charges contribute to the industrial electricity price differential between the UK and other countries thereby putting EIIs at a competitive disadvantage and increasing the risk of carbon leakage. An exemption from the charge will therefore reduce the risk of a decrease in output in the form of demand destruction in the UK.
3. Furthermore, EIIs will retain a strong economic incentive to increase energy efficiency, thereby lowering input cost, due to their exposure to the wholesale market cost in the retail electricity price. Moreover, strong regulatory incentives due to various energy efficiency policies, such as climate change agreements, streamlined energy and carbon reporting obligations, mandatory energy audits and application of ISO standards encourage EIIs to increase their energy efficiency as well. The incentive to increase energy efficiency will not diminish with the introduction of an exemption of the capacity market charge for EIIs.

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1. [Energy Intensive Industries: Review of the scheme to provide relief to energy intensive industries for a proportion of the indirect costs of funding renewable electricity policies (publishing.service.gov.uk)](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1097834/increase-of-subsidy-level-for-eii-exemption-schemes-consultation.pdf) [↑](#footnote-ref-1)