

Title: EII Support Levy & EII Network Charging Cost Compensation Scheme IA No: DBT022(F)-23-IM RPC Reference No: N/A Lead department or agency: DBT Other departments or agencies: DESNZ	Impact Assessment (IA)		
	Date: 06/06/2023		
	Stage: Development/Options		
	Source of intervention: Domestic		
	Type of measure: Primary legislation		
	Contact for enquiries: energybill2021@beis.gov.uk		
Summary: Intervention and Options			RPC Opinion: N/A

Cost of Preferred (or more likely) Option (in 2019 prices)			
Total Net Present Social Value	Business Net Present Value	Net cost to business per year	Business Impact Target Status
£0m	£0m	£0m	Qualifying provision

What is the problem under consideration? Why is government action or intervention necessary?
 GB industrial electricity costs are higher than those of comparable neighbouring countries, causing a risk of direct and indirect carbon leakage where production shifts to other jurisdictions because our energy intensive industries (EIIs) are not able to remain profitable. Electricity network costs paid by GB based EIIs are higher than in many other EU countries largely due to the discounts offered in some jurisdictions to EIIs that meet certain eligibility criteria regarding electricity consumption and off-peak grid utilisation. Failure to address the electricity price gap would result in production, and therefore output decreasing, and some firms facing increased risk of closure due to reduced liquidity.

What are the policy objectives of the action or intervention and the intended effects?
 The proposed intervention is intended to provide the Government (HMG) with the powers to lower the effective price paid for electricity by EIIs. The objective of the secondary legislation will be to provide EIIs with relief from the network costs on their electricity bills through a compensation scheme. Following this intervention, and other components of the British Industry Supercharger, electricity prices for eligible businesses will be comparable with international competitors.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)
Do nothing: without intervention, HMG will not have the powers to compensate network costs for electricity intensive and trade exposed businesses. The continued electricity price gap could lead to production, investment and employment leaving the UK market for markets with lower net zero ambitions and thus lower electricity prices.
Option 1: The levy and compensation scheme (preferred option) will contribute to closing the industrial electricity price gap without interfering in the market regulator (Ofgem)'s ability to set and change the design of network charge costs.
Other discounted options included private grants and loans which were deemed too complex and inefficient, investment in electricity infrastructure which was deemed not timely enough, and an exemption scheme which was deemed too complex.

Will the policy be reviewed? It will be reviewed. If applicable, set review date: /				
Is this measure likely to impact on international trade and investment?		Yes		
Are any of these organisations in scope?	Micro Yes	Small Yes	Medium Yes	Large Yes
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)		Traded: N/A		Non-traded:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible:  Date: 06/06/2023

Summary: Analysis & Evidence

Policy Option 1

Description:

FULL ECONOMIC ASSESSMENT

Price Base Year 2020	PV Base Year 2022	Time Period Years 2023-2035	Net Benefit (Present Value (PV)) (£m)		
			Low: £0m	High: £0m	Best Estimate: £0m

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	n/a	n/a	n/a
High	n/a	n/a	n/a
Best Estimate	n/a	n/a	n/a

Description and scale of key monetised costs by 'main affected groups'

The estimated cost of this primary legislation, by itself, is zero. Costs may be incurred when secondary legislation is passed at a later date which introduces a levy and the compensation scheme for eligible energy intensive industries. This impact assessment presents an illustrative estimate highlighting the potential distributional impacts and the trade-offs associated with future levy design, without providing full costings of secondary legislation decisions.

Other key non-monetised costs by 'main affected groups'

When implemented at secondary legislation stage the levy would create administrative costs which have not been monetised in this Impact Assessment. These are likely to include familiarisation costs, updating systems and engagement to notify customers of the new levy, and the costs of managing levy payments.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	n/a	n/a	n/a
High	n/a	n/a	n/a
Best Estimate	n/a	n/a	n/a

Description and scale of key monetised benefits by 'main affected groups'

The estimated benefit of this primary legislation, by itself, is zero. Benefits would be unlocked if secondary legislation is agreed at a later date resulting in a discounted electricity price for EIs. These could include increased employment, investment, company profits, and the prevention of firm closures. These are not monetised in this IA for reasons outlined above.

Other key non-monetised benefits by 'main affected groups'

When secondary legislation is agreed at a later date, there may also be additional non-monetised benefits. These might include decarbonisation benefits where lower electricity prices make electrification of industrial processes financially viable for firms sooner.

Key assumptions/sensitivities/risks

Discount rate (%)

N/A

This Impact Assessment assumes this primary legislation by itself will have no impact on businesses and consumers. When a new levy is implemented, its impact will depend on policy decisions about the costs that EIs will be compensated for and the required size of the levy. A full Impact Assessment setting out the impacts of the regulations will be published alongside the secondary legislation when brought forward.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs: 0	Benefits: 0	Net: 0	
			n/a

Evidence Base

Problem under consideration and rationale for intervention

Introduction

1. Energy intensive Industries (EIs) are trade-exposed and high electricity using businesses that cover a number of key foundations industries (e.g., Glass and Cement) as well as industries that are essential to critical national infrastructure (e.g., Steel and Chemicals) and/or form part of the supply chain for other important sectors (e.g., auto and aero). EI firms represent c. 400,000 key manufacturing jobs across the UK, predominantly in Wales, the North, and the Midlands, with many more in the wider supply chain.
2. GB industrial electricity costs are higher than those of comparable neighbouring countries, causing a risk of direct and indirect carbon leakage where production shifts to other jurisdictions with less ambitious climate policies because our EIs are not able to remain profitable. EIs include important strategic sectors such as steel and chemicals production and other foundational manufacturing, and high energy costs are a critical factor for decisions on inward investment.
3. The government's 2022 Energy Security Strategy¹ committed action to address the issue of high prices, which has been more recently compounded by rising domestic prices and uncertainty in the global energy market flowing from Russia's invasion of Ukraine.
4. High and volatile energy prices have been a central part of the UK's economic story for the last two years. Preceding Russia's invasion of Ukraine, prices had already been rising for some time due to a combination of factors – including increasing Asian demand, a cold winter in 2020, lower renewable generation (weather driven), and reduced supply from Russia.
5. The Energy Bill Relief Scheme (EBRS) was launched on 1 October 2022 to help all non-domestic energy customers, receiving energy from licensed suppliers with their bills. and mitigate against significantly inflated gas and electricity prices in light of global price pressures, triggered by Russia's invasion of Ukraine. The scheme provided a discount on eligible customers' gas and electricity unit prices, thereby reducing their energy bill.
6. In January 2023, the Chancellor announced a more targeted Energy Bill Discount Scheme (EBDS) that will provide capped support for all non-domestic consumers from April 2023 until April 2024 if energy prices reach a sufficiently high level. Energy and trade intensive industries were singled out for a more generous support package as energy costs made up a larger proportion of their total costs and they are less able to pass on costs to consumers due to international competition.
7. Whilst the EBDS and EBRS deal with the short-term wholesale electricity cost (the cost of generating electricity) increase caused by the Russian invasion of Ukraine, the long-term inequality in retail price (the price that appears on the bill) with comparator countries remains. This long-term gap is in part due to the UK's high level of ambition in decarbonising electricity generation. UK generation moved from coal to gas which tends to be a more expensive form of generation and puts UK EIs at a competitive disadvantage relative to EIs in other countries. The UK's ambitious deployment of renewable electricity generation leads to higher policy costs and higher prices for consumers.
8. The government has therefore announced the British Industry Supercharger² - a suite of measures designed to close the long-term electricity price gap between the UK and key competitor countries. The measures include:

¹ <https://www.gov.uk/government/publications/british-energy-security-strategy/british-energy-security-strategy#immediate-support-on-energy-bills>

² <https://www.gov.uk/government/news/government-action-to-supercharge-competitiveness-in-key-british-industries-and-grow-economy>

- a. An extension of the existing EII Exemption scheme from 85% to 100% aid intensity; which is anticipated to amount to a £5-7/MWh³ reduction in 2025 from current levels.
 - b. A new full exemption from the costs associated with the UK Capacity Market, which is anticipated to amount to around £5/MWh. In 2025⁴
 - c. A reduction in the charges paid for use of the electricity grid.
9. The focus of this impact assessment is the third pillar of the British Industry Supercharger- the reduction of network costs paid by EII.

Network costs

10. Electricity network costs paid by GB based EII are higher than in many other EU countries largely due to the discounts offered in some jurisdictions to EII that meet certain eligibility criteria regarding electricity consumption and off-peak grid utilisation. This allows eligible EII in those countries to lower their network costs by up to 90% in some cases. Equivalent discounts that offer an explicit reduction to network costs for EII have to date not been offered in GB. The effect of these discounts is to redistribute network costs between different user groups. Therefore, although aggregate network costs are not necessarily higher in GB than in comparator countries, the share of these total costs paid for by EII is higher than in comparator countries.
11. Unlike in much of the rest of Europe, GB network charges are typically categorised into:
 - a. “cost reflective” charges, which are intended to reflect the forward looking marginal cost network users place on the system, and therefore users will take these charges into account when deciding how to use the system, minimising overall system costs; and
 - b. “cost recovery” or “residual” charges, which ensure network companies can recover their full costs but which do not reflect costs attributable to any individual network user, and therefore typically are levied in a manner that minimises changes to behaviour.
12. The implication of this charging structure is that charges for EII are not uniform and will reflect to some degree the relative costs/benefits that they impose/bring to the system compared to other network users. In other words, EII will pay lower charges where they consume less in peak hours, or are more favourably located (e.g. closer to sources of generation). EII will also face significant residual charges, which typically are uniform and, by design, more difficult to avoid.
13. In GB, electricity network charges are paid by electricity network users and are split into three separate sets of charges.
 - a. Transmission Network Use of System (TNUoS) charges cover use of the transmission system;
 - b. Distribution Use of System (DUoS) charges cover use of the distribution system; and
 - c. Balancing Services Use of System (BSUoS) charges cover the cost of day-to-day operation of the transmission system.
14. Within these individual charges, there are elements that are either cost reflective or cost residual.

Table 1: Breakdown of network charges

Network cost	Cost Reflective charge	Residual cost charge
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³ Source: Q4 2022 DESNZ price and bills projections. The model assumes a high net zero ambition, a low to very high fossil fuel price range, and a high ETS price and is just one of a range of forecasts for 2025

⁴ As above

TNUoS	Peak consumption (“Triad”) based charge which can be avoided via demand response or BTMG (behind the meter generation i.e. as on site generation) at peak	Flat charge for each consumption or connection voltage band, which is difficult to avoid unless consumption can be reduced sufficiently to shift a site to a lower charge band or a site changes its connection capacity.
DUoS	At EDCM ⁵ , three different charges, with “super-red” volumetric based charge possible to avoid through demand response or BTMG at peak	Flat charge for each capacity band, which is difficult to avoid without adjustments to connection capacity or voltage level.
BSUoS	N/A	Exposed to higher volumetric charge (albeit offset by lower wholesale prices) which can be avoided through energy efficiency or baseload BTMG

15. This impact assessment is considering the impacts of the primary legislation powers to create the EII Support Levy and the EII Network Charging Cost Compensation Scheme. The type and size of the network cost that will be compensated will be assessed in the secondary legislation impact assessment. Meanwhile, The Department for Business and Trade (DBT) will consult on the measures to improve our understanding of network costs paid by EIIs, and the correct level of compensation.

Existing electricity price support offered to EIIs

16. HMG delivers two EII relief schemes to reduce the cumulative impact of some energy and climate change policies on industrial electricity prices for eligible EIIs in sectors such as steel, chemicals, cement, ceramics, paper and glass. This reduces the risk of carbon differentials and supports the competitiveness of key manufacturing industries to help keep production in the UK rather than risking them moving overseas to countries with less ambitious climate policies. Like all sectors of the economy, industry will need to decarbonise, but it is equally important that they remain competitive and that the UK remains an attractive location in which to invest during the transition to Net Zero.
- a. Since 2013, a compensation scheme has provided partial compensation for indirect carbon costs (the UK Emissions Trading Scheme – ETS and the Carbon Price Support Mechanism (CPS), which places additional carbon costs on electricity generation). Under this scheme, direct payments are made from HMG to eligible firms with the budget coming from the former Business and Energy department’s (BEIS’) RDEL (resource) allocation. Additional funds have been earmarked from the Department’s contingency to cover the greater level of relief announced in the British Energy Security.
 - b. Since 2017, an exemption scheme provides relief for the indirect costs passed on by electricity suppliers for the cost of schemes designed to increase the share of renewable electricity - the Contracts for Difference (CFD), Renewables Obligation (RO) and Feed-In-Tariff (FIT). The cost of funding the exemption is redistributed to all non-eligible consumers including other businesses and households.
17. The 2022 Energy Security Strategy announced that the EII Compensation Scheme will be extended for a further 3 years with an increased aid intensity which represents a doubling of the previous annual budget. It also included a commitment to consider measures to support business including increasing the subsidy intensity of the Exemption Scheme from 85% to up to 100%.

Rationale for intervention

⁵ For users that connect to the Extra High Voltage distribution network (EHV), charges are determined through the EHV Distribution Charging Methodology (EDCM). This applies to many EIIs.

18. The rationale for intervention is the risk of carbon leakage due to high electricity prices. For those energy intensive industries (EII) particularly exposed to international trade and heavily reliant on electricity, paying the full amount of electricity policy costs on their electricity consumption to support delivery of the Government's Net Zero Strategy can increase the risk of carbon leakage and the cost of electricity relative to other energy sources. Higher electricity prices may also make it more challenging for industrial users to switch from gas-intensive production to less carbon-intensive production relying on electrification.
19. Carbon leakage is the displacement of domestic production, and its associated emissions, due to different levels of carbon pricing and climate regulations across jurisdictions.
20. The risk of carbon leakage is supported by theoretical analysis and evidence. While the UK has committed to Net Zero by 2050, many other competitors have not. The ambitious target the UK has set to deliver Net Zero brings requirements for change and associated costs (as well as economic opportunities), which the UK will incur sooner given our legally binding requirements included in carbon budgets compared to less ambitious commitments by global competitors.
21. The indirect funding of renewable policy costs under the CfD, RO and FiT scheme represents a portion of a firm's electricity costs and is associated with supporting the transition to Net Zero. These levies are some of the highest in Europe and are not present in some other competing countries and as such, represent an additional climate policy cost when compared to these countries. Where there are instances of these costs being applied, there are often more extreme mitigations in place relative to the UK. While these costs alone are not always considered to be the most important factor for carbon leakage, with cost pass-through rates having a significant impact, they contribute to a wider carbon leakage risk. Other factors which affect carbon leakage include capital intensity, trade intensity/exposure, emissions output, and other industry associated costs.

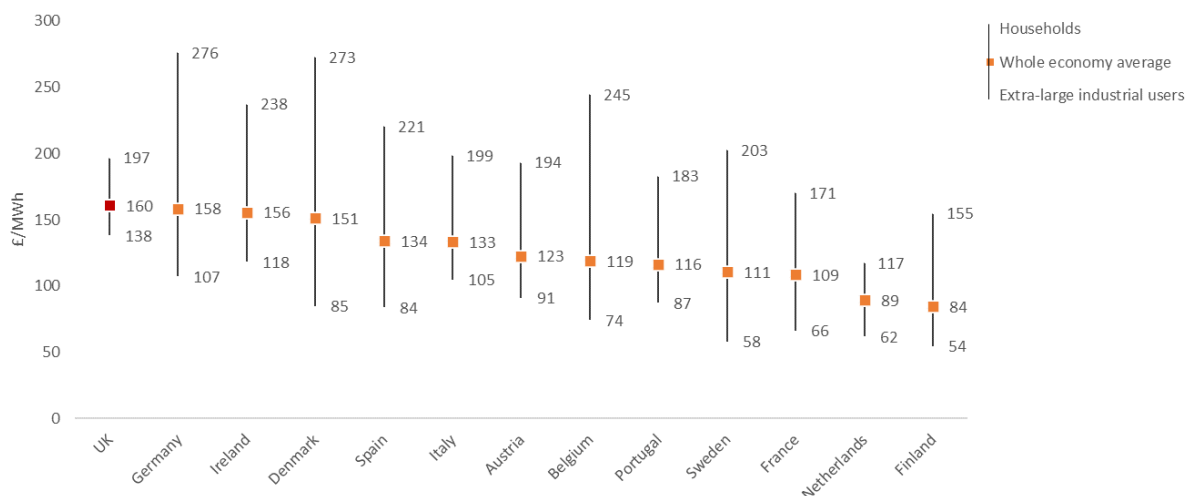
International electricity price gap for EIIs

22. UK industrial electricity costs have been historically higher than comparable neighbouring countries and our EIIs are unable to remain competitive without intervention. Three main components contribute to electricity prices for EIIs: wholesale prices, policy costs and network costs. Typical electricity costs for very energy intensive users in the UK were £56/MWh, compared to £38/MWh in the Netherlands, £34/MWh in France and £35/MWh in Germany in 2020.⁶
23. Prices are made up of the following components:
 - a. Wholesale prices – the cost of electricity generation on wholesale markets, including the carbon costs of generating electricity from fossil fuels.
 - b. Network costs – charges on the energy bills of households and businesses, which are used to fund both investment and maintenance of both the transmission and distribution networks and also balancing – ensuring that electricity can travel from the point of generation to the point of use, and that supply meets demand at any given time. The manner in which these costs are paid is set by Ofgem.
 - c. Policy costs – additional charges on the energy bills of households and businesses, set by HMG, which are used to fund energy policies that support grid decarbonisation, or to ensure security of supply.
24. While wholesale costs are broadly common to all energy consumers (although this can vary depending on time profile of demand and how different consumer groups pay for their electricity), policy and network costs vary across these groups. This leads to a complex

⁶ ICIS 2022 day-head prices used for wholesale prices across countries. DESNZ analysis used for UK network, policy and carbon cost analysis. Ofgem 2020 report used for policy and network costs estimate for other EU countries.

picture of electricity prices, both in the UK and in our key EU competitors. Figure 1 shows electricity prices in the UK and EU 14-countries. The household price is for a medium use household.

Figure 1: EU-14 + UK electricity price spread (household, average*, industry) 2021, £/MWh



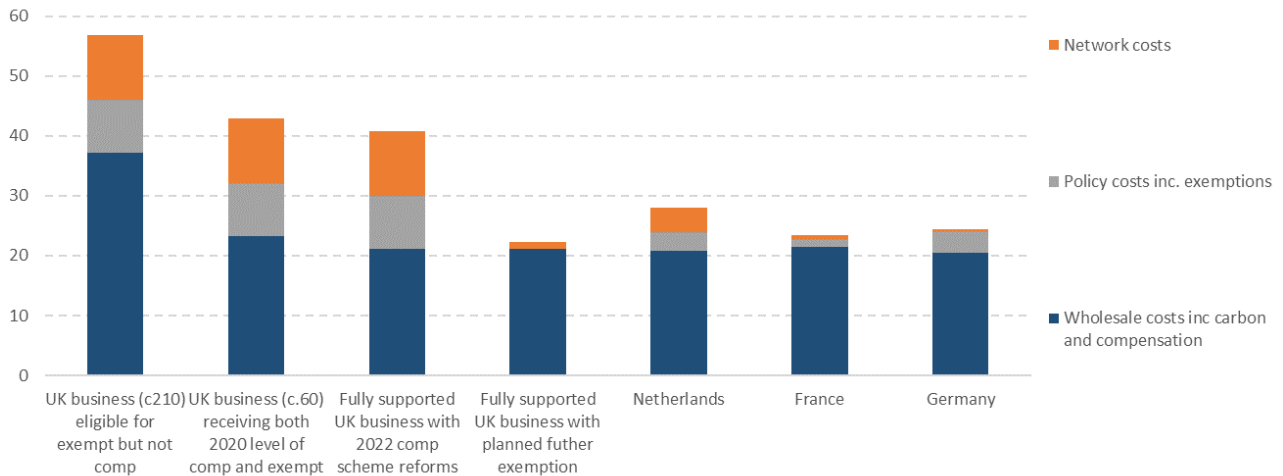
Source: Households and Extra-Large Industrial Users are from BEIS QEP 2021 data. Average based on Eurostat 2019 sectoral consumption values

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25. UK electricity wholesale prices have historically been higher than for main competitors, thus contributing to high retail prices. Despite this, figure 1 shows in 2021 UK household electricity prices were around average across EU countries, whereas among very large industrial consumers, UK prices were higher than any other EU-14 + UK country for which data is available, around 62% higher than the EU-median in 2021. This is reflective of how network and policy costs are distributed across different consumers; the UK has chosen to distribute policy and network costs relatively evenly across households and industrial users, whereas other countries have chosen to protect large industrial users with a greater share of these costs falling on households.
26. The UK does offer relief for some energy intensive businesses such as the Compensation (62 businesses) and exemption (c. 320 businesses) schemes. 210 businesses are eligible for the exemption scheme but not the compensation scheme. The ETS/CPS Compensation Scheme was increased in April 2022 and is estimated to compensate around 70% of indirect carbon costs for eligible EIs, whereas the Exemption Scheme exempts eligible EIs from 85% of RO, FiT and CfD costs. These schemes reduce electricity prices for eligible users, however, the relief offered in EU competitor countries is ultimately greater, and as a result supported UK EIs still face higher electricity prices than their key competitors in Germany, France and the Netherlands (Figure 2). The chart below shows the impact of the current exemption and compensation scheme on EIs, for the c.60 businesses eligible for both schemes, and the c. 210 eligible for just exemptions. For those 60 fully supported businesses it also tests the impact of proposed increases in the exemption scheme to extend to 100% of RO, FiT, CfD as well as capacity markets, and a reduction in network charges – The British Industry Supercharger.

Figure 2: Average EI Electricity prices (including exemptions and compensation) across different countries in 2020 (£/MWh)

⁷ DESNZ QEP data here: <https://www.gov.uk/government/statistical-data-sets/international-industrial-energy-prices>, <https://www.gov.uk/government/statistical-data-sets/international-domestic-energy-prices>



Source: ICIS (wholesale), BEIS analysis (UK policy and network), Ofgem report (2020) (international policy and network)

27. In 2020, the c.60 UK EILs receiving support from both the compensation and the exemption scheme paid more for electricity than French, German or Dutch EILs. In the UK they paid £43/MWh compared to £23/MWh for France, £24/MWh for Germany, and £28/MWh for the Netherlands. The c. 210 UK EILs who receive support only from the EIL exemption scheme paid £32-33/MWh more for electricity than fully supported German or French firms. Note – different firms will be eligible for different support in other countries, so comparing exempted-only firms in the UK with fully supported firms in Germany may not be a fair comparison.
28. Wholesale cost gaps will fluctuate year-to-year depending on fuel and carbon prices, but in 2020, the c. 60 firms that receive compensation had a wholesale cost gap at around £2-3/MWh with Germany and France. For the c. 210 firms who only benefit from exemptions, the wholesale cost gap was c. £16-17/MWh, representing roughly half of their total gap with Germany and France. Firms in the Netherlands, France and Germany are assumed to receive compensation for carbon costs.
29. For both groups of UK EILs receiving support, network costs make up c. £10/MWh of the gap with Germany and France, while policy costs make up c. £5-8/MWh of the gap. This means that network costs make up around 50% of the gap for firms that receive compensation and around 16-23% for firms that do not. Significant exemptions (up to 90%) on network costs are offered for EILs in Germany and France, with these costs spread across other consumers including households. Although the UK offers 85% exemptions from some policy costs, firms still pay Capacity Market (CM) charges in full and further exemptions are offered in other countries. Again, the cost of current UK exemptions are funded through other consumers.

Impact of the price gap on carbon leakage

30. While it is clear there is a significant diversion between UK electricity prices and those of similar competitor countries, the relationship between the price gap and carbon leakage needs to be established. The literature suggests that firms facing higher electricity costs, in part caused by stringent environmental regulation, will look to reduce investment and potentially move elsewhere.
31. This section will first discuss the relevant literature surrounding the relationship between higher electricity prices caused by environmental regulation leading to carbon leakage and then will assess evidence provided by companies as part of the EIL exemption scheme 2022 consultation – seen below.

32. The relevant literature highlights a relationship between where EII's decide to locate, and areas of low environmental regulation and electricity costs. Khan and Mansur (2013)⁸ found that high electricity intensive and polluting firms tend to cluster in areas of low regulation and electricity cost. While this paper was conducted within the USA and studied movement between states as opposed to among nations, the results for typically energy intensive industries (e.g., steel) were found to be significantly more elastic with regards to energy prices and employment.
33. Sato and Dechezleprêtre (2015)⁹ examined the influence of an energy price gap between two trading partners on bilateral trade flows for 42 countries and 62 manufacturing sectors between 1996 and 2011. On average, they found that a 10 percent increase in the energy price gap increases bilateral imports by 0.2 percent and that overall, energy price differences explained 0.01 percent of the variation in trade flows. This showed that where a country has higher electricity costs, such as that of the UK, caused in part by more stringent environmental policy, they will see an increase in the imported goods, which could be a risk factor for carbon leakage. This narrative is supported by the evidence provided by EII firms in the consultation.
34. Multinational corporations were found to have a marginally higher electricity elasticity of demand for employment (Dechezlepretre, Lovo, Martin, and Sato (2016))¹⁰, suggesting these companies were able to take advantage of their international status to move resources more responsively. This paper found in support of the pollution haven hypothesis, whereby firms will move production to areas of lower environmental regulation, as evidenced by an increase in imports of energy intensive goods increasing in response to tighter regulation. This would indicate that when a country has more stringent environmental regulation, consumption habits move to import from areas of lower environmental regulation and as such represent carbon leakage. This has been borne out by the consultation evidence, with many energy intensive sectors citing a significant increase in imports.
35. Bijnens et al (2021)¹¹ concerned electricity elasticity of demand for investment. This ECB paper found that investment was relatively elastic in response to a change in electricity prices, often more severe response than that for employment. This could imply that when faced with relatively high electricity prices firms may seek to reduce investment, which could be seen as a precursor to carbon leakage, whereby domestic productive capacity may be significantly reduced prior to exit. This investment, when not undertaken by a multinational firm, may go elsewhere.

Evidence of carbon leakage from EII exemption scheme summer 2022 consultation

36. Firms provided a mix of anecdotal and quantitative evidence to suggest a reduction/potential reduction in UK productive capacity as a result of higher electricity prices. SGL fibres stated their parent company (based in Germany) would potentially move their production to a similar plant based in the US with lower electricity costs because of the higher electricity prices. This would put c.250 jobs at risk.
37. Some firms cited reduced export demand and increased import demand as an indication of a loss of UK productive capacity such as Flour milling.
38. Cast Metals Federation stated they felt carbon leakage has occurred in their sector with their sector seeing an 80% shift in capacity offshoring since 2008, representing £8bn in lost GVA per annum. The steel industry also argued this. Tata Steel reported producing 60% less than they were in 1990, despite world steel production increasing by 150%.

⁸ Kahn and Mansur (2013) "Do local energy prices and regulation affect the geographic concentration of employment," *Journal of Public Economics* 101, 105-114.

⁹ Sato and Dechezleprêtre "Asymmetric industrial energy prices and international trade", *Energy Economics* 51,1, 130-141. (2015)

¹⁰ Dechezlepretre, Lovo, Martin and Sato (2016) "Does climate change policy pose a risk to competitiveness: Global firm-level evidence," LSE Grantham Institute.

¹¹ Bijnens, Hutchinson, Konings, Saint-Guilhem (2021) "The interplay between green policy, electricity prices, financial constraints and jobs: firm-level evidence," *European Central Bank Working Paper No 2537*.

39. Imports have been seen by firms as a proxy for carbon leakage, with firms stating that domestic demand is being met increasingly by international firms, indicating a loss of competitiveness and domestic productive capacity. The cement sector felt this was the case, with the Mineral Products Association (MPA) citing an increase of imports meeting domestic demand up to 22.6% in 2021, predominantly from countries not seeing these policy costs – providing Turkey, Morocco and China as examples. Cemex, a cement producer, also stated costs are too high to continue significant portions of supply chain be kept entirely domestic, stating that imports have effectively grown at 1% per annum over the past decade, coming to represent nearly a quarter of the market. Indeed, in 2020, CEMEX mothballed a kiln at their South Ferriby plant; as they were now supplementing their production at Rugby with imports. Other industry players also increased their importation as a way of managing costs and supplying the market competitively.

Rationale and evidence to justify the level of analysis used in the IA (proportionality approach)

40. This IA supports enabling powers and will be refined during the 2023 consultation on secondary legislation. At this stage there is significant uncertainty in the detail of the policy options that will be considered at this secondary legislation stage. Therefore, this IA has focused on creating a reasoned case for change by identifying a clear picture of the strategic and economic rationale for intervention to present a clear understanding of the costs and risks associated with our counterfactual, in the absence of intervention.
41. The IA goes further to describe the impact of a £1/MWh increase in electricity prices for all electricity consumers that are not eligible for the network cost compensation scheme-referred to as non-eligible consumers.

Description of options considered

42. This impact assessment considers the following options for funding the necessary compensation EILs for a proportion of their network charging costs:
- a. **Do-nothing:** We assume a counterfactual baseline scenario where in the absence of HMG interaction, there would be no further electricity price reduction for EILs. In this counterfactual scenario, UK based EILs would face a greater risk of carbon leakage as they would be exposed to the full competitive disadvantage of the higher industrial electricity prices. As such production, and therefore GVA, would decrease relative to the scenario of continued compensation and some firms would face increased risk of closure due to reduced liquidity as result of higher electricity costs and therefore no longer be able to compete internationally. However, EILs would not incur the cost of purchasing additional emissions allowances and environmental costs would decrease, due to the reduced production.
 - b. **Support investment in electricity infrastructure:** Support for development of private wire networks or a sector level Purchase Power Agreement do not guarantee a certain level cost reduction. Support for development of private wires also comes with significant policy delivery challenges. Private wires are predominantly used in conjuncture with onsite generation as a means of meeting an EILs energy demands. This form of behind the meter generation is not suitable to all eligible EILs and brings with it a series of alternative operating costs. A sector level Purchase Power Agreement is unlikely to meet the workstream design principles and could be expected to take 5+ years to become operational, due to complexity of the structure, negotiations with a large number of counterparties and difficulty accessing enough liquidity on the banking market.

- c. **European styled exemption:** We explored the feasibility of offering an exemption on network charging costs equivalent to those offered in Germany, France and the Netherlands. These exemptions are broadly offered on grounds that EILs with a constant and stable load profile (pattern of electricity usage by day and by year) is beneficial to the efficient operation of the electricity network. We commissioned external consultants, Frontier Economics, to review the GB electricity grid and ascertain whether a comparable exemption could be offered. The report concluded that the discounts applied in other European countries do not directly translate into the GB context. The structure of GB charges is different, and as a result some of the justifications for discounts applied in Europe are already reflected in the Cost Reflective elements of network charging costs. Consequently, this option was discounted.
- d. **Exemption Scheme:** We also explored the option of developing an exemption scheme based on the rationale of combatting carbon leakage. However, the design of the scheme proved undeliverable given it would have required the amendment of network charging codes which are set by Ofgem. The process for amending network charging codes is complex, lengthy and it would have proved challenging to offer this for a bespoke cohort of EILs, meaning HM Government would not have been able to offer targeted support to those sectors most in need of support. Furthermore, it would have interfered with Ofgem's responsibility to independently set the network charging regime. Consequently, this option was discounted.
- e. **Bespoke support:** An alternative approach would be to negotiate bespoke support for individual companies (through policy levers such as direct guarantees, loans and grants). This is not a suitable approach as it is slower, disproportionately burdensome in terms of government administration, and more likely to be seen as discriminatory due to the absence of a common approach, and due to the absence of political support for exchequer funding on this scale would not provide the support necessary to address the wider risk of carbon leakage as a result of high electricity prices.
- f. **Levy and compensation (preferred)**- the introduction of a levy on all licenced electricity suppliers and a compensation scheme paid out to EILs deemed most at risk of carbon leakage. This option achieves the policy objective of reducing the effective electricity price paid by EILs without interfering with Ofgem's ability to set and alter the design of network charges.

Policy objective

- 43. The policy objective is to provide relief to businesses within our most energy intensive industries (EILs) from historical policy costs applied by the UK - such as capacity market and network charges and costs arising from policies aimed at encouraging electricity generation from renewable and low carbon sources.
- 44. This is due to the failure of the market to provide electricity at prices which make it sustainable for the EILs to continue operating profitably, risking significant job loss and disinvestment in strategically important foundational industries such as the manufacture of steel and chemicals, which is a long-term strategic vulnerability for the UK which the recent volatility in wholesale energy markets has only served to highlight.
- 45. Whilst the EIL Support Levy and EIL Network Charging Cost Compensation Scheme will not directly contribute to the stated policy objective, they will provide HMG with the powers to lower the effective retail price paid by EILs for electricity.

Summary and preferred option with description of implementation plan

- 46. In order to provide support to EILs on their network charging costs and mitigate the additional cost burden placed on GB EILs through historic policy decisions, we will establish:

- a. An EII Support Levy raised on all licensed electricity suppliers, which will raise revenue that will be used to fund support;
 - b. An EII Network Charging Cost Compensation Scheme which will compensate eligible EII's for a portion of the network charging costs.
47. The proposal would not interfere with the ability of the regulator (Ofgem) to set the design of network charges. Nor would it seek to interfere in the payment of network charging costs by EII's (through paying their energy bills from energy suppliers) to the network operators. EII's would remain obligated to pay any and all network charging costs element in their energy bills.
48. The proposed levy would constitute a new policy cost on all licensed electricity suppliers across GB. The proceeds from the levy would be used to compensate eligible EII's for a proportion of the network charging costs element in their energy bills.
49. The schemes are due to be implemented by April 2025.
50. The Government has agreed for an amendment to the Energy Bill to include enabling powers for the establishment of the EII Support Levy and NCC Scheme, with technical detail to set out in secondary legislation. There will also be a consultation on the detail of the Schemes in Spring/Summer 2023 during which the details of the policy proposal will be tested with stakeholders before implementation through secondary legislation. This will inform a full Impact Assessment to support the secondary legislation, when brought forward.

EII support levy

51. The proposed levy would constitute a new policy cost on all licensed electricity suppliers across GB. As with other policy costs, the presumption is that this cost will be passed onto their customers.
52. There are currently no exemptions proposed for the levy, with the expectation that costs will be passed through suppliers onto all households and businesses. As a consequence, eligible EII's could expect to also be charged the levy costs by their supplier, though they will ultimately receive greater compensation under the scheme.
53. It is not proposed the Levy will be charged on gas suppliers on the basis the corresponding support scheme is designed to refund specific electricity costs. Consequently, there is no rationale for a levy on gas consumption.
54. Officials are still considering how the levy rate would be calculated, though this will be set out in subsequent regulations. The powers taken in the amendment are to provide HM Government with the ability to establish the levy and to appoint a willing party to administrate said levy. The details of the levy design and calculation will be subject to consultation and set out in regulation.

EII Network Charging Cost Compensation Scheme

55. The type and size of the network cost EII's will be compensated for is under review. HMG committed to exploring reductions on network charges for EII's in the announcement of the Business Industry Supercharger. However, details on the level of compensation will not be included in the amendment, but would be subject to public consultation and, once established, set out in regulations. The amendment seeks to provide HM Government with the enabling powers to establish the proposed scheme, which includes the ability to nominate an administrator for the scheme once one is identified.
56. Compensation would be provided to eligible EII's by the administrator of the ESL/ENCCCS.
57. The scheme would not extend to NI given energy is a devolved matter to NI and that NI operates under a separate grid to GB.

Monetised and non-monetised costs and benefits of each option (including administrative burden)

58. This section considers the choices DBT will have at secondary legislation stage in how the levy and compensation scheme are designed, and what the potential impacts of these might be. Given the uncertainties around the total cost of the scheme, this analysis focuses on how levy design might impact consumers and businesses and the distribution of these. It does not attempt to estimate the precise level of these impacts.
59. The analysis below applies an illustrative scenario where all non-eligible consumers pay an extra £1/MWh on their electricity bills to cover the cost of the levy. The analysis can only be illustrative at this stage because:
- The size of the network charge cost discount that ELLs will receive is currently unclear and will not become known until the secondary legislation is developed.
 - The volume of electricity consumed by eligible businesses over the next ten years, and so the size of the cost passed onto non-eligible consumers, is also uncertain.

Impact on non-eligible bills

60. For eligible ELLs to receive the required level of compensation, the costs will be passed on to all non-eligible consumers. This includes households, retail, public buildings, and non-eligible manufacturing sectors.
61. By distributing the cost of the network cost levy evenly across the entire GB economy, the proportional £ per MWh size is expected to be small.
62. Table 1 shows the expected percentage change in electricity price for non-eligible non-domestic consumers. Unlike with domestic consumers (households), there is a large variation in prices paid by non-domestic consumers depending on the volume of electricity they consume. For example, in 2021, an average very small consumer (0 - 20 MWh) paid £180/MWh in 2021, while an average very large user (70,000 – 150,000 MWh) paid £137/MWh.

Table 1: Change in 2021 retail electricity prices following £1/MWh ELL policy cost passthrough¹²

	<i>Very Small</i>	<i>Small</i>	<i>Small/ Medium</i>	<i>Medium</i>	<i>Large</i>	<i>Very Large</i>	<i>Extra Large</i>
<i>Annual consumption (MWh)</i>	<i>0 – 20</i>	<i>20 - 499</i>	<i>500 – 1,999</i>	<i>2,000 – 19,999</i>	<i>20,000 – 69,999</i>	<i>70,000 – 150,000</i>	<i>>150,000</i>
<i>Average price (£/MWh)</i>	<i>180</i>	<i>162</i>	<i>156</i>	<i>142</i>	<i>139</i>	<i>137</i>	<i>141</i>
<i>Price increase (£/MWh)</i>	<i>1</i>	<i>1</i>	<i>1</i>	<i>1</i>	<i>1</i>	<i>1</i>	<i>1</i>
<i>% increase</i>	<i>0.6%</i>	<i>0.6%</i>	<i>0.6%</i>	<i>0.7%</i>	<i>0.7%</i>	<i>0.7%</i>	<i>0.7%</i>
<i>New price (£/MWh)</i>	<i>181</i>	<i>163</i>	<i>157</i>	<i>143</i>	<i>140</i>	<i>138</i>	<i>142</i>

DESNZ statistics: Gas and electricity prices in the non-domestic sector

63. Small and medium non-domestic electricity consumers, such as pubs and restaurants, would see their prices increase by less than 1% if the £1/MWh ELL policy costs were passed

¹² DESNZ Quarterly Energy Prices Table 3.4.2: <https://www.gov.uk/government/statistical-data-sets/gas-and-electricity-prices-in-the-non-domestic-sector>

through in 2021. Large electricity consumers including non-exempt EIs would see their prices increase by up to 1%.

£3.50

Expected increase in the average dual fuel household bills

64. The average dual fuel UK household is estimated to have consumed 3.5 MWh of electricity in 2021.¹³ This resulted in an overall bill of £752 for the year. A £1/MWh increase in electricity prices would result in an increase of £3.50 for the average household bill. This 0.5% increase would have resulted in a new average bill of £755.50.¹⁴
65. The household bill impact described above is based on 2021 prices and bills, before the energy price crisis caused by the Russian invasion of Ukraine. The large increase in wholesale electricity prices means the proportional impact of the EI support levy would be considerably lower in 2022/23.

Administrative cost of the levy

66. In addition to the direct cost to consumers and businesses in the form of levy payments, the new measures will impose administrative costs on businesses directly responsible for collecting the levy (e.g. energy suppliers).
67. Parties responsible for collecting the levy (e.g. energy suppliers) will incur initial administrative costs through familiarising themselves with the policy, updating systems and engagement to notify customers of the levy. Once the policy is in place, suppliers will also face recurring costs from managing levy payments (including collecting and making payments, interacting with the counterparty to the hydrogen business model revenue support contracts).
68. There will also be a cost to government of collecting the levy and delivering the compensation scheme.

Direct costs and benefits to business calculations

69. As this is enabling legislation, there are no direct costs and benefits to businesses.
70. Following the introduction of the secondary legislation, we expect the following impacts on businesses:
- Direct familiarisation and administrative costs for all licenced GB electricity suppliers.
 - An electricity price increase for all GB consumers
 - A compensation payment paid out to eligible EIs.

Direct impacts on suppliers

71. There are 67 domestic and non-domestic electricity suppliers in the GB market with a further 37 suppliers which serve non-domestic consumers only¹⁵. All 114 licenced suppliers are expected to be in scope for the EI network charge levy and so will face familiarisation costs and the cost of passing through the levy. Both costs are expected to ultimately be faced by electricity customers.
72. The familiarisation cost will be faced by each supplier when an employee must read and comprehend the secondary legislation to determine any action that will need to be taken.

¹³ Source: DESNZ Annual Domestic Energy Bills 2022 (QEP 2.2.5) .

¹⁴ These values are illustrative of an average household. For those households which consume more electricity, such as those with heat pumps, the cost will be higher.

¹⁵ <https://www.ofgem.gov.uk/publications/list-all-electricity-licensees-including-suppliers>

The direct cost will be the lost output from the firm's labour due to the time spent on familiarisation.

73. To pass through the cost of the levy to all customers, suppliers will need to increase the prices. Suppliers incur administrative costs each time they change prices. These costs include:
- Obligations under the Supply Licence Conditions (SLCs) to provide notice to all customers who will be impacted by the change, leading to suppliers sending out notifications (physical and electronic) to customers to inform them of a price change.
 - Increases in the volumes of calls from customers wanting to understand the changes to their tariff, resulting in the requirement for additional call centre resource to respond to increased customer requests including training and amendments of response scripts.
 - Costs associated with reflecting changes in prices or discounts in suppliers' billing systems and on their websites.

Electricity bill increase on non-eligible consumers

74. As referenced in the section above "**impact on non-eligible bills**", the secondary legislation will lead to an increase in the £ per MWH price paid for electricity by non-eligible businesses. This will include sectors such as retail, hospitality, and non-eligible manufacturing. The size of that increase will be determined by the design of the levy. The levy will either be designed to cover a certain proportion of network costs or will cover a flat £ per MWH discount. The section above shows the impact of a levy that results in a flat £1/MWH increase for non-eligible consumers.

Impact of compensation scheme on eligible EIs

75. Eligible EIs will receive a discount on the network charges through a compensation scheme. This discount will result in an effective discount on electricity prices which will benefit them in the following ways:
76. **Increased production:** Reducing electricity prices for EIs leads to reduced costs and thus increased production. This leads to higher domestic profits and an expansion of employment, both of which increase GVA.
77. **Increased investment:** There is a statistically significant positive relationship between lower electricity prices and higher investment for existing businesses. The quantified benefit does not capture any investment associated with entry of new businesses attracted by lower electricity costs, so it likely understates the benefits.
78. **Prevention of firm closure:** Evidence suggests that about 22% of businesses receiving support would be at risk of closure without it.¹⁶ Quantified benefits are the reduction in wages that manufacturing workers can expect after firm closure. Eligible EIs currently employ over 70,000 people and provide skilled, well-paid jobs based predominantly outside of Southeast England.
79. An initial assessment suggests that overall benefits, including employment and output, would likely outweigh the costs to households and non-eligible businesses. This will be explored in detail when the precise form and scope of the levy is set out in the secondary legislation IA.

Risks and assumptions

Risks to the costs faced by non-eligible consumers

80. **Volume risk:** The eventual bill impact faced by non-eligible consumers will be dependent on the number of companies, and therefore the volume of electricity consumption, that is eligible for the compensation scheme delivered through the secondary legislation. This

¹⁶ Based on responses to the EII Compensation Scheme Review 2021

volume is sensitive to numerous factors including future electricity price volatility, changes to the UK industrial make-up and HMG Net Zero policies.

81. For a company to be eligible for the network charge cost compensation, they will need to be sufficiently electricity intensive and operate in an eligible sector. The list of eligible sectors can be found in the scheme guidance in Annex A.
82. **Changes in network costs:** Depending on the design of the levy in the secondary legislation, the size of the levy collected may vary with changes in the value of the network costs. If network costs increased through the late 2020s, the compensation for EIs may also increase and so too will the levy on non-eligible consumers.
83. The electricity network in Great Britain will require significant levels of investment to support the expected increase in peak electricity demand due to net zero. Analysis completed for the Electricity Networks Strategic Framework¹⁷ suggests the onshore electricity network could require an additional £100-240bn of investment by 2050 due to net zero.¹⁸
84. This investment is paid for by private electricity network operators, who are regulated regional monopolies. This is recovered from consumers through the network costs component of their electricity bills over a 45-year cost recovery period, as dictated by Ofgem's price control process. Our analysis suggests net zero could increase the electricity network costs portion of consumer bills by £40-110bn¹⁹ between 2021-2050, additional to BAU costs of £230-240bn.

Impact on small and micro businesses

85. The proposed new primary legislation is expected to have no impact by itself. Therefore, the estimated impact on small and micro businesses is zero. A full small and micro business assessment will be completed at the secondary legislation stage.
86. However, if a levy is implemented through secondary legislation, small and micro business may be affected.
87. As mentioned above, it is likely that all three major energy user groups (households, commercial users, and industry) will contribute to the cost of EI network cost support, and this will include small and micro businesses.
88. The factors determining levy impacts presented in the preceding section in relation to households will also play a role with respect to small businesses. While final decisions will be made at secondary legislation stage, it is expected the levy will have the same per unit impacts on small businesses as on individual consumers.
89. Small and micro businesses are likely to face different baseline energy prices to individual consumers. The overall bill impact will be driven by energy consumption of individual businesses. Unlike in the case of households, there is likely to be greater heterogeneity in energy consumption across businesses. By implication, levy impacts, when applied on volumetric basis, will vary significantly across businesses.
90. If the new levy is implemented, in addition to the additional cost of the levy payment itself, it would impact small and micro businesses through an increased administrative burden on parties responsible for collecting the levy (e.g. small energy suppliers) – these costs are expected to be passed through to consumers.

¹⁷ BEIS, 2022, Electricity Networks Strategic Framework, <https://www.gov.uk/government/publications/electricity-networks-strategic-framework>

¹⁸ Note that this analysis was completed prior to the publication of the British Energy Security Strategy, so the scenarios used in this analysis do not incorporate the latest generation assumptions. We would not expect this to impact the results substantially.

¹⁹ This is lower than the £100-240bn investment estimate because this captures the investment that will be repaid between 2021-2050 only. For example, investment made in 2035 would be repaid between 2035-2080, yet the network costs estimate captures repayments between 2021-2050 only.

Wider impacts (consider the impacts of your proposals)

Equalities Impact Assessment

91. A Public Sector Equality Duty (PSED) assessment has been completed for the Network Charge levy and compensation scheme.
92. This primary legislation is not expected to have any impact, by itself, on protected characteristic groups (PCGs). However, if secondary legislation is passed, there may be some impacts on PCGs. Those impacts are discussed below.
93. While the expected impacts on PCGs are likely to be small, three characteristics might potentially be affected: race/ethnicity²⁰, disability (long-term illness)²¹, and age (measured as the age of the oldest household member).
94. The remaining characteristics are either less relevant at a household level and/or there is limited energy consumption data available at this level of granularity; these characteristics are sex, gender reassignment, sexual orientation, marriage and civil partnership, religion or belief, and pregnancy and maternity.
95. The analysis below uses a hypothetical example of a volumetric electricity levy charged on all electricity consumers across the economy and leading to an increase in electricity prices of £1/MWh. The presented estimates below are used for illustrative purposes only and do not reflect the Government's position on the final design of the levy and the amount of revenue to be raised. This analysis focuses on relative differences in bill impacts across groups with different characteristics and, as such, won't be affected by changes in the absolute bill impact values.
96. For age, 16–24-year-olds and over 75s would be most impacted by the levy relative to income – this is driven primarily by lower median annual income of those two groups.
97. For disability/long-term illness, there is a small difference in the direct impact of the levy for groups with and without a long-term illness as their annual gas consumption is similar. However, as people in the former category tend to have much lower incomes, the levy would impact them disproportionately more.
98. For race/ethnicity, there is a small difference in relative bill impacts, once again, driven by differences in incomes.
99. In summary, at this early stage of policy design, DBT can identify that a levy where the costs are passed through to consumers has the potential to have a negative impact on certain groups with protected characteristics. We are likely to see small variations in direct bill impacts across domestic households with and without protected characteristics, but expect income differences to exacerbate these differences. Although analysis of protected characteristics can provide an indication of likely levy distribution, and impact on various groups, ultimately the levy bill impact will depend on individual household consumption which is heterogenous and may be influenced by a variety of factors.
100. This assessment will be kept under review. An updated PSED assessment will be conducted in the run-up to secondary legislation.

Fuel poverty

²⁰ Source data is available for 2 ethnic groups only: White – White ethnic groups (including White British and White ethnic minorities); Other (all other ethnic minorities). This is because the number of people surveyed was too small to make any reliable conclusions about any of the 18 ethnic groups or 5 aggregated groups. Source: BEIS Fuel Poverty Statistics 2021

²¹ A household that contains someone with a long-term illness/disability that states their condition reduces their ability to carry out day-to-day activities. Examples of long-term illnesses/disabilities include, but are not limited to, conditions which affect vision, hearing, mobility and/or mental health.

101. A household is considered to be fuel poor in England²² if: a) they are living in a property with a fuel poverty energy efficiency rating of band D or below²³; and b) when they spend the required amount to heat their home²⁴, they are left with a residual income below the official poverty line.²⁵²⁶
102. There are 3 important elements in determining whether a household is fuel poor: household income, household energy requirements, fuel prices.
103. There were 3,176,000 households in fuel poverty in England in 2019, which corresponds to 13.42% of all households.²⁷
104. For illustration, a hypothetical increase in natural gas price of £1/MWh would increase the number of fuel poor households in England by under 6000.

A summary of the potential trade implications of measure

105. The proposed primary legislation is not expected to impact international trade and investment.
106. We expect a decrease in imports for eligible EII sectors such as steel, glass and chemicals following the implementation of the EII levy and compensation scheme as part of the British Industry Supercharger. The objective of the secondary legislation is to reduce the risk of carbon leakage in EIIs by closing the electricity price-gap between GB and comparable countries. Electricity makes up a significant proportion of costs for EIIs so reducing electricity prices will make them more internationally competitive. EIIs will be able to better compete with imports from countries which already provide lower industrial electricity prices thus reducing imports.
107. The increased international competitiveness of EIIs from lower electricity prices could also increase exports.
108. As eligible EII electricity prices fall, prices will increase slightly for non-eligible non-domestic consumers. This could lead to an increase in imports and a decrease in exports for non-eligible sectors. However, the effects on non-eligible sectors are expected to be minimal for two reasons. First, if the cost of the levy is distributed evenly across the whole economy, then the size of the price increase on each consumer will be small. Second, non-eligible industries are less electricity intensive trade exposed, so they are competing less with imports in the domestic market.

Monitoring and Evaluation

109. A full monitoring and evaluation plan will be designed in the secondary legislation.
110. The EII Emissions Trading Scheme (ETS) and Carbon Pricing Scheme (CPS) Compensation scheme has been in operation since 2013. The team commissioned

²² Under Low Income Low Energy Efficiency (LILEE) methodology

²³ Energy efficiency rating is measured using the Fuel Poverty Energy Efficiency Rating (FPEER) Methodology, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/332236/fpeer_methodology.pdf

²⁴ Fuel costs required to have a warm, well-lit home, with hot water and the running of appliances. An equivalisation factor is applied to reflect that households require different levels of energy depending on who lives in the property. Further information on how fuel costs are calculated can be found in Section 5 of the Methodology Handbook: <https://www.gov.uk/government/publications/fuel-poverty-statistics-methodology-handbook>

²⁵ Residual income is defined as equivalised income after housing costs, tax and National Insurance. Equivalisation reflects that households have different spending requirements depending on who lives in the property. We note that sources of income counted has changed to remove some disability benefits. Further information on how income is modelled can be found in Section 3 of the Methodology Handbook (<https://www.gov.uk/government/publications/fuel-poverty-statistics-methodology-handbook>)

²⁶ The poverty line (income poverty) is defined as an equivalised disposable income of less than 60% of the national median in a given year: (see Section 2 in:

<https://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/incomeandwealth/articles/persistentpovertyintheukandu/2015>)

²⁷ Fuel Poverty 2019 data published in April 2021 Annual Fuel Poverty Report

Economic Insight for an evaluation of the schemes in 2018 and consulted on proposals for the future design of the schemes earlier in 2021.

111. The key monitoring indicators are:
- a. Payment of compensation (internal)
 - b. Industrial electricity price differential (Eurostat and internal analysis)
 - c. Production by eligible EIs
 - d. Imports of products manufactured by eligible EIs
 - e. (dis)investment by eligible EIs
 - f. wage and employment levels in eligible EIs
112. The main data sources are FAME for company and sector information and HMRC for trade data.
113. In addition, the project team placed the following information obligations on beneficiaries:
- a. Total capital expenditure
 - b. Total capital expenditure in the UK
 - c. Total UK capital expenditure on new assets
 - d. Total UK capital expenditure on existing assets
 - e. Total investment into energy efficiency measures
 - f. Annual earnings before interest, taxes, depreciation and amortization
 - g. Average wage by role and location.
114. A similar approach will be taken for the Network Charge levy and compensation scheme given the aligned nature of the policy design and the objective.

Inputs	Outputs	Outcomes	Impacts
Annual HMG expenditure in the form of compensation BEIS staff resource	Database of eligible recipients Payment of compensation to eligible EI	Reduced international EI electricity price differential Price-setting EI avoid need to increase prices to cover increasing indirect costs Price-taking EI avoid reduced profitability/operating surplus from higher input costs	Avoid decreased UK FDI Avoid decreased standard of living for EI employees Avoid decreased UK EI competitiveness by 2030 Mitigate long term increased emissions from carbon leakage Avoid increased regional economic inequality

Annex

Annex A: eligibility for the EII Exemption Scheme

115. There are five key requirements in determining whether a business is eligible for an EII certificate for an exemption from a proportion of the indirect costs of funding the CFD, RO and FIT:
- a. The business must manufacture a product in the UK within an eligible sector (defined by a 4-digit NACE Code) – the “sector level test”.
 - b. The business must pass a 20% electricity intensity test – the “business level test”.
 - c. The business must not be an Ailing or Insolvent Economic Actor (AIEA) (see paragraphs 24-29 below).
 - d. The business must have at least two quarters of financial data.
 - e. The application must contain evidence of the proportion of electricity used to manufacture the product for a period of at least three months.
116. In this guidance, “business” (or the “applicant”) refers to the legal entity manufacturing a product in the UK within an eligible NACE Code, such as a Company registered at Companies House.
117. If an agent is applying for an exemption on behalf of a client, they must submit a Letter of Authority (LoA) with the completed application which confirms they are acting on behalf of the applicant for this purpose. This should be signed by a Director or a senior manager within the business.
118. A business that successfully applies for the exemption will be issued with a certificate (an “EII certificate”) confirming their eligibility for the CFD, RO and FIT exemption.
119. Successful applicants should then pass their certificate on to their electricity supplier so that they receive the benefit of the exemption. Please note that electricity suppliers will need to set up the relevant arrangements before they receive, and therefore pass on, the exemptions.

Sector level test

120. The European Commission’s “Guidelines on State aid for environmental protection and energy 2014-2020” (referred to in this guidance as the EEAG) sets out which sectors (by 4-digit NACE code) could be eligible for exemption.
121. To ensure that support is targeted at those most at risk, the UK Government further limited eligibility to those sectors which are electricity intensive and subject to international competitive pressures using UK specific data from the Annual Business Survey, specifically, those found to have a trade intensity of at least 4% and an electricity-intensity of at least 7%. Eligible sectors are those carrying out the activities listed in Annex 1, referred to as “specified activities” in the Regulations.
122. Applicants will need to establish that they manufacture a product(s) in the UK that falls within one or more of the eligible 4-digit NACE codes in Annex 1. If a business does not manufacture a product in one of these sectors it will not be eligible for an EII certificate. Businesses that produce both eligible and ineligible products can apply but the exemption can only be applied to the proportion of electricity used to produce the eligible product.

The “Business Level Test”

123. The purpose of the business level test is to ensure that the exemptions target only those businesses where support is most needed, i.e. those that will be put at a significant competitive disadvantage from the costs of funding renewable and low carbon policies.
124. To satisfy the business level test, businesses will need to show that their electricity costs amount to 20% or more of their Gross Value Added (GVA) over a reference period – the “relevant period”.

125. GVA is defined as earnings before taxes, interest, depreciation and amortisation (EBITDA) excluding items which are extraordinary and all staff costs including employers pension and national insurance contributions, director's salaries and bonuses, casual or agency staff costs and other arrangements where employees are paid indirectly.
126. In line with the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102), which provides general accounting procedures on extraordinary expenditure, we define an extraordinary item as something which is highly unusual or infrequent in nature and not related to the ordinary and typical operating activities of the business.
127. If a business has a subsidiary business, they can apply at any level provided the applicant is a legal entity such as a Company registered at Companies House.
128. Eligibility will be assessed using data based on the applicant's financial year. If applicable, the accounts on which data has been based must have been submitted to Companies House to allow verification. A business cannot apply with fewer periods of data than exist i.e. it is not permissible to exclude a year to ensure eligibility. The relevant period for businesses is as follows:
- a. For businesses with three or more years of published annual accounts, the relevant period will be the three most recent consecutive years for which there are annual accounts.
 - b. For businesses with two years of published annual accounts, the relevant period will be those two years.
 - c. For businesses with one year of published annual accounts, the relevant period will be that one year.
 - d. A business that does not have any annual accounts and has been trading for 21 months or less can also apply. The relevant period in this circumstance will be the period for which they have been carrying out a specified activity and have financial data in the 12 months prior to making an application (which must be at least six months). Such businesses will need to supply a copy of their first set of annual accounts to BEIS within 30 days of the accounts being finalised.