Mineral Products Association Response to the DECC Call for Evidence on Energy: Review of the Balance of Competences

The Mineral Products Association (MPA) is the trade association for the aggregates, asphalt, cement, concrete, dimension stone, lime, mortar and silica sand industries. With the recent addition of The British Precast Concrete Federation (BPCF) and the British Association of Reinforcement (BAR), it has a growing membership of 465 companies and is the sectoral voice for mineral products. MPA membership is made up of the vast majority of independent SME companies throughout the UK, as well as the 9 major international and global companies. It covers 100% of GB cement production, 90% of aggregates production, 95% of asphalt and ready-mixed concrete production and 70% of precast concrete production. Each year the industry supplies £9 billion of materials and services to the £120 billion construction and other sectors. Industry production represents the largest materials flow in the UK economy and is also one of the largest manufacturing sectors[1].

This response is written from the perspective of the cement and lime product groups within the MPA membership which are the most energy intensive operations within MPA and are therefore amongst the industrial sectors most affected by energy policy.

General

1. To what extent does EU action in the energy field benefit and / or disadvantage the UK / your sector/stakeholders? Is there a sector where this is most marked?

The shared competence in the area of energy has put the UK cement and lime manufacturing sectors at a competitive disadvantage within and outside the EU because UK consumers are subject to UK domestic legislation and indirect legislative costs not faced by other EU and non-EU competitors. For example, the direct costs associated with levies paid on the use of fossil fuel energy (Climate Change Levy) and schemes designed to encourage energy efficiency improvements (CRC Energy Efficiency Scheme). Mineral product producers also face large indirect costs of electricity market changes and renewable subsidies including Carbon Price Support, Renewables Obligation and Feed-in-Tariffs, while receiving no incentives themselves for use of renewable energy through schemes such as the Renewable Heat incentive (RHI).

MPA welcomed the announcement by the Chancellor in Budget 2013 to apply the mineralogical processes exemption set out in Article 2.4 of the Taxation of Energy Products Directive as has been taken up in other European countries. However, this is an example of where the UK has been quick to burden mineralogical processes such as cement and lime with the cost of energy taxes. The impact of these taxes have been identified to HM Government over many years but the implementation and delivery of exemptions afforded to non-UK operators have been slow and UK operators will only be able to recover their competitive position from April 2014 onwards.

The lack of harmonisation of energy legislation across the EU has allowed the UK Government to favour certain sectors of the economy with available incentives. UK Government policy to date has concentrated on giving power generators certainty so that they can carry out low risk investment in renewable energy with the assistance of guaranteed subsidies and cost pass-through opportunities.

[1] For more information visit: www.mineralproducts.org

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Mineral products industries like the cement and lime sectors are not afforded the same privilege of low risk investment and in addition are having to bear the ever increasing pass through costs from the power generators. MPA has calculated that the indirect cost of energy (and climate change) policies faced by the cement sector could reach €80m a year by 2020. This significant cost is further reducing the ability for industry to invest in renewable energy and low carbon technologies.

2. Do you think that the EU has introduced legislation that is proportionate / disproportionate to the issue it aims to address?

Energy intensive industries are facing increased EU legislation that is disproportionate to the issues it aims to address. An example of this is the Energy Efficiency Directive and in particular the Article 8 requirement that all Member States introduce a programme of regular energy audits for 'large enterprises'.

There is an argument that suggests that proportionally SME's have most to gain from energy efficiency measures. Many large enterprises are already captured by one or more of CCA, CRC or EU ETS. As a result large enterprises that are energy intensive are fully aware of their energy use and where savings can be made. For example, energy costs in cement manufacture account for 40% of the Gross Value Added of the sector. As a consequence any energy savings that can be made cost effectively have already been implemented.

Government should analyse where proportionally the greatest energy savings can occur because our belief is that energy intensive industries are already maximising their energy saving potential and this would suggest that some of the larger SME's should be captured by the scheme, particularly those with high energy bills.

Furthermore, energy covered by existing schemes such as EU ETS, CRC and CCA should be excluded from the Article 8 audit. This will ensure that there is no duplication of effort.

3. In what areas might the UK's interests be served better if action were to be taken at:
a. EU level instead of national, regional or international level?
b. national, regional or international level instead of EU level?

a. Harmonised legislation at EU level is only useful when accompanied with harmonised regulatory implementation. Too often EU legislation is inconsistently implemented in Member States leading to inconsistent treatment of operators and potential market distortions within sectors. Poor policy making can also provide distortions between sectors that either compete in the same product markets or compete for the same energy resources. For example, EU level legislation could be implemented that would ensure a balanced approach to incentivising renewable energy use across all sectors of the economy. In addition, a harmonised approach to legislation would mean UK industry is not unduly penalised by an ever accumulating burden of UK energy policies that are not faced by EU and non-EU competitors.

b. At EU level the cement and lime sectors did not meet the criteria to receive compensation for the indirect costs of the EU Emissions Trading System, although if the calculation had been applied at the UK level both sectors would have qualified for important compensation against rising costs. Removing the need to apply to the EU for state aid would ensure that the UK could target compensation schemes at those industries in the UK that need to be protected from the high costs of energy and climate change policies and not just those determined by the EU to be at risk.

The EU and the UK have isolated themselves with national and regional policies on energy efficiency and renewables. All of these require global action and increased effort is required under international programmes like the UNFCCC to find a robust and globally harmonised solution to GHG emissions. This will ensure that EU and UK operators are not put at a competitive disadvantage in global markets because they are having to bear energy and climate change policy costs that are not faced by non-EU operators.

4. How could the EU's current competence for energy be used more effectively? For example, could more be done during the development stage of proposals and the preparation of impact assessments? Are there alternatives to legislation and how feasible / practical is it to have continuous review mechanisms to ensure existing legislation remains fit for purpose in the light of changing circumstances?

The fundamental flaw with most policy impact assessments (whether at EU or UK level) in this area is that they only assess the impact of the single policy or legislative proposal. In practice however, any new proposal adds to the array of energy policy and legislation already in place. As a result the cumulative burden of new policies within the current landscape is never assessed. A proposal that appears to be beneficial in isolation may add enough additional costs to the current burden on businesses and other energy consumers that any benefit is negated. All impact assessments should take account of the current cost burden of energy policy on consumers, and especially energy intensive industries.

Thematic Areas

5. What have been the benefits or disadvantages for the UK / your sector of the development of the internal energy market? Is further or deeper integration of EU energy markets desirable?

In principle liberalisation of the energy market through the removal of national protectionist intervention can offer many benefits to the UK. However, the UK power market is very concentrated, it lacks competition and is too dependent on imports for these benefits to be fully realised.

A more competitive energy market could be achieved by introducing a greater choice of competing energy suppliers. This would provide greater liquidity and transparency in the wholesale market and ensure UK energy supplies are more competitively priced, particularly for energy intensive consumers.

Reducing reliance on imports is required to secure future supply and prevent wide spread blackouts. This will also ensure industry is not burdened with energy curfews that would reduce production and damage economic growth.

Industry is currently bearing the cost burden of decarbonising power generation, while domestic consumers are not taking on as much of the burden and are making slower progress in terms of improving energy efficiency compared to industrial consumers. This imbalance needs to be addressed for the benefits of an internal energy market to be realised by all sectors.

6. To what extent do you think the UK has benefited or been disadvantaged by EU measures to increase security of supply and facilitate infrastructure development?

Consumers will pay immediately for increased capacity that will be developed later. This time lag between the costs and the benefits means that consumers are disadvantaged in the short term.

Eligibility for the Electricity Market Reform cost exemption for energy intensive industries is tied to that for Carbon Price Support (CPS) compensation. Therefore those sectors, such as cement and lime, that are still waiting to hear if they are eligible for CPS compensation are disadvantaged and given no certainty of the level of future energy policy cost they will face.

7. What effect have EU measures had on the development and exploitation of the UK's indigenous energy sources? Are further measures needed in regard to exploitation of unconventional sources, for example shale gas?

The USA has benefited considerably from the development of shale gas. The high calcium lime sector is nearly 100% dependent on gas as a fuel source because only the cleanest, highest quality fuels can meet the high specification requirements for lime products that are used in pharmaceuticals and drinking water purification. In order to keep high calcium lime production in the UK and therefore ensure security of supply for industries such as steel manufacture, water treatment and pharmaceuticals, the development of indigenous unconventional sources of natural gas will need to be a key component of future UK energy supply.

It is also important to ensure that supply can meet periods of peak demand when, for example, the wind doesn't blow. Unconventional sources will bridge the gap between coal/natural gas and low carbon. Measures that enable the exploitation of unconventional sources will therefore need to be at the forefront of EU and UK energy legislation.

8. How have measures and policies at an EU level helped or hindered the development and deployment of sustainability measures - energy efficiency, renewable and low carbon energy? What have been the impacts of these measures on other forms of energy generation and the internal market? Should the EU be doing more or less?

The lack of harmonisation of energy legislation across the EU has allowed the UK Government to favour certain sectors of the economy with available incentives.

One particular missed opportunity by the UK Government as far as cement manufacture is concerned is the Renewable Heat Incentive (RHI). RHI funds expensive technologies (e.g. small inefficient biomass boilers) for small energy users. Industry, which consumes energy on a large scale and more efficiently in directly fired operations rather than boilers, receives no incentive to use biomass.

The cement sector has the ability to significantly increase its use of biomass fuels. However, it is struggling to compete on the market because power generators are incentivised to use biomass through the Renewables Obligation and smaller businesses are incentivised to install biomass boilers through the RHI. Directly fired operations such cement clinker production, asphalt production and lime production fall within a 'policy incentive void' and are given no incentive to maximise the use of biomass.

Incentives have the potential to increase the market demand for biomass fuels and as a result their cost increases and the directly fired processes will become priced out of the market. This trend is already becoming apparent in the cement sector. ***Annex I*** shows the use of 100% biomass fuels in cement manufacture is levelling off while the use of part-biomass fuels (e.g. tyres), which are not incentivised elsewhere, is increasing. This is a missed opportunity for the UK as the cement sector, which requires around 24,000 TJ of fuel energy annually, could contribute significantly to UK renewable heat targets. The imbalanced targeting of sectors for renewable energy incentives is only going to result in a shift in

the use of biomass from one sector to another rather than a net increase as is required to meet the targets set. ***Annex II*** illustrates this shift as a schematic.

The EU could do more to ensure that member states take a balanced approach to meeting renewable energy targets that incentivises all sectors of the economy.

The EU could also do more to ensure that member states take a pragmatic approach to the implementation of EU Directives that does not overly burden industry. Some flexibility is required to ensure operators are not unduly penalised. The feeling by UK operators is that the UK implements every Directive to the letter of the law (and sometimes more stringently). Evidence suggests that other countries seem to take a more 'industry friendly approach in both the timetable for implementation and the interpretation of conditions. In terms of the requirement in the Energy Efficiency Directive for all large enterprises to undertake an energy audit, it is hoped that the UK will take a pragmatic approach to this, particularly for energy intensive industries that are already regulated under schemes such as the Emissions Trading Scheme.

9. To what extent might it be beneficial or disadvantageous for the EU to take on more initiatives and to exercise greater external competence in the field of energy, for example in negotiating international agreements and representing an EU view (speaking with one voice) in international meetings rather than Member States representing themselves?

To date the UNFCCC negotiations have failed to deliver an international agreement on climate change. Until there is an agreement EU industry is being placed at a disadvantage compared to non-EU competitors due to the increasing cost burden of EU climate change and energy policies. The EU should be pushing more for an international agreement, the lack of which shows a failure for the EU to negotiate either as a block or individually.

10. To what extent does EU action under the Euratom Treaty (for example, in relation to nuclear safety) contribute to / disadvantage the development of nuclear power in the UK and EU? To what extent do Euratom measures in respect of non-nuclear activities help or hinder occupational protection, protection of the general public, or the use of medical exposures and procedures?

No comment.

Future Challenges and Opportunities

11. What implications will future challenges in the energy field have for the UK and EU, for example the effects of increasing global demand for energy, potentially rising global market prices and the transition to a low carbon economy to meet climate change objectives?

The International Energy Agency has highlighted that emerging economies will account for more than 90% of net energy demand growth to 2035. This growth will create two significant problems for EU energy consumers:

1. The reduced security of supply for existing developed economies.
2. Reduced effectiveness of EU climate change policies in tackling global warming.

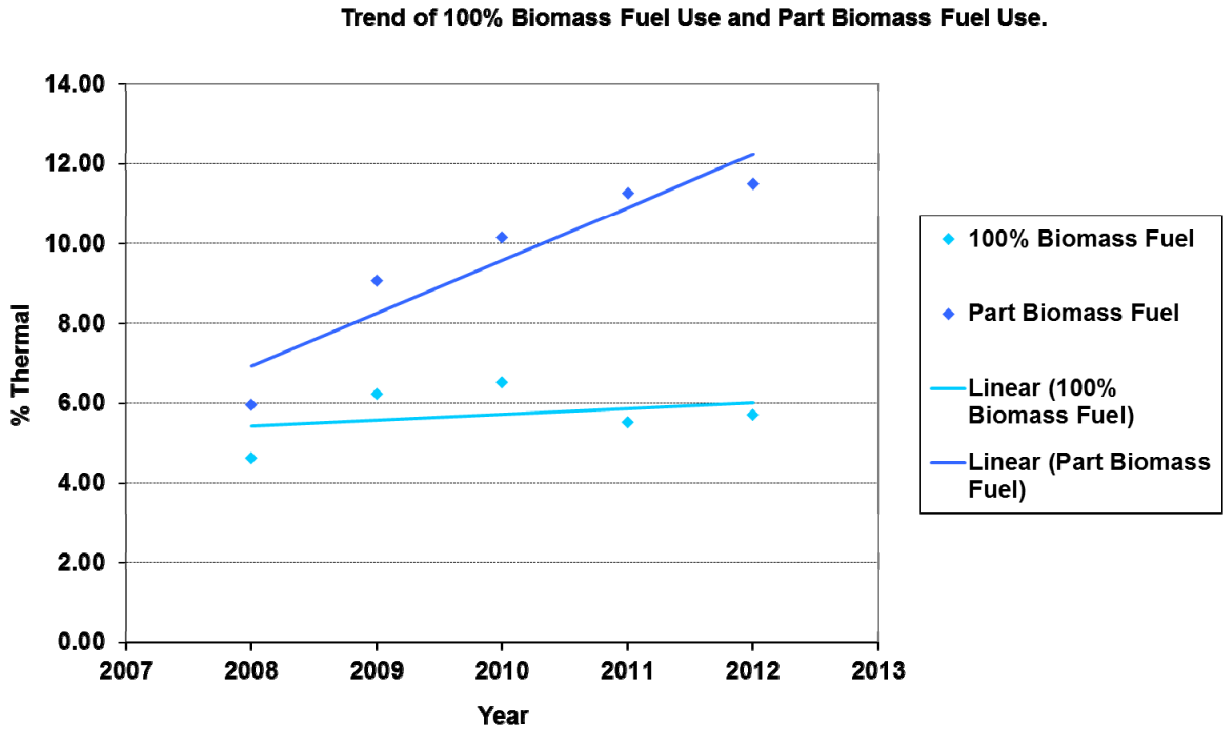
Just this one statistic illustrates that the EU ETS cannot survive for too much longer in global isolation. As the energy demand of the emerging economies grows it follows that the effectiveness of the EU ETS, as an instrument to tackle climate change, diminishes. The EU needs to ensure there is a global approach

to tackling climate change otherwise the EU contribution to emissions reduction will grow increasingly smaller and make little impact, while putting EU operators at a competitive disadvantage in global markets due to the additional burden of energy policy cost.

12. What would be the costs and benefits of facing these at an international, EU, or national level?
The Stern Review published in 2006 proposed that it is more cost effective to act to reduce global carbon emissions rather than not act. In particular the report noted that if nothing is done to reduce global carbon emissions, climate change could cost at least 5% of world GDP (an impact which the report stated could rise to 20%), while combating climate change would cost 1% of global GDP. This overly simplistic hypothesis does not take sufficient account of the time lag of upfront direct and indirect cost to consumers before the benefits of low carbon are realised.

This work should be updated taking into account the time lag between costs and benefits and also the impact of a global imbalance between those countries that are taking on the costs of tackling climate change now compared to those that are not.

Annex I


Trend of 100% Biomass Fuel Use and Part Biomass Fuel Use.
14.00
12.00
10.00
8.00
6.00
4.00
2.00
0.00
% Thermal
2007
2008
2009
2010
2011
2012
2013
Year
100% Biomass Fuel
Part Biomass Fuel
Linear (100% Biomass Fuel)
Linear (Part Biomass Fuel)

Annex II: The biased support for renewable fuel that disadvantages renewable fuel use in directly fired processes e.g. cement, lime and asphalt