

<b>Title:</b> EII Capacity Market Exemption Scheme <b>IA No:</b> DBT-007(IA-F)-23-BG <b>RPC Reference No:</b> N/A <b>Lead department or agency:</b> DBT <b>Other departments or agencies:</b> DESNZ	<b>Impact Assessment (IA)</b>
	<b>Date:</b> 22/01/24
	<b>Stage:</b> Final
	<b>Source of intervention:</b> Domestic
	<b>Type of measure:</b> Secondary legislation
	<b>Contact for enquiries:</b> energyintensiveindustries@businessandtrade.gov.uk

<b>Summary: Intervention and Options</b>	<b>RPC Opinion:</b> N/A
--	-------------------------

Cost of Preferred (or more likely) Option (in 2020 prices)			
Total Net Present Social Value	Business Net Present Value	Net cost to business per year	
£9.4 billion - Total Supercharger package £1.7bn - Capacity Market Exemption	£9.4 billion - Total Supercharger package £1.7bn - Capacity Market Exemption	£0.02m – Total Supercharger package £0 – Capacity Market Exemption	<b>Business Impact Target Status</b> Non-qualifying provision

**What is the problem under consideration? Why is government action or intervention necessary?**

GB industrial electricity costs are higher than those in comparable neighbouring countries, causing a risk of indirect carbon leakage where production shifts to other jurisdictions because our energy intensive industries (EIs) are not able to remain profitable in GB.

Capacity Market charges make up a higher proportion of EI energy bills and neighbouring countries have chosen to exempt firms from these charges. 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 EIs. The objective of the secondary legislation will be to provide EIs with relief from the Capacity Market costs on their electricity bills through an automatic exemption which will be worth on average £5/MWh.

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, the continued electricity price gap could lead to production, investment and employment leaving the GB market for markets with lower net zero ambitions and lower electricity prices. This is particularly true of nascent, internationally mobile EI sectors such as gigafactories.

**Part exemption scheme:** Exempting eligible EIs from part of the cost of the CM would be difficult to administer and more likely to lead to over/under-subsidy.

**Compensation scheme:** Would require significant resource, including design and administration of a levy to make payments to eligible EIs. Could also result in over/under-subsidy and related admin costs.

**Other discounted options:** Private grants and loans which were deemed too complex and inefficient. Investment in electricity infrastructure was deemed not timely enough.

Is this measure likely to impact on international trade and investment?	Yes
---	-----

Are any of these organisations in scope?	<b>Micro</b> Yes	<b>Small</b> Yes	<b>Medium</b> Yes	<b>Large</b> Yes
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)	<b>Traded:</b> +0.4 (annual)		<b>Non-traded:</b>	
<b>Will the policy be reviewed?</b> It will be reviewed. <b>If applicable, set review date:</b> Before 2029				

*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 Minister:

*N Ghem*

Date:

22/01/24

# Summary: Analysis & Evidence

# Policy Option 1

## Description:

### FULL ECONOMIC ASSESSMENT

Price Base Year 2020	PV Base Year 2023	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			<b>Low:</b> Supercharger - £3,999m CM Exemption - £908m	<b>High:</b> Supercharger - £24,041m CM Exemption - £3,402m	<b>Best Estimate:</b> Supercharger - £9,438m CM Exemption - £1,680m

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Present Value)	Total Cost (Present Value)
Low	-	Supercharger - 45 CM Exemption - 7	Supercharger - 453 CM Exemption - 66
High	-	Supercharger - 380 CM Exemption - 60	Supercharger - 3,802 CM Exemption - 603
Best Estimate	-	Supercharger - 141 CM Exemption - 24	Supercharger - 1,414 CM Exemption - 243

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

As the Supercharger and the CM Exemption are transfers, there are no fiscal impacts to consider. The main monetised costs are from increased carbon emissions (£400m-3,600m from the overall Supercharger with £100m-600m from the CM Exemption) and related air quality impacts (£30m-200m from the Supercharger with up to c. £30m from the CM Exemption) resulting from increased electricity usage by eligible businesses.

There are also administration and familiarisation costs that will be faced by eligible ELLs and administration costs for the administrator of the Supercharger which will potentially be passed through to customers. These have been included in the calculation of Direct Costs to Businesses and are estimated at c. £0.3m over the 10-year appraisal period, with a £0.02m annual cost. Note that we do not currently have an estimate for the administrator costs of the Network Charging Cost Compensation Scheme, but it is expected to be less than £10m over the 10-year appraisal period.

The CM Exemption alone is expected to have no to minimal administration or familiarisation costs as eligible businesses and the administrator are already familiar with the processes involved with the scheme.

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

N/A

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Present Value)	Total Benefit (Present Value)
Low	-	Supercharger - 374 CM Exemption - 59	Supercharger - 3,735 CM Exemption - 588
High	-	Supercharger - 2,784 CM Exemption - 459	Supercharger - 27,842 CM Exemption - 4,594
Best Estimate	-	Supercharger - 1,085 CM Exemption - 192	Supercharger - 10,853 CM Exemption - 1,923

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

The monetised benefits result from increased output and investment resulting from lower electricity prices for eligible firms. Increased employment is worth between £1.8bn-15bn for the Supercharger with £0.3bn-2.5bn for the CM Exemption. Increased investment is worth between £0.6bn-2.5bn for the Supercharger with £0.1bn-0.4bn for the CM Exemption. Increased domestic profits are worth £1.2bn-10.1bn for the Supercharger with £0.2bn-1.7bn for the CM Exemption.

We have also estimated the benefits from preventing potential firm closures with the support offered through the Supercharger and CM Exemption. These benefits are smaller than those estimated for the productivity and investment impacts at up to c. £200m for the Supercharger with up to c. £30m for the CM Exemption.

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

N/A

**Key assumptions/sensitivities/risks****Discount rate (%)**

3.5%

There are a range of elasticities taken from literature that have been used to estimate the production and investment impacts resulting from lower electricity prices. These are detailed in Section 6 on monetised costs and benefits.

Assumptions on future electricity prices and in particular fossil fuel prices are key assumptions which face inherent uncertainty. To mitigate these we have included Low and High Fossil Fuel sensitivity tests.

The benefits and costs are based on the current view of eligibility of the Supercharger scheme. If more sectors and businesses are deemed eligible for the scheme, the estimated costs and benefits of the scheme will increase.

The direct impacts on electricity prices for eligible and non-eligible businesses are treated as a transfer and therefore not considered in the calculation of the value for money of the scheme or the direct impact on business. The value for money assessment is based on the indirect impacts resulting from lower electricity prices for eligible businesses (increased production, investment) and assumes that the additional electricity costs for households and non-eligible businesses are not big enough to impact their behaviour.

The direct impact on business is treated as the costs that result from additional administration and familiarisation for eligible businesses. The direct benefits and costs in terms of electricity prices are treated as a transfer between businesses and therefore not considered.

**BUSINESS ASSESSMENT (Option 1)**

<b>Direct impact on business (Equivalent Annual) £m:</b>			<b>Score for Business Impact Target (qualifying provisions only) £m:</b>
<b>Costs:</b> 0.02	<b>Benefits:</b> -	<b>Net:</b> -0.02	
			N/A

# Contents

Section 1 - Problem under consideration and rationale for intervention .....	6
Section 2 - Rationale and evidence to justify the level of analysis used in the IA (proportionality approach).....	13
Section 3 - Description of options considered .....	14
Section 4 - Policy objective.....	14
Section 5 - Summary and preferred option with description of implementation plan .....	15
Section 6 - Monetised and non-monetised costs and benefits of each option.....	16
Section 7 - Risks and assumptions .....	26
Section 8 - Impact on small and micro businesses.....	27
Section 9 - Wider impacts.....	28
Section 10 - A summary of the potential trade implications of measure .....	30
Section 11 - Monitoring and Evaluation.....	31
Annex A – Supercharger Bills Impacts Modelling.....	32
Annex B – Network Charges Costs Analysis.....	35

# Evidence Base

## Section 1 - 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 foundation industries (e.g. glass and cement) as well as industries that are essential to critical national infrastructure (e.g. steel and chemicals) and form the supply chain for other important strategic sectors (e.g. auto and aero). EI firms represent c. 400,000 direct key manufacturing jobs within GB, 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 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 whose high energy costs have been cited as a critical factor for decisions on inward investment.
3. HMG's 2022 Energy Security Strategy committed to explore a series of measures designed to support EIs, committing 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 GB'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 increased by the Russian invasion of Ukraine, the long-term inequality in retail price with comparator countries remains for EIs in particular. This long-term gap is in part due to GB's ambition of decarbonising electricity generation, with a large reliance on gas which is more expensive than coal, putting GB at a disadvantage relative to EIs in comparable countries. GB's ambitious deployment of renewable electricity generation leads to higher policy costs and higher prices for consumers.
8. HMG has therefore announced the British Industry Supercharger – a suite of measures designed to close the long-term gap in electricity prices between GB and key competitor

countries. The measures include:

- a. Increasing the level of exemption offered by the existing EII Exemption Scheme from 85% to 100% aid intensity; which is anticipated to amount to a £5-£7/MWh reduction in 2025 from current levels;
  - b. Implementing a full exemption from the charges associated with the UK Capacity Market, which is anticipated to amount to around £5/MWh in 2025; and
  - c. A reduction in the charges paid for use on the electricity grid (also referred to as Network Charging costs).
9. The focus of this impact assessment is the second pillar of the British Industry Supercharger – **the exemption from UK Capacity Market charges paid by EIs.**

## Capacity Market

10. The GB Capacity Market (CM) is one of the government's tools to ensure a secure and reliable electricity system. The CM provides all forms of capacity capable of contributing to security of supply with incentives to be on the system and to deliver during periods of electricity stress – for example during cold, still periods when demand is high and wind generation is low.
11. The CM is technology neutral, with existing generators competing against a range of other technologies to obtain agreements under which they commit to making their capacity available when needed, in return for guaranteed payments.
12. The Department for Energy Security and Net Zero (DESNZ) has overall ownership of the CM and sets the direction of the policy. Ofgem's role is to ensure market arrangements are fit for purpose, monitor the CM and manage some Rules Changes and some appeals processes. National Grid EMR Delivery Body provides annual advice on capacity requirements and administers key elements of the CM. The Electricity Settlements Company (ESC) controls payments related to the CM which are settled and metered through EMR Settlement Ltd.
13. CM payments are funded by a charge on electricity suppliers who then recover costs from their customers. Total costs of the CM are made up of two elements:
  - a. The costs of the CM itself which funds capacity provider payments (the 'supplier charge'); and
  - b. A settlements costs levy to fund the operational costs of ESC, the Settlement Body (the 'costs levy').
14. A supplier's share of the CM 'supplier charge' costs is calculated based on their share of total electricity demand at peak times during weekdays over the winter period. As the system currently stands, EIs are included in each supplier's electricity demand, and the intention of the proposal is to set up a mechanism by which EIs may be indirectly exempted from 100% of CM charges passed on to them by electricity suppliers. It is anticipated that suppliers would redistribute total exempted costs between other non-eligible users.
15. The supplier charging mechanism for the CM currently works as follows:

- a. In a normal year, licensed electricity suppliers submit forecasts for their gross demand to the Settlement Body (ESC) by 1 June ahead of commencement of the CM Delivery Year (1 October).
  - b. EMRS, on behalf of ESC, then issue a Payment Schedule for the 12 months of the Delivery Year (October-September), at least two months ahead of the beginning of the Delivery Year. This is proposed to be the effective deadline for EII exemptions to be considered and taken into account to allow for adjustments to be calculated ahead of the Delivery Year.
  - c. Suppliers currently pay to the projected Payment Schedule until April the following year before a revised Payment Schedule is created based on Winter peak demand and actual metered usage data which is collected from November to February based on the peak Winter period.
  - d. A revised Payment Schedule is then created for the remaining months of the Delivery Year based on the new actual metered data, with the proposal that actual EII electricity usage is adjusted and a revised Payment Schedule is created for the remaining months of the Delivery Year (April-September) and paid for by non-eligible users.
16. The policy would amend formulas in the Electricity Capacity (Supplier Payment etc.) Regulations 2014 which describe how costs of the Capacity Market are paid for. Amendments will ensure accurate supplier calculations and collection of payment across relevant non-eligible users. The way we will do this is by amending definitions within formulas to include adjustments to exempt eligible EIIs relating to each supplier.
17. The proposal is for eligibility criteria to mirror that of the EII Exemption Scheme on the basis of the following criteria, reflecting firms who are at the greatest risk of carbon leakage:
- The business must manufacture a product in GB within an eligible sector (defined by a 4-digit NACE Code) – must be operating in one of the sectors deemed to be eligible for the scheme - the “sector-level test”.
  - The business must pass a 20% electricity intensity test, the “business-level test”.
  - The business must not be an AIEA (Ailing or Insolvent Economic Actor).
  - The business must have at least two quarters of financial data.
  - The application must contain evidence of the proportion of electricity used to manufacture the product for a period of at least three months.
18. The policy package is designed to mitigate carbon leakage by bringing electricity prices for EIIs down to a level more commensurate with comparable neighbouring countries. For those EIIs particularly exposed to international trade and heavily reliant on electricity, paying the full amount of electricity policy costs on their electricity consumption can increase the risk of carbon leakage and the cost of electricity relative to other energy sources.
19. The existing EII Exemption Scheme operates via a two-step test assessing sectoral electricity and trade intensity, and business level electricity intensity. For reasons of operational simplicity, we propose to use the same cohort for the other measures rather than running the same two-step test multiple times to the same outcome. We intend to apply the same methodology and include the same cohort for all three measures.
20. We will also exempt EIIs from the portion of their bills that fund the operational costs of ESC, keeping the design consistent with the Contracts for Difference (CfD) Exemption



Scheme mechanism. Although there will be an operational cost to introducing the mechanism itself, the preferred option is to exempt EILs from both the charges and levies imposed from the CM and rebalance these costs across non-eligible users. Ongoing delivery costs will be minimal once the mechanism is in place as it will be largely automated.

## Rationale for intervention

21. The rationale for intervention is the risk of carbon leakage due to high electricity prices. For those energy intensive industries (EILs) 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.
22. Carbon leakage is the displacement of domestic production, and its associated emissions, due to different levels of carbon pricing and climate regulations across jurisdictions.
23. 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.
24. 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 EILs

25. UK industrial electricity costs have been historically higher than comparable neighbouring countries and our EILs are unable to remain competitive without intervention. Three main components contribute to electricity prices for EILs: 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.<sup>1</sup>
26. Prices are made up of the following components:
  - Wholesale prices – the cost of electricity generation on wholesale markets, including the carbon costs of generating electricity from fossil fuels.

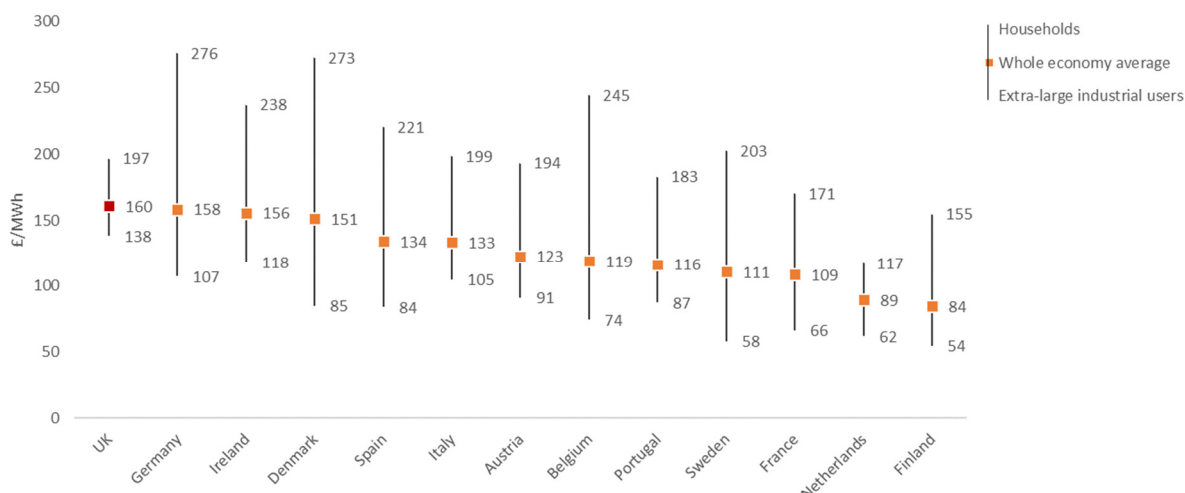
---

<sup>1</sup> 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.

- 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.
- 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.

27. 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 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

2

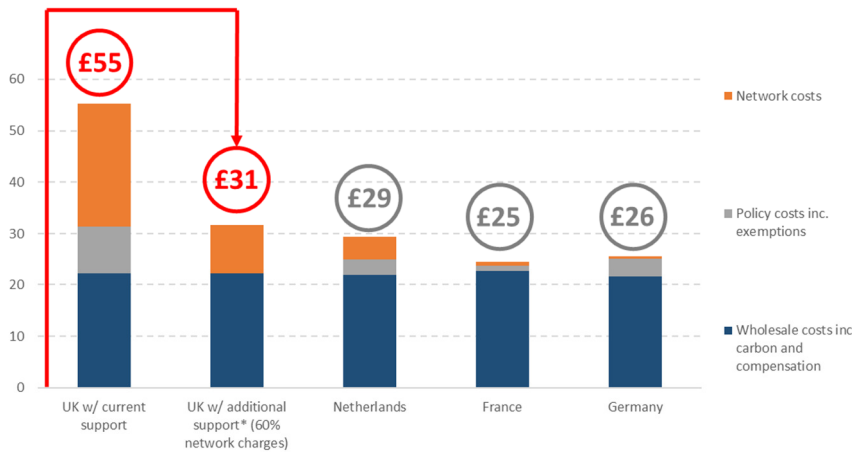
28. UK electricity wholesale prices have historically been higher than for main competitors, thus contributing to high retail prices. Despite this, figure 1 shows in 2021 UK household electricity prices were around average across EU countries, whereas among very large industrial consumers, UK prices 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.

29. The UK does offer relief for some energy intensive businesses such as the ETS/CPS Compensation and RO/ FiT/ CfD Exemption schemes. The ETS/CPS Compensation Scheme was increased in April 2022 and is estimated to compensate around 70% of indirect carbon costs for eligible EILs, whereas the Exemption Scheme exempts eligible EILs from 85% of RO, FiT and CfD costs.

<sup>2</sup> 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>

30. 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 EILs 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 EILs, for the businesses eligible for both schemes, and those eligible for just exemptions. It also shows the estimated impact of the Supercharger proposals.

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



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

Note – Figure 2 uses 2020 data as that is the latest available data for the network and policy costs international comparison and is the latest wholesale price data before the extreme volatility in prices seen since the reopening of economies post-COVID and the Russia/ Ukraine war. However, so that £ amounts can be compared to other analysis in this document, the prices have been adjusted to 2022 levels.

31. In 2020, the EILs receiving support from both the ETS/CPS Compensation and the renewables Exemption schemes paid more for electricity than French, German or Dutch EILs. In GB they paid £55/MWh compared to £25/MWh for France, £26/MWh for Germany, and £29/MWh for the Netherlands. EILs who receive support only from the EIL Exemption Scheme paid on average c. £40/MWh more for electricity than fully supported German or French firms. It is important to note that different firms will be eligible for different support in other countries, so comparing exempted-only domestic firms with fully supported firms in Germany may not be a fair comparison.
32. Wholesale cost gaps will fluctuate year-to-year depending on fuel and carbon prices, but in 2020 firms that received compensation had a wholesale cost gap at around £2-3/MWh with Germany and France. For EIL firms who only benefit from exemptions, the wholesale cost gap was c. £16-17/MWh, representing roughly a third of their total gap with Germany and France. Firms in the Netherlands, France and Germany are assumed to receive compensation for carbon costs.
33. For both groups of EILs receiving support, network costs make up c. £23/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 two thirds of the gap for firms that receive compensation and around half 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 GB 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 GB exemptions are funded through other consumers.

## Impact of the price gap on carbon leakage

34. 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.
35. 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 EII exemption scheme 2022 consultation – seen below.
36. The relevant literature highlights a relationship between where EII firms decide to locate, and areas of low environmental regulation and electricity costs. Khan and Mansur (2013)<sup>3</sup> 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.
37. Sato and Dechezleprêtre (2015)<sup>4</sup> 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.
38. Multinational corporations were found to have a marginally higher electricity elasticity of demand for employment (Dechezleprêtre, Lovo, Martin, and Sato (2016))<sup>5</sup>, 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.
39. Bijmans et al (2021)<sup>6</sup> concerned electricity elasticity of demand for investment. This ECB paper found that investment was relatively elastic in response to a change in electricity

---

<sup>3</sup> Kahn and Mansur (2013) "Do local energy prices and regulation affect the geographic concentration of employment," *Journal of Public Economics* 101, 105-114.

<sup>4</sup> Sato and Dechezleprêtre "Asymmetric industrial energy prices and international trade", *Energy Economics* 51,1, 130-141. (2015)

<sup>5</sup> Dechezleprêtre, Lovo, Martin and Sato (2016) "Does climate change policy pose a risk to competitiveness: Global firm-level evidence," LSE Grantham Institute.

<sup>6</sup> Bijmans, 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.

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**

40. 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.
41. Some firms cited reduced export demand and increased import demand as an indication of a loss of UK productive capacity such as Flour milling.
42. 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%.
43. 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.

### **Section 2 - Rationale and evidence to justify the level of analysis used in the IA (proportionality approach)**

44. The analysis in this Impact Assessment is considered to be proportionate. The monetised costs and benefits represent our best understanding of the impacts of both the Supercharger package and the individual CM Exemption. A number of sensitivities have been conducted to address the inherent uncertainty in forecasting electricity prices and the productivity and investment impacts resulting from the lower electricity prices for eligible EIIs that have been estimated.
45. The Supercharger and its policies are transfers that redistribute policy and network costs on electricity from eligible EIIs to other electricity users. Therefore, as per the Treasury Green Book there are deemed to be no fiscal costs and so the increased electricity costs for non-eligible businesses and households are not considered in the Value for Money assessment. In terms of the benefits, only the productivity and investment impacts

resulting from the reduced electricity prices eligible EILs face are considered, not the reduced electricity prices themselves.

### Section 3 - Description of options considered

46. **Do nothing** – A do nothing approach would lead to GB EILs continuing to suffer the burden of high electricity prices, coupled with high policy costs which government has historically failed to shield EILs from. GB electricity prices would continue to be higher than European counterparts and the result of not acting to support these core sectors could lead to the risk of closure due to reduced liquidity as a result of inability to compete internationally. EILs may risk significant job losses and increased reliance on import markets which may mean that GB sources goods from countries with less stringent climate policies, leading to carbon leakage and contributing to higher global emissions.
47. **Compensation scheme** – A compensation model was not deemed to be appropriate as, given previous experience with the EIL Compensation Scheme, this requires significant resource and management and is more likely to result in over and under-payments. Use of this kind of model would require additional administrative burden for Government, including assessment, reconciliation and clawback mechanisms in place.
48. **Part exemption** – We explored the option of exempting EILs from a proportion of Capacity Market costs, rather than the full 100%, however, suppliers and the Settlement Body were of the view that this would create unnecessary administrative burden and would require the design of a new complicated mechanism to calculate. This could also result in over or under-exemptions in the case of incorrect calculations and would therefore also require clawback mechanisms in place for suppliers and/or the Settlement Body. Incorrect payments to the Capacity Market could arguably impact the running of the Capacity Market itself and have a knock-on effect on security of supply, so the preference from all is to keep the exemption as simple and straightforward as possible.
49. **Private grants and loans** – We explored the option of grants, but the exemption provides for a real time benefit to eligible EILs and is less likely than a grant approach to lead to a situation where subsidy must be clawed back. A grant or loan approach would not necessarily achieve the desired outcome of helping reduce electricity costs and thus reduce the risk of carbon leakage as it would not be a specific policy cost in the same way as the exemption from the Capacity Market will be.

### Section 4 - Policy objective

50. The policy objective of the full British Industry Supercharger (BIS) package is to support the most electricity intensive industries with the high cost of electricity. These businesses are disproportionately impacted by high electricity prices due to the volume of consumption and their inability to pass on costs to their consumers, as they operate within highly internationally traded sectors. International competitors face lower electricity costs than their GB equivalents, e.g., because they operate in jurisdictions with less stringent environmental regulations, most notably in countries outside of the EU, leading to lower associated policy costs, or because they benefit from more generous subsidies for these costs than are offered in GB.
51. These two factors put GB EILs at an international competitive disadvantage and without intervention could lead to carbon leakage, hinder decarbonisation ambitions, and lead to disinvestment and subsequent job losses in key strategic sectors.
52. The intended outcome of providing support is to:

- a. Exempt particular EILs from certain policy costs associated with the Contracts for Difference, Renewable Obligations and Feed-In Tariff schemes, the Capacity Market and some costs associated with use of the electricity grid;
- b. Mitigate the risk of carbon leakage;
- c. Mitigate the risk of disinvestment and protect jobs in key industries; and
- d. Encourage decarbonisation and electrification longer term by lowering electricity costs.

53. We have identified that a reduction of around £24MW/h is expected to meet the needs of industry and supports the intended outcomes set out above, without seeking to undercut our nearest neighbours, given the interconnected nature of the energy systems across GB and Europe. This should be achieved from April 2024 onwards and the total saving should be reflected by 2025.

### **Indicators of success for the Capacity Market exemption**

54. We have identified that exempting eligible EILs from 100% of CM charges passed to them by electricity suppliers would reduce electricity costs by c.£5MW/h from October 2024 when we propose the measure should be implemented from.

55. A successful indicator for the policy will be EILs not paying any of the costs associated with the Capacity Market.

### **Section 5 - Summary and preferred option with description of implementation plan**

56. The preferred option will be given effect via secondary legislation to implement the CM lever under the Energy Act 2013. Amendments will be required to the Electricity Capacity (Supplier Payment) Regulations 2014/3354 and will:

- a. Adjust the way in which relevant supplier charges are calculated;
- b. Provide the means for the SoS to request information from the Settlement Body;
- c. Provide the means for the Settlement Body to require information from the CfD counterparty relating to supplier data;
- d. Provide the means to the Settlement Body to correct errors in payments for reconciliation purposes;
- e. Provide the mechanism by which the Settlement Body will deduct EIL data in relevant calculations to work out what suppliers must pay to fund the Capacity Market and costs of the Settlement Body; and
- f. Provide the means for DBT to share information with the Settlement Body.

57. Various formula changes are required in the Regulations to amend definitions found in calculations describing how costs of the CM are paid for. Full details of formula changes are outlined in policy instructions.

58. We propose to lay the Statutory Instrument by April 2024. If we take these measures forward, we anticipate implementation from July 2024 which would mean that the exemption would be in place from the beginning of the CM Delivery Year on 1 October 2024. The reason for having the SI laid by April 2024 is to show impetus and ensure the regulation is in place in good time. Having the mechanism ready by July will allow the Settlement Body, EILs and suppliers sufficient time to have provisions in place ahead of the beginning of the Delivery Year.

59. The Settlement Body will be responsible for overall management and administration of the scheme, which will largely be automatic once the mechanism is in place. This should

require minimal administrative burden once implemented, and therefore additional resource will not be required from their perspective and can be managed as business-as-usual. DBT will be responsible for issuing certification and assessing eligibility, which can also be managed as part of business-as-usual processes.

## Section 6 - Monetised and non-monetised costs and benefits of each option

60. This section covers the Value for Money analysis of the preferred option. The Capacity Market Exemption is one of three parts of the British Industry Supercharger package and is not intended to be implemented in isolation. Therefore, we will show both the overall Value for Money of the Supercharger as well as that of the individual Capacity Market Exemption.

61. The Supercharger value for money analysis assesses the combined costs and benefits of the three parts of the Supercharger package. The assumptions, methodology and types of costs and benefits also apply to the Capacity Market Exemption, with the only difference being the scale of costs and benefits.

### Value for Money analysis

62. The total annual value of the British Industry Supercharger Package to eligible businesses is expected to be between £320 mil - £410 mil. The expected total annual electricity consumption compensated in 2025 is 13.4TWhs and is based on actual consumption of the eligible cohort from 2022/23.

63. We estimate that in the central scenario the NPV and BCR of the Supercharger Package to be £9.4 billion and 7.7 respectively.

64. The individual annual value of the Capacity Market Exemption scheme is expected to be c. £65m. We estimate that in the central scenario, the NPV and BCR of the Capacity Market Exemption scheme in isolation to be £1.7 billion and 7.9 respectively.

**Table 1. NPV and BCR estimates**

	<b>Central</b>	<b>Low</b>	<b>High</b>
<b>Capacity Market Exemption NPV</b>	£1.7bn	£0.5bn	£4.0bn
<b>Capacity Market Exemption BCR</b>	7.9	8.9	7.6
<b>Supercharger NPV</b>	£9.4bn	£3.3bn	£24.0bn
<b>Supercharger BCR</b>	7.7	8.2	7.3

### Choice of counterfactual

65. We assume the benefits and costs are realised against a baseline scenario (in which the current level of support continues), where in the absence of the increased compensation/exemption the costs and benefits outlined below would be 0. In this counterfactual scenario, GB based EIs would face a greater risk of carbon leakage as they would continue to be exposed to the competitive disadvantage of the higher GB industrial electricity price caused by higher GB policy and network charges costs. As



such production, and therefore GVA, would decrease relative to the scenario of the introduction of the Supercharger Package and some firms would face increased risk of closure due to persistently higher GB electricity costs and therefore will struggle to be able to compete internationally.

66. In the central scenario, in the years that the Supercharger Package is in effect, eligible businesses will increase production relative to a baseline scenario without the Supercharger Package – generating GVA benefits and increasing the profitability of GB ELLs. However, this additional production will incur air quality and emission costs.

## Modelling Assumptions

67. The scenarios are modelled across central, high and low scenarios and assume annual compensation payment through the whole 10-year appraisal length beginning in 2025, with the benefits and costs of additional production and the increased profitability of GB ELLs incurred over the 10-year period. Sensitivity analysis has been carried out across key assumptions to reflect the inherent uncertainty in forecast modelling and the ranges of values brought out by evidence sources.

68. We have looked at a range of fossil fuel price scenarios for each of the high, central and low scenarios and have used the appropriate fuel price estimate to give the lowest and highest NPVs for the low and central scenarios respectively.

**Table 2. Modelling Assumptions**

Assumption	Central	Low	High
Production Elasticity	-0.41	-0.21	-0.86
Fossil fuel price scenario	Central	Very High	Low
Investment level	£957 mil	£957 mil	£957 mil
Investment Multiplier	0.33	0.503	0.257
Employment elasticity	0.0631	0.0162	0.243
% of eligible firms at risk of closure	6.4%	6.4%	6.4%
% of at risk firms saved	50%	0%	100%
<b>Capacity Market Exemption NPV</b>	<b>£1.7bn</b>	<b>£0.5bn</b>	<b>£4.0bn</b>
<b>Capacity Market Exemption BCR</b>	<b>7.9</b>	<b>8.9</b>	<b>7.6</b>
<b>Supercharger NPV</b>	<b>£9.4bn</b>	<b>£3.3bn</b>	<b>£24.0bn</b>
<b>Supercharger BCR</b>	<b>7.7</b>	<b>8.2</b>	<b>7.3</b>

69. An optimism bias of 10% is applied to all benefits in line with Green Book guidance regarding capital expenditures. The above scenarios are all appraised over a 10-year appraisal period, in 2025 prices. Overall additionality is subject to the sensitivity scenarios for each benefit strand, including the elasticities and deadweight applied.

## Benefits summary

70. The main benefits derived from the reduction in electricity prices for eligible firms are increased production, avoidance of firm closure and increased investment. We have split the benefits due to increases to production into increased profit and high employment in eligible firms, these benefits in the central scenario total £9.5 billion over 10 years for the whole Supercharger package. Our central estimate for total benefits over the 10-year period for the whole Supercharger package is £10.9 billion.

**Table 3. Monetised Benefits Summary – whole Supercharger package (2025 Present Values, 10-year appraisal period)**

PV 2025	Central	Low	High
<b>Benefits</b>			
Profit (domestic)	£3,815 mil	£1,243 mil	£10,121 mil
Employment	£5,655 mil	£1,843 mil	£15,001 mil
Avoid firm closure	£96 mil	£0	£196 mil
Investment	£1,286 mil	£649 mil	£2,525 mil
<b>Total benefits</b>	£10,853 mil	£3,735 mil	£27,842 mil

71. Our central estimate for total benefits for the Capacity Market Exemption scheme over the 10-year appraisal period in isolation is £1.9bn.

**Table 4. Monetised Benefits Summary – Capacity Market Exemption only (2025 Present Values, 10-year appraisal period)**

PV 2025	Central	Low	High
<b>Benefits</b>			
Profit (domestic)	£683 mil	£196 mil	£1,670 mil
Employment	£1,013 mil	£290 mil	£2,476 mil
Avoid firm closure	£16 mil	£0	£31 mil
Investment	£211 mil	£102 mil	£417 mil
<b>Total benefits</b>	£1,923 mil	£588 mil	£4,594 mil

## Production Increase

72. The Supercharger Package reduces the electricity price that recipient firms face, via exemptions from policy costs and compensation on a portion of the network charges. The fall in electricity price translates into a rise in firm electricity consumption (a movement along the demand curve), compared to what otherwise would have been in a counterfactual scenario, through a price elasticity of demand. The central case elasticity is  $-0.41$  with range  $-0.21$  to  $-0.86$ . This is based on an internal literature review of estimates of the price elasticity of demand for industrial electricity, which includes papers looking at relevant sector-level estimates.

73. The choice of low, central and high estimates is based on sector-level estimates from two key papers. The sectors that receive the most value from the Supercharger Package are chemicals, paper and pulp and metals (iron and steel as well as other metals). The following table shows sector-specific estimates from the two key papers mentioned above:

**Table 5. Production Elasticities used**

Authors	Chemicals	Metals	Paper and Pulp <sup>7</sup>	Unweighted Average	Weighted Average <sup>8</sup>
Agnolucci et al. (2017)	-0.32	-0.52 (Non-ferrous only)	-0.34	-0.39	-0.41
Steinbuks and Neuhoff (2014)	-0.21 <sup>9</sup>	-0.86 <sup>10</sup>	-0.54	-0.69	-0.56

74. The rise in electricity consumption is scaled up to a rise in gross value added (GVA) according to a GVA-MWh ratio. This ratio is developed using electricity consumption data obtained from recipients of the existing exemption scheme. The additional GVA is decomposed into profit and wage components using a profit-to-wage ratio. This ratio is based on FAME data for firms in the EII Exemption scheme, using this assumption gives 58% of GVA attributed to profit and 42% for wages.

### Production Increase – profit

75. For profits, multinational profits are again assumed to be transferred out of GB while domestic profits are fully retained within GB. The split is made according to the location of the global ultimate owner (GUO) of the firm. Using FAME<sup>11</sup> data for the location of the GUO of firms in the ETS/CPS compensation scheme, 25% of firms are classified as domestic and the remaining firms as multinational.

76. For domestic firms we assume that the profit remains in GB and is not subject to being transferred abroad, while for multinational firms we assume the profit is transferred abroad. This is in line with guidance from the Green Book, which states that ‘the relevant costs and benefits (to appraisal) are those to UK society overall’.

### Production Increase - employment benefits

77. The increase in GVA derived from the increase in production leads to increased employment in eligible businesses<sup>12</sup>. There is an associated wage premium of 38.5%<sup>13</sup>

<sup>7</sup> Includes publishing in both papers

<sup>8</sup> Weights are based on the fractions of EII exemption scheme support that goes to each of these sectors, excluding the 1% of compensation that goes to ‘other’ sectors. The weights used to calculate the weighted average are: chemicals 33%, paper and pulp 25%, metals 42%.

<sup>9</sup> Refers to chemicals, rubber, plastics and fuel products.

<sup>10</sup> Refers to basic metals and fabricated metal products.

<sup>11</sup> [FAME, Bureau Van Dijk database](#) - FAME collates data provided by companies in filings with Companies House

<sup>12</sup> We assume that 42% of the increase in GVA will be spent on wages, this ratio is based on FAME data for firms in the EII exemption scheme.

<sup>13</sup> Source

associated with jobs in these sectors, giving a societal benefit for the new hours worked in these businesses.

78. In the central scenario for the whole Supercharger package, this benefit is worth around £5.7 billion over the 10 years in additional wages due to the reduction in electricity price through the exemption provided.

79. In the central scenario for the Capacity Market Exemption in isolation, this benefit is worth around £1 billion over the 10-year appraisal period.

## Investment Benefits

80. This benefit measures the impact on investment from reducing the electricity price for eligible firms. An elasticity has been calculated using regression analysis from a European Central Bank working paper<sup>14</sup> analysing how changes in electricity prices affect investment.

81. The paper finds that there is a negative elasticity of between -0.2 and -0.5. This implies that a 10% fall in electricity prices increases next year's investment by 2% to 5%. The model calculates the average electricity price impact of applying the Supercharger Package in each year. This is then combined with the elasticity from the ECB paper. We adjust the elasticities for our sensitivity analysis to account for the range provided in the paper and the wage and fixed asset factors they considered when running their analysis.

82. The output of the change in electricity price and elasticity is then multiplied by the existing domestic investment across the firms on the scheme. This has been sourced using ABS average for 2016-2018 data for investment in fixed and current assets.

83. In the central scenario for the whole Supercharger package, this benefit is worth £1.3 billion over the 10 years in additional investment due to the reduction in electricity price through the exemption provided.

84. In the central scenario for the Capacity Market Exemption in isolation, this benefit is worth c. £200m over the 10-year appraisal period.

## Benefits from Preventing Firm Closure

85. Based on ONS business demography 2021 data we can see that there was around a 6% death rate of businesses in eligible sectors, we assume that a portion of these businesses would avoid closure with the additional support of the Supercharger Package and that workers in businesses facing closure are displaced and wages follow a lower path than if the business avoided closure. This lower wage path is based on 'The Losses of Displaced Workers' BEIS paper<sup>15</sup>. Therefore, a benefit of the scheme is that it keeps some firms open and prevents large wage losses for displaced workers. The table below gives the implied percentage difference in wages under a firm closure scenario relative to the scenario where the firm remains open.

---

<sup>14</sup> Bijmans et. al (2021), [The interplay between green policy, electricity prices, financial constraints and jobs](https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2537~002be51914.en.pdf). Working Paper Series No 2537. Available online at: <https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2537~002be51914.en.pdf>

<sup>15</sup> Page 97, BEIS Research Paper Number 6, 'The Losses of Displaced Workers', March 2017, prepared by Frontier Economics.

**Table 6. Annual wage loss due to firm closure**

Years after firm closure	1	2	3	4	5	6
% Difference in wages under firm closure scenario relative to open firm scenario	-52.2%	-27.9%	-23.7%	-9.2%	-7.2%	-7.2%

86. We assume that on a yearly basis there are around 6% of eligible businesses at risk of closure based on ONS business demography 2021 data. In our high scenario we assume that all of the businesses that are at risk of closure would avoid closure. In our central scenario and low scenario, we assume half and none of the at-risk businesses avoid closure due to the impact of the Supercharger Package.

87. Using FAME data we look at the level of employment spending in eligible businesses and apply the displaced worker wage discount rate to the portion of businesses that avoided closure. This gives us the estimated loss of total wages that would be avoided as a benefit.

88. We are aware of GB sites that have closed whilst being supported by existing schemes. While it is difficult to prove that high electricity prices caused these sites to close, these closures do provide some evidence of the risk faced by these companies from carbon leakage due to higher electricity prices.

### **Carbon Leakage**

89. Avoidance of carbon leakage is a potentially large portion of benefits which are too difficult to quantify in a meaningful way, as it is impossible to separate the impact of higher electricity prices from other factors that have also caused a decline over time in the domestic demand for products domestically produced from eligible sectors.

90. As the purchasing of equipment used by the sectors supported by the Supercharger Package are a substantial portion of their costs, and due to the long-lived nature of this equipment (over 10 years in many cases) we expect that the riskiest time for carbon leakage to occur would be when old equipment would need replacing. We assume that without the reduced electricity prices more firms would choose to relocate but we don't have the required data to forecast when these major investments to replace equipment would happen and therefore we cannot quantify the impact of this specifically.

### **Costs summary**

91. The main costs derived from the reduction in electricity prices for eligible firms are air quality impacts and increased emission due to increased production. Due to the proportionally small cost impact to households and ineligible businesses, we assume there is no behavioural change from this policy and thus no associated cost impact from behavioural changes.

92. Our central estimate for total costs for the whole Supercharger package over the 10-year period is c. £1.4 billion.

**Table 7. Monetised Costs summary – whole Supercharger package (2025 Present Values, 10-year appraisal period)**

PV 2025	Central	Low	High
<b>Costs</b>			
Additional Air quality impacts	-£72 mil	-£24 mil	-£186 mil
Additional emissions	-£1,342 mil	-£429 mil	-£3,616 mil
<b>Total costs</b>	-£1,414 mil	-£453 mil	-£3,802 mil

93. Our central estimate for total costs for the Capacity Market Exemption in isolation over the 10-year period is c. £230 million.

**Table 8. Monetised Costs summary – Capacity Market Exemption only (2025 Present Values, 10-year appraisal period)**

PV 2025	Central	Low	High
<b>Costs</b>			
Additional Air quality impacts	-£13 mil	-£4 mil	-£31 mil
Additional emissions	-£230 mil	-£62 mil	-£571 mil
<b>Total costs</b>	-£243 mil	-£66 mil	-£603 mil

### Transfer of energy costs

94. The Supercharger package is a transfer of electricity costs from eligible consumers to ineligible consumers. This means that, in line with Green Book guidance, there is no cost associated with the funding of the reduction in electricity costs given to the eligible cohort.

95. The estimated total value of reduced electricity prices by eligible firms borne by all non-eligible users in 2025 is estimated to be between £320 mil - £410 mil and around £5.1 billion over the ten financial years.

96. These costs, when spread out across ineligible electricity consumption, are estimated to cost the average household £4-£5 per annum and £1-1.5/MWh for ineligible businesses in 2025. Given that electricity prices have been and are expected to be over £100 /MWh, this translates to less than a 1% increase to ineligible businesses' electricity costs. We do not expect these costs to be substantive enough to impact household or ineligible businesses' behaviour, and therefore do not attribute any indirect cost from a change in behaviour due to this transfer.

97. A sensitivity to show what the Value for Money of the Supercharger would be if the bill impacts were not funded through a transfer has been carried out. This sensitivity suggests that the BCR of the scheme would be between 0.8 and 3.4, with a central BCR of 1.9 and an NPV of between -£0.7 to £19.7 billion with a central estimate of £5.1 billion.

**Table 9. Summary of energy bills impacts of Supercharger policies**

2025	Total cost (£m)	Annual Household bill increase (£)	Price increase for non-eligible consumers (£/MWh)	Discount to eligible EIs (£/MWh)
100% Exemption	64 - 88	0.8 - 1.1	0.2 - 0.3	5 - 7
100% Capacity Market reduction	65	0.8	0.2	5
60% reduction in network charges	191 - 259	2.4 - 3.2	0.7 - 1	14 - 19
<b>Total</b>	320 - 412	4 - 5	1.1 - 1.5	24 - 31

## Air Quality Impacts

98. Increasing production is associated with air damage costs compared to what otherwise would have been the case. The model uses £/MWh costs from Defra’s Air Quality Impact calculator<sup>16</sup> to convert the electricity consumption in MWh into air quality damage costs in £.

99. In the central scenario the additional electricity consumed over the 10 years is around 40 TWh and the cost of air damage from additional production averages at around £2/MWh per annum over the ten financial years. Therefore, the total cost of air damage is £82 million.

100. Similarly increasing electricity consumption leads correspondingly to higher emissions of greenhouse gases. The model uses a £/MWh emissions factor to convert the change in electricity consumption due to reduced electricity prices into a greenhouse gas cost which averages at £32/MWh over the 10-year period. This approach is based on Green Book supplementary guidance for the valuation of greenhouse gas emissions for appraisal<sup>17</sup>.

101. In the central scenario the additional electricity consumed over the 10 years is around 40 TWh and the corresponding cost of emissions from electricity consumption over the 10 year period averages at around £32/MWh. Therefore, the total GHG costs from additional electricity consumption estimated from the whole Supercharger package is £1,342 million. The individual impact of the Capacity Market Exemption is estimated at £230 million.

## Administration/ Familiarisation Impacts

102. There are also administration and familiarisation costs faced by eligible businesses and the administrator of the policies within the Supercharger package.

103. The EII Exemption Scheme Extension and the Capacity Market Exemption are likely to have no or minimal administrative burdens on businesses. This is due to the existing EII Exemption scheme already having the administrative processes in place that are needed for these schemes.

<sup>16</sup> Defra’s air quality guidance is available at: <https://www.gov.uk/government/publications/assess-the-impact-of-air-quality>

<sup>17</sup> <https://www.gov.uk/government/publications/valuation-of-energy-use-and-greenhouse-gas-emissions-for-appraisal>

104. Therefore, most of the administration and familiarisation costs are likely to be from the Network Charges Compensation scheme.

105. There will be a small familiarisation cost and continuous administrative burden on the EIs eligible for network charges compensation. Under the proposed policy design, eligible EIs will be required to submit data from their electricity bills to the scheme administrator on a quarterly basis to receive compensation from network charging costs. For some firms, this will mean compiling data from bills from multiple sites.

106. In our consultation on the Network Charging Compensation scheme<sup>18</sup> we provided an estimate for the administration costs across all eligible EIs of £26,000 per year. This assumes that a worker in an administrative occupation would spend 1 hour per-quarter to collate and share their electricity bills with the scheme administrator.

**Table 10 – Estimated administrative burden costs on EIs receiving Network Charging Compensation**

Hourly pay of administrative occupations in manufacturing sector	£13.41
Time taken to collate and submit electricity bills to administrator	1.5 hours
Annual frequency of submissions	4
Annual administrative cost to an eligible EI	£80.46
<b>Annual cost to 320 eligible EIs</b>	<b>£26,000</b>

107. We also provided a one-time familiarisation cost of £12,000 to EIs. Familiarisation costs entail the time taken for a senior official in the eligible EI to read and comprehend the legislation.

**Table 11 – Estimated familiarisation cost for EIs receiving Network Charging Compensation**

Hourly pay of management occupations in manufacturing sector	£24.85
Time taken for manager to review and comprehend the legislation	1.5 hours
Familiarisation cost to an eligible EI	£37.28
<b>Familiarisation cost to 320 eligible EIs</b>	<b>£12,000</b>

108. The administrator of the Network Charges Compensation scheme will also face administration costs that may be passed on to consumers. We are currently in discussions with the potential scheme administrator on what these costs may be. Given the scale of the benefits from the Supercharger, the administration costs would have to be in the tens of millions of pounds per year to have even a minor impact on the Value for Money of the scheme.

109. Low and high sensitivities of 50% and 150% of the central estimates have been provided to reflect uncertainty in the central estimates.

<sup>18</sup> Network Charges Compensation scheme consultation available at: [https://assets.publishing.service.gov.uk/media/64a590654dd8b3000c7fa521/consultation-on-the-proposed-network-charging-compensation-scheme-for-energy-intensive-industries-\\_ells.pdf](https://assets.publishing.service.gov.uk/media/64a590654dd8b3000c7fa521/consultation-on-the-proposed-network-charging-compensation-scheme-for-energy-intensive-industries-_ells.pdf)



110. For the combined Supercharger package these costs are estimated at £0.1m - £0.4m (2025 PV) over the 10-year appraisal period, with a central estimate of £0.3m.

**Table 12 – Administration and Familiarisation costs – combined Supercharger package. 10-year, 2025 Present Values**

Description	Low Estimate (£m)	Central Estimate (£m)	High Estimate (£m)
<b>Costs</b>			
Familiarisation costs to eligible EILs for Network Charges Compensation scheme	0.01	0.01	0.02
High-level Administration costs of Network Charges Compensation scheme for scheme administrator	Unknown at this stage but expected to be <£10m		
Annual admin burden for EILs to provide electricity info to electricity suppliers	0.1	0.3	0.4
<b>Total Administration and Familiarisation costs</b>	<b>0.1</b>	<b>0.3</b>	<b>0.4</b>

### Equivalent Annual Net Direct Cost to Business (EANDCB)

111. The direct costs to business from the Supercharger are the increased electricity bills for non-eligible businesses and the administrative and familiarisation costs for eligible businesses. The direct benefits to business are the lower electricity prices for eligible businesses.
112. As with the Value for Money assessment above, the direct electricity bills impacts are a transfer from non-eligible businesses and households to EILs. As such, they are not considered in the EANDCB calculation as the increased costs for those not eligible for the Supercharger would be cancelled out by the benefit of lower electricity prices for EILs.
113. Therefore, only the administration and familiarisation costs to businesses noted in Table 12 are considered in the EANDCB. The benefits to the wider economy from the increased production for EILs resulting from lower electricity prices are not direct benefits to EILs and so are not considered in the EANDCB calculation.
114. With a central estimate of administration and familiarisation costs to businesses of £0.3m over the 10 year appraisal period this leaves the EANDCB for the overall Supercharger package at £0.02m, subject to estimated administrator costs for the Network Charges Compensation Scheme.
115. As detailed above, there are expected to be minimal if any administration and familiarisation costs for the CM Exemption and therefore there is no EANDCB for this individual policy.

### Capacity Market Auction Impacts

116. The British Industry Supercharger is expected to result in increased production from eligible firms and therefore increased electricity demand. DESNZ have conducted analysis to assess potential impacts this may have on the clearing price of the CM auctions for both the year ahead auction and the four year ahead auction.

117. To reflect the uncertainty in estimating electricity demand increases resulting from the Supercharger, two demand increase scenarios were tested. A minimum impact scenario of a 0.08GW increase in peak electricity demand and a maximum impact scenario of a 0.24GW increase in peak electricity demand in 2026. These peak demand increases were then used to estimate changes in clearing prices on the auctions, compared to a baseline where the Supercharger does not come into effect and there is no increase in electricity demand.
118. Due to the low increase in peak demand, analysis suggests there would be no impact on clearing prices in the four years ahead auction, while the year ahead auction would see a potential increase of £10/kW from a clearing price of £60/kW to £70/kW in the maximum scenario.
119. This £10/kW increase in the maximum scenario of the year ahead auction could result in an additional £60m of costs as part of the CM auction which would be distributed across all non-Supercharger eligible customers. The gross impact on the average household bill would be less than an additional £1 per year.
120. Note that this analysis is highly uncertain as predicting the outcome of auctions comes with inherent uncertainty. This analysis is using the results from last two CM auctions with the estimated increased peak electricity demand from the Supercharger in place, not future auctions as we have limited capability to model future auctions. The future auctions can have different dynamics with differences in available capacity at different prices. Moreover, the Capacity Market auctions have tolerances up to 1.5 GW around the demand target to limit the market power of large units in the auction. As the maximum estimated impact of Supercharger on peak demand is well within these limits, the likely impact of the increased demand on the clearing price is small.

## Section 7 - Risks and assumptions

121. **Risks to Value for Money estimates:** Assumptions used to estimate monetised benefits and costs have been outlined in Section 6. The estimated benefits are based on a range of production elasticities taken from the literature on the relationship between reduced electricity prices and production.
122. High and low sensitivities have been presented alongside the central estimates of benefits and costs to mitigate the uncertainty present in these estimates.
123. **Risks to the costs faced by non-eligible consumers:** The eventual bill impact faced by non-eligible consumers will be dependent on the number of companies eligible for the Supercharger, and therefore the total volume of electricity consumption that is supported through the Supercharger. This volume is sensitive to numerous factors including future electricity price volatility, changes to GB's industrial make-up and HMG Net Zero policies.
124. For companies to be eligible for the Supercharger and therefore the CM exemption, 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.
125. **Risk to the running of the Capacity Market:** The CM funding mechanism was designed to incentivise demand reduction during peak periods, as a way to reduce peak

demand and manage the overall cost of the CM scheme. Exempting EIs could increase the cost of the CM given EIs will not be incentivised to reduce electricity usage. While there is a risk that the proposed EI exemption could increase electricity demand from EIs (seeing as electricity will not be as expensive), this should be minimal as CM charges alone are low and spread across a large time period (Winter peak). Additionally, given the CM Exemption is part of a wider package which incentivises electrification, CM charges by themselves are not sufficient to create substantial risk to the CM overall, and therefore security of supply. The cost saving and incentive to reduce shift demand for a prolonged period is likely to be of limited benefit, so unlikely to be taken up by EIs.

126. **Risk of suppliers not passing on the exemption:** This exemption will be paid for by suppliers who pay for the overall running of the CM and then recoup the costs from the energy users they supply, via their electricity bills. There is a potential delivery risk that suppliers do not pass on the savings to the eligible EIs, given the legislative mechanism we are proposing cannot impose direct obligations for them to do so. We have observed the current EI exemption scheme and, given this works well in practice without the need to force suppliers to pass on savings, we do not foresee any difficulty with running the CM exemption in a similar fashion. EIs are a well-informed, well-represented sector so if a supplier is shown not to pass on the full exemption to the EI then we would expect the EI to change supplier. Therefore, it is within the interest of suppliers to act in accordance with the guidance, which will largely be a simple process of recalculation. Supplier bodies have agreed with this rationale.

## Section 8 - Impact on small and micro businesses

127. The policy package will be paid for by contributions from all non-eligible electricity consumers (domestic and non-domestic) therefore small and micro businesses will be impacted.
128. 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 variance in energy consumption across businesses.
129. In total, the Supercharger is expected to put an additional c. £1-1.5/MWh on the electricity costs of non-eligible firms. Depending on the energy usage of these firms, the absolute cost will vary, however the relative increase on their electricity bills is expected to be below 1%.
130. In terms of energy usage, Ofgem define a microbusiness as one that uses less than 100,000kWh or 100MWh of electricity per year<sup>19</sup>. Based on this assumption, the annual cost of the Supercharger package to a non-eligible microbusiness's electricity bill would be at most £150.
131. Individually, the Capacity Market Exemption is estimated to add £0.2/MWh on the electricity costs of non-eligible businesses. Therefore, the individual impact to a non-eligible microbusiness is estimated to be c. £20 annually.
132. Eligible small and microbusinesses will benefit from the c. £24-31/MWh average reduction in electricity prices. It is estimated that based on the eligibility of the existing EI Exemption scheme, c. 8% of all support through the Supercharger package will go to small and micro businesses.

---

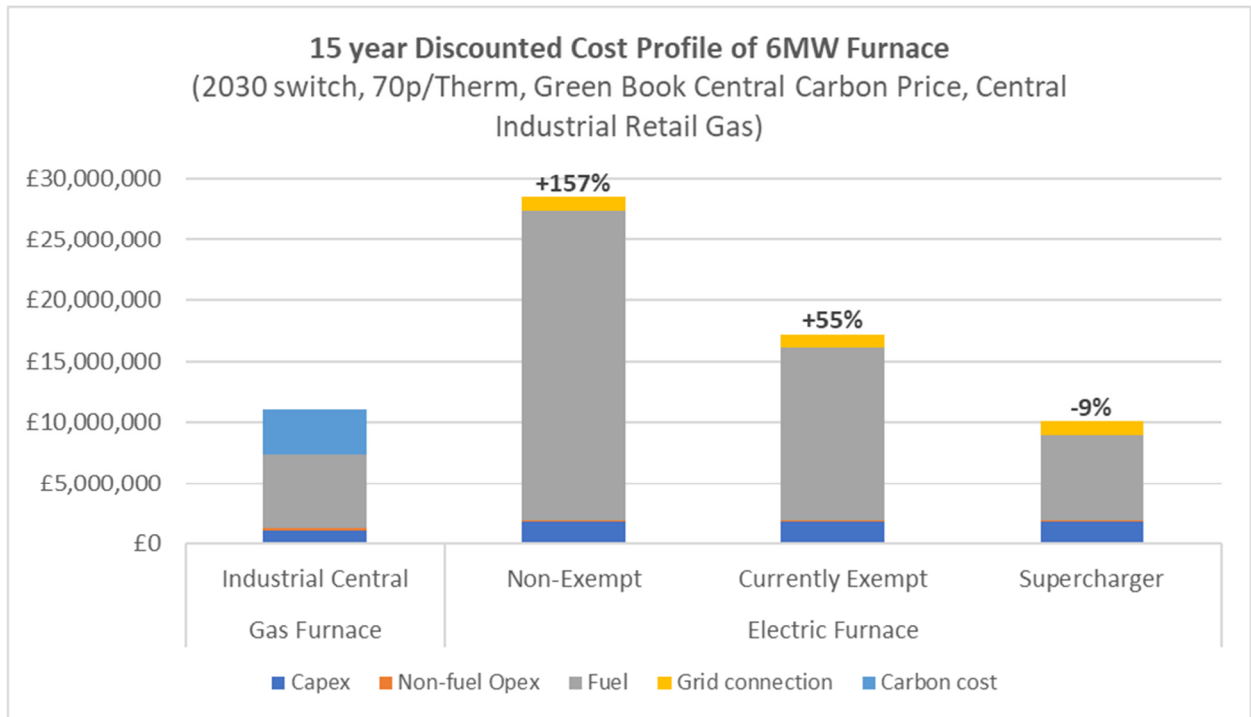
<sup>19</sup> <https://www.ofgem.gov.uk/information-consumers/energy-advice-businesses/guidance-microbusinesses>

## Section 9 - Wider impacts

### Technology switching impacts

133. Analysis suggests that the electricity price reduction from the Supercharger is sufficient to make it financially viable for Supercharger-eligible firms to switch from using industrial gas furnaces to electric furnaces, when also considering the costs of replacing these furnaces. This will help to encourage electrification among EIIIs where feasible and decrease carbon emissions.
134. One of the objectives of the Supercharger is to encourage decarbonisation for energy intensive firms through fuel switching away from fossil fuels to electricity by lowering electricity prices.
135. However, the cost of replacing fossil fuel reliant technologies with electric replacements (for example, replacing industrial gas fired furnaces for heat used in industrial processes with electric furnaces) is also a consideration when it comes to firms deciding if it is financially viable to fuel switch.
136. We have conducted analysis to show the Net Present Cost (NPC) of purchasing and operating an industrial natural gas fired furnace compared with an industrial electric powered furnace. To show the impact of the Supercharger we have considered the following electricity price scenarios:
- The full industrial retail electricity price with no policy cost exemptions drawn from Green Book Industrial retail price series.
  - The current EII Exemption scheme with an 85% exemption from RO/CfD/FIT costs and the current EII ETS/ CPS indirect cost Compensation scheme compensating for c. 86% of the indirect costs of the UK ETS and CPS
  - The proposed Supercharger scheme with the increase in RO/CfD/FIT exemption to 100%, Capacity Market exemption and Network Charges compensation and the current EII ETS/ CPS indirect cost Compensation scheme as above
137. Across the low, high and central scenarios, we have assumed firms have a furnace with a 2030 replacement date with the option of installing and using a 6MW gas furnace or a 6MW electric furnace over a 15-year appraisal period (2030-44). We have also assumed that firms will be fully exposed to the Central Green Book Carbon costs and will incur a £350/kW capacity grid connection cost for the electric furnace option. Electricity and gas price forecasts for exempt EIIIs have been created from the DESNZ Average Prices & Bills Model (APBM), while Green Book Industrial retail prices have been used for non-Exempt EII firms.
138. When comparing the discounted cost of purchasing and operating an industrial gas fired furnace with the discounted cost of an industrial electricity powered furnace, the analysis indicates that Supercharger-eligible firms are projected to have 9% lower costs if they use the electric powered furnace over the appraisal period.

**Figure 3 – 15-year Discounted Cost Profile of 6MW Furnace in the central scenario**



139. Firms that are eligible for the existing EII Exemption and Compensation Schemes would face a 55% higher discounted cost from switching to an electric furnace compared to replacing a natural gas furnace. A non-exempt firm using electricity would see their costs more than double (+157%).

140. This indicates that the electricity price reductions from the Supercharger could make it financially beneficial for firms eligible for the full range of EII support (Supercharger and indirect ETS/ CPS costs compensation scheme) to switch from gas furnaces to electric furnaces, thus encouraging decarbonisation.

141. Note that the ability for firms to fuel switch to electricity is also dependent on other factors such as the ability for firms to connect to the electricity grid and assuming that there are no exogenous shocks that will impact the forecasted gas and electricity prices within the model.

**Table 13 – Summary of projected net present cost impacts over a 15-year appraisal period**

Technology	Electricity price scenario	Central	Low	High
Discounted Cost				
Gas fired furnace	Costs are not dependent on the electricity price scenario	£11,100,000	£9,200,000	£13,300,000
Electricity powered furnace	Non-Exempt	£28,500,000	£28,200,000	£29,500,000
	Currently Exempt (EII Exemption and indirect ETS/ CPS Compensation)	£17,200,000	£16,200,000	£18,700,000
	Supercharger (incl. indirect ETS/ CPS Compensation)	£10,100,000	£9,200,000	£11,400,000
Net Present Cost differential (discounted electricity premium)				
Electric powered furnace (£)	Non-Exempt	£17,400,000 (+157%)	£19,000,000 (+207%)	£16,200,000 (+122%)

<b>minus</b> Gas fired furnace (£)	Currently Exempt (EII Exemption and indirect ETS/ CPS Compensation)	£6,100,000 <b>(+55%)</b>	£7,000,000 <b>(+77%)</b>	£5,500,000 <b>(+41%)</b>
	Supercharger (incl. indirect ETS/ CPS Compensation)	-£1,000,000 <b>(-9%)</b>	-£4,000 <b>(0%)</b>	-£1,900,000 <b>(-14%)</b>

Note: Net present cost (NPC) differs from actual cost difference. In Figure 3 NPC refers to the difference between the present value of costs (discounted cost) from installing and using an electric powered furnace instead of a gas fired furnace. To work out the present value of costs we have used a discount rate of 10% to mirror what might be used in the private sector.

## Public Sector Equality Duty Assessment

142. The Supercharger is expected to have impacts on electricity bills for all electricity consumers, lowering electricity bills for eligible businesses and slightly increasing bills for households by £4-5 per year and non-eligible businesses by c. £1-1.5/MWh. As a result, there may be some impacts on Protected Characteristic Groups (PCGs).
143. In terms of household impacts, the additional electricity bill costs faced by households are small at £4-5 per year. At this level of cost, the impacts on PCGs are minimal, with any potential impacts being greater for those PCGs with lower incomes.
144. As the schemes provide exemption and compensation to corporate entities, it is unlikely that the policy will directly affect individuals with “protected characteristics” (age, gender, race etc). Our equality analysis shows that people sharing some of the protected characteristics under the Equality Duty are less represented in energy intensive sectors.
145. If the Supercharger scheme has the effect of enabling the beneficiaries to employ more people who do not share the protected characteristics and fewer people who do share the protected characteristics, it could be argued that the policy is likely to perpetuate but not worsen some of the inequalities that the Equality Duty aims to reduce.

## Section 10 - A summary of the potential trade implications of measure

146. 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 EII by closing the electricity price-gap between GB and comparable countries. Electricity makes up a significant proportion of costs for EII so reducing electricity prices will make them more internationally competitive. EII will be able to better compete with imports from countries which already provide lower industrial electricity prices thus reducing imports.
147. The increased international competitiveness of EII from lower electricity prices could also increase exports.
148. 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.

## Section 11 - Monitoring and Evaluation

149. As part of the existing EII Exemption scheme, monitoring of the following variables already occurs through data provided by eligible businesses on an annual basis:
- Number of eligible businesses
  - Electricity usage
  - Electricity costs
  - Earnings Before Investment, Taxes and Deprecation (EBITDA)
  - Staff costs
150. The monitoring and data gathering of these variables will continue under the Supercharger. The monitoring of these variables will continue to provide the means to check continued eligibility for businesses as well as a view as to whether the Supercharger is supporting employment and production activity for eligible businesses.
151. In particular, monitoring of electricity usage, staff costs and EBITDA will allow us to monitor the impact of the Supercharger on the employment and production activity of eligible businesses.
152. In addition, the policy and network charges which the Supercharger impacts will also be monitored as well as the prices paid by eligible businesses to ensure that the exemptions offered by the Supercharger are being passed through to eligible businesses by their suppliers.
153. A review of eligibility for the Supercharger alongside a data refresh will be carried out in 2026. The monitoring and evaluation of the data collected from eligible firms will also be reviewed at this point.

## Annex A – Supercharger Bills Impacts Modelling

### How the £4-£5 annual household bill increase for households was calculated.

This note describes the calculation and the relevant inputs for the estimated £4-£5 increase in household bills following the introduction of the proposed EII policy support package. The estimate assumes that EII prices receive a 100% exemption from RO, FITs & CFDs (increased from 85%), a 100% exemption from capacity market charges, and a 60% reduction in Network charges from 2025. The ranges of estimates are created using different fossil fuel scenarios.

#### The calculation

- A) Volume of electricity consumption eligible for the Supercharger (MWH)
- B) Price discount for eligible EIIs (£/MWH)
- C) Total cost to be redistributed (£)

$$A * B = C$$

- D) Total volume of UK electricity consumption (MWH)
- E) Volume of non-eligible consumption (MWH)
- F) Price increase for non-eligible consumers (£/MWH)

$$D - A = E$$
$$\frac{C}{E} = F$$

- G) Average Dual Fuel<sup>20</sup> Household Consumption (MWH)
- H) Average increase to dual fuel household bills (£)**

$$F * G = H$$

H) Average increase to dual fuel household bills is the £4-£5 cost estimate that has been included in the Subsidy Control Assessment.

#### The inputs

- A) Volume of eligible consumption (MWH)

The volume of eligible consumption is based on the annual electricity consumption of the c.300 firms which are currently part of the EII Exemption Scheme. It is therefore assumed that the full package of EII support measures will be offered to the same group of exempt firms.

- B) Price discount for eligible EIIs. (£/MWH)

Four price scenarios are used for this analysis. All four are Net Zero Higher Electrification scenarios: they are consistent with Net Zero target by 2050, including the expected increase in demand as a result of EV and heat pump take up. They account for changes to prices as a result of Covid-19 and account for recent volatility in the gas market (up to Q2 2022), however the large amount of uncertainty around short-term gas prices makes these price projections more uncertain than those usually produced.

---

<sup>20</sup> Without a heat-pump or an electric vehicle



The difference between the four scenarios is assumptions around fossil fuel prices. NZH LFF assumes fossil fuel prices at around 45p/therm in 2030, NZH CFF is a 70p/therm in 2030, NZH HFF assumes ~95p/therm in 2030, and NZH VHFF assumes current very high prices remain high in future at 150p/therm.

Price estimates are inherently uncertain and influenced by several key factors including wholesale gas prices, carbon prices, the evolution of the generation mix, future policy decisions regarding who pays for the cost of decarbonisation and the way that consumers use energy. This uncertainty increases the further forward analysis looks, and prices are especially uncertain beyond the early 2030s.

The ex-BEIS Annual Prices and Bills Model breaks down the price paid by large exempt EIs into the wholesale cost, transmission cost, balancing cost, ETS cost, RO support cost, CFD support cost, capacity market support cost, and the feed in tariff cost. We applied the proposed policy options to the different cost components to work out the discount each MWh of EI consumption received.

- 1) Increasing the Exemption Scheme from 85% to 100%- Take the remaining RO, FITs, CFD costs off from the exempt EI price.
- 2) 100% exemption from capacity market charges- Take the entire capacity market charge component of the EI price.
- 3) 60% exemption from network charges- Take 60% of BSUs, TNUoS and DUoS costs off the EI price. This price was estimated via an evidence gathering exercise in the summer of 2023 which collected electricity bill data for April 2021, 2022 and 2023 from eligible EIs.

The sum of 1), 2) & 3) is the estimated £/MWh price discount for EIs following the delivery of the EI policy support package.

The size of the discount for EIs changes over time because the relevant policy costs are sensitive to the chosen fossil fuel price assumption.

The EI exemption scheme covers three renewables policies – Renewables Obligation (RO), Feed-in-tariffs (FITs), and Contracts for Difference (CfDs) – which are designed to incentivise the deployment of renewable generation. The EI exemption exempts companies from a proportion of these costs. The RO and FITs are legacy policies and the price of these does not change with fossil fuel scenarios. RO and FIT as legacy policies will start to decrease from the late 2020s to zero by the 2040s. For CfDs, when fossil fuel prices are low, the difference between the electricity wholesale price and the CfD strike price will be higher. Therefore, generators will receive higher payments, and the value of the exemption will therefore be higher when prices are low. The opposite is true for higher prices.

Capacity Market is a policy designed to ensure there is enough electricity generation capacity to ensure security of supply. Broadly speaking when prices are higher, there needs to be less incentive for suppliers to generate and less need for Capacity market payments. Therefore, capacity market exemption is lower when prices are high.

For network charges, higher fossil fuel prices incentivise renewable generation. More renewable generation on the grid might mean that there needs to be more investment in the networks to ensure the supply can reach its demand – e.g. more offshore wind means more networks are required.

- D) Total volume of UK electricity consumption (MWh)

Total electricity consumption comes from total electricity demand in the Dynamic Dispatch Model (DDM) and has been revised down slightly to estimate actual sales (accounting for distributional losses and theft). This consumption is consistent with the net zero higher electrification scenario, including the expected increase in demand as a result of EV and heat pump take up.

#### G) Average household consumption (MWH)

We assume that the average (mean) dual fuel household consumes around 3MWH of electricity in 2025. The average household consumption figures do not include the introduction of EVs and heat pumps. This ensures estimates are comparable with today's bills.

### **Risks - how the size of the household bill impact could change**

The estimate of the household bill impact of the EII policy support package is sensitive to the following factors:

- **Electricity prices and policy costs:** Price estimates are inherently uncertain and influenced by several key factors including wholesale gas prices, carbon prices, the evolution of the generation mix, future policy decisions regarding who pays for the cost of decarbonisation and the way that consumers use energy.
- **Volume risk:** The volume of EII electricity demand eligible for support is subject to change. An increase in the eligible volume will lead to an increase in the costs to households. DBT analysts have already accounted for proposed increases to steel and battery electricity demand, but there could be other increases that have not been accounted for. The DBT EII team is planning a review of sector level eligibility which may change the total volume of eligible electricity.
- **Household volume increase:** The household bill increase is based on an average estimate of a dual fuel household's electricity demand for 2025 without a heat-pump or EV. While the £/MWH price increase may not change, a household with larger electricity demand would face a larger increase in absolute terms.

## Annex B – Network Charges Costs Analysis

### Data gathering exercise for network charges.

What are network charges?

- The energy network are the gas pipes and electricity cables that carry energy across the country into homes and businesses.
- Network companies charge energy suppliers an Ofgem-regulated price for their use of the energy network. This money goes towards maintaining, running and upgrading the networks.

The main categories of network charges are Transmission Network Use of System charge (TNUoS), Balancing Services Use of System charge (BSUoS) and Distribution Use of Systems (DUoS):

- The TNUoS charge is paid to and set by the system operator and recovered on behalf of the transmission owners for the cost of building and maintaining the shared transmission network.
- The BSUoS charge is paid to the electricity system operator for the cost of balancing the system minute by minute. It pays for the skills, tools and services the system operator needs to balance supply and demand in real time.
- The DUoS charge covers the costs of the electricity distribution network. The DUoS charge is based on the amount of electricity consumed by a business. The DUoS charge covers the cost of maintaining the local electricity distribution network infrastructure including the cables, substations, poles, and transformers.

In the summer of 2023, we undertook an exercise to gather up to date data on network charges. The purpose of this project was to help remedy our evidence gap on how much exactly EII's were paying in network charges, as there had been several recent impactful reforms to how TNUoS and DUoS were charged since our last view on network costs.

In particular, following the introduction of Ofgem's Targeted Charge Reform (TCR), our previous method for estimating EII network charging costs was outdated and likely leading to an underestimate of the Supercharger costs.

In June 2023 we contacted the ~320 eligible for the EII exemption scheme requesting their April 2023 (and 2022, 2021) electricity bill information on network charges. We received just over 150 responses covering around 300 sites, accounting for ~70% of eligible exemption scheme electricity.

We found that network charges vary significantly across users, with the majority of sites facing costs between £24 - £52 per MWh. However, due to DUoS and TNUoS network charges now being charged largely as a standing charge determined by which band a site falls into (based on an average 24 months of consumption and voltage), the £/MWh for smaller electricity consumers was quite volatile.

To get an estimate of the £/MWh cost of supporting network charges, the collected data was weighted by electricity usage using exemption scheme eligible electricity usage data. We found that network charges for our cohort cost on average £24 -£31/MWh, which at a 60% compensation rate averages £14 - £19/MWh.

### **The calculation**

- A) Total network charges – TNUoS + DUoS + BSUoS
- B) Electricity usage on bill
- C) Proportion of eligible electricity the business was responsible for in 2022/23
- D) Weighted average of network charges in terms of £/MWh, for the eligible exemption scheme businesses.

$$Sum\left(\left(\frac{A}{B}\right) * C\right) = D$$

### **Risks and limitations**

Due to the recency of the TCR changes we could only collect information regarding businesses April 2023 bills. There were also some adjustments from suppliers during the first month of implementation of these changes, which was reflected in some bills. Ideally, we would have been able to collect several months of data which included the TCR changes but preferred to receive timely information and limit administrative burden for businesses.

These estimated costs are very specific to this cohort of businesses and should not be used to extrapolate to the wider economy.