

# Balance of Competences Review on Energy - Energy UK Response

15<sup>th</sup> January 2014

## Introduction

Energy UK is the Trade Association for the energy industry. Energy UK has over 80 companies as members that together cover the broad range of energy providers and suppliers and include companies of all sizes working in all forms of gas and electricity supply and energy networks. Energy UK members generate more than 90% of UK electricity, provide light and heat to some 26 million homes and invested over £11 billion in the British economy in 2012.

## Summary

In the current state of development of energy markets, Energy UK urges that there should be better clarity in the balance of energy competences, between that which is for the EU and that which is the responsibility of national Governments. Below, we set out what we consider to be the key points and key criteria for effective energy market decision making in future.

- ▶ EU decisions on energy should aim to set a framework and to avoid unnecessary prescription:
  - Member States should as far as possible be given flexibility in how to implement decisions taken at EU level.
  - Significant care is essential to ensure that national initiatives do not cut across or duplicate decisions taken at European level; EU decisions must fully take into account national priorities, specificities and economic pressures.
- ▶ All EU proposals and in particular any targets should be evidence-based and underpinned by a comprehensive regulatory impact assessment (RIA). This should involve a systematic assessment of costs, benefits and impacts on the sector and its customers, both from a stand-alone and from a cumulative perspective.
- ▶ All EU proposals should be considered through the lens of energy security, regional and international competitiveness and affordability to consumers; and the affordability of all proposals should be considered both on an individual and cumulative basis.

- ▶ Efforts should be made to reduce “red tape”, by minimising detailed prescription and devolving the responsibility for meeting the desired policy outcomes to national governments.
- ▶ Energy UK believes that climate change is best tackled at European level and that the EU should continue to push for an international agreement on greenhouse gases (GHGs).
- ▶ The EU cannot afford to “go it alone” on climate change and so it is all the more important that policy should be cost-effective and avoid damage to competitiveness both regional and international.
- ▶ Energy UK considers it essential that there should be a more holistic approach to energy policy from the Commission, with greater recognition of the interaction between environmental regulation and national energy policy.
- ▶ Energy UK takes the view that the primary responsibility for security of supply should remain with Member States and supports the maintenance of Art. 194.2 of the Treaty, allowing Member States flexibility to determine their own energy mix. As the European energy system becomes more integrated, there will be an increased rationale for cooperation and policy convergence within the EU on security of supply.
- ▶ Energy UK is not convinced of the need to set European energy efficiency targets or harmonise national policies on energy efficiency.
- ▶ Most Energy UK members do not see the need for binding EU renewable targets beyond 2020, but it is recognised that measures will be necessary to ensure continued development of renewables, particularly in relation to immature technologies.
- ▶ Additional efforts will be needed at EU and national level to drive innovation in energy technologies. Public support should focus on the research, development and demonstration of immature technologies rather than on bringing unproven or high cost technologies to market early and subsidising their operation.
- ▶ The single market agenda should recognise that EU climate and renewable policy may require governments to take specific measures to promote low-carbon energies and ensure security of supply, e.g. long-term contracts and capacity mechanisms. Such measures should be carefully designed to minimise market distortions. However, it is for national governments to decide how to achieve the necessary outcomes, within a broad framework set by the EU.
- ▶ A single European market benefits UK customers and the energy industry alike by promoting competition, providing access to a wider market and enhancing security of supply. These benefits are likely to increase as the market becomes more integrated and more physically interconnected.
- ▶ Further EU market integration would be desirable. However this cannot take place without fully integrating renewable energy effectively into wholesale markets.

- ▶ It is important that the EU Network Codes should tackle truly cross-border issues and strike a balance between ensuring a level playing field and prescribing requirements which could be dealt with at national level
- ▶ There should be a greater emphasis on enforcement of existing legislation, particularly on the single market, and EU measures should allow adequate time for national transposition
- ▶ Energy UK considers that the UK Government should avoid “goldplating” of EU legislation and should pay particular attention to costs and burdens on business when going beyond agreed EU policies.
- ▶ A key point for energy companies is that, at whatever level political decisions are taken, they should be clear and consistent, and provide for a stable long-term investment framework.

## General

Energy UK welcomes the opportunity to respond to this call for evidence on the balance of competences in energy. Although the Energy Chapter in the Treaty is relatively recent, EU policy and legislation has been having an increasing impact on the UK energy sector as a result of European single market and environmental initiatives. It is thus timely to look at how competences are exercised, particularly at a time of rapid change in the energy markets.

At present energy is a “shared competence” with European activity focussing on the development of a single energy market and on environmental issues, particularly climate change (which have a major influence on energy policy). Member States continue to have considerable autonomy to determine their own energy policy, particularly in relation to security of supply and the fuel mix, and this is reflected in very different policies across Europe. In the current state of development of energy markets, Energy UK does not see the need for a shift in the balance of competences on energy, whether from national to EU or EU to national level. However, we do consider that there needs to be better clarity of responsibilities, the avoidance of unnecessary prescription at EU level and a focus on costs and impacts of proposals.

A key point for the energy sector is that, at whatever level political decisions are taken, they should be clear and consistent, and provide for a stable long-term investment framework. Where decisions are taken at EU level, unnecessary prescription should be avoided and sufficient flexibility should be allowed for implementation across all Member States. On the other hand, national initiatives should not take a “short-termist” approach or cut across decisions taken at European level.

A major concern about EU policy in recent years is that sustainability issues have tended to take priority over cost and security of supply. Energy UK accepts the importance of the low-carbon agenda, but energy prices and reliability of supply are key elements in European competitiveness. The policy framework must therefore be affordable for EU customers and not put European industry at an undue competitive disadvantage relative to other trading blocs.

Energy UK would like to see a more holistic approach to energy policy from the Commission, and in particular a greater recognition of the interaction between environmental regulation and national energy policy. Environmental measures such as the Large Combustion Plant and Industrial Emissions Directives have had (or will have) a major impact on generation capacity in the UK and it is not clear that the security of supply implications were considered in sufficient

depth. Moreover, there are tensions between the market-driven approach to energy liberalisation and to EU ETS and the various sectoral targets in renewables, energy efficiency etc being promoted by the Commission. These tensions need to be resolved before the EU adopts a framework for energy and climate policy post-2020.

Energy UK would like to see a greater emphasis on enforcement of existing legislation, particularly on the single market. The Commission should in our view focus its effort on major rather than procedural infringements. For instance, it should be looking to promote retail competition and to remove price controls which distort competition in some Member States, particularly those which are set below cost. We are less convinced of the value of extensive proceedings for non-notification, which seem likely to take up enforcement resources without necessarily contributing much to liberalising energy markets.

It is essential that EU legislation contains adequate time for national transposition, in particular where it requires investment by companies, e.g. in IT systems. As the EU legislative process generally takes longer than expected, there is a temptation to save time by telescoping the implementation period. This can be extremely costly if, for instance, all companies within a sector are required to purchase IT systems and services from a limited number of vendors at the same time

## Specific Questions

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

A single European market in electricity and gas is bringing benefits to the UK through greater competition, more efficient resource use and the economies of scale of a larger market. Stronger energy infrastructure and the convergence of market arrangements will further facilitate cross-border trade, which should also enhance UK security of supply. Although the UK thus far has limited interconnection, gas trade with the Continent has been developing rapidly, and a number of electricity interconnectors are likely to be built in the medium term. Interconnection and market integration will also play an important role in allowing greater use of renewable energy, which should benefit the UK, given its significant renewables resource.

It is worth noting the successful development of the Single Electricity Market (SEM), which has brought significant progress in integrating the Irish and Northern Irish wholesale markets. The introduction of common EU rules through the Network Codes should help to integrate the Irish and UK markets further, though some market and policy design issues will need to be tackled.

Environmental and in particular climate change policy has become a major element in energy policy. Energy UK considers that there are benefits in tackling climate change at European and indeed international level and believes that the EU should continue to push for an international agreement on greenhouse gases (GHGs) by 2015. We see the EU Emissions Trading System (EU ETS) as the most cost-effective means to achieve GHG reductions in the traded sector: ETS is technology neutral, carbon markets are the cost-effective way to drive investment choice in GHG reduction and the ETS is fully compatible with the Internal Energy Market.

Disadvantages have tended to arise when EU legislation adopts an inflexible and prescriptive approach to regulation. The uncoordinated political agreement of renewable and energy efficiency targets has had the unintended consequence of undermining the carbon price (though we accept that the recession has had the greatest impact), so that more cost-effective carbon

abatement measures have been postponed. The EU institutions should now give due consideration to the interactions between EU targets in the upcoming 2030 Climate and Energy Package. Most Energy UK members take the view that a strong carbon price should drive much increased investment in renewables and energy efficiency, thus reducing the need for specific targets. In general, we would like to see a greater focus on outcomes rather than prescription in European policy.

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

It has taken a considerable time to liberalise the EU's electricity and gas markets – the original Directives were proposed over twenty years ago and the impact of competition has only started to be felt in some national markets over the last few years. This is an indication that legislation on the single market has not been disproportionate – and arguably that a more prescriptive approach and stronger enforcement could have been beneficial.

With the advent of the Network Codes, the EU has started to produce more detailed technical rules for electricity and gas markets. It is important that these Codes tackle truly cross-border issues and strike a balance between ensuring a level playing field and prescribing requirements which could be dealt with at national level. Energy UK's major concern with the Codes so far relates to the draft Requirements for Generators Code, which brings very small generation into the scope of regulation (units as small as 800 W, e.g. a small solar panel.) Such units are in our view not of cross-border significance and it is disproportionate to include them in a European Code of this type. Energy UK also takes the view that stakeholders need to be more closely involved in the preparation of Network Codes.

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

Energy UK believes that there should be greater clarity about the balance of competences in energy and that it would be helpful to set out some guiding principles on competence. In the current state of development of energy markets, Energy UK does not see the need for policy decisions to be shifted to EU level. As energy markets become more integrated across Europe, there will probably be a need for greater coordination among national governments but this can be handled within the existing split of competences.

It is worth noting that the UK Government has tended in some areas to go beyond EU requirements, particularly in the area of climate change policy, e.g. the adoption of an emissions performance standard for fossil plant. This form of "goldplating" could disadvantage UK industry relative to EU competitors. In general, Energy UK believes that the UK Government should pay particular attention to costs and burdens on business when going beyond agreed EU policies. On a wider scale, EU competitiveness could also become a concern if the rest of the world does not follow the EU lead on climate action and no international agreement is reached.

**b) National, regional or international level instead of EU level?**

In general terms, Energy UK does not see any need to shift existing European competences to national or regional level. By definition, the rules for a European energy market cannot be agreed at national level and we do not believe that bilateral negotiation would be a feasible option for integrating 28+ national markets.

Energy UK believes that climate change objectives are best handled at European level and that EU ETS should remain the key mechanism for delivering GHG reductions in the traded sector. However, beyond that there should be flexibility for Member States to meet targets in the most cost-effective way. This could be through energy efficiency, renewables or other low-carbon technologies. Member States should take care to ensure that their policy measures do not unduly distort the energy market or cut across mechanisms such as EU ETS.

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

Energy UK believes that the process of developing EU energy legislation could be improved. EU policies and in particular any targets put in place should be evidence-based and underpinned by a comprehensive regulatory impact assessment (RIA) covering affordability, competitiveness and security of supply as well as sustainability. The models used for analysing data at EU level should also be open and transparent to allow robust scrutiny by stakeholders.

We welcome the fact that all proposals for EU legislation must now be supported by an RIA, as this mechanism provides an opportunity to take account of the wider economic interests of Member States. However, the reliability and relevance to individual Member States of RIAs carried out at EU level can be questionable as it is very difficult to represent accurately the circumstances of 28 individual countries. There are some signs that the quality of impact assessment is improving, though RIAs sometimes appear to be undertaken to justify decisions rather than serving to evaluate policy alternatives.

Commission proposals are often significantly modified by the Council and Parliament during the negotiation process, but these changes are not subject to any impact assessment. An example would be the three-week limit for customer switching which was included as a late amendment in the Third Package, but whose costs were never assessed. This appears to be an important gap in the EU process which Energy UK would like to see addressed.

The EU has an important role as a forum for discussion on energy issues, tackling emergency issues such as the Russia/Ukraine crisis and more general coordination of policies. Voluntary agreements and best-practice guidelines have a role to play in some policy areas and the need for some EU measures could be questioned, e.g. the 2003 Electricity Security Directive which followed on from the Italian blackout. However, there does not appear to be an alternative to most European legislation on energy, as it either relates to market rules or imposes costs, making non-compliance an attractive option unless the measures are compulsory.

Energy UK believes that a greater effort could be made to avoid "red tape" in EU legislation. Most existing EU legislation has a review clause but succeeding versions tend to become more onerous without notable efforts to lighten the regulatory burden.

Adequate time needs to be allowed for the implementation of EU legislation and the sequencing of requirements needs to be carefully determined during the legislative process. For instance, in the case of REMIT, the prohibition on insider trading was introduced before there was any clarity about reporting requirements or any agreed routes for publishing the data. This resulted in significant regulatory uncertainty which could have been avoided.

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

A single market with stronger interconnection will benefit UK customers and the energy industry alike by promoting competition, providing access to a wider market and enhancing security of supply. It will also help to accommodate a higher share of renewable energy by using available resource more efficiently.

Energy UK supports the efforts to achieve further integration of the EU electricity and gas markets and accepts that some detailed rules will be needed to align wholesale market arrangements. It is important in our view that the Network Codes focus particularly on overcoming barriers to trade and do not impose unnecessary costs. This is particularly important for a mature competitive market such as the UK, where costly system changes could be required without major benefit in terms of promoting cross-border competition. This underlines the need to provide thorough impact assessment of EU regulatory measures.

The single market agenda should recognise that EU climate and renewable policy may require governments to take specific measures to promote low-carbon energies and ensure security of supply, e.g. long-term contracts and capacity mechanisms. The UK faces a particular challenge in the period to 2020, as a significant proportion of current generating capacity is expected to close. Consequently, the UK has introduced an Electricity Market Reform package (EMR) in order to bring forward the investment needed in low-carbon generation. This is consistent with the EU's long-term energy and climate ambitions and should be recognised as such.

The EU renewable targets have resulted in a much greater development of intermittent renewables sources than was envisaged when the EU target model for wholesale markets was established. Consequently the UK and several other governments are proposing to introduce capacity mechanisms to safeguard generation adequacy. Such measures should be carefully designed to minimise market distortions, but it is for national governments to decide how to achieve the necessary outcomes, Energy UK agrees that the EU should set high-level guidelines for capacity mechanisms to ensure that there is no discrimination between technology types or age of plant, and that undue distortions to trade are avoided.

Market integration of renewable energies is essential if the single energy market is to be completed (see our response to Q.8 below).

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

Legislation such as the Electricity Security Directive, Gas Security Directive and Regulation on Trans-European Energy Networks has not required major changes to arrangements in the UK. To the extent that the Directives provide a common framework and minimum standards for network operation, emergency plans etc which all Member States have to meet, they could be viewed as beneficial.

A Regulation on Energy Infrastructure which seeks to remove barriers to the development of electricity and gas interconnectors has recently been agreed. Energy UK supports this measure, which aims to ensure greater coordination among regulators and speedier authorisation of projects. We would also support the provision of limited EU funding for energy infrastructure on the basis that it can have security of supply or other benefits which the market alone would not

provide. However, Energy UK believes that network infrastructure should generally be funded through the tariff mechanism (with costs borne by the beneficiaries) and that interconnectors should predominantly be built where cost-effective.

Interconnection is likely to become increasingly important for an island system such as the UK. However, it must be stressed that interconnectors are not a panacea and that the European power system requires not only a strong grid but also adequate local and regional generation capacity. Interconnection on its own does not guarantee that there will be sufficient capacity to meet demand. Energy UK would not support the establishment of targets for interconnection, as have sometimes been proposed: undersea DC interconnectors such as those required for island markets such as GB are significantly more costly than conventional AC interconnection, so a one-size-fits-all EU approach is not appropriate. In general, infrastructure should be built on the basis of need evidenced by market appetite rather than arbitrary targets. It is also important to ensure that interconnection charging principles do not undermine the potential development of storage and demand-side response measures.

One concern of Energy UK is that the Commission applies to be applying increasingly stringent criteria to the authorisation of merchant interconnectors. Energy UK accepts that most interconnection will be built through the regulated route, but it is important that the merchant option (which has been used for most existing UK interconnection) remains open.

Energy UK takes the view that the primary responsibility for security of supply should remain with Member States. The availability and public acceptability of different energy sources and technologies varies across Europe and so a wholly unified policy is unfeasible. National Governments should be accountable to their electorates for the policies they pursue and for the associated costs. Furthermore, the arrangements should be transparent, so that customers are clear about what they are paying for.

As the European energy system becomes more integrated, policy decisions by individual Member States will have an increasing impact on their neighbours. This is already visible in, for instance, the German decision to phase out nuclear energy which has had both cost and operational impacts on other Member States. It follows that the European Union should act as a proactive forum for discussion on energy issues and should where appropriate help coordinate energy security policies.

Europe needs to maintain a diversified mix of fuels and technologies to ensure security of supply and minimise costs. However, the current picture is not encouraging with several Member States effectively banning the development of nuclear energy, carbon capture & storage (CCS) and shale gas, all of which have a potential role to play in ensuring reliable low-carbon energy provision. Similarly, some renewable sources of energy are facing increasing planning and other barriers. It is important that the Commission and European policy-makers collectively work to keep energy options open rather than closing them down.

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

The development of indigenous renewable energies such as wind, solar and biomass has been accelerated by European policy (see our response to Q.8 below).

Utilisation of UK coal resources and UK coal generation has certainly been adversely affected by EU policy on climate change (EU ETS etc) and on power station emissions (LCPD and IED). However, it could be argued that domestic policy decisions have had the greater impact, e.g. liberalisation of the UK power market, the Climate Change Act and carbon floor price.

In Energy UK's view, national and EU policy-makers should promote a diversified fuel mix and should help ensure that potential new energy resources including shale gas are exploited where environmentally acceptable and cost-effective. Energy UK takes the view that national competent authorities should be responsible for assessing and monitoring the environmental impacts of shale gas extraction and does not see the need for EU-wide legislation at this juncture.

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

*Energy Efficiency*

The EU has a role to play in certain aspects of energy efficiency policy, notably the setting of appliance efficiency standards, which has played a major role in reducing the energy consumption in the household sector. Energy labelling of traded goods is also best tackled at European level and Energy UK believes that there is a role for the Commission in disseminating best practice and promoting technology innovation. Encouraging research and development into home energy management systems and smart appliances should help to accelerate the production of white label goods that can be purchased by consumers to assist with the adoption of smart grid technologies. There also needs to be greater recognition by national regulators of the value of smart grid technologies in lowering electricity consumption at peak periods and overall. To date Ofgem has, to our knowledge, been the only regulator to introduce specific initiatives to reward network companies for innovative use of smart grid technology.

However, Energy UK is much less convinced of the need to set European energy efficiency targets or harmonise national policies. EU Member States differ considerably in terms of climate, geography, industrial development, housing stock, generation mix etc and use a variety of policy instruments to promote energy efficiency (taxes, supplier obligations etc). The Commission has tended in our view to take an over-prescriptive approach to regulation, including the recent attempt in the Energy Efficiency Directive to impose CHP for all new fossil plant (though this was not included in the final text).

Most Energy UK members believe that it would be preferable to set a target for greenhouse gas reduction and to allow Member States flexibility in the extent to which they achieve this through energy efficiency or through other measures.

*Renewables*

The 2009 Renewables Directive has had a major positive impact on the development of renewables in the UK. It is very unlikely that such an ambitious target would have been adopted without the Directive. This has had a number of benefits in terms of contributing to the low-carbon transition, promoting technology development and employment and reducing

dependency on fossil fuels. On the other hand, the UK has accepted a considerably tougher target than other Member States (effectively a tenfold increase compared to a doubling in most Member States), which inevitably has cost implications.

Energy UK members agree that the development of renewables must continue into the 2020s and there will still be a need for dedicated support, particularly for immature technologies that require assistance to achieve commercialisation. This type of support is likely to be technology specific, with deployment concentrated at the most suitable sites. For these reasons, specific support for certain technologies should remain a decision taken at the Member State level.

In future, greater cooperation among Member States is likely to be needed to develop some renewable energies, in particular offshore wind and marine technologies. It will be important to have a supportive and consistent regulatory framework for such technologies and Energy UK welcomes, for instance, the work being done in the North Seas Grid initiative in this respect. This is particularly relevant to the UK, given its large renewable resource. There is also a case for cooperation on storage and demand-side response issues – market-based solutions should be implemented in these areas.

A future priority should be to ensure that renewable energy production across Europe is integrated with the market in terms of selling power into the wholesale market, balancing responsibility and non-discriminatory network charges.

#### *Carbon Capture & Storage (CCS)*

The CCS Directive establishes a regulatory framework for carbon capture and storage and the EU has also been active in trying to develop a demonstration programme for CCS. The demonstration programme has encountered a number of setbacks and progress has been much slower than expected. Elements of the CCS Directive, e.g. the financial security requirements could be viewed as too onerous, but are not in our view a major factor in delaying the development of CCS. The impacts of the financial crisis, e.g. decreased energy demand, low carbon prices and reduced investment funds available to major utilities are likely to be the major factors. In the case of the demonstration programme, a major lesson is the importance of coordinating EU and national funding schemes and avoiding over-rigid deadlines.

It remains important in Energy UK's view to demonstrate CCS at industrial scale if Europe's longer term carbon objectives are to be met. The EU and Member States should work together to bring forward a demonstration programme and address any regulatory barriers to CCS.

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

At a time of increased competition for energy resources, Energy UK believes that there are benefits in the EU taking a coordinated approach to discussions with the major energy-producing countries. Nevertheless, it must be recognised that Member States will sometimes have competing interests and that a collective view will not always be reached. We would envisage the European Commission taking a high-level facilitation role rather than becoming directly involved in commercial negotiation.

Energy UK supports the role which the EU has played in the UNFCCC discussions on GHG emission reductions and stresses the importance of the ongoing negotiations around a global agreement to succeed the Kyoto Protocol. The UK has more influence with UNFCCC and other countries by working through the EU than it would have on its own.

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

The Euratom Treaty provides an appropriate framework for the development of nuclear energy in Europe while leaving the decision on whether to deploy the technology to each Member State. Energy UK does not see any need to change this framework at present.

National nuclear safety regulators should continue to have the primary responsibility for overseeing the safety and security of nuclear installations. Energy UK welcomes the closer cooperation between national regulators that has been developed in recent years. Any action at EU level should not encroach on the competence or credibility of national safety regulators and should complement the requirements of the relevant international conventions and IAEA Guidelines.

Nuclear energy is an important element in a diversified fuel mix, which can help to reduce Europe's import dependency as well as reducing carbon emissions. The Commission should ensure that nuclear energy is able to compete on a level playing field with other decarbonisation options and should promote a dispassionate debate on energy provision.

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

Europe faces considerable future challenges in energy, notably in respect of industrial competitiveness and meeting its longer-term GHG targets. Europe currently has energy prices which are significantly higher than those in the US in particular and it is vital that the competitiveness of EU industry is safeguarded. Europe's energy import dependency is also continuing to increase. If these challenges are to be met, Europe and national governments must implement cost-effective and market-based policies, promote a diversified fuel mix and focus on improving energy efficiency.

A particularly significant future challenge is to achieve the European Council goal of an economy-wide 80 to 95% reduction in GHG emissions by 2050. To meet this level of ambition, the electricity generation sector will have to be essentially decarbonised and electricity will increasingly be used to decarbonise the heating and transport sectors. If the transition to a low-carbon generating portfolio is to be made successfully, energy and environmental legislation will have to be carefully coordinated to ensure that secure and affordable energy provision can be maintained.

Major investment will be needed to achieve this transition and policy-makers must therefore provide an attractive climate for investment within the EU. Energy is a capital-intensive sector with long asset lifetimes and clear visibility of policy objectives is essential. Clear greenhouse

gas reduction targets need to be set for 2030 and 2050 and a credible policy framework must be established. Improvements will be needed to strengthen the EU ETS given that the current carbon price is insufficient to incentivise investment in low-carbon generation or energy efficiency. Energy UK advocates the early structural reform of EU ETS and notably a revision of the annual linear factor.

The EU cannot afford to “go it alone” on climate change and so it is all the more important that policy should be cost-effective and avoid damage to competitiveness. Europe should continue to prioritise the establishment of an international agreement on climate change and maintain efforts to link the EU ETS with other trading schemes.

Additional efforts will also be needed at EU and national level to drive innovation in energy technologies. In particular, greater investment should be focused on research, development and demonstration to ensure that the most effective technologies are deployed at scale. This can be best achieved by ensuring that policy at an EU and nation state level is coordinated, so that funding sources can be aligned in terms of both objectives and timing.

## **12. What would be the costs and benefits of facing these at an international, EU, or national level?**

Climate change is a global problem which is best tackled at the international level, with strong coordination within the major economic regions such as the EU. Energy UK believes that an international agreement on climate change should remain a key EU objective, as otherwise Europe and the UK could be placed at a serious competitive disadvantage.

As the European energy market becomes more integrated, there will be an increased rationale for cooperation and policy convergence within the EU to ensure secure and affordable energy supplies. For the foreseeable future, energy policy will require a mix of actions at EU and national level. This requires flexibility in how legislation is both set and implemented. It is important that EU measures are not over-prescriptive and equally that action at the UK level does not undermine EU mechanisms.

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