Subsidy Advice Unit Report on Phase 3 of the Industrial Energy Transformation Fund

Referred by the Department for Energy Security and Net Zero

11 January 2024

Subsidy Advice Unit

Part of the Competition and Markets Authority

CONTENTS

1. Introduction

1.1 This report is an evaluation prepared by the Subsidy Advice Unit (SAU), part of the Competition and Markets Authority, under section 59 of the Subsidy Control Act 2022 (the Act).

1.2 The SAU has evaluated the assessment of compliance from the Department for Energy Security and Net Zero (DESNZ) of Phase 3 of the Industrial Energy Transformation Fund (IETF) scheme (IETF Phase 3), with the requirements of Chapters 1 and 2 of Part 2 of the Act (the Assessment).[1]

1.3 This report is based on the information provided to the SAU by DESNZ in its Assessment and evidence submitted relevant to that Assessment.

1.4 This report is provided as non-binding advice to DESNZ. The purpose of the SAU's report is not to make a recommendation on whether the scheme should be implemented, or directly assess whether it complies with the subsidy control requirements. DESNZ is ultimately responsible for making the scheme, based on its own assessment, having the benefit of the SAU's evaluation.

1.5 A summary of our observations is set out at section 2 of this report.

The referred scheme/subsidy[2]

1.6 The IETF provides grant funding to help industrial sites overcome barriers to investment in low carbon, energy efficient technologies. DESNZ has already administered two phases of the IETF, allocating up to £289 million over six competition windows between 2020 and 2023.

1.7 On 30 March 2023, an extension to the IETF was announced as part of the 'Powering Up Britain' plan.[3] The scheme will provide £185 million in funding and will be allocated by DESNZ across two application windows. Applications for IETF Phase 3 are expected open in January 2024.

1.8 The IETF targets existing industrial processes, helping businesses to reduce energy consumption by investing in more efficient technologies and reduce emissions by bringing down the costs and risks associated with investing in decarbonisation technologies.

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[1] Chapter 1 of Part 2 of the Act requires a public authority to consider the subsidy control principles and energy and environment principles before deciding to give a subsidy. The public authority must not award the subsidy unless it is of the view that it is consistent with those principles. Chapter 2 of Part 2 of the Act prohibits the giving of certain kinds of subsidies and, in relation to certain other categories of subsidy creates a number of requirements with which public authorities must comply.

[2] Referral of the proposed Industrial Energy Transformation Fund Phase 3 subsidy scheme, by the Department for Energy Security and Net Zero - GOV.UK (www.gov.uk).

[3] Powering up Britain - GOV.UK (www.gov.uk).

1.9 The funding will be open to a broad range of industrial sectors, supporting businesses of all sizes. Qualifying businesses must operate an existing site which falls within certain specified sectors.[4]

1.10 Funding will be allocated across three strands to support the deployment of energy efficient technologies, the deployment of decarbonisation technologies, and studies to help sites investigate what solutions would work on their sites.

1.11 The funding for IETF Phase 3 will be open to companies registered in the UK with industrial sites located in England, Wales, or Northern Ireland. However, this referral and report, relates to the IETF Phase 3 scheme covering sites in England and Wales only.

SAU referral process

1.12 On 20 November 2023, DESNZ requested a report from the SAU in relation to IETF Phase 3.

1.13 DESNZ explained[5] that IETF Phase 3 is a Subsidy Scheme of Particular Interest because it allows for the provision of one or more Subsidies of Particular Interest (SOPI) to be given.[6] In particular, DESNZ explained that a recipient can receive a grant of up to £30 million (for decarbonisation deployment projects) and therefore is higher than the SOPI threshold of £10 million.

1.14 The SAU notified DESNZ on 24 November 2023 that it would prepare and publish a report within 30 working days (ie on or before 11 January 2024).[7] The SAU published details of the referral on 27 November 2023.[8]

[4] Mining and quarrying (with the exception of coal mining operations, removed for Phase 3); Manufacturing; Recovery and recycling materials; Data centres; Industrial Laundries (added for Phase 3); and Controlled environment horticulture (added for Phase 3).
[5] In the information provided under section 52(2) of the Act.
[6] Within the meaning of regulation 3 of The Subsidy Control (Subsidies and Schemes of Interest or Particular Interest) Regulations 2022 which sets out the conditions under which a subsidy or scheme is considered to be of particular interest.
[7] Sections 53(1) and 53(2) of the Act.
[8] Referral of the proposed Industrial Energy Transformation Fund Phase 3 subsidy scheme, by the Department for Energy Security and Net Zero - GOV.UK (www.gov.uk)

2. Summary of the SAU's observations

2.1 The Assessment uses the four-step process described in the Statutory Guidance for the United Kingdom Subsidy Control Regime (the Statutory Guidance) and as reflected in the SAU's Guidance on the operation of the subsidy control functions of the Subsidy Advice Unit (the SAU Guidance).

2.2 We consider that DESNZ has articulated a clear policy objective and explained the relevant set of market failures well. It has also carried out a well-structured assessment of alternative options by commencing with a long-list of options, shortened to the chosen approach using a clear set of criteria.

2.3 We note that DESNZ could strengthen parts of its Assessment, in particular:

(a) While it has done so in part, in general we consider that DESNZ could rely more on its experience and evidence from the first two phases of the IETF to inform its conclusions. Additionally, the Assessment would benefit from more clearly referencing the evidence that has been provided.

(b) In Step 3, the Assessment could be improved by considering proportionate approaches to assess the effects of the scheme on competition and investment (such as case studies based on evidence and experience from the previous two phases of the IETF). The Assessment could also be improved by providing an explanation as to why the sectors eligible for IETF funding (see footnote 4 to paragraph 1.9) were chosen, including the reasons why certain sectors were added for Phase 3.

(c) In Step 4, the Assessment could be enhanced by detailing any costs or negative effects which may arise, including any effects on competition and investment within the UK or international trade and investment.

(d) In the Energy and Environment Principles, the Assessment could be strengthened by clearly addressing all the considerations set out in the Statutory Guidance, including clear statements of compliance for each relevant principle.

2.4 As set out in paragraph 1.11, while IETF Phase 3 will be open to companies registered in the UK with industrial sites located in England, Wales and Northern Ireland, this referral and report relates only to the IETF Phase 3 scheme covering sites in England and Wales. The Assessment and relevant evidence are sufficiently disaggregated such that the assessment against the principles (and the supporting evidence cited) is specific to the referred aspects of the subsidy or scheme.

2.5 Our report is advisory only and does not directly assess whether IETF Phase 3 complies with the subsidy control requirements. The report does not constitute a

recommendation on whether the scheme should be implemented by DESNZ. We have not considered it necessary to provide any advice about how the proposed scheme may be modified to ensure compliance with the subsidy control requirements.[9]

[9] Section 59(3)(b) of the Act.

3. The SAU's Evaluation

3.1 This section sets out our evaluation of the Assessment, following the four-step framework structure used by DESNZ.

Step 1: Identifying the policy objective, ensuring it addresses a market failure or equity concern, and determining whether a subsidy is the right tool to use

3.2 The first step involves an evaluation of the Assessment against:

(a) Principle A: Subsidies should pursue a specific policy objective in order to (a) remedy an identified market failure or (b) address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns); and

(b) Principle E: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.[10]

Policy objectives

3.3 The Assessment sets out an overall objective of assisting beneficiaries to overcome barriers to investment in order to: reduce industrial energy demand; reduce industrial emissions to support the delivery of carbon budgets 5 and 6;[11] and build and de-risk the market for decarbonisation technologies through supporting 'early mover investment.'

3.4 It sets out the sectors in which eligible beneficiaries must be active[12] as well as the three areas of activity which the scheme aims to support (see paragraph 1.10).

3.5 The Assessment refers to a range of appropriate evidence on industrial emissions in the UK, and overall UK government objectives on Net Zero which the IETF Phase 3 aims to support.[13] It also notes the 2023 Progress Report to Government by the Climate Change Committee,[14] which indicated that progress in emissions reduction was off track to meet Net Zero targets, and that the scheme was one part of an overall package to address this.

[10] Further information about the Principles A and E can be found in the Statutory Guidance (paragraphs 3.32 to 3.56) and the SAU Guidance (paragraphs 4.7 to 4.11).
[11] Carbon Budgets - GOV.UK (www.gov.uk)
[12] See footnote 4 to paragraph 1.9.
[13] See Net Zero Strategy: Build Back Greener - GOV.UK (www.gov.uk)
[14] 2023 Progress Report to Parliament - Climate Change Committee (theccc.org.uk)

3.6 In our view the Assessment clearly sets out the intended policy objectives, which are well-focused and provide appropriate context.

Market failure

3.7 The Statutory Guidance sets out that market failure occurs where market forces alone do not produce an efficient outcome.[15]

3.8 The Assessment sets out a number of market failures which are well explained and supported by appropriate evidence, including experience from previous phases of the IETF and feedback from consultations with the industry and with lenders. These include externalities involved in greenhouse gases produced from industrial processes, early mover disadvantage, and spillover effects. The Assessment also sets out other barriers to investment as to why companies are not funding these investments themselves.[16]

3.9 We consider that the Assessment sets out and explains well a range of market failures preventing investment in low carbon, energy efficient technologies. We consider that the Assessment provides an appropriate level of relevant detail and evidence.

Consideration of alternative policy options and why the IETF Phase 3 scheme is the most appropriate and least distortive instrument

3.10 In order to comply with Principle E, public authorities should consider why the decision to give a subsidy is the most appropriate instrument for addressing the identified policy objective, and why other means are not appropriate for achieving the identified policy objective.[17]

3.11 The Assessment takes a structured approach in considering alternative policy options. A longlist of 13 options covering funding (grant, loan, capital guarantee etc), tax, regulatory and market creation solutions, is reduced to a shortlist of four after consideration against criteria set out in the Assessment and supporting evidence (including 'critical success factors' in line with the Green Book Appraisal Guidance).[18]

3.12 The four shortlisted options are then considered against an economic model used in previous phases of the IETF, updated with inputs relating to technology costs and associated energy savings to assess the quantitative and qualitative benefits. Following this exercise, DESNZ concludes that grant funding split equally between

[15] Statutory Guidance, paragraphs 3.35 to 3.46.
[16] High payback periods on decarbonisation projects, that the equipment to be replaced is still early on in its economic lifecycle, lack of expertise to identify and deploy solutions, and general economic uncertainty.
[17] Statutory Guidance, paragraphs 3.54 to 3.56.
[18] HM Treasury (2022), *The Green Book*, pages 23 to 56.

energy efficiency and decarbonisation was the most appropriate option to address the market barriers to investment in low carbon, energy efficient technologies.

3.13 The Assessment also considers the drawbacks to its chosen option, recognising that loans are less distortive than grants but that evidence from industry indicated minimal appetite for loans given economic uncertainty and risks to business.

3.14 The Assessment could have provided a clearer conclusion explaining why the chosen option is the most appropriate. However, overall, our view is that the approach taken is an appropriate and practical way to demonstrate that the public authority has properly considered different policy options for achieving the policy objective, including their respective drawbacks.

Step 2: Ensuring that the subsidy is designed to create the right incentives for the beneficiary and bring about a change

3.15 The second step involves an evaluation of the assessment against:

(a) Principle C: First, subsidies should be designed to bring about a change of economic behaviour of the beneficiary. Second, that change, in relation to a subsidy, should be conducive to achieving its specific policy objective, and something that would not happen without the subsidy; and

(b) Principle D: Subsidies should not normally compensate for the costs the beneficiary would have funded in the absence of any subsidy.[19]

Counterfactual assessment

3.16 In assessing the counterfactual, the Statutory Guidance explains that public authorities should assess any change against a baseline of what would happen in the absence of the subsidy (the 'do nothing' scenario').[20] This baseline would not necessarily be the current 'as is' situation (the 'status quo') but what would likely happen in the future – over both the long and short term – if no subsidy were awarded.

3.17 The Assessment states that in the absence of IETF Phase 3, qualifying firms would either choose not to invest in ways that would help achieve the policy objectives or would potentially move investment overseas to take advantage of similar types of subsidy support from other countries.

3.18 The Assessment notes that industry specific investment barriers limit the prospective investors' willingness and ability to invest in green technologies. The

[19] Further information about the Principles C and D can be found in the Statutory Guidance (paragraphs 3.57 to 3.71) and the SAU Guidance (paragraphs 4.12 to 4.14).
[20] Statutory Guidance, paragraphs 3.60 to 3.62.

Assessment provides evidence indicating that this includes access to funding on terms acceptable to industry and an unwillingness to abandon current equipment and technologies still in use that are still economically viable. It also notes that payback periods are longer than those that would usually be acceptable to the private sector, and first-mover disadvantages due to uncertainties of a nascent market.

3.19 In our view, the Assessment sets out a sufficiently clear counterfactual explaining that absent IETF Phase 3, the levels of investment in energy efficiency and decarbonisation technologies will be lower and industry will not make the required progress towards Net Zero and energy reduction targets. Nonetheless, in relation to the potential for companies to move investments overseas absent the scheme, we consider that the Assessment could be improved with supporting evidence from previous IETF phases, for example showing companies not in receipt of IETF funding having moved investment overseas.

Changes in economic behaviour of the beneficiary

3.20 The Statutory Guidance sets out that subsidies must bring about something that would not have occurred without the subsidy.[21] In demonstrating this, public authorities should consider the likely change or additional net benefit.

3.21 The Assessment notes industry reluctance to pursue energy efficiency and decarbonisation projects, using evidence from industry consultation to conclude that capex costs are, in particular, a significant barrier to investment but also other aspects such as the fact that equipment is still economically viable (see paragraph 3.18). As such, the Assessment concludes that the provision of a subsidy to assist with those costs will incentivise industry to make investments that would otherwise not be made.

3.22 We are of the view that that the Assessment sets out how IETF Phase 3 will encourage industry investment in green technologies and change their economic behaviour. We note that the supporting evidence sets out how matching funds will be required from the beneficiaries; we consider that the Assessment could have been strengthened if it noted this detail directly. We also consider the Assessment could be further strengthened by using evidence from the first two phases of the IETF to demonstrate how the IETF has changed the economic behaviour of previous beneficiaries.

Additionality assessment

3.23 ‘Additionality’ means that subsidies should not be used to finance a project or activity that the beneficiary would have undertaken in a similar form, manner, and

[21] Statutory Guidance, paragraph 3.64.

timeframe without the subsidy.[22] For schemes, public authorities should also, where possible and reasonable, ensure the scheme's design can identify in advance and exclude those beneficiaries for which it can be reasonably determined would likely proceed without the subsidy.[23]

3.24 The Assessment sets out that applicants to IETF Phase 3 must provide data and evidence to prove that they would not have undertaken projects without government's financial support. A supporting annex provides the guidance for applicants on what must be submitted for evaluation to prove that they would not have gone ahead without a grant. This includes a requirement to submit information explaining the projects they would invest in or actions they would take absent the grant. In this way, the Assessment demonstrates that IETF Phase 3 would not cover costs or fund projects that would have occurred in the absence of the subsidy.

3.25 The Assessment notes that IETF Phase 3 will not support costs incurred from energy efficiency and decarbonisation measures that bring sites and equipment to minimum legal standards, nor support projects that stem from improvement required by regulatory bodies. Applicants must outline their future plans to achieve energy efficiency and emission reductions and how these go beyond what they propose to do with a grant from IETF Phase 3.

3.26 In our view the Assessment demonstrates that the due diligence to be undertaken on applicants, and the data and evidence to be evaluated, clearly assesses additionality. In particular, it is designed to exclude energy efficiency and decarbonisation projects or activities that would have proceeded in a similar form, manner, and timeframe without the subsidy.

3.27 The Assessment states that the grant money provided by IETF Phase 3 will accelerate the rate of decarbonisation in the UK. In our view, the Assessment could have been strengthened by including evidence to support this assertion. In particular, given this is the third phase of the IETF, such evidence could feasibly include an evaluation of the decarbonisation which has resulted, or can be expected to result, from the IETF's previous phases.

Step 3: Considering the distortive impacts that the subsidy may have and keeping them as low as possible

3.28 The third step involves an evaluation of the Assessment against:

[22] Statutory Guidance, paragraphs 3.63 to 3.67.
[23] Statutory Guidance, paragraph 3.69.

(a) Principle B: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it; and

(b) Principle F: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the United Kingdom.[24]

Proportionality

3.29 The Assessment considers whether the size of IETF Phase 3 could be decreased. It compares the budget of £185 million, with the estimated £19 billion of capital expenditure required over the period 2020-2037 to meet the objectives of the scheme on the overall policy objective of reducing emissions.

3.30 The Assessment also provides extensive detail on the sizes of awards open to beneficiaries of IETF Phase 3, as well as on the design features of the Scheme which aim to limit the intervention to only what is necessary, including:

(a) checks on eligibility;

(b) an economic assessment of applications to ensure that the projects deliver best value for money (covering the calculation of benefit cost ratios for both the energy efficiency and decarbonisation strands);

(c) an assessment by technical experts to assess the project for validity; and

(d) financial due diligence.

3.31 In our view, the approach to Principle B is broadly appropriate, in particular by considering proportionality explicitly against the policy objective. The details on how the design of IETF Phase 3 aims to limit the amounts given to what is necessary are also appropriate and sufficiently detailed.

3.32 The Assessment could, however, be improved by providing further detail on how the total budget was determined, potentially informed by the results from earlier phases of the IETF (or from similar schemes in the UK and elsewhere). The Assessment could have also been strengthened by considering other subsidies given to the same recipients for similar purposes, as set out in the Statutory Guidance.[25] This includes not only subsidies that have already been given at the point the scheme is made, but also those that could be given in the time period between the scheme being made and the subsidies under it being given.

[24] Further information about the Principles B and F can be found in the Statutory Guidance (paragraphs 3.72 to 3.108) and the SAU Guidance (paragraphs 4.15 to 4.19).
[25] See Statutory Guidance paragraphs 3.91 and 3.92.

Design of subsidy to minimise negative effects on competition and investment

3.33 The Assessment sets out in detail those aspects of IETF Phase 3 that safeguard against negative effects, including the scope of potential beneficiaries, the assessment process, the caps on individual grants, time limits, the nature of costs covered (capital costs only), monitoring and evaluation arrangements, and measures to ensure there are no subsidy races.

3.34 Our view is that the Assessment provides a good overview of how the design of IETF Phase 3 will help minimise negative impacts on competition and investment. However, we consider that it could be strengthened by providing an explanation of why the industrial sectors eligible to participate have been chosen, especially with respect to those added for Phase 3 of the IETF that were previously ineligible.

Assessment of effects on competition or investment

3.35 The Assessment indicates that maximum grant awards are most likely to give rise to distortions. In our view the Assessment could be strengthened by including a more detailed explanation of this, such as how it might affect beneficiaries' prices or outputs, and the steps taken to mitigate this. In particular, the ongoing cost impact of awards under the energy efficiency strand of the Scheme is potentially more likely to lead to changes in beneficiaries' outputs, and hence could potentially lead to greater distortions than the other parts of the Scheme.[26]

3.36 The Assessment indicates that eligibility for support is judged on a sectoral basis. It notes the wide range of markets potentially affected by IETF Phase 3 and states that it would be disproportionate to analyse all of these for potential distortions. However, the Assessment does note that limiting the eligibility of IETF Phase 3 to existing processes on industrial sites may affect efficient entry and exit into the market, but that any such impact is expected to be minimal.

3.37 We consider that the Assessment could benefit from further analysis of the markets potentially affected. While we accept that it would not be commensurate to carry out a full market analysis of each of the markets affected (given the number of industrial sectors involved in IETF Phase 3) it would be possible to carry out case studies potentially focused on the markets or aspects of IETF Phase 3 most likely to suffer from distortions (see paragraphs 3.35 and 3.36).[27] Further, given this is the third phase of the IETF, there may be an opportunity to assess the extent of distortionary impacts in those previous phases, particularly relating to beneficiaries who received the maximum grant awards available.

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[26] This aspect of the Scheme will reduce energy costs over time for beneficiaries. Such an ongoing impact on costs is more likely to lead to higher distortions than subsidies that only impact initial capital costs.
[27] See Statutory Guidance paragraph 3.30 for further detail.

3.38 The Statutory Guidance[28] also states that public authorities should identify whether a subsidy may have an impact on competition and investment in the UK (and international trade and investment) in input and related markets.

3.39 The Assessment states that one of the three objectives of IETF Phase 3 is to reduce industrial energy demand and notes that there may be competitive impacts in particular regions. Our view is the Assessment could be improved by considering, in a proportionate manner (eg as part of a case study):

(a) the potential competitive impact of IETF Phase 3 on upstream markets, for example energy generation and distribution; and

(b) how local input and related markets may be impacted, particularly noting material in the wider Assessment which suggests the potential for the energy efficiency strand of IETF Phase 3 to lead to an increase in beneficiaries' outputs.

3.40 The Assessment elsewhere notes that the majority of applicants to previous IETF phases have been from large companies, and that those in energy intensive industries (who typically compete internationally) received the majority of funding. Our view is that the Assessment could be improved by considering the implications of the likely scale of beneficiaries and the extent of international competition they face for both competition and trade respectively and (as noted in paragraph 3.32) the impact of other subsidies given to the same recipients for similar purposes.

3.41 Overall, we note that the competition assessment only considers distortions to competition at a high-level and states that the impact is likely to be small. We consider the Assessment could therefore be strengthened with further, proportionate explanation and evidence on the markets that may face competitive distortions, the likelihood of occurrence and the extent of the distortion.

Assessment of impact on international trade and investment

3.42 The Assessment notes that energy intensive industries received the majority of funding in the earlier phases of the IETF and that these are typically more engaged in international competition. It states that any impacts on international trade are likely to be small.

3.43 The Assessment does not attempt to quantify the impact on international trade and investment. We consider that the Assessment could benefit from carrying out such analysis to gain some insight into the likely size of the possible impact (given the

[28] See Statutory Guidance (paragraphs 17.46 to 17.51).

number of sectors involved, it may be similarly proportionate to use a case study approach as noted in paragraph 3.37).

Step 4: Carrying out the balancing exercise

3.44 The fourth step involves an evaluation of the assessment against subsidy control Principle G: subsidies' beneficial effects (in terms of achieving their specific policy objective) should outweigh any negative effects, including in particular negative effects on: (a) competition or investment within the United Kingdom; (b) international trade or investment.[29]

3.45 The Assessment sets out both quantifiable and qualitative benefits of IETF Phase 3, including:

(a) The benefit cost ratio (based on energy benefits, carbon benefits, air quality benefits and Gross Value Added benefits).

(b) A range of qualitative benefits from the studies strand such as: identifying a pipeline of future projects and helping to demonstrate the viability of transformational technologies; developing industry and government knowledge of the risks and benefits associated with new technologies; and knowledge spillovers for other companies. It also set out benefits from overcoming barriers to funding novel decarbonisation technologies (lowering the risk for others who wish to use similar approaches) and for energy efficiency (although notes these would be less significant than for the decarbonisation funding).

3.46 The Assessment briefly mentions some possible negative effects including:

(a) geographic impacts arising from the potential for a large accumulation of support in specific regions where industry is concentrated (due to the scheme being demand-led and not targeting specific regions);[30]

(b) affecting international investment by making the UK more attractive to invest in for large multinationals; and

(c) the risk of crowding out private investment, which is mitigated by the limits to the scheme and additionality tests.

3.47 The Assessment sets out that the overall need for the benefits that can be generated by IETF Phase 3 outweigh any potential negative effects, including

[29] See Statutory Guidance (paragraphs 3.110 to 3.117) and SAU Guidance (paragraphs 4.20 to 4.22) for further detail.
[30] The Assessment sets out that DESNZ will mitigate against this by considering, if necessary, location as one of the factors in allocating subsidies.

market distortions. It also sets out that the benefits outweigh any negative effects on competition domestically and internationally.

3.48 In our view, the Assessment could be strengthened by more clearly explaining the benefits and negative impacts, and how they arise, referring to relevant material in the supporting evidence. In particular, the treatment of negative effects is, as noted, brief, and generally only mentioned in passing. Consequently, the Assessment could also be improved with a greater explanation as to how the conclusion that the benefits outweigh the negative impacts was reached, in particular by drawing upon the evidence from the previous two IETF phases.

Energy and Environment Principles

3.49 This step involves an evaluation of the Assessment with regard to compliance with the energy and environment principles, where these are applicable to the scheme.[31]

3.50 The Statutory Guidance summarises the scope of the different energy and environment principles that apply to different types of subsidies.[32] DESNZ has conducted an assessment of IETF Phase 3 against Principles A, B, H and I. We are satisfied that the other energy and environment principles are not applicable to this scheme.

Principle A: Aim of subsidies in relation to energy and environment

3.51 The assessment against Principle A should show how the subsidy is consistent with delivering a secure, affordable and sustainable energy system and a well-functioning and competitive energy market, or increasing the level of environmental protection compared to the level that would be achieved in the absence of the subsidy. If a subsidy is in relation to both energy and environment, it should meet both of these limbs.[33]

3.52 The Assessment gives a brief high-level summary of the objectives of IETF Phase 3 and where it sits within wider government decarbonisation policy. It sets out that through its contribution to reductions in energy demand, the IETF will contribute to the delivery of greater energy security and through its contribution to industrial emissions it will contribute to greater environmental protection.

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[31] See Schedule 2 to the Act.
[32] Principles A and B apply to all subsidies in relation to energy and environment. Principle C applies for subsidies for electricity generation adequacy, renewable energy or cogeneration. Principle D applies to subsidies for electricity generation only. Principle E applies to subsidies for renewable energy or cogeneration. Principle F applies to subsidies in the form of partial exemptions from energy related taxes and levies. Principle G applies to subsidies that compensate electricity intensive users for increases in electricity costs, Principle H relates to subsidies for decarbonisation of industrial emissions. Principle I relates to subsidies for improving energy efficiency of industrial activities.
[33] Statutory Guidance, paragraphs 4.19 to 4.28.

3.53 In our view the Assessment has only set out it complies at a high-level and could be improved by making a clearer statement about which limbs of Principle A apply (or if both do) and then clearly explaining how the subsidy complies with the relevant limb(s). For example, if the first limb of Principle A applies, the Assessment should more clearly explain how the subsidy delivers a secure, affordable and sustainable energy system.

Principle B: Subsidies not to relieve beneficiaries from liabilities as a polluter

3.54 The assessment against Principle B should explain clearly how the proposed subsidy or scheme does not relieve a polluter from having to bear the full costs of the pollution caused.[34]

3.55 The Assessment sets out that there are no provisions within the Grant Funding Agreement or Grant Offer Letter which relieve beneficiaries from liabilities arising from their responsibilities as a polluter. It clearly explains that the subsidy does not relieve beneficiaries from liabilities as a polluter. In our view this sufficiently explains how IETF Phase 3 complies with energy and environment Principle B.

Principle H: Subsidies for the decarbonisation of emissions linked to industrial activities

3.56 Under Principle H, subsidies for the decarbonisation of emissions linked to industrial activities in the United Kingdom should achieve an overall reduction in greenhouse gas emissions, and reduce the emissions directly resulting from the industrial activities concerned. The assessment should identify clearly the relevant greenhouse gases (with reference to those identified as such in the Climate Change Act), and the industrial activities (as described in the Act) responsible for those gases, and show that such emissions would be reduced compared to the situation absent the subsidy or scheme.[35]

3.57 The Assessment sets out that IETF Phase 3 will deliver lifetime carbon emissions savings of an estimated 3.21 million tonnes of CO_2 equivalent, including direct emissions savings. In our view, this sufficiently explains how IETF Phase 3 complies with energy and environment Principle H. We note that the supporting evidence breaks this down into carbon emissions savings from energy efficiency and from decarbonisation measures. The Assessment could have been strengthened by also referring to this further information.

3.58 The Assessment also sets out that there are air quality benefits arising from IETF Phase 3. Similarly, the supporting evidence specifies that these benefits result from changes to the amounts some fuels are used and we note that the

[34] Statutory Guidance, paragraphs 4.29 to 4.35.
[35] Statutory Guidance, paragraphs 4.61 to 4.69.

Assessment would be improved by either directly including this detail or referring to it. Furthermore, the Assessment would be further improved by considering whether these changes would result in emissions savings not included in the estimate in paragraph 3.57.

3.59 Finally, we consider that the Assessment could be improved by more closely following the Statutory Guidance and considering the impact on greenhouse gas emissions from enterprises, locations or sectors that are not in receipt of the subsidy and how IETF Phase 3 does not simply reduce emissions in the inputs to the industrial activities.[36]

Principle I: Subsidies for improvements of the energy efficiency of industrial activities

3.60 Under Principle I, subsidies for improvements of the energy efficiency of industrial activities should improve energy efficiency by reducing energy consumption, either directly or per unit of production. The Statutory Guidance sets out a non-exhaustive illustrative list, and the assessment should demonstrate clearly how emissions are reduced relative to the situation without the subsidy or scheme.[37]

3.61 The Assessment sets out that IETF Phase 3 helps industrial sites to overcome capital barriers to investing in technologies which can immediately reduce their electricity consumption. It sets out it will deliver an estimated £130.7 million in discounted lifetime energy bill savings, with a target of 6,244.9 gigawatt-hours of lifetime energy savings.

3.62 In our view, the Assessment clearly explains how the scheme complies with energy and environment Principle I.

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[36] Statutory Guidance, paragraphs 4.67 and 4.68.
[37] Statutory Guidance, paragraph 4.73.