Committee on Climate Change

The Rt. Hon. Amber Rudd MP
Secretary of State for Energy and Climate Change
Department of Energy and Climate Change
3 Whitehall Place
Westminster
London SW1A 2AW

22 September 2015

Dear Secretary of State,

Clarifying the direction for low-carbon policy

The Committee is much encouraged that since your appointment you have confirmed the Government's support for the 2050 target to reduce greenhouse gas emissions and for the carbon budgets that provide for steady progress to that target.

However, the Government has also made a series of announcements about existing low-carbon policies. Unfortunately, these have been widely interpreted to have reduced the action being taken to meet the clear commitment to carbon budgets. They have, in some areas, left a policy gap which urgently needs to be addressed. As a package, they have raised questions over the future direction of low-carbon policies.

On the basis of policy effectiveness (cost-effectiveness; contribution to reducing emissions; policy overlap), there is no doubt that there is evidence to support many of the individual announcements. At a time of fiscal constraint, it is also understandable that the Government should want to bring spending under control.

The UK's ability to meet carbon budgets at least cost depends on firms and households making long-term investments and decisions based on how they think UK policy will unfold over a 10-15 year period. From that perspective, the announcements potentially present problems as the cumulative impression has been of a weakening of the policy framework. This is largely because the ending of measures has not been accompanied by a clear statement about what improved measures will be put in place. For example:

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- The announcement of reforms to reduce spend under the Levy Control Framework (LCF) to 2020/21 was accompanied by a statement that the LCF will be extended into the 2020s, but there is no date for when this will occur, and at what level. This is vital to boost confidence in the market for low-carbon generation.
- The Green Deal has been abolished, to be replaced with an unspecified "new value-for-money approach" on which the Government intends to work with the building industry and consumer groups. The Energy Company Obligation will continue in the short-term, but is to be part of the discussions to formulate a "new, better-integrated policy."
- The Zero-Carbon Standard for new homes will not now go ahead, replaced only by a commitment to "keep energy efficiency standards under review".

Action in each of these (and other) areas is important to meet future carbon budgets and the 2050 target cost-effectively. It is helpful that the party leaders' pledge, in the run up to the General Election, included cross-party commitment to agree carbon budgets in accordance with the Climate Change Act and to end the use of unabated coal for power generation. It would be particularly useful were the Government to set out its plans for achieving this, which should be possible with minimal impact on energy bills.

In relation to spending control, the Committee consistently considers value for money in its recommendations. The Committee has supported transparent mechanisms to reduce government funding as technologies either prove they can compete or demonstrate they are not capable of being part of meeting carbon budgets cost-effectively. At the same time, it is important to recognise that these new technologies are often competing against incumbents who do not pay their full cost and that innovation through all stages often requires public support. It is essential therefore that funding is not withdrawn too early.

The key message in our 2015 Progress Report to the new Parliament was that early action will be needed to keep UK emissions on track. Specifically, we noted that many policies designed to reduce future emissions come to an end over the course of this Parliament.

The recent changes to low-carbon policies have not sought to address this need, while bringing forward the expiry of some existing measures. The uncertainty created by changes to existing policies and a lack of replacement

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policies up to and after 2020 could well lead to stop-start investment, higher costs and a risk that targets to reduce emissions will be missed.

Given the uncertainty created by the announcements to-date, **we emphasise the importance of making the next announcements as early as possible**. We advise that they cover both what the Government plans to put in place between now and 2020 and plans beyond 2020. We have made it clear that we would prefer to assess the Government's plans as a whole, but we will necessarily have to assess the overall impact on the UK's ability to meet its carbon budgets, both of the recent announcements and any future announcements, in our 2016 Progress Report.

In the attachment to this letter we summarise the key elements of a stable policy framework that we believe now need to be put in place.

We would be happy to discuss these points further.

I have copied this letter to the Chancellor and to the Secretaries of State for Communities and Local Government, and Transport.

Yours sincerely,

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Lord Deben

Chair, Committee on Climate Change

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Annex A

Creating a stable policy framework – key elements

It is vital that the policy framework going forward should maintain the principles of carbon pricing, technology support and tackling barriers to behaviour change. We set out recommendations for action in our June 2015 Progress Report to Parliament. This annex sets out key elements of the required framework.

Power sector

- **An investable instrument to incentivise low-carbon generation:** Contracts for Difference under the EMR provide this; winning bids in the low-carbon auctions set a price at the level required to incentivise investment.
- **Support for emerging options:** The separate auction pot for emerging technologies and the CCS competition provides this, complemented by public support that leverages private investment, such as through the catapult programme.
- **Visibility of the future market for low-carbon power:** this is required to ensure that innovation takes place and that new projects are developed. Setting a well-specified LCF at an appropriate level to 2025, with a 10-year rolling window, could achieve this.

We have set out our views on the LCF and budget management more fully in a technical note published on our website[1].

Buildings

- **Policy instrument.** The Green Deal was not working. However, its end leaves a gap: there is now no mechanism to encourage able-to-pay households to implement measures. The demise of the Green Deal also leaves a question over how the private-rented sector energy efficiency regulations will be delivered. The future of the Energy Company Obligation beyond 2017 needs to be set out.

[1] http://www.theccc.org.uk/publication/technical-note-budget-management-and-funding-for-low-carbon-electricity-generation/

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- **Support for emerging options**. It is also clear that take-up of renewable heat is falling well short of the Government's ambition. A clear action plan that recognises the diversity of options for reducing emissions from heat is needed. Such an action plan should allow various options to be pursued reflecting the fact that different options will be appropriate for different types of buildings. Pursuing a variety of options also allows the market to test them and for the most effective options to emerge from the competing alternatives.

- **Visibility of future market.** With the demise of the Green Deal and uncertainty attached to ECO and the RHI, there is now no certainty beyond the Manifesto commitment to insulate a million more homes over the next five years. This is a lower level of ambition than has been delivered in recent years or is consistent with the commitment to reduce fuel poverty.

In relation to Zero Carbon Homes, we understand the Government's desire to do away with some of the complexities that had attached to the policy, notably "allowable solutions". But there is a risk that the useful components of the policy, which have attracted a high degree of industry and wider support, have been thrown out alongside those complexities. There will be a need to comply with "nearly zero energy" requirements under the EU Energy Performance in Buildings Directive from 2021. The Government should look at the options for going beyond the requirements of Part L of the English Building regulations.

The need is for a detailed action plan, to deliver low-carbon heat, considering this alongside energy efficiency. This should include setting out the future of the Renewable Heat Incentive (RHI) and of the Energy Company Obligation (ECO).

Transport

- **Policy instrument**: EU regulations on CO_2 intensity of new vehicles towards 2020 have acted as a highly effective instrument to require manufacturers to a shift towards more efficient cars and vans. Evaluation evidence suggests that this has been achieved to date at relatively low cost.

- **Visibility of future market:** To maintain visibility the Government should push for clear, stretching 2030 EU targets for new cars and vans that take account of the need for ultra-low emission vehicles.

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- **Support for emerging options**: In support of an emerging EV market, the Government is investing in charging infrastructure and has provided a grant towards the additional up-front cost of EVs. The most important need is to maintain up-front support while EVs remain more expensive than conventional vehicles, and not to withdraw this too early. The Government recently announced a short-term extension for cars, until at least February 2016, but – perhaps in amended form – this will need to be extended further.

Pricing signals can support the shift towards lower emission vehicles within the UK. In relation to Vehicle Excise Duty (VED), we have previously recognised the need to look again at the structure of VED rates for cars, as emissions of new vehicles fall. The changes announced in the Budget, however, appear to be a missed opportunity. In terms of incentives to buy low-emission vehicles they heavily weight the first year rates, ignoring the incentives provided by VED in subsequent years. Whilst they promote zero emission vehicles, they fail to recognise the case for differentiation below 100gCO_2. This is particularly unhelpful for the encouragement of PHEVs. The Government has committed to review the new system as necessary to ensure that it continues to incentivise the cleanest cars. There is an immediate case for doing this.

<u>Business energy efficiency</u>

We welcome the review of business energy efficiency measures announced in the Budget. We have previously recognised the complex policy landscape and suggested scope for rationalisation. We have previously suggested a strengthened CCL and use of ESOS might be way forward. Ideally this rationalisation should look towards use of one instrument per issue – incentivisation; provision of information; regulation where necessary.

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