

How Brexit will affect UK energy and climate policy

Briefing for parliamentarians and policy makers
November 2017

The UK's energy market and climate policies are closely linked with those of other member states in the European Union. This co-operative relationship has enhanced European energy security, lowered energy bills for consumers, increased business opportunities and facilitated the transition to a low carbon economy. The UK has also carved a niche as a climate leader, achieving the fastest rate of power sector decarbonisation in the world over the past five years.¹ If the UK were to leave the EU without an agreement for continued co-operation, these benefits and the UK's leadership would be put at significant risk.

In recent oral evidence to the EU energy and environment subcommittee, the Energy Minister Richard Harrington stated that the government's "top priority is to be as near as possible to the current arrangements" on energy and climate policy.² We agree with the minister and we strongly recommend that the government sets up a co-operative track within the negotiations, built on international commitments like the Paris Agreement on climate change. Collaborative approaches could be agreed early on to secure mutually beneficial outcomes, which would build a foundation of trust between the two parties for the remainder of the negotiations.

Avoiding energy and climate risks: summary of recommendations

- Commit to continued climate co-operation with the EU, to preserve the integrity of the Paris Agreement on climate change.
 - The UK should seek to fully participate in the EU internal energy market and avoid disrupting the Irish Integrated Single Energy Market.
 - Negotiate a zero tariff trade agreement for low carbon goods with the EU alongside measures to reduce non-tariff barriers to clean energy trade.
 - Negotiate a close partnership with the European Investment Bank that ensures a sustained source of finance to support the government's clean growth strategy.
 - Continue to co-operate on ecodesign and emissions standards to benefit consumers, the economy and the environment.
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The Brexit risks and opportunities for climate and energy

1. Climate change leadership

Risk: Any negative economic and political conditions following a disorderly Brexit are likely to reduce the political space for climate leadership in the UK. At the same time, the EU's Effort Sharing Regulation, where member states share the burden of carbon mitigation based on their GDP per capita, would be significantly complicated by a chaotic UK withdrawal. Losing the UK, which is closely integrated with the internal energy market, would raise the cost to the EU of meeting its 2030 climate targets. The worst case scenario could result in the EU weakening its 2030 targets, just at the point when parties to the Paris Agreement on climate change are required to increase their targets. Similarly, it is crucial that the integrity of the EU Emissions Trading Scheme (EU-ETS) is maintained with the UK's exit from the mechanism.

Recommendation: The UK should voluntarily contribute to the EU 2030 climate targets through the Effort Sharing Regulation, to avoid any weakening of EU, and thereby global, climate ambition. But the UK should aim to do so while seeking enhanced EU ambition on its emission reductions. On the EU-ETS, the UK should negotiate a transitional arrangement to participate at least till the end of phase 3 (2020).

2. EU Internal energy market

Risk: A no deal scenario would lead to the UK chaotically leaving the EU's internal energy market, resulting in an increase in UK energy bills. National Grid forecasted a tentative increase of up to £0.5 billion on consumer bills annually in the early 2020s, or roughly an increase of £20 per household. This excludes the bigger challenge of increased costs of domestic power generation resulting from costly manufacturing imports. These estimates are hard to calculate but generators can be expected to pass on their increased costs to consumers. It creates the prospect of a more expensive transition to a low carbon economy, as the UK would have to build more expensive domestic infrastructure to maintain system security. The Irish Integrated Single Energy Market (I-SEM) and its connection to the EU energy market, currently via the UK, would be jeopardised.³

Recommendation: The UK should seek to fully participate in the internal energy market and processes for ensuring policy coherence with the EU should be developed. The I-SEM should be maintained, either by giving it a special status or by designating Northern Ireland as a special zone.

3. Energy sector investment

Risk: A no deal Brexit and its unpredictable regulatory consequences would lead to substantial uncertainty for investors and an investment hiatus in the UK. This would

stall the quantity of low carbon energy being brought onto the grid. Similarly, a disorderly exit from the European Investment Bank (EIB), one of the largest sources of energy infrastructure finance for the UK, could lead to a substantial shortfall in the availability of project finance for new low carbon developments, exacerbated by the recent privatisation of the UK's Green Investment Bank.⁴ Losing the UK as an EIB shareholder would also bring into question its ambitious target to lend \$100 billion to climate-related projects over the next five years.

Recommendation: The UK should maintain as close a relationship as possible with the EIB, and contribute to European funds for innovation and infrastructure to promote low carbon technologies, ensuring it can continue to benefit from favourable future funding arrangements. Projects with EIB finance benefit from cheap loans and the backing of a funding agency with an international reputation. The EIB also offers patient capital that is often necessary to launch technologies in their early commercial development phase and where other investment banks might not venture. A major attribute for the success of the UK's offshore wind industry, for instance, has been finance from the EIB. If the UK were to lose access to major EIB loans, the government would need to sustain low carbon infrastructure finance through domestic measures.

4. Trade in low carbon goods and services

Risk: Under a World Trade Organisation (WTO) scenario, tariffs would be applicable to several goods that are traded with the EU. While electricity is traded at a zero per cent tariff, electric cars could face tariffs as high as ten per cent. Such tariffs would deal a significant blow to low carbon trade and seriously hamper the government's clean growth strategy.

Recommendation: The UK should push to secure the Environmental Goods Agreement, a plurilateral agreement under the WTO between major low carbon goods trading nations, aimed at eliminating all tariff barriers to accelerating trade in environmental goods. The UK can then take maximum advantage of the growth in the low carbon market emerging from the implementation of the Paris Agreement on climate change, expected to be \$1 trillion a year of investment between now and 2050.⁵ Any future free trade agreement with the EU should minimise tariff and, more significantly, non-tariff barriers to low carbon energy trade.

5. Product and emissions standards

Risk: Any divergence from the EU on product and emissions standards would raise the cost of trade for UK and EU businesses forced to operate under two different regulatory systems. From electrical appliances to automobiles, a variety of goods are traded freely on the basis of common standards. The EU's growing set of free trade agreements sets it up as a regulatory superpower that several key trading

nations align with, such as Japan and China, which is a strong incentive for the UK to co-operate on standards.

Recommendation: The UK should maintain product and emissions standards on a par with, or higher than, the EU regulations and continue to adopt the latest guidelines, particularly within the Ecodesign Directive and industry emission standards. It should synchronise its product standards testing mechanisms with new, more effective methods being implemented by the European Commission.

Conclusion

The government has shown praiseworthy ambition in its recently published clean growth strategy, particularly on the growth of offshore wind, electric vehicles and home energy efficiency. Sustaining the UK's climate leadership and achieving these goals at least cost to consumers will require, before the exit day, the full conversion of EU law into domestic law via the Withdrawal Bill and, in the future, greater collaboration with the EU, our largest energy trading partner.⁶ The UK's importance in this sector can be leveraged to sustain significant mutual benefit, and to shape the EU's future regulatory environment, while creating sufficient flexibility for the UK to operate through its own innovative decarbonisation policies.

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Endnotes

¹ Drax, November 2017, *Electric insights quarterly*

² Select committee on the European Union, October 2017, *Oral evidence: Brexit: energy security*

³ Green Alliance, July 2017, *Negotiating Brexit*

⁴ The EIB has provided around £10 billion in finance from 2011 to 2017 to build energy infrastructure in the UK, which is 2.5 times the funding from the Green Investment Bank in the same period.

⁵ OECD, November 2016, *The Paris climate agreement: what implications for trade?*

⁶ Sixty four per cent of low carbon goods with a UK trade deficit are imported from the EU and 55 per cent of low carbon goods with trade surplus are exported to EU.

Greener UK is a group of 13 major environmental organisations, with a combined public membership of over eight million, united in the belief that leaving the EU is a pivotal moment to restore and enhance the UK's environment.

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