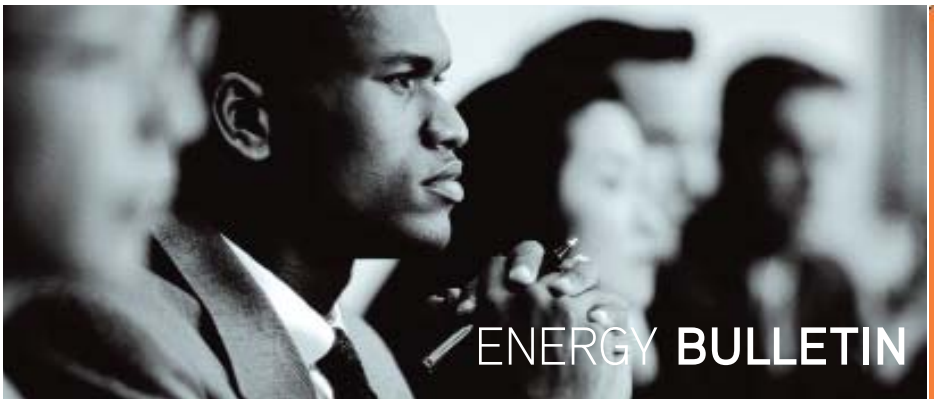

martineau

ENERGY EFFICIENCY - IS THERE MORE TO BE DONE?

This is the second in a series of bulletins on aspects of the recently announced BERR Consultation on the UK's Renewable Energy Strategy.

Previous bulletins have covered, and future issues will cover:

- Renewable Heat
- Centralised Energy
- Decentralised energy
- Transport
- Bio-energy

Any strategy on renewable energy must include somewhere a section on energy efficiency. This is because energy efficiency measures are generally cheaper than the costs of building new renewable supply, and reductions in energy demand - whether at the individual, business or public sector level - therefore have the potential to reduce the amount of renewables needed to be installed to meet new capacity targets.

Indeed, in its latest consultation on the UK's Renewable Energy Strategy published in June, BERR estimates that the energy efficiency measures already in place - agreed and set out in the 2007 Energy White Paper - will reduce demand by 152TWh, equivalent to 8% of the business as usual figure in 2020. According to BERR, this will displace around 20TWh of renewable energy which would otherwise be required to meet 2020 targets.

However, energy efficiency is multi-faceted, in that it has a key contribution to make in various policy areas. Notably:

- carbon reduction - energy efficiency is one of the most cost effective means of reducing emissions
- costs - increasing energy efficiency and hence productivity can contribute to reducing exposure to high energy costs
- fuel poverty - by improving the energy performance of homes through energy saving measures, households can be taken out of fuel poverty.

Policy backdrop

The contribution which energy efficiency can make towards our energy and climate change goals has been recognised for some time now. The UK government produced an Energy Efficiency Action Plan back in 2004, and the UK's Climate Change Programme of 2006 also highlighted the key role of energy efficiency. Further energy efficiency measures were introduced in the 2007 Energy White Paper.

Impetus was given by the EU Commission's Action Plan for Energy Efficiency which was published in late 2006 in response to the alarming statistic that Europe wastes at least 20% of its energy due to inefficiency. The Action Plan set out a package of measures designed to put the EU on track towards saving 20% of its energy by 2020. Building on existing EU energy efficiency legislation - for example around energy performance of buildings, efficiency of boilers and labelling of appliances - the plan identified 10 priority actions (- see box).

EU priority actions:

- Performance standards and labelling of products
- Building performance and low-energy houses
- More efficient power generation and distribution
- Fuel efficiency of cars
- Finance for energy efficiency investments
- Energy efficiency in the new EU Member States
- A coherent use of taxation
- Awareness
- Energy efficiency in cities
- Energy efficiency worldwide

This latest BERR consultation document highlights the current key policies to reduce energy consumption in the UK, by reference to three sectors - household, business & public sector and transport.

Household

At the household level, policies and

initiatives are two pronged.

Firstly, Building Regulations will continue to introduce ever tightening energy efficiency standards for new homes, with the aim that all new homes will be zero carbon by 2016. And Energy Performance Certificates - providing information on the energy efficiency of homes - will be required for all homes to be sold or rented from October 2008.

Household energy consumption has increased by 28% since 1970, due to:
- increasing household numbers
- rising income
- lifestyle changes (eg increased numbers of appliances)

Still rising at 1.5% per annum

Secondly, the role of energy suppliers is undergoing a transformation - as heralded in the 2007 Energy White Paper - from suppliers of a commodity (electricity and gas) to energy services companies, embracing the full range of energy efficiency goods and services. The key measure on suppliers - the Carbon Emissions Reduction Target (CERT) - was introduced in April this year to replace the Energy Efficiency Commitment. It requires energy suppliers to deliver low carbon and energy efficiency improvement measures to households to the tune of around £2.8 billion of investment over the period to 2011.

"Any strategy on renewable energy must include somewhere a section on energy efficiency."

Business & Public Sector

The flagship policy measure here is the EU's Emission Trading Scheme, which operates as a mandatory carbon emissions cap and trade scheme applying to the power sector and high energy intensive industry. Controversial in its early phase, the scheme entered its second phase in January this year, and due to rigorous national emissions caps this time around is expected generate a clear and forward looking price for carbon, and in so doing create a financial incentive on those businesses caught by it to reduce their energy usage and in turn their emissions.

Based on this scheme, a second cap and trade scheme - just for the UK - will launch in 2010. This scheme - called the Carbon Reduction Commitment - is also mandatory , and will cover around 5,000 non-energy intensive business and the public sector; essentially anyone with an annual half-hourly metered electricity supply above 6,000 MWh. Those caught will need to acquire allowances to match their energy use, and like those caught by the EU Emissions Trading Scheme will be faced with a sharp financial incentive to reduce energy consumption. A consultation from Defra on the detailed rules for the scheme are expected later this year.

Energy efficiency is also encouraged through a an index linked taxation measure - the Climate Change Levy. This tax, which applies only to non-domestic consumption, is subject to an 80% reduction if companies sign up to Climate Change Agreements via industry trade associations, which require a range of energy efficiency measures to be implemented.

Public sector initiatives:
- voluntary emissions targets for the government estate (30% reductions by 2020)
- full participation in the CRC (including all central government departments regardless of size)
- carbon efficiency target for all new government cars
- new funding for energy efficiency work in public sector
- zero carbon goals, including all new schools from 2016

Like the household sector, non-domestic buildings are also now subject to energy efficiency standards. Energy Performance Certificates will be required on sale for all non-domestic buildings by the end of the year, and the government has a stated ambition that all new non-domestic buildings will be zero carbon by 2019.

Transport

The transport sector is always the difficult egg to crack when it comes to energy efficiency, because transport usage is so inextricably linked to social development.

Nonetheless, for vehicles, energy efficiency is being encouraged in the UK through the controversial banded Vehicle Excise Duty proposals, and at an EU level by the European Commission, which has an overall objective of limiting average CO2 emissions from new cars to 120g/km by 2012. This objective, however, is unlikely to be achieved by the current system of voluntary agreements between the Commission and

the Association of European Automobile Manufacturers, which has lead to calls for binding limits to be placed on car manufacturers. The Commission has taken a tough stance, proposing a binding 130g/km limit by 2012, with the 10g/km shortfall between the Commission's overall objective and its binding emissions limit to come largely from measures such as eco-tyres, low energy air conditioning and increased use of biofuels. Despite hard lobbying by the industry, EU legislation is proposed later this year to confirm the 130g/km target for 2012.

There seems no doubt, however, that behavioural change in transport habits will not come about without major investment in public transport, especially in and around our major cities.

What next?

So what are the next steps - what more can be done?

Well, the BERR Consultation document points to a number of upcoming initiatives and policies, but it has little new to say.

On homes, as we pointed out in our previous bulletin on renewable heat, aspirations and mandated targets in relation to new buildings is not the whole picture; far from it. For the foreseeable future, most of us will still be living in existing building stock. This places a large onus on the energy suppliers to refine their service offerings and move away from a business model which, as a supplier of a commodity, rewards them with greater revenue as consumption increases.

So far as business and the public sector are concerned, the government has already set out its stall in terms of favouring a market based approach via cap and trade schemes. It is clearly pinning its hopes on the new CRC to deliver savings, and has signalled its clear intent to set an ambitious cap and in time to broaden the coverage of the scheme to a greater number of business - possibly by reducing the 6,000 MWh limit to 3,000 MWh as first proposed. It will also seek to encourage trading between the the CRC on the one hand and Climate Change Agreements on the other. At the same time, the government will be pressing for a tougher cap for the EU Emission Trading Scheme when it starts its third phase in 2013.

Perhaps the government is saving its best ideas for a wide ranging consultation on options for further energy efficiency measures which is expected in the Autumn. This might explain why such a key policy area merits a miserly 11 pages in a document running to nearly 300 pages.

This Brief aims to update you on legal issues of concern or interest. It is not a substitute for taking specialist advice in individual cases. For more information about these or any other issues please Andrew Whitehead, Partner on: T: 0870 763 1528 or E: andrew.whitehead@martineau-uk.com.