



Department for
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& Industrial Strategy

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Dear Chair and Comptroller & Auditor General,

RESPONDING TO BRITISH STEEL'S REQUEST FOR GOVERNMENT SUPPORT TO HELP MEET THEIR 2018 EU ETS COMPLIANCE REQUIREMENTS

After careful consideration, the Department for Business, Energy and Industrial Strategy (BEIS) has taken the decision to provide British Steel Ltd (BSL) with a short-term Bridge Facility of EU Emissions Trading Scheme (EU ETS) allowances, valued at around £120m, to help the company meet its 2018 emissions obligations.

These allowances have been purchased and then surrendered, via BSL's Operator Holding Account, to the EU Surrender Account. This has occurred before the 30th April compliance deadline to surrender allowances for the 2018 reporting year, thus enabling BSL to meet its environmental obligations under the EU ETS and avoid any subsequent penalties that would otherwise have resulted from non-compliance.

The Bridge Facility has been legally protected by a Deed of Forfeiture (DoF) in respect of BSL's 2019 free allocation of EU ETS allowances. This Bridge Facility will be repaid, via the DoF, upon BSL's allocation of 2019 free EU ETS allowances.

The Department signed this agreement with BSL on 24 April, but, given its market sensitive nature has waited until the EU ETS compliance transactions under this agreement have been completed before reporting it to Parliament.

It is my personal responsibility as Accounting Officer to ensure that the Department's use of resources is appropriate. This is clearly an exceptional proposal which falls outside the ordinary course of business and as such I believe that it merits additional transparency and scrutiny. I have therefore set out a summary of my Accounting Officer assessment of this proposal below, from which I have removed all commercial or other sensitive material relating to the company and its shareholder.

Background and context

The EU ETS requires major energy-intensive businesses to give up from their account one allowance for each tonne of verified carbon dioxide (or equivalent) emitted at the end of each compliance year. These allowances must be surrendered for compliance purposes by 30 April each year. Given EU Exit, the compliance deadline for UK companies to surrender allowances for the 2018 reporting year was initially moved forward to 15 March 2019 to ensure that the date fell before the UK left the EU. This date has subsequently been moved back to 30 April 2019 as the country's departure from the EU has been delayed. The Department first informed companies of their revised obligations in November 2017 and we have continued to provide regular reminders since.

Given the uncertainty around when the UK would ratify a withdrawal deal with the EU, the EU Commission took the decision (in December 2018) to suspend EU ETS allocations for the UK from 1 January 2019. BSL, like some other scheme participants, has been using future years' free allocations of allowances to meet previous years' compliance. The UK suspension meant that BSL was unable to do this and now needed to buy allowances on the open market in order to meet their 2018 compliance requirements. Should it have failed to meet its carbon obligation then it would have been liable to a significant and immovable fine from the Environmental Agency. The company therefore requested support from Government to help them to manage this situation and to avoid a major and avoidable impact on the business.

There are a number of reasons to justify providing British Steel with support in this exceptional situation. The Government has been clear that companies in the UK should comply with the requirements of the ETS regime. British Steel is a significant employer and the fine for non-compliance could have a significant and regrettable impact on individuals in the local area, as well as businesses in the broader supply chain. There would be significant additional costs for the Exchequer in this scenario. British Steel is also a major supplier of a range of steel products, such as high quality steel rails which it provides to Network Rail and ScotRail, among other rail companies.

Assessment against the Accounting Officer standards

Regularity

The Bridge Facility is delivered under Section 7 of the Industrial Development Act, the use of which requires that the views of the Industrial Development Advisory Board (IDAB) are sought. I have judged that this proposal is novel, contentious and potentially repercussive in nature and as such HM Treasury consent is also required. Both have provided their views and are content for this proposal to proceed.

Following discussions between the Department and the company, analysis by the Department and its legal advisers, and independent commercial advice; I am satisfied the bridging facility that has been negotiated is commercial and that it is on terms that a private investor could have been prompted to make (this includes legal and contractual protections, as well as pricing). As such, I am content that the proposed bridging facility is consistent with State Aid rules.

The Department has agreed a funding mechanism for this proposal with HM Treasury.

Propriety

The Department has taken steps to mitigate a number of key risks associated with this proposal and to help ensure that it protects value for money for the taxpayer as best as is possible, noting that the

risk cannot be eliminated entirely. These include ensuring that there is adequate security over the receivable and that there is a robust mechanism in place to protect Government against EU ETS price risk.

I have judged that this proposal is novel and contentious on the basis that this is a new approach for the Department and that it could provoke public reaction. It also has the potential to be repercussive as there is a risk that it raises expectations that the Government will intervene to assist companies facing similar issues in the future. *Managing Public Money* explicitly states that HM Treasury consent is required for policies which are considered novel, contentious and repercussive. Treasury have given their agreement for this proposal to proceed.

Value for money

The Department's value for money assessment shows that the DoF offers value for money to the taxpayer. This is based on a conservative view of the likely benefits and the assumption that the legal protections relating to the security provided by the future release of EU ETS allowances are implemented, such that the overall risk of Government not recovering its funding is low. IDAB have agreed with this assessment.

Feasibility

The Bridge Facility has been successfully delivered to a tight deadline and within the financial parameters set.

Conclusion

In the unwelcome situation that we find ourselves in, and with the legitimate public policy goals set out above, the proposed policy option is eminently justifiable. I am confident that the specific mechanism chosen, of acquiring allowances to be surrendered via BSL's operator account for 2018 compliance, and agreeing with BSL to forfeit the right to future allowances via a prior DoF, offers the best available security and hence the best way to achieve these goals at the lowest cost and risk.

The Department will continue to monitor this situation going forward and I will provide a further update if anything material changes.

Yours faithfully



Alex Chisholm