



House of Commons  
Environment, Food and Rural  
Affairs Committee

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**Biofuels:  
Government Reply to  
the Committee's  
Report**

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**Third Special Report**

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## The Environment, Food and Rural Affairs Committee

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### Committee staff

The current staff of the Committee are Gavin Devine (Clerk), Fiona McLean (Second Clerk), Dr Kate Trumper and Jonathan Little (Committee Specialists), Andy Boyd and Louise Combs (Committee Assistants), Anne Woolhouse (Secretary) and Rebecca Flynn (Intern).

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# THIRD SPECIAL REPORT

The Environment, Food and Rural Affairs Committee reported to the House on *Biofuels* in its Seventeenth Report of Session 2002–03, published on 6 November 2003 as HC 929-I. The Government's Reply to the Report was received on 14 January 2004.

## Government response

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### Introduction

The Government welcomes the EFRA Select Committee report about the range of issues affecting biofuels policy.

Biofuels have an important role in supporting the Government's objectives for sustainable development and protecting the environment. The Energy White Paper makes it clear that transport biofuels have a key role to play in reducing carbon dioxide emissions. Biofuels (especially tomorrow's biofuels) offer the prospect of moving to a truly low carbon transport economy. Biodiesel and bioethanol are supported through duty rate cuts because of the environmental benefit they offer in terms of reducing carbon dioxide emissions compared to conventional fuels. Biofuels can also make a contribution to better fuel security, to farm diversification and supporting rural jobs and areas.

In common with other policies and issues which are wide-ranging in their impact on the UK, there are a number of Government Departments with an interest in biofuels. Lead responsibility depends on the particular aspect of policy. The Treasury and HM Customs and Excise lead on issues regarding taxation and other fiscal aspects. Defra has responsibility for the role biofuels can play in sustainable development, climate change, air quality and rural issues, and the promotion of agricultural feedstocks to produce biofuels. The Department for Transport (DfT) has responsibility for the use of low carbon fuels for transport purposes and is co-ordinating the assessment of the energy and other implications of the large scale use of biofuels. DfT is also co-ordinating the implementation in the UK of the EU Biofuels Directive. The Department of Trade and Industry is responsible for renewable energy policy and co-ordinated overall implications of biofuels for the Energy White Paper.

There is strong liaison across the departments both at Ministerial and official level to ensure co-ordinated policy. Ministerial involvement is through the Ministerial Committee on the Environment, the Ministerial Sub-Committee on Energy Policy, the Ministerial Low Carbon Group, the Ministerial Group on the Implementation of the Energy White Paper and ad hoc meetings.

## Conclusions and recommendations

### Recommendation 1

**We too would like to see how Government balances the considerations of the environment, the economy and society in developing its policy on biofuels. (Paragraph 13)**

In December, the Pre-Budget Report 2003 set out the rationale underpinning support for transport biofuels in its Alternative Fuels Framework (see Box 1). This outlined a clear, systematic set of principles applying to decisions in this sector, with environmental, social and economic considerations all taken into account in determining the level of support for these fuels.

The Government has always made it clear that the overriding consideration when determining fuel duty levels for alternative fuels was evidence of environmental benefit; the framework confirms this as the principal basis for decisions placing environmental benefit at the heart of Government policy on support for alternative fuels. It also provides an unprecedented level of transparency to the market about future rates for biofuels with its commitment to a rolling three-year period of certainty on the differentials in duty rates for alternative fuels.

### Recommendation 2

**The Treasury should publish clear data showing the current and future levels of taxpayer subsidy aimed at promoting a renewable energy industry. Such information would enable a better informed debate to take place as to how a broad based renewable strategy should develop. (Paragraph 26)**

As far as duty incentives for biofuels are concerned, the Government already publishes the costs, in terms of revenue forgone, in the Financial Statement and Budget Report. The Government has created a substantial support programme for renewable energy worth £348m over the four years from 2002-3. Details of these initiatives are on the Sustainable Energy Policy Network's website at:

<http://www.dti.gov.uk/energy/sepn/index.shtml>

### Recommendation 3

**Although increasing the use of biofuels may not be the most efficient way to reduce greenhouse gas emissions when considering the whole economy, we agree with the Treasury that all sectors should make a contribution towards reducing the United Kingdom's emissions. Biofuels offer one attractive means of doing so for transport, although other measures such as engine efficiency and managing the demand for road transport are also important. (Paragraph 28)**

Diversity of energy sources is an important element of our overall energy policy. In order to meet the Government's targets to reduce greenhouse gas emissions, we are

**Box 1: Extract from the 2003 Pre-Budget report (Cm 6042, p155), 10 December 2003**

**Alternative Fuels Framework**

The Government recognises the contribution that alternative fuels can make in delivering environmental objectives. This is reflected through the significant support that the Government has given to the sector over recent years.

With this framework, the Government goes further. The purpose of the framework is to ensure that policy continues to reflect the environmental benefits that alternative fuels can deliver and to establish a clear rationale for decisions on Government support. This approach is based on the principles set out in the Treasury document: 'Tax and the Environment: Using Economic Instruments', published alongside the 2002 Pre-Budget Report. The principal application of this framework is to policy on duty differentials for alternative fuels but the approach is equally relevant to decisions on the full range of potential economic instruments.

**Statement of principles:**

Policy must be environmentally sustainable. Levels of support should reflect the full environmental impact of the fuel.

Policy must be economically sustainable. The Government should not support an industry whose long-term survival is dependent on excessive levels of subsidy unjustified by environmental benefit.

Policy must be socially sustainable. Support should reflect broader considerations of social impact and fairness.

Policy must be affordable and provide value for money. Where fuels fulfil the criteria set, support will be given where it is both cost effective and affordable.

**The Principle of Certainty**

The Government recognises the importance of providing as much certainty as it can on duty differentials, to help provide the necessary stability, confidence and market conditions for investors. The Government will therefore commit to a rolling three-year period of certainty on the differentials in duty rates for alternative fuels.

**The Environmental Case:**

The central priority will continue to be on environmental gains, with the emphasis being on quantified benefits that are based on the life-cycle carbon performance of the fuel. Recognising the comparatively high cost of carbon reduction in the transport sector, the Government will nevertheless seek to meet key environmental objectives in a cost-effective way; and

The Government will take account of fuels that have additional environmental benefits by, for example, improving air quality and reducing waste.

**The Economic and Social Case:**

The Government will only offer support beyond that justified by environmental benefit if there is clear evidence that this support will result in enhanced future benefit;

In assessing the level and types of support available, the Government may also take into account other benefits to the economy arising from the use of alternative fuels; and where there is a direct link to Government priorities, and clear and well-established evidence of benefit.

**General Application:**

This framework sets out principles, which can be applied to all types of support for the take up of greener road fuels. Duty incentives alone can be a very blunt instrument, so where there are clear reasons for incentives to be more focused on specific objectives, the Government will also consider other means of support, such as capital incentives, grants or regulatory solutions which may be more suitable, better targeted and better value for money.

promoting a package of integrated policies supporting a broad range of renewable energy sources including liquid and solid biofuels and wind, solar, wave and tidal power.

As the Energy White Paper makes clear, the transport sector has a key role to play in reducing carbon emissions. Biofuels are one possible way of improving the carbon efficiency of transport. As the Alternative Fuels Framework makes clear, the Government already recognises the high cost of carbon abatement in the transport sector, reflected in the existing levels of support in place for biodiesel and bioethanol.

The Government recognises that all sectors of the economy must play their part in reducing climate change emissions and we welcome the Committee's endorsement of this approach.

#### **Recommendation 4**

**There is not yet clear enough evidence of what will be the impact of expanding biofuels production on habitats and biodiversity here and elsewhere: but the prospect of greatly increased planting of autumn-sown oilseed rape or winter wheat causes understandable concern. We call on the Government to commission a full scientific study to assess the effects on biodiversity of expanding the cultivation of biofuel crops. (Paragraph 32)**

Defra's Central Science Laboratory has already assessed the impact of biofuels on habitats and biodiversity in the UK. Their assessment is that biofuel production from a broad mix of arable crop feedstocks will have a neutral effect on the farmed environment. Direct replacement of cereals with oilseed rape would have no effect. Any replacement of spring sown break crops by an expanding winter oilseed rape or cereal area would have a negative effect on crop diversity and farmland birds. Growing biofuel crops on un-cropped land or replacement of natural-regeneration set-aside with biofuel crops would on balance be environmentally detrimental, due to the resulting increase in intensification of nitrogen and pesticide use and reduction in habitat diversity. Environmental damage could be minimised by avoiding large-scale block-cropping and introducing a percentage of non-crop habitat. In the longer term, as technology improves, cereal straw and other arable crop wastes could provide raw material for bioethanol production without significantly affecting the farmed environment.

However, the Government recognises the potential value of further work on biodiversity. We shall undertake this alongside the work on conservation (recommendation 13).

These issues are also being considered in the Government's assessment of the overall impacts of significant use of biofuels and/or hydrogen as transport fuels, which is due to be published in early 2004. Details are on the Department of Trade and Industry's website at: [www.dti.gov.uk/energy/sepn/futuretransport.shtml](http://www.dti.gov.uk/energy/sepn/futuretransport.shtml). To contribute to this assessment, the Government has commissioned further research on the environmental

impacts of biofuels from the Institute for European Environmental Policy (IEEP) and the National Society for Clean Air (NSCA).

#### **Recommendation 5**

**While we welcome the development of new markets for crops and opportunities for farmers to diversify and respond to market demands, we have not seen enough evidence to allow us to make an accurate assessment of what impact increasing the use of biofuels would have on farm incomes. We recommend that Defra, as a matter of urgency, carry out an economic appraisal of the effect that a UK-based biofuels industry would have on farming. (Paragraph 40)**

The Government accepts this recommendation. Some work has been undertaken on the production costs of biofuels and the impact of a range of feedstock prices but we will carry out a fuller economic appraisal of the effect that a UK-based biofuels industry would have on farming.

#### **Recommendation 6**

**Estimates of the number of jobs that would be created by a UK-based biofuels industry vary widely. The extent to which a domestic industry would boost rural prosperity is of crucial importance in determining whether home-grown or imported biofuels should be used. We call on all parties involved to publish robust models with which to back up their claims. (Paragraph 44)**

The Government fully endorses this recommendation. Defra's Central Science Laboratory has estimated that about 2 farming jobs are created or sustained for each 1000 tonnes of biodiesel produced and 5.5 farming jobs are created or sustained for each 1000 tonnes of bioethanol produced. In processing and blending, a 100,000 tonne biodiesel plant is estimated to create 62 jobs at the plant itself. A similar bioethanol plant is estimated to create 66-83 jobs at the plant. We will publish the detailed workings for these estimates and we look forward to an opportunity to share information with others.

#### **Recommendation 7**

**Whatever targets the Government chooses to set under the Biofuels Directive, it must make firm decisions quickly if farmers and processors are to be able to plant crops and build processing plant in time to meet the targets. (Paragraph 46)**

The Department for Transport intends to consult in Spring 2004 on the Government's plans for implementing the EU's Biofuels Directive. The Directive requires the UK to set indicative targets which the Government believes should be set at a realistic level appropriate to the UK's own circumstances.

#### **Recommendation 8**

**We share the Treasury's view that a greater level of duty derogation on biofuels introduced now would be more likely to encourage imports of biofuels than the development of domestic production. (Paragraph 49)**

Most biofuels are grown for consumption in the country in which they are produced, and there is consequently a scarcity of supply for international markets. It is therefore anticipated that there will be limited international trade in refined liquid biofuels in the medium term. However, the Government has always considered that a higher level of duty derogation on biofuels could encourage imports of biofuels.

Ethanol can be procured cheaply on international markets. However taxation and distribution costs mean that it is unlikely that the UK would be flooded with biofuel imports. It has been estimated that Brazilian ethanol landed in the UK, after accounting for blending and retail margins, would be in the region of 10p/l cheaper than UK produced bioethanol from wheat and sugar beet. However, application of import duty for denatured alcohol (of 6-7 p/l) would bring costs closer in line with that of UK produced bioethanol. Other EU Member States with lower duty rates for biofuels than the UK are likely to be higher priority targets for imported supplies. This would change should the level of duty incentive in the UK start to exceed that offered elsewhere in Europe.

#### **Recommendation 9**

**If the Government decides to increase the support available for the production of biofuels, any such support must be designed to achieve the underlying policy goal it has set. For example, an increase in the duty derogation may encourage imports, but this may not matter if the prime policy goal is to reduce emissions. If the Government wants to further its rural development objectives as well, a combination of other instruments such as grants to support capital investment may be necessary. (Paragraph 50)**

As the response to recommendation 1 makes clear, capturing the environmental benefits of biofuels is the principal policy reason for Government support with duty incentives. Other considerations such as economic and social factors, though secondary, are also taken into account in the Chancellor's fiscal decisions.

It is not the Government's intention to establish industries based on excessive Government subsidy not justified by clear and well-established evidence of environmental, social and economic benefits. Where fuels fulfil the criteria set, the Government is determined to achieve the best outcome for both the tax-payer and the economy as a whole. Support will therefore be given where it is both cost-effective and affordable.

The Government welcomes the Committee's recognition that simply increasing the duty incentive might not encourage the development of a UK biofuels industry and could simply attract more imports. Support for producers of biofuels and feedstocks already exists:



Regional support grants for capital investment in production plants are already available through the Regional Development Agencies (RDAs). It is largely a matter for the RDAs about how these are spent;

Payments of €45 per hectare will also be available to UK growers of energy crops following the agreement for reform of the Common Agricultural Policy.

One of the other key issues that the Government has focused on is the importance to the industry of future certainty on duty rates for alternative fuels. Recognising this need for certainty and reflecting the commitment the Government has to the biofuels sector, the Alternative Fuels Framework published in the Pre Budget Report 2003 included an unprecedented commitment by the Government to a rolling three-year period of certainty for duty differentials. Subject to affordability, this approach is designed to strike the right balance between providing a high degree of future certainty for these fuels and ensuring that adequate medium term flexibility is possible to reflect the fuels' environmental and other benefits.

#### **Recommendation 10**

**If the Treasury is not prepared to subsidise the biofuels industry directly, it should evaluate different strategies for minimum cost introduction of biofuels, while making the price attractive to consumers. (Paragraph 54)**

The Government has already made it clear that it is only prepared to subsidise the industry up to the point justified by the fuel's full range of benefits. The Government will only offer support beyond that where there is clear and well-established evidence that this support will result in enhanced future benefit.

The Government continues to explore innovative options for supporting these fuels, including the option of focusing the duty regime on input taxation in addition to product-based taxation. This would allow the Government to tax different fuels according to the type of feedstock or process used, allowing support to be better focused on the most economic and environmentally beneficial production plants.

The Government fully agrees that fiscal incentives should always be considered alongside alternative methods of support, such as capital incentives, grants or regulatory solutions. The Government keeps all types of support under review.

It is also important to note that the Energy Products Directive forbids the granting of fuel duty incentives in excess of a biofuel's additional production costs, meaning that retailers will have limited opportunity to price biofuels below the cost of conventional fuels. In such instances of price neutrality, evidence from the market suggests that consumers find the environmental properties of biofuels sufficiently attractive to influence their purchasing decision.

**Recommendation 11**

**It is clear from the evidence we took from Defra and the Treasury that the departments involved do not speak with one voice. In a policy area such as this it is inevitable that different departments will each have a legitimate interest and perhaps different priorities. However, we deplore the fact that the Government has not nominated any one Department to lead on biofuels and consider that this is a prime reason for the slow progress that has been made in this area. (Paragraph 56)**

As the Committee notes, it is inevitable that different Government Departments have, and will continue to have, an interest in various aspects of biofuels policy. This is not unique to biofuels - there are other policy areas where no single Government Department has overall lead responsibility. The Government does not accept that current arrangements have slowed down progress. Government Departments work extremely closely in developing policy on this issue, helping to ensure that the multi-dimensional nature of the biofuels sector is properly reflected in policy, and that proper consideration is given to the full range of relevant environmental, social and economic factors.

**Recommendation 12**

**The debate about the need for Government support for domestic biofuels production has been going on for some time without reaching a firm conclusion. The Government's biofuels policy still appears to be muddled and unfocussed: it has expressed support for biofuels but the mechanisms used to promote their use have had little effect so far. (Paragraph 57)**

The Government does not accept that its policy is muddled and unfocused or that its support for biofuels has had little effect. In particular, the Government emphasises that the duty incentive for biodiesel was only introduced in July 2002 and the duty incentive for bioethanol will not come into effect until January 2005 when it is hoped that British companies will be ready to produce it for the UK market. It is too early to judge how far the policy has been a success but there have been some encouraging results from biodiesel already. Since the duty incentive was introduced in July 2002, production has risen steadily to over 2 million litres a month at present and the market is still growing. Production is expected to accelerate further, both as the new production plants which are currently planned come on stream, and as other outlets for waste vegetable oils cease to be available. Companies are now looking to produce biodiesel from UK-grown oilseed rape.

From 31 October 2004, the UK will be introducing a ban on the use of used vegetable oils as animal feed, which will lead to a further sizeable increase in the quantity of economically priced waste vegetable oil being made available to biodiesel processors. There are well-developed plans to build more production plants to take advantage of this and other opportunities, such as the use of tallow as a feedstock, made possible by Government support for the sector.

The Department for Transport will shortly be seeking views on a draft transposition strategy for the Biofuels Directive. This will include targets for the level of biofuels use in the UK for 2005 and 2010, giving further clear signals about what the Government believes is an appropriate level of biofuels consumption taking all factors into account.

### **Recommendation 13**

**We encourage Defra to work closely with the statutory conservation agencies to find ways to maximise the benefits biofuels can offer to conservation and to minimise the negative impacts associated with some biofuel crops. If imported crops, or fuels derived from them, are to furnish a significant proportion of the biofuels used in the United Kingdom, we encourage Defra to develop cost effective ways of auditing their environmental impact in the countries in which they are produced. (Paragraph 60)**

The Government accepts that its aim should be to put in place measures, where practicable, to encourage best environmental practice. The Government will therefore consider, together with the statutory conservation agencies, ways to maximise the benefits biofuels can offer to conservation and to minimise the negative impacts associated with some biofuel crops.

However, auditing the environmental impact of biofuels in the countries in which they are produced is extremely problematic and it is unlikely that a cost-effective and robust system of regulation could be introduced. The Government therefore does not accept this recommendation. It would be very difficult to assess the environmental impact of imported fuels in sufficient detail to give an accurate picture or a comparison between different systems. Any biofuel shipped to the UK would be bulked from a range of individual sources and producers. It would not be possible to guarantee any environmental impacts for a particular imported batch of fuels or raw material without auditing every individual producer. In any case, any attempt to refuse imports on the basis of perceived or measured environmental impacts could be seen as a barrier to free trade and would almost certainly lead to conflict with the World Trade Organisation.

### **Recommendation 14**

**Defra has responsibility for championing sustainable development within Government. The development of a sensible biofuels policy could provide a good showcase for the Department's thinking in this area. Defra should set out how the various environmental, economic and social costs and benefits represented by the different options have been weighed against one another. This would allow the Department's stakeholders to judge the policy fairly. At present it appears that the Government is still testing the waters with regard to supporting the development of a domestic biofuels industry and the current level of support reflects this ambivalent attitude. The Government should recognise that compared to other forms of renewable energy, either imported or domestically produced, agriculturally derived biofuels do represent a predictable and secure source of energy and this fact should be given due weight in deciding future policy in this area. (Paragraph 61)**

The Government accepts this recommendation and Defra will set out the various environmental, economic and social costs and benefits that Defra has taken into account in formulating its policy on biofuels as part of its sustainable development programme.

The area of biofuels policy has been the subject of a great deal of well informed research and a considerable body of work has been undertaken in recent years, both by Government and outside bodies, into the environmental, economic and social impacts of biofuels. Building on this, further research is underway to inform the Government's policy for implementation of the Biofuels Directive in 2004.

Department for Environment, Food and Rural Affairs  
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