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Treasury Chambers, Parliament Street, SW1P 3AG

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Secretary of State
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Dear David,

**GOVERNMENT RESPONSE TO ENERGY SELECT COMMITTEE REPORT ON THE
POLICY IMPLICATIONS OF THE GREENHOUSE EFFECT**

I enclose drafting comments on the reply that you are intending to send to the Energy Select Committee. Our main concern in commenting has been to provide a consistent explanation in the text of when Government action is needed and when the market solution is to be preferred. Our object should be to allow the market to operate freely unless there is some divergence between the private and social costs.

Copies of this letter go to the recipients of yours.

MALCOLM BUCKLER
Private Secretary

NOTE OF DRAFTING COMMENTS

Paragraph 3, line 8 - delete "eventually".

Paragraph 1.2, line 2, delete "relatively". . . Although UK production of greenhouse gases is small, relatively, i.e. relative to other countries, and to our GNP, it is significant.

Paragraph 1.8, delete the 2nd and 3rd sentences. It is not possible to disown commitments the Government made earlier, quite as bluntly as is done in this draft.

Paragraph 2.7, we were a little surprised to read the strong endorsement of wood as a fuel. While it is true that increasing the efficiency of wood burning would be beneficial, substitution towards wood as a fuel is less obviously beneficial, unless it is also associated with improved husbandry.

Paragraph 3.2, if the private sector decided that gas imports were more economic at some point in the next 10 years, we would not have any objection to the proposal for a connection to the European gas grid. We therefore suggest deleting "existing UK gas reserves are sufficient to take us into the next century and" and replace that with "at current gas prices the need for a European connection to allow imports in large quantities is not clear."

Paragraph 3.7, please redraft the second sentence to read "These estimates are being used as the basis for the Department's resource planning for renewables R&D..." We should not refer to the public expenditure negotiations at this stage.

Paragraph 3.8, the second sentence is rather strong. And does not seem to take account of the use of land-fill gas, described earlier in the paper, or of solar panels.

Paragraph 4.1, the effect of measures to promote energy efficiency on our international competitiveness would not necessarily be "profound", for example Japanese experience has been positive. The overall effect on international competitiveness depends on whether price rises are disproportionately in the traded goods sector. At the moment we have no analysis of this point.

Paragraph 4.3, delete the second sentence. This is inconsistent with the explanation of the role of markets given in paragraph 5.2. It is important that a consistent framework is presented in the note in which it is explained that it is only when the market fails to align prices with true resource costs that Government action is justified, for example to internalise external costs. This may involve regulation, but the key point is that Government has to intervene to set the framework within which market forces operate freely. A similar point arises on paragraph 4.7 in the second sentence. Since peoples' rationality is bounded, the Government may need to address divergences between private and social costs, albeit carefully.

Paragraph 5.2 the final sentence appears to be somewhat rhetorical.

Paragraph 5.4, insert "producers' and " before "consumers'".

Paragraph 5.2 the cross reference to paragraph 3.10 should presumably be paragraph 4.5.

Paragraph 5.5, please could we refer here to "proposals for fiscal measures...".

Paragraph 6.3, the final sentence is somewhat tautologous. Significant costs might be economically punitive, but not all measures beyond those currently being pursued would necessarily be so.