DIAGEO RESPONSE TO THE SCOTTISH PARLIAMENT’S ECONOMY, ENERGY AND TOURISM COMMITTEE INQUIRY INTO THE SCOTTISH GOVERNMENT’S RENEWABLE ENERGY TARGETS
About Diageo
Diageo is the world’s leading premium drinks business and a top-20 FTSE 100 company. We employ more than 22,000 people worldwide, in more than 80 countries, including over 5,000 people in the UK, in more than 50 sites. Our brands include: Bell’s, Johnnie Walker and J&B whiskies as well as a range of malt whiskies alongside Smirnoff vodka, Captain Morgan rum, Baileys liqueur, José Cuervo tequila, Tanqueray and Gordon's gin, Guinness beer and Blossom Hill wines.

About Diageo in Scotland
Scotland is one of Diageo’s largest spirit supply centres responsible for producing nearly 500 million cases of leading brands of Scotch whisky and white spirits annually. Around 85 per cent of Diageo’s brands produced in Scotland are sold overseas. Diageo in Scotland currently employs around 4,000 people. Diageo operates 28 malt distilleries, one grain distillery and has a 50 per cent share in the North British grain distillery in Edinburgh. As well as engineering and technical support functions, there are extensive warehousing operations in Scotland, which store more than seven million casks of maturing spirit.

Diageo in Scotland spends over £400 million each year on goods and services with Scottish-based suppliers. The company’s brands account for over 20 per cent of Scotland’s food and drinks exports, making it the country’s largest manufacturing exporter. Each year over 200,000 people visit our 12 distillery visitor centres, generating more than £70 million for Scotland’s tourist economy every year.

Diageo also owns The Gleneagles Hotel in Perthshire, one of the world’s most coveted 5-star resorts. With three Championship Golf Courses, Gleneagles is home to the Johnnie Walker Championship and is the host venue for Ryder Cup 2014.

The company’s Scottish headquarters are in Edinburgh.

Executive Summary
The purpose of this submission is to bring to the attention of the Committee a significant challenge which has recently become apparent in the development of renewable energy projects in Scotland. This challenge relates to the Rating and Valuation system which currently exists in Scotland.

Diageo believes that the Rating and Valuation system as it currently exists in Scotland does not provide a level playing field and generates significant financial differences on the building of on-site renewable energy plants. There is evidence set out below that this can result in a renewable energy plant which wholly or mainly supplies power to the National Grid having a much lower Rateable Value than a plant producing roughly half the power but wholly or mainly for on-site purposes (a difference of over £1m in the Rateable Value in the case study cited below). Diageo believes this is a serious anomaly in the system which needs to be addressed as it creates a potential disincentive to future development of on-site renewable plants and may be considered as a significant barrier to the Scottish Government achieving its renewable energy targets.

Diageo’s environmental commitment
Diageo is recognised as one of the global corporate leaders in sustainability, scoring highly in the Dow Jones Sustainability Indices, FTSE4GOOD and the Carbon Disclosure Project. For Diageo investing in environmental sustainability is core to the future of our business. Because of this, in 2008 Diageo set itself ambitious global environmental targets including cutting carbon emissions at our production sites by 50 per cent by 2015.

Scotland has been at the forefront of Diageo’s global drive towards greater environmental sustainability and the company has invested nearly £100million to develop renewable energy with the potential to reduce carbon emissions by over 70,000 tonnes per year. In addition, Diageo has been making year on year improvements in improving energy and water efficiency, reducing waste, and addressing waste water. The main focus for Diageo in Scotland has been the development of on-site renewable energy facilities which use the co-products of the distillation process to generate renewable energy to power the distilleries. The three key projects for Diageo in Scotland are:

Cameronbridge distillery, Fife
Diageo has invested £65 million in a state-of-the-art bioenergy facility. It is one of the largest single investments in renewable technology by a non-utility company in the UK, and aims to reduce annual CO₂ emissions at the site by approximately 56,000 tonnes. It aims to provide 98% of the thermal steam and 80% of electrical power used at the distillery. The bioenergy plant is currently in the commissioning phase and will be fully operational later this year.

Roseisle distillery, Speyside
Roseisle distillery, which opened in 2010 and is the first major malt distillery to be built in Scotland for over 30 years, was built with its own on-site renewable energy plant. The majority of the co-products of distillation (draff and pot ale) are recycled on site in a bioenergy facility, helping the distillery to generate its own energy and reduce potential CO₂ emissions by up to approximately 13,000 tonnes through direct savings on fuel use for steam-raising.

Glenlossie distillery, Speyside
Diageo recently started construction work on a £6million bioenergy plant at the Glenlossie distillery in Speyside. The plant will produce steam which will be used in the operations on site. The bioenergy plant aims to reduce annual CO₂ emissions by approximately 6,000 tonnes.

GOVERNMENT’S RENEWABLE ENERGY TARGETS

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The Scottish Government’s Renewable Energy Targets

Overview
Diageo is strongly supportive of the leadership position the Scottish Government has taken on renewable energy. Diageo believes that setting ambitious targets is crucial to the transformation to a low carbon economy which the Scottish Government wishes to achieve. Diageo has set itself the ambitious target of reducing greenhouse gas emissions from its production sites around the world by 50 per cent by 2015. We are working hard to achieve these goals and we believe that our efforts will make a significant contribution towards the achievement of the Scottish Government’s targets.

Diageo has worked closely with the Scottish Government and its agencies, such as SEPA, on the development of our renewable energy projects and we value highly the strong relationship we enjoy with our stakeholders on this agenda. While there are challenges and issues which may impact on the achievability of the Scottish Government’s targets, Diageo is wholly committed to working with all of the agencies concerned towards the achievement of these goals.

In terms of other issues the Committee may wish to consider in its inquiry, Diageo has contributed to and endorses the submission from the Scotch Whisky Association, which discusses other challenges which may impact on the Scottish Government’s renewable energy targets.

Challenges – Impact of the Scottish Rating and Valuation system on on-site renewable facilities
Diageo wishes to bring to the attention of the committee a significant challenge which has recently become apparent in the development of renewable energy projects in Scotland. This challenge relates to the Rating and Valuation system which currently exists in Scotland.

It has become apparent that the current regime for business rates valuation in Scotland contains an in-built financial discrimination against renewable energy facilities which produce energy for use on-site, compared to those which supply energy to the National Grid. It means that companies, such as Diageo, which are developing renewable energy facilities for on-site use could face rates bills which are well in excess of those faced by comparable renewable energy facilities which sell their power to the National Grid. Diageo understands that this is an issue which not only affects its operations, but one which has already impacted on other companies and industries in Scotland – companies that are all making important investments that will contribute to the Scottish Government’s ambitious carbon reduction commitments.

Diageo understands that the apparent financial disparity in the system has only come to light recently as the first wave of large scale on-site renewable energy plants have come into use in Scotland and therefore been subject to rating valuations for the first time. We believe this is an inadvertent anomaly in the system which needs to be addressed, rather than a deliberate objective of Scottish Government policy.

In some respects it would appear that the legislation governing the rating valuation of such renewable energy plants requires up-dating. In particular, the Plant and Machinery legislation, as it currently exists, was effectively laid down in the mid 1980’s, and has a major detrimental impact on the rating of biomass plants, again causing an imbalance between those bio-mass plants used to produce power to the National Grid and those used to produce power for their own operational purposes, and for which an alternative basis of valuation is used.

Detailed summary of the Ratings and Valuation issue
The Rating and Valuation landscape in relation to renewable energy is complex. This section sets out the key legislative background and how it has been applied in two recent examples.

Renewable energy resources, such as biomass or Combined Heat and Power (CHP) Plants, attract a business rates liability. In arriving at an appropriate Rateable Value to apply to the plant, the Assessor has to take into consideration the current rating legislation in place.

For utility companies, such as Scottish Power, valuations are rated under the Non-Domestic Rating (Valuation of Utilities) (Scotland) Order 2005 and their valuations are based on the Receipts and Expenditure (R&E) method of valuation. One entry, covering the whole of Scotland, for each of the utility companies is made in the Valuation Roll.

For operators of wind farms and hydro energy, who sell power direct to the National Grid, the designate Assessor (in this case, the Assessor for Lanarkshire) values these subjects based on a rate of MegaWatt (MW) produced. The rates applied are based on a sliding scale depending on the amount of power produced.

For operators of biomass or equivalent plants, who produce energy, mainly or wholly for their own purpose, the Receipts and Expenditure and the rate per MW methods are deemed to be inappropriate as the power produced is not sold on to the National Grid. In these cases, the Assessor has valued these plants on the Contractors method of valuation which is based on either actual or notional costs from a Scottish Assessors Association (SAA) Cost Guide. All buildings are rateable and certain items of plant are rateable/non rateable following the Valuation for Rating (Plant & Machinery) (Scotland) Regulations 2000, as amended by the Valuation for Rating (Plant and Machinery) (Scotland) Amendment Regulations 2001. The plant and machinery that is to be valued for rating purposes is set out in the schedule to the Order.
An example of the disparity:
The E.ON Steven’s Croft biomass power plant at Lockerbie, Dumfriesshire, was valued during the 2005 Revaluation period at a Rateable Value of £500,000. It is understood this valuation was arrived at according to the rate-per-MW method.

At the same time UPM Kymmene’s (Caledonian Paper) biomass plant in Irvine, Ayrshire, which was built to power the on-site paper mill, was valued by the Contractor method and attracted a Rateable Value of £1.6m. This is despite the fact that the Caledonian biomass plant produces 24MW, around half the size of the E.ON plant’s 44MW. Following the 2010 Revaluation, the Rateable Value of the Caledonian Paper Mill bioenergy plant has risen to £2.1m.

Therefore, from the above examples, it can be seen that on site renewable plants can be liable to pay a substantially higher rates bill than that incurred by renewable plants which sell power to the National Grid.

(Note: The appropriate rates poundage is applied to the Rateable Value to arrive at their rates payment for any one financial year.)

Diageo cites these examples from the publicly available Valuation Rolls to illustrate the disparity which companies developing on-site renewable plants face in relation to the Rating and Valuation system and how it is applied. As Diageo’s own renewable energy plants are in the process of coming on stream they have yet to be subject to rating valuation. However, it is apparent from the independent advice Diageo has received that it can expect to be valued in the same way as the Caledonian Paper Mill, with likely similar resultant disparities.

Diageo recognises that the Scottish Government took steps to assist smaller renewable energy projects with the introduction of the Non-Domestic Rates (Renewable Energy Generation Relief) (Scotland) Regulations 2010, which allowed rates relief to renewable energy schemes producing less than 50kilowatts of electricity. However, this only relates to micro-generation and does not extend to industrial-scale renewable energy facilities.

Conclusion
On-site renewable energy facilities have the potential to make a substantial contribution to the achievement of the Scottish Government’s renewable energy targets and ambitions for a low carbon economy. On-site renewable energy facilities significantly reduce the reliance of industries on power from the National Grid, substituting reliance on traditional fossil fuel energy for renewable energy sources. Diageo believes that the Rating and Valuation system as it currently exists in Scotland does not provide a level playing field and generates significant financial penalties on the operating of on-site renewable energy plants. This in turn creates a potential disincentive to future development of such plants and may be considered as a barrier to the Scottish Government achieving its renewable energy targets. We ask the Committee to investigate this issue in more detail as part of its inquiry into the Scottish Government’s renewable energy targets and to explore the options for creating a level playing field for the Rating and Valuation of all renewable energy developments in Scotland.

February 2012

References

i Valuation Roll 2005

ii Valuation Roll 2005 & 2010