EXPLANATORY MEMORANDUM TO

THE CLIMATE CHANGE AGREEMENTS (ADMINISTRATION AND ELIGIBLE FACILITIES) (AMENDMENT) REGULATIONS 2023

2023 No. 1226

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Energy Security & Net Zero and is laid before the House of Commons by Command of His Majesty.

2. Purpose of the instrument

2.1 The purpose of this statutory instrument is to make amendments to the Climate Change Agreements (Administration) Regulations 2012 (S.I. 2012/1976) and the Climate Change Agreements (Eligible Facilities) Regulations 2012 (S.I. 2012/2999) to enable a two-year extension to the Climate Change Agreements scheme, add a new Target Period from 1 January to 31 December 2024 (Target Period 6) and enable eligibility for a reduced rate of Climate Change Levy through to 31 March 2027.

2.2 This instrument amends the terms which the administrator must include in climate change agreements "CCAs" to increase the buy-out fee and amends S.I. 2012/1976 to increase the amount of the financial penalty that may be imposed, enable the administrator to impose a lower amount if it considers appropriate and amend or withdraw a financial penalty once issued. It will also require the administrator to publish certain information relating to penalties imposed after the instrument comes into force.

3. Matters of special interest to Parliament

3.1 None.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is the United Kingdom.

4.2 The territorial application of this instrument is the United Kingdom.

5. European Convention on Human Rights

5.1 As the instrument [is subject to negative resolution procedure and does not amend primary legislation no statement is required.

6. Legislative Context

6.1 Section 30 of, and Schedule 6 to the Finance Act 2000 make provision for Climate Change Levy (CCL) to be charged on certain supplies of energy. Schedule 6 to the Finance Act 2000 makes provision for a reduced rate of CCL to be charged if a facility which receives supplies of energy is certified as being covered by a Climate Change Agreement, as defined at paragraph 48 of Schedule 6, for a certification period. Part IV of Schedule 6 makes provision in relation to CCAs and confers powers on the Secretary of State to make regulations in relation to the CCA scheme.

6.2 The Climate Change Agreements (Administration) Regulations 2012 (S.I. 2012/1976) appoint the Environment Agency to administer CCAs and makes provision in relation to the administration of the scheme. The Climate Change Agreements (Eligible Facilities) Regulations 2012 (S.I. 2012/2999) define what is an eligible facility for the purposes of entering into a CCA and how reckonable energy is to be calculated.

6.3 This instrument makes amendments to those statutory instruments to:

- Add a new Target Period (TP6) and extend the scheme providing for a reduced rate of CCL until 31st March 2027.
- Amend the terms the administrator must include in agreements relating to the Target Period 6 buy-out fee, which is being increased to £25/tCO2e.
- Provide that any surplus will not be taken into account in calculating the buy-out fee for the new target period.
- Amend the terms that must be included in underlying agreements in relation to the provision of information to the administrator.
- Expand the circumstances in which the administrator may terminate an underlying agreement.

6.4 This instrument also amends the financial penalty provisions in the Climate Change Agreements (Administration) Regulations 2012. Pursuant to paragraph 52F(1)(a), 52F(7) and paragraph 146 (7) of Schedule 6 to the Finance Act 2000 the maximum level of financial penalty which the administrator may impose is increased. The administrator is given the power to impose a penalty of such lower amount as they determine appropriate, where they consider it appropriate. However, the administrator's discretion is constrained by the maximum amounts specified in amended Regulation 15 of SI 2012/1976.

6.5 Amendments are also made to require the administrator to publish certain information about the financial penalties that it imposes and to enable the administrator to withdraw a financial penalty, reduce the penalty amount or allow additional time for payment of the penalty.

7. Policy background

What is being done and why?

7.1 Climate Change Levy (CCL) is a tax on the supply of a range of fuels including electricity, natural gas, liquefied petroleum gas and solid fuels when supplied for use by the business and public sectors. It was introduced on 1 April 2001.

7.2 The CCA scheme is a voluntary scheme pursuant to which CCA scheme participants enter into agreements with the Government to reduce their energy use or emissions and, in exchange, are entitled to pay reduced rate of CCL.

7.3 The CCA scheme supports the Government's objectives to deliver affordable and secure energy and decarbonisation while also helping productivity and the growth agenda.

7.4 In the CCA scheme, the agreements between sector associations, which are industry sector representative bodies for the eligible industry sectors in the scheme, and the administrator are called umbrella agreements. Agreements between operators and the administrator are called underlying agreements, while 'Target Unit' means the facility or group of facilities to which an underlying agreement applies.

Explanations

<u>What did any law do before the changes to be made by this instrument?</u>

7.5 CCA operators can remain compliant with the CCA scheme and retain their entitlement to the reduced rate of CCL either by meeting agreed energy efficiency or carbon reduction targets or by paying the buy-out fee. The buy-out fee is payable on each tonne of carbon dioxide equivalent by which a Target Unit falls short of meeting any target for a Target Period. There were four initial Target Periods in the CCA scheme for which Target Units are were required to meet their targets, covering the four two-year periods from 2013 to 2020 inclusive, followed by Target Period 5 (during the first extension to the CCA scheme) running from 2021 to 2022.

7.6 Alternatively, operators who do not meet their targets may choose not to pay the buy-out fee and lose their certification to claim the discount on CCL for the next certification period. If a Target Unit overachieves against its target for a Target Period, there will be a surplus, being the amount by which the reduction in emissions has exceeded the target.

7.7 Operators who comply with the scheme (either by meeting their targets or by paying the buy-out fee) will benefit from the reduced rate of CCL until the present CCA scheme ends, which was 31 March 2025 prior to these amendments.

<u>Why is it being changed?</u>

7.8 The policy intent behind this instrument is to extend the CCA scheme to 31 March 2027. It does so by amending the Climate Change Agreements (Administration) Regulations 2012 (S.I. 2012/1976) to provide for a new target period (Target Period 6) from 1 January 2024 to 31 December 2024, and amending the Climate Change Agreements (Eligible Facilities) Regulations 2012 (S.I. 2012/2999) so they remain in force until 31 March 2027. The instrument also makes amendments to the existing scheme following consideration of responses from the consultation that ran from 15 March 2023 to 10 May 2023 and engagement with the Environment Agency.

<u>What will it now do?</u>

7.9 This instrument amends the terms to be included in an underlying agreement relating to the buy-out fee, which is being increased to £25/tCO2e for the added target period to ensure this is commensurate with the increased value of the CCL discount and it amends the formulas to provide that any surplus will not be taken into account in calculating the buy-out fee for the new target period. It also introduces a mandatory disclosure to the scheme administrator, further to a request by the scheme administrator, in relation to certain actions that have been taken to meet the target, which will enable the administrator to request information which demonstrates that scheme participants are taking action in return for the CCL discount.

7.10 This instrument increases the maximum level of financial penalty which the administrator may impose and gives them discretion to impose a lower amount, if appropriate. The maximum penalty amount has not been increased since the current scheme began in 2013 and is being increased to ensure that the maximum penalty is set at an appropriate level to act as an effective deterrent in relation to non-compliance. Given the increase in the maximum penalty amount and in light of the consultation responses received the administrator will be able to impose a lower financial penalty, if they consider it appropriate, to ensure that the financial penalties imposed are proportionate to the breach in question.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 There are no plans for consolidation of the amended instruments.

10. Consultation outcome

10.1 A consultation on the details of the extension to the CCA scheme ran from 15 March 2023 to 10 May 2023, 55 responses were received. The extension was generally welcomed by respondents. There was broad support for maintaining existing rules and eligibility criteria as this provided consistency for operators during a time of economic uncertainty.

10.2 While responses to the proposals were generally positive, some respondents raised concerns about specific aspects, such as an increase to the buy-out price and inability to use surplus in the added Target Period. The department has decided to implement this change as the buy-out is intended to incentivise participants to continue implementation of energy efficiency measures while offering a safeguard for participants to maintain their certification for reduced rates of CCL. In addition, the gas and other taxable commodity rates of CCL have increased, therefore increasing the value of the reduced rate for those who use significant amounts of natural gas and/ or solid fuels. Further detailed responses and justification for these decisions is set out in the Government response.

10.3 The majority of respondents disagreed with the proposal that surplus from previous Target Periods should not be brought forward for use in Target Period 6. Some respondents considered that this would penalise those companies that have already made savings beyond their agreed targets. It was noted that the scheme had previously used carry-over in Target Periods1-4. A few respondents did agree with the proposal, with one reason being that the proposal provides continuity with Target Period 5, we are therefore taking the same approach into Target Period 6. Further detailed responses and justification for these decisions is set out in the Government response.

10.4 The majority of respondents agreed with the proposal to increase the minimum financial penalty. Some stated that a higher financial penalty would increase compliance, as the penalty does need to act as a deterrent for non-compliance and noted that it has not been increased since the current scheme began. Of those that did not agree, some highlighted the current economic climate. Other respondents agreed with the increase, as long as the administrator was given discretion.

10.5 A large majority of respondents agreed with giving the scheme administrator discretion to waive or reduce the penalty amount when considered appropriate.

10.6 This instrument implements the changes set out in the Government response to the CCA scheme extension, which will be published in November 2023.

10.7 There has been ongoing engagement with the Environment Agency, who administer the scheme, on this instrument.

11. Guidance

11.1 Guidance previously issued under paragraph 52D(6) of Schedule 6 to the Finance Act 2000 is being updated to take account of the extension to the scheme and will be published in November 2023.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies. CCAs are voluntary and provide eligible energy intensive businesses with the opportunity to receive reduced rate of CCL if they meet energy efficiency or emission reduction targets. For those businesses signed up to agreements there is a potential positive impact on their CCL tax bill. The vast majority of current scheme rules will remain in place for the extension and therefore the additional administrative burden is expected to be minimal for businesses to continue their voluntary participation in the scheme.

12.2 The buy-out fee increase is commensurate with the increased value of the reduced rate of CCL provided since the buy-out was last reviewed in 2020. The penalty has not been increased since the current scheme began in 2013 and is being increased in order to maintain the deterrent effect. We assess this will have no significant impact as the increased penalty is proportionate to other similar schemes and the scheme administrator will have discretion to amend penalties. The CCA scheme is also a voluntary scheme.

12.3 There is no, or no significant, impact on the public sector.

12.4 A full Impact Assessment has not been prepared for this instrument because the CCA scheme relates to a tax and is therefore treated as non-regulatory.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses.

13.2 No specific action is proposed to minimise regulatory burdens on small businesses (employing up to 50 people).

13.3 The basis for the final decision on what action to take to assist small businesses is that this is an extension to an existing, voluntary scheme which small businesses do not have to participate in. If they do, then they will receive the reduced rate of CCL which should outweigh any of the voluntary participatory costs.

14. Monitoring & review

14.1 This instrument is exempt from the requirement under section 28(2) of the Small Business, Enterprise and Employment Act 2015 to make provision to carry out a review as it falls within the exception in section 28(3) of that Act.

14.2 No further monitoring or review is planned. The regulations extend the current scheme by two years and application is, therefore, time-limited.

15. Contact

15.1 Holly Denny at the Department for Energy Security & Net Zero. Telephone: 07341 804 580 or email: holly.denny@energysecurity.gov.uk can be contacted with any queries regarding the instrument.

15.2 Andrew Cooke, Deputy Director for Business Energy Transformation, at the Department for Energy Security & Net Zero can confirm that this Explanatory Memorandum meets the required standard.

15.3 Lord Callanan, Minister for Energy Efficiency and Green Finance, at the Department for Energy Security and Net Zero can confirm that this Explanatory Memorandum meets the required standard.