

**EXPLANATORY MEMORANDUM TO**  
**THE GREENHOUSE GAS EMISSIONS TRADING SCHEME (AMENDMENT)**  
**ORDER 2023**

**2023 No. 850**

**1. Introduction**

- 1.1 This explanatory memorandum has been prepared by the Department for Energy Security and Net Zero and is laid before Parliament by Command of His Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

**2. Purpose of the instrument**

- 2.1 This instrument makes various operational and clarificatory amendments to the UK Emissions Trading Scheme (the “UK ETS”) including increasing free allocation for installations that produce lime and malt extract and enabling operators of installations whose free allocation of allowances was reduced by the 2021 activity level changes process to apply for the allocation to be redetermined in light of the COVID-19 pandemic.

**3. Matters of special interest to Parliament**

*Matters of special interest to the Joint Committee on Statutory Instruments*

- 3.1 This instrument rectifies an omission in Schedule 8A to the Greenhouse Gas Emissions Trading Scheme Order 2020 (the “2020 Order”), which was inserted by the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2021. The Department has decided to apply the free issue procedure in relation to recipients of the latter instrument. In accordance with paragraph 4.7.6 of *Statutory Instrument Practice*, the Department has consulted the SI Registrar.

**4. Extent and Territorial Application**

- 4.1 The extent of this instrument is the whole of the United Kingdom.
- 4.2 The territorial application of this instrument is the whole of 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 The UK ETS was established under the Climate Change Act 2008 by the 2020 Order as a UK-wide greenhouse gas emissions trading scheme to encourage cost-effective emissions reductions which will contribute to the UK’s emissions reduction targets and net zero goal. The UK ETS is operated by the UK ETS Authority, comprising the UK Government, Scottish Government, Welsh Government and the Department of Agriculture, Environment and Rural Affairs in Northern Ireland. The scheme is

regulated by the Environment Agency, the Scottish Environment Protection Agency, Natural Resources Wales, the Northern Ireland Environment Agency, and the Offshore Petroleum Regulator for Environment and Decommissioning. This scheme replaced the UK's participation in the EU Emissions Trading System (EU ETS), and the 2020 Order applied EU ETS rules on the monitoring, reporting and verification of emissions with modifications to ensure that they work for the UK ETS.

- 6.2 The 2020 Order was subsequently amended by the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2020 to include provisions for the free allocation of allowances and the UK ETS Registry, including by amending the domestic law versions of Commission Delegated Regulation (EU) 2019/331 (the "Free Allocation Regulation") and Commission Implementing Regulation (EU) 2019/1842 (the "Activity Level Changes Regulation" or "ALCR"). The Greenhouse Gas Emissions Trading Scheme Auctioning Regulations 2021 made under the Finance Act 2020 established the rules for auctioning allowances and mechanisms to support market stability.
- 6.3 Technical and operational amendments, including additional penalties, and improvements to monitoring, reporting and enforcement of scheme rules were made by the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2021, the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2022, and the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2022.
- 6.4 A further amendment to include flights to Switzerland within the scope of the UK ETS from 1 January 2023 was made by the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 3) Order 2022.
- 6.5 Additional legislation to implement the policy decisions in the Main UK ETS Authority Response to the Developing the UK ETS Consultation will be forthcoming later this year. This includes an affirmative-procedure instrument under the Climate Change Act 2008 and amendments to the Greenhouse Gas Emissions Trading Scheme Auctioning Regulations 2021.

## **7. Policy background**

### *What is being done and why?*

- 7.1 Under the UK ETS, participants are required to monitor and report on, and surrender allowances in respect of, their greenhouse gas emissions. The UK ETS provides free allocation of emission allowances to eligible installation operators in order to reduce the risk of carbon leakage. Free allocation for installations is calculated using industry benchmarks and the carbon leakage list, which are the same as those for Phase IV of the EU ETS.
- 7.2 Installations that receive free allocation are required to monitor and report activity levels each year. Regulators are required to recalculate the free allocation of allowances due to activity level changes in line with the ALCR. The UK ETS Registry records the movement of allowances between accounts and details of verified emissions and allowances surrendered by operators.
- 7.3 *Hospital or Small Emitters (HSEs) and Ultra-Small Emitters (USEs) going into the main scheme (UK ETS):* There are opt out schemes for hospitals and eligible small/ultra-small emitters, as they either provide services to hospitals or are

installations emitting less than 25,000/2,500 tonnes respectively of carbon dioxide equivalent (CO<sub>2</sub>eq) per year. Eligible installations do not have to surrender allowances in respect of their emissions. Over the course of forthcoming ETS allocation periods, HSEs and USEs may cease to be eligible for the relevant opt-out scheme and join the main UK ETS scheme. In this case, they may claim a free allocation of allowances if a successful application for free allocation was previously made. The legislation does not currently require operators to provide all the activity information required for regulators to be able calculate the free allocation of these installations. This instrument rectifies this omission, by requiring information to be provided to enable regulators to determine the “historical activity levels” of sub-installations that started operating late in, or after, the “baseline period” (by reference to which historical activity levels of other sub-installations were determined).

- 7.4 *Putting current benchmark values in UK law:* The UK ETS currently uses EU ETS benchmarks that are adopted under EU law and made applicable in UK law. This instrument brings current benchmark values, as they currently stand, into UK law by direct inclusion in the Free Allocation Regulation.
- 7.5 *Temporary amendments to benchmarks and carbon leakage list:* This instrument effects a temporary change to the lime benchmark and the carbon leakage classification of malt extract production for both existing and new installations. The sector made representations that the existing lime benchmark was unattainable due to distortions by data from EU operators with access to biomass. Therefore, the UK ETS Authority has decided to temporarily increase the benchmark value by 10%. For malt extract production, the sector made representations that the trade intensity data for malt production should be used, resulting in the activity meeting the carbon leakage indicator threshold. Consequently, the UK ETS Authority has decided to temporarily set the activity to carbon leakage exposed. This would only apply to increase free allocation for the 2024 and 2025 scheme years and does not pre-empt broader changes to free allocation methodology which will be implemented for the next allocation period (2026-2030).
- 7.6 *COVID 2021 Activity Level Changes (ALCs):* An amendment to the ALCR will enable operators whose free allocation was reduced by the 2021 activity level change process to apply for the 2021 and subsequent annual change processes to be re-run, with changes to free allocation being based on activity levels calculated with the omission of the 2020 year, if they can demonstrate a discrepancy of at least 15% between reductions in output and emissions caused by the COVID-19 pandemic when comparing the 2019 and 2020 years. The purpose is to enable the activity level change process to take account of the effect of the COVID-19 pandemic. (A previous amendment to the ALCR related to the 2022 activity level change process only.)
- 7.7 *Article 6 ALCR amendment:* Article 6 of the ALCR provides for when adjustments to free allocation as part of the activity level change process may be rejected on energy efficiency grounds. An amendment to Article 6(3) provides that where there is no PRODCOM code available to attach to a product, the codes in Section B or C of Annex 1 of NACE rev. 2 (a statistical classification of economic activities in the EU) are to be used. The amendment clarifies that the provisions apply to all products within scope of sections B and C. The amendment refers to NACE rather than the UK Standard Industrial Classification of Economic Activities for consistency with other

references to NACE in UK ETS legislation. This may be updated in future along with all other references once other policy aspects are in place e.g., a UK ETS carbon leakage list.

- 7.8 *New permission for the UK ETS Registry account authorised representatives:* A new provision permits operators to appoint authorised representatives for their accounts in the UK ETS Registry with the permission only to surrender, or return overallocated, allowances. The administrative burden on operators of appointing such an authorised representative would be less onerous than that of appointing an authorised representative currently with a broader range of permissions, as the former would be permitted to perform fewer operations. Creating this route for appointing authorised representatives will help some operators who have historically not always achieved compliance to do so.
- 7.9 *Monitoring and Reporting Regulation 2018 – Commission Implementing Regulation (EU) 2018/2066 (the “Monitoring and Reporting Regulation 2018”)* has effect for the purpose of the UK ETS with modifications set out in Schedule 4 to the 2020 Order. This instrument makes a further minor (non-operative) modification to assist the reader of the legislation.

### ***Explanations***

#### *What did any law do before the changes to be made by this instrument?*

- 7.10 Currently, existing legislation does not provide for the amendments referred to in sections 7.3-7.9 of this explanatory memorandum. The provisions in this instrument make minor amendments and additions to existing elements of the scheme.

#### *Why is it being changed?*

- 7.11 As a result of feedback from the public consultation the UK ETS Authority are proposing amendments which will support businesses and effective scheme operation. In addition, UK ETS delivery partners identified a list of technical amendments and clarifications needed to support effective operation. This has led to a package of issues included in this instrument and the other legislation referred to in section 6.5.

#### *What will it now do?*

- 7.12 The instrument will make changes to a broad range of operational scheme aspects and will amend the 2020 Order and other UK ETS legislation to reflect the policies outlined in sections 7.3 to 7.9.

## **8. European Union Withdrawal and Future Relationship**

- 8.1 This instrument is not being made under the European Union (Withdrawal) Act 2018 but relates to the withdrawal of the United Kingdom from the European Union because the UK ETS is a policy replacement for the UK’s participation in the EU ETS.

## **9. Consolidation**

- 9.1 There are no plans to consolidate the legislation amended by this instrument.

## **10. Consultation outcome**

- 10.1 Between 25 March 2022 and 17 June 2022, the UK Government, Scottish Government, Welsh Government and Department for Agriculture Environment, and Rural Affairs, Northern Ireland (DAERA), ran a public consultation on a package of proposals to develop the UK ETS, including much of the policy content of this instrument referred to in sections 7.3 to 7.9.
- 10.2 Alongside the consultation, the advice of the Committee on Climate Change (CCC) on the policy proposals in this instrument was sought. The CCC reviewed the policy content of these proposals and only had clarification questions and no further comments.
- 10.3 The consultation resulted in received responses from over 300 organisations, representing a wide range of stakeholders from a variety of sectors, such as the energy, industrial and aviation sectors, as well as Non-Government Organisations (NGOs), Think Tanks, Local Authorities, trade associations, academia and advocacy groups.
- 10.4 The policy represented by the amendments referred to in sections 7.3 and 7.7 to 7.9 above were not consulted on as part of the Developing the UK ETS consultation. The Department takes the view that the policy represented by some of these amendments is within the scope of the consultations previously carried out (including previous advice from the CCC) and is covered by the Government Responses to those consultations. The policy relating to HSEs and USEs going into the main scheme was publicly consulted on in 2021. The amendment is a minor additional detail to ensure effective implementation. The amendment to Article 6(3) of the Activity Level Changes Regulation represents a minor clarification to existing policy. The new permission for authorised representatives is something that operators may take advantage of, but they are not required to do so. Consequently, the Department did not consider it necessary to consult more widely. In all cases, the scheme regulators and the CCC were separately consulted on the proposals that were not in the Developing the UK ETS consultation. Neither exercise raised substantive concern or observation that had a material impact on the policy proposals.
- 10.5 The Government Response to the consultation was published on 3 July 2023.
- 10.6 Full details of the consultation and response can be found at: <https://www.gov.uk/government/consultations/developing-the-uk-emissions-trading-scheme-uk-ets>.

## **11. Guidance**

- 11.1 The UK ETS guidance has been published and is available at: <https://www.gov.uk/government/publications/participating-in-the-uk-ets/participating-in-the-uk-ets>. Guidance will be updated regularly, and updates will take account of relevant changes to legislation as necessary.

## **12. Impact**

- 12.1 The impacts on business, charities or voluntary bodies of the provision relating to the temporary amendments to benchmarks and carbon leakage list are outlined in the Impact Assessment. This was published alongside the Main UK ETS Authority

Response to the Developing the UK ETS Consultation, in which the UK ETS Authority announced the changes to the UK ETS made in this legislation.

- 12.2 The other amendments are not covered in the Impact Assessment as they are technical amendments with no substantial direct impacts to be assessed.
- 12.3 A June 2020 regulatory impact assessment of the effect of the UK ETS on the costs of business, the voluntary sector and the public sector is available from the Industrial Decarbonisation and Emissions Trading Directorate, Department for Energy Security and Net Zero, 1 Victoria Street, London SW1H 0ET and is available alongside the 2020 Order on [www.legislation.gov.uk](http://www.legislation.gov.uk).
- 12.4 There is no, or no significant, impact on the public sector.
- 12.5 The full Impact Assessment is submitted with this memorandum and published alongside the explanatory memorandum on the [legislation.gov.uk](http://legislation.gov.uk) website.

### **13. Regulating small business**

- 13.1 The legislation applies to activities that are undertaken by small businesses.
- 13.2 To minimise the impact of the requirements of the UK ETS on small businesses, operators with relatively low levels of emissions are either not caught by the scheme or participate in the HSE or USE schemes.

### **14. Monitoring & review**

- 14.1 Article 17 of the 2020 Order requires the UK ETS authority to review the operation of the UK ETS (including the measures introduced by this instrument) in 2023 and in 2028. The UK ETS Authority must subsequently publish a report setting out the conclusions of the review.
- 14.2 The instrument does not include a statutory review clause. The requirement under section 28(2) of the Small Business, Enterprise and Employment Act 2015 to make provision for review does not apply to this instrument as it falls within an exception in section 28(3) of that Act.

### **15. Contact**

- 15.1 Samuel West at the Department for Energy Security and Net Zero (Telephone: 07720158592 or Email: [Samuel.west2@beis.gov.uk](mailto:Samuel.west2@beis.gov.uk)) can be contacted with any queries regarding the instrument.
- 15.2 Seamus Gallagher, Deputy Director for UK ETS Operations and Delivery, at the Department for Energy Security and 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.