

Explanatory Memorandum to the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023

This Explanatory Memorandum has been prepared for the Minister for Climate Change by the Directorate of Climate Change, Energy and Planning and is laid before Senedd Cymru in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

Minister's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023.

Julie James
Minister for Climate Change

19 September 2023

PART 1

1. Description

1.1 The UK Emissions Trading Scheme (“ETS”) was established by the Greenhouse Gas Emissions Trading Scheme Order 2020 (“the principal Order”) as a UK-wide greenhouse gas emissions trading scheme, to encourage cost-effective emissions reductions from the power, industry, and aviation sectors. It was designed jointly by the Governments of the UK, Scotland, Wales, and the Northern Ireland Executive. It contributes to the UK’s emissions reduction targets and net zero goal, as well as the emissions reduction pathway we have in Wales. Amendments to the principal Order were made at the end of 2020¹ to enable the UK ETS to operate from 1 January 2021.

1.2 The legislation underpinning the UK ETS is being delivered incrementally, through a series of statutory instruments. The timing and order of this series has been designed to ensure that specific legal provisions are introduced as they become operationally necessary, with five further amendments made since 2020, with the latest being in July 2023².

1.3 In 2022, the UK ETS Authority consulted on “Developing the UK Emissions Trading Scheme (UK ETS)” which alongside proposals for fundamental change to the scheme, also contained proposed amendments considered necessary to regularise the operation of the UK ETS moving forward. These technical amendments need to be implemented before February 2024 for operational reasons.

1.4 The joint Government response published in July 2023 sets out the UK ETS Authority position regarding the consulted-upon technical amendments.

1.5 The current amending Order also includes one amendment that was not specifically consulted-upon, since it contains a minor clarification on the policy intent and there was agreement across the Authority that this did not require consultation.

1.6 Overall, the current amendments cover technical changes in response to changing needs of the scheme participants ascertained via the consultation responses and helps streamline the UK ETS policy.

2. Matters of special interest to the Legislation, Justice and Constitution Committee

2.1 Part 3 of Schedule 3 to the Climate Change Act 2008 (“CCA”) states that provision may be made for a trading scheme that applies to England,

¹ The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2020 (S.I. 2020/1557).

² The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2023 (S.I. 2023/850).

Scotland, Wales and Northern Ireland (or any combination thereof that includes Scotland) – such as in this case – by Order in Council.

2.2 The appropriate procedure for an Order in Council is prescribed by section 48 and paragraph 11 of Schedule 3 to the CCA.

2.3 The Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023 contains provisions which are caught by section 48(3) of the CCA. Therefore, the draft affirmative procedure applies.

2.4 As the Order in Council will be subject to UK Parliamentary scrutiny, it is not considered reasonably practicable for this instrument to be made or laid bilingually.

2.5 While the UK ETS is a four-nation scheme currently Northern Ireland cannot pass affirmative legislation as the Assembly have failed to nominate a Speaker and an Executive has not been formed. As a result, officials have secured approval from the Permanent Secretary for Northern Ireland (under the interim arrangements) to proceed in the first instance with legislation covering Great Britain only.

2.6 The legislation covering installations and aviation operators in Great Britain (England, Scotland and Wales), would be in effect from 1 January 2024. The legislation covering Northern Ireland would be implemented as soon as the Northern Ireland Assembly is able to progress legislation.

3. Legislative background

3.1 The principal Order set up the UK ETS to be operational from 1 January 2021 and runs for ten scheme years. The scheme works by requiring operators of energy intensive industrial installations, power generators, and aircraft operators to monitor, report on, and surrender “allowances” equivalent to their greenhouse gas emissions in each scheme year. Some participants receive an allocation of allowances free of charge, details of which are published in allocation tables.

3.2 There have been several amendments to the principal order –

- 3.2.1 The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2020 (S.I. 2020/1557);
- 3.2.2 The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2021 (S.I. 2021/1455);
- 3.2.3 The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2022 (S.I. 2022/454);
- 3.2.4 The Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2022 (S.I. 2022/1173);
- 3.2.5 The Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 3) Order 2022 (S.I. 2022/1336) and
- 3.2.6 The Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2023 (S.I. 2023/850)

3.3 The purpose of the above amendments was to effect technical changes to improve the operation of the UK ETS for both participants and regulators.

3.4 From “Developing the UK Emissions Trading Scheme (UK ETS)” consultation responses, certain elements of the ETS have been identified as needing improvement, to make it a more effective instrument for decarbonisation.

3.5 The principal Order and the several amendments were made in exercise of the power conferred by section 44 of the CCA, as well as other powers conferred by the CCA. The Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023 is made in exercise of this power, together with others conferred by the CCA, including sections 54, 90(3) of, and Schedule 2 and paragraph 9 of Schedule 3.

3.6 The Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023 is being made subject to the draft affirmative procedure.

4. Purpose and intended effect of the legislation

4.1 The purpose of the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2023 is to amend the principal Order and associated legislation to:

- 4.1.1 Streamline the classification of electricity generators to allow more equitable access to free allocation (FAs)
- 4.1.2 Cap the FAs of aircraft operators at 100% of their verified emissions; and
- 4.1.3 Allow operators of carbon capture plants to receive FAs.

4.2 The territorial extent of this Order is England, Wales, and Scotland. The Order has an indirect impact on aviation. However, it should be noted that there are no aviation operators in Wales under the definitions of the UK ETS.

4.3 The main changes are summarised below:

Changes to Greenhouse Gas Emissions Trading Scheme Order 2020

4.4 **Articles 5 to 9** of the amending Order updates the ETS Order (provisions relating to the administration of Free Allocations) to accommodate substantive changes in FAs to electricity generators, installations and aviation operators as effected by provisions following thereafter.

4.5 Amendments to articles 34K and 34T particularly requires Aircraft operators to return any excess allowances where their FAs for the 2024 and 2025 scheme years exceeds their emissions.

4.6 **Article 10** amends the meaning of regulated activity to reflect that capturing greenhouse gases from a regulated activity (whether carried out at the same or another installation) is a regulated activity for which a permit is required. Ancillary changes emanating from this are made under **Article 21**.

Changes to the Free Allocation Regulation (FAR)

4.7 **Articles 11 and 12** link the changes made to the classification of electricity generators elsewhere to the definition of the same under Article 2.

4.8 **Article 13** increases the eligibility for FAs for carbon capture plants (except those for transporting and storage) and electricity generators following the changes made to their definitions.

4.9 Amendment by **Article 14**, by inserting Article 2b to FAR allows electricity generators that do not sell electricity to third parties to apply and receive FAs. It also makes provision for FAs to be re-claimed should such sales occur subsequently.

4.10 Amendment by **Article 14**, to Article 2c reduces the reference period taken into account when considering electricity exports to be classified as electricity generators (thereby becoming ineligible for FAs). It also excludes those supplying 5% or less to external parties. This helps a more equitable access to FAs.

4.11 A further amendment by **Article 14**, to article 2c further excludes from the electricity generator definition, those producing electricity for sale by means of a Combined Heat and Power Quality Assurance (CHPQA)-certified plant. This allows qualifying plants to apply and receive FAs.

4.12 **Articles 15 to 19** makes ancillary changes to cross-referenced sections of FAR, to ensure the overall integrity of the legislation.

4.13 **Article 20** amends Annex 4 of FAR, to incorporate criteria required to prove the qualifying changes to electricity generator classification described above like exports and CHPQA.

4.14 **Articles 22 and 23** make changes to cross-referenced legislation to ensure the smooth operability of the ETS scheme overall.

5. Consultation

5.1 A consultation, “Developing the UK Emissions Trading Scheme (UK ETS)” was held from 25 March to 12 June 2022, running for 12 weeks on the proposed amendments. It also contained other proposals not subject to this Order.

5.2 Full details of the consultation and response covering the current amendment can be found at: [Developing the UK Emissions Trading Scheme \(UK ETS\) - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/developing-the-uk-emissions-trading-scheme)

6. Regulatory Impact Assessment (RIA)

6.1 While this Order contains minor changes to regulatory provisions, the amendments do not alter the policy (or its impact) in any significant way or how it is applied in a given situation. There is no or negligible costs or savings on the public, private, charity or voluntary sectors as a result of this amendment. Therefore, an RIA is not required. This is in line with the policy set out in the Welsh Ministers’ code of practice for carrying out regulatory impact assessments for subordinate legislation.

6.2 It should also be noted that the overall level of climate ambition in the UK ETS is unchanged by the proposals.

6.3 Although not required by Government policy, a regulatory impact assessment of the effect of the UK ETS on the costs of business, the voluntary sector and the public sector was produced and is available alongside the principal Order at: [The Greenhouse Gas Emissions Trading Scheme Order 2020 - Impact Assessment \(legislation.gov.uk\)](https://legislation.gov.uk/uksi/2020/1251/impact-assessment).