



## LATEST NEWS – CHANGES TO PROPOSALS FOR THE CARBON REDUCTION COMMITMENT

7 October 2009

The Department of Energy and Climate Change (DECC) has today published its Response and Policy Decisions following the Consultation on the Draft Order to implement the Carbon Reduction Commitment (CRC).

The Response has made a number of significant changes to the structure of the CRC scheme that was proposed in the Consultation document. This note summarises the key changes to the CRC proposals as announced today.

### CARBON REDUCTION COMMITMENT ENERGY EFFICIENCY SCHEME

From today, the CRC will now be known as the Carbon Reduction Commitment Energy Efficiency Scheme (CRC). DECC is of the opinion that this title better reflects the purpose of the scheme, namely to achieve a significant reduction in the UK's carbon dioxide emissions by encouraging energy efficiency.

### INITIAL PURCHASE OF ALLOWANCES – CASH FLOW

Perhaps the most important change set out in the Government Response is that a double purchase of allowances will no longer be required in April 2011. This will essentially halve the cost of the allowance purchases that organisations have been expecting to make in April 2011. It was initially proposed that, when the CRC scheme comes into force on 1 April 2011, participant organisations would be required to purchase allowances to cover both their reported emissions from the 2010/2011 year and their forecast emissions for the 2011/2012 year.

During the Consultation period, many organisations objected to this due to the impact it will have on cash flow, particularly given the current state of the UK economy. The Response has amended this position. The first sale of allowances in April 2011 will now only require CRC participants to purchase allowances for the year ahead, from 1 April 2011 to 31 March 2012 and, as a result, the first year of the Introductory Period will become a monitoring period.

### SIGNIFICANT GROUP UNDERTAKINGS

The previously termed 'Principal Subsidiaries' (which have over 6,000 MWh of half hourly metered electricity use in 2008) are to be known as 'Significant Group Undertakings' (SGUs). The Government Response has noted that the updated CRC Order will allow for SGUs to participate in the CRC in their own right. Participants will be able to nominate SGUs that will be required to participate separately at registration and this is expected to help organisations with complicated structures who have quite distinct operating entities at subsidiary level. Any SGUs that are disaggregated will be listed as separate entities in the league table and receive separate recycling payments. Legal responsibility will also fall on any disaggregated SGU such that joint and several liability between the original group and the SGU will not apply and the SGU itself will be responsible for meeting CRC requirements and will be liable for any penalties.

### EARLY ACTION METRIC

The Carbon Trust Standard (CTS) aspect of the early action metric (EAM) has been expanded so that certified verification under schemes that are equivalent to the CTS will also be recognised. The Government Response sets out a list of the criteria that a scheme must satisfy in order to count towards the EAM. The Government has made limited comment on specific schemes that may qualify under this criteria, however it is noted that ISO14000 would not meet this standard. Accreditation under the Energy Efficiency Accreditation Scheme will still be recognised as noted in previous consultation documents.

**Disclaimer:** This briefing is not intended to be a complete coverage of the law in this area. Legal advice should always be taken in any particular case.

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Greater clarity on the other aspect of the EAM, the exact nature of voluntary AMR meters that will count towards the EAM, is also provided through the definitions set out in the Government Response (at page 72).

In addition to expanding the scope of certification the percentage weighting of recognition of the EAM has been updated. This will be 100% in year 1 (Oct 2011), 40% in year 2 (Oct 2012) and 20% in year 3 (Oct 2013). The respective amendments to the Absolute metric are 0% in year 1, 45% in year 2 and 60% in year 3, and for the Growth metric, 0% in year 1, 15% in year 2 and 20% in year 3. It is expected that this change in weighting of the EAM will encourage CRC participants to take more steps to achieve a better EAM ranking through achieving the Carbon Trust Standard, use of equivalent schemes or fitting of relevant meters.

## **TREATMENT OF RENEWABLES**

One of the key aspects that had been noted as being 'under consideration' by the Government was the treatment of renewables under the CRC. While there have been some minor amendments to this aspect of the CRC the treatment of renewables remains largely unchanged. There will be some recognition for renewable generation through the publication of data on renewable electricity generated by participants alongside the Performance League Table. However this publication will not affect how renewable energy will be treated under the ranking or reporting requirements in the scheme, and will therefore not reduce the amount of allowances to be purchased or increase revenue recycling for those generating or purchasing renewable energy. The failure of Government to move on this issue will be a serious disappointment to CRC participants, a proportion of which have argued that the CRC will discourage use of green electricity and energy generation from renewable sources.

## **DEFINITION OF SUPPLY**

A fundamental element of the previous draft of the CRC was that participants would be responsible for emissions where they were the 'counterparty to the energy supply'. The definition of supply is to be updated in an attempt to clarify what will be included, and expand on the circumstances of supply that will be included. The updated definition will attempt to capture: direct supply (which in the case of electricity and gas will need to be through a fiscal meter); indirect supply; self supply and the landlord/tenant rule. Participants may need to revisit supply arrangements to ascertain whether any additional emissions will need to be accounted for.

## **CLIMATE CHANGE AGREEMENT AND EU ETS EXEMPTIONS**

Two key modifications have been made to the CCA exemption. Firstly, information for the CCA exemption will be based on a qualification year, not on the footprint year. This change will provide organisations seeking the CCA exemption with greater certainty now as to whether or not they are included in the CRC. For the introductory period only, organisations that do not have 2008 CCA data will be able to apply for the CCA exemption as part of the footprint report. For those who do hold 2008 data, and for those seeking CCA exemptions in future phases, this change will also be of assistance to organisations when determining whether they will need to provide footprint reporting information.

The second key modification is that participants will be able to submit data collected for the CCA target period ending in the qualification year, rather than over the CRC scheme year. This will also apply to those seeking to exclude EU ETS emissions.

## **PASSING ON OF COSTS FROM LANDLORDS TO TENANTS**

A key issue for many organisations will be how the energy supplied to their property holdings will be covered by the CRC. The key requirement for landlords to be responsible for emissions where it is responsible for the related energy supply, even where that energy is used by a tenant, remains. It is worth noting that there has not been any mention in the Response of introduction of steps to allow landlords to pass on CRC costs to tenants where appropriate metering is in place and the parties agree. The Government has simply stated that an additional provision will be inserted that will require tenants to cooperate with landlords for the purpose of complying with the CRC. This leaves landlords in the position of having to review existing leases, or negotiate new leases, and reach commercial agreement on how to pass on CRC costs.

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## **ADDITIONAL KEY CHANGES**

There are other changes to the CRC that may affect your organisation and we have not attempted to list them all here. However, it is worth noting additional changes that include the following:

- A revised definition of franchises, a new obligation on franchisees to provide information to franchisors and an additional power serve enforcement notices on a franchisee.
- An estimate with a margin of error of 20% will be allowed to determine HHM usage where the 6,000 MWh threshold is exceeded for the purposes of registration.
- A revised definition of onward transmission has been provided.
- The definition of transport has been amended to restrict energy used to power road going vehicles, a vessel, an aircraft or a train, and the exemption can now be applied prior to qualification.
- There will be no safety valve sales in July of each year.
- New fuels will be added including peat, BOS gas and different grades of coals and fuel reporting will be done on a use basis rather than on a fuel delivery basis.
- VAT will not be charged on safety valve allowances during the introductory phase.

## **KEY DATES**

End of October 2009 - The Environment Agency (EA) will publish its Qualification and Registration Guidance (on its website) and will continue to publish guidance six months prior to any obligation arising under the CRC.

End of 2009 – Publication of updated CRC Order, which is to be laid before Parliament and made publicly available at the end of this year.

Early 2010 - Accompanying allocation regulations setting out details of the allowance sales will be revised and then laid before Parliament and made publicly available in early 2010.

## **PREPARATIONS FOR CRC SCHEME**

The key steps that we recommend organisations take to prepare for the CRC remain, on the face of it, unchanged. However, the steps will need to be reconsidered again in light of the Government Response. For example, organisations will need to look again at:

- Defining the organisation and nominating UK subsidiaries, or agreeing Significant Group Undertakings to participate in the CRC in their own right.
- Preparing an accurate list of half hourly electricity meters, in view of revised definitions for these.
- Calculating total organisation-wide energy use emissions in light of new fuels that are to be included in the CRC, revisions to exemptions and the proposed amendments to the definition of supply.
- Planning for the early action metric in view of key changes to weighting of the EAM and its qualifying components.
- Reviewing existing lease arrangements for pass on of CRC costs.
- Considering CRC implications in transactions, regulatory documents, franchise arrangements, project pitches, future lease arrangements and service contracts.

Needless to say, for organisations that will be included in the CRC it will be important over the coming months to scrutinise the draft legislation once it is published and confirm expectations of the potential implications of the scheme. This will enable CRC participants to budget and make preparations for the CRC and ensure that systems and processes have been put in place to collate the information required for compliance.

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## FURTHER INFORMATION

If you would like to receive information on how Burges Salmon could assist you with preparations for the CRC, updates on the CRC, or details of our team's capabilities on the full range of environmental issues, please contact :-



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