

The Carbon Reduction Commitment Order 2010

SUMMARY OF MAIN POINTS

A. Introduction

This note has been prepared to assist readers in understanding the draft Carbon Reduction Commitment Order 2010 (“the Order”); readers should note that it is not intended to be comprehensive.

DECC will be using the consultation period to consider ways in which the structure and conceptual clarity of the Order can be improved to help readability – the final Order may differ from the consultation version in its structure and drafting.

B. Key points

The Order:

- establishes an **emissions trading scheme** (relating to direct and indirect CO₂ emissions from non-domestic energy consumption). The main obligation of this scheme is the annual requirement on **participants to cancel allowances** equalling the quantity of their emissions from energy consumption; and
- also imposes related obligations on participants, and related powers on the scheme administrator – and imposes obligations on other persons (including electricity and gas suppliers).

C. Participation – the basics

Unlike the EU Emissions Trading Scheme (“EU ETS”) (Directive 2003/87/EC) and Climate Change Agreements (“CCAs”), CRC applies to persons and organisations (rather than to installations or particular processes).

Who is required to participate?

- Any person or organisation may be liable to participate, where they meet the qualification criterion. That criterion is that a person or organisation consumes 6,000 MWh electricity from half hourly metered electricity supplies during a qualifying year. Such participants are referred to as “qualifying undertakings” See Chapter 3 of Part 2 for detail on the qualification criteria.

There are special rules dealing with combinations of related organisations (“combined participants”) – these are explained in section D of this note.

- Government departments, and the Scottish and Welsh Administrators are required to participate regardless of their electricity consumption. They are referred to as “government participants”. See Chapter 2 of Part 2.

How long must participants participate?

Qualifying participants must participate for the duration of a phase following a qualification year in respect of which they meet the qualification criteria.

Government participants must participate during each phase

The phases consist of a first phase of three years commencing on 1st April 2010 and subsequent phases consisting of seven years, the first of which commences on 1st April 2011. These phases do overlap, but participants will only be required to cancel allowances relating to one phase at a time. Phases and years are dealt with in article 5, and the duration of participation in Part 2.

What does the scheme cover?

The scheme covers participants' direct and indirect emissions of carbon dioxide from energy consumption.

Energy consumption is the consumption of supplies of electricity or gas and the consumption of certain other fuels but only insofar as the consumption relates to the conduct of a business, a public function or a charitable function. Readers should refer to Chapter 1 of Part 3 and, in particular, to Schedules 5 and 6 of the Order.

The Order provides for exemptions. In particular, emissions covered by EU ETS and CCAs are not counted as emissions for the purposes of CRC. Thus, CRC does not overlap with those schemes. There is also an exemption for emissions related to energy consumption in transport. See Schedule 7.

Rules on the calculation of CO₂ emissions attributable to energy consumption are set out in articles 33 and 34, and Schedule 9.

What do participants have to do?

The central requirement is for **participants to cancel allowances**. That requirement applies for particular years of a phase of the scheme. There are obligations related to that requirement which apply to participants before, during and after a phase. Those obligations are explained below. To participate in the scheme means to cancel allowances as required, and to comply with the related obligations.

The requirement on participants to cancel allowances is called the “**performance commitment**” (see below). The obligations on participants related to the performance commitment are set out chronologically in the Order.

There are several one-off “**up-front**” obligations. These are:

- **To register.** See article 36 and Schedule 10. This must be done by 30th September 2010 for the first phase and by the last working day of the first year of a subsequent phase.

- **To provide a footprint report.** See articles 37 and Schedule 11. This is a one-off report on various matters required by the scheme administrator in order to monitor the participant during a phase. The report must be provided to the scheme administrator by the final working day of July following the first year of a phase.
- **To prepare a residual measurement list, where one is required.** See article 38 and Schedule 12.

The list is required to ensure that at least 90% of a participant's emissions from its energy consumption are regulated under EU ETS, CCAs or CRC. That percentage may be higher after the first phase of the scheme.

So that the scheme administrator can ensure this occurs, participants must report two classes of energy consumption in their annual report (see below). First, all of their consumption of certain electricity and gas supplies (core consumption: see Schedule 8). Secondly, their other energy consumption (residual consumption).

However, only that amount of residual consumption needs to be reported which shows that this amount plus the participant's emissions from its core consumption and the emissions covered by EU ETS and CCAs meets the 90% threshold. Participants must therefore compile a list (the residual measurement list) which shows the residual consumption they will include in their annual reports during a phase.

There are specific rules applying in the case of local authorities and schools.

The residual measurement list must be compiled by the final working day of July following the first year of a phase.

The **annual obligations** imposed on participants are:

- **To provide an annual report.** See articles 39 and Schedule 13. This relates to each year of a phase (except where two phases overlap, in which case the report is required only in respect of the earlier phase), and must be provided by the final working day of July following the end of the relevant year.

The information to be provided to the administrator includes that participant's core consumption during the year, and its residual energy consumption included in its residual measurement list.

- **To sign a statement of records.** See article 40. On behalf of a participant, an individual must sign a statement confirming that adequate records have been kept (see below). The signatory must be a director (for a company) or a person of similar status such that there is a high-level awareness of the requirements of the scheme by the participant. The statement must then be retained along with the rest of the records. The deadline is the same as the deadline for providing an annual report.

- **To comply with the performance commitment.** See articles 41 to 43. A participant must, cancel sufficient allowances to match the quantity of its emissions from the energy consumption reported for a year of a phase. Those emissions will be the emissions from the energy use required to be reported in the participant’s annual report. The cancellation must take place by the final working day of July following the year of a phase. If it does not do this, it must hold sufficient allowances in its compliance account at that time – which the administrator is then entitled to cancel. Otherwise, the administrator must impose a civil penalty. There are specific rules as to the allowances which are valid for use in compliance.

Allowances are sold to participants under regulations made by the Treasury. These allowances may thereafter be **traded** between participants, and third parties, under Part 7 of the Order – to which readers should refer in relation to allowances and the **secondary market**.

There are two **ongoing obligations**:

- **Record keeping.** See article 44 and Schedule 14. This is to facilitate the administrator’s conduct of an effective audit.
- **General cooperation** with the administrator (in relation to the administrator carrying out its functions). See article 45.

Failure by a participant to comply with its obligations results in **civil penalties** imposed by the administrator. See article 71 and Schedule 22.

Participants are exempt from the performance commitment, the obligation to compile a residual measurement list and the annual report where they fall within the **climate change agreement exemption**. See article 50. There are specific rules for this exemption for combined participants.

D. Combined participants

A participant may consist of more than one person or body, e.g:

- parent and subsidiary companies (or other undertakings) – “group members” for the purpose of the Order.
- some types of franchising arrangements identified in the Order and various other categories of connected persons – “associated persons” in the Order.

In such cases, the members who together constitute the participant must participate together (a “combined participant”).

The Order seeks to encompass some of the changes which may occur to the members of a combined participant over the course of its participation in the scheme.

Qualification as a combined participant

The members of a combined participant are determined on the final day of a qualification year. There may also be cases where a participant was not a combined participant on the final day of a qualification year but persons or bodies enter into some form of relationship with that participant after that date during the phase of the scheme. In such cases, the participant may become a combined participant.

Changes during the period of participation

To deal with changes to a participant, including to the members of a combined participant:

- the Order identifies a particular legal person (or partnership) which has the status of a **qualifying undertaking**. Where an organisation does not have any subsidiaries or associated persons at the time it qualifies, that organisation is the qualifying undertaking. Otherwise, in the case of a group, the qualifying undertaking is the **parent at the time of qualification** – thus, the “combined participant” is built around the identity of the qualifying undertaking.
- the Order also identifies legal persons (or partnership) with the status of a **principal subsidiary**. This is a person which is a subsidiary at the time it qualifies as part of a combined participant – but which would have qualified in its own right (or together with subsidiaries) had it been a parent at that time (and is thus a significant business in its own right).

Articles 22, 26 and 27 deal with subsidiaries and associated persons of a qualifying undertaking, i.e. **structural changes below the level of the qualifying undertaking**. Those subsidiaries and associated persons must participate for as much of the period during which the qualifying undertaking is required to participate as they remain the subsidiary or associated person (as relevant) of that undertaking.

Schedules 16 and 17 deal with major structural changes (**takeovers, mergers and demergers**) arising outside of the normal course of events. These cover:

- **changes above the level of the qualifying undertaking** (e.g. where a third party takes over the participant by becoming its parent); **and**
- **changes in which a principal subsidiary ceases to be a subsidiary of the qualifying undertaking** - under the normal course of events a subsidiary would then be lost to CRC; it is important that such large subsidiaries (and their emissions) do not fall out of CRC coverage.

Schedule 17 deals with the effect these changes have on participant’s responsibilities and duration of participation.

Responsibility

In any case of a combined participant, there may be problems of assigning legal responsibility for the performance (or the non-performance) by the participant of its obligations under the Order – and also for the administrator in establishing whether a

particular constituent person (or employee) has the authority of the participant as a whole. Article 46 and Schedule 15 prescribe rules to deal with this:

- Some constituent persons are given legal responsibility under CRC – in the case of a group, this is joint and several across group members.
- Other constituent persons (e.g. a franchisee) are given a duty of providing the responsible person with reasonable assistance – if they fail to do this, that person will thus have been in breach of its statutory duty.
- The administrator may take one particular constituent person (the “primary member”) as acting on the combined participant’s authority and behalf – this is normally the parent (but may be another group member).

Limitations

It will thus be seen that obligations attach to particular legal persons. It follows that legal persons other than those identified in accordance with the Order will not be subject to the obligations imposed by CRC.

E. Performance assessment and publicity

After each year of a phase, the administrator is required to publish performance tables scoring and ranking participants. See articles 64 to 66 and Schedule 20. The performance tables deal with:

- In the first phase only, early action by the participant to reduce emissions.
- Absolute emissions reductions by the participant
- Relative emissions reductions (i.e. reductions against turnover)
- An overall score (achieved by a weighting of the above scores).

The administrator may also publish other information in relation to participants. See article 67 and Part 3 of Schedule 20.

F. Revenue recycling grants

Revenue recycling grants are not dealt with by the Order. This is because they are paid under the stand-alone power at section 53 of the Climate Change Act 2008. The performance tables, will, however, be a key determinant in the allocation of the amounts of grant to different participants.

G. Obligations on persons other than participants

Organisations which consume settled half hourly electricity supplies, but which do not meet the qualification criteria, are required to provide the administrator with information as to their electricity consumption. See Chapter 1 of Part 5. They must comply with this requirement by the deadline for participants’ registration.

Electricity suppliers and distributors and gas suppliers are required to provide the administrator, and any participant who is their customer, with information in accordance with Chapter 2 of Part 5. In particular, they must provide customers with information relating to their electricity or gas use (or both): see article 57.

H. Allowance trading

Both participants and third parties may trade allowances on the CRC secondary market. The relevant requirements are set out in Parts 7 and 8.

I. The administrator and enforcement

The administrators of the scheme are the Environment Agency (EA) (for England and Wales), the Scottish Environment Protection Agency (SEPA) and the Northern Ireland Department of the Environment (DOENI). Most functions will be performed separately by each of these bodies within the relevant part of the UK but with appropriate coordination between them.

The main functions of the administrator are as listed below. Some of these functions apply to persons other than participants:

- Power to postpone deadlines. See article 59.
- Powers to require participants to provide information about their energy consumption, emissions, or business. See articles 60 to 62.
- Power to audit and verify information. See article 63.
- Duty to publish information. This function is to be performed by the EA on a UK-wide basis.
- Power to conduct inspections, if necessary under warrant. See articles 63 and 68 and Schedule 21.
- Power to issue enforcement notices. See article 69.
- Power to determine information. See article 70.
- Duty to impose civil penalties for failure to comply with the scheme. See article 71 and Schedule 22. This is subject to some discretion (article 71(2)).
- Powers and duties imposed in relation to allowances and the secondary market. See Part 7. This function is to be performed by the EA on a UK-wide basis.
- Duty to establish and maintain a Registry. See Part 8. This function is also to be performed by the EA on a UK-wide basis.
- Power to recover its administrative costs, by way of charges. See article 89 and Schedule 23.

Participants (and, where relevant, other persons) may **appeal** against the administrator's decisions. See article 93 and Schedule 25.