



EMISSIONS TRADING: EU AND UK SEEK TO MITIGATE BREXIT 'CLIFF EDGE'

EU Institutions and the UK Government have made separate proposals in relation to the EU Emissions Trading System for dealing with the immediate consequences of the UK leaving the EU in March 2019 and minimising the impact of a “cliff edge departure”. Responses to the UK Government’s proposals must be made by 24 November 2017.

Since the UK’s referendum on leaving the EU, there has been continuing uncertainty over the UK’s future participation in the EU Emissions Trading System (EU ETS); in particular the EU has raised concerns as to what would happen if there was no deal on UK participation prior to the UK’s departure from the EU in March 2019 (almost two years before the end of Phase III of the EU ETS in 2020). This concern revolves around the fact that UK operators would have no compliance obligations under the EU ETS after March 2019 (and in particular no obligation to surrender allowances at the 30 April 2019 deadline). Unless the UK either stays in the EU ETS after Brexit or establishes a new system for which its UK-issued EU ETS allowances can be used, large scale sell-offs of such allowances are likely and could lead to a further depression in allowance prices.

The EU and UK have now both set out their respective positions for dealing with the possibility of the UK leaving the EU without a deal on the EU ETS.

EU PROPOSAL – EXCLUSION OF NEW UK ALLOWANCES

In September/October 2017, EU institutions announced a proposal to minimise the impacts on the EU ETS of the UK’s departure from the EU by excluding new allowances issued by the UK from the EU ETS in the event there is no UK/EU deal on the EU ETS prior to March 2019. The approach would be implemented by the following changes to the EU ETS Directive and the Registries Regulation:

- Allowances issued as from January 2018 by the UK under auction or free allocation would be marked as UK allowances (New UK Allowances). Currently, allowances are not differentiated as to their origin of issue. Technically, the amendments relate to any allowances issued by a State whose obligations under the EU ETS are going to lapse.
- As from January 2018, New UK Allowances will not be accepted for compliance purposes in the EU ETS.

The prohibition would, in particular, mean that New UK Allowances could not be used for surrender against 2017 emissions (for which the surrender deadline is 30 April 2018 – i.e. while the UK is still fully subject to EU obligations). A key implication is that UK operators who do not hold sufficient allowances for their 2017 emissions before the

Key Issues

- EU and UK have made separate proposals to deal with the impact of the UK leaving the EU before the end of Phase III of the EU ETS
- EU proposes to prevent new UK allowances issued from January 2018 being used for compliance
- UK proposes to bring forward the compliance deadline for 2018 emissions, and suspend the allocation/auction of allowances in January 2019

20 April 2018 surrender deadline will need to acquire their allowances through trading on the registry rather than through allowances allocated or auctioned by the UK in January 2018.

UK – BRINGING FORWARD THE 2019 COMPLIANCE DEADLINE

Little had been said by the UK Government in the period following the referendum in relation to the UK's future position in the EU ETS. While the Government had confirmed that it intended for the full body of EU law to be implemented in UK law upon Brexit, it has thus far remained unclear as to what this would mean for compliance with EU ETS obligations. The Department for Business, Energy and Industrial Strategy (BEIS) has now responded to the EU position with its own proposals set out in a Consultation Paper. Firstly, it is proposing that, during a transitional period of 2 years from March 2019, the UK and EU would have access to each other's carbon markets upon current terms.

Secondly, BEIS recognises the EU's concerns about the potential impacts upon the carbon markets of a cliff edge departure with no deal in March 2019. However, it is also concerned about the impact upon operators of prohibiting use of New UK Allowances in the EU ETS from January 2018 onwards particularly given the April 2018 compliance deadline. For this reason, BEIS makes 2 proposals to deal with the EU's concerns:

- The compliance deadline for surrendering 2018 emissions would be brought forward to 22 March 2019 from 30 April 2019 (i.e. to a date before the UK's departure). Similarly, the reporting deadline would move forward to 28 February 2019 from 31 March 2019.
- The UK Government will suspend issuing New UK Allowances in 2019 (both through auctioning and allocation) unless and until arrangements between the UK/EU as to the post-Brexit deal on the EU ETS become clear.

COMMENT

The proposal to bring forward 2018 compliance dates may well be sufficient to put on hold the EU proposals to ring-fence and exclude new UK allowances for the time being as it should give comfort that New UK Allowances issued in January 2018 will not be dumped en masse into the EU market. However, the issue will remain in relation to 2019 allowances and, unless a negotiated agreement is forthcoming before January 2019, the EU proposal seems likely to be applied to UK 2019 allowances unless the UK has formally agreed, by that time, to remain in the EU ETS for future years (either for a transitional period or more permanently). BEIS' announcement to suspend 2019 allowances does not take the position much further, but at least amounts to a public recognition by the Government of the need to resolve the issue one way or another.

BEIS has given a short deadline for responding to this consultation; responses must be received by 24 November 2017.

The Consultation Paper can be found at:

https://beisgovuk.citizenspace.com/heat/eu-ets/user_uploads/eu-ets-consultation-bringing-forward-2018-compliance-deadlines-in-the-uk-6nov2017-final.pdf

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