

Appendix C

NEW ENTRANTS, CLOSURES AND AUCTIONING

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A. Introduction

1. The UK government has set aside a number of allowances from the overall total of allowances into a New Entrant Reserve (NER) to allocate free of charge to eligible new entrants. This Appendix sets out the detailed plans made by the UK government with respect to new entrant and closure eligibility and treatment.

B. Quantifying the NER

2. The NER will comprise 46.8m allowances, representing 6.3% of total allowances. The methodology for its calculation, was presented in Annex 2 of the explanatory note to the UK National Allocation Plan Revised list of installations and allocations published on 14 February 2005. This information, with some minor modifications, is set out below.
3. The methodology for calculating the size of the NER has combined two approaches. The first approach, the 'bottom-up' method, used information on new entrant and closures provided to us by installations detailing expected future investments or those that are already underway. Many installations provided the UK DTI with completed benchmarked spreadsheets, based on work commissioned by Future Energy Solutions (FES)¹. The most up to date version of this spreadsheet will be used to determine actual allowances for new entrants. Data collected has been input into the NER calculations, disaggregated by sector.
4. The second approach, the 'top down' method, was to estimate the amount of new entry in each sector that underlie the projected growth rates used to determine sectoral allocations. The cut-off date used for the purposes

¹ The FES report can be found at http://www.dti.gov.uk/energy/sepn/allocation_report.pdf.

of calculating the size of the NER in the UK is 31 December 2003, and growth after this point gives an indication of net allowances needed in each sector for allocation to all possible new entrants or to expansion by existing installations. Growth rates used are those underlying the sectoral allocations and consistent with the Updated Energy Projections (UEP). For Climate Change Agreement (CCA) sectors these are output growth rates, and for non-CCA sectors the emissions growth rates have been applied. The output growth rates in the NAP are based on independent research we commissioned from Oxford Economic Forecasting (OEF)² and from CRU Strategies for the Steel sector³ combined with Government's own assessment of prospects in these sectors.

5. Although some of the growth after December 31, 2003 will be due to new entrants, it has been recognised that not all the predicted growth will come from new entrants that are eligible for the NER – some could come from increased output from existing installations. This consideration has been taken into account in determining the overall NER, and has adjusted the 'top-down' estimates according to what information is available from the 'bottom-up' approach detailed above. Different combinations of these approaches, and how these have been used to determine the NER are detailed below:
 - (i) Where there are no known new entrants in the sector, the NER from the 'top-down' method is halved. This allows half the growth contained in the sectoral growth rates to go to new installations and half is assumed to apply to existing installations;
 - (ii) Where the 'bottom-up' information suggested a NER of less than that shown by the 'top-down' method, we have assumed that the remaining growth (the difference between these two approaches) is more likely to be with respect to existing installations than further new ones. In this case the NER is the sum of the 'bottom-up' estimate plus one third of the difference between the 'bottom-up' and 'top-down' methods;
 - (iii) Where there are more allowances for known new entrants than that suggested by the underlying growth rates, the NER is determined by the 'bottom-up' method alone;
 - (iv) Where the best estimate of known new entrants is zero and where growth rates are positive we have allowed for a nominal NER of 10% of 'top-down' NER estimate. This is a cautious assumption reflecting inherent uncertainty about predicting into the future;
 - (v) Where no information has been obtained on known new entrants, or where our best estimate of them is zero and where

² See: http://www.dti.gov.uk/energy/sepn/oef_final.pdf

³ See: <http://www.defra.gov.uk/environment/climatechange/trading/eu/pdf/ironsteel-report.pdf>

sectoral growth rates are negative we have set the NER to zero. This is because both sources of estimates of the NER suggest no net new sectoral growth.

6. Sectors with an absolute CCA target have been treated slightly differently in terms of the way in which their contribution to the NER has been calculated. The approach used depends on whether growth in the sector was taken into account in determining the target. Where the absolute target already includes an estimate of new entry in the sector, that estimate has been included in the NER. Where new entrant growth is not included in the CCA target, growth has been added to the sector allocation before the new entrant contribution was removed.
7. Part of the NER will be ring-fenced for use by any Good Quality Combined Heat and Power (GQCHP) new entrants who are fully qualified (see paragraphs 36 and 37). New entrant applicants which are partially good quality only will be expected to indicate this on their application forms and only the GQCHP part of their application will come from the ring-fence, with the rest coming from the general NER. This CHP ring-fence will function in the same way as the rest of the NER, except where otherwise indicated in this document. Should the GQCHP portion of the NER not be fully utilised, Government may re-allocate these allowances to the main NER.
8. The size of the CHP ring-fence has been based on research the DTI commissioned by Cambridge Econometrics which suggested that, under central case assumptions and with policy measures currently in place, there will be 8.1GW of installed good quality CHP capacity in the UK by 2010. In order to convert this into an estimate of likely ETS allowances during phase one, assumptions on the profile of capacity build between now and 2010, the proportion of new build likely to be covered by ETS, plant load factors, efficiency and emission factors were applied. The final size of the CHP set aside part of the NER is 13.9 million allowances.
9. The bottom-up element of the CHP reserve has been taken from incumbents as described in paragraph 5. The difference between the bottom-up estimates of CHP and the top-down estimate described above has been delivered by taking an equal proportion from all incumbents, after the NER is taken into account, and from all new entrants, including CHP new entrants.
10. Installations that enter the EU ETS after the cut-off date to be in the final installation level allocation but should have entered the scheme before are not eligible as new entrants. However, a small number of allowances has been set aside from the total quantity of NER allowances (1.5 MtCO₂, approximately 0.2% of the total) to issue allowances to late applicants.

Table 1: Breakdown of the new entrant reserve⁴

	Total NER during Phase I
	MtCO ₂
New Entrants (non CHP)	31.4
GQCHP NER	13.9
Set aside for late applicants	1.5
Total set asides	46.8

11. The size of the NER and the GQCHP NER will decrease as allowances are issued to new entrants both in their first year of operation, and during their subsequent years of operation during the first phase. The NER will increase in size when installations fully close and surrender their permit, at which point all non-issued allowances will go into the NER. Where GQCHP installations fully close the non-issued allowances associated with those sites will go into the GQCHP NER.
12. Some of the allowances that have not yet been issued from the NER, and therefore still remain a part of the NER, will be tagged and therefore reserved for certain operators as the result of their successful application to the NER and will not be available for the use of any operator, despite the fact that they have not been issued.
13. Where, in accordance with UK legislation, the amount of allowances allocated to an installation is reduced in order to correct an over-allocation of allowances to that installation as a result of the installation providing false or misleading information, non-issued allowances to the equivalent of the over-allocation will be added to the NER (thereby increasing the size of the NER).

C. Eligibility for access to the NER

14. In order to qualify as a new entrant and thus be eligible for allowances from the NER, an installation must have commenced or extended, or have plans to commence or extend, a Schedule I activity after 31 December 2003 but before the end of 2007. The installation must also fulfil the criteria set out in the following paragraphs.
15. The following are eligible types of new entrant:
 - new installations that commence a Schedule 1 activity after 31 December 2003 (either a brand new plant or where an increase in

⁴ The details of sectoral contributions to the NER are given in Appendix B

output capacity brings an existing plant within the scope of the scheme);

- extensions to existing installations that result in either a net increase in capacity of a Schedule 1 activity carried out in the installation and/or the carrying out of an additional Schedule 1 activity in the installation after 31 December 2003. This eligibility is subject to the detailed definitions set out in Section C1;
- installations that recommence operations (after 31 December 2003) following temporary closure (which took place on or before 31 December 2003);
- changes in offshore installations reflecting new tiebacks and installation modifications to enhance the recovery of offshore oil and gas reserves (after 31 December 2003, see Section C2); and
- increases in Good Quality Combined Heat and Power (CHP) capacity (after 31 December 2003, see Section C3).

To be eligible these installations require a variation in their permit, however, any variation to the permit other than those outlined above, will not qualify for access to the NER.

16. The UK Government has made an exception to the closure rules to recognise site rationalisation during Phase I of the scheme, as such rationalisations can improve overall energy efficiency (see section F3).

17. Installations or pieces of equipment returning from partial or temporary closure after 31 December 2003, where this closure took place during the baseline period, or before, can apply for allowances from the NER. These installations, or part installations, will only be eligible for free allowances from the NER where the temporarily closed piece of equipment was not permitted in the baseline period and therefore not included in the baseline allocation. The size of the free allocation due to such installations or parts of installations will be calculated on the basis of their disaggregated historical data, if this is available. Where this is not available the allocation will be based on the benchmarked spreadsheet, as for other new entrants.

Types of New Entrant: Further Details

C1. Extensions

18. A change at an installation which takes place after 31 December 2003 will be considered potentially to constitute an eligible extension, if it involves a physical change that increases the net output capacity of the Schedule 1 activity. Subject to the following paragraphs, the physical change may be either:

- (i) the introduction of a new piece of equipment; or

(ii) an extension to an existing piece of equipment.

19. For the majority of sectors, an extension will only be eligible for allowances from the NER where it involves a piece of equipment which directly produces emissions which must be accounted for under the scheme. These pieces of equipment are listed in the new entrants calculation spreadsheet (described in paragraph 50). For these sectors, the calculation of allowances to be allocated to an eligible extension will be based on a direct emissions approach, i.e. the allocation will be based on the benchmark associated with the piece of equipment that has been introduced or extended.
20. For extensions in the iron and steel and refineries sectors, the allocation will be calculated using an integrated approach, instead of the direct emissions approach i.e. the calculation will be based on how the new or extended piece of equipment affects the overall throughput capacity of the Schedule I activities at the installation (for more information see paragraph 42). It is only in these two sectors that pieces of equipment, which do not directly produce emissions themselves, can be eligible for allowances from the NER through a calculation of the effect that they have on the system.
21. Extensions in the electricity generation sector and refineries sector to meet low-sulphur fuel obligations will not be eligible for allowances from the NER. The increase in emissions attributable to the installation of such units will be taken into account in the allocation given to the electricity generation sector and refineries under the final installation level allocation.
22. Operators extending the capacity of their installations or planning a new installation must provide a realistic start date for the extension. Operators are also obliged to inform the regulators of any change to the nominated start date.
23. As part of the application process, operators will be asked to provide information on the installation's capacity before the changes, and information on all of the changes to the installation that have had an effect on the relevant capacity of the installation and that have taken place since either:
 - a. The time of the installation's last successful application to the NER;
or
 - b. The end of the baseline period on which the allocation given in the final installation level allocation was based, where there has been no previous application to the NER.

24. For the purposes of this determination, capacity here refers to the capacity that is comparable to the new entrant application. For example, if the application is referring to a new boiler, the information required is on previous boiler capacity. The notion of comparable capacity should cover all cases where equipment may replace other equipment, even where they are not the same e.g. boilers replacing power plant. The regulator has the discretion to determine what is considered comparable capacity and may ask for further information from the operator if necessary.
25. For the purposes of calculating the net capacity in a way that covers overlap of operation with existing pieces of equipment that are being replaced, installations are required to provide information about replacements taking place within six months of the start date of the new entrant (i.e. expected closures of the equipment that is being replaced). Regulators will award allowances to the new entrant on the basis of the overall net difference in capacity expected when the replacement is complete.

C2. Changes in offshore

26. Offshore projects that are eligible new entrants and begin operation after 31st December 2003 may qualify for free allowances from the NER. The following types of offshore installations are considered to be eligible new entrants:
- new installations and new combustion capacity at existing installations;
 - tie backs i.e. drilling centres and oil and gas wells serving new fields or new areas of a reservoir that are connected to existing installations; and facility modifications to existing installations directly related to the production, processing and delivery of the offshore oil and gas reserves which meet the following criteria:
 - i. the tiebacks/modifications will result in a quantified enhanced recovery of reserves;
 - ii. the tiebacks/modifications will require a variation of the relevant permit; and
 - iii. the tiebacks/modifications will result in a quantified increased additional power demand that will generate additional emissions from the existing combustion plant.
27. All of the offshore projects eligible for free allowances from the NER are important for enhancing offshore oil and gas capture and thus ensuring security of supply. Operators face a range of investment opportunities, worldwide, to recover oil and gas. Access to the NER will help to ensure that investment in projects to maximise recovery of Continental Shelf oil and gas remains attractive. If these reserves are not accessed at this present time, there is a strong possibility that they may be impossible to recover in the future.

28. It will not be possible to obtain allowances from the NER for any drilling programmes related to the enhancement projects, as the historic baseline data is assumed to include a component relating to past drilling activity.
29. It will only be possible for installations that are physically offshore, i.e. platforms and floating installations, to apply for this type of extension. Installations that are physically onshore, although they may have previously been included in the offshore sector for the purposes of forecasting, are not eligible.
30. In all cases, there will be a requirement to verify the applications for allowances from the NER, to confirm that the proposals meet the criteria listed above.
31. The allocation to the new entrant offshore installation will be calculated using the standardised benchmarking methodology for offshore new entrants. This calculation will need to be certified by the verifier, as part of the verification of the NER application.
32. The additional allocation will be calculated based on the date from which the changes to the installation become operational.

C3. Increase in good quality CHP capacity

33. New GQCHP installations, which fall within the EU Emissions Trading Scheme and begin operation after the 31st December 2003 will be eligible for allowances from the NER as new installations. In addition, extensions to the existing power capacity of a GQCHP installation will also be eligible for allowances from the NER on the same basis as extensions in any other sector. A proportion of the NER will be set aside for GQCHP schemes.
34. Increases in good quality capacity⁵ of an installation after 31 December 2003 which fall outside those changes described above will also be eligible to apply for allowances from the NER in the circumstances set out below.
35. Where the good quality capacity of a CHP installation is expected to increase (by a minimum of 5% as a proportion of total power capacity "TPC"), as compared to the rating of the installation on which the previous

⁵ The boundaries of a CHP scheme under the CHPQA certification programme do not necessarily fit the boundaries of the EU ETS installation. The allocation of allowances will only relate to that part of the CHP scheme that fits within the relevant boundary of the EU ETS installation.

allocation was based, the CHP installation will be eligible to apply for allowances from the NER.

36. For a CHP scheme to qualify as GQCHP, it has to meet the following criteria:
 - the power efficiency (power output divided by fuel input) is greater than or equal to 20%; and
 - the Quality Index (QI) (which combines the power and heat efficiencies, adjusted by factors to take into account the size, technology and fuel of the individual scheme) is greater than or equal to 100.
37. CHP capacity that meets both these criteria is considered to be good quality. Where a scheme's QI is 100 or more, its full power output, and therefore total installed power capacity, is considered to be good quality. In other schemes, where the QI is less than 100, only a proportion of its power output, and so only some of its power capacity, is considered to be good quality (partially qualified CHP Schemes). As a consequence, the proportion of a scheme that is considered GQCHP may vary from year to year.
38. Operators of CHP schemes, who propose to increase their good quality capacity at some point during the phase, may apply to the regulator for allowances and a variation to their permits.
39. Prior to making its application to the regulator, the operator must obtain a new certification from the CHPQA (Combined Heat and Power Quality Assessment) programme to show its expected increase in GQ CHP capacity. In calculating the increase in qualifying capacity the CHPQA Administrator will "map" the boundaries of the CHP Scheme against the relevant boundaries of the EU ETS installation and only include the increase in qualifying capacity that falls within the EU ETS installation boundary.
40. The allocation to the installation will be calculated using the published benchmarks for new entrants. The benchmarked allocation before and after the expected increase (using the certified TPC and qualifying capacity values for each) will be calculated. This additional allocation from the NER to the installation will be equal to the difference between the two benchmark calculations. Any NER allowances will come from the GQCHP set-aside element of the NER, or the general NER should there be insufficient allowances remaining in the proportion of the NER set aside for GQCHP. The additional allocation will be based on the date from which the installation increases its GQCHP capacity. As set out in paragraph 7, the GQCHP NER may be merged with the main NER towards the end of Phase I.

D. Calculating the allowances to be allocated to new entrants

41. The allocation to a new entrant will be calculated through the application of standardised allocation methodologies. These methodologies reflect technology, load and fuel specific factors, and applicable reduction factors.
42. In the iron & steel and refineries sectors all the installations can be considered as highly complex systems i.e. there is a feedback of gases or fuels within the installation to be used as fuels elsewhere in the EU ETS installation, where a fuel is a product that can be converted to heat. This complexity has made it very difficult to calculate standardised emissions figures for every potential new entrant. It has therefore been decided that, for these sectors, the more appropriate method of calculating an indicative allocation is to calculate the increase in emissions of the system as a whole i.e. an integrated approach.
43. The majority of sectors are dealt with using a fully standardised approach, however, in the case of: onshore gas distribution; mineral oil refineries; offshore; and iron and steel, it has not been possible to develop a fully standardised approach. In these cases the approach is partially standardised, with a systems approach used in the iron and steel and refineries sectors. For all of these partially standardised sectors, individual pieces of data on utilisation or throughput will be required for most applications, and verification from accredited independent experts will also be needed to support the use of this individual data. In the cases where an applicant in these sectors is applying for a fully standardised new entrant e.g. a boiler at an offshore installation this verification will not be required.
44. Using a standardised spreadsheet methodology, which also includes formulae for the partially-standardised sectors, the allocations to new entrants will be calculated in advance, and the allocation will not be subject to ex-post adjustment of allowances once the new entrant activity has commenced.
45. For extensions, the allocation will be based on the net increase in relevant capacity at the installation. The benchmarked allocation based on the capacity of the installation before and after the changes will be calculated. The allocation from the NER to the installation will be equal to the difference between the two benchmark calculations. Capacity for these purposes, should be understood according to the explanation in paragraph 23, i.e. relating to the change proposed under the new entrant application. Furthermore, in the cases of overlapping pieces of equipment during a replacement net increase relates to increase in capacity after six months, as described in paragraph 25. Paragraph 25 also explains that the

regulator may wish to allocate different amount of allowances in the first calendar year, or part of calendar year, in relation to this overlap.

46. In the case of new combustion equipment, where the increase in capacity is due to an additional piece of equipment being added, the regulator may choose to run the spreadsheet once for the difference in the capacity of the new piece of equipment to determine the allocation rather, than using the difference between the two benchmarked calculations. This is because the spreadsheet provides a non-linear estimate of emissions produced by certain types of combustion equipment.
47. For extensions in the sectors where an integrated approach has been used, the additional allocation will also be based on the net increase in capacity. In these cases, the operator must provide an opinion from an independent verifier confirming that the initial and final capacity, or other relevant parameters e.g. throughput, in a modeled version of the installation, are fairly stated.
48. A new entrant will receive a partial allocation of allowances from the NER for the first calendar year in which operations commence on a pro-rata basis and a full allocation for subsequent years in Phase I.
49. An extended period of commissioning is only taken into account when calculating the allocation to new entrants in the cement and electricity generation sectors. These were considered the only two sectors where it was both appropriate and possible to devise an average extended period of commissioning. A standardised approach is taken to commissioning that assumes a commissioning period of 50 days, during which new entrants in these sectors will receive only 50% of their allocation. New entrants in all other sectors will receive an allocation based on the full, commercial rate of operation from the start date of the new entrant activity.
50. Operators will be asked to run the standardised spreadsheet when making a new entrant application. The most up-to-date version of this spreadsheet can be found at the following link: <http://www.dti.gov.uk/energy/sepn/euets.shtml#neca> entitled "Calculating the allocation for new entrants – spreadsheet for applicants." For extensions, or in the case of changes such as increases in GQCHP or offshore modifications, operators will need to run the spreadsheet twice, as described above, providing a "before" and an "after" scenario. The difference should indicate the number of allowances that the installation is eligible to apply for.

E. Closure

51. An installation is considered to have ceased production when:

- the Schedule I activity at the installation has ceased operating; or
- the capacity of the Schedule I activity at the installation has dropped below the thresholds contained in Schedule I.

52. It is mandatory for an installation that is ceasing the operation of its Schedule I activity to notify the relevant regulator in order to surrender its permit.

53. Installations may claim that they are not permanently ceasing operations according to paragraph 51 but have only temporarily shut the installation. The regulators will use their discretion to distinguish between permanent closures and cases where a “temporary period” of closure has occurred during the normal course of business. Only closures that are outside the “normal course of business” would trigger the notification requirement.

54. Installations that permanently cease operation in accordance with paragraph 51 will retain allowances for the year in which closure occurs but the allowances allocated for the years after closure will not be issued to such installations. Allowances will not be allocated in respect of an installation where the permit has been revoked or surrendered.

55. There are several situations relating to closure where the issuing of allowances to an installation may be delayed. These situations will occur where, at the time of issuing allowances:

- (i) an application to surrender a permit is being processed by the regulator;
- (ii) there is an unresolved appeal on a permit surrender or revocation application;
- (iii) a decision has been made to revoke a permit or for it to be surrendered, but this decision has not yet taken effect;
- (iv) a rationalisation application being processed by the regulator (see E1 below);
- (v) there is an outstanding appeal on a rationalisation application; or
- (vi) the decision on a rationalisation application has been made but has not yet taken effect;
- (vii) the government is aware that an installation has closed in 2004, prior to legislation being in force imposing an obligation on the operator to surrender its permit on closure, and that permit has not yet been surrendered or revoked.

56. The decision of whether or not to delay the issuance of allowances in the situations outlined above will depend solely on the date of the relevant closure, or the closing installation in relation to the rationalisation where rationalisation applications are concerned. The delay of issuing

allowances will take place in circumstances where this closure has taken place up to and including the 31st December in the year preceding the issuance of allowances or when there is doubt as to when the closure has taken place. A delay in issuing allowances will not take place in the circumstances outlined in paragraph 55 where the closure has taken place on or after the 1st January in the year of issuing allowances in question.

57. Where, according to the circumstances described above, a delay in issuing allowances will take place, the delay will last until such a time as the regulator has completed the task of assessing the revocation or rationalisation, and the resulting outcome has taken place (e.g. the revocation of the permit), or the delay will last until the appeal has been decided, where an appeal is involved.
58. Where a closure has taken place, this will be reflected by making a correction to the UK's national allocation plan table to reflect the fact that no allocation shall be made to the installation in the years after that in which it closed, and that those allowances are to be added to the NER.

E1. Rationalisation

59. In the context of new entrant and closure considerations, rationalisation occurs where the Schedule I activities at one installation are closed and operations are moved to another installation or installations during the period 2004-7. Under the closure rules described above the closed installation will lose its right to further allocation, potentially leaving the remaining installation(s) short of allowances with respect to the transferred production.
60. Where an operator considers that rationalisation has taken place, the operator may apply to continue to receive a percentage of the allowances from the installation where the Schedule I activity closed. These allowances could be used to cover the emissions from the production transferred to the other installation(s).
61. The proportion of allowances retained will be equal to the proportion of production associated with the EU ETS activity that will and can be transferred to the remaining installation(s).
62. The installation(s) receiving the transferred production may also be eligible to apply for NER allowances. However, such an application must be distinct from the rationalisation application. The operator cannot apply for NER allowances for an investment that is needed to extend the installation so that the operator can receive the amount of production being transferred under the rationalisation rule. Rationalisation will only be

allowed where the receiving installations have sufficient existing capacity, not extended through an NER application in the first phase, to accept the transferred production claimed in the application.

63. Rationalisation rules will not apply to the electricity generating sector because:
- it is deemed important to create an incentive to retain capacity within the generation sector to support security of supply objectives. Fossil fuel powered generating plant approaching closure is most likely to be operated at times of high power demand and so are important for maintaining supply in these periods;
 - at times of peak demand, other generating stations are likely to be producing at close to full capacity and so it is unlikely to be possible to transfer production at these times to other stations; and
 - there is no objective way in which it can be determined whether reduced generation from one station has been compensated for by increased output at another specified station or at some combination of other stations.
64. The rationalisation rule will only be applicable where both the closing and the receiving installation(s) have the same EU ETS permit holder. The installations involved in the rationalisation must all be within the UK and fall within the scope of the EU ETS.
65. The rationalisation rules set out above do not apply if the rationalisation is to an installation that has been temporarily excluded from the EU ETS. The rationalisation rule will also not apply if the rationalisation is to an installation that has ceased to carry out a Schedule I activity.
66. Where the receiving installation used as the basis of a rationalisation application subsequently ceases to carry out a Schedule I activity, the rationalised permit will lapse and the related allowances will no longer be issued in the years following this closure unless another rationalisation application is made and accepted for the transfer of production to another installation(s). In this case, it may be that some of the allowances under the retained rationalised permit, as well as the permit itself, will be retained. Where there was more than one receiving installation as part of the rationalisation application, the Schedule I activity must cease at all of the receiving installations before the rationalised permit lapses and the related allowances are not issued.
67. To qualify for rationalisation the transfer of production must take place between installations within the same sector. Also, at least 50% of production (i.e. final output of goods and services) taken as an average of the three previous years, from the closing site must be transferred to another site owned by the operator. The production being transferred must

be classified as the same product according to the Standard Industrial Classification code taken to the three digit level.

68. To qualify for rationalisation there must be full and permanent closure of the closing installation. The operator must apply to the relevant regulator for this closure and must make an application for rationalisation at the same time.
69. Where a rationalisation application has been determined and where appropriate, this will be reflected by making a correction to the UK's national allocation plan table to reflect the change in allocations.

F. Allocation process

F1. The Role of the Regulator

70. The regulators for this legislation are the [Environment Agency](#) for installations in England and Wales, [Scottish Environment Protection Agency](#) for installations in Scotland, the [Chief Inspector](#) for installations in Northern Ireland and the [DTI \(Energy Resources and Development Unit\)](#) for installations situated offshore.
71. The regulators are responsible for issuing and varying permits in respect of the installations covered by the EU ETS. The identification of new entrants and closures will be linked to the granting, variation or revocation/surrender of permits, and therefore the regulators will have an important role to play. The regulators will be responsible for processing all new entrant and closure applications.
72. The operator of an installation requesting free allowances from the NER, or carrying out a closure (including a rationalisation), needs to apply to the relevant regulator. Application forms are available from the regulator outlining the information that must be provided.
73. The specific information required in new entrant applications should serve to establish in more detail the nature and timing of the new entrant, to obtain emissions information, and to establish that the application is serious and advanced enough to receive a place in the queue for free allowances.
74. In some cases an operator may wish to apply for a sequence of changes on one application form. The regulator will process such multiple changes for one fee provided only one start date is used. This start date must be the realistic estimate of the start date for the final change. The operator may choose whether to submit several application forms, and several fees, or include more than one change on one application form as described above.

75. The regulator will reject any application for allocations from the NER which it considers to be speculative, unrealistic or false. The purpose of this approach is to ensure that the allowances from the NER are not committed to developments that are unlikely to take place during Phase I.
76. The regulator will decide whether the application should receive free allowances from the NER and what the size of this allocation should be in accordance with the rules set out earlier in this Appendix. The regulator will also decide whether correct information has been given about closures.
77. For rationalisation, the onus will be on the operator to provide verified evidence to support its application to the NER alongside the rationalisation application. The regulator will determine whether the transfer of production is taking place within a time period after production has ceased at the closing plant, such that it can be considered as rationalisation. The regulators' role in the case of rationalisation will be to ensure that the verified opinion is provided and that any extra data relevant to the application has also been submitted. It is this verified opinion that will inform the regulator whether or not the operator is making a sound claim.
78. The Environment Agency will act as manager of the queue system that determines the priority of receipt of free allowances from the NER, for all of the regulators in the UK.

Changes to applications

79. Where an operator's plans change to involve a fundamentally different type of technology or process, or to require the use of a different benchmark, the operator will have to notify the relevant regulator. These are considered major changes and if required by the regulator, the operator will then have to withdraw its current application, losing its place in the queue, and submit a new application to the NER with respect to the new plans.
80. Operators must provide a realistic start date for their application and are obliged to inform the regulators of any change to the nominated start date.
81. Operators must provide a realistic estimate of capacity in their application form and must inform the regulator of any change to the original capacity. Where changes in capacity result in a decrease in emissions the allowances tagged for the installation will be modified accordingly. Where the change results in an increase in the emissions required the operator must submit a new application with respect to the increase.

82. In the case of applications that require verification, revisions to capacity will require the submission of a new verification document. This will not result in loss of their place in the queue for any application for allowances up to the original quantity of allowances applied for.
83. Changes to capacity and start date are likely to be viewed as minor changes and will not result in the operator losing their place in the queue. However, if the original application provides insufficient evidence to satisfy the regulator that the application is speculative with respect to start date or capacity, applicants may not secure their place in the queue at the outset.

F2. The Queuing system

84. The total size of the NER will vary, increasing as closures are processed and de-allocated allowances are returned, and decreasing as new entrant applications are processed and allowances are issued.
85. A queuing system will enable operators to have fair access to the NER as it changes in size.
86. The queue will operate in two stages. First, a provisional place will be awarded in relation to the date on which a completed application has been deemed “duly made” by the relevant regulator. Secondly, a confirmed place will be given when the relevant regulator has processed the application.
87. An application will be approved as “duly made” where all of the relevant information needed for the application has been provided, even though at this stage the application has not yet been assessed.
88. The information provided to the regulator as part of the new entrant application must include:
- (i) a completed NER application form;
 - (ii) the input data used in the new entrant spreadsheet showing the technologies eligible for NER allowances and giving an indicative allowance figure. This spreadsheet should be completed and available should the regulator require it. For new technologies that do not appear on the spreadsheet, the technology should be indicated in the application form, noting that benchmarks for the applicable technology are not included in the spreadsheet;
 - (iii) a description of the installation in its new configuration, with details of the changes (to be) made, including expected changes in relevant emissions;

- (iv) the date that emissions will start, as indicated in the spreadsheet, with a timetable for construction and commissioning. The operator must state a date that is reasonable and provide supporting evidence;
- (v) evidence that shows to the regulator's satisfaction that the NER application is not speculative, contingent, unrealistic or false. The evidence required for these purposes will vary depending on the size, nature and scale of the new entrant (see paragraph 89 below);
- (vi) verification of the spreadsheet information submitted for the sectors where a verified opinion is required i.e. iron and steel throughput, rationalisation, onshore gas distribution; increase in GQCHP qualifying output capacity; mineral oil refineries and offshore installations. See paragraph 43 for the details of when verification is required and paragraph 96 for the situation as regards verification for the period of time where accredited verifiers are not available;
- (vii) for all CHP applications, a certificate of the Good Quality status of the planned installation or extension, indicating the percentage GQ of the extension or installation. This certification should be obtained in line with the description in paragraph 39 (which relates to cases where the GQ qualifying output capacity is changing in the absence of an extension or new build installation) ; and
- (viii) for extensions, applications should also include details of the capacity before and after the proposed change, where "before" is interpreted according to the description in paragraph 23, and the nature of the change.

89. Evidence that the NER application is not speculative, contingent, unrealistic or false would include:

- a) for all applications -
 - i. recorded management decisions that enable the expenditure to proceed and which indicate that this expenditure has been committed at a senior level;
 - ii. applications or permissions under planning laws or Integrated Pollution Prevention and Control legislation (IPPC) where relevant;
 - iii. information demonstrating a contractual agreement or purchase in respect of the new entrant equipment and building/installation;
 - iv. sector specific information where relevant; and/or
- b) for applications in respect of extensions - the original verification of baseline data used for calculating the final installation level

- allocation, where relevant, and data submitted for the purposes of the original allocation to the installation.
- c) for applications for extended use of CHP- information on new connections to CHP;

Whether the information provided by the applicant, according to the list above, is sufficient to show that the application is not speculative, contingent, unrealistic or false will be determined by the regulator at their discretion.

90. As well as providing the relevant information, an application will only be considered “duly made” if accompanied by the appropriate application fee. For applications received before the legislation requiring new entrant applicants to pay a fee has come into force, this fee must be received by the relevant regulator within 15 working days of the legislation coming into force to meet the “duly made” requirement and to prevent operators losing their place in the queue.
91. For installations in the offshore sector, payment procedures are different and therefore the application can become “duly made” without the application fee having been received. The relevant regulator will send an invoice to the operator within 28 days of receiving an application and payment must be received by the regulator within 28 days of the date of this invoice otherwise the applicant will immediately lose the place in the queue that had been previously secured by being considered “duly made” without payment. In the case of offshore installations who have made their application before the amendment to the EU Emissions Trading Regulations have come into force, the regulator will be obliged to send the invoice within 28 days from the date on which the Regulations come into force. Then the deadlines and penalties apply as described above.

Obtaining a provisional place in the queue

92. The operator’s provisional place in the queue for NER allowances is determined by the date and time at which the Environment Agency receives the new entrant application. The date for taking a provisional place in the queue as a “duly made” applicant is 15 working days from this time. The operator can only take this place in the queue if the relevant regulator approves the application as “duly made”. The relevant regulator will notify the Environment Agency once the determination of “duly made” has been completed.
93. Applicants have been instructed to send their application forms to both their relevant regulator and the Environment Agency, and their completed

- spreadsheet to their relevant regulator only. This is to ensure that such applicants are registered in the queue at the appropriate time, and the regulators have the information that they need to process the application further.
94. For offshore installations the “duly made” status and position in the queue that is obtained after 15 working days can be compromised if the payment of an invoice is not received in time in the future, as outlined in paragraph 91.
95. In cases where the regulator requests more information, the date of determination for “duly made” will be delayed until the regulator has received the complete set of information requested. In the event that the relevant regulator has neither requested more information, nor confirmed the “duly made” status of the application, the application will automatically be considered “duly made” after 15 working days.
96. The relevant regulator will notify the operator of its provisional place in the queue and the likely allocation. If no system of verification is available at the time an application is made, applicants will be given a provisional place in the queue without the necessary verification required. Verification has been specified for the sectors where some element of the input is not standardised and would therefore benefit from an independent expert opinion. This initially applies to: iron and steel throughput, rationalisation, non-fully standardised applications in onshore gas distribution; increase in GQCHP qualifying output capacity, mineral oil refineries and offshore installations. These applications will not be processed further, or allowances issued, until a verified opinion is provided but while there is no means to obtain verification, these applicants will not lose their place in the queue. Information on obtaining verification will be available from the DTI website.
97. Where the application has been rejected, the operator will lose its provisional place in the queue after 15 working days (unless the operator lodges an appeal).
98. Applicants that lodge an appeal within the time limit (see Section G5) will have their provisional place in the queue and full allocation in the initial application frozen until the appeal has been determined. However, an operator’s place in the queue will not be frozen in any other circumstances.
99. Where an appeal is approved, the operator will have its place in the queue and allocation confirmed. Where the appeal is rejected, the operator will lose its provisional place in the queue and the frozen allowances will become available for other applicants to the NER. Where the appeal

decision is an adjustment of the allocation sought by the operator, the quantity approved will be allocated to the operator and the remainder made available to other applicants to the NER.

F3. Issuing allowances

100. Allowances that have been reserved for a particular applicant to the NER will be tagged. The tagged allowances will be issued within 10 working days of the relevant regulator receiving confirmation from the operator that the new entrant activity has commenced.
101. In the event that the date on which emissions from the new entrant begin is later than foreseen in the original application, the operator shall receive a pro-rata amount of allowances based on the reduced number of days in the year to be covered. The surplus tagged allowances will be untagged and will be available for allocation to other eligible new entrants.
102. Similarly, where the capacity is less than in the original application, in accordance with the description of minor changes above, the surplus number of allowances tagged will be untagged and will be available for allocation to other eligible new entrants.
103. At the same time as that the first set of allowances are issued to the operator, the relevant regulator will serve a notice on the operator setting out the allocation for each remaining year of the phase. The notice will act as an instruction to the registry administrator to issue allowances.

F4. Penalties

104. Operators are liable to penalties for providing false or misleading information in their new entrant/closure applications and for not notifying the regulator of relevant changes.
105. Operators are not allowed to apply for free allocation from the NER for the same change more than once. It will be an offence to provide false or misleading information in relation to an application for an allocation from the NER or in order to retain an allocation where the installation has ceased carrying out a Schedule 1 activity. Operators convicted of an offence will be liable to a fine or imprisonment.

F5. Appeals

106. Should the operator disagree with the decision made by the relevant regulator, the operator is entitled to appeal within 15 working days of the decision.

107. Appeals should be made to the appropriate authority depending on the jurisdiction (this being the Secretary of State for England and offshore, the National Assembly for Wales (NAW) for Wales, Scottish Ministers for Scotland and the Planning Appeals Commission for Northern Ireland.)
108. The process for appeals will be set out in the Greenhouse Gas Emissions Trading Scheme Regulations.

F6. Availability of Allowances

109. If the demand for allowances from the NER exceeds the supply in the NER, operators will retain their place in the queue. These operators will still be able to obtain allowances from the NER if installations close, in which case the allowances surrendered on closure will be returned to the NER for redistribution to the applicants waiting in the queue. Those new entrants that do not receive an allocation by the time the allowances need to be surrendered will have to buy allowances from the market.
110. The permit holder of an installation that ceases to carry out a Schedule 1 activity will retain allowances already issued, but will not be issued with further allowances in the years following cessation. Allowances that are not issued in respect of installations that cease a Schedule 1 activity will be added to the NER.
111. Applicants for the GQCHP ring-fence of the NER will be able to access NER allowances in the broader NER should the GQCHP ring-fence run out, but the reverse is not possible. As outlined in paragraph 7 the GQCHP ring-fenced NER may be merged with the general NER towards the end of the first phase.

G. Auction or Sale

112. The Government intends to have an auction or sale of surplus allowances remaining in the NER, should there be a sufficient surplus to justify a release onto the market.
113. The amount of allowances to be auctioned or sold will not exceed 5% of allowances. If there are any allowances remaining in the NER after the final auction of Phase I, these allowances will be cancelled.
114. The UK Government will consult in 2005 on proposed methodologies for such an auction or sale.

H. Treatment of Late installations

115. As discussed in paragraph 10, the Government has determined that a small number of allowances (1.5MtCO₂) should be set aside from the NER to issue to late installations entering the Scheme after the final installation level allocation.
116. Installations that qualify for this set aside, include all existing EU ETS installations that received or applied for their GHG permits after 1 January 2005, and have been unable to submit data and information to the Government (such as verified baseline emissions data) in time for the installation to be included in the final installation level allocation. Eligible installations will also include those that apply for GHG Permits after the final installation level allocation.
117. Installations that received their GHG Permits before 1 January 2005 have had plenty of time to submit verified emissions data to the Government and therefore these installations are not eligible for receiving allowances from this set aside.
118. Allocations will be calculated using the installation's historical emissions data and, so far as possible, the allocation methodology in the NAP, adjusted by a reduction factor. The reduction factor will be 10% for those entering the Scheme up to 6 months after the cut-off date for the final installation level allocation (28 February 2005), increasing to a 25% reduction after 6 months from this date. No free allowances would be granted after February 2007 and if the set aside runs out before that, operators of late installations have to buy the required allowances and they will not be eligible for the NER. The late entrant set aside will not be topped up by allowances coming from closures. If the set aside still contains some allowances after February 2007 they will enter the NER.

119. The reduction factor has been proposed on the basis that it strikes the right balance between the expectations of those already in the EU ETS, who met tight deadlines under the threat that they might not receive any allowances, and the need to encourage any 'missing installations' to come forward to ensure that the UK complies with its obligations under the Directive.
120. There will also be a strict timetable (to be published shortly) for these installations to obtain GHG permits, and submit information and verification opinions to Defra. Failure to meet these timeframes will result in no free allowances. They are also potentially subject to enforcement action by regulators for failing to hold a GHG Permit by 1 January 2005.