

Simplifying the CRC Energy Efficiency Scheme: Next Steps

Introduction

1. The UK needs to adopt a range of measures in order to meet our stringent carbon budgets and greenhouse gas (GHG) emission reduction targets (34% reduction in GHG emissions by 2020, and at least 80% by 2050). These include the use of renewables, Carbon Capture and Storage and the deployment of low carbon energy. The most cost effective way to reduce our emissions while increasing our energy security is to improve energy efficiency throughout our economy.
2. Despite the cost effective savings that are available to large non-energy intensive organisations, their emissions have remained more or less constant for the last twenty years. The Carbon Trust concluded, after analysing abatement potential within the sector, that a 35% CO₂ reduction by 2020 from 2005 levels from buildings can be achieved with a net benefit to the UK of at least £4bn¹. They also showed that price signal alone was not an effective measure to improve energy efficiency in the non-energy intensive sector and that there were four key barriers to progress, namely:
 - Financial incentives to reduce emissions
 - Uncertain reputational benefits of demonstrating leadership on energy efficiency
 - Split incentives within and between organisations, such as between landlords and tenants
 - Organisational inertia.
3. The CRC Energy Efficiency Scheme (CRC) was developed to tackle this mix of barriers and thereby to drive energy efficiency in large electricity users (outside the energy intensive industrial sector), covering both business and the public sector. By tackling these barriers, the scheme is estimated to save 11 MtCO₂ from the non traded sector between now and 2022.
4. Although the CRC began in 2010, the first league table will not be published until October 2011 and the price mechanism of the scheme will take effect from 2011/12 with the first sale in 2012 so it is too early to assess the impact of the CRC on energy efficiency. However, the introduction of the CRC has already increased attention on energy efficiency and energy and carbon management amongst large businesses and the public sector. For example, organisations are

¹ http://www.decc.gov.uk/en/content/cms/what_we_do/lc_uk/crc/policy/policy.aspx. Also updated CT 2009 report:
<http://www.carbontrust.co.uk/Publications/pages/publicationdetail.aspx?id=CTA001&respos=0&q=the+business+of+energy+efficiency&o=Rank&od=asc&pn=0&ps=10>

using the CRC to build a business case for installation of Automatic Meters (AMR) that can recoup their costs in less than a year and will continue to deliver energy savings. The CRC has also boosted awareness of energy efficiency: senior management of some organisations are taking notice of energy bills for the first time. The CRC has enabled carbon and energy-related officers to have an open dialogue with finance and resource teams in new ways as there was little incentive to do so in the past. Preparation for the CRC has required better assurance of energy use data and its analysis. The CRC is also boosting demand from public and private sector organisations for energy efficiency goods and services, such as voltage optimisation equipment (a technology which reduces the voltages received by energy consumers in order to reduce energy use). Voltage optimisation can reduce electricity consumption by 10-20% and have a payback on investment of one to four years, depending on the energy intensity of a site and whether other energy saving measures have been undertaken.

The case for simplification

5. However since the CRC scheme began in 2010, a number of aspects of the policy have been criticised by stakeholders. In particular representations have argued;
 - The rules of the scheme are too complex, difficult to understand and costly for participants to administer;
 - Aspects of the scheme overlap with other climate change/energy efficiency policies (e.g. EUETS, CCAs and greenhouse gas reporting);
 - The scheme forces organisations to participate in ways which do not accommodate their natural business/energy management structures and processes.
6. Consequently Government committed to simplify the CRC scheme. In the 2010 Annual Energy Statement (AES) to Parliament, DECC committed to *“keep the CRC under review and look at the future of Climate Change Agreements in order to ensure that we deliver significant improvements in energy efficiency with minimal complexity and policy overlap.”* We did this because we wanted to ensure that the policies were fit for the future, and that any regulations we retained were less burdensome for business, and more practicable.
7. Furthermore the 2010 Spending Review decision not to proceed with revenue recycling has been criticised by stakeholders. This difficult decision was taken to help tackle the deficit against a background of unprecedented pressure on the public finances. The resulting revenue streams were factored into the Governments spending projections² for the remainder of the Spending Review period (to the end of FY 2014/15). At the Spending Review it was also announced that the first allowance sale for 2011/12 emissions would be a retrospective sale in 2012 giving participants more time to get to grips with the measuring and monitoring requirements of the scheme.

² http://www.thm-treasury.gov.uk/spend_index.htm

Simplifying the CRC – progress to date

8. In November 2010, following up on the AES statement on the CRC scheme, the Government published an initial simplification proposal to amend the legislation underpinning the scheme. The proposal focused on extending the introductory phase which provides participants with an additional year's experience managing compliance and performance within the introductory phase and provided a window to consider further simplifications. Other amendments included changing the treatment of Northern Ireland Departments, updating a number of references in the original CRC Order, and removing any 'information disclosure' requirements on organisations for future phases of the scheme (thereby removing all future CRC obligations on 12,000 organisations). These proposals related to the first phase of the CRC came into force in April 2011.

9. In January 2011, Government published a set of discussion papers, as part of an informal dialogue with participants, which suggested a number of more significant changes and simplifications to the scheme for the second phase of the CRC³. The objective was to revisit the scheme to take into account the following context:
 - the effectiveness of the CRC framework for driving energy efficiency in large private and public sector organisations, in light of wider policy developments in other areas such as the implementation of a carbon price floor⁴, Electricity Market Reform⁵, implementation of a Green Deal for business⁶ and the review of the Climate Change Agreements⁷, and company reporting of greenhouse gas emissions⁸.

 - The perceived complexity of the CRC scheme and hence the administrative burden on:
 - those organisations that are subject to the scheme
 - the administrators of the scheme (Environment Agency, the Scottish Environment Protection Agency and the Northern Ireland Environment Agency)

 - Optimising the projected energy savings attributable to the CRC scheme. Projected savings attributable to the CRC are outlined in Annex G of the June 2010 DECC's analytical projections⁹.

³ http://www.decc.gov.uk/en/content/cms/emissions/crc_efficiency/simplification/simplification.aspx

⁴ http://www.hm-treasury.gov.uk/consult_carbon_price_support.htm

⁵ <http://www.decc.gov.uk/en/content/cms/consultations/emr/emr.aspx>

⁶ http://www.decc.gov.uk/en/content/cms/legislation/energy_bill/energy_bill.aspx

⁷ <http://www.decc.gov.uk/en/content/cms/emissions/ccas/ccas.aspx>

⁸ <http://www.defra.gov.uk/environment/economy/business-efficiency/reporting/>

⁹ http://www.decc.gov.uk/en/content/cms/about/ec_social_res/analytic_projs/analytic_projs.aspx

10. Stakeholder views were sought on a number of specific areas of possible simplification (supply rules, organisational rules, qualification criteria, reducing the overlap between schemes and allowance sales) and proposals and suggestions on any other aspect of the scheme were also invited. A summary of stakeholder responses to these papers is included in Annex III.

Simplifying the CRC – preliminary conclusions and proposals

11. Government will implement a simplified organisation-based CRC from phase two onwards (April 2013) which will retain the elements of reporting on energy use against a number of criteria; purchasing allowances to cover emissions and the publishing of participants results. To facilitate this, in early 2012 we will publish draft legislative proposals for formal public consultation which will amend the existing CRC. A detailed timeline of forthcoming CRC milestones and simplification steps is outlined in Annex I.

12. The key elements that are intended to be included in the formal Government proposals in early 2012 are described in Annex II and summarised below. The elements discussed in Annex II will be considered in the light of further analysis of participant data collected in July 2011 before being formalised in draft legislative proposals so that Government can ensure that the simplifications proposed do not undermine the environmental or fiscal effectiveness of the CRC scheme. However, our preliminary analysis is that the simplifications and changes proposed in Annex II will be broadly neutral in terms of their impact on the emissions coverage of the scheme.

13. In summary these proposals will:

- provide greater business certainty by introducing two fixed price sales a year (one forecast and one retrospective), rather than auctions of allowances in a capped system, in the second phase.
- allow for greater flexibility for organisations to participate in ‘natural business units’;
- reduce the administrative burden (in particular by reducing the number of the fuels reported from 29 to 4; using only electricity measured by settled half hourly meters (HHMs) for qualification purposes; ending the requirement for footprint reports; and other practical measures such as requirements on maintaining records);
- reduce scheme complexity (by removing the complex residual percentage rule (‘90% rule’) and CCA exemption rules, but aiming to achieve broadly the same outcomes)
- reducing overlap with other schemes (so that businesses covered entirely by CCAs do not need to register; no longer requiring EU ETS installations to purchase allowances for electricity supplies).

14. Some have suggested that we should replace the CRC with a more conventional tax. After considering this and other policy alternatives suggested by stakeholders, we have decided to retain the CRC, in a simplified form. The tailored combination of reputational, financial and standardised energy measurement and monitoring drivers remain, in our view, the most effective way to tackle the barriers to the uptake of energy efficiency. We have ample evidence that price alone does not ensure organisations implement cost effective energy efficiency measures. Therefore, we consider the simplified CRC – alongside the Green Deal – is the best way to achieve greater energy efficiency and contribute to meeting our carbon budgets in the relevant sectors.

Key proposals to simplify the CRC scheme

Simplifications and changes to the **qualification and registration** processes for the scheme:

15. The process of assessing qualification for organisations which have CCA target units or EU ETS sites will be simplified as the supply and self-supply definitions will be amended so that energy supplies provided to CCA target units and EU ETS installations are not considered as supplies for CRC purposes. Organisations would no longer be required to consider electricity supplied to such facilities when assessing their CRC qualification status, nor report or surrender CRC allowances for any energy supplies to CCA target units/EU ETS installations. This exclusion would include electricity generated and 'self-supplied' to EU ETS installations. This would reduce the need for organisations to register and claim exemptions from the CRC scheme and would remove CRC obligations from organisations whose great majority of emissions are covered by the ETS or by CCAs. It would also facilitate the removal of the complex rules covering CCA exemptions. (Annex II, sections 1 and 3)
16. Replace the current qualification rules with a simpler process focused only on settled half hourly electricity meters. An organisation would therefore qualify for participation if it is supplied with a threshold level of qualifying electricity through settled half hourly meters at non CCA Target Units and non EU ETS installations. As the rules about the type of meter involved in qualification will be simplified, there may be a requirement for the level of the threshold for the scheme to be revisited to ensure the bulk of coverage of the scheme is retained. The level of the threshold will be proposed in the light of analysis of the footprint and annual

reports which will be submitted by the end of July 2011. It is important to note that the threshold will not be set in order to expand the scope of the scheme but to maintain current coverage. (Annex II, section 1)

17. Re-registration for current participants will be light touch and where details remain unchanged the registry will automatically populate participants' information.

Simplifications and beneficial changes to the year-on-year **compliance** elements of the CRC scheme:

18. We propose to reduce the number of fuels covered by the scheme from 29 to 4 – electricity, gas, kerosene and diesel, where the latter two are used for heating purposes. The proposal would also help to address the unintended consequence of diesel use by off-road vehicles being captured by the scheme as such usage would no longer be within scope of the scheme. As a result of this proposal we do not intend to make any amendment to the scheme's definition of transport. (Annex II, section 2)

19. Smaller sources will be excluded from the scheme's definition of supply, by restricting electricity supply to that measured through a meter with a profile class¹⁰ of 00 and 03 to 08. Profile classes 01 and 02 (domestic meters) and equivalent Northern Irish classifications will therefore be excluded from the definition and will not need to be considered by participants. We propose to adopt similar approaches for the supplies of gas, kerosene and diesel. (Annex II, section 2)

20. The 90% applicable percentage rule will be removed, by requiring participants to report on 100% of their non EU ETS/CCA electricity, gas and kerosene & diesel supplies (the latter two used for heating purposes). This would enable the commensurate removal of the footprint report and residual measurement list requirements, which effectively required participants to monitor all their minor fuels at all their sites and to maintain a list of fuel sources to meet the 90% level.

¹⁰ Profile Class 1 Domestic Unrestricted Customers, Profile Class 2 Domestic Economy 7 Customers, Profile Class 3 Non-Domestic Unrestricted Customers, Profile Class 4 Non-Domestic Economy 7 Customers, Profile Class 5 Non-Domestic Maximum Demand (MD) Customers with a Peak Load Factor (LF) of less than 20%, Profile Class 6 Non-Domestic Maximum Demand Customers with a Peak Load Factor between 20% and 30%, Profile Class 7 Non-Domestic Maximum Demand Customers with a Peak Load Factor between 30% and 40%, Profile Class 8 Non-Domestic Maximum Demand Customers with a Peak Load Factor over 40%

The core/residual distinction would also be removed under this approach. (Annex II, section 2)

21. From the second phase of the scheme, there will be two yearly sales of fixed price allowances instead of establishing an emissions cap and allowance auctioning regime. This would greatly simplify the sales aspect of the scheme as it would remove the need for participants to develop auctioning strategies and thereby reduce administrative burdens. It also gives price certainty to participants, where a clearer price signal means more accurate business cases within organisations for investment in energy efficiency. This approach will feature two Government sales of allowances each year - a sale of allowances at a lower price at the beginning of the year and a retrospective sale of more expensive allowances at the end of each year. This provides flexibility to participants about how they participate in sales; ie they can forecast their energy use at the start of the year and take advantage of the cheaper allowances, or, if they do not want to engage in forecasting and simply 'buy-to-comply', they can purchase in the retrospective sale or from other participants who have excess allowances. Adopting a differential price in the two Government sales of allowances ensures that we create the conditions for a secondary market in allowances. (Annex II, section 6)
22. Removing the cap means that for the remainder of the introductory phase, we propose to continue with retrospective sales, where participants will purchase allowances to cover their emissions using a purely 'buy-to-comply' approach after the end of each compliance year. This means that there will be no forecast sales of allowances in the introductory phase. (Annex II, section 6)
23. After one reporting and auditing cycle (i.e. by the end of 2011/early 2012), the Environment Agency, in consultation with the other scheme administrators, will review burdens associated with evidence packs, with a view to reducing administrative burdens on participants and producing simplified guidance which is more closely aligned to the legislation and which provides greater flexibility to participants in terms of the manner in which they retain evidence for audit purposes. (Annex II, section 7)
24. The current data retention requirements will be made proportionate and less onerous; currently, participants are required to keep records of their energy

usage for up to twelve years after the compliance year to which they relate. This will be reduced so that participants will be required to retain records for six years, in line with other regulatory schemes. (Annex II, section 7)

25. To produce greater alignment between the policies, the CRC scheme will seek to adopt the emissions factors used for greenhouse gas reporting purposes as opposed to fixing emissions factors for each phase as under the current scheme.
26. The organisational rules of the scheme will be changed to provide greater flexibility to businesses as to how they participate in the scheme. We will retain the current rules for qualification, so that at the beginning of each phase, top parents notify the Environment Agency of the overall structure of their group. However, the group will have the option to disaggregate more flexibly to allow the monitoring, management and reporting of energy use for CRC compliance purposes to proceed for natural business units, instead of for large groups which seldom/never act together for energy management purposes. This would provide flexibility for participation in the scheme where genuinely different groups are, under the current CRC rules, amalgamated only by virtue of a common parent. This more flexible disaggregation could therefore potentially enable greater alignment with organisational boundaries used for financial accounts consolidation (Annex II, section 4).

Additional proposed changes

27. The Performance League Table will be retained as the reputational driver for the scheme. However, the detailed rules on the metrics which underpin the table will be removed from the legislation and placed in guidance. This would allow Government to more easily revisit the nature of the reputational element of the scheme in future, in the light of evidence from the operation of the scheme in its early years.
28. We propose expanding the supply definition to include unmetered supplies provided on both a passive pseudo half hourly basis¹¹ and pseudo non half hourly basis¹². However under our qualification proposals, unmetered supplies will not contribute to an organisation's CRC qualification status, which is a change for dynamic supplies¹³. This is in response to stakeholder feedback, which

¹¹ Passive pseudo Half Hourly meters allocate the unmetered consumption across half hourly periods by reference to the calculated sunrise/sunset times

¹² Pseudo Non Half Hourly meters allocate an estimated annual consumption figure across the half hourly periods using settlement profiles.

¹³ Dynamic pseudo Half Hourly meters allocate the unmetered consumption across half hourly periods by reference to the operation of PECU photocells or actual switching times as reported by a Central Management System

highlighted a perverse incentive for organisations to ‘downgrade’ their dynamic unmetered supplies in order to reduce their CRC exposure, along with an associated reduction in their reporting functionality.

29. The current rules of the CRC scheme will be amended to ensure that when they are applied to Trusts, the scheme will allocate responsibility for CRC to an entity with a genuine commercial interest in the property and its use, and with access to the information and resources necessary for effective and efficient compliance with the scheme. (Annex II, section 5)
30. Currently Local Authorities are responsible for their maintained schools and any Academies located in their jurisdiction. We intend to review the treatment of Academies in light of stakeholder feedback about the relationship between local authorities and Academies, and will publish an options paper shortly.
31. Beyond the legal drafting required to implement the simplification measures we will take this opportunity to suggest further legal drafting changes to clarify other parts of the Order. These will be included as part of the formal consultation.

Areas where we are not proposing changes

32. In the responses to the January 2011 informal dialogue simplification papers, calls for other changes were made by a number of stakeholders. We do not propose to include changes in the areas discussed below at the current time, for the reasons indicated.
33. We do not propose to modify the rule on claiming extra benefits for renewable electricity generation, as these are already subsidised. There are other policies that incentivise the development and uptake of renewables such as the Renewables Obligation and Feed in Tariffs. The CRC is the only energy efficiency scheme that is applicable to the target sector.
34. We do not propose to reform the landlord/tenant rules, which state that where landlords are responsible for supplies of energy to their tenants, the landlords are responsible (tenants are responsible if they arrange and receive the supplies themselves). We recognise that the split between landlords and tenants is a difficult area – a classic case of split incentives. We have previously explored options of joint responsibility, but this would neither be simple nor easy to operate. Our view is that most cost effective energy efficiency measures can be implemented by the landlord, rather than the tenant, hence the current rules on landlord/tenant relationships will be retained. However, we are considering the case for revisiting the landlord/tenant rules where the landlord owns only the land

that the structures are built on by the tenant, the landlord supplies the energy but the tenant is the sole occupant of the building and is wholly responsible for its maintenance and hence can control its energy performance.

35. We do not propose to revisit the franchising rules. Where the franchise definition is met (primarily where the public recognises the franchise as one brand or business) responsibility for CRC is placed with the franchisor as they have the potential to influence the way in which energy is used by franchisees. Our view is that this remains in line with our overall aim of CRC to drive improvements in energy efficiency.
36. At this time, we do not propose to take forward a suggestion to use Display Energy Certificates (DEC), if mandated across all commercial buildings, as a basis for CRC reporting. Government has yet to decide on the future of DEC and any changes to policy on DEC would take time to roll out on a national basis. However, this suggestion will be kept under review as we would be open to identifying areas for reducing regulatory burdens.

Questions to you

37. In the Autumn/Winter, Government will draft a package of legislative measures which aim to put these simplifications and changes into effect. Should you wish to comment on the content of this paper before the formal package is drafted, please write to DECC by 2nd September 2011 (crc@decc.gsi.gov.uk).

Annex I – Draft timeline of CRC scheme milestones during the introductory phase and steps to be taken to implement simplified CRC scheme legislation

39. The draft timeline relating to the implementation of simplification measures for phase 2 of the scheme is subject to further analysis in the light of annual report/footprint report data submitted by participants in July 2011 and further dialogue with stakeholders.
40. The timeline provides a breakdown of actions which will be taken by Government, by the scheme administrators and by scheme participants

	2011	Action by:
Announcement on the proposed way forward for simplifying the CRC.	June	Government
Submit annual report for 2010/11.	July	Participants
Submit footprint report for 2010/11.	July	Participants
Publication of the first CRC performance league table (based on early action performance).	October	EA
	2012	
Publish formal consultation on simplified CRC (beginning of February to end of April)	February	Government
Qualification period for the second phase of the CRC begins (April 2012 to March 2013).	April	EA/Participants
First retrospective sale of CRC allowances for 2011/12 emissions	June	EA/Participants
Submit annual report for 2011/12.	July	Participants
Surrender allowances for 2011/12.	July	Participants
Government response to simplified CRC consultation is published.	September	Government
Updated guidance is published on the qualification, registration, supply and organisational rules of the simplified scheme.	September	EA/ NEIA/SEPA
Publication of the second CRC performance league table (based on 3 metrics for the 2011/2012	October	EA

compliance year).		
Remaining guidance covering amendments to the simplified scheme is published.	December	EA/NEIA/SEPA
	2013	
Qualification period for the second phase of the CRC ends (April 2012 to March 2013).	March	EA
Legislation to implement a simplified CRC comes into force.	April	Government
Registration for the second phase of the CRC opens (April to September 2013).	April	EA/Participants
Second sale of CRC allowances for retrospective 2012/13 emissions.	June	EA/Participants
Submit annual report for 2012/13.	July	Participants
Surrender allowances for 2012/13.	July	Participants
Registration for the second phase of the CRC ends (April to September 2013).	September	EA/Participants
Publication of the third CRC performance league table for 2012/13 (based on 3 metrics).	October	EA

Annex II – Discussion of the simplifications intended to be included in the formal public consultation on amended CRC scheme legislation

Section 1 – Simplifying qualification rules

Section 2 – Simplifying supply rules

Section 3 – Reducing overlaps

Section 4 – Simplifying organisational rules

Section 5 – Treatment of Trusts

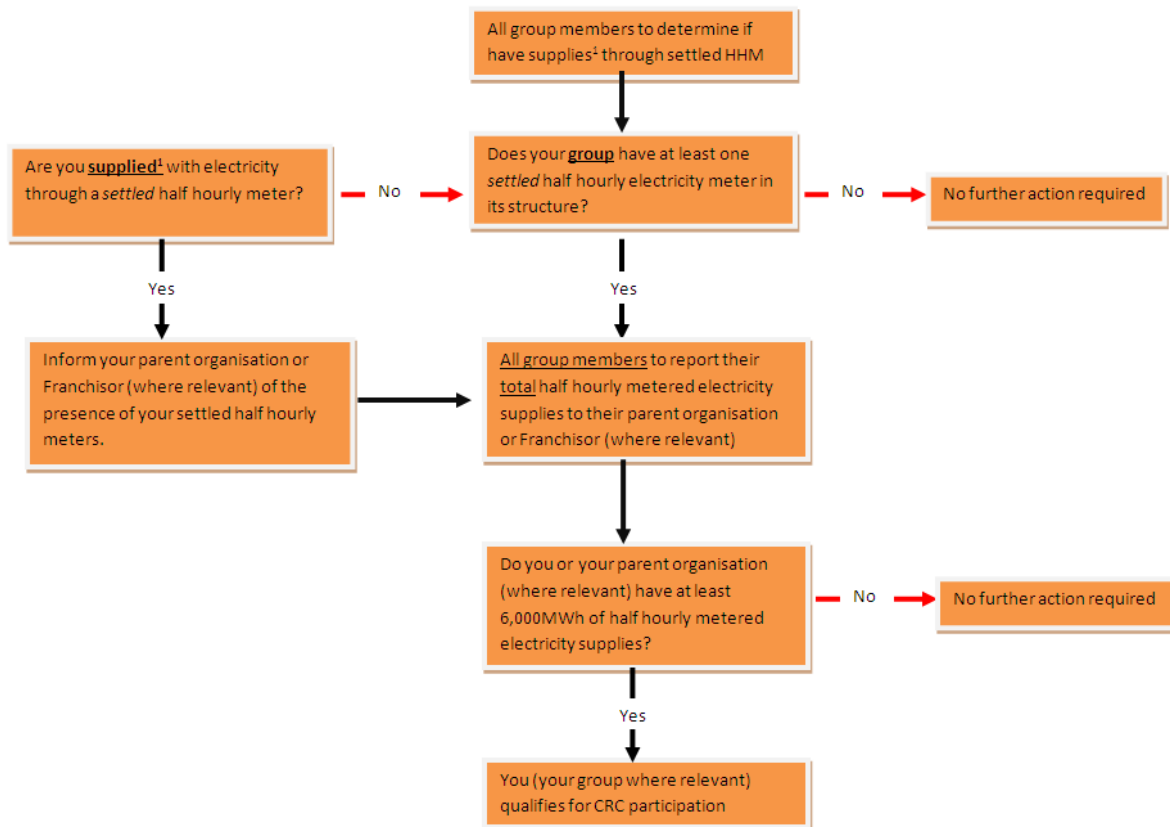
Section 6 – Simplifying CRC scheme allowance sales

Section 7 – Reducing burdens associated with evidence packs and data retention

Section 1 - Simplifying qualification assessment

43. Organisations must currently assess their status against two qualification criteria in order to determine whether they qualify for CRC participation - i) presence of one or more settled half hourly electricity meters and ii) a total half hourly metered (HHM) qualifying electricity supply of at least 6,000MWh in the qualification year. Organisations meeting both criteria are required to participate in the CRC – as per Figure 1 below.

44. Figure 1 – current qualification approach



1. As per CRC Energy Efficiency scheme's definition of supply

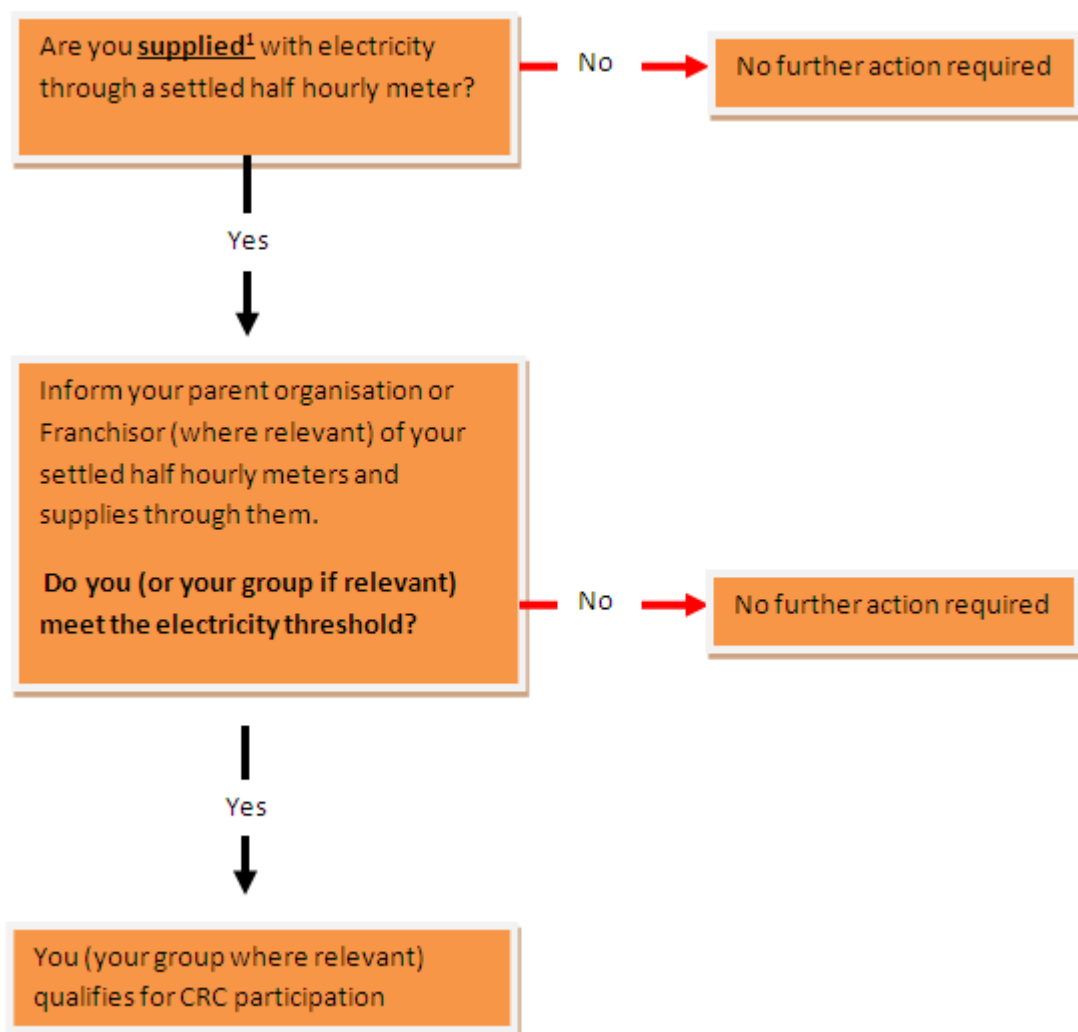
45. Feedback has shown that stakeholders found the different scopes of the two criteria confusing, with resultant difficulties in determining whether they actually qualified for participation. In addition we are aware of an unintended consequence where organisations are disincentivised from installing and

activating Smart electricity meters on account of their contribution towards the CRC qualifying supplies.

46. We therefore propose to replace the current rules with a simpler one-step process focused on settled half hourly electricity meters. Such an approach is welcomed by stakeholders as a clear simplification measure with a reduction in their administrative burdens. It would address the current confusion between the settled and total half hourly metered distinction as well as facilitating the administrators' checking of registration data through cross referencing with supplier data. It would also remove the perverse incentive not to install/activate Smart meters as such meters would no longer contribute to CRC qualification.
47. Whilst the majority of stakeholders' responses to the discussion paper were supportive of this approach, a small minority challenged this position. However we do not intend to progress with qualification criteria based on total energy supply, on account of the increased administrative burden, or total energy expenditure on account of the influence of energy prices and procurement strategies/hedging arrangements.
48. Amending the qualification criterion to settled HHMs without a commensurate reduction in the threshold would result in an emissions reduction from the scheme. In order to keep broadly the same amount of emissions and participants in the scheme we may need to reduce the qualification threshold from 6,000MWh *through all meters* to a different qualification threshold level *through settled half hourly meters only*. Data from annual and footprint reports, submitted by participants in July 2011, will be analysed to determine whether the threshold needs to be revisited and if so, what level the threshold should be set at. The threshold reduction is not being used as an opportunity to increase the scope of the scheme. It is acknowledged that for individual organisations near the threshold, some would fall into CRC whilst others would fall out. This is an inevitable consequence of almost any change in qualification criteria, but we believe that on balance the increased simplicity and transparency outweighs this effect.
49. An organisation would therefore qualify for participation if it is supplied with at least a threshold level of qualifying electricity through settled half hourly meters at

non CCA Target Units and non EU ETS installations – as shown in Figure 2 below.

50. Figure 2 – proposed qualification approach



Section 2 - Supply rules

51. There are four criteria which organisations have to consider when determining responsibility for energy supplies - i) agreement with another party for the supply to the organisation ii) payment by the organisation to that party for the supply iii) receipt of the supply and iv) measurement through a meter – the latter being relevant for electricity and gas only. Organisations purchasing energy for third parties may claim unconsumed supply in such circumstances. However this provision is not available for landlords in respect of supplies on-charged to their tenants.
52. Currently organisations have to consider all their supply arrangements which meet the aforementioned definition, although some may subsequently be excluded under the transport and domestic accommodation exclusions. In combination with the result of the proposal to require participants to report on 100% of their supplies (please see text on removing burdens associated with 90% rule at the end of this section), we propose to exclude smaller sources from the scheme’s definition of supply. This will be along the lines of restricting electricity supply to that measured through a meter with a profile class¹⁴ of 00 and 03 to 08. Profile classes 01 and 02 (domestic meters) and equivalent Northern Irish classifications will therefore be excluded from the definition and would not need to be considered by participants. We propose to adopt similar approaches for the supplies of gas, kerosene and diesel should it prove practical to do so.
53. Participants are also currently required to consider any unmetered electricity supplies provided on a dynamic pseudo half hourly basis¹⁵ for the purposes of qualification and participation. Such supplies are typically provided for streetlighting purposes. Unmetered supplies provided on a passive pseudo half hourly basis¹⁶ or pseudo non half hourly basis¹⁷ are currently excluded from the

¹⁴ Profile Class 1 Domestic Unrestricted Customers, Profile Class 2 Domestic Economy 7 Customers, Profile Class 3 Non-Domestic Unrestricted Customers, Profile Class 4 Non-Domestic Economy 7 Customers, Profile Class 5 Non-Domestic Maximum Demand (MD) Customers with a Peak Load Factor (LF) of less than 20%, Profile Class 6 Non-Domestic Maximum Demand Customers with a Peak Load Factor between 20% and 30%, Profile Class 7 Non-Domestic Maximum Demand Customers with a Peak Load Factor between 30% and 40%, Profile Class 8 Non-Domestic Maximum Demand Customers with a Peak Load Factor over 40%

¹⁵ Dynamic pseudo Half Hourly meters allocate the unmetered consumption across half hourly periods by reference to the operation of PECU photocells or actual switching times as reported by a Central Management System.

¹⁶ Passive pseudo Half Hourly meters allocate the unmetered consumption across half hourly periods by reference to the calculated sunrise/sunset times.

scheme. Stakeholder feedback has highlighted a perverse incentive for organisations to ‘downgrade’ their dynamic unmetered supplies in order to reduce their CRC exposure, along with an associated reduction in their reporting functionality. We are mindful of this position and propose expanding the supply definition to include unmetered supplies provided on both a passive pseudo half hourly basis and pseudo non half hourly basis. However under our qualification proposals, unmetered supplies will not contribute to an organisation’s CRC qualification status, which is a change for dynamic supplies.

54. In addition we are considering whether the four supply criteria can be streamlined to address stakeholders’ concerns over the complexity of these issues and will publish further details in due course.

Landlord/tenant

55. Currently any party meeting the four supply criteria is responsible for the associated emissions under the CRC. This places the CRC obligation on the party receiving the supply, which for many tenanted properties will be the landlord, except where a tenant has a supply relationship with a third party other than their landlord. This is a deliberate policy position to address the split incentives for investment in energy efficiency and to align responsibility with the party most able to influence energy consumption for the building. However there are differences in opinions between the landlord and tenant community as to their respective influences on energy consumption.

56. As part of the informal dialogue we gauged stakeholder views on whether the treatment of landlord/tenant relationships could be simplified. There was no clear consensus as to which party has the more significant influence, nor how to simplify the arrangements. As such we do not intend to fundamentally review our position on supplies to tenanted properties, although we are considering reviewing our definition of a landlord to ensure it works at the correct asset level (e.g. ownership of a building on land versus the ownership of the land on which the tenant builds).

¹⁷ Pseudo Non Half Hourly meters allocate an estimated annual consumption figure across the half hourly periods using settlement profiles.

57. We do not intend to progress the consumption based supply option (option 7 of the supply paper) as it would not distinguish between fully repairing and insuring leases and landlord insuring and repairing leases and their respective influences on energy supplies. In addition the number of organisations deemed to be receiving a CRC supply would increase from current levels (e.g. several tenants in a multi-tenanted building rather than one landlord) thereby placing administrative requirements on a larger number of organisations. There is also the risk of emissions loss from the scheme due to the combination of tenants' organisational size and their higher rate of occupancy turnover, which may result in organisations failing to qualify for the scheme. There is also an issue as to how such an approach would align with the amended qualification criteria – given there would be a disconnect between responsibility for settled half hourly meters and sub meters.

58. We also do not intend to progress the proposal for transferring supply responsibility where mutually agreed between two parties. Stakeholders did not consider this a simplification measure, and concurred that it would introduce additional complexity as every landlord/tenant relationship would require negotiation regarding CRC responsibility, with associated legal input and evidence requirements. In addition this would introduce auditing difficulties for the scheme's administrators, especially involving changes to the parties to the agreement.

Reducing the number of fuels covered by the scheme

59. Currently participants are required to report on their energy supplies from a list of 29 fuels. Core sources and any fuels listed on their residual measurement list are reported on an annual basis, whilst participants include all their fuel supplies in their footprint report, which is completed once per phase. Stakeholder representation has indicated that this results in disproportionate administrative burdens for participants as they are spending time and resources measuring and reporting on the usage of a wide range of fuels which account for very little of the emissions covered by the scheme.

60. We therefore propose to reduce the number of fuels covered by the scheme from 29 to four – electricity, gas, kerosene and diesel; the latter two where used for

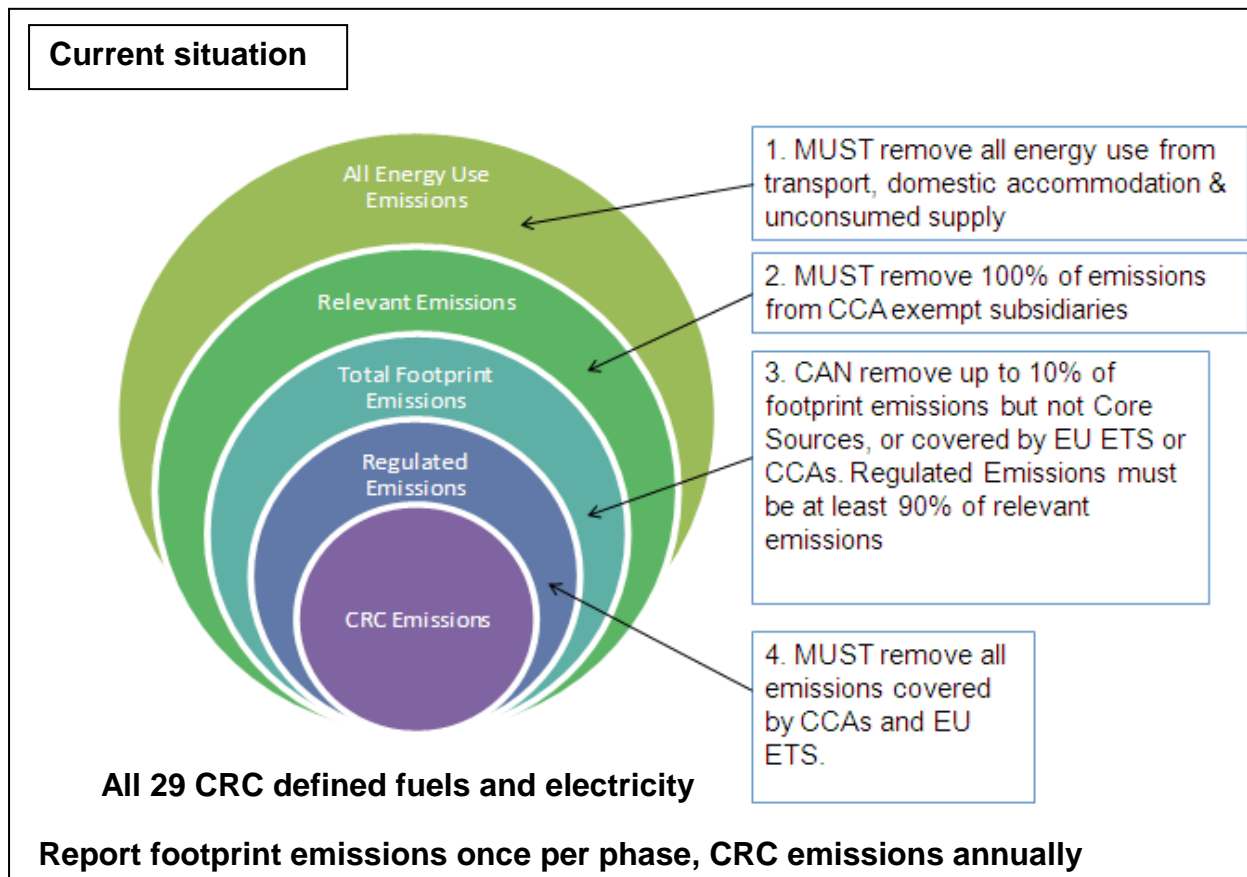
heating purposes. Our original proposal to focus on only electricity and gas has been expanded to include kerosene and diesel when used for heating as a direct result of stakeholder feedback, which highlighted the widespread use of these fuels in areas with a limited gas infrastructure, such as rural areas and in Northern Ireland.

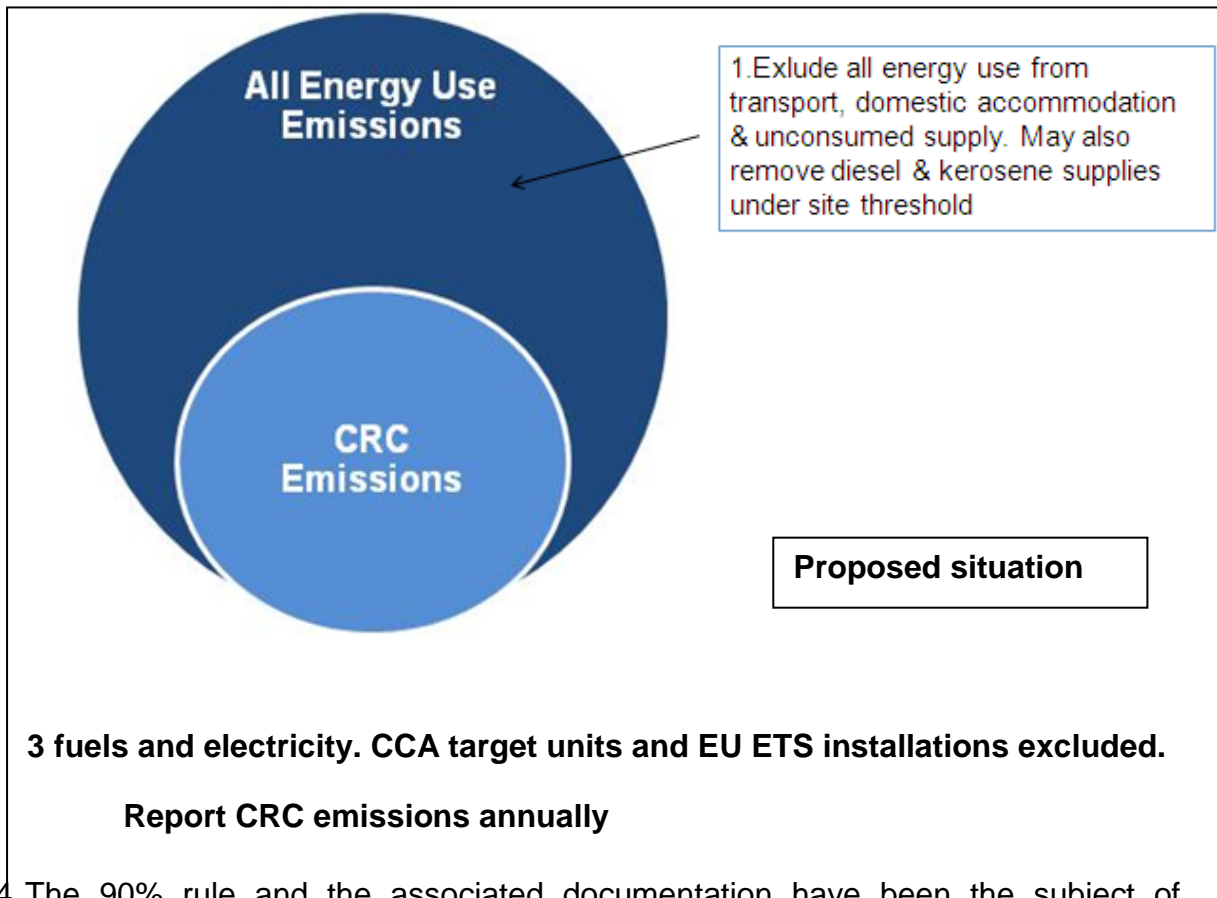
61. This option was very strongly supported by stakeholders in their responses to our informal dialogue on the grounds of significant reductions in their administration burden. There would be a minimal risk of fuel switching to fuels outside the scope of the scheme, given the additional conversion and infrastructure costs. It would also have minimal impact on the scheme's emissions coverage as the four fuels account for the majority of the scheme's emissions.
62. The proposal would also help to readdress the unintended consequence of diesel use by off-road vehicles being captured by the scheme as such usage would be no longer be within scope of the scheme. As a result of this proposal we do not intend to further amend the scheme's definition of transport.

Removing burdens associated with the '90% rule'

63. Participants are currently required to produce a 'footprint report' once per phase, the purpose of which is to establish a participant's total emissions and their compliance with the scheme's '90% applicable percentage rule'. Under this rule participants have to prove that at least 90% of their emissions are regulated under EU ETS, CCA and CRC. Additional complexity is introduced through the CRC's core/residual distinction, where supplies meeting the core definition have to be included in a participant's footprint and annual report. Residual sources are only reported annually where they have been included on the participant's residual measurement list to make up any shortfall below the 90% figure – as shown in Figure 3 below.

Figure 3 – Reporting Methodology





64. ~~The 90% rule and the associated documentation have been the subject of significant stakeholder criticism, primarily due to the complexity of the requirements and the associated administrative burden for compliance. We therefore propose to remove the 90% applicable percentage rule, by requiring participants to report on 100% of their non EU ETS/CCA electricity, gas, kerosene and diesel supplies – the latter two where used for heating purposes. This would enable the commensurate removal of the footprint report and residual measurement list requirements, which effectively required participants to monitor all their minor fuels at all their sites and to maintain a list of fuel sources to meet the 90% level. The core/residual distinction would also be removed under this approach.~~

65. This proposal was widely welcomed by stakeholders as a significant simplification measure, both in terms of reduced complexity and associated reduction in administrative burden. The move to 100% reporting was challenged by a minority of stakeholders, on account of the increased reporting requirements. However we propose to facilitate the additional reporting through the extension of the existing annual energy statement requirement to kerosene and diesel suppliers (*nb - this*

requirement already exists for electricity and gas companies). In addition we will be examining the potential for a site based de-minimis approach for kerosene and diesel supplies.

Section 3 - Reducing/removing overlaps between the CRC scheme and other energy efficiency/climate change policies

67. Currently several hundred organisations with a Climate Change Agreement (CCA) may claim exemption from the CRC. There are three exemption types¹⁸ which operate at different levels of an organisational structure, and if claimed result in either an organisation's partial or full exemption from the scheme. However stakeholder feedback indicates that the process for claiming and subsequently proving eligibility for such exemptions are disproportionately administratively burdensome.
68. In addition a significant number of stakeholders have expressed concerns about the double regulation, and associated administrative burden, resulting from the CRC's treatment of EU ETS emissions. Currently organisations with EU ETS installations are required to consider electricity supplies to such sites when assessing CRC qualification, as well as reporting and surrendering CRC allowances in certain circumstances. This has led to stakeholder claims of an overlap with the EU ETS, especially where organisations have the majority of their emissions covered by the EU ETS.
69. It is therefore proposed to amend the supply and self-supply definitions so that energy supplies provided to CCA target units and EU ETS installations are not considered as supplies for CRC purposes. Organisations would no longer be required to consider electricity supplied to such sites when assessing their CRC qualification status, nor report or surrender CRC allowances for any energy supplies to CCA target units/EU ETS installations. This exclusion would include electricity generated and 'self-supplied' to EU ETS installations.
70. This proposal would facilitate the removal of the complexities associated with the three CCA exemptions. However, we acknowledge that in order to realise the significant simplification for the majority of organisations, this proposal may result in some organisations being required to participate in CRC that would have previously been exempt.

¹⁸ The three exemptions (i) Member, ii) General and iii) Group) are detailed in articles 32-34 of the CRC Energy Efficiency Scheme Order 2010

71. We do not intend to progress the blanket exclusion approach – whereby an organisation would be exempt if any of its undertakings holds a CCA or included an EU ETS installation. We consider that the emissions coverage loss from such an approach would outweigh the simplification benefits, as well as introduce a perverse incentive for organisations to acquire small installation or site with CCA/EU ETS status in order to benefit from the exclusion for the whole organisation.

Section 4 – Simplifying organisational rules

What is the policy challenge on the organisational rules of the CRC?

72. Stakeholder feedback has shown that the current scheme can require businesses to participate in ways which do not necessarily reflect their natural business structures and processes. Businesses have to participate either as large groups under their top parent (including when the latter are overseas), or the top parent has to 'disaggregate' their group into entities which meet the qualification criteria and which can then participate in their own right; but these can be 'artificial' entities created for the purposes of CRC. Specifically, disaggregation is limited to significant group undertakings (single entities or groups of undertakings under a parent that would qualify for CRC in their own right), whilst any disaggregation which results in the parent falling below the qualification threshold is not permitted. Where a group qualifies for CRC, but its parent is based overseas, it must nominate a UK based undertaking member of the group to register as the compliance account holder.
73. A number of participating organisations consider they are now over the hurdle of identifying their organisational structure for compliance with CRC and would be content with keeping current rules. Others, however, claimed that these same rules have caused significant administrative burden and practical complexity, for example when there are large and complex organisations (including private equity funds, trusts and Joint Ventures (JVs)) and where the parent is based overseas.

What is the proposed solution?

74. We propose to change the organisational rules of the scheme to provide greater flexibility to businesses as to how they participate in the scheme. We would retain current rules for qualification, so that at the beginning of each phase, top parents notify the scheme administrator of the overall structure of their group. The group can then be disaggregated to allow the monitoring, management and reporting of energy use for CRC compliance purposes to proceed in accordance with natural business units instead of large groups which seldom/never act together for energy management purposes. Disaggregated undertakings would be required to register and participate in their own right for the whole phase. The current requirement for the remainder of the group not to fall below the qualification threshold would be removed. However, if top parents do want to continue participating as a group, the new rules will allow this also. Hence, this option provides additional flexibility within current rules.
75. This simplification option received significant support in the informal consultation held early this year, as it would involve the following benefits:

- There would be no disruption for those organisations that are content with the current organisational rules, groups can choose to either continue participating as a whole, or take advantage of the option to disaggregate parts of their group so participation in CRC better reflects their operational reality
- Given that organisational rules for qualification remain the same, there will be no emissions loss from the scheme.
- Where there are large or complex structures, this option would allow participants to align CRC compliance with operational management/energy management structures thus would be potentially more effective in driving energy efficiency.
- Where there are overseas parents, it would allow these to disaggregate their UK subsidiaries, rather than imposing the burden of collecting data, reporting and buying allowances on one UK account holder.
- Where there are complex legal entities, such as private equity funds or JVs, these could be disaggregated and would participate in the scheme as separate entities. We understand this would considerably reduce burdens for participants and resolve issues with cross-contamination of separate organisations. The proposed simplification of the treatment of trusts under the scheme is illustrated in section 5 .
- Disaggregation could enable CRC participants to further align CRC compliance with organisational boundaries used for financial accounts consolidation.

76. DECC informally consulted on other simplification options, which received considerably less support from stakeholders:

- A bottom-up option for qualification and with an option to aggregate for participation. Stakeholders showed some support for this option, on account that it would remove the burdens for large groups including a multiplicity of smaller entities. However, overall this was counterbalanced by a widespread concern around the resulting emissions loss from the scheme. Also stakeholders commented that this option would be a complete re-design of the scheme, potentially complex to manage, costly to implement and not reflecting energy management structures.
- Participants showed no appetite for the option to determine the CRC group on the basis of financial accounting consolidation as it would create complexity and may dilute drivers for energy efficiency. Also, on balance, the leading option outlined above was considered a better way to achieve alignment with GHG voluntary corporate reporting. Moreover, importantly, financial accounting rules are currently under revision, thus creating significant uncertainty around the final make-up of organisational boundaries.

- A few organisations were in favour of removing the requirement for determining the group under an overseas parent for the purposes of CRC qualification; however they noted this would involve a potentially significant emissions loss from the scheme and that issues around the nomination of a UK account holder could be adequately addressed by the leading option outlined above.

77. DECC is also considering the organisational structure change rules (so called 'designated changes') in light of stakeholders views, with a view to simplify these and to ensure there is no emissions loss when undertakings/assets and their associated CRC liabilities are transferred between groups.

Section 5 – Treatment of Trusts

What is the simplification challenge?

78. Much of the commercial property in the UK is tenanted and for a number of commercial, legal and tax related reasons, investment in UK commercial property often takes place through a variety of holding structures and involve complex arrangements including assets through a trust structure.
79. The only trust assets which are relevant for the purposes of the CRC Scheme are those which are capable of receiving a supply of electricity, gas or other fuels. Such assets fall in two categories:
- real property;
 - shareholdings in companies (or analogous interests in other types of undertaking) which own real property.
80. Assets held on trust are held by the trustee for the benefit of one or more beneficiary. Such assets are said to be held by the trustee in a “fiduciary” capacity. The provisions of the Companies Act 2006 operate to treat shareholdings held in a fiduciary capacity differently from real property assets held in a fiduciary capacity. The Companies Act states that shareholdings in companies held by a person in a fiduciary capacity shall be treated as not held by him (i.e. it belongs to the beneficial owner for which the trustee holds the legal title). Therefore CRC responsibility is with the beneficiaries of the trust for shareholdings.
81. However the Companies Act does not treat real property assets held in a fiduciary capacity in the same way. In this case, if the trustee is an undertaking and is responsible for the supply to the trust, then the CRC responsible lies with the trustee. The trustee must aggregate energy supplies in relation to property assets which they hold for different trusts and beneficiaries.
82. Feedback from stakeholders has raised concerns about the current CRC rules in relation to assets held on trust. The current CRC rules places responsibility for CRC on the party (the trustee) that has no economic interest in the property (unlike a parent undertaking) and no control over the energy efficiency performance of its trusts.
83. When real property assets are held on trust, the CRC groups the trustee’s own assets and the separate trusts it holds together, for the purposes of participation under the scheme. In some cases this has meant that unrelated trusts are grouped together for the purposes of reporting and purchasing allowances. This

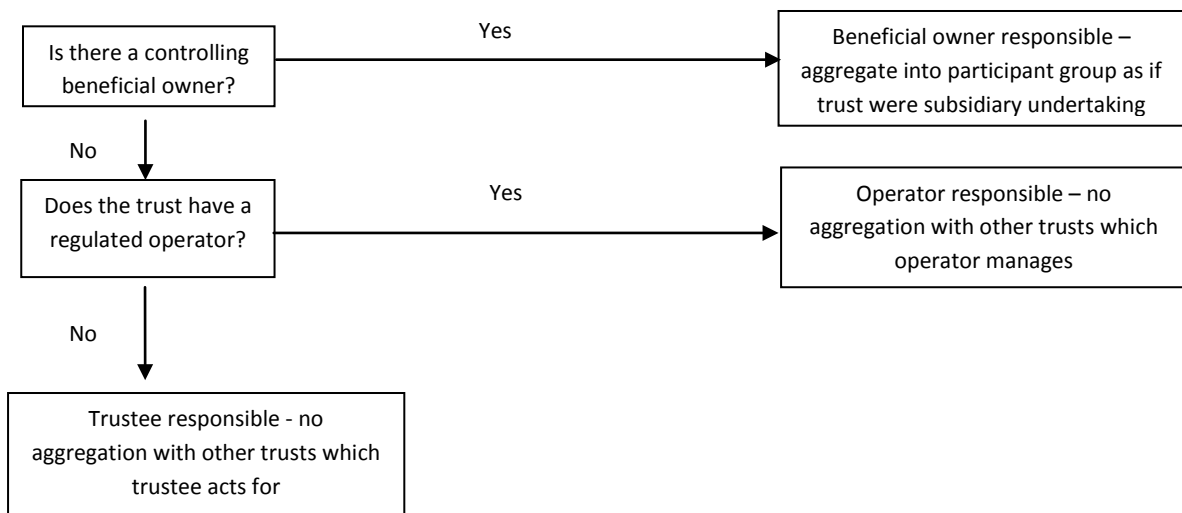
is in contrast to tax and insolvency law which views each trust separately and does not group them with the trustees own assets.

What is the proposed solution?

84. A number of options have been considered. Our proposed solution is to treat trusts as undertakings for purposes of CRC. Treating trusts as undertakings would keep the CRC responsibility of individual trusts separate from each other and trustees. This would reflect commercial reality and would also create a level playing field between funds (e.g. Open-ended Investment Companies (OEICs) and English limited partnerships which are undertakings). This option would ensure the removal of joint and several liability among separate trusts.
85. Due to the range of ways that investors can hold property and the different categories of property trust there is not a one size fits all policy solution for where CRC responsibility should lie. Therefore we are proposing a hierarchical rules approach to determine where CRC responsibility should lie.
86. In the cases where there is one beneficial owner and economic ownership sits with one or two beneficiaries (such as captive trusts) then the responsibility for CRC would sit with that beneficiary or beneficiaries. For qualification and participation purposes, these trusts would be aggregated with their beneficial or majority share owners supplies.
87. In the case where there are many beneficial owners and the trust is registered with and regulated by the Financial Services Authority (FSA), then the CRC responsibility would sit with the operator. These trusts, with regulated operators, would be treated as separate entities for qualification and participation purposes and CRC responsibility should rest with the operator of each trust.
88. In relatively few cases not covered in paragraphs 86 or 87 the responsibility for CRC would then lie with the trustee but the trusts would be treated separately. Trustees of unrelated trusts would not have to group the trusts together as under the current system including for qualification purposes.
89. Where the real property assets are held on trust by more than one trustee, the qualifying electricity supply to the property in a particular trust should be the responsibility of the trustee which assumes responsibility for the electricity supply to those property assets held in trust. Where no one trustee assumes individual

responsibility for such supplies, the trustees must decide amongst themselves which of them is to assume such responsibility for the purposes of the Scheme. In the event that the trustees cannot decide who is to assume such responsibility, they should notify the relevant administrator of such inability to make a decision. The administrator will then liaise with the trustees with a view to brokering an agreement regarding which trustee assumes responsibility for the supplies. This is in line with the current rules.

90. The flow chart below shows the decision making process to be followed in determining who should take CRC responsibility in different types of trust.



91. Government considers that this proposed approach would avoid the imposition of disproportionate burdens on trustees. This approach would allocate responsibility for CRC to an entity with a genuine commercial interest in the property and its use, and with reasonable access to the information and resources necessary for effective and efficient compliance with the CRC.

Section 6 – Simplifying CRC scheme allowance sales in Phase 1 and Phase 2

What is the simplification challenge?

92. Prior to Government's commitment to simplify the CRC and Spending Review 2010¹⁹ (SR 2010) announcement CRC allowances were going to be sold –

- In the **introductory phase** via upfront annual fixed price sales with an unlimited number of allowances, starting in April 2011 (for emissions year 11/12). Participants who under-bought at the fixed price sale would have had the option to either purchase allowances on the secondary market or ask the administrator to purchase EU Allowances (EUAs) on their behalf via the 'safety-valve' mechanism.
- In the **second phase** via an upfront sealed bid uniform price auction. The number of allowances would have been capped, if participants did not, or were not able, to purchase sufficient allowances at the auction²⁰ they would have had the option to purchase allowances on the secondary market or via the 'safety-valve' mechanism noted above.

93. Feedback from participants at registration showed that for some organisations measuring, monitoring and reporting their groups' emissions was more complex than anticipated and forecasted emissions (and allowance purchase) in April 2011 was likely to be inaccurate. Participants also raised concerns that auctioning creates an additional layer of complexity particularly for those organisations who are inexperienced at trading. In providing their recommendations to Government on the level at which the cap should be set for the second phase the Committee on Climate Change²¹ (CCC) recommended that alternatives to auctioning and a cap be considered for the second phase.

What is the proposed solution?

94. In the introductory phase

- To delay the first fixed price sale of allowances until after the end of the 2011/12 compliance year, as announced in SR 2010. Participants will have certainty over both their emissions (as the sale is retrospective) and the price per allowance – confirmed at £12/tonne in Budget 2011²²

¹⁹ http://www.hm-treasury.gov.uk/spend_index.htm

²⁰ Either because they chose not to participate in the auction or the clearing price was higher than their bids

²¹ <http://www.theccc.org.uk/reports/carbon-reduction-commitment>

²² http://cdn.hm-treasury.gov.uk/2011budget_complete.pdf

- For the remainder of the phase Government's proposal is to continue with retrospective sales of fixed price allowances. Participants will be able to purchase allowances once their emissions are known thereby removing the need for the safety valve mechanism
- Draft regulations covering 11/12 and 12/13 retrospective sales will be published in autumn and will come into force by 1st April 2012.

95. As set out in our 'Timing and Frequency of Allowance Sales'²³ paper, allowances sales for 11/12 and 12/13 emissions years are retrospective and the majority of respondents who commented on this paper stated their preference was for a continuation of this approach.

96. Continuing retrospective sales throughout the whole of the introductory phase gives participants certainty – over price and the number of allowances they need to purchase (as the sales take place at the end of the compliance year). It gives participants time to fully get to grips with the measuring and monitoring requirements of the scheme in the introductory phase before moving to forecast sales in phase 2.

97. In the **second phase**

- To sell allowances via an upfront forecast fixed price allowance sales and a second retrospective fixed price allowance sale at a higher price. Participants would then have the option to purchase sufficient allowances in the forecast sale, trade on the secondary market or at the higher priced end of year sale.
- This means there will be no cap or auctioning in the second phase (and therefore remove the need to transition to forecast sales in the introductory phase enabling the retrospective only sales as proposed above)
- The benefits and disadvantages of setting a cap will be reviewed for phase three when there is more robust data on the CRC sector and abatement potential in it.

98. Government proposes this recognising that introducing a cap and an auction mechanism will add an additional layer of complexity at an early stage of the CRC. Removing the cap and moving to unlimited upfront fixed price allowance sales from 2014/15 (the first year in phase 2 when allowances must be purchased and surrendered) was the overwhelming preference of attendees at the DECC stakeholder event and respondents to the informal dialogue paper who commented on a sales mechanism for the second phase. It is also in line with the CCC's recommendation.

²³ http://www.decc.gov.uk/en/content/cms/emissions/crc_efficiency/simplification/simplification.aspx

99. This proposal will

- provide greater business certainty; participants will have a clearer price signal enabling accurate cases for investment in energy efficiency to be made
- incentivise forecasting and good energy management
- reduce administrative burdens and administrative costs; participants will not have to develop auctioning strategies and it removes the need for the safety-valve link to the EU Emissions Trading System (EU ETS) so participants do not need to track EU Allowance (EUA) price.
- ensure the difference in price between the two sales is sufficient to incentivise forecasting and create a market to trade allowances.

100. Whilst only a small number of organisations supported a move to cap and trade in phase two they claimed two main benefits:

- Greater environmental certainty and
- Market price discovery (and emissions reductions at least cost to UK PLC)

101. On the first point a cap will not give greater certainty over the level of UK territorial emissions because of the CRC safety valve link to the EU ETS market (or any other carbon market), which limits the price allowances can reach. If the cap is set tight enough for allowance prices to reach the safety valve level then further tightening of the cap would be ineffective at incentivising further abatement – it would simply drive greater use of the safety valve. However it is recognised that the cap with the link to the EU ETS maintains the overall environmental integrity of the scheme as less EU CO₂ can be emitted as a result.

102. On the latter point while cap and trade can, in theory, achieve a given level of abatement at least cost; data limitations around coverage and abatement potential result in uncertainty about the level at which abatement should be set²⁴, risking price collapse and potentially missed cost effective abatement opportunities or extensive use of the safety valve. By contrast a fixed price delivers least cost abatement up to the price per tonne.

103. In weighing up the costs, benefits and risks of a cap versus fixed price allowance sales Government believes that the complexity and higher administrative burdens of the cap along with the inherent uncertainty over the allowance price for participants and data limitations are outweighed by the benefits of a fixed price sale. However Government will review the costs, benefits and risks

²⁴ <http://www.theccc.org.uk/reports/carbon-reduction-commitment>

associated with the options for phase 3 in light of phase 2 experience and improved data on the abatement potential of the CRC sector.

Section 7 – Reducing burdens associated with evidence packs and data retention

104. Currently the scheme requires that participants maintain records of their first footprint report, first annual report and their first position in the performance table for as long as they are subject to the CRC. For other annual reports, apart from the first annual report, there is a requirement to keep these for at least 7 years after the end of the phase. This means that for phase 2 onwards, the records for annual reports would need to be held by participants for up to 12 years. Stakeholder feedback has indicated that this is an excessive period of time to retain records associated with the CRC and has a significant cost impact in data storage terms. A number of stakeholders have also commented that the requirements/guidance on maintaining information in evidence packs is overly burdensome.

105. In the light of this, we propose that:

- The length of time that individual annual reports are required to be kept should be reduced to six years after the end of the scheme year in question. This would mean that for annual report 2010/11 this would now have to be held for 6 years, until April 2017 - under the current scheme requirements this would have been until April 2021.
- After the first year of annual reporting and the associated auditing, is complete, the scheme administrators will review the guidance on evidence packs with a view to revising it to ensure that the advice is light-touch and fully aligned with the simplified legislation.

Annex III – A summary of stakeholder responses to the January 2010 discussion papers

In January 2011 DECC published a set of discussion papers as part of an informal dialogue with stakeholders suggesting a number of significant changes and simplifications to the scheme. Stakeholders' views were sought on a number of specific areas of possible simplification (supply rules, organisational rules, qualification criteria, reducing the overlaps between schemes and allowance sales) and proposals and suggestions on any other aspects of the scheme were also invited by 11th March 2011.

DECC received 249 written responses from stakeholders. There were a wide range of views from stakeholders on the discussion papers and other aspects of the scheme. A summary of stakeholders' views is provided below and therefore may not capture every individual comment.

Timing and frequency of allowance sales

Phase 1: Background

As announced in the Spending Review 2010 the first CRC allowance sale (for 2011/12 emissions) will take place in 2012. Two options were set out in the discussion paper for the mechanics of the sale in the introductory phase and transition to the second phase and are summarised below.

- Option 1 - Retrospective sales for 11/12 and 12/13 emissions (sales to take place before allowances need to be surrendered on the last working day of July 2012 and 2013 respectively). For 13/14 emissions an April 2013 forecast sale and a retrospective sale before allowances need to be surrendered by end of July 2014. The 'safety valve' link to the EU market is no longer required
- Option 2 - As above for 11/12 and 12/13 emissions but from 13/14 multiple sales held throughout the year.

Summary of responses

Are there any other issues that should be considered (to determine the options?) and should double sale options be considered further?

Almost all respondents who commented on this question shared the view that a compulsory double sale should be avoided. However one public sector organisation commented that as costs are budgeted for the year in which costs are accrued so a double sale for two different financial years would not be as much of an issue for public sector participants.

Views on the proposed options

- Many respondents commented that neither option simplified CRC compared with the retrospective sale proposed for 2012.

- The majority of respondents who commented on sales in the first phase proposed continuing retrospective sales throughout the phase

Option 1

- Of those respondents who expressed a view of the two options proposed two thirds stated a preference for option one. Those favouring this option felt it presented a reasonable compromise to transition from allowance purchase based on known emissions to forecasting.
- A discounted first sale would incentivise forecasting and forward purchasing allowing a secondary market to develop without the complexity of price uncertainty of allowance purchase through an auction. The secondary market means organisations who overbought in the forecast sale would not lose out financially, but the second fixed price sale would prevent organisations making a significant profit.

Option 2

- Of those respondents who expressed a view on the two options proposed, the remaining third expressed a preference for a multi sale approach. Those favouring this option felt that multiple sales would benefit business as it would ease their forecasts (easier to forecast for a couple of months rather than a year) and allow for correction in year.
- Respondents also suggested that option 2 would simplify the scheme further as there would be no need to trade on the secondary market and allows participants more flexibility when purchasing allowances It would reduce the need for the safety valve and links to EU ETS and other carbon markets
- Others commented that the cost-burden would be spread throughout the year and would allow more 'real-time' correction of allowance holdings to match emissions However others commented that it was difficult to see how this would encourage forecasting

Alternatives

- Others re-iterated their view that allowance sales were an unnecessary administrative burden which should be replaced with a tax, either merged with the CCL or a tax invoice applied retrospectively.
- One organisation suggested EUAs should be purchased rather than CRC allowances to ensure carbon savings from reduction in electricity demand are realised by the UK

Forecasting

Several respondents took the opportunity to set out their views on the need (or otherwise) to have a forecasted sale

- A number of organisations commented that up front allowance purchase would not be a driver for forecasting – they are already doing so, the cost of energy is a big enough incentive to do this already.

- That prevailing weather conditions can have a 13% impact per year and therefore accurate forecasting is difficult. One public sector organisation suggested they would face difficulties accurately forecasting due to a large asset rationalisation programme where they are currently not able to accurately account for the changes.
- Others suggested that the price throughout phase 1 should not change so that organisations that were new to forecasting and still learning were not penalised. Some commented that companies with lower cash flows will be able to buy fewer 'forecast' credits and may therefore be financially penalised in later trades for further emissions
- The argument was made that there is no advantage to require participants to buy ahead of when the energy is used. Participants still need to forecast allowance costs in order to accurately budget – the date on which the allowance is purchased does not (they believed) improve or influence energy management activities in any way. The belief that forecasting and multiple allowance sales will improve energy efficiency activities assumes that projects are conceived, planned, implemented and deliver savings within a year. In reality most energy saving projects take multiple years between conception and realisation of savings.
- A number of organisations felt the forecasting elements of the scheme are crucial to its success. Forecasting encourages companies to understand their energy usage in detail and to learn how to lower energy use in advance as well as facilitating the cap and trade nature of the scheme.
- One organisation suggested the league table should also recognise organisations who forecast emissions as this reflects good management of energy
- It was raised that unless the landlord/tenant responsibilities are changed to make the tenant responsible (some) landlords remain in a position of not being able to forecast the usage of tenants who can highly volatile energy use

The mechanics of the sale (timing of sales, other transition issues to be considered and need for the safety valve/link to the EU ETS market)

Few respondents expressed a view on these points, of those that did

- Several wanted as late a retrospective sale within the window as possible (June or July), some argued it should follow reporting and therefore be after the last working day in July.
- Some proposed either an April forecast sale or both sales to be held at the same time. A couple of responses proposed moving to forecast allowance only either in 2012/13 (so no allowance sale for 11/12 emissions) or 2015 (so no allowance sales in the introductory phase)
- One organisation proposed delaying the payment of allowances in the forecasted sale throughout the year to reduce cash flow burden on participants.
- There were mixed views on banking of allowances, some felt it was necessary to allow banking between phases or even years while others felt allowances should be allowed to be transferred between phases.

- All agreed there was no need for the safety valve in the first phase if there was a retrospective sale (unless as one organisation commented, the sale period was held for too short a time).
- A number of organisations were concerned that only participants should be able to purchase and trade CRC allowances.
- One organisation raised the issue that any organisation who goes into administration and had purchased allowances in the forecast sale should be able to claim a refund or sell those allowances on.

Allowance sale prices

- There was consensus that a financial incentive was needed to drive participants from a retrospective sale to a forecasted emissions sale and this price difference needed to be 'sufficiently high'
- Few respondents indicated a price range, those that did thought the retrospective sale needed to be 10-15% higher than the forecast emissions. Some organisations expressed a clear preference for the end of year sale to be based on £12/tonne with discounting from that rate for the forecast sale
- A large number of respondents wanted prices to be set well in advance (some suggested seven year visibility).
- A number of organisations suggested the landfill tax escalator provided a good model where price certainty and a moderated price increase known well in advance had driven investment.
- Other organisations commented that the price should not be linked to the EUA price as it is subject to speculation and could drive price increases and one suggested the price should not be higher than the EUA price.
- That with the ending of revenue recycling the allowance price in the introductory phase should be greatly reduced given the increased costs on organisations.
- Some respondents took the opportunity to raise other comments or propose alternative options including the re-introduction of revenue recycling and cancelling the 2012 retrospective sale so the first sale would be a forecast sale for 2012/13 emissions. The allowance sales should be merged with or replaced by an increased CCL or CCL (or other tax) and mandatory reporting

Phase 2 - Background

In addition to maintaining the status quo (cap and trade with a sealed bid uniform price auction) the following potential options were included in the discussion paper –

Option A - Auction allowances but use different auctioning mechanisms (eg English auction²⁵)

Option B - Auction allowances but in order to reduce complexity and cost remove the safety valve link to the EUA market and replace with regular higher price CRC

²⁵ Also known as the also known as an *open ascending price auction*.

allowance sales (potentially linked to the EUA price) in order to continue to incentivise participants to purchase allowances in the auction.

Option C - Auction with a minimum price (CCC alternative option 1)

Option D - Replace the auction with unlimited allowances at a fixed price (CCC alternative option 2)

Option E - Extend the proposed first phase design (ie two fixed price sales at different prices) a variation of CCC alternative option 2,

Option F – use a carbon exchange

Option G - more fundamental reform of the scheme.

The options fall into four broad categories:

- Options A to C are all variations on the cap and trade with auctioning model
- Options D and E are unlimited fixed price sales, with variations on the mechanics of the sales
- Option F is a means by which to facilitate the sale and trading of CRC allowances rather than an approach that determines how allowances are sold and is therefore complementary to options a to e.
- Option G gave respondents' the opportunity to set out the arguments for alternative approaches

Summary of responses

Options A to C

- A minority of respondents supported retaining the cap suggesting it gives the ability to guarantee carbon emissions reductions and would ensure organisations internalise the cost of carbon
- Others stated market price discovery is vital to encourage cost-effective emissions reductions as well as actively engaging companies in potential efficiency improvements - taxes or simple sales of allowances will not incentivise energy efficiency improvements in the most cost effective way.
- In addition tradable permits would be a manageable cost and an opportunity for participants to make a return on energy efficiency investment.
- There were very few comments on the preferred auctioning mechanisms although one organisation²⁶ supported the CCC's proposal for a minimum price (of at least £12/tonne) and set out key principles any mechanism should follow
- Respondents also recognised that whilst the EU ETS safety valve link introduced a level of complexity there would need to be a mechanism allowing participants to correct for changes in their forecast, additional unabated CRC allowances above the cap should not be available for purchase.
- Whilst many respondents did not comment on the individual merits and limitations of options A to C a large number of respondents and attendees at the stakeholder event expressed strong views to move away from a CRC cap and auctioning. They felt a hard 'cap' is not compatible with the CRC scheme – CRC coverage is based on commercial arrangements (supply contracts and organisational boundaries) and therefore subject to legitimate fluctuations (unlike the installation based approach of EU ETS).

- It was felt that auctions and cap and trade introduce an extra layer of complexity and new ‘non core’ skills for participants to get to grips with. As such smaller, less experienced organisations would be penalised and greater outsourcing of carbon management would be encouraged
- Price uncertainty and consequent uncertainty over the likely level of return available from energy efficiency investment could lead to delays in investment and increases in the cost of capital. Increased price volatility in the market for allowance prices could mask any monetary benefit for participants from energy saving measures. This would make investing in trading skills a more profitable activity than investing in energy efficiency.
- Public sector respondents were concerned about speculating with public money in a traded market and potential cross subsidisation of public money to the private sector. Auctioning and secondary markets with speculators participating in the market could artificially increase the allowance price – concerns that traders/speculators would be the biggest beneficiaries.

Options D and E

Respondents to the discussion paper who commented on options for the second phase sales were broadly in favour of retaining fixed price sales – either the CCC’s recommended option to continue the scheme’s first original first phase design (upfront unlimited fixed price sale, with a link to the safety valve), a continuation of DECC’s proposed option for phase one (a forecast (or multiple forecast) sales and retrospective sale each year) or retrospective only sales. In some cases it was difficult to distinguish whether respondents’ were stating a preference for a continuation of phase one as outlined by the CCC or a continuation of DECC’s revised proposal. The differences in the proposals are not significant therefore for analysis purposes these responses have been grouped together.

- Those in favour of a continuation of fixed price allowance sales stated it would simplify the transition from introductory phase. Would allow participants to learn and build on their experiences and a secondary market to develop without the complexity of price uncertainty created by auctions
- It was also felt that known allowance costs would mean that an accurate case for investment in energy efficiency could be made. The clearer price of carbon would set a clear investment signal
- Simpler fairer and lower administrative costs, as predictable and (with a retrospective sale) allows end of year balancing of allowance requirements and cap and trade favours cash rich organisations.
- Some concerns were raised by stakeholders that a fixed price allowance sale faces the risk of setting a price too low so that organisations pay a financial penalty for their energy use but fail to cut carbon as a result. Alternatively setting the price too high would facilitate carbon reduction but be an unnecessary burden on the financial viability of participants
- Some felt it would mean allowance costs would quickly become a burden that participants endure, perhaps passing costs on to customers rather than investing in energy efficiency measures and that trading may be stifled if badly designed

Private (business) sector organisational rules of the CRC Energy Efficiency Scheme

Background

Whilst a number of participating organisations consider they are now over the hurdle of understanding and identifying their organisational structure for CRC, for other organisations these same rules have caused significant administrative burden and practical complexity. In response to feedback, we set out several simplification options:

- Option 1 – Retain current rules to determine groups for qualification purposes – with option to disaggregate any undertaking or group of undertakings for participation.
- Option 2 – Qualification for the scheme would be assessed at single undertaking level, with optional grouping for participation.
- Option 3 – Groups of undertakings will be determined on the basis of consolidation of financial accounts rules.
- Option 4 – Inclusion of provisions for assets held in a fiduciary capacity.
- Option 5 - Organisations would group under their highest parent in the UK, no longer under their overseas highest parent for the purposes of CRC qualification.
- Option 6 - Review of designated changes (ie remove the use of the SGU concept and include capture assets).

Summary

- Option 1 was preferred by a significant majority of stakeholders, as it would involve minimal disruption for organisations that are content with current rules, whilst providing flexibility to reduce burdens for large and complex groups.
- Option 2 and 3 received considerably less support than option 1 and, although some benefits were highlighted, the majority of respondents saw these as a complete re-design of the scheme, potentially complex to manage and not reflecting energy management structures.
- A few respondents commented on the inclusion of provisions to deal with assets held on trusts, mainly to provide evidence and suggestions for simplification.
- Some respondents were in favour of removing the overseas parent rule, however they noted this would involve a potentially significant emissions loss from the scheme and that issues could be adequately addressed by Option 1.
- A small proportion of respondents commented on the review of designated changes. Most were in favour of a review of the rules.

Summary of stakeholders feedback on the options

Option 1 - Retaining current rules to determine groups for qualification purposes – with an option to disaggregate any undertaking or group of undertakings

- Option 1 was preferred by a significant majority of stakeholders, as it would involve minimal disruption for organisations that are content with current rules, whilst providing flexibility to reduce burdens for large and complex group structures.
- Many felt it would provide flexibility where CRC rules have previously cut across established corporate compliance arrangements (eg where different groups are currently amalgamated only through a foreign parent or where there is no common culture, branding, name, personnel or accounting systems or where separate funds are held together under one common venture capital holding company).
- A couple of respondents commented that the organisational boundaries for CRC reporting could be as near as possible to those used for consolidating financial accounts, so that, in so far as possible, the same data collection and validation mechanisms can be used both for CRC reporting and for GHG company reporting.
- Some stated that it could be more effective than current rules at driving energy efficiency, as investment decisions could be made at the correct managerial level and an organisation will be able to justify abatement measures without reference to costs incurred elsewhere in the group.
- It was also raised that it retains the opportunity to leverage the group exposure (eg by keeping a link to the highest parent via the league table).
- One respondent stated that via disaggregation tenants could be insulated from the effects of the landlord's baseline as this would not necessarily apply across their portfolios.
- A couple of respondents had concerns that it does not remove the complexities associated with combining initial information for registration purposes.
- It was mentioned by one respondent that it may end up costing more in CRC administrative fees compared to the status quo.
- Another felt there would be a risk of increased non-compliance without joint liability.

OPTION 2: Bottom-up approach for qualification, with optional grouping for participation

- Most respondents replied that, as the work to determine organisational structure has already been done, refocusing the scheme on single undertakings would be effectively a complete redesign of the scheme, requiring a new organisational structure analysis.
- Several felt that this option would likely incur substantial administrative burden where energy is managed centrally, with the potential for extensive role duplication and compliance obligations falling on operations with limited capacity to deal with them.
- Few were concerned that the costs of registration would increase across the group.
- A lone respondent raised concerns that it would not align with GHG company reporting.

- A small minority were concerned the league table might lose its reputational impact.
- There was also concern about emissions loss from the scheme and that this option would require a lower qualification threshold to avoid emissions loss.
- One organisation noted that that similar organisations with different structures could be treated completely differently under this option.
- However, a fraction felt that it was more consistent with the 'polluter pays principle' placing responsibility at the point of consumption.
- One respondent highlighted it would provide more equality of participation, whilst allowing 'aggregation' of administrative groupings that are cost-effective.
- Another noted it would remove the complexities associated with combining initial information for registration purposes.
- A few felt it removes the requirement for organisations to identify their overseas parent. It was however considered that this would be achieved through Option 1 also.
- A small number stated it would simplify rules for JVs and venture capital. Similarly to the above it was felt that this would be achieved also through Option 1.

OPTION 3: Group structure determined following financial accounting rules

- Option 3 received low levels of support and, although some benefits were highlighted, the majority of respondents saw this as complex.
- The majority of those who commented on this option felt that it was likely to increase complexity of the scheme and therefore add uncertainty and burden, it would imply reassessing the group for CRC liabilities based on new criteria, involving a significant amount of administration.
- A couple stated reporting emissions equity investments in line with the proportion of the equity would be complex to operate, create administrative burdens whenever the equity changes and would not be effective in driving energy efficiency.
- There were concerns that it would be complex when dealing with companies exempted from preparing consolidated financial accounts.
- It was also raised was that there would be no link (or marginal) between reporting structure and energy efficiency drivers.
- One suggested that financial accounting rules could be followed to determining the boundaries for disaggregation under Option 1 and that the latter would be preferable for a mandatory policy.
- One respondent however highlighted that this option is the one with more commonality amongst different participants.
- Another respondent raised that the mechanism for financial accounts consolidation is already in place and is audited.

OPTION 4 - Provisions for assets held in a fiduciary capacity

- In response to this option, some respondents provided evidence about the treatment of trusts in the scheme and suggested simplification options. (see section 5 in this Annex)

OPTION 5: Replace the overseas top parent rule with a UK top parent rule

- Some respondents were in favour of replacing the overseas top parent rule with a UK top parent rule as it would remove burdens where different entities are currently amalgamated only by virtue of a common overseas parent (.
- Some however recognised that this option could result in a substantial loss of scheme emission coverage and commented that, on balance, Option 1 would provide a simplification with no emissions loss.
- One noted that it would be less favourable to some organisations e.g. where an organisation reports outside the UK, but generally trades as one brand, and has good knowledge of its corporate structure up to its highest overseas parent.
- One flagged that it might give more scope for company structural re-organisation designed to take some parts of an organisation outside the scope of CRC.

OPTION 6 – Review of designated changes rules

A smaller proportion of respondents commented on the options for the review of designated changes, most were in favour of a review of the rules. There was support for the removal of the concept of SGU and for accounting for structural changes based on emissions already visible via annual reporting. It was also noted that using a specified % of an organisation's energy use would not reflect the fact that there could be a wide range in the size of CRC participants, thus setting a 'fair' % threshold would be difficult if not impossible.

Respondent proposed additional simplifications of designated changes rules:

- Remove the requirement to notify changes to the EA during the year.
- Remove designated changes rules and simply provide that divested subsidiaries must continue to participate in the CRC, either as members of a CRC participant or register mid-phase as new standalone participants otherwise.
- Use emissions density as the baseline measure: this would remove the need to rebase mid-phase.
- Include an 'exit mechanism' where the transfer of undertakings or assets leads to a participant falling below the qualifying threshold.
- Provide that the same rules on designated changes are used in the qualification year and after.
- Extend existing rules to only cover specific types of asset transfers (eg rail franchise changes).
- Exclude temporary construction sites under any revised definition of designated changes.

Review of the CRC supply rules

Background

- Option 1 - Government considers that instead of meeting a number of tests to qualify as a CRC supply, a counterparty to an energy contract could instead be deemed to be supplied with energy provided under the provisions of a contract. The current requirements, that a payment should be made for the supply and that the supply be measured by a meter or be a dynamic supply, would no longer exist.
- Option 2 - Government is also considering applying the supply and self-supply definitions at the participant, rather than the undertaking or public body level. This would simplify the CRC's treatment of complex intra-group arrangements and enable the existing treatment of Significant Group Undertakings.
- Option 3 - Government proposes retaining the self-supply provision for electricity and gas supply. This will help to incentivise efficiency of use by those organisations falling within this definition. An option currently under consideration is to extend the self-supply exclusion for licensed activities, such as electricity generation, transmission and distribution, to electricity and gas supplies from third party organisations (i.e. paragraphs 1 & 2, Schedule 1 of the CRC Order)
- Option 4 - Another option is to exclude fuels, as currently defined under Schedule 1 of the CRC Order, from the definition of supply. This would have the impact of reducing emissions coverage by focusing the scheme on electricity and gas only, but significantly simplifying the administrative burden as participants could obtain all their data under the suppliers' annual energy statement obligation.
- Option 5 - Government is also aware of the need to simplify the treatment of transport related activities and proposes an additional option to tie in the supply definition with that of supply to a site. This would therefore exclude supplies made for the purpose of transport
- Option 6 - Alternative options have been considered with respect to allowing organisations to decide CRC responsibility between them, on the proviso that supplies which would have been included within the scheme when assigned to the counterparty, are not eligible for transfer outside of the scheme to an organisation which subsequently fails to qualify for participation. If it qualifies for participation, the counterparty would need to complete some form of registration process prior to transferring emissions responsibility to ensure the transfer was captured within the scheme. Whilst this is not necessarily a simplification, on account of the additional checks required to ensure compliance with the previous transfer point, it would provide an often requested degree of flexibility to the scheme.
- Option 7 - Another option under consideration would be to assign emissions responsibility on the basis of consumption rather than supply (effectively the 'polluter pays' principle). This would primarily reverse the treatment of landlord/tenant relationships, effectively moving the CRC obligation from the landlord to the consuming tenant or end party in a supply chain.
- Option 8 - Government is also considering whether to remove or amend the applicable percentage, where participants have to ensure that at least 90% of their EU ETS, CCA and CRC emissions are covered by the CRC. Removal of this

percentage would facilitate the removal of the core and residual source distinction and meter definitions - a source of significant stakeholder confusion. It would also remove the requirement for a footprint report to be submitted once per phase, further reducing the administrative requirements on participants.

Summary of responses

- The first option was welcomed by several respondents on the account that the identity of the counterparty is usually clear and unambiguous and generally aligned with ability to influence energy consumption.
- Several stakeholders expressed concern about the proposal to remove the meter requirement in order to establish a supply relationship. They cite potential difficulties with the annual energy statement if there is no MPAN/MPRN to link with the energy account. In addition concerns were expressed about the increased liability such an amendment would introduce – as additional private wire and unmetered supplies are brought within the scheme.
- Several respondents challenged that the requirement for a meter should be retained but restricted to certain electricity profile classes – primarily 00 (half-hourly settled), 05 to 08, and 03 to 04 but excluding 01 and 02 which are predominately used by domestic customers, and equivalent gas meters. They argue that such an approach would facilitate the domestic accommodation exclusion as well as providing much needed clarity to the meter definitions.
- Limited feedback was received on option 2, primarily due to its technical nature and implications. However the feedback was supportive of defining supply relationships at the participant level on the grounds of administrative simplicity.
- Stakeholder feedback on the 3rd option was limited, reflecting its technical nature. Those respondents that did respond were broadly supportive of this option on the grounds of equity and fairness between supply models. A couple of respondents proposed extending the licensed activity definition for self-supplies to include ancillary facilities, such as security and workshops, citing the difficulties in accurately distinguishing the energy usage between such activities.
- Option 4 received the most stakeholder responses and was broadly welcomed by all as a significant simplification and reduction in administrative burden. Many respondents questioned the potential emissions loss associated with this option and the unintended consequence of the incentive to switch to fuels not covered by the scheme. However other respondents challenged that the cost implications of fuel switching would outweigh the benefits of switching solely to reduce CRC coverage. Several respondents stated that the proposed approach should be expanded to include heating oil, as well as electricity and gas, in order to recognise the use of such fuel in rural locations and Northern Ireland. One organisation also challenged whether the proposed approach would incentivise

the retention of alternative fuels when electricity models should be encouraged to facilitate grid decarbonisation.

- Several respondents stated that the annual energy statement obligation should be expanded to cover the supplies of liquid fuels as well as electricity and gas. Such an approach would fully realise the simplification benefits of this option for participants.
- Relatively few stakeholders responded to option 5 presumably due to its limited applicability. Those that did respond agreed with the need to simplifying the transport definition but challenged the proposed building-related approach, instead suggesting a focus on stationary usage. An alternative suggestion focused on defining a building with reference to its primary use.
- Option 6 was welcomed by several respondents on the grounds of flexibility, especially for complex supply relationships. A couple of stakeholders proposed a caveated option 6, whereby the transfer option would be conditional on the landlord achieving a 'gateway' requirement such as a high EPC rating (A-C) for the relevant building.
- However a number of respondents stated that whilst addressing the fairness and flexibility issue, the additional administration and legal agreements would not be a simplification.
- The seventh option was welcomed by a sizeable number of stakeholders who cited a better alignment between CRC responsibility and ability to influence energy consumption. A couple of stakeholders also cited an increased driver for tenants to seek energy efficient buildings from prospective landlords.
- Several respondents questioned how the tenant would obtain accurate supply information from the landlord under this option, given the landlord generally has the contractual relationship with the energy supply company. Several respondents suggested extending the annual energy statement obligation to supplies from landlords. Many respondents suggested this option should only be available in respect of sub-metered supplies, which would incentivise landlords to sub-meter their tenant's supplies as well as facilitating information provision for participating tenants.
- Several stakeholders recognised that the respective influences of landlord and tenants on energy consumption varies subject to the lease arrangements. Tenants holding a fully repairing and insuring lease, and therefore responsible for repairing, maintaining and insuring the interior and exterior of the premises, have a greater influence over total energy consumption than tenants in a shared building with centralised metering and energy arrangements.
- A number of respondents expressed concern that this option could result in double/multiple reporting of the supplies in complex supply chain arrangements,

due to confusion over the identification of the obligated consumer. Respondents highlighted that for this option to work in practice all parties would need to be aware of their relative positions in the supply chain.

- In option 8, there was significant support from respondents for the proposal to remove the footprint report, the core/residual distinction and the residual measurement list – especially in conjunction with option 4 (restriction of fuels).
- The majority of respondents favoured the simplification presented by option 8i although a sizeable minority favoured option 8ii, arguing that reporting on all electricity and gas supplies (option 8i) would increase the overall administrative burden, even in conjunction with option 4 (reduction of fuels).
- A couple of respondents expressed concern over changing the reporting requirements at this stage given participants have already established mechanisms for phase one reporting.

Review of the CRC qualification criteria

Background

- Organisations must currently assess their status against two criteria in order to determine whether they qualify for CRC participation. Stakeholder representation has indicated confusion resulting from the slightly different scope of the two criteria.
- Government is also aware of a perverse incentive for organisations not to install Smart meters on account of such meters contributing towards their CRC qualifying supplies.
- Government is therefore considering simplifying the criteria to reduce the complexity surrounding qualification assessment and registration and to address the unintended consequence surrounding Smart meters.
- In light of experience gained through the phase one registration period, Government is considering aligning the scope of both qualification criteria to focus on settled half hourly meters only.
- The draft criteria are shown below:
 - Presence of one or more half hourly electricity meters (HHMs) settled on the half hourly market; and
 - Total **settled** half hourly metered electricity of a figure to be agreed in the qualification year.

Summary of responses

- Stakeholders' responses generally acknowledged the potential confusion associated with the settled/non settled half hourly meter distinction and were significantly in favour of this proposal on the grounds of simplification and the associated reduction in administrative burden.

- Several also welcomed the clarity and unambiguous nature of the proposal. However several stakeholders challenged the potential reduction in the qualification threshold.
- Several stakeholders challenged that qualification should be focused on total electricity or total energy supply rather than on a subset of total electricity supply. These views were to ensure the scheme assesses qualification in an equitable manner across all sectors/business models and does not disproportionately target organisations based on their building profile.
- Several other respondents proposed that qualification should be based on a financial expenditure basis in order to facilitate understanding by potential participants' finance community.
- A couple of respondents proposed that that selected option should allow for Government to increase future coverage without changing the scheme rules again. However others questioned whether current non half hourly profiles will move to half hourly metering and settlement over time, effectively bringing such profiles into the scope for qualification.
- There was mixed support for the proposal to proportionally reduce the qualification threshold, with several requests to provide confirmation as soon as possible in order to give potential participants the maximum preparation time.
- Very few supporting responses were received for the mandatory settled half hourly meter option, primarily due to the difficulty in determining whether individual meters were installed on a mandatory or voluntary basis.

Reducing the overlap between schemes

Background

The CRC scheme places a number of requirements on organisations which are subject to obligations under the EU ETS and/or CCAs. Stakeholders had raised concerns about the burdens associated with claiming an exemption based on their CCA coverage and more widely the interaction between the CRC scheme and wider climate change and energy efficiency policies. Stakeholder views were sought on the following proposals -

- **Blanket exclusion** - a group which has an undertaking that is in the EU ETS or which has a CCA should be excluded from the CRC.
- **Exclusions at qualification** - organisations with EU ETS and/or CCA obligations would no longer have to report their EU ETS/CCA emissions within the CRC for compliance purposes. One way to achieve this would be to assess qualification on the basis of non-CCA supplies. For those groups which are not excluded, CCA and EU ETS emissions reporting would not be required at any point within the CRC, but reporting on other energy use in line with the approach for other CRC participants would be required.
- **Addressing wider overlap** - more fundamental approaches to merge or recast climate change instruments. Respondent were asked to provide

evidence on likely carbon savings and administrative burdens to support any more radical proposals and how they would overcome the barriers to energy efficiency

Summary of responses

- Approximately half of the stakeholder who provided a view on the overlap/wider landscape issues (including retail, ports, publishing, water, property, oil refining, electricity distribution and business trade bodies) stated in their responses that their strong preference would be to replace the CRC scheme as part of a reform of the climate change/energy efficiency policy landscape. The main suggestion for replacing the CRC scheme was to drive emissions reductions by implementing mandatory reporting and a tax (ie an increased Climate Change Levy).
- A smaller number of responses did not support such an approach, noting that a simple tax regime would be difficult to make effective, in terms of driving energy improvements. A price signal high enough to influence behaviour in low energy intensity operations could create major financial problems for high energy intensity organisations. It was also noted that mandatory reporting would be a 'supporting' policy mechanism and would be unlikely to maximise the potential for energy efficiency as a standalone measure and was not an alternative to the CRC scheme.
- A minority of responses also stated that they did not favour merging the CRC scheme with other policies.
- There was significant support for 'Option 2' in the overlap discussion paper, which proposed that organisations should exclude their supplies to CCA sites when considering whether they qualify for the scheme.
- Under such an approach, one respondent said that overlap could be reduced by amending the qualification criteria so that an organisation qualifies only if it has one or more meters operating in the >100 kW market (as denoted by measurement class 'E') and supplies to its non-CCA target units/EUETS sites of more than 6000 MWh of electricity.
- Excluding installations covered by the EUETS and activities within an organisation covered by a CCA from CRC at qualification was supported as they are already covered by other climate change instruments.
- However, activities carried out within such organisations, which are not covered by CCAs or subject to EUETS should be covered by the same qualification criteria as other organisations as long as disproportionate administrative burdens can be avoided.
- However, a number of organisations/sector associations with CCAs did not support a simple exclusion of supplies to CCA target units/EUETS installations at

qualification as they said it would bring in new participants who are currently excluded because of the existing CCA rules.

- Views on 'Option 1' (a blanket exclusion for any organisation which has one or more sites in a CCA or which is responsible for EUETS installations) were mixed. These views are summarised below:
 - Favour a blanket exclusion if an organisation has the bulk of its emissions (for discussion purposes, 75-80%) in other schemes such as CCAs and/or EUETS
 - Allow a blanket exemption for 100% of an organisation if more than 50% of its emissions are in a CCA or in the EUETS or permit exclusion at the legal entity scale if more than 25% of the emissions are in a CCA/in EUETS.
 - Exempt sectors with high energy usage which are subject to international competition and carbon leakage (eg the coal sector, by excluding supply to premises subject to the MASHAM regulations or Mines and Quarries Act).
 - Do not support blanket exclusion as this would result in a high degree of emissions loss from the scheme
 - Blanket exemption not supported, but further work should be done on impacts of reducing emissions coverage before the option is ruled out. Supportive of exclusions from the scheme at qualification for those organisations with CCAs, but the current '25% CCA rule' or a variation of it should be retained to avoid extra companies joining CRC. Exclusions for CCA and ETS sites should be treated similarly.
 - Disagree with an exemption for those organisations with emissions covered by CCAs or the EUETS as this would disadvantage those organisations without such exemptions

A number of other comments or proposals were made in response to questions regarding overlaps:

- Any simplification of the overlap should safeguard the effectiveness of the scheme.
- If mandatory GHG reporting is to be established, it has to add minimal burden for companies. This could be achieved by building GHG reporting on a modular basis, up from its component parts in EUETS and CRC and adding in other GHG emissions not regulated under CRC.
- All the different current and future carbon reporting schemes (including CCAs, EUETS, CRC scheme and GHG reporting) should be aligned to have the same start and end dates and duplication of administrative reporting should be removed as far as possible.
- Exempt all offshore facilities as they are regulated under the EUETS.
- Combine CCAs and the CRC so that all emissions outside EUETS are subject to a CRC where all participants are offered discounts on allowance purchases

based on a fixed scale of percentage reductions in emissions (as measured against a baseline in footprint year), with extra reductions for industries subject to carbon leakage.

- Subsume the CRC into the CCL but with relief granted to those who volunteer to reduce emissions in a verifiable way
- Use DEC's to administer the CRC
- Use MWh/KWh as the metric of the scheme and not carbon, to better reflect the energy efficiency focus of the policy.

Reputational drivers

- A relatively small number of respondents commented on the performance league table and the need for a reputational driver more generally. Views were mixed on the need for a reputational driver with some arguing price alone was not enough to drive improvement in energy efficiency and others stating that the financial drivers would be sufficient.
- Specifically on the league table, as set out in current legislation, respondents argued
 - It was no longer necessary without revenue recycling
 - The current metrics did not fairly reflect an organisation's performance on energy efficiency, nor the previous efforts they had made. Views were mixed on whether the growth metric should have a higher or lower weighting.
 - A couple of organisations noted that removing the league table would facilitate further simplification (potentially removing the need for the designated change rules).
 - The league table should be split by sector or there should be separate tables for the public and private sector
- Some respondents proposed amendments to the league table including
 - Changing the unit of measurement from CO₂ to Mwh or Kwh to better reflect CRC's energy efficiency policy aims
 - Using sectoral benchmarking
 - Display Energy Certificates as the metric (this was considered at length by one member organisation)
 - Allowance price discounts should be available for those organisations at the top of the league table
 - Data should be published but there is no need to rank organisations
- Those organisations arguing that a reputational driver was necessary also highlighted the opportunity to link more closely with greenhouse gas corporate reports rather than have a separate CRC league table.

Fees and Charges

- Only a small number of responses were received on the issue of fees and charges. These centred around the payment of fees and charges after the announcement on revenue recycling in the Spending Review. Now that revenue recycling is no longer going ahead, those that have addressed the question of fees and charges, no longer believe that they should be paying either the registration fee or the subsistence fee.

Responses to the informal discussion on Guidance and record retention

- Of these responses received on the issue of guidance the consistent call was for simplification. Some called for a generic simplification of guidance or the format in which the guidance was published. Others focused their responses on requests for specific simplification of evidence pack guidance or the requirements of which were set out in the evidence pack guidance.
- Some respondents raised concerns about the amount of information that needed to be retained as part of the evidence pack and the length of time it needed to be kept for citing the increased costs of this storage which was significantly more than for EU ETS.

Franchises

- A small number of stakeholders responded with suggested amendments or simplifications to the franchise rules.
- Those that did respond on this issue questioned the rule for franchisors to be responsible for franchisees' emissions and therefore the cost of allowances.
- There was also concern raised on the franchisor being able to obtain data from franchisees and chasing this down could add to increased admin costs.
- A small number of responses raised the concern that the franchisee business that fell into CRC through the franchisor and the cost of allowances passed down would make them less competitive compared with similar business' that did not fall in CRC.

Transport

- There were a number of stakeholders who responded on the issues of transport in the CRC.
- The majority of responses supported the exemption of all transport in CRC. Some of these responses specifically mentioned that off road vehicles should be excluded particularly where they were fuelled by diesel. In addition some thought that this should be widened to include off road vehicles powered by electricity.
- Some responses commented that we should widen the definition of transport to include harbour cranes and port materials and conveyor belts so they would be excluded from CRC.

Landlord tenant

A number of respondents commented on the landlord/tenant rules of the scheme

- The main argument highlighted was that many felt the rule was unfair and did not work in practice as respondents felt that landlords did not have any control over their tenants energy use.
- Many of those who commented on this issue felt that allocation of responsibility should be with the ultimate consumer of the energy, as in option 7 of the supply rules paper, rather than with the counterparty for supply.
- There were some concerns raised that the CRC caused discrimination between CRC landlord and non CRC landlords
- Some respondents argued that the landlord rule will not drive behavioural change in tenants.
- Some respondents commented that where tenants were metered they should be responsible for their own emissions and the landlord responsible for the common areas/systems.
- Very few current leases allowed the landlord to recover CRC costs from their tenants.
- A number of stakeholders commented that the landlord tenant rule did not work for ports as in many cases, port tenants operate and manage their own buildings and storage/processing facilities, controlling the amount of power used for their day-to-day operations. Therefore ports as the landlord cannot control the amount of energy their tenants use.

There were some respondents who supported the landlord tenants rule

- Some respondents commented that landlords were in a better position to reduce emissions in a building as they could make infrastructure improvements. If landlord passed on the CRC costs to tenants there is little incentive for them to improve the energy efficiency of their estate.
- Concerns were raised that if responsibility for CRC was passed to the tenant it would be very difficult to ensure that the emissions stayed under the scheme if, for example, the tenant was an SME and so would fall outside of the scheme.
- Tenants often have no choice in the procurement of the energy tariff for the building, in terms of whether the landlord is getting the cheapest or paying a premium for green energy. If there is no choice in the procurement it is hard to pass the total responsibility to the tenant.
- Issues raised around ensuring that emissions from properties that are void or between leases are captured. There is generally a period between the tenant leaving and either a new tenant or the landlord taking over responsibility. Transferring responsibility between landlord and tenants when the tenant leaves could result in an over complication of the scheme rather than a simplification.

Some respondents provided suggestions on how to improve the rule

- Some respondents said that green clauses were a way to encourage tenants to be more energy efficient but it was commented that very few current leases contained such a clause.
- There were some suggestions for the Government to help industry determine a fair way to allocate responsibility for contributing to the cost of participation in CRC

- There needs to be clear guidance for landlords and documented evidence by all parties on who is responsible under CRC as failing this there could be unreported emissions or double counting
- Suggestion to allow the transfer of energy responsibility between landlords and tenants.
- There was support for landlords and tenants to work together to drive energy efficiency and suggestions for both parties to come to an agreement outlining how they will work together to make energy reductions.
- Tenants should be allowed to ask landlords to improve their area but tenants would be responsible for the cost.

Treatment of public versus private sector participants

- It was suggested there should be no difference in the treatment of the public and private sectors within the CRC. Sector variances could be removed by comparing organisations on their own benchmarks and targets.
- A simpler alternative to the CRC was suggested by adding an additional levy on the cost of electricity direct from suppliers at source, utilising current public sector emission reporting requirements and Government using the powers under the Companies Act 2008 to make Greenhouse Gas reporting mandatory.
- Government should conduct a full impact assessment for the public sector's CRC participation covering material/fiscal and administrative impacts before final decisions on CRC changes are made
- The public sector should not be part of the CRC as the cost of purchasing CRC allowances would be difficult to meet in current financial restraints.
- Separate CRC league tables for the public and private sectors was suggested by a number of respondent due to budget cuts and the public sector not having the necessary funds to improve energy efficiency.
- Government should return CRC revenue to public sector participants via zero interest loans for energy efficiency and as funding for expertise on energy efficiency. This would help investment in energy efficiency measures at the time of budget cuts across the public sector.

Schools

- Government should commit to review the scheme's treatment of Academies and PFI schemes, as local authorities have no mechanisms to influence energy use or to directly recoup the cost of CRC allowance from these schools.
- Several simplification options for schools were proposed, including schools being responsible for their CRC participation, the Department for Education becoming responsible for schools participation, including buying their allowances, and LAs remaining responsible for schools under a more fair and proportionate reasonable assistance duty.
- It was suggested that schools should remain within the CRC and be responsible for the cost of their CRC allowances as this will help encourage energy efficiency and emission reductions

- LAs should be able to pass on CRC costs direct to individual schools rather than through the schools central fund as this would address the barriers LAs have to reducing emissions in school buildings.

Renewables

- The majority of stakeholders who expressed a view on this topic felt the scheme should be changed to recognise and/or incentivise renewable energy.
- Amongst those whose comments gave more detailed responses, there were several suggestions on how to change CRC to incentivise renewables. The majority of comments felt that the counting of energy generated by renewable sources as part of CRC usage was wrong. Several further added that it could act as disincentive for the adoption of renewables.
- A small number of respondents felt the scheme directly conflicted with the ROCs scheme.
- Two water companies suggested that the CRC scheme be merged with the CCL.

Metering

- The overall feeling that came through in the comments was that efforts should be made to reduce the reporting burden.
- Of the other respondents, two suggested excluding all unmetered electricity until its position in the scheme had been clarified to stop possible attempts at avoidance.
- One local authority raised concerns over street lighting and another that the change in supplier should not be treated as a special event as it would be difficult to monitor.
- A number of respondents stated that the current reporting regime should be either removed, reviewed or simplified as at present it place a large administration burden on organisation.
- Several felt CRC should be harmonise it's reporting with other schemes. This was suggested would lower the administration burden and avoid possible confusion with the different requirements of different scheme. It was suggested the reported period be the same as EU ETS, that the information already in CCL should be used for CRC and the reporting requirements match those already required under DEC and being proposed under mandatory GHG reporting.
- Several suggested that it would be easier if the suppliers provided the data required. One stated that this would avoid duplication in data collection.

Other

- Several respondents felt the scheme had become a tax, there were some concerns raised that organisations would attempt to avoid the CRC by changing the meters they use.

- A few organisations stated that it would represent a massive new cost that could cause staff redundancies in order to be met, or that it would harm the economic recovery.
- A small proportion of respondents proposed that either their organisation or some part of it, or their entire industry should be exempted from the scheme. This included several primary producers. Those in the coal industry that commented were particularly worried that it could increase their vulnerability to foreign competition.
- There was concern raised about the relationship between CRCs and CCAs. This included two energy intensive industry sector associations felt that such industries should not be in the CRC at all as the CCA is designed for them and that it should not be used to replace CCAs
- A small fraction of respondents raised the issue of revenue recycling removal from the scheme, or that the scope of the dialogue failed to include the option of its reinstatement.
- A minority suggested some or all the money raised through allowance sales should be invested in energy efficiency schemes. One suggested all revenue from the scheme be used to fund the green investment bank.
- Several water companies complained that as their sector was regulated they would be unable to pass costs on to their customers as in other industries.
- One energy company also commented that they had seen increased demand for energy efficient measures from their customers.

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