International Carbon Action Partnership
ETS Detailed Information

United Kingdom

General Information

Summary	**Status:** ETS in force **Jurisdictions:** United Kingdom In December 2020, the United Kingdom (UK) government confirmed that a UK Emissions Trading Scheme (UK ETS) would be in place from January 2021. Many design elements of the new system mirror those in Phase 4 of the EU ETS, in which the UK had participated since 2005. The UK ETS covers energy-intensive industries, the power sector, and aviation within the UK and European Economic Area (EEA), together making up about one third of the UK's GHG emissions. The scheme's cap is 5% below the UK's notional share of the EU ETS cap (i.e., the EUAs that would have been available to the UK government for allocation) and will decline by 4.2 Mt per year initially. Provisions to ensure market stability include a Supply Adjustment Mechanism (SAM), a Cost Containment Mechanism (CCM), and – quite distinct from the EU ETS – a transitional Allowance Reserve Price of GBP 22 (USD 28.21). Moreover, in the first years, triggers for the UK ETS CCM will be lower than those of the equivalent EU ETS provisions, so as to allow for a smooth transition. To safeguard competitiveness and minimize the risk of carbon leakage, a share of allowances will be freely allocated to Emissions Intensive Trade Exposed (EITE) sectors using an approach similar to Phase 4 of the EU ETS. The UK government remains open to the possibility of linking the UK ETS to other systems, but no decision has been made on the preferred linking partners. The first trading phase of the UK ETS will run until 2030. The entire scheme is due to be reviewed in 2023 and 2028, with ongoing reforms and developments of specific elements in the meantime.
Year in Review	The UK formally exited the EU on 1 January 2020 and the transition period ended on 31 December 2020. The UK no longer participates in the EU ETS, but the covered entities in the country have to surrender allowances under the EU ETS by 30 April 2021 for their 2020 compliance obligations. On 1 January 2021, the UK ETS was launched to ensure the continued contribution of a carbon price to the UK's decarbonization efforts. These efforts, described in more detail in the country's recently announced NDC, include a GHG emission reduction goal of 68% below 1990 levels by 2030 as well as a legislated net-zero emissions target by 2050. In June 2020, the UK government completed a consultation process on "The Future of UK Carbon Pricing" and published an accompanying impact assessment. In November 2020, draft legislation was introduced for the UK ETS; however, the official decision to establish an ETS rather than a carbon tax was not taken until December 2020, after which the draft legislation was made into a statutory instrument.
Overall GHG emissions (excluding LULUCF)	**Emissions:** 461.7 $MtC0_2e$ (2018)
Overall GHG emissions by sector (in MtCO2)	Sector Name: MtCO2e Transport (124.4): 124.4 Energy (104.9): 104.9 Business (79): 79.0 Residential (69.1): 69.1

	Sector Name — MtCO2e Agriculture (45.4) — 45.4 Waste (20.7) — 20.7 Industrial Processes (10.2) — 10.2 Public Sector Buildings (8) — 8.0
GHG reduction target	**By 2030**: 68% reduction from 1990 GHG levels (updated NDC) **By 2050**: Net-zero GHG emissions (2019 amendment to the Climate Change Act 2008)
Carbon Price	*Current Allowance Price (per t/CO2e):* No information available yet.

ETS Size

Covered emissions	0.31 (verified emissions of the regulated entities under the EU ETS are used as an approximation)
GHGs covered	CO2, N2O, PFCs
Sectors and thresholds	**POWER SECTOR & INDUSTRY:** The ETS applies to a specified list of activities of installations in the power and industry sector. This includes activities involving combustion of fuels in installations with a total rated thermal input exceeding 20MW, as well as activities in refining, heavy industry, and manufacturing. Power generators in Northern Ireland still fall under the EU ETS, as they are part of the Isle of Ireland's Single Electricity Market. In addition to the power sector's participation in the UK ETS, the UK's Carbon Price Support (CPS) policy imposes a minimum carbon price of GBP 18/tCO2 (USD 23.08) for power generators using fossil fuels. The CPS will continue to support the decarbonization of the power sector and will stay in place at least until unabated coal-fired power generation is phased out. The government has committed to end the use of unabated coal by 2024. **Small Emitter and Hospital Opt-Out Scheme:** Hospitals and small emitters with emissions lower than 25,000 tCO2e per year and a net-rated thermal input lower than 35 MW can opt out of the ETS and instead monitor and report their emissions and meet annual emission reduction targets. This approach is similar to the UK's opt-out scheme in Phase 3 of the EU ETS. **Ultra-Small Emitter Exemption:** For stationary installations emitting less than 2,500 tCO2e per year, an ultra-small emitter exemption is in place. These installations are exempt from participation in the ETS, except for a requirement to monitor emissions and notify the regulator if emissions exceed the threshold. **AVIATION:** Emissions are included from flights within the UK and flights from the UK to and from Gibraltar or to a country within the EEA. Exemptions are made for aircraft operators with less than 243 flights per calendar year for three consecutive four-month periods or total annual emissions of less than 10,000 tonnes of CO2.
Point of regulation	Downstream
Number of entities	~1,000 installations in the UK were subject to the EU ETS in Phase 3 and are now covered under the UK ETS.
Cap	**FIRST ALLOCATION PERIOD (2021-2025):** 736.0 MtCO2e, to be adjusted to reflect the hospital and small emitter opt-outs. **SECOND ALLOCATION PERIOD (2026-2030):** 630.1 MtCO2e, to be adjusted to reflect the hospital and small emitter opt-outs. The cap was set at 5% below the UK's notional share of the EU ETS cap for Phase 4 of the EU ETS. The annual cap for 2021 is 155.7 MtCO2e and will decline by 4.2 MtCO2e each year,

	which is equivalent to a reduction of 2.7% in the first year. Allowances for the New Entrants Reserve (NER) are part of the overall cap. The government indicated that it will consult on the cap's trajectory within 9 months of the national Climate Change Committee's advice on a cost-effective pathway to net-zero emissions. This advice, published in December 2020, included a recommended level of emissions from covered sectors of 106 MtCO2e in 2023, decreasing to 61 MtCO2e in 2030.

Phases & Allocation

Trading periods	First trading period: 2021-2030
Allocation	**AUCTIONING:** Auctioning is the primary means of allowance allocation under the UK ETS. Auctions have a GBP 22 (USD 28.21) transitional Auction Reserve Price, which will be in place until a SAM (if implemented – see "Market Stability Provisions" section) becomes operational. Auctions clear even when not all allowances are sold. Unsold allowances are carried over to the next four auctions, up to 125% of those originally intended for sale at that auction. If all four subsequent auctions have reached the 125% limit, the remaining unsold allowances are transferred into a reserve in the Market Stability Mechanism Account. **FREE ALLOCATION:** A limited number of allowances are allocated for free to industrial participants at risk of carbon leakage. The number of free allowances that an installation is entitled to is determined using the historical activity level, an industry benchmark, and a carbon leakage exposure factor (CLEF). The benchmarks and CLEFs to be used initially are those of the EU ETS during Phase 4. Historical activity levels are also based on data collected under the EU ETS. These parallels will likely result in comparable levels of free allocations for an installation in the UK ETS as it would have received had the UK participated in Phase 4 of the EU ETS. The maximum number of allowances allocated for free (industry cap) is initially set at the UK's notional share of the EU ETS industry cap for Phase 4, which is ~58 million allowances for 2021 (~37% of the UK ETS cap) and will decline by 1.6 million allowances per year. A review of the free allocation rules is planned to be carried out in 2021. **NER:** A reserve of free allowances is set aside for installations that become eligible for participation within the first trading period and for covered installations that significantly increase their activity level. In line with the EU ETS Phase 4 approach, free allowance amounts are adjusted when activity levels of an installation increase or decrease by more than 15%. The number of free allowances for new entrants is determined based on their activity in the first year of operation, industry benchmark, and CLEF.

Flexibility

Banking and borrowing	Banking of allowances is permitted, and allowances remain valid indefinitely. Limited and implicit borrowing is allowed, i.e., using allowances allocated for free in the current year for compliance in the previous year. Covered entities are not allowed to use allowances left over from their participation in the EU ETS for compliance with the UK ETS.
Offsets and credits	The use of offsets for compliance is not permitted at this time, although the UK government has indicated it is open to reviewing this as the scheme evolves, especially in deciding on how to implement obligations under the Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) alongside the ETS for aviation.
Market Stability Provisions	**SUPPLY ADJUSTMENT MECHANISM (SAM):** A Supply Adjustment Mechanism based on the EU ETS Market Stability Reserve (MSR) may be implemented after the launch of the UK ETS. If the UK government decides to implement a SAM along these lines, it will hold a separate consultation on the design of the

	mechanism. Given that a SAM similar to the MSR would require a measure of the allowance surplus in the UK ETS (analogous to the Total Number of Allowances in Circulation in the EU ETS), a SAM cannot be operational until mid-2022 at the earliest. To reduce the risks at the early stages of the UK ETS and ensure minimum price continuity, the UK government has put in place a transitional Auction Reserve Price (see "Allocation" and "Transitional Auction Reserve Price (ARP)" sections). **COST CONTAINMENT MECHANISM (CCM):** The UK ETS has a Cost Containment Mechanism to avoid spikes in allowance prices by auctioning additional allowances. If the CCM is triggered, regulators can decide on whether and how to intervene. Additional allowances from within the cap can be introduced from three possible sources: the reserve in the Market Stability Mechanism Account; future auctions; or the auctioning of up to 25% of remaining allowances in the NER. The CCM is similar to the measures described in paragraph 29a of the EU ETS Directive. **Triggers:** In the first two years of the UK ETS, the CCM has lower price and time triggers than the equivalent EU ETS provisions, to ensure its reactiveness. In the first year, the CCM is triggered if, for three consecutive months, the ETS carbon price is two times the average allowance price in effect in the UK in the two preceding years. In the second year, the trigger is increased to two and a half times the carbon price for three months. The CCM will revert to the EU ETS price triggers in the third year. This means it would be triggered if, for six consecutive months, the allowance price is more than three times the average market price of allowances during the two preceding years. **TRANSITIONAL AUCTION RESERVE PRICE (ARP):** To ensure a minimum level of ambition in the transition from the EU ETS to the UK ETS, a transitional Auction Reserve Price of GBP 22 (USD 28.21) is in place. The transitional ARP will be kept under review and the government will consult on withdrawing it as the system matures or if a SAM becomes operational. An ARP would not be implemented in a UK ETS fully linked to the EU ETS, as price convergence would be expected between the two markets.

Compliance

Compliance Period	One year (1 January to 31 December). Covered entities have until 30 April of the following year to surrender allowances. These provisions are the same as under the EU ETS.
Monitoring, Reporting, Verification (MRV)	The UK ETS has adopted the EU ETS approach to MRV, with some changes. **REPORTING FREQUENCY:** Annual self-reporting **VERIFICATION:** Verification by independent accredited verifiers is required before 31 March each year. **FRAMEWORK:** The UK ETS has adopted the MRV framework of Phase 4 of the EU ETS, including discretionary changes regarding reduced frequency of improvement reporting and the simplification of monitoring plans.
Enforcement	Regulated entities must pay an excess emissions penalty for each tonne of CO_2 emitted without surrendering a permit. This penalty is equal to GBP 100/tCO_2e (USD 128.21) initially, but is adjusted for inflation over time. The names of non-compliant operators are published.

Linking

Links with other systems	No link with another system is currently in place. The UK government has indicated it is open to the possibility of internationally linking the scheme in the future, but has not made any decision on preferred linking partners. The post-Brexit Trade and Cooperation Agreement between the EU and UK stipulates that the jurisdictions "shall give serious consideration to linking their respective carbon pricing systems in a way that preserves the integrity of these systems and provides for the possibility to increase their effectiveness."

Other Information

Institutions involved	UK Department for Business, Energy & Industrial Strategy HM Treasury UK Department for Transport Scottish Government Welsh Government Northern Ireland Executive Environment Agency UK Scottish Environment Protection Agency Natural Resources Body for Wales Northern Ireland Environment Agency Offshore Petroleum Regulator for Environment and Decommissioning
Evaluation / ETS review	The first trading period (2021-2030) includes two mandatory whole-system reviews. The first review must be carried out by the end of 2023 and the second by the end of 2028. A report will be published on the conclusions of each review round. Changes to the ETS design following the reviews should be implemented by 2026 and 2031, respectively. In addition to the whole-system reviews, the government will conduct targeted reviews of inter alia free allocation for stationary installations and aviation and changes required to align with CORSIA.
Revenue	No information available yet. The UK government is exploring the possibility of establishing a Fund for Industrial Decarbonisation, to which UK ETS auction revenues would contribute.
Implementing Legislation	The Greenhouse Gas Emissions Trading Scheme Order 2020 The Climate Change Act 2008 (2050 Target Amendment) Order 2019

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