

Environment, Planning and Countryside Committee

EPC(2) 14-06(p6)

Date: 26 October 2006

Venue: Committee Room, Senedd, Cardiff Bay

Title: The Emission Trading Scheme (Wales) Directions 2006

Purpose

1. This paper provides details of the Emission Trading Scheme (Wales) Directions 2006

Summary / Recommendation

2. Committee wish to scrutinise this Direction and this paper provides background and details of the purpose of the Direction.

Background

3. The EU Emissions Trading Scheme (EU ETS) is one of the key policies introduced by the European Union to help meet the EU's greenhouse gas emissions reduction target under the Kyoto Protocol. The scheme operates through the allocation and trade of greenhouse gas emissions allowances throughout the EU: one allowance represents one tonne of carbon dioxide equivalent. An overall cap or limit is set by each Member State on the total amount of emissions allowed from all the installations covered by the scheme. The allowances are then distributed to the installations in the scheme. At the end of each year operators must ensure that they have enough allowances to account for their installation's actual emissions. If they do not have enough allowances to cover their emissions then they can buy more. If they have surplus allowances then they can sell these. The buying and selling of allowances takes place on the EU wide market.

4. The EU ETS was established by Directive 2003/87/EC in October 2003 and was transposed into national legislation via the Greenhouse Gas Emissions Trading Scheme Regulations 2003 and the Greenhouse Gas Emissions Trading Scheme (Amendment) Regulations 2004, and consolidated in the Greenhouse Gas Emissions Trading Scheme Regulations 2005.

5. The scheme is divided into periods (phases). Phase I of the scheme started on 1 January 2005 and runs for a three year period. Following phases of the EU ETS will each last for five years. Phase II of the EU ETS will commence on 1 January 2008. Member States must develop a National Allocation Plan(NAP) for emissions allowances. The UK NAP for Phase II is currently with the Commission for approval.

6. The EU Directive defines the activities that are covered by the scheme and any installation carrying out these activities must hold a greenhouse gas emissions permit which in effect is a licence to operate and emit carbon dioxide. Permits are issued to installations in Wales by the Environment Agency. This Direction concerns the issue of permits to new entrants under Phase II of the scheme.

7. The European Trading Scheme Directive defines new entrants as those who have obtained a permit, or an update to a permit, after the date that the NAP for that phase was submitted to the Commission.

8. However, in Phase I the UK defined new entrants by reference to the date that an installation or extension started operating, rather than the date the permit was obtained. Although this approach was appropriate for Phase I, the Department for Trade and Industry received legal advice that there was a substantial legal risk in maintaining this approach in Phase II. The draft Phase II NAP therefore defines new entrants by reference to the date a permit was obtained.

9. Changing the definition creates two circumstances where an operator might obtain a permit or a permit variation before the Phase II NAP is submitted to the Commission:

- where the operator applies for, and obtains, a permit before the Phase II NAP is finally submitted to the Commission, even though they will not start operation before Phase II has started; and
- where a permit has already been issued on the basis that the new entrant will start operating in Phase I, but the start date slips to Phase II.

10. In these circumstances, operators would be able to argue that they should be treated as a Phase II incumbent, not a new entrant. They would have an incentive to challenge their treatment, as non-CHP new entrants will be allocated at less than 100% in Phase II. DTI consider that the best way of minimising the risk of legal challenge by operators is to issue directions to the regulators (under the Greenhouse Gas Emissions Trading Scheme Regulations 2005) stating that:

- the regulator should refuse applications for a permit or variation before the Phase II NAP is submitted where the application relates to a new installation or extension which will not start operating until Phase II; and
- where a permit has already been granted prior to the final submission of the Phase II NAP, or where it has been varied prior to final submission of the Phase II NAP on the basis that the new entrant will start in Phase I, the regulator should use its general powers to revoke or vary permits in order to revoke the permit, or to reverse the variation previously made (by way of a further variation back to the original conditions) if the new installation or extension will not in fact start operating until Phase II.

11. This will ensure that an operator will not be able to obtain a permit - and thus claim that they should be treated as a Phase II incumbent - where they will not actually start operations until after 1 January 2008. The policy intention for Phase I was that requirements for permits were only in respect of Phase I. If, having been permitted, an operator did not start in Phase I then the intention was that they would surrender their permit or their permit would be revoked (and they would have to

subsequently apply for a permit/variation). It should also be noted that where the start date of an operator slips from Phase I to Phase II, any Phase I allowances already reserved will go back into the new entrant reserve. The operator would have to make a new application to the Phase II reserve, under the rules contained in the Phase II NAP.

12. The proposed Directions are to be made under regulation 42 of the Greenhouse Gas Emissions Trading Scheme Regulations 2005, which confers a power to direct the Environment Agency. This power is exercisable by the Assembly in relation to installations (other than offshore installations) which are, or will be, situated in Wales. Standing Order 29 confers a power on the Minister for EPC to propose that the Directions be made and to determine, in accordance with paragraph 29.3 of that Standing Order, the procedural arrangements that are appropriate for their making.

13. We have sought the advice of Legal Services and we agree with DTI's suggested approach to this new entrant issue. The other DA's have issued similar Directions to address the problem and the Directions at annex 1 should be issued to the Environment Agency Wales as soon as possible.

Cross Cutting Themes

14. Climate Change is one of the greatest environmental challenges facing the world today and represents a significant challenge to the UK and the international community.

15. The Assembly Government's commitment to tackling climate change is set out in the Environment Strategy for Wales and the Sustainable Development Action Plan. The EU ETS regulates emissions of carbon dioxide from over 11,500 installations across the EU and includes electricity generators, oil refineries, offshore platforms, industrial plants in the iron and steel cement and chemicals sectors.

Action for Committee

16. The Committee is invited to consider the Direction.

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