

Huw Irranca-Davies AS/MS
Y Dirprwy Brif Weinidog ac Ysgrifennydd y Cabinet dros New
Hinsawdd a Materion Gwledig
Deputy First Minister and Cabinet Secretary for Climate
Change & Rural Affairs



Llywodraeth Cymru
Welsh Government

Ein cyf/Our ref: MA/HIDCC/PO/0393/24

Mike Hedges MS
Chair
Legislation, Justice and Constitution Committee
Welsh Parliament
Cardiff Bay
Cardiff
CF99 1SN

16 December 2024

Dear Mike,

I am writing to inform you the UK Emissions Trading Scheme (ETS) Authority (comprising of the Welsh Government, the UK Government, the Scottish Government, and the Northern Ireland Executive), has today published a consultation document and an Authority response related to ongoing work to review free allocation of allowances within the scheme. Free allocation policy is designed to mitigate carbon leakage resulting from exposure to the UK ETS carbon price. They are allowances that are provided for free to industries who face competition globally from competitors based in countries with weaker climate change mitigation policy (carbon leakage). Free allocations are currently the primary policy lever in mitigating carbon leakage.

In December 2023 the Free Allocation Review consultation was published, which sought views on how free allocation policy could be adjusted to be better targeted to UK sectors most at risk of carbon leakage. The aim was to implement any changes ahead of the second allocation period in 2026. However, in September 2024 the Authority launched a targeted consultation which asked for views on delaying the implementation of any changes until 2027. This was proposed to provide additional time for careful consideration of stakeholder views and policy development in what is a complex and challenging area, as well as align changes to free allocation policy with the UK Governments plans to introduce a UK Carbon Border Adjustment Mechanism (CBAM) in 2027. The alignment with a UK CBAM is particularly important as it is another way to mitigate carbon leakage and, as such, is likely to impact the UK ETS free allocations policy. Stakeholders were therefore strongly in favour of aligning the implementation of these policies. The "*UK Emissions Trading Scheme: Moving the Second UK ETS Free Allocation Period Authority Response*" published today confirms that the proposed delay will take place.

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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.

The consultation document being released is the “*UK Emissions Trading Scheme Free Allocation Review: Carbon Leakage Consultation*.” This follows the proposals from the December 2023 consultation aimed at updating the Carbon Leakage List, which is a list of sectors at risk of carbon leakage. This new consultation provides more detail on those proposals and seeks further input from stakeholders regarding our approach to carbon leakage. It offers additional details on the methodology behind the Carbon Leakage List and considers revised Carbon Leakage Indicator values based on the carbon leakage risks faced by UK industries. Moreover, it invites stakeholders to provide their opinions on whether to adopt a UK-specific Carbon Leakage List or to maintain the existing one. Lastly, the consultation includes proposals and solicits feedback on how free allocations should be adjusted for sectors that will be subject to the proposed UK CBAM.

Through the UK ETS, we must encourage decarbonisation in a way that does not risk disadvantaging Welsh industry and supports their decarbonisation pathways to a net zero world. These publications represent a crucial next step in improving free allocation within the UK ETS, ensuring support is given to those industries who need it most. I expect to write again regarding the outcome of further consultations and policy proposals in the coming months. I am copying this letter to the Chair of the Climate Change, Environment and Infrastructure Committee.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Huw Irranca-Davies', written in a cursive style.

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