Net Zero, Energy and Transport Committee
Tuesday 4 March 2025
9th Meeting, 2025 (Session 6)

Note by the Clerk on the Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2025 (SI 2025/124)

Overview

1. At this meeting, the Committee will consider the following Statutory Instrument (SI), which is subject to the negative procedure. The Committee is invited to consider the instrument and decide what, if any, recommendations to make.

2. More information about the instrument is summarised below:

   Title of instrument: Greenhouse Gas Emissions Trading Scheme (Amendment) (No. 2) Order 2025 (SI 2025/124)

   Laid under: the Climate Change Act 2008

   Laid on: 12 February 2025

   Procedure: Negative

   Deadline for committee consideration: 24 March 2025 (Advisory deadline for any committee report to be published)

   Deadline for Chamber consideration: 28 March 2025 (Statutory 40-day deadline for any decision whether to annul the instrument)

   Commencement: 31 March 2024

Procedure

3. Under the negative procedure, an instrument is laid after it is made, and is subject to annulment by resolution of the Parliament for a period of 40 days beginning on the day it is laid. In this instance, the instrument is also subject to annulment by resolution of Senedd Cymru, the Northern Ireland Assembly and both Houses of the UK Parliament.

4. Once laid, the instrument is referred to:

   - the Delegated Powers and Law Reform (DPLR) Committee, for scrutiny on various technical grounds, and

   - a lead committee, whose remit includes the subject-matter of the instrument, for scrutiny on policy grounds.

5. Any MSP may propose, by motion, that the lead committee recommend annulment of the instrument. If such a motion is lodged, it needs to be debated at

a meeting of the Committee, and the Committee then needs to report to the Parliament (by the advisory deadline referred to above).

6. If there is no motion recommending annulment, the lead committee is not required to report on the instrument.

Delegated Powers and Law Reform Committee consideration

7. The DPLR Committee considered this instrument on 25 February and reported on it in its 13th Report 2025. The DPLR Committee made no recommendations in relation to the instrument.

Purpose of the instrument

8. This instrument makes various changes to the UK Emissions Trading Scheme (UK ETS), including a change to the start of the second free allocation (FA) period, which will now commence in 2027 instead of 2026. As a result, the second FA period will be shortened from five years to four, and 2026 will be treated as a standalone year, subject to the same rules as the first FA period (2021-2025).

9. Additionally, the instrument implements three key changes to other aspects of the scheme. First, it mandates the publication of full details of transactions between accounts in the UK ETS Registry after a three-year delay, aligning with international transparency standards. Second, it introduces limited exemptions to the prohibition on disclosing scheme data, allowing the information to be shared for policy development and to support the statutory functions of the Climate Change Committee (CCC). Third, it extends eligibility criteria for the Ultra-Small Emitter (USE) scheme, permitting installations with low emissions that began operations between 2 January 2021 and 1 January 2024 to apply for USE status during the 2026-2030 period, reducing their administrative burden.

10. The UK ETS was established under the Climate Change Act 2008 by the 2020 Order to facilitate cost-effective emissions reductions, contributing to the UK's net zero targets. It is administered by the UK ETS Authority, which includes the UK Government, Scottish Government, Welsh Government, and the Department of Agriculture, Environment and Rural Affairs for Northern Ireland. Regulatory oversight is provided by the Environment Agency, the Scottish Environment Protection Agency, Natural Resources Wales, the Northern Ireland Environment Agency, and the Offshore Petroleum Regulator for Environment and Decommissioning. The UK ETS replaced the UK's participation in the EU Emissions Trading System (EU ETS) while incorporating modified EU ETS rules on monitoring, reporting, and verification.

11. Under the scheme, participants must monitor, report, and surrender allowances based on their greenhouse gas emissions. To mitigate carbon leakage risks, businesses exposed to carbon pricing receive a proportion of their allowances for free, while additional allowances can be purchased at auctions or in secondary markets. The UK ETS also includes opt-out provisions for Hospital and Small

Emitters (HSE) and Ultra-Small Emitters (USE), with these installations exempt from surrendering allowances.

12. The UK Government Explanatory Note and the Scottish Government Policy Note are included in Annexe A. The Policy Note includes a summary of consultation undertaken on the instrument, impact assessments carried out, and the anticipated financial effects.

Committee consideration

13. So far, no motion recommending annulment has been lodged.

14. Members are invited to consider the instrument and decide whether there are any points they wish to raise. If there are, options include.

    - seeking further information from the Scottish Government (and/or other stakeholders) through correspondence, and/or

    - inviting the Minister (and/or other stakeholders) to attend the next meeting to give evidence on the instrument.

    It would then be for the Committee, at the next meeting, to consider the additional information gathered and decide whether to make recommendations in relation to the instrument.

15. If members have no points to raise, the Committee should note the instrument (that is, agree that it has no recommendations to make).

16. However, should a motion recommending annulment be lodged later in the 40-day period, it may be necessary for the Committee to consider the instrument again.

Clerks to the Committee
March 2025

Annexe A: Scottish Government Policy Note

THE GREENHOUSE GAS EMISSIONS TRADING SCHEME (AMENDMENT) (No. 2) ORDER 2025 (SI 2025/124)

The above instrument is to be made in exercise of the powers conferred by sections 44, 54 and 90(3) of, and Schedule 2 and paragraph 9 of Schedule 3 to the Climate Change Act 2008. The instrument is subject to negative procedure.

Summary Box

This instrument makes various changes to the UK Emissions Trading Scheme (the "UK ETS") including changing the start of the second free allocation (FA) period from 2026 to 2027, therefore, reducing the second FA period from five to four years, and making 2026 a standalone year.

In addition, this instrument makes three changes to other aspects of the scheme. Specifically, these will: require the publication of full details of transactions between accounts in the scheme's Registry after a three year delay; add limited exceptions to the prohibition on disclosure of scheme data in order to support the development and implementation of related policies, and support the statutory functions of the Climate Change Committee (CCC); and extend qualification criteria so that installations with low levels of emissions which started operations between 2nd January 2021 and 1st January 2024 inclusive can apply to be classed as Ultra-Small Emitters (USEs) during the 2026-2030 period, thereby benefitting from a reduced administrative burden.

Policy Objectives

The UK ETS was established under the Climate Change Act 2008 by the 2020 Order as a UK-wide greenhouse gas emissions trading scheme to encourage cost-effective emissions reductions which will contribute to the UK's emissions reduction targets and net zero goal. The UK ETS is operated by the UK ETS Authority, comprising of the UK Government, Scottish Government, Welsh Government and the Department of Agriculture, Environment and Rural Affairs for Northern Ireland. The scheme is regulated by the Environment Agency, the Scottish Environment Protection Agency, Natural Resources Wales, the Northern Ireland Environment Agency, and the Offshore Petroleum Regulator for Environment and Decommissioning. This scheme replaced the UK's participation in the EU Emissions Trading System (EU ETS), and the 2020 Order applied EU ETS rules on the monitoring, reporting and verification of emissions with modifications to ensure that they work for the UK ETS.

Under the UK ETS, participants are required to monitor, report on, and surrender allowances in respect of their greenhouse gas emissions. Participating operators at risk of carbon leakage are given a certain number of UK ETS allowances for free, to manage their exposure to the carbon price and the risk that business' decarbonisation efforts could be undermined by higher-carbon imports. Participants can also buy emission allowances at auction and in secondary markets.

The UK ETS has opt-out schemes for Hospital and Small Emitter (“HSE”) installations and Ultra Small Emitter (“USE”) installations, as they either provide services to hospitals or are installations emitting less than 25,000 and 2,500 tonnes of carbon dioxide equivalent (CO2eq) respectively per year. Installations eligible for these schemes do not have to surrender allowances in respect of their emissions.

This instrument will make changes to free allocations (FAs), Registry transaction publication, information disclosure, and ultra-Small Emitters (USE) policy. The main changes made by this instrument are in relation to:

- *The second free allocation period:* The scheme has two FA allocation periods, 2021-2025 and 2026-2030, in which FAs are calculated and provided to eligible operators. This will change the UK ETS legislation such that the second allocation period commences in 2027 instead of 2026. The 2026 year will become a standalone year subject to the same rules that apply in the first FA allocation period of 2021-2025.

- The onset of the second FA allocation period is being moved to 2027 to ensure that any prospective changes to FA policy align with the UK Carbon Border Adjustment Mechanism (UK CBAM). UK ETS stakeholders have been calling for changes to FA policy to align with the UK CBAM introduction in 2027 and to give more time for decisions from the consultation the UK ETS Free Allocation Review to be considered, a move announced in the Authority Response in December 2024.

- *Publication of Registry transaction details:* The UK ETS Authority will be required to publish details of all transfers of allowances between accounts in the UK ETS Registry (other than those between UK ETS Authority accounts) annually, after a three-year delay. This is in line with international standards including the EU ETS. This change will provide transparency and so support effective market analysis.

- *Information Disclosure Exemption:* An exemption to the general prohibition on disclosure of information obtained or held under five pieces of UK ETS legislation for the specific purposes of policy development relating to climate change will be introduced. Where necessary or expedient, such disclosures will improve policy development or implementation in the following specific areas: (i) the limitation, reduction, or removal of greenhouse gas emissions; (ii) countering carbon leakage; (iii) mitigating the effects of climate change. An exemption such that a national authority is permitted to disclose UK ETS information where necessary or expedient for the purpose of supporting the CCC in performing its statutory functions will also be introduced.

- *Ultra-small emitter (USE) scheme:* The 2020 Order did not permit applications for USE status from operators which started operations after the start of the scheme on 1 January 2021. It is appropriate that operators which started operations after that date should be able to apply for USE status, and the UK ETS Authority has determined that one full scheme year of data is sufficient to demonstrate eligibility for USE status. Therefore, this instrument amends the criteria so that operators with at least one full scheme year of operation are permitted to apply for USE status for the 2026-2030 period. This means that operators which started operations between 2 January 2021 and 1 January 2024 inclusive are eligible to apply for USE status for the 2026-2030 period.

EU Alignment Consideration

The UK ETS was established under the Climate Change Act 2008 by the Greenhouse Gas Emissions Trading Scheme Order 2020 (the “2020 Order”) as a UK-wide greenhouse gas emissions trading scheme to encourage cost-effective emissions reductions which will contribute to the UK’s emissions reduction targets and net zero goal. The UK ETS is operated by the UK ETS Authority, comprising the UK Government, Scottish Government, Welsh Government and the Department of Agriculture, Environment and Rural Affairs in Northern Ireland. The UK ETS replaces the UK membership of the EU Emissions Trading Scheme following the UK’s exit from the EU. Directive 2003/87/EC (as amended) established the EU emissions trading scheme, which created a European Union market in greenhouse gas emissions allowances. The 2020 Order applied EU ETS rules on the monitoring, reporting and verification of emissions with modifications to ensure that they work for the UK ETS.

The FA provisions in this instrument will move the start of the next allocation period to 2027, although this is misaligned with the start of the next period in the EU ETS, which will be in 2026, the intent of aligning allocation periods with CBAM introduction is the same across the UK and the EU. In addition the change to the allocation period will not impact FA methodology which is still broadly in line with the way Free Allocations are calculated in the EU ETS

Regarding the data and USE changes, this instrument aligns in intent with EU ETS policy and is not expected to have any impact on any wider interactions with the EU. That is because all the changes in this instrument match or exceed ambitions and commitments of the EU ETS. This is also the case for the other provisions in this instrument.

Consultation

Two targeted consultations to the affected parties have been published in relation to the provisions provided for by this instrument.

A targeted consultation on moving the second UK ETS free allocation period was sent by the Regulators to relevant participants in September 2024. It asked current UK ETS participants if they agreed that the year 2026 should be treated as an extension of the 2021-2025 allocation period for the purposes of determining the quantity of free allowances that eligible participants could receive.

The UK ETS Authority received 26 responses to the consultation with 20 (77%) respondents agreeing to the proposal and three (11.5%) disagreeing, indicating broad support among participants for the changes and proposed implementation.

The “UK Emissions Trading Scheme: Moving the Second UK ETS Free Allocation Period Authority Response” was published on 16/12/2024 and can be found here:

https://assets.publishing.service.gov.uk/media/676000e81857548bccbcfa2a/ukets-moving-second-free-allocation-period-authority-response.pdf

A targeted consultation on Registry transaction publication, UK ETS information disclosure and USE criteria for 2026-2030 was sent to operators, trading account holders and trade bodies representing operators in September 2024.

The UK ETS Authority received 27 responses to the consultation. Responses to the transaction publication proposal were balanced between support and opposition. There was a balance of support and opposition for the proposals to permit disclosure of UK ETS information for the purposes of policy development or implementation, and to aid the CCC in the delivery of its statutory functions. All responses to the proposal to extend the 2026-2030 USE eligibility criteria expressed support.

The UK ETS Authority will issue its response to the consultation ahead of, or concurrently with, laying the instrument.

The Information Commissioners Office was informed of the transaction publication proposal in line with Article 36(4) of the General Data Protection Regulation.

Impact Assessments

A full Impact Assessment has not been prepared for this instrument because it is not a regulatory provision.

Financial Effects

The impact on business, charities or voluntary bodies from the free allocation provisions are minimal as 2026 free allocation will continue to be awarded on the basis of current rules and the ability of businesses who were previously ineligible for free allocation during the first period will still be able to apply for the 2026 scheme year.

The legislation does impact small or micro businesses. To minimise the impact of the requirements on small or micro businesses (employing up to 50 people), operators with relatively low levels of emissions are either not caught by the scheme or participate in the HSE or USE schemes, which have lower compliance burdens than the main UK ETS. This provision extends the eligibility criteria for the USE scheme, helping those newly eligible small businesses to reduce their compliance burdens.

There is no significant, impact on the public sector. Hospitals participate in the HSE scheme, which has lower compliance burdens than the main UK ETS.

Scottish Government
Energy and Climate Change Directorate
February 2025