EXPLANATORY MEMORANDUM TO

THE CARBON ACCOUNTING (PROVISION FOR 2020) REGULATIONS 2022

2022 No. 62

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Business, Energy and Industrial Strategy and is laid before Parliament by Command of Her Majesty.

1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 These Regulations ("the Regulations") update the carbon accounting system which is used to monitor compliance with the targets for reducing greenhouse gas emissions introduced by the Climate Change Act 2008 ("the Act"). The Regulations update the accounting system, as set out in the Carbon Accounting Regulations 2009 ("the 2009 Regulations")[1], the Carbon Accounting (2013-2017 Budgetary Period) Regulations 2015 ("the 2015 Regulations")[2], the Carbon Accounting (Provision for 2018) Regulations 2020 ("the 2020 Regulations")[3] for the first year (2018) of the third carbon budget period (2018-2022), and the Carbon Accounting (Provision for 2019) Regulations 2021 ("the 2021 Regulations")[4] for the second year (2019) of the third carbon budget period.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 The Regulations are made for the third year (2020) of the third budgetary period (2018-2022). The provision in respect of 2020 is needed in time for the 2020 Annual Statement of Emissions which, under section 16 of the Act, must be laid before Parliament by 31 March 2022.

3.2 Carbon Accounting Regulations are typically set for the entire carbon budget period, however this was not possible for the first two years of the third carbon budget (2018 and 2019) due to uncertainties arising from the UK leaving the European Union Emissions Trading System (EU ETS) and incomplete negotiations on the handling of carbon markets under the Paris Agreement. As there are still outstanding considerations on the UK ETS and the application of international guidance, the decision was taken to make provision in this instrument for just one year (2020), as

[1] The Carbon Accounting Regulations 2009:
https://www.legislation.gov.uk/uksi/2009/1257/contents/made
[2] The Carbon Accounting (2013-2017 Budgetary Period) Regulations 2015
https://www.legislation.gov.uk/uksi/2015/775/contents/made
[3] The Carbon Accounting (Provision for 2018) Regulations 2020
https://www.legislation.gov.uk/uksi/2020/115/contents/made
[4] The Carbon Accounting (Provision for 2019) Regulations 2021
https://www.legislation.gov.uk/uksi/2021/189/contents/made

the 2020 Regulations did in respect of 2018, and the 2021 Regulations did in respect of 2019. Further carbon accounting regulations will be made in early 2023 for the fourth year of the third budgetary period (2021) as a minimum.

3.3 Section 27(5) of the Act requires Carbon Accounting Regulations to contain provision for calculating and cancelling any excess emission allowances allocated to the UK under UK emissions reduction targets (i.e. under the Kyoto Protocol) compared to those targets under the Act. The 2009 Regulations set out these provisions relating to the first commitment period of the Kyoto Protocol (2008-2012). Subsequent Regulations have not set out these provisions for the second commitment period of the Kyoto Protocol (KP2 – 2013-2020) because, due to late ratification of KP2, the UK only received KP2 emissions allowances (Assigned Amount Units – AAUs) in 2021.

3.4 Although we anticipated (in section 3.3 of the Explanatory Memorandum to the 2021 Regulations) that we might be in a position to include calculations in respect of KP2 excess emissions allowances in this 2022 instrument, this has not been the case. Discussions continue and the issue remains under review.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is the whole of the United Kingdom.

4.2 The territorial application of this instrument is the whole of the United Kingdom together with UK coastal waters and the UK sector of the continental shelf (see section 89 of the Act).

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

6.1 The Regulations are made pursuant to section 27 of the Act, which provides for the Secretary of State to make regulations for carbon accounting. They are an important part of the system set up by the Act for limiting greenhouse gas emissions. Under the Act, there is a 2050 target for reducing emissions (section 1) and the Government sets limits on emissions for successive five-year periods (carbon budgets, set under sections 4 and 8). These provisions work by reference to the "net UK carbon account", defined in section 27. The amount of the net UK carbon account depends in part on carbon accounting regulations made under section 27 (see below). The 2009 Regulations were the first regulations to be made under section 27, and the 2015 Regulations, the 2020 Regulations and the 2021 Regulations were also made under these powers, but certain provisions in those regulations relate to specific carbon budget periods or years.

6.2 The Regulations provide the accounting system for the third year (2020) of the third carbon budget period (2018-2022) by:

a) providing a mechanism to account for credits and debits to the net UK carbon account as a result of the operation of the EU ETS other than in respect of aviation during 2020;

b) providing a mechanism to account for domestic aviation (flights between UK airports) during 2020, which is included in the EU ETS;

c) requiring the Secretary of State, at the end of the third carbon budget period, to cancel any carbon units bought on international markets or otherwise acquired by the Secretary of State in respect of 2020 to help meet the third carbon budget (this is extremely unlikely to be needed but section 27(4) requires the Regulations to ensure that carbon units held by the Secretary of State for this purpose are put beyond use).

7. Policy background

What is being done and why?

7.1 The Act mandates a legally binding framework for the UK to achieve its goals of reducing greenhouse gas emissions and ensuring steps are taken towards adapting to the impacts of climate change. It puts the UK firmly on a pathway to becoming a net zero economy. It also demonstrates, at home and abroad, the Government's commitment to taking the action necessary to avoid dangerous climate change.

7.2 The Climate Change Act 2008 (2050 Target Amendment) Order 2019 put into statute the UK's net zero target to reduce greenhouse gas emissions by at least 100% by 2050 compared to emissions in 1990 which represent the baseline. To set the trajectory towards this target, and help provide certainty for business planning and investment, the Act establishes a system of "carbon budgets" capping emissions over successive five-year periods.

7.3 The Act established the concept of the "net UK carbon account", which is the number we compare against the carbon budgets to determine whether we are meeting them. The net UK carbon account is calculated by taking net UK emissions for a given period and then taking account of carbon units representing emissions reductions that have been brought into the UK from other countries ("credits") or that have been debited or credited in accordance with carbon accounting regulations.

7.4 The principal reason for making the Regulations is to make provision for carbon accounting in respect of the third year (2020) of the third carbon budget period.

EU ETS (stationary installations)

7.5 The Regulations provide a mechanism to account for credits and debits as a result of the operation of the EU ETS during the third year (2020) of the third carbon budget period, when the UK was still an EU Member State. The underlying policy rationale is that any amount of emissions from EU ETS operators in the UK in excess of the UK's cap on emissions under the system (which is expressed as the "annual allocation") must be considered as a credit, as this suggests operators have bought units from overseas to offset UK emissions or relate to units which could have been used at an earlier time (as the EU ETS rules allow). Conversely, where emissions from the EU ETS sector are lower than the cap, the difference between these two must be considered a debit, as this suggests operators are either in possession of, or have sold excess units which have not been used to offset emissions in the UK but could be used to offset emissions elsewhere or at a different time.

7.6 For the first three years (2018-2020) of the third budgetary period, the rules governing operation of the EU ETS third phase are such that Member States do not receive a

national cap as the EU ETS is operated at installation level[5]. Therefore, in place of using a fixed cap as defined in EU legislation (as was the case for the first carbon budget period), components of the cap are replicated to create a 'notional' cap. The notional cap is created by adding together the volume of EU allowances freely allocated to stationary UK operators (45,876,077[6]), the volume of EU allowances freely allocated a share of the New Entrants Reserve to stationary UK operators (2,183,806[7]), and the volume of allowances in the EU-wide auction pot to be auctioned by the UK to stationary operators (55,963,500[8]). Therefore, the UK 'notional' cap (which is expressed as the "annual allocation") totals 104,023,383 units.

7.7 The 2020 Annual Statement of Emissions will contain further background on this calculation. The figure for ETS allowances allocated to the UK ("annual allocation") for 2020 is similar to the 2019 figure of 104,424,206, however both the 2019 and 2020 figures are significantly lower than previous years. This reflects a number of complexities in the EU ETS phase III (2013-20) – most notably the launch of the EU ETS Market Stability Mechanism, where a substantial number of allowances from Member State auctions were put into a reserve instead of being sold. This has resulted in a less uniform distribution of allowances over time than envisaged when the Carbon Budgets were set.

Domestic Aviation

7.8 The Regulations provide a mechanism to account for domestic aviation during the third year (2020) of the third budgetary period which is the same as the mechanism used during the second budgetary period under the 2015 Regulations, for 2018 under the 2020 Regulations, and for 2019 under the 2021 Regulations. Whilst the EU ETS provided an EU-wide cap for aviation emissions and units to confirm UK compliance it did not provide a cap for UK only domestic aviation (flights between UK airports) emissions and so it is not possible to distinguish between domestic aviation emissions and international aviation emissions, which are excluded for the purposes of the third carbon budget[9].

7.9 Using civil aviation data from the UK greenhouse gas inventory submitted under the EEA, and published on the European Environment Agency website, the steps listed below are used to estimate a fixed cap against which we will report emissions from UK domestic aviation. This approach uses a baseline of total European Economic Area (EEA) domestic flights (i.e. total flights within individual EU countries plus Norway, Liechtenstein and Iceland), and an estimate of what share of this total can be attributed to the UK. The cap is set at 95% of the estimated UK share. The Schedule to the Regulations sets out the methodology to be used for the calculation. The 2020

[5] Further information on how the EU ETS operates:
https://www.gov.uk/participating-in-the-eu-ets
[6] European Union Registry, verified emissions report 2020 (April 2021)
https://ec.europa.eu/clima/policies/ets/registry_en#tab-0-1
[7] European Union Registry, verified emissions report 2020 (April 2021)
https://ec.europa.eu/clima/policies/ets/registry_en#tab-0-1
[8] Intercontinental Exchange
https://www.theice.com/marketdata/reports/148
[9] Under section 30 of the Act. The Climate Change Act 2008 (2020 Target, Credit Limit and Definitions) Order 2009, sets out a definition of "international aviation" for the purposes of section 30

Annual Statement of Emissions will contain background on this calculation but in summary there are three steps to the calculation:

a. **Calculate a baseline of total EU domestic aviation:** The baseline is the average of 2004-06 EEA domestic aviation emissions (flights within individual EEA countries). 2004-06 is used as this is a common baseline used for EU environmental targets.

b. **Calculate UK share and apply to the baseline:** The UK's share of EEA domestic emissions is taken from 2010. The UK's domestic aviation emissions are compared to total EEA domestic aviation emissions in this year (data for both are taken from the EU inventories as reported by the European Environment Agency). 2010 is used because this was the benchmarking year for the allocation of free allowances to aircraft operators. This UK share of EEA domestic aviation is then applied to the 2004-06 EEA average.

c. **Apply a reduction to the resulting figure:** For 2020 the cap will be 95% of this annual average.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 This instrument does not give rise to the need for any consolidation.

10. Consultation outcome

10.1 There was no public consultation required by the Regulations.

11. Guidance

11.1 It is the responsibility of Government to determine compliance with carbon budgets, and the Regulations do not place any requirements, or have any users, outside Government. The Annual Statement of Emissions for 2020 will contain further information relevant to calculating the net UK carbon account.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 A full Impact Assessment has not been prepared for this instrument because there is no, or no significant, impact on businesses, charities, voluntary bodies or the public sector.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 The approach to monitoring of this legislation is that, as the Regulations are for the third year (2020) of the third carbon budget period, the Regulations will be updated again in early 2023 for the fourth year (2021) as a minimum.

14.2 The Regulations do not include a statutory review clause as the legal obligations in this regard under the Small Business, Enterprise and Employment Act 2015 do not apply.

15. Contact

15.1 Rachel Armitage at the Department for Business, Energy and Industrial Strategy Telephone: 0300 068 6230 or email: carbonbudgets@beis.gov.uk can be contacted with any queries regarding the instrument.

15.2 Joanna Warner and Helen Martin at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.

15.3 The Rt Hon Greg Hands MP at the Department for Business, Energy and Industrial Strategy can confirm that this Explanatory Memorandum meets the required standard.