business action on climate change

where next after emissions trading?

"green alliance...

Business Action on Climate Change: Where next after emissions trading?

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about the organisations

Green Alliance

Green Alliance is one of the UK's foremost environmental groups. An independent charity, its mission is to promote sustainable development by ensuring that the environment is at the heart of decision-making. It works with senior people in government, parliament, business and the environmental movement to encourage new ideas, dialogue and constructive solutions.

Institute for European Environmental Policy (IEEP)

The IEEP is a leading centre for the analysis and development of environmental and related policies in Europe. An independent, not for profit organisation, the Institute has offices in London and Brussels. IEEP brings a non-partisan analytical perspective to policy questions, engaging in both pressing short-term questions and long-term strategic studies. We focus primarily on European Union environmental and sustainable development policies, and relevant aspects of other policies such as agriculture, transport, rural and regional development and fisheries. We are also actively engaged in the development of policy at a national level in Europe. The Institute seeks both to raise awareness of the policies that shape the European environment and to advance policy-making along sustainable paths.

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The recommendations presented in this report are put forward by Green Alliance and IEEP, and do not necessarily represent the position of project partners or steering group members.

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executive summary

The UK has a clear commitment to tackling climate change – yet government estimates suggest that we are not currently on track to meet targets for carbon dioxide reduction – particularly the pledge to reduce carbon dioxide emissions by 20 per cent below 1990 levels by 2010.

This report focuses on the business sector, evaluating the policies in place to help business take action on climate change. It looks in particular at the implications of the EU's Emissions Trading Scheme (EU ETS), which began on 1 January 2005 and creates an EU-wide market for carbon. This report reviews the incentives in place to encourage business action on climate change, and makes recommendations for strengthening and simplifying the policy framework. It considers the following policies: the EU ETS, the Climate Change Levy (CCL), the Climate Change Agreements (CCAs), the Carbon Trust, the UK Emissions Trading Scheme and the Renewables Obligation. Descriptions of each of these policies are set out in the introduction.

Methodology

The report is based on research conducted in the second half of 2004, while the arrangements for the EU ETS were being finalised. The research consisted of an initial literature review; a series of semi-structured interviews with 25 key stakeholders representing government, industry, NGOs and independent experts; and finally a stakeholder seminar, held in November 2004, at which draft findings and recommendations were presented and discussed.

The report contains three sets of research findings and recommendations, as follows.

The Climate Change Programme (CCP) Review

Our research showed a clear need to review domestic climate change policy, irrespective of the EU ETS, because the UK is not on track to meet its targets. Participants felt that the government was providing clear signals about the importance of climate change and the need to take action, but that there was no clear link between this overall message and individual policies. Many criticised the complexity and lack of coherence of the package of measures in place. Based on these findings, the following recommendations are put forward:

> " our research showed a clear need to review domestic climate change policy, irrespective of the EU ETS, because the UK is not on track to meet its targets "

- Set out a clear path to meeting targets. The aim of the CCP Review should be to establish a longer-term, defined pathway that sets out objectives, dates, actions and reviews, to make it clear how objectives will be achieved.
- Recognise the limitations of carbon pricing. The EU ETS is unlikely to result in a significant price for carbon in the short term. Even if this does occur over the longer term, there will still be a need for a package of measures. A price for carbon is necessary but not sufficient. It will

not automatically encourage the development of innovative technological solutions. Other policy measures also provide vital awareness-raising benefits, which might be lost if the price of carbon is just subsumed into the general price of energy. Finally, emissions trading cannot incorporate all businesses, particularly small business, so other measures will be needed to incentivise this group.

- Plan ahead for Phase II of the EU ETS. The Review should map out the process of preparing for the next phase of the EU ETS, to overcome the weaknesses of Phase I.
- Address gaps in climate policy. Policy needs to be developed to incentivise the commercial sector and SMEs, as well as the transport and domestic sectors.
- Address competitiveness concerns. Few participants saw the EU ETS or UK policy measures as a threat to competitiveness. However, these concerns continue to be expressed, and there is a need for further research to consider whether well-designed environmental regulation can aid competitiveness.
- Raise awareness. The Government, NGOs, the media and business need to help raise awareness of climate change both amongst the public and the business community.

EU Emissions Trading

Our research shows strong support for the principle of EU emissions trading. However, concerns were expressed about the way the scheme is being implemented, both at an EU level and in the UK. The scheme will only achieve its aims if emission allocations are limited, and this may not happen, as member states have been given considerable leeway in allocating allowances. There was significant criticism of the way the UK developed its National Allocation Plan (NAP), particularly the October 2004 decision to increase the number of allowances issued. Given these difficulties, we make the following recommendations for the second phase of the EU ETS:

> “ there was significant criticism of the way the UK developed its National Allocation Plan, particularly the decision to increase the number of allowances issued ”

- The Commission should conduct a thorough review of Phase I. It should build the lessons learned into Phase II, particularly looking at the use of emissions projections as the basis of NAPs.
- The UK's approach should be considered in the context of the CCP Review. There should be a particular focus on the way in which the National Allocation Plan is drawn up.
- Develop NAPs early. The UK should use its 2005 Presidency of the European Council to push for early development of NAPs for Phase II.
- Strengthen the NAP process. The Commission and all member states should take a stronger line to ensure that there is not the same degree of over-allocation of permits in Phase II.
- Harmonise implementation. Greater harmonisation across member states could help prevent over-allocation. An EU-wide cap is desirable but unlikely. Member states could, however, co-ordinate development of their NAPs.

The domestic policy framework

It is clear from our research that the EU ETS should not prompt major revisions of policy in the short-term. It is not clear yet how effective the scheme will be, or whether a significant price for carbon will emerge. The major driver of change for the domestic policy framework should be a strengthening of policies to meet carbon targets. On the basis of the research findings, we put forward a package of measures that will complement the EU ETS, and help the UK achieve its domestic targets.

" it is not clear whether a significant price for carbon will emerge "

We recommend the following policy measures, to strengthen and simplify domestic policy:

The Climate Change Levy, Climate Change Agreements and the Carbon Trust

The Climate Change Agreements (CCAs) were considered to be an effective measure, though uncertainties were expressed over whether they were ambitious enough, and if it was realistic for SMEs to participate. However, the CCL was considered to be less effective as an incentive to reduce energy use, and so there is a need to further incentivise sectors outside the CCA system. The work of the Carbon Trust was supported, though there were concerns that many businesses are not aware of its schemes and do not make use of the opportunities offered. The following recommendations are therefore put forward:

- Maintain the CCL as an energy tax, with the aim of promoting energy efficiency to all businesses. Increase the CCL, whilst recycling the revenues, to stimulate action on energy efficiency in line with the UK's targets. The CCL would therefore remain as a downstream measure to stimulate energy efficiency in those sectors not in the EU ETS, thereby complementing the trading scheme. The CCL should also be increased, with revenues recycled, to a level that stimulates further energy efficiency measures.
- Maintain the Climate Change Agreements, but open the process of target-setting to public scrutiny. The EU ETS was developed through an open process of target-setting, which proves that this is feasible.
- Incentivise CCL-payers to invest in energy efficiency, by offering temporary or partial reductions in the CCL, linked to participation in Carbon Trust schemes. This would encourage all businesses to consider energy efficiency improvements. The system would need to be administratively simple, so that SMEs could access it.

The UK Emissions Trading Scheme (UK ETS)

This was not considered to be an effective policy instrument in its current state. Most thought that it had not resulted in emissions reductions beyond what would have been achieved without the scheme. However it was seen as useful in preparing businesses for trading and establishing a UK infrastructure for trading. Most felt that the UK ETS had served its purpose, but there was support for the idea of changing the scheme to incentivise energy efficiency in non-energy-intensive sectors. Therefore we recommend the following:

- The UK Emissions Trading Scheme should not continue in its current form. The scope for restructuring the Scheme into an instrument that incentivises action

in other sectors not covered by the EU ETS, such as the commercial building sector, should be explored.

The Renewables Obligation

This was considered to be one of the most effective UK instruments, with success in stimulating investment in renewable energy. However, its scope is seen as narrow, only benefiting certain technologies. It was noted that there is a lack of policy instruments to encourage the development of technologies that are less able to compete commercially. We therefore recommend:

- The Renewables Obligation should be maintained. There is a need to simplify procedures to help small-scale generators to participate.
- The Climate Change Programme Review, and forthcoming review of the Renewables Obligation, should look at ways of encouraging renewables technologies that do not currently benefit from the Renewables Obligation.

Introduction

The UK has a clear commitment to tackling climate change, reflected in the goal of reducing carbon dioxide emissions by 20 per cent below 1990 levels by 2010 – and the long-term pledge to reduce emissions by 60 per cent over the next fifty years, as set out in the 2003 Energy White Paper. These ambitious targets will require robust policies, support and encouragement from government to bring about sustained action by business and consumers.

Recent Government estimates suggest that we are not on track to meet our targets. 'Carbon dioxide emissions could, on the basis of current policies and measures, be about 14 per cent below 1990 levels by 2010', falling short of the 20 per cent target, as the Government admitted in launching its Review of the Climate Change Programme in December 2004. This report aims to help in evaluating existing measures, and suggesting improvements, in order to achieve the 20 per cent goal.

> " ambitious targets will require robust policies, support and encouragement from government "

This report focuses on the business sector, evaluating the policies in place to help business take action on climate change. It looks in particular on the implications of the EU's Emissions Trading Scheme (EU ETS), which began on 1 January 2005. The research for this report took place in the second half of 2004, while the final arrangements for the EU ETS were being negotiated.

The EU ETS is an ambitious attempt to create a Europe-wide market for carbon, and incentivise businesses across the EU to reduce their emissions. But what does it mean for the policies that the UK already has in place? This report presents research which assesses the impact of the EU ETS on domestic climate change policy, to inform the review of the UK's Climate Change Programme, which Defra is currently undertaking. The aims of the research were:

- To review the incentives in place to encourage business action on climate change, following implementation of the EU emissions trading scheme, through a survey of senior energy stakeholders in government, business and the voluntary sector.
- To make recommendations for simplifying and strengthening the policy framework for business action on climate change.

Current policies

Since 1997, a range of policy measures have been put in place to encourage business action on climate change. These were set out in the Government's 1999 UK Climate Change Programme, and are now under review.

As part of this research, we considered the following measures:

The Climate Change Levy (CCL): this is a tax on business and public sector energy use, introduced in April 2001. The tax applies to electricity, gas, liquid petroleum gas (LPG) and solid fuels. Good-quality combined heat and power (CHP) and renewable energy are exempt. The charge appears on energy bills. Revenue raised from the Levy is recycled through a 0.3 per cent reduction in employers' National

Insurance Contributions, and additional government support for energy efficiency measures through the Carbon Trust (see below). Energy intensive sectors can gain an 80 per cent exemption from the Levy if they participate in a Climate Change Agreement (see below).

Climate Change Agreements (CCAs): part of the CCL package, the CCAs are negotiated agreements between government and energy intensive sectors. These industries receive an 80 per cent discount on the CCL in return for meeting targets on energy efficiency and carbon emissions. Nearly 6000 companies in 46 industrial sectors participate. Companies in the same sector commit to an overall target, through an industry association. If the sector target is achieved, all companies in the sector receive the rebate irrespective of individual performance. Companies also receive the rebate if they achieve their individual target, even if the sector as a whole does not.

The Carbon Trust: the Carbon Trust is an independent company funded by Government and revenue from the CCL. Its role is to help business and the public sector reduce carbon emissions and capture the commercial opportunities of low carbon technologies. The Carbon Trust delivers advice and support to help business and public sector organisations reduce their emissions, primarily through energy efficiency. It administers the Enhanced Capital Allowance scheme on behalf of Government. The Carbon Trust also supports and invests in the development of new and emerging low carbon technologies.

The UK Emissions Trading Scheme: this voluntary initiative allows businesses to trade carbon permits. Its aims are to contribute to 3.96 million tonnes of carbon dioxide reductions by 2006; help UK firms learn about emissions trading and prepare for international trading; and establish the City of London and the UK as an international centre for emissions trading. It is a 'cap and trade' scheme, which sets an overall emissions reduction target. 34 companies, known as 'direct participants', bid for emissions reductions for the period 2002-06 in return for a share of £215 million funding from Defra in March 2002. Participants can either reduce their own emissions or buy emissions allowances. The scheme is also open to the 6000 organisations in a CCA (see above), who can trade but are not direct participants. Since the scheme began, the market for emissions allowances has been variable in terms of quantities traded and the prices obtained. The price for allowances peaked at £12.50 per tonne in September/October 2002, but has averaged around £2.50 per tonne. At no time has it met the price set at auction of £17.79 per tonne.

The Renewables Obligation (RO): introduced in April 2002, it requires all licensed electricity suppliers in England and Wales to supply a specified proportion of their sales from renewable sources. Suppliers demonstrate compliance either through presenting Renewable Obligation Certificates (ROCs), paying the buy-out price, or a combination of both. The aim is to increase the proportion of electricity provided by renewable sources to 10.4 per cent by 2010/11 (subject to the cost to consumers being acceptable), and the Government intends to raise this to 15.4 per cent by 2015. The RO also covers Scotland, under a similar arrangement.

The scope of this report

In addition to the measures described above, there are other policies in place that affect the business sector. These include: the Energy Efficiency Commitment, a requirement for electricity and gas suppliers to meet targets for the promotion of improvements in domestic energy efficiency; Buildings Regulations, which set mandatory standards for energy efficiency in buildings; product-related measures

Box 1: The research methodology

The methodology had four stages: literature review; interviews with key stakeholders; analysis; and a stakeholder seminar. In addition, a Steering Committee consisting of representatives from the business community and green groups was set up to provide advice at various key stages of the project.

Literature review: all the key reports of importance to this study were reviewed. An initial list was drawn up, and amended by the Steering Committee. The list of reports can be seen at Annex A. The research report, containing the full literature review is available online, at www.green-alliance.org.uk or www.ieep.org.uk

Interviews: a series of semi-structured interviews was undertaken with 25 key stakeholders representing various stakeholder groups. A potential list of interviewees was drawn up on the basis of consultation with the Steering Committee. A representative sample of the full list was approached for interview. A breakdown of the stakeholder groups to which the interviewees belonged is given in the table, below.

Stakeholder group	Number of interviewees
Government	6
Industry	8
NGOs	5
Independent experts/policy watchers	6
Total	25

The content and format of the questionnaire was also guided by the Steering Committee. A draft set of questions was discussed with the Steering Committee, before being finalised. The interviews were held from July to September 2004, while the UK was finalising its NAP and before the announcement of the additional revision in October 2004. Interviewees were asked their views on:

- The effectiveness of existing UK climate change policy instruments aimed at the business sector;
- The implementation of the EU Emissions Trading Scheme; and
- The implications for the future of UK climate change policy.

Analysis: The interviews were written up and verified with the respective interviewees. A matrix of responses to the various questions was drawn up, with the various responses categorised according to the stakeholder group to which the interviewee belonged. This was used as the basis of the analysis. On the basis of the literature review, the analysis of the interview responses and consultation with the Steering Committee, the researchers developed a set of recommendations.

Stakeholder seminar: A stakeholder seminar was held on 17 November 2004 at which the draft findings and recommendations, as set out in the interim report, were presented. This report has been developed in light of the discussion at that seminar.

This report is closely informed by the project partners, interviewees, seminar participants and steering group. However, the views and recommendations expressed do not represent a formal consensus and should not be taken as representative of all involved.

aimed at stimulating the market for energy efficient products; and measures focused on transport, agriculture and the public sector.

This study does not consider these policies in any detail. They were only addressed to the extent that they were seen to interact with the policies detailed above.

Report structure

The report contains three sets of recommendations, set out in the following three sections.

- The Climate Change Programme Review: this section sets out, in general terms, recommendations for the direction of the Climate Change Programme Review, in the light of the EU Emissions Trading Scheme.
- EU Emissions Trading: this section offers an assessment of the EU Emissions Trading Scheme, now that member states have submitted National Allocation Plans, and Phase I is about to commence. It offers recommendations for Phase II of the scheme, from 2008.
- Domestic policies: the final section describes how the main domestic policies are affected by the EU ETS, and puts forward recommendations for each policy. It focuses on the Climate Change Levy, Climate Change Agreements and the Carbon Trust; the UK Emissions Trading Scheme; and the Renewables Obligation.

The Climate Change Programme Review

The Government is currently reviewing the Climate Change Programme. The Programme, launched in 1999, sets out the Government's strategy for achieving targets for reduction of greenhouse gas emissions – principally, the goal of reducing carbon dioxide by 20 per cent below 1990 levels by 2010, and its long-term pledge, established in the 2003 Energy White Paper, to reduce emissions by 60 per cent by 2050. The measures within the Programme that are aimed at business are outlined in the introduction, above.

This section presents findings on the Climate Change Programme in general. In the following sections, we look specifically at the EU Emissions Trading Scheme, and at particular policies, including the Climate Change Levy, Renewables Obligation, UK Emissions Trading Scheme and the Carbon Trust.

Research Findings

The study asked interviewees for their views on the existing policies in place to encourage business action on climate change, before the advent of emissions trading. A mix of views was expressed by the different stakeholder groups – although industry groups and NGOs differ in their responses, no clear NGO position or industry position emerged.

Most interviewees felt that there was a need to review UK climate change policy, irrespective of the introduction of the EU ETS, to address the problems highlighted below. A number of ways to improve individual instruments were put forward, aimed at addressing gaps and overlaps, reducing conflicts and reinforcing signals. These are discussed in more detail in subsequent sections.

> "*If we started with a blank piece of paper, we probably wouldn't end up with the mixture that we have… but in terms of the way it has built up, it does work as a package.*"
> government representative
>
> "*As a package the CCP is a mess because each measure has been built up by a different part of government with its own objectives.*"
> independent expert

Most interviewees felt that the government was providing clear signals about the importance of climate change and the need to take action. The link between the overall message and individual policies, however, was not so clear. In particular, many criticised the complexity and lack of coherence of the package of measures in place.

Different policies have different objectives – some support energy efficiency, whereas others encourage renewable energy. This is not in itself problematic, but it is not clear enough at present how the different measures relate to, or are affected by, each other – and how they add up to a coherent package which helps business to contribute toward the UK's climate change targets.

A further conflict was perceived between policy instruments which aim to raise the price of energy, and instruments which aim to keep domestic energy affordable,

to counter fuel poverty. A number of gaps in UK climate change policy were also identified: transport (particularly aviation), the commercial/service sector, and the domestic sector. Concern was also expressed that some parts of the business community, particularly SMEs and low energy users, did not have a high level of understanding about their contribution to tackling climate change, and were not helped greatly by the policy measures currently in place. Some participants stressed the need for more regulation, such as labelling requirements and product standards, particularly to target smaller businesses who are less responsive to economic instruments.

> *"The majority of small businesses will be slightly aware of climate change, but beyond that they are not certain of the reasons for why it is important, why there is a focus on it, and why the UK is doing what it is doing."*
> industry expert
>
> *"There is still a massive lack of awareness about what we are trying to do."*
> industry expert

Looking at the effectiveness of particular instruments, some measures were seen as more effective than others. The Renewables Obligation and Climate Change Agreements were seen as most effective, with the Climate Change Levy and the UK Emissions Trading Scheme cited as being less effective. It was recognised, however, that the Climate Change Levy provided the overall context for the Agreements. There was broad support for information and advice services, including those provided by the Carbon Trust, but some doubted whether they had succeeded in raising awareness among business or delivered significant improvements.

Recommendations

Based on the interviews conducted, and the outcome of the stakeholder seminar, we put forward the following recommendations for the Review of the Climate Change Programme. Recommendations on specific instruments are set out in the final section of this report.

Set out a clear path to meeting targets

Many are sceptical about the UK's ability to meet its domestic target of reducing carbon dioxide emissions by 20 per cent by 2010, unless action is taken now to improve the policy framework. The Government itself admits that the 20 per cent target is unachievable with current policy measures. In the longer term, the 2050 target set out in the White Paper is an important signal, but interviewees were sceptical about how, and even if, this could be met. Therefore it is crucial that the CCP review clarifies how both targets will be achieved. The CCP review should set out a long-term programme of assessment and monitoring of the effectiveness of policy measures, looking not just at individual instruments but at the whole policy package. Interactions between policy instruments, and with the EU scheme, need to be

"the Government itself admits that the 20 per cent target is unachievable with current policy measures"

clearly explained. The Review should set out a clearly defined pathway that outlines not only objectives but also dates, actions and review mechanisms, so it is possible to see how objectives will be achieved.

Recognise the limitations of carbon pricing

It is unclear at present whether the EU ETS will result in a significant price for carbon. Even if this does happen over time, it will not on its own be enough to drive emissions reductions. Both the stakeholder interviews and a survey of the literature showed support for a package of measures to address aspects of climate policy. There are three reasons for this:

- Having a carbon price is necessary but not sufficient. Used in isolation, it will not automatically encourage innovation and the development of the clean technological solutions necessary to meet the goal of a significantly lower carbon future.
- There are other vital awareness raising benefits provided by some policy measures, which might be lost if the price of carbon is just subsumed into the price of electricity.
- Emissions trading might never practically or efficiently be able to incorporate all businesses. There is a need for measures to capture business emissions outside its scope.

There is, therefore, no argument for dismantling or radically altering the domestic policy framework for climate change in order to account for emissions trading. This point is discussed further in the section below on specific instruments.

> “ there is no argument for dismantling or radically altering the domestic policy framework for climate change to account for emissions trading ”

Plan ahead to Phase II of the EU ETS

The CCP review will set policy for the next five years. It should, therefore, map out the process of preparing for Phase II of the EU ETS. The following section offers more detail on this point.

Address gaps in climate change policy

Participants in the survey were asked to identify the main gaps in climate policy. Interviewees repeatedly highlighted the need to address the commercial sector, and SMEs. The CCP review should therefore concentrate in particular on these parts of the business community, and consider regulatory solutions for these sectors, in addition to economic instruments. More widely, the Government should also be seen to be tackling other sectors responsible for an increasing proportion of emissions i.e. the transport (including aviation) and domestic sectors.

Address competitiveness concerns

The UK Government should sponsor a detailed research study to examine the effects of climate change policy on business competitiveness. The findings of this study should inform UK policy and Phase II of the EU ETS. Few participants in our research project saw the EU ETS or UK policy measures as a threat to competitiveness. However, concern continues to be expressed that such policies could affect the competitiveness of UK firms. It seems, therefore, that there is a need

for further research into competitiveness concerns. This research should consider whether well-designed environmental regulation can aid competitiveness.

Raise awareness

To ensure support for climate change policy, there needs to be better communication from stakeholders, including the government, but also NGOs, proactive businesses and the media. There is a need to engage the public and other businesses such as SMEs in the debate, and to make people aware of the role that they can play in reducing greenhouse gas emissions.

In the following sections, we offer more detail on these findings, as they apply to specific policies: the EU's Emissions Trading Scheme, and the domestic policies currently in place.

EU Emissions Trading: an assessment and recommendations for Phase II

The Directive establishing an EU-wide emissions trading scheme (EU ETS) was agreed in 2003, following protracted negotiations between member states. The scheme forms the central plank of the EU's collective response to Kyoto. Phase I of the EU ETS, which is effectively a pilot stage, began on 1 January 2005 and operates until the end of 2007. Phase II runs from 2008 to 2012 to coincide with the Kyoto commitment period.

The EU ETS aims to establish a Europe-wide market for carbon. Emission allowances are allocated to companies that operate within the participating sectors (see box 2 for list of sectors covered). From 2005, operators of plants must hold sufficient allowances to cover their carbon dioxide emissions, or they will incur fines. However, if they emit more than the allowances originally allocated to them, then they are able to purchase allowances from any companies with spare allowances.

" the development of the UK's NAP has been marred by controversy "

Although the market is Europe-wide, many specific decisions about the working of the scheme are made at member state level. Each country produces a National Allocation Plan (NAP) to be submitted to the European Commission for assessment and approval. The NAP states the total quantity of allowances that the member state will allocate, and how it proposes to allocate them. NAPs are assessed by the European Commission to ensure that they are compatible with the Directive and each member state's Kyoto target. Phase I of the EU ETS only covers carbon dioxide emissions, and each member state is also allowed to exclude certain installations if they are covered by national policy measures instead. In Phase II, member states are allowed to extend the coverage to other greenhouse gases and to other sectors.

The development of the UK's NAP has been marred by controversy. In January 2004, a draft plan was published, which set out reductions of 16.3 per cent in Phase I, rising to 20 per cent in Phase II. In April, the draft NAP was submitted to the Commission, and contained slightly less stringent targets than the January plan. In October 2004, the Government further revised the plan (after the research interviews for this project had been undertaken) in spite of the fact that the Commission had approved the plan submitted in April. The final revision increased the number of allowances that would be made available in Phase I. The allocations were reviewed in the light of a 7.6 per cent increase in the projected emissions of installations covered by the EU ETS. Given the projected increases in emissions, the Government maintained that the revised NAP required a greater reduction compared to business-as-usual projections. However, the increase in allowances was widely criticised by environmental groups.

" The UK NAP… doesn't match the 2010 domestic carbon dioxide target and doesn't support the goals and aspirations of the Energy White Paper. In terms of the allocations, too many have been given."
NGO representative

> *"The extent to which it will encourage business action will depend on the caps. If right it will send strong signals. If too loose the carbon price will be too low and so it won't do anything."*
> government representative

> *"Achievements will be driven by the strength of action and commitments of other people in the scheme as well as ourselves. Therefore the UK will need to focus more on making a better case."*
> government representative

By the end of June 2006, the Commission is to present a progress report on the operation of the first phase of the scheme and make recommendations on how the scheme is to be further developed. By the same date, member states have to submit their NAPs for the second phase of trading.

Box 2: The sectors covered by the EU Emissions Trading Scheme

The EU Emissions Trading Scheme is mandatory for the following sectors, which are a selection of those covered by the 1996 Integrated Pollution Prevention and Control Directive (IPPC; Directive 96/61/EC):

1. Energy industries, including power stations and refineries;
2. Production and processing of ferrous metals;
3. Mineral industries, including cement and lime, glass, brick and tile production; and
4. Other activities, including paper and pulp production.

Other IPPC activities, such as those relating to non-ferrous metal production, the chemical industry, waste management and intensive farming are not covered by the EU ETS.

Research findings

During our research interviews and seminar, participants were asked for their views on the development, establishment and likely effectiveness of the EU ETS. There was strong support for the principle of EU emissions trading amongst all stakeholder groups. Concerns were expressed, however, about the way the EU ETS is being implemented, both at EU level and in the UK. It was widely recognised that the scheme will only achieve its aims if emission allocations are limited, so that a significant price for carbon is established. This may not happen, as member states have been given considerable leeway in allocating allowances.

"the scheme will only achieve its aims if emission allocations are limited, so that a significant price for carbon is established"

There were particular concerns about the way in which each member state had allocated its emission allowances. Under the Directive, member states have the freedom to determine how many allowances they allocate. Some participants felt that this had led to a 'race to the bottom', with individual member states shying away from tight restrictions on allowances in their own country too much, for fear of competitive disadvantage if other countries' allowances were more generous. The very different approaches taken by different member states could lead to distortions in the market for allowances, and to a low price of carbon in the market if too many allowances have been issued.

Most interviewees were initially supportive of the way in which the UK developed its NAP. However, the interviews were undertaken before the revised NAP was published in November 2004. At the seminar held following the revised NAP, there was widespread criticism of the decision to increase the number of allowances issued. The Commission was also criticised for not being rigorous enough in its assessment of NAPs.

Finally, a clear finding of the research was that the EU ETS does not present a systematic threat to the competitiveness of EU industry. It was agreed that having a price for carbon will make businesses think commercially about their emissions, which could have advantages for competitiveness. In addition, clear opportunities were seen for those businesses which will support the working of the trading system – verifiers, traders, brokers and lawyers.

Annex B summarises the strengths and weaknesses of the EU ETS, as identified by the different groups of interviewees.

Recommendations for Phase II

As described above, many participants expressed concerns about the way that Phase I had been developed, and said that there were a number of lessons to be learned for Phase II. This report recommends the following approach to Phase II:

The Commission should conduct a thorough review of Phase I

Phase I of the EU ETS is widely seen as a trial period, allowing the scheme to become established. However, given the difficulties over National Allocation Plans, Phase I is unlikely to result in a price of carbon that drives significant action. The Commission's 2006 progress report should allow a thorough review of Phase I, to ensure a more robust Phase II. The review should consider, in particular, questions about the use of emissions projections as the basis of NAPs, and consider alternatives.

The UK's approach should be considered in the context of the current review of the Climate Change Programme

There is a need to plan ahead to ensure that the lessons of Phase I are learned, at both national and EU level. The Government has already begun a general discussion about how to approach Phase II, in the context of the Review of the Climate Change Programme, but there is a need to move swiftly onto discussing the detail, particularly the allocation methodology used.

Develop NAPs early

The UK should use its presidency of the European Council in the second half of 2005 to push for early development of NAPs for Phase II, across the EU. Many interviewees in our survey blamed the failings of Phase I NAPs in part on the lack of time that member states had to prepare them.

Strengthen the NAP process

In Phase II, the Commission should take a stronger line with member states and this approach should be supported by member states' governments via the Council. There should also be advocacy on the part of proactive member states to ensure that over-allocation does not occur in Phase II, thus increasing the chance of a higher carbon price and a stronger emissions trading scheme.

Harmonise implementation

The process of developing NAPs in Phase I was widely seen as a 'race to the bottom', with member states over-allocating permits because of concerns over competitiveness. For Phase II there must be a harmonisation of actions in member states in order to achieve a level playing field based on the identification of best practice from Phase I. For example, there could be an EU-wide cap on allocations, although this may be unrealistic. At the very least, there needs to be co-ordination between member states on the development of their respective NAPs so that competitiveness concerns can be dealt with pragmatically, in a way that ensures emission reductions, rather than in a similar 'race to the bottom'. For other aspects of the Directive, including permitting and monitoring, harmonisation could also usefully take place based on agreements between the appropriate regulatory authorities and the Commission.

The domestic policy framework

The Climate Change Programme Review asks whether changes are needed to existing policy following the introduction of the EU ETS. It is clear from our research that the EU scheme should not prompt major revisions of domestic policy. This is partly because it is not clear yet how effective the scheme will be, especially given the difficulties over the National Allocation Plan process described above. The Scheme may lead to a low price for carbon, which does not incentivise action. If negotiations for Phase II are more successful, and emissions are capped at an appropriate level to meet targets, the EU ETS could eventually become the central plank of UK climate change policy for business. However, there would still be a need for additional policies, such as encouraging low-carbon innovation. A carbon price in isolation may not achieve this, particularly for technologies that are not competitive in the short-term. There is also a need for policies which raise awareness for businesses not directly engaged in the EU ETS. They will be affected indirectly by the increased carbon price, but this may not be enough to spur action.

There is, therefore, no argument for dismantling or radically altering the domestic policy framework in order to account for emissions trading. However, as the Climate Change Programme Review acknowledges, there is a need to strengthen domestic policies in order to achieve our goal of 20 per cent reduction in carbon dioxide emissions. The weakness of Phase I of the EU ETS puts more pressure on domestic policy to achieve its aims.

A further clear finding from the research is that, under the EU ETS, the UK no longer retains the same degree of control over whether its domestic target is met. Reductions from UK companies could result from purchases of reductions made by companies in other countries, or even be the result of projects in non-EU countries, as a result of the links between the EU ETS and other flexible mechanisms, such as the Clean Development Mechanism. This underlines the need for an EU ETS that operates well, as highlighted above. It also underlines the need for the UK to play a proactive advocacy role, both at the European-level and internationally. With respect to Kyoto, this needs to focus on ensuring that other EU member states take the necessary action to reduce their emissions. In the longer-term, it is needed to engage other EU member states and other large polluters, such as Russia, the US, China and India, in the development of a post-Kyoto international climate change policy framework.

“ under the EU ETS, the UK no longer retains the same degree of control over whether its domestic target is met ”

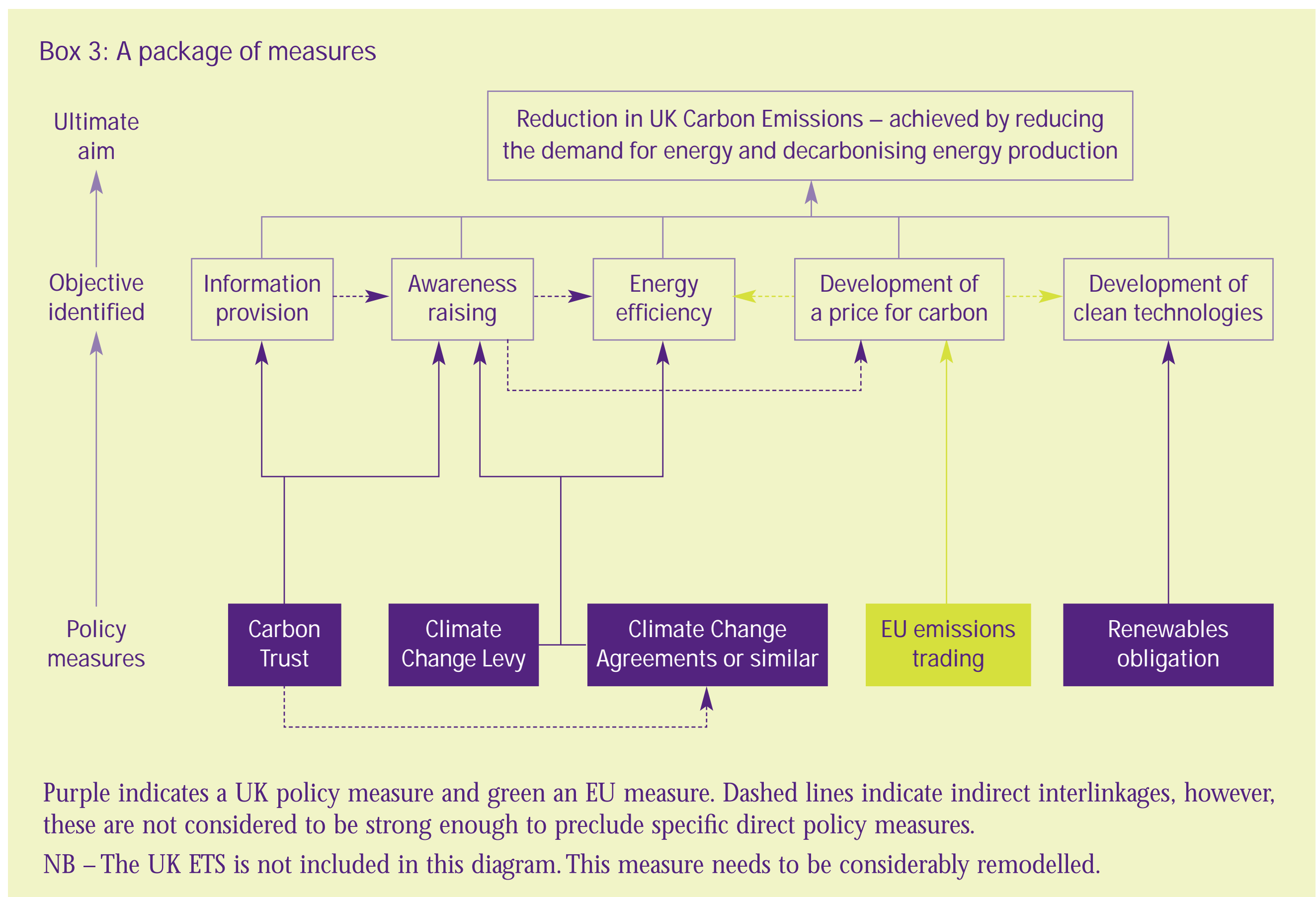
Participants in our research were also keen to point out the need for policy to address emissions from other sectors, especially road transport, aviation, and the domestic sector.

Our recommendations below focus on the need to refine and strengthen UK domestic policy. On the basis of the research findings, we put forward a package of measures that will complement the EU ETS, and help the UK achieve its domestic targets, as follows:

- Maintain the CCL as an energy tax, with the aim of promoting energy efficiency to all businesses. Increase its level, whilst recycling the revenues, in order to stimulate action on energy efficiency in line with the UK’s targets.

- Maintain the Climate Change Agreements, but open the process of target-setting to public scrutiny.
- Incentivise CCL-payers to invest in energy efficiency, by offering temporary or partial reductions in the CCL, linked to participation in Carbon Trust schemes.
- The UK Emissions Trading Scheme should not continue in its current form. The scope for restructuring the Scheme into a domestic instrument that incentivises action in other sectors not covered by the EU ETS, such as the commercial building sector should be explored.
- The Renewables Obligation (RO) should be maintained, and additional measures are needed to bring forward technologies currently not supported by the RO.
- The Climate Change Programme Review, and forthcoming Review of the Renewables Obligation, should look at ways of encouraging renewables technologies that do not benefit from the Renewables Obligation.

Box 3 shows how these measures fit together with the EU ETS to provide a co-ordinated package of measures to incentivise business to take action. Below, each of the recommendations are explained in more detail.



Purple indicates a UK policy measure and green an EU measure. Dashed lines indicate indirect interlinkages, however, these are not considered to be strong enough to preclude specific direct policy measures.

NB – The UK ETS is not included in this diagram. This measure needs to be considerably remodelled.

The Climate Change Levy, Climate Change Agreements and the Carbon Trust

Research findings

Participants were generally familiar with the Climate Change Levy (CCL) and Climate Change Agreements (CCAs). They were less familiar with the Carbon Trust. Annex C sets out further details of the findings of the research interviews relating to each of these measures.

The most effective part of the package was considered to be the CCAs. The 80 per cent reduction in the CCL in return for agreed emissions reductions was seen to drive action better than the CCL itself, and has helped to raise the issue of energy higher up the business agenda. It was felt that the CCAs created ownership of energy issues in those businesses which entered into them; allowed businesses the flexibility of policy responses (including the possibility of trading); and, at a practical level, facilitated dialogue between industry and government. The main criticism of the CCAs was that they were only applicable to high energy-users. Some suggested that the targets set were not as strict as they could have been, and would have happened anyway under a business-as-usual scenario. The lack of transparency in negotiations may have contributed to this. The administrative aspects were criticised as being overly complex and bureaucratic, including the fact that SMEs found it difficult to participate.

“ some questioned whether the levy should continue once emissions trading has commenced ”

For the sectors that fall outside the scope of the CCAs, for whom energy was generally not that significant a proportion of their costs, the CCL on its own was considered to be one of the least effective instruments. It was considered that, for these sectors, there was little incentive to reduce energy use given the inelasticity of energy demand and the low level of the levy. There was a wide consensus that this had been exacerbated by the falling cost of energy at the time of the CCL's introduction. There was also criticism that the CCL is based on energy, not carbon.

Some questioned whether the levy should continue once emissions trading has commenced. A number of sectors will be subject to both the CCL/CCA and the EU ETS package, and work is continuing to allow them to opt out of the first phase of the EU ETS, although they will not be able to opt out of the second phase from 2008. There is also a concern that energy users in general will face increased costs as energy prices increase, to reflect the cost of carbon, and they continue to pay the CCL. It is too early to say with any confidence what the impact of the EU ETS will be on final energy consumers.

Some interviewees argued that businesses would become more energy efficient if the price of carbon (and therefore energy) rises due to the EU ETS. However, because of the uncertainty about whether the price of carbon will send a strong enough signal to drive change, at least in Phase I of the scheme, there is a clear argument to keep the CCL in place.

A clear finding was the need to further incentivise the non-CCA sectors, particularly SMEs and the commercial sector, which were widely considered to be

insufficiently engaged in greenhouse gas reduction measures. Suggestions were made for further exemptions from the CCL for companies willing to commit to energy efficiency.

Of those interviewees that expressed an opinion on the Carbon Trust, the work of the Trust was supported as it helps businesses understand climate change policy, how to respond and raises awareness of the issues. However, there were some concerns that the uptake of its initiatives is not as broad as it could be, or that there is not a high level of awareness for its work. This may be due to the voluntary nature of working with the Trust. Those who have worked with it are generally positive, while those who have not have little to say about them.

Recommendations

On the basis of these findings, and because of the uncertainty over the EU ETS, we recommend keeping the CCL/CCA package intact whilst strengthening it and widening its reach, and continuing the work of the Carbon Trust. There is still a need for measures that encourage energy efficiency in all businesses, not just those directly involved in the EU ETS. The following recommendations offer specific suggestions for adjustments to the policies that could be undertaken during the Climate Change Programme Review.

Maintain the CCL as an energy tax, with the aim of promoting energy efficiency to all businesses. Increase the level of the CCL, whilst recycling the revenues, in order to stimulate action on energy efficiency in line with the UK's targets.

This way, the CCL would remain as a downstream measure to secure the involvement of businesses not in the EU ETS, and stimulate energy efficiency. As such, it will complement the EU ETS, which involves only certain sectors and focuses on carbon. Even if the EU ETS eventually gives rise to a higher price for carbon, there is still a need for a measure that is addressed directly at all businesses.

Given that the CCL is not effective at current levels, consideration should be given to increasing the level of the Levy, whilst recycling the revenues. It should be set at a level that stimulates energy efficiency measures in non-energy intensive sectors. The CCL should, at the very least, be indexed to inflation. Consideration could be given to increasing the rebate for energy-intensive sectors.

Maintain the Climate Change Agreements, but open the process of target-setting to public scrutiny.

The CCAs should be maintained for those sectors not covered by the EU ETS. In order to address concerns that CCAs are currently lacking transparency, we recommend that the next round of CCA negotiations, in 2007, are transparent and open to public scrutiny.

Incentivise CCL-payers to invest in energy efficiency, by offering temporary or partial reductions in the CCL, linked to participation in Carbon Trust schemes.

For sectors not covered by the EU ETS, particularly SMEs and the commercial buildings sector, there may be a case for offering reductions in the Climate Change Levy in return for agreed energy efficiency improvements. These could be temporary – such as a two-year 'payment holiday' from the Levy – or a percentage reduction. They would be overseen by the Carbon Trust. Care would be needed to ensure that

the system was administratively much simpler than the current arrangement for CCAs so that businesses, such as SMEs, would not be put off from participating.

Given the general support for the Carbon Trust, coupled with the need to increase awareness of it, the services it offers and to encourage the uptake of emission reduction activities, we recommend that the Carbon Trust should keep its important information provision role. However, this could be linked into other policy measures, such as the additional CCL tax breaks mentioned above, in order to incentivise businesses to take up the services on offer.

UK Emissions Trading Scheme

Research Findings

There was a fair degree of familiarity with the UK Emissions Trading Scheme (UK ETS), although it was not considered to be an effective policy instrument. Most thought that it had not resulted in emissions reductions beyond what would have been achieved without the scheme. Some commented on the high cost of delivering these reductions, given the £215 million funding provided for the scheme. They claimed that it was not a cost-effective instrument, given that reduction targets were weak.

Despite these criticisms, however, it was recognised that the scheme had helped to prepare businesses for trading, and to and establish the necessary infrastructure. The benefits of establishing London as a centre; the development of verifiers, auditors, and so on; and the business 'hands on' experience of trading were considered to outweigh the weaknesses of the scheme.

Most participants felt that the UK ETS may have served its purpose and that there was little point in continuing with the scheme into Phase II. Once the EU ETS sector companies leave, it was considered that the scheme would not have enough participants to enable trading to occur. Some interviewees, however, felt that it might be beneficial to extend the scope of UK trading to include other sectors, such as the commercial buildings sector, in order to prepare them for possible future expansions of the EU emissions trading system or to help them increase their energy efficiency.

" most participants felt that the UK ETS may have served its purpose and that there was little point in continuing with the scheme in its current form "

Recommendation

The UK Emissions Trading Scheme should not continue in its current form. Consideration should be given to developing it into an instrument that incentivises action in sectors not covered by the EU ETS, particularly the commercial buildings sector.

Discontinuing the UK ETS in its current form would simplify the policy package at a domestic level. The funding for a further phase should be set aside for other energy efficiency measures. The architecture, expertise and knowledge developed in the process of the UK ETS could be used to develop a trading scheme focussed on key sectors outside the scope of the EU ETS, such as the commercial buildings sector where energy use and emissions continue to grow.

The Renewables Obligation

Research findings

The Renewables Obligation (RO) was considered by the participants to be one of the most effective UK instruments. The reasons given for the success of the RO included the fact that it sets clear targets; is relatively long term in focus therefore providing investor confidence; and has been successful in stimulating investment in renewable energy. Many commented, however, that it benefits a narrow range of technologies, primarily onshore wind energy. It does not encourage the development of all renewable technology or stimulate development where there has been less progress to date, such as in photovoltaics. It was noted that there is a lack of policy instruments to encourage the development of technologies that are less able to compete commercially in the current electricity market. There is a need for other policies and measures to benefit these technologies.

Recommendations

The Renewables Obligation should be maintained.

As the Renewables Obligation has been effective and is an important lever for driving innovation, it should be maintained. This approach is compatible with the EU emissions trading scheme, as price alone will not necessarily drive innovation. It also helps promote security of supply by encouraging UK energy generation. The only criticisms highlighted relate to its relatively narrow focus in terms of the technologies that it encourages. There is a need to simplify procedures for accessing Renewables Obligation Certificates to help small-scale generators to participate.

The Climate Change Programme Review, and forthcoming review of the Renewables Obligation, should look at ways of encouraging renewables technologies that do not benefit from the Renewables Obligation.

It is clear that the Renewables Obligation only works, at present, for a narrow set of technologies. Therefore the Review should consider the measures needed to bring forward other renewable technologies, particularly small-scale technologies. This could include, for example, changes to planning policy and buildings regulations to facilitate micro-generation; reduced VAT for technologies such as solar power and micro-CHP; and changes to metering systems to encourage export of power from micro-generation.

Annex A – References

A full literature review and discussion is available from the Green Alliance and IEEP websites.

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Annex B: Strengths and weaknesses of the EU ETS identified by different groups of interviewees (nb interviews were conducted in August and September 2004, before publication of the UK's final NAP)

Table showing the strengths of the EU Emissions Trading Scheme identified by different groups of interviewees

Government	Independent groups/NGOs	Business	Experts/Policy watchers
An EU wide scheme with mandatory involvement in all member states:			
'Covers half of the EU's carbon with a firm cap – can't get better than that'; 'A big plus is that it is mandatory'	'Single scheme across Europe instead of piecemeal, approximately half of EU emissions covered, mandatory involvement of companies'	'Tradable across the EU therefore large market and should lead to reasonable amount of liquidity, transparency and certainty'	'Large market and mandatory'; 'Good that it is mandatory'; 'It is a robust model covering the whole of the EU'; 'The scope of coverage ie 25 member states, means in theory there should be a meaningful market'
Reducing carbon emissions:			
'Could be an extremely important policy tool and could well be successful'; 'Some step towards bringing the EU nearer to [its Kyoto] target (although will not necessarily mean we achieve it)'	'Rewards those making efforts to cut carbon'; 'Will help the UK meet its Kyoto commitment, but it has to be done properly'	'Ultimately should reduce the amount of carbon being emitted because of the financial penalties. Should encourage investment in cleaner technology'	'In theory should be the ideal instrument for reaching Kyoto targets'
A price for carbon:			
'Fairly simple process of getting a price on carbon. Better than a tax as the market sets the price'	'A price on carbon across sectors in a way that will cover the whole EU is a huge step forward'; 'Puts price on carbon' and should 'internalise externalities'	'Wider area of EU will be beneficial for the market, better price for carbon'	'Price to carbon – unlike the CCL'
Trading as a tool:			
'The Energy White Paper says trading most effective instrument so hoping that is will prove to be the least cost market solution'	'Market based' and 'Cost effective if done properly'	'In principle is an excellent scheme…Any market driven tradable scheme tends to be good'; 'Flexible – can decide whether to do energy efficiency themselves or trade'	'In principle, could achieve reductions in carbon at a significantly lower cost than many of the other policies'; 'It is relatively simple being a cap and trade system'; 'Flexible – next NAPs can be tougher'
Sectoral coverage:			
'Includes electricity generators'; 'Brings in major carbon emitters, e.g. generators and refineries, sends a significant signal in power-generation market for the first time'			'covers a large number of sources'; 'Comprehensive scheme as opposed to the UK scheme which excludes electricity generation'

Table showing the strengths of the EU Emissions Trading Scheme identified by different groups of interviewees (continued)

Government	Independent groups/NGOs	Business	Experts/Policy-watchers
Subsidiarity:		Political Message:	Simplicity:
'Member states have been allowed discretion to try to transpose the Directive so that is suits their own starting positions'		'Great potential, would be the largest trading market which is a very import clear global message and an important political step'; 'if we can get EU emissions trading to work it will be very difficult for those across the world who argue against trading to genuinely maintain opposition'	Simplicity: 'relatively simple [policy measure] being a cap and trade system', 'one of the best Directives in terms of simplicity and clarity'; 'Very well designed scheme'
A learning opportunity:		Level playing field:	Low pilot Phase targets:
'There is flexibility in terms of allocation setting methodologies, benchmarking etc…. therefore there will be a high diversity of systems which provides an opportunity to learn a lot in relation best practice'		'Consistent rules [EU wide] therefore should be level playing field'	'three year pilot Phase with light caps has kept the co-operation of business and was probably the way to take it forward' industry expert; 'Pragmatic compromise between the ideal and what was politically feasible'
Better understanding of member states:		Allocations:	
'Given the UK government a better view about where other member states stand in relation to climate issues. Have been able to see who is making an effort to meet obligations'		'From UK perspective, permit allocations have been based on historic emissions data'	
Enouraged wider action on climate issues:			
'It has jolted people to say implement a Climate Change programme, ie identify what it is expecting from other sectors'			

Table showing the weaknesses of the EU Emissions Trading Scheme identified by different groups of interviewees

Government	Independent groups/NGOs	Business	Experts/Policy watchers
Differences between member state implementation leading to distortions:			
'Conflicts between member states on competitiveness distortions of the NAPs – it could undermine the whole thing'; 'Discretion brings difficulties due to differences which may have materially different effects on competition. There is an issue in relation to new entry policies, big questions relating to overlaps, growth rate assumptions, allowances may be given to incumbents and on top of this they may be allowed more allocations. There are very different investment incentives across EU'; 'Competitiveness issues if MS have less stringent caps'	'Subsidiarity of NAPs'	'Issues re liquidity and tradability if not all [member states] are playing to the same rules'; 'Lot of politics being played between member states on how to implement the scheme. Suspicion that the UK has gone further, and others have gone for a business as usual approach'	'Variable application meaning variable burden meaning that there may well be financial flows from high burden to low burden countries'
Scarcity of allowances:			
'Not yet clear if there will be scarcity of supply of credits in the EU'; 'To be a credible ETS it needs credible caps: question over the robustness of caps set by other member states'	'Not material enough – although it is only Phase 1. Switch to gas won't happen in Phase 1'	'Disappointing as it is weakened because of a lack of stringent requirements'	'Whether the EU ETS will result in carbon savings will depend on how many permits are granted, and this is not yet clear. This is the Achilles heel'; 'The cap being set at MS level – early indications show that it will be weak'; 'If the Phase 1 cap is weak, the affected industries may not contribute as much as they could or should to a member state burden sharing target'
Assessment of National Allocation Plans:			
'The NAP approval system has been far too politicised, the Commission has not delivered a vigorous assessment based on Annex 3 which was so painstakingly negotiated'	'Commission wasn't able to moderate all NAPs at once – had to look at as they came in. Some member states may have waited for others to submit their plans before submitting their own. Commission not strong enough'		'The Commission gave an enormous amount of leeway for NAPs'; 'It is difficult if member states are acting unilaterally and NAPs are political documents'; 'The Commission has not shown itself to be able/willing to affect significant change to member state NAPs with different approaches'

Table showing the weaknesses of the EU Emissions Trading Scheme identified by different groups of interviewees (continued)

Government	Independent groups/NGOs	Business	Experts/Policy watchers
Scope of the scheme:			
'Interface with the way electricity is handled – misses a trick in terms of encouraging demand side energy efficiency improvements'; 'Would be better if the EU ETS allocations were more in line with Kyoto targets'; 'No non-carbon dioxide gases at the moment'	'Limited sectors – this needn't be a weakness as long as others are covered elsewhere. DTI view ETS as all that is needed – this would be a weakness'		'Doesn't engage energy users in the correct way because it is aimed at producers. Therefore it is not likely to affect consumption reducing its effect'; 'There is a possibility that the way the system is set up, ie based on grandfathering, may act as a disincentive to higher efficiency gas fired power stations with companies keeping coal fired stations running longer … as these can be managed to reduce emissions'
Price of carbon:			Harmonising implementation:
'Too easy for member states to buy credits rather than take action themselves, not good from a sustainable development point'	'Prices will probably be quite low so the impact will be less that it could be, especially in Phase 1 – as the caps have been set low across the EU'; 'Not clear what the price will be'		'Concerns about a lack of a single auditing standard'; 'There are some areas where decisions should be harmonised'; 'Too much subsidiarity built in, this was the price the Commission had to pay to bring all member states on board'
Bad precedent for Phase II:			
'Everyone will have problems negotiating Phase II with industry because of the discretion allowed has meant there has been a race to the bottom in the first phase. All this doesn't bode well for Kyoto compliance'			'Whether there is political will to ensure 2008/2012 programme is really consistent with targets'

Annex C: The CCL, CCAs and Carbon Trust: Selected comments from interviewees

Climate Change Levy (CCL)	Climate Change Agreements (CCAs)	Carbon Trust
Strengths:		
• Financial incentive to make changes by raising price of energy. • Awareness raising: Sends signal of government's intention just by announcing it and having it. • Puts energy on the agenda of businesses. • Mandatory. • Tax easier to administrate to a wider range of businesses. • Lever to get companies into the CCA. • Goes across business and the public sector.	• Effective in reducing emissions (up to the targets). • Awareness raising. • Set targets. • Negotiation process/dialogue brought attention to issue and made industry think about what was possible. • Required companies to monitor and report emissions systematically. • Financial incentive. • Offers business the option of CCA or paying levy.	• Good overall aims. • Helps to overcome barriers. • More action than before on trying to engage with industry and targeting business energy use. • Helping and therefore reducing cost to industry of meeting legislation and targets, rather than bringing about further emissions reductions. • Capacity building. • Free advice. • Financial resources. • Strong base of intelligence and research capacity. • Independence from government – arms length and credibility.
Weaknesses:		
• Taxing energy use not carbon. • Level of the levy is weak compared to the underlying price movements of energy. Has been frozen for three years so the incentive is lower than when it started. • Strong signal to energy intensive industry but energy demand is inelastic as it is such a small component of costs for non-energy intensive industries. Therefore less effect in non energy-intensive industries. • Blunt instrument. • Little evidence that it changes business use of energy, especially in the sectors it is targeting, as these tend to be non energy-intensive. • Lack of clarity over main aim of the measure. • Does not distinguish between the different sources of energy (apart from the exemption for biofuels).	• Overlap with UK ETS and relationship with EU ETS. • Targets not ambitious enough so easy to achieve and over-achieve. • Question over whether achieved reduction beyond BAU. • Complexity and level of bureaucracy. • Only certain sectors, including energy intensive sectors. • Suggested that verification procedures in place were not adequate. Question of comprehensiveness and validity of verification process, and transparency.	• Lack of public awareness of what the Trust is trying to do – need better promotion to a wider audience. • Is it effective in promoting energy efficiency? • Less effective in capturing SMEs. • Scope for more coordination with the Energy Saving Trust. • Insufficient resources (even after Spending Review).

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