

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

Second Delegated Legislation Committee

DRAFT GREENHOUSE GAS EMISSIONS TRADING  
SCHEME (AMENDMENT) ORDER 2022

*Monday 31 January 2022*

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**The Committee consisted of the following Members:**

*Chair:* MRS MARIA MILLER

- |   |   |
|---|---|
| † Baillie, Siobhan ( <i>Stroud</i> ) (Con)                                    | Osamor, Kate ( <i>Edmonton</i> ) (Lab/Co-op)                              |
| Brown, Alan ( <i>Kilmarnock and Loudoun</i> ) (SNP)                           | † Stevenson, Jane ( <i>Wolverhampton North East</i> ) (Con)               |
| † Butler, Rob ( <i>Aylesbury</i> ) (Con)                                      | Sturdy, Julian ( <i>York Outer</i> ) (Con)                                |
| † Champion, Sarah ( <i>Rotherham</i> ) (Lab)                                  | † Vara, Shailesh ( <i>North West Cambridgeshire</i> ) (Con)               |
| † Davies, Geraint ( <i>Swansea West</i> ) (Lab/Co-op)                         | † Whitehead, Dr Alan ( <i>Southampton, Test</i> ) (Lab)                   |
| † Hands, Greg ( <i>Minister for Energy, Clean Growth and Climate Change</i> ) | † Whittaker, Craig ( <i>Lord Commissioner of Her Majesty's Treasury</i> ) |
| † Jenkinson, Mark ( <i>Workington</i> ) (Con)                                 | † Wood, Mike ( <i>Dudley South</i> ) (Con)                                |
| Keeley, Barbara ( <i>Worsley and Eccles South</i> ) (Lab)                     | Seb Newman, <i>Committee Clerk</i>  |
| † Morden, Jessica ( <i>Newport East</i> ) (Lab)                               |   |
| Morrissey, Joy ( <i>Beaconsfield</i> ) (Con)                                  | † <b>attended the Committee</b>   |

## Second Delegated Legislation Committee

Monday 31 January 2022

[MRS MARIA MILLER *in the Chair*]

### Draft Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2022

6 pm

**The Chair:** Before we begin, I remind everybody that we are still under socially distanced rules, and please to wear masks if you are not speaking, as ordered by Mr Speaker and the Commission. I call the Minister to move the motion.

#### The Minister for Energy, Clean Growth and Climate Change (Greg Hands): I beg to move,

That the Committee has considered the draft Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2022.

The draft order was laid before the House on 6 January.

The UK emissions trading scheme—the UK ETS—was established under the Climate Change Act 2008 by the Greenhouse Gas Emissions Trading Scheme Order 2020 as a UK-wide greenhouse gas emissions trading scheme to encourage cost-effective emissions reductions that will contribute to the UK's emissions reduction targets and net zero goal. The scheme replaced the UK's participation in the EU emissions trading system—the 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.

The 2020 order was subsequently amended by the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2020 to include provisions for the free allocation of emissions allowances and to create the UK ETS registry. Regulations under the Finance Act 2020 established the rules for auctioning allowances and mechanisms to support market stability. The UK ETS launched on 1 January 2021, and the first auction successfully completed on 19 May. The scheme has been running well since its launch, but there is a need to continue to improve its operation.

Further amendments have been made by the Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2021, which is subject to the negative procedure and comes into force on 7 February 2022. In broad terms, the 2021 order makes various technical and operational amendments to the UK ETS across a number of scheme aspects, including providing for installations in the hospital and small emitter opt-out scheme to be able to increase their emissions targets, and for installations in both opt-out schemes that return to the main scheme to benefit from free allocation.

The purpose of this order is to amend the 2020 order to address several residual operational issues identified during the development and legislation of the scheme, and to support the scheme's technical operation. This legislation also addresses an issue of doubtful vires relating to previous amendments, raised by the Joint

Committee on Statutory Instruments. This proposed order consists of various operational issues identified by the Department for Business, Energy and Industrial Strategy, the devolved Administrations and the national scheme regulators during the establishment of the scheme that were required to be legislated for via an affirmative procedure.

This order does three things: introduces a civil penalty to enforce an existing obligation to return overallocated allowances; creates an offence of intentionally obstructing the scheme regulators that are exercising enforcement powers; and makes it clear that some enforcement powers previously introduced by the negative procedure are valid.

In conclusion, this order will help to improve the effective operation of the UK ETS. This in turn will help to ensure that the scheme plays its part in reducing emissions. I therefore commend the order to the Committee.

6.4 pm

**Dr Alan Whitehead** (Southampton, Test) (Lab): It is a pleasure to serve under your chairmanship, Mrs Miller, albeit I have a slight apology to make for turning up at the very last moment. I ought perhaps to advise the Committee that the recently refurbished lift that takes hon. Members from the ground floor opposite the Strangers' Bar does not stop at the first floor, which necessitated a rather circuitous route to get here. I apologise for being right on time, or marginally later, and I hope that the House of Commons authorities may have a look at whether the lift ought to stop at the first floor, which would be a good idea for good order in this House.

This statutory instrument is essentially uncontroversial, although the operation of the UK ETS is perhaps a little more controversial. The reason we are here this afternoon is because the SI seeks to put right an amendment order of 2020, which was put through under the negative procedure. However, the Joint Committee on Statutory Instruments decided that it should have gone through the affirmative procedure, which is why we are debating this SI.

The changes in this SI, as opposed to those in the 2021 amendment order, are minimal to the point of being nothing. What we have in front of us is an amendment to the 2020 order, clarifying and adding various things in the way the Minister has described on aviation, on unused allowances and on definitions of how certain procedures of the order would work. One could argue that those perhaps might have been put in the 2020 order in the first place, but I am pleased that they are with us now.

I do not have any particular concerns or objections about those particular things in the order itself but, since we do not get many, or any, opportunities to examine the operation of the UK ETS, it is worth considering briefly what is happening to the scheme and whether it might have been a good idea to place some further amendments to the scheme before the House, both in terms of what has happened in the EU as far as the UK ETS is concerned and what has happened during the early stages of the scheme's operation.

I therefore have two brief questions for the Minister about the operation of the UK ETS. Although my hon. Friend the Member for Rotherham kindly sent me a

note of what she intends to talk about, I will not—in the best traditions of theatre critics not to give away the plot of the play—tell the Committee exactly what she will say. However, I want to reflect on two things that are important to the operation of the UK ETS.

First, the intention of the UK ETS, at least for the first few years of operation, is that it should pretty closely shadow the EU ETS. As we know, that has not been the case. UK ETS prices have come in considerably higher than those of the EU ETS over that period. The intention behind the 2020 order, as set out in its impact assessment, has not been realised. It might have been wise to put in place linking mechanisms with the EU ETS much earlier—the Government have said they would consider doing so at some future date but have not done anything about it, as far as I know—bearing in mind that the EU ETS and the UK ETS have diverged in price in a way that was not originally envisaged.

My first question to the Minister is this. Does he intend to look at linking mechanisms with the EU ETS at an early stage to prevent future divergence, which may otherwise be increasingly wide? Among other things, businesses and commerce in this country want to be able to anticipate what will happen with carbon pricing. We do not disagree with the principle of carbon pricing, but businesses need some stability in their forward understanding of it.

Since the 2020 order, from which this amendment order derives, the EU has adopted in principle a proposal for a new carbon border adjustment mechanism. That mechanism would deal with the consequences of carbon leakage—that is, where the EU's carbon taxes and carbon trading arrangements mean that third countries have a considerable trade advantage, because they can import goods without such arrangements attached and bring them within the EU's borders. As far as I know, the UK has not yet taken any action on considering or implementing a carbon border adjustment mechanism. If the EU proceeds with such a mechanism, as seems likely, the UK will be in an even worse position than it is now when it comes to carbon leakage. We will be external to a carbon adjustment mechanism, so we will have punitive elements against us. At the same time, people will be able to import goods into the UK, safe in the knowledge that they are not subject to the same sorts of arrangements.

The Minister knows that various members of the Government—he is not one of them—have indicated that the UK should take the idea of a carbon border adjustment mechanism very seriously. My second question to him is this. Has he considered adding a carbon border adjustment mechanism to the 2020 order that brought about the UK scheme, as a successor to the EU ETS? If he has considered it, what action is his Department taking to forward the idea of a UK carbon border adjustment mechanism?

I hope that I have not stolen my hon. Friend's thunder and that between us we will get some clarification at least from the Minister about how these things will work as the UK ETS proceeds. As a great supporter of carbon trading, I would say that a UK carbon trading mechanism—the UK ETS—should have been the obvious thing to introduce after the UK's exit from the EU. I fully support that. What I am concerned about is ensuring that the UK ETS works as well as possible, to the net

benefit of the UK and UK industry, rather than causing problems for it, as it sometimes looks like it might. I am sure the Minister will give me a full and frank run-down of the Government's intentions in these areas. I look forward to hearing from him, but first I am very happy to hear from my hon. Friend the Member for Rotherham, who I think will develop this theme a little further in relation to particular businesses in her constituency.

6.16 pm

**Sarah Champion** (Rotherham) (Lab): It is always a pleasure to serve under your chairship, Mrs Miller. I thank my hon. Friend the Member for Southampton, Test for encapsulating the issues we are facing.

It is extremely fortunate for me that I am on the Committee considering this piece of secondary legislation, because it is so pertinent to one of the oldest businesses in my constituency—one that I am extremely nervous may be thrown into considerable, if not terminal, economic problems because of the situation with the emissions trading scheme, among other things.

The rationale behind the UK emissions trading scheme and its predecessor, the EU ETS, was to encourage investment in decarbonising by charging industrial emitters of CO<sub>2</sub> for the pollution they were causing. The system placed a legal requirement on polluters to purchase CO<sub>2</sub> or carbon allowances from the state and surrender them to match the quantum of emissions emitted by an industrial installation on an annual basis, with strict penalties for non-compliance or failure to surrender allowances. It was designed to reduce the availability of CO<sub>2</sub> allowances over time, thereby pushing CO<sub>2</sub> allowance prices up, as decarbonisation technology developed and became an investable alternative to paying for emission allowances.

It was recognised that the scheme could have a negative effect on competitiveness and lead to production being moved to countries where costs were lower and operators did not face carbon emissions controls—what is called carbon leakage. To protect against this, businesses deemed at risk of carbon leakage received a percentage of free allowances to assist in minimising the risk. The logic behind the system appears sound, but sadly, as happens in so many cases, the reality does not match the theory.

Beatson Clark in my constituency is a small UK-owned glass manufacturer that has operated from the same site in my constituency since 1751. It employs 351 direct employees, as well as supporting many local businesses throughout its supply chain. It produces glass containers for the food, drinks and pharmaceutical markets, and is the only remaining producer of amber pharmaceutical glass in the UK. Beatson Clark has led the way in reducing its CO<sub>2</sub> emissions by increasing the levels of recycled materials in the glass it produces. It has invested millions of pounds in its own recycling plant in order to secure recycled materials for its glass furnaces. It is the only UK glass manufacturer that actually owns and operates its own recycling plant. Basically, Beatson Clark is a green, recycling business that the UK should be proud of; but, due to both commercial and physical factors, it is unable to reduce emissions further.

Glass can be melted using electrical energy, but the infrastructure to deliver sufficient energy to the site is not in place, and the costs associated with it would be prohibitive. It would also take years to implement. The

[Sarah Champion]

switch from melting using natural gas to using electricity would add between £4 million and £5 million in costs—costs that were calculated before the current energy price spike. These additional costs would increase to around £30 million in electricity energy against gas at the peak of the current crisis. It would simply not be commercially viable to switch, even if the infrastructure were in place.

The UK market is now being offered glass at prices below the UK production costs. Increasingly, these imports are coming from the middle east and Turkey. Beatson Clark asked British Gas to conduct an assessment of the production costs and CO<sub>2</sub> impact associated with glass produced in Turkey. It established that shipping glass produced there to the UK—and no doubt bringing it from ferries to the actual sites on lorries—resulted in a 36% increase in CO<sub>2</sub> emissions. However, the cost of manufacturing in Turkey was around 39% lower. As a result of both lower energy costs, and the fact that there is no carbon allowance burden, such glass is made considerably cheaper than anything that can be produced in the UK.

In the last year, the UK ETS allowance prices, like the energy prices, have increased beyond what could have been anticipated by industry. When the first auction of UK allowances took place in May 2021, the reserve was set at £22 per tonne. The actual sale price was £43.99 per tonne. Prices have continued to rise over the year to around £80 per tonne. The equivalent EU CO<sub>2</sub> allowance price has also risen, but on average the cost of a UK allowance is around £4 a tonne more expensive.

**The Chair:** May I encourage the hon. Member to talk about operational improvements in respect of the UK ETS? I am sure she was about to come on to that.

**Sarah Champion:** Thank you, Mrs Miller; I will do so. I know what a good Chair you are, so I know that I am pushing my luck.

As a result, Beatson Clark, like many other essential UK businesses, has seen its carbon compliance costs triple. It cannot reduce its emissions further without significant investment in energy infrastructure. Even if the infrastructure were in place, the cost of alternative energy would be prohibitive. It is therefore in a Catch-22; it wishes to further decarbonise, but there is no commercially viable method of doing so. It feels that it is trapped, leaving the purchase of allowances simply as a tax on business. It also has concerns that some of the increase in the CO<sub>2</sub> allowance is being driven by speculators.

The Government have made over £4.5 billion from the sale of carbon allowances since May 2021. While the Treasury is enjoying the windfall as a result of higher carbon prices, UK obligated companies and institutions are suffering. Businesses need stability. They cannot realistically plan for all the unforeseeable circumstances, such as the massive increases in energy and carbon costs that we have seen over the past six months. The current system and policies are failing companies that want to do the right thing, and I fear that we may see businesses closing as a consequence.

The impact assessment published alongside the design of the UK ETS in June 2020 did not envisage the present situation. Can I therefore ask the Minister, at the very least, to recommission the impact assessment to

bring it line with the current reality? More broadly, will the Minister commit to a total review of energy, energy policies, energy taxation and environmental policies? This would ensure that the Government are focused on levelling up costs across Europe, protecting against carbon leakage from beyond Europe and allowing sustainable CO<sub>2</sub> reduction while maintaining affordable production in the UK.

Finally, I say to the Minister: Beatson Clark is an absolutely fantastic example of how a business can support a local community and local suppliers. I know that it would really welcome a visit if the Minister is passing.

**The Chair:** Before I bring in the next Member, I would like to remind everybody that Delegated Legislation Committees are tightly focused on the measure in front of us. We really do need to focus on the issue in question: the operational improvements of the UK ETS.

6.24 pm

**Geraint Davies** (Swansea West) (Lab/Co-op): It is a great joy to serve under your chairmanship, Mrs Miller. I would like to make a couple of quick points on the operational improvements of the trading scheme.

First, I support the points made by my hon. Friends the Members for Southampton, Test and for Rotherham about the carbon border adjustment mechanism or tax, which could be in these changes. The steel produced in Wales, for example, has half the carbon of Chinese steel coming in. Over time, we want to be in a situation where we support jobs rather than export them to China and elsewhere, where dirtier production occurs. China produces some 30% of overall carbon emissions and uses half the world's coal-fired power stations—we are talking about 1,037, with another 300 on the way. Perhaps the Minister could comment on that.

Secondly, will the Minister comment on why Drax is not included in the emissions trading scheme? Drax burns 7 million tonnes of wood pellets. That wood is grown in America. It is argued that the wood that is cut down is replaced. Even if it is, that in itself is a neutral operation, but then it is burned here, and it is not counted in our carbon emissions. That is amazing, given that it is the biggest emitter of PM10 in Europe. We basically spend £800 million subsidising it, which is £114 a tonne. In burning wood and coal, we burn a carbon store, but in burning wood, we also destroy a way of absorbing CO<sub>2</sub> and producing oxygen.

Thirdly, on airlines and aircraft, I am aware that British Airways is buying up Welsh farms in order to get the carbon offset to fly more planes. Some of those farms are sheep farms, so we will end up flying in Australian sheep and lamb, having basically allowed BA to use this scheme to create more carbon emissions through their planes.

Finally, will the Minister comment on the Government's plan to double incineration by 2030? What impact will that have, and how will it be factored into the scheme, if at all?

6.27 pm

**Greg Hands:** I thank all Members for participating in this debate. The hon. Member for Southampton, Test mentioned the trouble with the lift opposite the Strangers'

Bar. It can sometimes be confusing, taking a lift directly outside a bar. I have to say that I took one of the two lifts there and came up without any difficulty. To be fair, he may well have taken the other lift, and it may well also not stop at the first floor. I am sure that the House authorities will want to have a look at it. Perhaps they might also find an explanation for the SNP's failure to attend the Committee, which may also have its origin in that interesting feature of the House as it has been reconstructed.

The hon. Gentleman said that the draft order was not controversial, and I agree. He described the evolution of the affirmative SI that we are considering today, and he is correct that it is generated out of the 2020 order. One set of changes is subject to the negative procedure, and one set is subject to the affirmative procedure—particularly those changes that create new offences, which is what is before us today.

The hon. Gentleman asked two questions about the UK ETS system in general. Its intention, as he sees it, is to shadow the EU ETS. I do not think that is the right way to describe it. Its original features were based on the EU's ETS scheme. He is right that our prices have been higher, but I would not say drastically so; as the hon. Member for Rotherham pointed out, they have been around 5% higher. We never said that the prices—or, indeed, the eligible elements within the scheme—would necessarily track, but the hon. Member for Southampton, Test is right that there is a common origin.

In terms of linking mechanisms, we are open to dialogue with the European Union in consideration of linking to the EU scheme. That follows our commitments in the trade and co-operation agreement. The two sides updated each other at the trade specialised committee on 12 October.

The hon. Gentleman also asked about the EU carbon border adjustment mechanisms. As he will know, that is an EU proposal that has not yet been legislated for. In my previous ministerial role at the Department for International Trade, the UK was well aware of that proposal, and we continue to watch it very closely. The two things that I would say in relation to it are that it needs to be World Trade Organisation compliant, and that we must make sure it does not discriminate against genuine developing countries. I know that the hon. Member for Rotherham, in her role as Chair of the International Development Committee, will take a strong interest in that point as well.

It is always good to hear about the practical impact that Government decisions and policies can have on successful small and medium-sized enterprises such as Beatson Clark in the constituency of the hon. Member for Rotherham, which has been there since 1751—a remarkable achievement in its own right. We want to make sure that, having been around for 271 years, that company might have a future for the next 271 years, so I will pass on the information about it to the Minister for Industry, my hon. Friend the Member for North East Derbyshire (Lee Rowley), who is more directly involved with the glass sector.

To respond to the points that the hon. Lady raised, we are in daily contact with energy-intensive industry stakeholders regarding ongoing concerns over energy markets. Ministers and officials continue to engage with industry to further understand the impacts of high

global gas prices. Our priority is to ensure that costs are managed and supplies of energy are maintained. We are committed to minimising energy costs for businesses, which is vital. In 2020, relief to energy-intensive industries for electricity policy costs alone was worth over £470 million.

**Sarah Champion:** In debates like this I am normally arguing for steel, which I also have in my constituency. I know that Liberty Steel was a beneficiary of those grants, but I do not think that glass is getting the same support as steel. If the Minister could look into that issue, I would be extremely grateful.

**Greg Hands:** I will certainly look into that in conjunction with the Minister for Industry; I will make sure that he is aware of the issue that the hon. Lady raises. As she rightly pointed out in her speech, allowances were allocated freely in 2021. The 2022 free allocation amounted to 42 million allowances, as it did the year before, and will be issued by 28 February 2022, in advance of the 2021 compliance deadline of 30 April 2022. There is good continuity of approach there.

By putting a price on carbon emissions, the UK ETS incentivises market participants to find the most cost-effective solutions to decarbonising. We understand, of course, that there is a risk of carbon leakage, which we mentioned just a moment ago in relation to the EU's approach. The UK ETS authority, which is the four Governments in the United Kingdom together, will consult in the coming months on the trajectory of the scheme's cap, particularly to keep it aligned to our net zero obligation. As part of that consultation, we intend to review our free allocation in the UK ETS, for which we will start a call for evidence in the spring. Energy prices, policy and taxes are all things that we keep under constant review—particularly taxes—so I can assure the hon. Lady that we already have a total review.

Turning to the points made by the hon. Member for Swansea West, in terms of Drax, it is important to recognise that policies are not specific to any particular company. Currently, installations that use only biomass are out of the scope of the ETS, but I can take away the points that he made and follow up on them. He mentioned British Airways flying in Australian sheep; I think he might have meant sheepmeat or lamb meat, rather than the sheep themselves. Having negotiated the Australian trade deal, I am pretty sure that the movement of sheep themselves would not be within scope.

**Geraint Davies:** Just for clarity, the point I was trying to make was simply that British Airways is buying up sheep farms in order to offset the aircraft it uses to send people on holiday or whatever, and—separately from that—that obviously gives rise to less sheep production in Wales. We have an open-door deal with Australia to allow exports of sheep, so we end up displacing consumption of Welsh sheep with consumption of Australian sheep and burning more carbon, which does not seem to be very good, either economically or environmentally.

**Greg Hands:** The hon. Gentleman is tempting me down the path of debating the Australia free trade agreement—

**The Chair:** Which the Minister will not follow.

**Greg Hands:** Which I will not go down. The two of us have been here before—I know that he is a member of the International Trade Committee—but I will not engage with him on the topic of British Airways and Welsh farms.

I thank hon. Members for their valuable contributions to today's debate. This order will help improve the effective operation of the UK ETS and, in doing so, will help support delivery of our climate ambitions. I therefore commend it to the Committee.

*Question put and agreed to.*

*Resolved,*

That the Committee has considered the draft Greenhouse Gas Emissions Trading Scheme (Amendment) Order 2022.

6.35 pm

*Committee rose.*