



HM Revenue  
& Customs



HM Treasury

# Carbon Emissions Tax

## Consultation

Publication date: 21 July 2020

Closing date for comments: 29 September 2020

<b>Subject of this consultation:</b>	The detailed operation of the Carbon Emissions Tax.
<b>Scope of this consultation:</b>	<p>In line with the withdrawal agreement, the UK will remain in the European Union Emissions Trading System (EU ETS) until 31 December 2020. As set out in the UK's Approach to Negotiations, published on 27 February 2020, the UK would be open to considering a link between any future UK ETS and the EU ETS. If a link cannot be agreed, the UK will implement either an unlinked UK ETS or the Carbon Emissions Tax from 1 January 2021.</p> <p>Under the Carbon Emissions Tax, installations currently in the EU ETS whose emissions exceed their annual tax emission allowance would become liable to pay the tax on their emissions from 1 January 2021. This consultation sets out details on how Her Majesty's Revenue &amp; Customs (HMRC) propose to operate the tax if it were introduced, and seeks comments on the proposals to inform secondary legislation. We are also consulting on some proposals for how the tax might develop. If there were an interest in developing any of these proposals, we would consult further on the details. We are not consulting on the basic structure of the tax (including who pays) which was set out in Finance Act 2019 (as amended).</p>
<b>Who should read this:</b>	This consultation is open to any individual or organisation. Those most likely to be affected by it are: permit holders for installations that would have to pay Carbon Emissions Tax (see chapter 2); accountants/ advisers of permit holders; and verifiers of emissions reports. Sectors that would not be covered by the tax at introduction will be interested in the consideration in chapter 3 of making other sectors liable to Carbon Emissions Tax in the future, should the tax be introduced.
<b>Duration:</b>	10 weeks. The deadline for responses is 29 September 2020.
<b>Lead official:</b>	Michael Lyttle, Excise & Environmental Taxes Policy Design, HMRC.
<b>How to respond or enquire about this consultation:</b>	Responses/enquiries should be e-mailed to: Michael Lyttle at the following address: <a href="mailto:carbon.taxation@hmrc.gov.uk">carbon.taxation@hmrc.gov.uk</a>
<b>Additional ways to be involved:</b>	During the consultation period, HMRC and HM Treasury are planning to set up discussions with operators and industry associations to explain the proposals, listen to views and answer questions. If you would like to be involved in these discussions, or if you have any other queries, please email <a href="mailto:Razia.Sultana@hmrc.gov.uk">Razia.Sultana@hmrc.gov.uk</a>
<b>After the consultation:</b>	Responses will help HMRC to refine the design of the tax and produce the necessary secondary legislation. HMRC will publish a response to this consultation during 2020 and, if the tax were to be introduced, some secondary legislation would be laid before Parliament by the end of 2020 with more in 2021 or 2022.

**Getting to this stage:**

The government announced at Budget 2018 that the Carbon Emissions Tax would be introduced in the event of a no deal EU exit and legislated for the tax in Finance Act 2019. The tax remains an alternative to linked emissions trading systems between the UK and EU, and its design has been updated since that Act became law. This consultation is designed to inform the secondary legislation covering the operation of the tax.

**Previous engagement:**

HM Treasury and HMRC carried out some informal engagement with stakeholders in advance of announcing the tax at Budget 2018. Along with the Department for Business, Energy and Industrial Strategy these departments also held a webinar in October 2019 which was available to operators of all UK installations.

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# 1. Introduction

## Context

- 1.1. Tackling climate change is one of the defining challenges of our time, and the UK is proud of its record as an international leader in that fight. In 2019, the UK affirmed its leadership role and became the first major economy in the world to legislate to end its contribution to global warming by 2050.
- 1.2. Reaching net zero by 2050 will require the UK to go much further than the progress made between 1990 and 2018, when the UK reduced its emissions by 43% while growing our economy by more than two thirds. An essential driver of this progress has been the UK's deployment of carbon pricing. In the power sector alone, carbon pricing has reduced the share of coal-based power generation from 40% in 2012 to 2.1% in 2019. Taken together, decarbonisation in the power sector has accounted for almost 78% of the reduction in the UK's carbon emissions between 2012-2018. This is why the UK remains committed to carbon pricing as a key policy in decarbonising its economy, as reaffirmed in the government's policy paper *The Future Relationship with the EU: The UK's Approach to Negotiations*. In this publication, the UK has confirmed it would be open to considering a link between any future UK Emissions Trading System (ETS) and the EU ETS (as Switzerland has done with its ETS), if it suited both sides' interests. This position is unchanged. If it was not possible to agree with the EU the terms of a linked emissions trading system, the UK would implement either an unlinked UK ETS or the Carbon Emissions Tax to set the carbon price from 1 January 2021, in order to help meet our legally binding carbon reduction targets.
- 1.3. Irrespective of whether the UK implements an emissions trading system or the Carbon Emissions Tax, the government wants to ensure that we meet our environmental obligations in a way that works best for the economy. Decarbonisation and economic growth are not mutually exclusive – they must go hand in hand. This consultation sets out the government's proposal for how the Carbon Emissions Tax would balance the UK's environmental, economic and fiscal priorities.

## Policy landscape

- 1.4. Under the terms of the Withdrawal Agreement, the UK will remain a participant in the EU ETS until the end of the Transition Period, and UK participants must fulfil their obligations to surrender allowances by 30 April 2021.
- 1.5. The outline of a UK ETS, which could either be standalone or linked to the EU ETS, is available in the 2019 consultation *The Future of UK Carbon Pricing* published by the Department for Business, Energy & Industrial Strategy and the Devolved Governments of the UK, with the detailed design confirmed in the government response published on 1 June 2020 and legislation laid before Parliament this month. Further legislation to provide the powers to establish a UK ETS that could be linked to

the EU ETS was included in Finance Bill 2020<sup>1</sup> alongside updates to the Carbon Emissions Tax legislation in Finance Act 2019. The updated Finance Act 2019 legislation covering the tax is set out at Annex A.

- 1.6. The government remains committed to maintaining the Single Electricity Market on the island of Ireland and understands the importance of carbon pricing to this market. It will aim to ensure that carbon pricing does not hinder the effective operation of the market after the Transition Period. Emissions from electricity generation in Northern Ireland that, under the terms of the Northern Ireland Protocol, remain within the EU ETS from 1 January 2021 would not be taxed.

## This consultation

- 1.7. The Carbon Emissions Tax was established in Finance Act 2019, which provides for most of the operational detail for the tax to be set out in secondary legislation. To ensure continuity for businesses in switching from the EU ETS to a Carbon Emissions Tax, the tax would align with existing processes for monitoring, reporting and verification of emissions. By building the tax on top of existing structures, we are seeking to minimise changes and limit the costs of introducing the tax for business.
- 1.8. As part of this approach, the emissions reporting periods already established under the EU ETS would continue to run on a calendar year basis under the tax. If the tax were to be introduced, permit holders for UK installations that exceeded their annual tax emission allowance would become liable to tax on the excess emissions from 1 January 2021. The tax could also be extended to include emissions from other sectors in the future (see chapter 3). Tax bills would be issued annually each August (starting in August 2022) covering emissions from the previous calendar year.
- 1.9. Chapter 2 of this consultation sets out proposals for how the tax would operate, focusing on ensuring that the operational processes HMRC would put in place would be as effective as possible. It invites comments from stakeholders and interested parties to that effect. Chapter 3 includes some proposals on how the tax might develop following implementation if it were to be introduced, and the government is interested in as wide a range of views on these proposals as possible.
- 1.10. HMRC and HM Treasury look forward to discussing the proposals in this consultation paper with stakeholders and interested parties.

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<sup>1</sup> At publication of this consultation, the Bill had passed all its parliamentary stages but had not received Royal Assent

## 2. Proposed operation of the Carbon Emissions Tax from 1 January 2021

### Introduction

- 2.1. This chapter sets out our plan for how we would operate the Carbon Emissions Tax.
- 2.2. Part A of the chapter largely deals with aspects of the tax that for the most part have already been legislated – such as the scope and reporting periods. Part B deals with parts that have yet to be legislated. We would therefore be particularly interested in views on the practicality of the proposals in Part B, as well as any omissions, concerns or other suggestions about the operation of the tax.
- 2.3. A glossary of terms used in this chapter (and/or in the glossary itself) is set out at Annex B.

### Part A – Legislated aspects of the Carbon Emissions Tax

#### Permit holders and liability to pay the tax

- 2.4. The European Union Emissions Trading System (EU ETS) requires installation operators (referred to in this chapter as operators) to obtain permits from the relevant regulator<sup>2</sup> to carry out regulated activities in installations which result in emissions of greenhouse gases. Operators are required to monitor their emissions and submit a verified annual report of these emissions to their regulator.
- 2.5. Under Phase III of the EU ETS running from 2013 to the end of 2020, installations are either:
  - subject to the full requirements of the EU ETS and require a greenhouse gas emissions permit. These are referred to in this consultation paper as “**main scheme installations**”, or
  - in the Small Emitter and Hospital Opt-out Scheme, requiring an excluded installation emissions permit. They are sometimes known as Article 27 or excluded installations – in this consultation paper we refer to them as “**small emitters**”.
- 2.6. Both types of permit holder would become a taxable person under a Carbon Emissions Tax. A Northern Ireland electricity generator whose electricity emissions continued to be reported under the EU ETS after 1 January 2021 would not become liable to pay the tax on those emissions.
- 2.7. The system of permitting will continue from 2021 and holders of permits issued for EU ETS compliance before 2021 would become liable to the Carbon Emissions Tax from

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<sup>2</sup> See glossary at Annex B



January 2021 if they emitted above the tax emission allowance set for their installation. Minor amendments will be made to permits by regulators to reflect the end of participation in the EU ETS (and additional changes to the permit conditions for those eligible for free allocations). If the tax were introduced changes would also be made to highlight the permit holder's liability to Carbon Emissions Tax.

- 2.8. For Phase IV of the EU ETS running from 1 January 2021, a new category of regulated installation has been created: ultra-small emitters. Installations that qualify as an ultra-small emitter from 1 January 2021 will be exempt from the main requirements of the EU ETS. Such installations would not be liable for the Carbon Emissions Tax for the period they qualify for the ultra-small emitter scheme, because they would not hold the relevant permits as outlined above. However, they will be required to monitor their emissions to confirm that they remain below the relevant emissions thresholds.
- 2.9. For both main scheme installations and small emitters, the permit holder at 31 March each year would be liable to pay the Carbon Emissions Tax on their emissions above their tax emission allowance for the previous calendar year. For example, the permit holder at 31 March 2022 would be liable to pay tax on emissions made from 1 January to 31 December 2021. This would be the case even if there were to be a change of permit holder during this period or between the end of this period and 31 March 2022. Those taking over a permit may therefore need to consider that they would assume liability for tax on emissions made before the permit was transferred to them.
- 2.10. The process of surrendering a permit would not affect the liability to pay the tax. If there was a surrender or revocation of a permit, the permit holder at the latest date for which the permit was valid for would be liable for the tax and billed accordingly.

## Registering for the tax and submitting tax returns

- 2.11. In order to avoid introducing new burdens and obligations, there would be no requirement for permit holders to register with HMRC for this tax or to submit a tax return. Information needed to establish a register of taxpayers, calculate tax liability and bill the permit holder would be undertaken by HMRC using relevant data that operators submit to their regulators.

## Emissions reporting periods under the tax

- 2.12. The UK will continue to operate a monitoring, reporting and verification regime from 2021. This will be updated to reflect changes to the system under Phase IV of the EU ETS on the departure of the UK from the EU and the transition to setting a carbon price using the tax (if the government opted for a tax).
- 2.13. All operators covered by the permits outlined in paragraph 2.5 must monitor their emissions and report these annually. Operators that would have received a free allocation of EU allowances under the EU ETS must also submit annual activity level reports at a sub-installation level (see section "*Activity level reports*" below). Further

details of the monitoring, reporting and verification regime can be found at <https://www.gov.uk/guidance/eu-ets-monitoring-and-reporting>

- 2.14. The emissions reporting periods under the tax would be aligned with the monitoring period which runs from 1 January to 31 December each year.
- 2.15. Operators will submit verified data to the regulator covering their emissions in the previous year. They will do this by 31 March each year and this will establish their emissions on a carbon dioxide equivalent basis. Small emitters can continue to choose self-verification or third-party verification.
- 2.16. For 2021 emissions, all operators will be required to submit verified emissions reports by 31 March 2022 covering the period of 1 January to 31 December 2021. These reports will fulfil emissions reporting obligations and would also be used for tax purposes. In summer 2022, regulators would send data needed for tax purposes to HMRC who would calculate tax liability for 2021 emissions and issue tax bills (see section “*Issuing tax bills*” below). This process would continue annually for as long as the tax remained in place.

## Determining the level of emissions

- 2.17. Each year, HMRC would use relevant data from an installation’s annual emissions report for the purposes of calculating the tax liability, specifically how many tonnes of carbon dioxide equivalent were emitted by the installation in the period covered by the report. Using data that regulators already hold on installations (for example, names and addresses and details about their level of emissions) would make submitting tax returns by installations unnecessary, minimising administrative burdens for business.
- 2.18. Where the annual emissions report is absent or erroneous, regulators currently make a ‘determination of emissions’ to determine the correct level of emissions for the installation and that information is notified to the operator and held on the regulator’s IT system. If the tax were introduced, the determination process would continue where appropriate and the determination would in these circumstances be used by HMRC for the purposes of calculating the tax liability.
- 2.19. Whenever necessary, regulators would provide updates to HMRC of changes to emissions or tax emission allowances that would affect tax liability of permit holders under their jurisdiction. Where there was an amended tax liability, HMRC would issue amended bills to affected permit holders and would, where appropriate, refund any overpaid tax.

## Activity level reporting from 2021

- 2.20. Operators of main scheme installations will be subject to revised reporting arrangements from 2021<sup>3</sup>, with a new obligation for operators that are eligible and

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<sup>3</sup> [https://ec.europa.eu/clima/news/adoption-regulation-adjustments-free-allocation-emission-allowances-due-activity-level-changes\\_en](https://ec.europa.eu/clima/news/adoption-regulation-adjustments-free-allocation-emission-allowances-due-activity-level-changes_en)

wish to apply for a tax emission allowance to submit to their regulator an annual activity level report by 31 March each year, broken down to a sub-installation level. The report will contain information on their activities in the previous year. The first annual activity level report, due in March 2021, must contain information relating to 2019 and 2020 activity levels. In following years, just one year's worth of data would be required (for example, the March 2022 report would contain activity level data covering 2021).

- 2.21. These activity level reports would be used to assess whether main scheme permit holders that had a tax emission allowance above zero needed to have that allowance adjusted (see next section "*Tax emission allowances*").

## Part B – Aspects of Carbon Emissions Tax yet to be legislated

### Tax emission allowances

#### i. Introduction

- 2.22. If the government opted to introduce the tax from 2021, a tax emission allowance would be set for each installation covered by the tax i.e. all main scheme installations and small emitters. The methodology to determine the level of the tax emission allowance would be largely the same as that for calculating the level of free allocation of allowances under a UK ETS. The tax emission allowance would be calculated at a sub-installation level and each sub-installation's allowance would be aggregated to produce an overall tax emission allowance for the installation as a whole. Secondary legislation would be laid later this year confirming this methodology.
- 2.23. This section sets out how these allowances would be set, adjusted where appropriate, and notified to operators for the first two years of the tax. The government would review the tax in 2022, focusing on the mechanism for determining tax emission allowances for 2023 onwards. This might include greater alignment of the processes for main scheme installations and small emitters.

#### ii. Purpose

- 2.24. The tax emission allowance would be the number of tonnes of carbon dioxide equivalent that an installation would be able to emit without being taxed – so emissions above the allowance would be liable to the tax. Each tax emission allowance would be specific to a reporting year and to an installation. An installation would not be able to transfer any part of its allowance to any other installation – even another installation owned by the same business.
- 2.25. For at least the first two years of the tax the government would intend to set the tax emission allowance to equate broadly to the allocation of free allowances or targets that would have applied in the EU ETS. The methodology for setting the tax emission allowance is outlined in the section "*Setting the tax emission allowance*" below.

### iii. Setting, adjusting and confirming levels

2.26. The process by which the tax emission allowance would be set, adjusted where appropriate and confirmed, including the timeline, is summarised in the following table. More detail is set out below the table.

<b>Date</b>	<b>Main scheme installations</b>	<b>Small emitters</b>
Late 2020/early 2021	<b>Informed of benchmarks as soon as data received from European Commission. Indicative tax emission allowances for 2021 and 2022</b> calculated using these benchmarks and historical data and then notified to installations.	<b>Informed of indicative tax emission allowances for 2021 and 2022</b> once calculated using historical emissions data.
By 31 March 2021	Submit activity level report covering 2019 and 2020	May apply to regulator for a change to their tax emission allowance, supplying evidence to justify one. If the regulator agreed, relevant tax emission allowance would be amended. Either way <b>the tax emission allowance for 2021 would be confirmed at this point.</b>
From April through to summer 2021	Activity level reports reviewed by regulator and, if adjustment criteria were met (see below this table), tax emission allowances for 2021 and 2022 would be amended. Either way, <b>the 2021 tax emission allowance would be confirmed at this point.</b>	
By autumn 2021	<b>Confirmed tax emission allowance for 2021 published by the government.</b> For main scheme installations, this would be the indicative figure as updated by any decisions on activities etc. arising from spring 2021 activity level reports; and, for small emitters, it would incorporate any decisions by regulators arising from applications to change their tax emission allowance.	
By 31 March 2022	Report 2021 emissions and activity levels to regulator.	Report 2021 emissions to regulator.
From April through to summer 2022	Activity level reports reviewed by regulator and, if adjustment criteria were met, tax emission allowance for 2022 would be amended. Either way <b>the tax emission allowance for 2022 would be confirmed at this point.</b>	At any point, they may apply to regulator for change to their tax emission allowance with evidence to justify one. If the regulator agreed, relevant tax emission allowance would be amended and confirmed. Either way <b>the tax emission allowance for 2022 would be confirmed at this point.</b>
July 2022	Data on 2021 emissions and confirmed tax emission allowances for 2021 transferred from regulators to HMRC.	
August 2022	<b>Receive statement of liability from HMRC on 2021 emissions</b> - either a bill for 2021 emissions using confirmed tax emission	<b>Receive statement of liability from HMRC on 2021 emissions</b> using confirmed tax emission allowance for 2021.

	allowance for 2021; or details of amount of unused tax emission allowances relating to 2021.	
By autumn 2022	<b>Confirmed tax emission allowance for 2022 published by the government.</b> For main scheme installations, this would be the indicative figure as updated by any decisions on activities etc. arising from spring 2022 activity level reports; and, for small emitters, it would incorporate any decisions by regulators arising from applications to change their tax emission allowance as well as adding any unused tax emission allowances from the 2021 tax year.	

### *Setting the tax emission allowance*

- 2.27. Those installations that would not have been eligible for free allowances under Phase IV of the EU ETS (including most electricity generators) would be set a tax emission allowance of zero, and would therefore pay tax on all their emissions.
- 2.28. For each main scheme installation eligible for free allowances under Phase IV, an indicative tax emission allowance for 2021 and 2022 would be calculated using the data from the 2019 National Implementation Measures (NIMs) exercise, which produces an Historical Activity Level (HAL), along with the EU ETS Phase IV benchmarks and Carbon Leakage Exposure Factor (CLEF). This would be done at a sub-installation level and then all sub-installations' totals would be aggregated to arrive at the overall tax emission allowance for the installation as a whole. The methodology that would be used would be broadly in line with that used to allocate free allowances under a UK ETS, with minor changes such as not applying a Cross-Sectoral Correction Factor. The tax emission allowance would be based on the following calculation:

$$\text{Tax emission allowance} = \text{historical activity level} \times \text{benchmark} \times \text{CLEF}$$

Which CLEF applies to each sub-installation would be determined using the Phase IV Carbon Leakage List. This is why the tax emission allowance would be calculated at a sub-installation level and then aggregated to arrive at the overall tax emission allowance.

- 2.29. Small emitters would have their tax emission allowance for both 2021 and 2022 set in line with the methodology for setting their 'emissions targets' under the EU ETS. This methodology is the installation's average reported emissions over a baseline period (2016, 2017 and 2018) multiplied by an annual reduction factor. The figures could only change in the following circumstances:
- for both the 2021 and 2022 allowances, where the small emitter applied to its regulator for an increase to its tax emission allowance due to a capacity increase at one or more of its sub-installations, and this application was agreed; or

- for the 2022 allowance, as a result of increasing it by the amount of any unused tax emission allowance from 2021 (see section “*Small emitters’ unused tax emission allowances*” below).

2.30. Main scheme installations would be Informed of the benchmarks as soon as they become available (expected later in 2020). All installations receiving a tax emission allowance would be notified of the levels for 2021 and 2022 once these had been calculated (using these benchmarks where appropriate).

### *Adjusting the tax emission allowance*

2.31. Indicative tax emission allowances for 2021 and 2022 would be reviewed for each main scheme installation by regulators upon receipt of the annual activity level reports submitted by 31 March each year, mirroring the approach to Activity Level Changes for Phase IV of the EU ETS. Each year, the regulator would calculate the annual average activity level over the two previous calendar years and compare that average with the HAL.

2.32. The activity level reports submitted by 31 March 2021 would cover two years (2019 and 2020) and that submitted by 31 March 2022 would cover 1 year (2021). An installation’s tax emission allowance would be an aggregate of all its sub-installations’ tax emission allowances and similarly the activity changes are considered at a sub-installation level. If there was a permanent cessation of a sub-installation, then the tax emission allowance for that sub-installation would be set to zero in the year following cessation and this would be reflected in the overall tax emission allowance for the installation.

2.33. To qualify for an adjustment, average annual activity levels on a two-year rolling basis at a sub-installation would need to increase or decrease compared with the sub-installation’s HAL. If the activity level reports covering 2020 and 2021 showed an average increase or decrease of more than 15% compared with its HAL, the sub-installation’s tax emission allowances for both 2021 and 2022 would be adjusted by the same percentage increase or decrease to reflect these activity changes<sup>4</sup>. If the 15% threshold applied at a sub-installation level was not met, this sub-installation’s tax emission allowance would remain unchanged. All sub-installations’ revised or unchanged tax emission allowances would then be aggregated to derive an overall figure for the installation.

2.34. In 2022 the tax emission allowance for 2022 would again be reviewed and adjusted if necessary – the details are set out in the following table (which also summarises whether, and if so how, the 2021 allowance would be changed).

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<sup>4</sup> If the percentage was met for a sub-installation but the result was a change of under 100 tax emission allowances, no update would be made to the sub-installation’s tax emission allowance.

Date	Regulator action	Sub-installation activity level changes	Sub-installation tax emission allowance 2021	Sub-installation tax emission allowance 2022
After 31 March 2021	Work out average activity levels for 2019 and 2020 (from activity levels reports)	If average met threshold for change (+/- 15% or more than HAL)	Adjust indicative tax emission allowance by same percentage and confirm tax emission allowance	Indicative tax emission allowance would be revised by same percentage
		If average did not meet threshold for change	Indicative tax emission allowance would become confirmed tax emission allowance	No change would be made to indicative tax emission allowance
After 31 March 2022	Work out average activity levels for 2020 and 2021 (from activity levels reports)	If average continued to meet threshold (+/- 15% or more than HAL)	n/a	Tax emission allowance would be confirmed at level agreed following activity report submitted in spring 2021 (see blue box above)
		If average was a further +/-5% or more over the previous average		Original tax emission allowance would be adjusted by this percentage
		If average did not meet threshold for change		Indicative tax emission allowance would become confirmed tax emission allowance

2.35. In line with the EU ETS approach with targets, at any time small emitters would be able to apply to the regulator for an increase to their tax emission allowance but there would be no reduction made for reductions in capacity. If the application was in line with the rules, the regulator would adjust the tax emission allowance. They would also make adjustments to take account of unused tax emission allowances from the previous tax year (see section “*Unused tax emission allowances*” below).

#### *Confirming the tax emission allowance*

2.36. Following the review of activity levels and any applications made by small emitters, by autumn each year regulators would aggregate all sub-installations’ confirmed tax emission allowances to arrive at an overall figure for the installation.



2.37. Once the process of reviewing tax emission allowances for all installations was complete, the regulator would refer the tax emission allowances to the Department for Business, Energy and Industrial Strategy (BEIS) for approval.

**Q: Do you have any views on the methodology and process for setting tax emission allowances and adjusting them in light of activity level reports?**

iv. Publishing confirmed levels

2.38. The government would publish a table of confirmed tax emission allowances for all permit holders covered by the tax at installation level annually in the autumn, starting in autumn 2021. So, the confirmed figure for 2021 would be published in autumn 2021 and the confirmed figure for 2022 would be published in autumn 2022.

v. New entrants

2.39. Those main scheme installations that became permitted after 30 June 2019 would not have the necessary data to enable a tax emission allowance to be set for 2021 or 2022. Such permit holders would be able to apply to their regulator for a tax emission allowance, but would only be able to do so in the year following the start of operation. However, they would become eligible for tax from the date their permit came into force (or from 1 January 2021 if that date was between 30 June and 31 December 2020).

2.40. This would mean that, for at least the first year, all the installation's emissions could be taxed as there would be no corresponding tax emission allowance. Therefore, to avoid unnecessary hardship caused by this, HMRC may agree to defer billing new entrants for up to 9 months to allow a tax emission allowance to be set, or it may agree to issue a bill using a temporary tax emission allowance agreed by the regulator.

2.41. For new entrants, the activity level in the first (partial) year of operation would be used to set the tax emission allowance for this year using the following calculation:

$$\textit{Tax emission allowance} = \textit{activity level} \times \textit{benchmark} \times \textit{CLEF}$$

This would not be subject to any adjustment. The activity level for the second year of operation would be used to set the historical activity level (and would also not be subject to adjustment) and the tax emission allowance would be set for this year using the following calculation:

$$\textit{Tax emission allowance} = \textit{historical activity level} \times \textit{benchmark} \times \textit{CLEF}$$

2.42. A regulator's decision for setting a tax emission allowance for a new entrant would be referred to BEIS for approval. Once approved, the regulator would notify the installation of its confirmed tax emission allowance.



vi. Billing where the tax emission allowance was not confirmed or later changed

- 2.43. It is possible that, in a very small number of cases, established installations would not have their tax emission allowance confirmed by the time HMRC was ready to issue bills. In these circumstances, HMRC would issue the bill using the latest available tax emission allowance and would, if necessary, issue a revised bill if that figure was later amended.
- 2.44. As indicated in the section “*New entrants*” above, HMRC could defer issuing a bill to new entrants for up to 9 months to allow time for their first year’s tax emission allowance to be set.

vii. Small emitters’ unused tax emission allowances

- 2.45. The government proposes that it would maintain the benefit available to small emitters under the EU ETS where unused targets in one year can be used against liabilities in the following year. So, tax emission allowances for small emitters for 2022 would be increased by the amount of any unused tax emission allowance in 2021. What happened beyond that would form part of the 2022 review of the tax mentioned above.
- 2.46. To reward main scheme permit holders who emitted below their tax emission allowance, the government has set out proposals on which it is seeking views through this consultation (see section “*Payments to reward decarbonisation*” below).

**Q. Do you agree that small emitters should have their tax emission allowance for 2022 increased by the amount of their unused tax emission allowances from 2021? Do you think that, instead, a payment scheme as outlined below for main scheme installations would be an appropriate means of incentivising decarbonisation for small emitters?**

## Payments to reward decarbonisation for main scheme installations

i. Purpose

- 2.47. Under the EU ETS, some installations are allocated a portion of emission allowances for free. Where their actual emissions are lower than the amount of free allocations they receive – for example, because they have taken steps to reduce their carbon intensity – they end up with surplus allowances. These surplus allowances can be sold or banked for future use. This gives installations a financial incentive to decarbonise their processes.
- 2.48. Under the Carbon Emissions Tax, installations would receive the same level of free allowances (the tax emission allowance) as they would have received under Phase IV of the EU ETS. However, as currently designed, installations would not be able to benefit financially if their actual emissions fell below the tax emission allowance (they would pay no tax, but since there would be no surplus allowances, they would have nothing to sell on). Following representations from industry, we are concerned that this

would not give installations a financial incentive to decarbonise processes beyond the tax emission allowance.

- 2.49. In order to continue to ensure a financial incentive to decarbonise beyond the level of the tax emission allowance and drive innovation through the tax system, the government considers that, if the tax were introduced and subject to satisfying subsidy control rules, a payments system should be introduced alongside it. It would reward those main scheme installations that reduced their emissions beneath their tax emission allowance where that was a result of genuine steps to decarbonise, as opposed to a reduction in activity.
- 2.50. The rest of this section sets out a proposal for how the payments system could work for the first two years of the tax. The government would consider implications of the 2022 review of the tax on the payment system before deciding how any scheme would work beyond that.

## ii. Eligibility criteria

- 2.51. An installation would have to fulfil each of the following criteria to be eligible for a payment. It would have to:
- be a main scheme installation;
  - have a tax emission allowance above zero;
  - have a total emissions figure (i.e. the aggregate emissions across all of its sub-installations) of less than its tax emission allowance; and
  - demonstrate the extent to which the emissions reductions were achieved through decarbonisation.

Installations that did so would receive a payment for emissions attributable to decarbonisation capped at the level of the unused tax emission allowance.

- 2.52. Main scheme installations that decarbonised but continued to emit more than their tax emission allowance or had a tax emission allowance of zero would not be eligible for a payment. This is because they would be benefiting financially from their investments, via a reduced tax bill. Small emitters would also not be eligible for a payment but their unused tax emission allowance from one year would be used to increase their tax emission allowance in the following year, so reducing their tax bill in that year. Any small emitter that would like access to the payment system would be able to apply for a permit under the main scheme.
- 2.53. Where there was a change of permit holder during a tax year or between the end of a tax year and when a claim was submitted, the person eligible to make the claim would be the permit holder at the time the claim was made rather than the original permit holder.

### iii. Measuring decarbonisation of activities

- 2.54. Installations would need to submit additional data to support their claims of decarbonisation, in order to enable regulators to assess whether their emissions reductions had been achieved through decarbonisation. The additional data would need to set out the emissions attributable to each sub-installation. The government proposes that the submission of this additional data should be done on a voluntary basis to avoid imposing excessive regulatory burdens across all eligible installations. This would ensure that only businesses that believed they were eligible for a payment would need to submit additional data. Installations could submit the additional data as part of their annual activity level report or could wait until they had confirmation that the installation as a whole had emitted below its tax emission allowance.
- 2.55. To ensure that taxpayers' money was spent rewarding the right activities, the payment system would reward only those installations that could demonstrate that their emission reductions were achieved through decarbonisation, such that their level of emissions of carbon dioxide (or carbon dioxide equivalent) per unit of output had reduced. If eligibility to payment was based simply on how much an installation had emitted beneath its tax emission allowance, installations could be incentivised to reduce activity in order to become eligible for, or maximise, their potential payment.
- 2.56. The additional data would enable regulators to calculate a sub-installation's emissions per unit of activity. This figure would differ according to whether a sub-installation produced a benchmarked or non-benchmarked product:
- For benchmarked products (see glossary at Annex B), regulators would calculate the tonnes of carbon dioxide (or equivalent) per tonne of product.
  - For other products, regulators would calculate the tonnes of carbon dioxide (or equivalent) per terajoule of heat/fuel.
- 2.57. These figures would subsequently be assessed against the data from the NIMs baseline period (2014-18) to calculate the percentage reduction in tonnes of carbon dioxide equivalent per unit of product for the relevant sub-installation. This percentage would then be multiplied by the total emissions of the sub-installation, to calculate the total abated emissions that were attributable to decarbonisation for that sub-installation.
- 2.58. Regulators would repeat these calculations across all sub-installations and add up all of the abated emissions that were attributable to decarbonisation.

**Q: Do you agree that, if the Carbon Emissions Tax were to be introduced, a mechanism should be introduced to reward decarbonisation?**

**Q: Do you agree that there should be no obligation on operators that did not wish to make a claim to submit this additional data? How easily could your installation provide this additional data? How much additional work would it take to calculate (please set out the employee hours and expected costs of doing this)?**

**Q: Do you agree that the methodology outlined above would accurately demonstrate the extent to which an installation's emissions reductions were achieved through decarbonisation?**

iv. Verification of data

2.59. The government considers that the additional data provided by installations should be verified appropriately. It recognises that, while operators that produce benchmarked products have transparent and harmonised rules for how they must quantify their production, and for the types of data sources used for this purpose, this is not the case for operators that produce non-benchmarked products. Therefore, guidance would be issued to ensure that consistent and appropriate units of measurement were used across all installations that produce non-benchmarked products.

v. Payment rate

2.60. Subject to stakeholder views on the inclusion of the payment policy under the tax, the payment rate would be set as a percentage of the overall tax rate. For example, the payment rate for 2021 could be set at 50% of the confirmed 2021 tax rate.

vi. Timing of claims/payments

2.61. The government would not start making payments under the proposed scheme until 2023. Operators would be able to submit claims to the regulator for 2021 and 2022 at the same time (for example, in March 2023 when the activity level report for 2022 became due). However, claims for 2021 and 2022 would have to contain separately identifiable data for each year – regulators would not accept an aggregated claim covering two years.

2.62. The government proposes a deadline for installations to submit the data for 2021 and 2022 of 31 March 2024.

**Q: Do you agree with the government's proposal to enable installations to submit data with activity level reports and to allow a final deadline of 31 March 2024 for claims relating to the 2021 and 2022 tax years?**

### Data sent to HMRC by regulators

2.63. As indicated above, to avoid introducing new burdens and obligations on permit holders, there would be no requirement for permit holders to register with HMRC for the tax or to submit a tax return. Instead, HMRC would use data that operators submit to their regulators. Data would be limited to that needed to collect and assure the tax and HMRC would, of course, be bound by data protections laws in relation to this data.

2.64. For each taxable installation, regulators would be required to provide the following information to HMRC:

- Details of the installation and of the permit holder at 31 March each year (for example, for the 2021 tax year this would be 31 March 2022) - including name, address, type of permit (main scheme or small installation), permit number
- The permit holder's Companies' House registration number and VAT registration number
- The date that the installation became permitted and/or ceased to become permitted (where relevant)
- Contact details of those who would liaise with HMRC over payment of tax or any queries about the installation's tax affairs
- Verified emissions over the relevant period (e.g. 1 January to 31 December 2021 for the first reporting period) on a carbon dioxide equivalent basis from the installation's annual emissions report or, any determination of emissions made by the regulator e.g. where an annual emissions report was not submitted, was incorrect or was submitted late
- The installation's confirmed tax emission allowance for the year being billed. The regulator would also be required to provide details of any subsequent changes to the allowance, for example arising from corrections to activity levels or where errors were identified.

## Rate in 2021 and 2022

2.65. The government is committed to maintaining an ambitious carbon price to help meet the UK's carbon reduction obligations. To maintain continuity in the carbon price paid by UK businesses, indicative rates for 2021 and 2022 (which would be announced at Autumn Budget 2020 and Budget 2021 respectively) would be based on:

- the average December 2021 and 2022 EU ETS allowance futures prices (for the rate in 2021 and 2022 respectively), PLUS
- an uplift to that average ETS allowance futures price, which would be determined before the indicative rate was set, to allow for the potential for actual ETS prices to overshoot the average futures price.

2.66. When confirming rates for 2021 and 2022 in early 2022 and 2023 respectively (before tax bills were issued), the government would adjust the indicative rates for 2021 and 2022 downward (to the ETS prices) if they turned out to be higher than the average EU ETS auction clearing prices in these years by £1 or more. This would give businesses certainty about their maximum liability under the tax, and would ensure that UK industry would not face a higher carbon price than EU competitors.

**Q: Do you agree that the Carbon Emissions Tax rate should be set using EU ETS price data?**

**Q: What are your views on the proposal to adjust the rate?**

## Determining the tax liability

- 2.67. Installations whose emissions exceeded their tax emission allowance would be charged on each tonne of carbon dioxide equivalent in excess of the allowance. Total emissions are rounded to the nearest whole tonne in the annual emissions report and HMRC would use this rounded figure to calculate tax liability.
- 2.68. HMRC would use the following calculation to establish how much tax was due:
- Total emissions - tax emission allowance = taxable emissions
  - Taxable emissions x £xx (the confirmed tax rate) = Carbon Emissions Tax due
- 2.69. An installation that did not exceed its annual tax emission allowance would pay no tax.

## Issuing tax bills

- 2.70. In August each year, starting in 2022, HMRC would send a Carbon Emissions Tax bill to each installation that emitted in excess of its tax emission allowance over the emissions reporting period. To calculate bills, it would use the information sent to it by regulators (listed in “*Data sent to HMRC by regulators*” above).
- 2.71. An installation that was potentially liable to tax but had a nil liability by virtue of emitting less than its tax emission allowance would be sent a statement confirming it had a nil tax liability for the relevant reporting period and setting out how much tax emission allocation was unused. Small emitters would be able to increase their tax emission allowance for the following year by the unused amount, to be offset against the tax liability.
- 2.72. Where operators, verifiers or regulators identified errors in the emissions reported after HMRC had sent out the tax bill, HMRC would be sent details of any changes by regulators to enable it to recalculate the tax liability for the relevant period using the new data. This could result in a request for payment of additional tax liability, a refund of overpaid tax, or an adjustment to the tax emission allowance for small emitters arising from unused tax emission allowances from the previous year. If the decarbonisation payment scheme outlined above were introduced, any changes to reported emissions could also affect eligibility to payments under that scheme.
- 2.73. If a tax bill was issued and subsequently information came to light which meant the bill was incorrect (e.g. as a result of late notification of an error in an activity level change, incorrect emissions data or regulator determinations based on incorrect data), the regulator would be required to notify any changes to HMRC who would then issue a revised bill.



## Paying the tax to HMRC

- 2.74. The deadline for paying the tax would be 30 days from the date the tax bill was issued (the date stated on the bill). If full payment was not received by HMRC within that period, interest would be due and HMRC would consider charging a late payment penalty (see section “*Ensuring compliance with the tax*” below).
- 2.75. Administration and payments of the tax would not initially be available via HMRC online accounts but HMRC would allow the following methods of payment:
- direct debit
  - corporate credit or debit card
  - bank transfers

Refunds from HMRC to taxpayers would be made by BACS or CHAPS.

- 2.76. Operators would need to provide HMRC with bank details to help facilitate payments and refunds of tax.
- 2.77. Installations would not be allowed to use EU Allowances under the EU ETS (whether free, bought at auction or traded) to pay the tax. Any unused EU Allowances or any Kyoto Protocol International credits held at the time of the introduction of the tax would not be valid for tax purposes.

**Q: For the longer term, do you think other payment methods should be made available (e.g. a transfer involving the Business Tax Account)?**

## Ensuring compliance with the tax

- 2.78. HMRC would be responsible for enforcement and compliance with tax matters and regulators would be responsible for enforcement and compliance with emissions and activity level monitoring and reporting.
- 2.79. The government would seek to minimise non-compliance, avoidance or evasion and provide a fair and level playing field for compliant operators. It would use available information about operators to identify risks as they arose and would take appropriate action in response to non-compliance.
- 2.80. Permit holders will continue to be liable for civil penalties for breaching permit obligations and in relation to the failure to report activity level changes. If the tax were introduced, these compliance penalties would be reviewed by the government to ensure they worked alongside HMRC’s collection of the tax e.g. whether any penalties needed to be increased to ensure that there was no incentive for non-compliance with the rules as a means of reducing the amount of tax due or evading tax completely.
- 2.81. HMRC’s involvement in the processes needed under the tax would start after the operator had submitted their annual emissions and activity level reports to the regulator and a summary of those reports was passed to HMRC. Non-compliance with the processes prior to that would generally be covered by existing penalties which

would be retained, where appropriate. The regulators will have new penalties available to them to cover failure to report activity changes.

- 2.82. New HMRC penalties would be introduced that could be applied to any permit holder that did not pay all the tax due by the due date or did not comply with record-keeping requirements under the tax. The new tax would follow the approach of most other indirect taxes for late payment. The penalty for a permit holder that did not pay all the tax due by the due date would be 5% of the tax payable, rising to 10% if the amount was not paid within 5 months of the due date, and 15% if the amount was not paid within 11 months of the due date. HMRC would consider reducing the penalty if there were special circumstances, and the penalty would not be payable at all where there was a reasonable excuse for the late payment. The penalty would be appealable to the First-tier Tribunal.
- 2.83. In addition to the non-payment penalty, interest would be payable on unpaid amounts at the Bank of England official bank rate plus 2.5%. Interest would be payable regardless of the reason for the late payment and it would not be appealable to the Tribunal, although if the underlying liability was varied on appeal, any late payment interest would be recalculated.
- 2.84. In view of the existing sanctions available to regulators, HMRC is not proposing that it would introduce any other specific tax penalties.

## Reviews and appeals

- 2.85. Those affected by the tax (including permit holders and their representatives) would be able to challenge any decision or action taken by HMRC in collecting the tax. They would have the right to request a review and then appeal to the First Tier Tax Tribunal, including on the following matters:
  - whether HMRC had charged the correct person for the tax
  - whether the amount of tax in the bill had been calculated correctly
  - taxpayer claims for refunds of tax
  - taxpayer liability to, or the amount of, any HMRC imposed penalty
  - any assessment for an amount that HMRC refunded to a taxpayer in error
- 2.86. HMRC would expect the permit holder to pay the tax bill as a condition of considering any appeal (in line with the standard HMRC appeal process).
- 2.87. The regulators already have review and appeal structures to deal with challenges to their decisions and these would remain, updated as necessary to reflect departure from the EU ETS and the setting up of the tax.
- 2.88. Provision would be made relating to decisions on the setting of the tax emission allowance and decarbonisation payment provisions.



## Record-keeping requirements

2.89. Most of the information that HMRC would require to collect the tax would be taken from the emissions report that operators submit to their regulator by March each year, and activity level reports in the case of main scheme permit holders. Details of these reports and information relating to the tax emission allowance would need to be retained by operators to compare against their tax bill. Operators would need to preserve these tax related records and associated business records, for example evidence of payments, for 10 years in accordance with record retention requirements for the Greenhouse Gas Emissions Trading Scheme Regulations 2012.

## Conclusion

**Q: Do you have any views on the practicality of the proposals in Part B of chapter 2 that you cannot cover in responses to other questions?**

**Q: Are there any omissions or do you have any concerns or other suggestions about the operation of the tax?**

# 3. Possible future changes to the tax

## Introduction

- 3.1. If the Carbon Emissions Tax were to be implemented, it would become a key pillar of the UK's efforts to combat climate change. As it stands, the tax would apply to almost one-third of UK emissions. But to deliver on our net zero commitment by 2050, the Carbon Emissions Tax would need to evolve.
- 3.2. In addition to the operational design of the tax (outlined in chapter 2 of this document), this consultation is seeking views on how the tax may be adapted and its scope widened to ensure that it continued to be as effective as possible in supporting decarbonisation. The government also wants to explore whether other ideas, such as allowing tax offsets under the tax, could reinforce wider initiatives to support emerging decarbonisation technologies.

## Broadening the scope of the tax: capturing additional emissions

- 3.3. Recognising that there may be other sectors where a carbon price could prove an effective lever to support the transition to less carbon-intensive operations, the government would like to take this opportunity to invite views and evidence from stakeholders about whether other sectors of the economy, for example the shipping and aviation sectors, should be covered by the tax in the years after 2021.
- 3.4. Aviation emissions are already subject to a carbon price - albeit with significant free allowances – as they are within an aviation EU ETS (which also means monitoring and reporting systems are already in place). Shipping emissions are not currently subject to a carbon price but applying one to domestic shipping might help incentivise a shift to lower carbon fuels. However, shipping and aviation may not be the only sectors where a carbon price might be effective, subject to the creation or adaptation of appropriate monitoring, reporting and verification regimes.
- 3.5. Any extension of the tax would need to be done in a way that provided affected sectors with sufficient notice. There would be consultation in advance of commencement on how it would apply, including confirmation of the start date and how the tax emission allowance would be set.

**Q: Do you have any views on how, in the years after 2021, a Carbon Emissions Tax could drive decarbonisation in sectors beyond those that would be subject to the tax at introduction?**

## Incentivising negative emissions in the longer term

- 3.6. The Committee on Climate Change has been clear that the only way for the UK to meet its net zero target by 2050 is for negative emissions technologies, such as direct air capture or bioenergy with carbon capture and storage, to be deployed at scale. These 'negative emissions' are needed to offset continued emissions from

sectors, like aviation, that are not expected to be able to decarbonise completely by 2050. The government is interested in whether the tax could play a role in supporting the emergence of new negative emissions technologies and industries and wants stakeholders to come forward with views of how the Carbon Emissions Tax, or other policies, could be enhanced over the medium term to support this.

3.7. Views are particularly welcome on:

- the most effective areas to target any incentives
- how verification challenges can be overcome, so that government has confidence that emissions have been captured and stored permanently before any relief was granted
- the level of support that would make a serious impact on investment decisions by businesses, and
- what, if any, other complementary policies the government should consider.

3.8. Evidence and views submitted in response to this consultation will help inform a more detailed call for evidence on negative emissions technologies and carbon pricing later this year.

**Q: Do you agree that the government should explore the case for tax incentives to support negative emissions technologies?**

**Q: In designing any tax incentive, what issues should the government consider regarding negative emissions technologies?**

## 4. Assessment of impacts

- 4.1. An impact assessment was published at Budget 2018 and has now been updated to reflect further work on the detail of how the tax would operate. The assessment will be further updated to reflect the outcome of this consultation if the government opts to introduce the tax.
- 4.2. The assessment has been written on the assumption that the tax will be introduced but does not include the proposal relating to a decarbonisation payment scheme or any of the potential changes covered in chapter 3.

### Table of impacts

<b>Exchequer impact (£m)</b>	2019 -20	2020 -21	2021 -22	2022 -23	2023 - 2024
	The final costing will be subject to scrutiny by the Office for Budget Responsibility and will be set out at a future fiscal event.				
<b>Economic impact</b>	This measure is expected to have a negligible economic impact.				
<b>Impact on individuals, households and families</b>	<p>This measure will replace the EU ETS and is expected to have a similar impact on household bills to the measure it is replacing. It is not expected to have any other impacts on individuals as Carbon Emissions Tax will be a business tax.</p> <p>The measure is not expected to have an impact on family formation, stability or breakdown.</p>				
<b>Equalities impacts</b>	This measure is not expected to have any impacts for groups sharing protected characteristics.				
<b>Impact on businesses and Civil Society Organisations</b>	<p>This measure is expected to impact an estimated 1,000 UK stationary installations that participate in the EU ETS comprising electricity generators, offshore installations and manufacturing plants, mostly operated by large businesses, but also including between 100-200 smaller emitters and hospitals.</p> <p>The tax will be charged on the annual tonnage of greenhouse gases emitted by the installation during a reporting period of 12 months, over and above a tax emission allowance. The means of establishing an annual tonnage figure of greenhouse gases emitted is already well established and businesses should already be familiar with it. The process for setting the tax emission allowance will be new. For the</p>				

	<p>first reporting period running from 1 January to 31 December 2021, the tax emission allowance will be based on already established free allocation and target setting methodologies used in the EU ETS.</p> <p>For the annual tonnage figure, installations should already be aware of how to report their activities under a monitoring, verification and reporting scheme that has been needed for both EU ETS purposes and to establish the extent to which the UK is meeting its internationally agreed emissions reduction commitments. From these activities an annual tonnage figure of greenhouse gases emitted at each installation is derived. The mechanism for reporting emissions continues unchanged now we are no longer in the EU. Tax will be due on each tonne of greenhouse gases on a carbon dioxide equivalent basis that exceeds the installation's tax emission allowance. HMRC will send out a tax bill once a year and revise these bills to reflect any changes in emissions or tax emission allowances as appropriate.</p> <p>There will be no need for businesses to register for the tax because HMRC will take information about all taxable installations from an IT system operated by regulators. Most existing penalties for failures to monitor, verify and report will continue as they currently do. There will be new penalties introduced under the tax for any failure to pay the tax due on time and for failure to keep relevant records.</p> <p>All installation permit holders will be required to report their activities and emissions annually by 31 March. In advance of the start of the tax on 1 January 2021, installations will be required to carry out the usual checks carried out at the start of a calendar year to provide a baseline for their emissions. This negligible one-off cost would be incurred whether there was a tax or not.</p> <p>For those installation permit holders whose emissions exceed their tax emission allowance there will be an additional requirement to familiarise themselves with this measure and an ongoing cost of paying a tax bill once a year, starting in 2022, both of which are negligible. Installations that have lower emissions than the tax emission allowance will face no tax liability. Small emitters will be able to add any 'unused' element of their tax emission allowance from tax year 2021 to 2022.</p> <p>This measure is not expected to impact on civil society organisations.</p>
<p><b>Impact on HMRC or other public sector delivery organisations</b></p>	<p>HMRC will incur costs to build IT systems to support this new tax. This includes obtaining the information from regulators' IT system needed to bill installations and providing an IT system to enable bills to be generated and tax to be accounted for accurately. These costs are provisionally estimated at £2.75 million. HMRC will also incur staff costs, initially estimated at £620,000. All costs will be reviewed once tax and system designs are final.</p>

	<p>There will also be costs to regulators, provisionally estimated at less than £100,000, from adding functionality to ensure their IT system can provide relevant information to HMRC. Any such changes will be made alongside changes needed to reflect leaving the EU ETS and, where possible, be done in a way that enables them to be used for any long-term carbon pricing solution.</p>
<p><b>Other impacts</b></p>	<p><u>Carbon assessment</u> - at present the rate of tax has not been set but it is intended that the rate would provide an incentive for electricity generators and energy intensive industries to reduce their emissions. It is expected that the rate will be set to maintain carbon pricing at a broadly similar level to that which would have occurred had the UK remained in the EU ETS, and it will therefore have a broadly similar impact to the EU ETS in reducing carbon dioxide emissions.</p> <p><u>A Justice Impact Test</u> has been completed with the Ministry of Justice considering whether additional burdens would fall on Courts and tribunals. This concluded that the risks of creating additional burdens on the tribunal system was small.</p> <p><u>Other impacts</u> have been considered and none have been identified.</p>

# 5. Summary of consultation questions

## Chapter 2

### Tax emission allowances

1. Do you have any views on the methodology and process for setting tax emission allowances and adjusting them in light of activity level reports?
2. Do you agree that small emitters should have their tax emission allowance for 2022 increased by the amount of their unused tax emission allowances from 2021? Do you think that, instead, a payment scheme as outlined below for main scheme installations would be an appropriate means of incentivising decarbonisation for small emitters?

### Payments to reward decarbonisation for main scheme installations

3. Do you agree that, if the Carbon Emissions Tax were to be introduced, a mechanism should be introduced to reward decarbonisation?
4. Do you agree that there should be no obligation on operators that did not wish to make a claim to submit this additional data? How easily could your installation provide this additional data? How much additional work would it take to calculate (please set out the employee hours and expected costs of doing this)?
5. Do you agree that the methodology outlined above would accurately demonstrate the extent to which an installation's emissions reductions were achieved through decarbonisation?
6. Do you agree with the government's proposal to enable installations to submit data with activity level reports and to allow a final deadline of 31 March 2024 for claims relating to the 2021 and 2022 tax years?

### Rate in 2021 and 2022

7. Do you agree that the Carbon Emissions Tax rate should be set using EU ETS price data?
8. What are your views on the proposal to adjust the rate?

### Paying the tax to HMRC

9. For the longer term, do you think other payment methods should be made available (e.g. a transfer involving the Business Tax Account)?

## Conclusion

- 10. Do you have any views on the practicality of the proposals in Part B of chapter 2 that you cannot cover in responses to other questions?**
- 11. Are there any omissions or do you have any concerns or other suggestions about the operation of the tax?**

## Chapter 3

### Broadening the scope of the tax: capturing additional emissions

- 12. Do you have any views on how, in the years after 2021, a Carbon Emissions Tax could drive decarbonisation in sectors beyond those that would be subject to the tax at introduction?**

### Incentivising negative emissions in the longer term

- 13. Do you agree that the government should explore the case for tax incentives to support negative emissions technologies?**
- 14. In designing any tax incentive, what issues should the government consider regarding negative emissions technologies?**



## 6. The consultation process

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

- Stage 1 Setting out objectives and identifying options.
- Stage 2 Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 Drafting legislation to effect the proposed change.
- Stage 4 Implementing and monitoring the change.
- Stage 5 Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of a specific proposal, rather than to seek views on alternative proposals.

### How to respond

A summary of the questions in this consultation is included at chapter 5 of this consultation paper.

Responses should be sent by 29 September 2020, by e-mail to Michael Lyttle of HM Revenue & Customs [carbon.taxation@hmrc.gov.uk](mailto:carbon.taxation@hmrc.gov.uk).

Telephone enquiries 03000 585637 (from a text phone prefix this number with 18001)

### **Please do not send consultation responses to the Consultation Coordinator.**

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from [HMRC's GOV.UK pages](#). All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

### Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018, General Data Protection Regulation (GDPR) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be

aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs.

## Consultation Privacy Notice

This notice sets out how we will use your personal data, and your rights. It is made under Articles 13 and/or 14 of the General Data Protection Regulation.

## Your Data

### The data

We will process the following personal data (*delete/add as appropriate*):

*Name*  
*Email address*  
*Postal address*  
*Phone number*  
*Job title*

### Purpose

The purpose(s) for which we are processing your personal data is: *add the title of your consultation*

### Legal basis of processing

The legal basis for processing your personal data is that the processing is necessary for the exercise of a function of a government department.

### Recipients

Your personal data will be shared by us with (*provide details of recipients of the personal data, if applicable e.g. HM Treasury*).

### Retention

Your personal data will be kept by us for six years and will then be deleted.

### Your rights

- You have the right to request information about how your personal data are processed, and to request a copy of that personal data.

- You have the right to request that any inaccuracies in your personal data are rectified without delay.
- You have the right to request that any incomplete personal data are completed, including by means of a supplementary statement.
- You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.
- You have the right in certain circumstances (for example, where accuracy is contested) to request that the processing of your personal data is restricted.

## Complaints

If you consider that your personal data has been misused or mishandled, you may make a complaint to the Information Commissioner, who is an independent regulator. The Information Commissioner can be contacted at:

Information Commissioner's Office  
Wycliffe House  
Water Lane  
Wilmslow  
Cheshire, SK9 5AF  
0303 123 1113  
[casework@ico.org.uk](mailto:casework@ico.org.uk)

Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

## Contact details

The data controller for your personal data is HM Revenue and Customs. The contact details for the data controller are:

HM Revenue and Customs  
100 Parliament Street  
London, SW1A 2BQ

The contact details for HMRC's Data Protection Officer are:

The Data Protection Officer  
HM Revenue and Customs  
7th Floor, 10 South Colonnade  
Canary Wharf, London E14 4PU  
[advice.dpa@hmrc.gsi.gov.uk](mailto:advice.dpa@hmrc.gsi.gov.uk)

## Consultation Principles

This call for evidence is being run in accordance with the government's Consultation Principles. The Consultation Principles are available on the Cabinet Office website: <http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance>

If you have any comments or complaints about the consultation process, please contact:

John Pay,  
Consultation Co-ordinator, Budget Team  
HM Revenue and Customs  
100 Parliament Street  
London, SW1A 2BQ.

**Please do not send responses to the consultation to this address.**

# Annex A: Carbon Emissions Tax primary legislation

This annex sets out the relevant legislation in Finance Act 2019. The legislation in the annex shows how the Act reads as amended by legislation that is currently before Parliament (which, at the time of publication of this consultation, had passed all its parliamentary stages but had not received Royal Assent). Further changes to the Act would be included in a Finance Bill in autumn 2020, including amending section 70(3) to set the rate for 2021 and to provide for the rate to be adjusted in line with paragraphs 2.65 – 2.66 of this consultation paper.

## **Finance Act 2019 (c. 1)**

### **Part 3**

### **Carbon Emissions Tax**

#### *Introductory*

#### **69 Carbon emissions tax**

- (1) A tax called “carbon emissions tax” is to be charged in accordance with this Part.
- (2) The Commissioners are responsible for the collection and management of carbon emissions tax.

#### *Charge to tax*

#### **70 Charge to carbon emissions tax**

- (1) Carbon emissions tax is charged, in relation to a regulated installation, if the amount of reported carbon emissions for a reporting period exceeds the emissions allowance for the period.
- (2) The amount of “taxable carbon emissions” in relation to the installation for the reporting period is the amount of the excess.
- (3) Carbon emissions tax is charged on taxable carbon emissions at the rate of £16 per tonne of carbon dioxide equivalent.
- (4) The Treasury may by regulations provide that carbon emissions tax is not charged in relation to regulated installations of a specified description.

## **71 “Reported carbon emissions”**

- (1) The amount of “reported carbon emissions” in relation to an installation for a reporting period is the total amount of emissions from the installation, in tonnes of carbon dioxide equivalent, that is stated—
  - (a) in the emissions determination (or, if there is more than one, the latest emissions determination) for the period, or
  - (b) if there is no such determination, in the emissions report for the period.
- (2) In subsection (1), “emissions determination” means the regulator’s estimate of the total amount of emissions from the installation for the period, determined in accordance with—
  - (a) article 70 of the Monitoring and Reporting Regulation, or
  - (b) regulation 44 of the Emissions Regulations.

## **72 “Emissions report” and “reporting period”**

- (1) In this Part, “emissions report” means a report of emissions that is submitted to the regulator for the purpose of complying with—
  - (a) the monitoring and reporting requirements or, in the case of an excluded installation, the monitoring and reporting conditions, or
  - (b) a requirement of a notice of surrender or of a revocation notice.
- (2) “Reporting period”, in relation to a regulated installation, means—
  - (a) a scheme year, or
  - (b) such shorter period for which an emissions report for the installation is required by a notice of surrender or a revocation notice.

## **73 “Emissions allowance”**

- (1) The “emissions allowance”, in relation to an installation for a reporting period, is the amount of emissions, in tonnes of carbon dioxide equivalent, specified by or under, or determined in accordance with, regulations made by the Commissioners under this section.
- (2) Regulations under this section:
  - (a) may have effect in relation to the reporting period during which they are made, and
  - (b) may make provision by reference to data relating to times before they are made.

#### **74 Liability to pay carbon emissions tax**

- (1) Carbon emissions tax in relation to an installation is payable by the person who, at the end of the reporting date, holds the permit for the installation.
- (2) The “reporting date”, in relation to a reporting period, means the day on which the emissions report for that period is required to be submitted to the regulator under the Emissions Regulations.

*Administration etc.*

#### **75 Power to make further provision about carbon emissions tax**

- (1) The Commissioners may by regulations—
  - (a) make provision about the assessment, payment, collection and recovery of carbon emissions tax, including provision about the recovery of overpayments;
  - (b) require persons to keep, for purposes connected with carbon emissions tax, records of specified matters, and to preserve those records for a specified period;
  - (c) make provision for the review of, and a right of appeal against, specified decisions of HMRC in connection with carbon emissions tax;
  - (d) make provision about the enforcement of carbon emissions tax (including provision for the imposition of civil penalties for failure to comply with a requirement of regulations under this Part);
  - (e) permit or require the sharing of information between HMRC, authorities and regulators for purposes in connection with carbon emissions tax;
  - (f) make provision about the form, manner and content of any notice, application or other communication with HMRC in connection with carbon emissions tax (including provision about communications in electronic form);
  - (g) make provision in relation to cases where an individual liable for carbon emissions tax dies or becomes incapacitated, or where a person (whether or not an individual) is subject to an insolvency procedure.
- (2) The Commissioners may by regulations make provision for purposes in connection with carbon emissions tax—
  - (a) about the submission of emissions reports to a regulator;
  - (b) about emissions determinations, including provision permitting or requiring a regulator to make an emissions determination in specified circumstances;

- (c) specifying conditions to be included in a permit granted by a regulator;
  - (d) for the review of, and a right of appeal against, specified decisions;
  - (e) about the performance of a function of a regulator;
  - (f) about the form, manner and content of any notice, application or other communication with a regulator (including provision about communications in electronic form).
- (3) Regulations under this section may, in particular—
- (a) make provision that is equivalent to, or applies with or without modification, any provision of an enactment relating to tax;
  - (b) modify;
    - (i) The Monitoring and Reporting Regulation
    - (ii) The Verification Regulation;
    - (iii) subordinate legislation relating to the monitoring or regulation of carbon emissions.

## **76 Consequential provision**

- (1) In section 1 of the Provisional Collection of Taxes Act 1968 (temporary statutory effect of House of Commons resolutions), in subsection (1), after “petroleum revenue tax” insert “, carbon emissions tax,”.
- (2) In regulation 52 of the Emissions Regulations (penalty for carrying out a regulated activity without a permit), after paragraph (2) insert—
 

“(2A) In paragraph (2), the reference to “costs” includes a reference to carbon emissions tax.”
- (3) Section 4(1) of the European Union (Withdrawal) Act 2018 does not apply, for the purposes of carbon emissions tax, in relation to any rights, powers, liabilities, obligations, restrictions, remedies and procedures so far as they arise under—
  - (a) Council Directive 2008/118/EC of 16 December 2008 concerning the general arrangements for excise duty, or
  - (b) Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity.
- (4) The Commissioners may by regulations make such provision as they consider appropriate in consequence of this Part.
- (5) Regulations under subsection (4) may modify;
  - (a) any enactment



(b) The Monitoring and Reporting Regulation;

(c) the Verification Regulation

*General*

**77 Interpretation**

(1) In this Part—

“the Commissioners” means the Commissioners for Her Majesty’s Revenue and Customs;

“emissions allowance” has the meaning given by section 73;

“emissions determination” has the meaning given by section 71;

“the Emissions Regulations” means the Greenhouse Gas Emissions Trading Scheme Regulations 2012 (S.I. 2012/3038);

“emissions report” has the meaning given by section 72;

“enactment” includes an enactment contained in subordinate legislation within the meaning of the Interpretation Act 1978;

“HMRC” means Her Majesty’s Revenue and Customs;

“installation” has the meaning given by regulation 3 of the Emissions Regulations (and references to an installation include references to an offshore installation, as defined in those Regulations);

“modify” includes amend, repeal or revoke;

“the Monitoring and Reporting Regulation” means Commission Implementing Regulation (EU) 2018/ 2066 of 19 December 2018 on the monitoring and reporting of greenhouse gas emissions pursuant to Directive 2003/87/EC of the European Parliament and of the Council and amending Commission Regulation (EU) No 601/2012 (as amended from time to time);

“operator” has the meaning given by regulation 3 of the Emissions Regulations (as read with Schedule 1 to those Regulations);

“reporting period” has the meaning given by section 72;

“specified” means specified in regulations under this Part;

“the Verification Regulation” means Commission Implementing Regulation (EU) No 2018/2067 of 19 December 2018 on the verification of data and on the accreditation of verifiers pursuant to Directive 2003/87/EC of the European Parliament and of the Council (as amended from time to time).

(2) In this Part, the following terms have the meaning given by regulation 3 of the Emissions Regulations—

“authority”,

“emissions”,

“excluded installation”,

“monitoring and reporting conditions”,

“monitoring and reporting requirements”,

“notice of surrender”,

“permit”,

“regulator”,

“revocation notice”,

“scheme year”, and

“tonne of carbon dioxide equivalent”.

(3) An “installation” is a “regulated installation” for a reporting period if, at any time during the period, the operator holds a permit for the installation.

(4) For the purposes of this Part, the Monitoring and Reporting Regulation is to be treated for the purposes of section 3 of the European Union (Withdrawal) Act 2018 as if it is fully in force immediately before IP completion day (even if it is not).

## **78 Regulations**

(1) Regulations under section 73, 75 or 76 may—

(a) make provision conferring functions or discretions on HMRC, the Secretary of State, an authority, a regulator or any other person;

(b) impose charges as a means of recovering costs incurred by a person in exercising a function conferred under the regulations or in anticipation of the conferral of such a function;

(c) make provision by reference to matters determined or published by HMRC, the Secretary of State, an authority or a regulator (whether before or after the regulations are made);

(d) make different provision for different purposes;

(e) include incidental, consequential, supplementary, transitional or transitory provision.

- (2) Regulations under this Part are to be made by statutory instrument.
- (3) A statutory instrument containing regulations under section 76(4) that make provision amending or repealing any provision of an Act of Parliament must be laid before the House of Commons after being made and, unless approved by that House before the end of the period of 40 days beginning with the date on which the instrument is made, ceases to have effect at the end of that period.”
- (4) Any other statutory instrument containing regulations under this Part is subject to annulment in pursuance of a resolution of the House of Commons.
- (5) But subsection (4) does not apply to a statutory instrument containing only regulations under section 79 (commencement).
- (6) The fact that a statutory instrument ceases to have effect as a result of subsection (3) does not affect—
  - (a) anything previously done under the instrument, or
  - (b) the making of a new instrument.
- (7) In calculating the period of 40 days mentioned in subsection (3), no account is to be taken of any time—
  - (a) during which Parliament is dissolved or prorogued, or
  - (b) during which the House of Commons is adjourned for more than four days.

## **79 Commencement and transitional provision**

This Part comes into force—

- (a) for the purposes of making regulations under section 70, 73, 75 or 76, on the day after the day on which paragraphs 1 to 8 of Schedule {j8591s} to FA 2020 come into force, and
  - (b) for all other purposes, on such day as the Commissioners may by regulations appoint.
- (2) Regulations under subsection (1) may—
  - (a) appoint different days for different purposes;
  - (b) include transitional or transitory provision.

## Annex B: Glossary of terms used

Term	Description
Activity Level Changes (ALC)	All installations holding a greenhouse gas emissions permit have to submit an activity level report each year which is used by the regulator to assess activity level changes (on a two-year rolling basis).
Activity level report	An annual report of the activities made by an installation covered by a greenhouse gas emissions permit.
Annual Activity Level (AAL)	Annual activity levels (on a two-year rolling basis) are compared with the historic activity level to assess whether changes to the tax emission allowance are required.
Baseline	The amount of emissions emitted by a sub-installation in a defined period. For assessing tax emission allowance in 2021 and 2022, it is proposed that the Historical Activity Level baseline period would be 2014 – 2018 and the benchmark baseline period would be 2016 – 2017.
Benchmark	<p>A reference value for greenhouse gas emissions relative to production activity. There are 52 product benchmarks, each representing the average of the top 10% most efficient installations for a given product across Europe. Where use of a product benchmark is not possible, two fall-back benchmarks based on heat production and fuel consumption, or a process emissions factor, can be used.</p> <p>For UK carbon pricing, the government will initially use benchmarks referenced from the EU ETS Phase IV. This provides confidence that the benchmarks will be based on sufficiently broad sets of data, maintains best available real-world levels of efficiency standards and supports fair and open competition internationally.</p>
Benchmarked products	These are defined in Annex I of the Free Allocation Regulation.
Carbon dioxide equivalent	Emissions of greenhouse gases other than carbon dioxide are converted to a carbon dioxide equivalent tonnage. Emissions and the tax emission allowance would be expressed in terms of carbon dioxide equivalent and the tax rate would also be set on this basis.
Carbon Emissions Tax	A tax on carbon emissions which, in the UK, may replace the EU ETS from January 2021.
Carbon Leakage Exposure Factor (CLEF)	CLEF is used in the EU ETS to set free allocation of emission allowances for different industrial sectors. The CLEF varies depending on the carbon leakage status of the industrial sector.
Carbon Leakage List (CLL)	The CLL is a list of industrial sectors drawn up by the European Commission that are deemed to be at significant risk of carbon leakage.
Confirmed tax emission allocation	The tax emission allowance that would be used to calculate the tax due. It takes into account any changes required as a result of activity changes reported in the annual activity level reports. Confirmed tax emission allowances would be published each autumn (starting in 2021).
Cross-Sectoral Correction Factor (CSCF)	Under a trading scheme, if the total volume of calculated preliminary free allocation made to eligible scheme participants breached the industry cap, any unallocated allowances from the industry cap in previous years and (if needed) allowances from the flexible shares of other industry sectors

	<p>would be used to ‘top up’ the industry cap. If this is still insufficient, a uniform reduction using the Cross-Sectoral Correction Factor (CSCF) could be applied to proportionately reduce any preliminary free allocation entitlement above the industry cap across all eligible recipients.</p> <p>Should the government introduce a tax, it proposes not to apply a CSCF to the tax emission allowance in 2021 and 2022.</p>
Department of Business Energy and Industrial Strategy (BEIS)	The government department responsible for approving tax emission allowance figures under the rules.
Devolved Administration	The governments of Scotland, Wales and Northern Ireland.
Emissions report	Annual report that is submitted by the installation, verified by the verifier and which details the total emissions for the year in tonnes on a carbon dioxide equivalent basis.
EU Allowance	Under the EU ETS, for each tonne of carbon dioxide emitted an installation must acquire and then surrender an EU Allowance. These may be allocated free of charge to installations in line with the free allocation rules, or an installation may buy or trade them at auction or on the open market.
EU Emissions Trading System (EU ETS)	The system by which the EU sets a price for carbon emissions.
Her Majesty’s Revenue and Customs (HMRC)	The government department that would be responsible for calculating the tax due, billing installations and collecting the tax.
Historical Activity Level (HAL)	The measurable heat produced by an ETS installation and consumed within that installation’s boundaries.
Indicative tax emission allowance	The tax emission allowance originally calculated and notified to the installation. If subsequently there were activity level or other changes that amend this figure it would be updated and become formally set (and published) as the confirmed tax emission allowance.
Industry cap	The total number of free allowances available for free allocation to a particular sector under a trading scheme.
Installation	The premises that is permitted to emit by virtue of holding either a greenhouse gas emissions permit (main scheme installation) or an excluded installation emissions permit (small emitters).
Linear Reduction Factor (LRF)	The annual rate by which the total cap on emissions under a trading scheme reduces.
Main scheme installations	Installations that hold greenhouse gas emissions permits.
National Implementation Measures (NIMs)	Under the EU ETS, National Implementation Measures (NIMs) is the once-per-allocation-period data collection exercise that is used to establish Historical Activity Levels (HAL) and set benchmarks for free allocation.
New entrants	Installations that are newly permitted.
Operator	The person / organisation that is responsible for the operation of the permitted installation.

Permit holder	The legal entity that holds the permit for the installation.
Phase III	The third phase of the EU ETS – running from January 2013 to December 2020.
Phase IV	The fourth phase of the EU ETS – it will run from January 2021 to December 2030.
Preliminary allocation	This is the provisional allocation of free EU Allowances to installations under the EU ETS (it does not take into account the Cross Sectoral Correction Factor). Once the Cross Sectoral Correction Factor has been applied the preliminary allocation becomes the finalised allocation.
The regulator	One of the following: <ul style="list-style-type: none"> <li>• Environment Agency</li> <li>• Natural Resources Wales</li> <li>• Northern Ireland Environment Agency</li> <li>• Offshore Petroleum Regulator for Environment and Decommissioning</li> <li>• Scottish Environmental Protection Agency</li> </ul> is responsible for ensuring compliance with the permitting, monitoring, reporting and verification system.
Small emitters	Installations in the Small Emitter and Hospital Opt-out Scheme, sometimes referred to as Article 27 or excluded installations, require an excluded installation emissions permit - these are referred to in this consultation paper as ‘small emitters’.
Sub-installation	For the purposes of data collection, each operator is required to divide each installation eligible for free allocation into sub-installations. Described by system boundaries that encompass inputs, outputs and emissions, sub-installations are designed to make the many different circumstances of installations comparable within one single benchmark.
Taxable emissions	Emissions that exceeded the tax emission allowance in any given year would be liable to be taxed under Carbon Emissions Tax.
Tax emission allowance	A threshold that would be set for each installation (roughly equivalent to the free allowances that would have been allocated under the EU ETS). Emissions that exceeded this threshold would be taxed under the Carbon Emissions Tax.
Ultra-low emitters	An installation is ultra-small if it is included in the list (the “ultra-small emitter list for 2021-2025”) of installations to be excluded from the EU ETS from 1 January 2021 under Article 27a of the Directive published for the purposes of the EU ETS.
Unused tax emission allowance	Where emissions were lower than the tax emission allowance the difference between the two would be the unused tax emission allowance.
Verified emissions	Emissions that have been verified by the installation’s verifier. This data needs to be submitted to the regulator each year. Small emitters still report their emissions to their regulator but do not need to have them independently verified.