HM Treasury

HM Revenue & Customs

Carbon Emissions Tax

Summary of Responses to the Consultation

March 2021

Contents

1. Introduction

1.1. In summer 2020 the government consulted on how a Carbon Emissions Tax would operate from 1 January 2021 if implemented. In December 2020, the government confirmed that it would implement a UK Emissions Trading System from 1 January 2021, and that the Carbon Emissions Tax would not be implemented. Chapter 2 of the consultation set out proposals for how the tax would operate from introduction and chapter 3 sought views on how the tax might be adapted and its scope widened to support decarbonisation. This document sets out a summary of responses to the consultation (which includes discussions from a number of meetings as well as written responses).

Engagement with the consultation

1.2. The consultation was launched on 21 July 2020 and closed on 29 September 2020. The government received a total of 171 responses broken down as follows.

	Category of respondent	**Numbers**
1	Generators (including renewable generators)	17
2	Industrial sectors and businesses	29
3	Trade associations and representative bodies	30
4	Aviation and shipping	12
5	Environmental groups	13
6	Think tanks and academics	10
7	Tax and other advisors	3
8	Members of the public	57
	Total respondents	**171**

1.3. As well as these written responses, the government held an online event which was available for any stakeholder who expressed an interest in attending. This was attended by more than 50 stakeholders. In addition, HM Treasury held a number of targeted meetings to discuss the proposals with a range of different stakeholders.

1.4. A full breakdown of respondents (excluding members of the public) is available in the annex. This includes those sending in written responses and those attending the online event.

2. Summary of responses to the consultation

Proposed operation of the Carbon Emissions Tax from 1 January 2021

Tax emission allowances

2.1. This section outlined the proposals for setting the tax emission allowance, an installation specific threshold above which an installation's carbon emissions would be taxed.

2.2. The consultation paper outlined that the tax emission allowance would be set initially, as far as possible, in line with the free allowances and targets that installations would have received for both main scheme emitters and small emitters under Phase IV of the EU ETS in order to provide continuity and minimise administrative burdens. It set out that the tax emission allowance would be calculated based on an installation's historical activity level data, EU ETS benchmark, and carbon leakage exposure factor. This figure would then be adjusted to reflect any qualifying activity level changes reported by installations. The tax emission allowance would be an allocation specific to each installation and wouldn't be tradeable, nor would be possible to carry over unused tax emission allowances from one year to the next.

2.3. Respondents were asked:

> **Q1. Do you have any views on the methodology and process for setting tax emission allowances and adjusting them in light of activity level reports?**
>
> **Q2. 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?**

2.4. The majority of business respondents that commented on this section agreed with the principle of aligning the tax and the arrangements for determining the tax emission allowances with EU ETS, particularly as they would welcome continuity to minimise business disruption and burdens. Amongst those who supported the tax emission allowance being set in line with the current free allocation arrangements some respondents pointed out that:

- using EU ETS Phase IV benchmarks to set tax emission allowances would be suboptimal for UK businesses unless the EU benchmarks reflected UK data;
- the inability to transfer or trade the tax emission allowance would mean that the tax would be a less flexible carbon pricing mechanism than EU ETS;
- at a meeting with Treasury officials, some stakeholders highlighted the anomaly of allocations/tax emission allowances to installations that are physically connected for the purpose of transferring heat and steam. They pointed out that applying the EU ETS free allocation rules to the tax without further refinement would see steam generators and the industrial site, as a whole, significantly disadvantaged;

- Covid-19 has affected activity levels in 2020 for some installations, which some respondents pointed out could result in reduced 2021 tax emission allowances because of the Phase IV formula, which compares recent activity levels with historical activity level data. As 2020 is an exceptional year, some proposed that Covid-19 related activity level changes should therefore be disregarded for the purposes of setting tax emission allowances.

2.5. Environmental groups also saw the value in alignment in the short term although the majority felt that this should be the starting point for a stronger carbon price and suggested the tax emission allowances should gradually be phased out or reduced to zero.

2.6. More generally, there respondents commented that a key aspect of the proposed review of the tax should cover the tax emission allowance policy.

Decarbonisation reward payments

2.7. This section sought views on proposals to incentivise decarbonisation through the tax, by introducing a reward system for installations whose actual emissions fall below their tax emission allowance. Like the EU ETS free allowance scheme, the goal of this reward scheme would be to incentivise decarbonisation.

2.8. The consultation proposed that, to assess eligibility for decarbonisation reward payments under the tax, each installation would be required to submit information to the government – potentially in the form of additional data to be submitted alongside an annual activity level report - supporting their claims for decarbonisation reward payments. Respondents were asked whether this reporting system would be an effective means of assessing eligibility for decarbonisation reward payments.

2.9. Respondents were asked:

Q3. Do you agree that, if the Carbon Emissions Tax were to be introduced, a mechanism should be introduced to reward decarbonisation?

Q4. 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)?

Q5. Do you agree that the methodology outlined above would accurately demonstrate the extent to which an installation's emissions reductions were achieved through decarbonisation?

Q6. 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?

Payments to reward decarbonisation for main scheme installations (Q3)

2.10. Whilst a large proportion of responses presented no view on this issue, around half of respondents that addressed the issue agreed with the idea of some form of decarbonisation reward. Differences generally lay in how a payment mechanism would be implemented in stakeholders' specific sectors and the repayment rate itself.

2.11. Those in favour of the decarbonisation payments mainly argued that there should be a clear differentiation between rewards for active efforts to decarbonise as opposed to decarbonisation through decreased output.

2.12. Many who opposed the decarbonisation reward payments did not state opposition to the principle of rewarding decarbonisation through payments, though some suggested that such a mechanism should not be linked to the tax. Other reasons given for not supporting the proposal were the anticipated administrative burden (especially on smaller companies), a preference for allowing banking or transfer of tax emission allowances, or a belief that the new activity level reports would reward decarbonisation without the need for a reward payment scheme.

2.13. A number of industrial respondents noted that the reward payment rate should be set at 100% of the tax rate, as opposed to the 50% which had been set out for illustrative purposes in the consultation, in order to maximise the incentive for installations to decarbonise their processes. Several responses also called for clarity on how the decarbonisation rewards would be applied to small emitters and combined heat and power plants.

2.14. A number of responses from individuals and green groups outlined that the long-term goal of the decarbonisation reward payment mechanism should be the reduction of the tax emission allowance to zero.

Submission of additional information to assess eligibility for decarbonisation reward payments (Q4)

2.15. The overwhelming majority of those that responded to this question agreed with the government proposal that there should be no obligation on operators to submit additional data unless they wished to receive a decarbonisation reward payment, arguing that obliging all operators to do so would become an administrative burden for those that did not wish to apply for reward payments.

2.16. Many respondents also stressed that adequate data would be essential in ensuring that reward payments were given as a result of operators actively using decarbonisation technology, as opposed to reduced overall output.

Methodology to outline emissions reductions through decarbonisation (Q5)

2.17. The majority of respondents to this question agreed with the proposed methodology for demonstrating decarbonisation in principle. A number of respondents did add, however, that they would like further detail on how the process would work in practice, and some flagged that the proposal could add a new cost to installations, because it would require new monitoring processes.

2.18. Several responses from the energy sector argued that clarity was required on what specific measures would constitute 'decarbonisation', suggesting that measures such as fuel switching should be included within the definition. Some industrial stakeholders took the view that energy efficiency calculations should also be taken into account when deciding on whether to award decarbonisation reward payments.

2.19. More widely, environmental groups supported the intention of the methodology proposal and called for reassurance from the government that installations would not take advantage of decarbonisation reward payments by simply reducing their overall output.

Timeline for submission of activity level reports (Q6)

2.20. Respondents to this question generally supported the proposed deadline for submitting data for decarbonisation reward payments.

2.21. Those respondents opposed to the timeframes for submitting claims frequently cited the length of the gap between the 2024 deadline and the submission of activity reports from 2021 and 2022. It was argued that decarbonisation pay-outs should instead take place in the same year as the submission of emissions data by installations, enabling companies to continue to investment in technologies to drive decarbonisation

2.22. Those who expressed support for the proposal of a 2024 deadline argued that this would provide installations with sufficient time to process and submit activity level reports to the government.

Rate in 2021 and 2022

2.23. This section sought views on the government's proposal for determining the rate of the Carbon Emissions Tax in 2021 and 2022. To maintain continuity for businesses following the UK's withdrawal from the EU ETS, the consultation proposed that in 2021 and 2022 indicative tax rates would be announced in Autumn 2020 and at Budget 2021 respectively, based on:

- the average December 2021 and December 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.

It was proposed these tax rates would be adjusted downwards (to EU ETS prices) if they turned out to be higher than the average EU ETS auction clearing prices by £1 or more. The aim of this proposal was to give businesses certainty about their maximum liability under the tax, and to ensure that UK industry would not face a higher carbon price than EU competitors. The final tax rate for 2021 and 2022 reflecting any adjustment would be announced in early 2022 and early 2023 respectively before tax bills were issued in the summers of 2022 and 2023 respectively.

2.24. Respondents were asked:

Q7. Do you agree that the Carbon Emissions Tax rate should be set using EU ETS price data?

Q8. What are your views on the proposal to adjust the rate?

Using EU ETS data to set tax rate (Q7)

2.25. The majority of respondents to this question agreed with the principle of basing the tax rate on EU price data as a short-term measure, but many also expressed doubts on whether this would be the correct approach to take in the longer term.

2.26. Those in favour of using EU price data for the tax rate highlighted the continuity offered by this approach to UK companies, arguing that it would maintain competitiveness during the early years of transition between the EU ETS and the Carbon Emissions Tax.

2.27. Some respondents argued that, in the long term, the UK should base its carbon pricing policy on its own climate goals – namely reaching net zero carbon emissions by 2050.

Tax rate adjustment proposals (Q8)

2.28. Although many respondents to this question agreed with the principle of aligning the tax with EU prices to ensure competitiveness of UK industry, a significant number were opposed to the tax rate adjustment methodology as proposed in the consultation document.

2.29. Some respondents argued that the proposed uplift and adjustment approach to match the tax rate with EU future prices would be too complex and volatile for companies, especially as the UK would have no influence over EU prices following its exit from the EU ETS. Many respondents instead suggested that prices be set in advance and remain fixed, as opposed to being reviewed and adjusted periodically.

2.30. Many stakeholders opposed to the rate adjustment mechanism focused on the £1 rate adjustment threshold, which several respondents argued was too high, and should instead be lowered or scrapped in order to mirror EU ETS prices. Responses also called for any rate setting changes after 2022 to be gradual, to prevent large carbon price fluctuations, which could have a detrimental effect on UK businesses.

Paying the tax to HMRC

2.31. This section set out HMRC's proposals for how and when the tax should be paid to them.

2.32. Respondents were asked:

> **Q9. For the longer term, do you think other payment methods should be made available (e.g. a transfer involving the Business Tax Account)?**

2.33. Most respondents to this question did not have strong views or were content with the payment methods being proposed with few respondents commenting about payment methods. A small number of respondents said that if the tax were to be more than a short- term measure, they would prefer to have more options for paying their bill.

2.34. Some respondents thought that 30 days would not be long enough for businesses to pay the tax bill. Others proposed that a fixed annual date be set for when the payment of the bill should be made, with one saying that they would prefer to know as soon as possible what their liability for the tax was rather than wait until August for the bill.

2.35. Two installations said they favoured the Business Tax Account being available to use to pay the bill. One other installation said that they did not favour using the Business Tax Account for bill payment and one other said that using bank transfers would be sufficient.

2.36. Most of the businesses that responded to the question also said that they had concerns that, unless HMRC verified the names and addresses of those it was planning to bill in August each year, there was a risk that some bills would not be received and therefore paid in time.

2.37. A few respondents suggested that HMRC should bill the business (as was more usual) rather than the installation, as sometimes these addresses differed.

Chapter 2 conclusion

2.38. This section sought views and concerns of respondents that were not covered by previous questions in chapter 2.

2.39. Respondents were asked:

> **Q10. 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?**
>
> **Q11. Are there any omissions or do you have any concerns or other suggestions about the operation of the tax?**

2.40. Many of the comments made were about the future of the tax which is considered in chapter 3 – some respondents repeated comments under these two questions in their responses to chapter 3. In this document we have covered comments that were made about the future of the tax in the response to chapter 3 (see "Possible future changes to the tax" section below).

2.41. A number of respondents thought that there needed to be an urgent decision on whether the tax would be implemented, arguing that businesses needed clarity and certainty both to be able to comply with the new tax and so that the right investment decisions could be made. The uncertainty was impacting those decisions which in turn was not incentivising decarbonisation. Some respondents believed the tax and the uncertainty would lead to higher prices.

2.42. Greater clarity was sought around the compliance regimes that would operate under the tax and the supporting penalty regimes, again so that businesses could understand their obligations.

2.43. Other respondents expressed the need for a clear definition of who the person liable to pay the tax would be; and the need for a simple tax.

Possible future changes to the tax

2.44. Chapter 3 sought views on how, if implemented, the Carbon Emissions Tax would evolve to support the UK's long-term policy objective of reaching net zero carbon emissions by 2050. There was a section on broadening the scope of the tax and another dealing with negative emissions technologies.

Broadening the scope of the tax: capturing additional emissions

2.45. Respondents were asked:

Q12. 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?

2.46. Respondents' views on broadening the scope of the tax varied greatly by sector. Some supported proposals to expand the tax into new sectors after 2021. Those opposed to broadening the scope of the tax mainly expressed concern over the adverse effects this could have on specific sectors – particularly aviation and shipping, which were mentioned in the consultation as examples of sectors which the Carbon Emissions Tax could cover in the future. Many respondents agreed with the principle of extending the tax into new sectors but suggested that a detailed sector-by-sector analysis would be required ahead of doing so.

2.47. Individuals and green groups were strongly supportive of extending the scope of the tax to more sectors, with some respondents arguing that the tax should be extended to cover the entire economy to maximise its effectiveness. Several responses from individuals suggested that the revenues from a Carbon Emissions Tax should be redistributed as dividends across the economy.

2.48. Several respondents from industry and academia proposed extending the Carbon Emissions Tax to the aviation and shipping sectors specifically. Shipping was cited by one respondent as a heavy emitting industry with no decarbonisation incentive currently in place, while one consultancy suggested that the current CORSIA scheme alone is not sufficient to reduce emissions in the aviation sector.

2.49. Respondents from within the aviation and shipping sectors opposed the proposal of extending the tax to include them, although a few respondents acknowledged that their industries had scope to decarbonise.

2.50. One aviation trade association argued that the sector is already subject to emissions regulations through CORSIA, while one airline argued that Air Passenger Duty could be transformed to incentivise decarbonisation. Similarly, one respondent argued that steps are already being taken to decarbonise seaports, with the introduction of a tax likely to add costs.

Incentivising negative emissions technologies in the longer term

2.51. Respondents were asked:

Q13. Do you agree that the government should explore the case for tax incentives to support negative emissions technologies?

Q14. In designing any tax incentive, what issues should the government consider regarding negative emissions technologies?

2.52. The majority of respondents that answered these questions were in favour of the government exploring tax incentives for the use of negative emissions technologies (NETs). This included respondents from industry (including the energy sector and trade associations) as well as several green groups, who argued that tax incentives would attract investment into NETs, which in turn would support the UK in reaching its net-zero targets.

2.53. Several advocates for NETs incentives also highlighted the importance of encouraging emissions reduction as a means of allowing industry to offset the costs of investing in decarbonisation technologies such as carbon capture.

2.54. A handful of trade association and industrial respondents argued that government funding would be required for industrial investment in decarbonisation technologies.

2.55. A small number of respondents on this issue outlined the need for more clarity on negative emissions technologies and how it could be applied to their sector, with one respondent from the aviation sector arguing that the incentives proposed would not be applicable in their sector.

2.56. A few respondents opposed incentives for negative emission technologies, on the basis that disincentivising high emissions through a comprehensive carbon taxation system without any untaxed emissions would be a more effective and transparent means of reaching the government's net-zero goals than the introduction of incentives for negative carbon emissions technologies.

Annex A: List of stakeholders consulted

This list includes those who responded in writing to the consultation paper and those that attended the online event (see paragraphs 1.6 and 1.7 above).

1. Aggregate Industries
2. Ahlstrom Munksjo
3. Airlines for America
4. Airline UK
5. Airport Operators Association
6. Anaerobic Digestion & Bioresources Association
7. Ancala Midstream
8. AMP Clean Energy
9. Arcadis
10. Assessing the Mitigation Deterrence Effects of GGRs
11. Associated British Ports
12. The Association for Decentralised Energy
13. Aviation Environment Federation
14. Avocet Risk Management Ltd
15. Bairds Malt
16. Belfast Trust
17. Breedon Group
18. Brindex
19. Bristol Airport
20. British Ceramic Confederation
21. British Glass
22. British Ports Association
23. British Sugar
24. BP
25. CalaChem
26. Campaign Against Gatwick Noise Emissions
27. Carbon Capture and Storage Association
28. Carlsberg
29. Celestial Aviation
30. Centrica
31. CF Fertilisers
32. Chemical Industries Association
33. Chrysaor
34. Citi Group Investment Bank
35. Citizens Climate Lobby UK
36. Colibri Energy
37. Confederation of British Industry
38. Confederation of paper industries
39. Conrad Energy
40. Dairy UK
41. Deloitte

42. DHL
43. Drax
44. DSM
45. E.ON
46. Earthly Biochar
47. Easy Jet
48. EDF Energy
49. EDF Europe
50. Ember Climate
51. Energy Shot Catapult
52. Energy UK
53. Engie
54. Eni
55. Environmental Defense Fund UK
56. Environmental Services Association
57. EP UK Investments
58. Equinor
59. ESB Generation and Trading
60. European Federation of Energy Traders
61. FCC Environment
62. Flight Free UK
63. Food and Drink Federation
64. Foodchain & Biomass Renewables Association
65. Forest Carbon
66. Green Alliance
67. Greenergy
68. Greensand
69. Heathrow Airport
70. HDR Inc
71. INEOS
72. Infinis
73. Ingevity
74. Intergen
75. International Air Transport Association
76. International Emissions Trading Association
77. Jacobs
78. JRP Solutions
79. Kellogg
80. LSE
81. Make UK
82. Manchester Airports Group
83. Mineral Products Association
84. Muntons plc
85. National Airlines Council of Canada
86. National Grid
87. Natural Energy Action
88. Neptune Energy
89. NHS Scotland
90. O-I
91. Oil & Gas UK
92. OKOOG
93. Orsted

94. Oxford Martin School
95. Peak Gen
96. Peel & Co
97. Petro INEOS
98. PO Ferries
99. Prinovis
100. PwC
101. PX Ltd
102. RBS (Property Services)
103. Redshaw Advisors
104. Renewable Transport Fuel Association
105. Renewable UK
106. Restore our Climate
107. Rosetta Advisory Services
108. RWE
109. Schneider Electric
110. Scarthin books
111. Scotch Whisky Association
112. Scottish Power
113. Shell UK
114. Shetland Islands Council
115. The Society of Motor Manufacturers and Traders Ltd
116. South Hook LNG
117. SSE
118. Statera Energy
119. Statkraft AS
120. Suez Recycling and Recovery
121. Sustainable Aviation Swan Energy
122. Syngenta
123. Tarmac
124. Tata Chemicals
125. Tata Steel
126. Tech UK
127. TFL
128. Total E&P Group
129. Total Oil
130. UK Emissions Trading Group
131. UKMPG
132. UK Petroleum Industry Association
133. Uniper
134. University of Aberdeen
135. University of Edinburgh
136. University of London
137. University of Manchester
138. Valero
139. Velocycs
140. Veolia
141. Viridor
142. Volac
143. Whyte & Mackay
144. World Kinect
145. Zero Carbon Campaign