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To Whom it may concern,

The UK ETS Authority is seeking views on amendments to existing civil penalties within the scheme. This consultation proposes four amendments. The first two are to ensure penalty amounts are comparable with similar penalties under the scheme and are proportionate to the type of breach. The third amendment introduces a technical change to how the inflation factor is calculated and applied to penalties. The final amendment will align the penalties included in the upcoming deficit notice penalty so that they are also applied consistently in cases where a permit is transferred.

The proposed amendments are:

1. Amendment to the punitive element of penalties related to operating without a permit.

There are three penalties within the Greenhouse Gas Emissions Trading Scheme Order 2020 (the Order) relating to the breach of operating without a permit. They are:

- Article 50 – Installations: carrying out a regulated activity without a permit contrary to Article 26 (Installations: requirement for permit to carry out regulated activity).
- Article 57 – Hospital and small emitters: failure to notify when ceasing to meet criteria.
- Article 60 – Ultra-small emitters: failure to notify where reportable emissions exceed maximum amount.

Each of these penalties are calculated by assessing (a) avoided costs as a result of the breach and (b) a punitive element.

On 6th October 2023, Directions came into force for Articles 50 and 60 of the Order¹. These Directions are required under the Order and ensure consistency of approach by the

¹ <https://www.daera-ni.gov.uk/articles/emissions-trading-schemes-fees-charges-and-civil-penalties>
<https://www.gov.wales/direction-natural-resources-body-wales-article-504-greenhouse-gas-emissions-trading-scheme-order>
<https://www.gov.wales/direction-natural-resources-body-wales-article-606-greenhouse-gas-emissions-trading-scheme-order>

2. Amendment to the civil penalty associated with Article 56

Articles 52 (4) (Failure to surrender allowances) and 56 (Hospital and small emitters: under-reporting of emissions) of the Greenhouse Gas Emissions Trading Scheme Order 2020 both contain penalties related to under-reporting discovered after submission of an annual emissions report.

Under the main UK ETS, if an installation's reportable emissions in a scheme year are discovered to exceed the installation's verified reportable emissions and this resulted in a failure to surrender allowances by the relevant deadline, the penalty in Article 52 applies. In addition, the operator is required to surrender the excess allowances to cover the unreported emissions.

Where a hospital or small emitter (HSE) does not include emissions in its annual emissions report for a scheme year, the penalty in Article 56 applies to the unreported emissions. In addition, the operator may be liable to the penalty in Article 54 (Hospitals and small emitters: exceeding emissions target) for reportable emissions exceeding its emissions target.

The Article 52 (4) and 56 penalties are calculated as follows:

- **Article 52 (4) (Current):** £20 (x the inflation factor as defined in Article 52 (11)) for each allowance that the operator surrender.

Please note that the inflation factor is subject to change, as referenced in proposal 3 of this document.

- **Article 56 (Current):** £5000 + (Unreported emissions in the scheme year in tonnes of carbon dioxide equivalent x Carbon Price for the scheme year, as published by the UK ETS Authority under Article 46 (Carbon Price)).

As they currently function, the Article 56 penalty is disproportionately punitive when compared to the Article 52 penalty. The UK ETS Authority considers that an under-reporting breach for HSEs is less serious than a similar breach by an operator in the main UK ETS because the breach has less impact on the integrity of the scheme's UK Allowance market. In addition, it is intended that there is a lower compliance burden on HSEs compared to operators in the main UK ETS. The UK ETS Authority is therefore proposing the following amendments to how the civil penalty is calculated:

1. To remove the link to the carbon price for the scheme year from Article 56. This would not impact the HSEs liability to pay the carbon price for the year in which their emissions were made, in the instance that reportable emissions exceed their emissions targets for the scheme year under Article 54.
2. To set the value of the Article 56 penalty for unreported emissions at £10 per tonne of carbon dioxide equivalent x the inflation factor, to reflect the seriousness of the breach and intended lower compliance burdens associated for HSEs.

Article 56 (Proposed): (Unreported Emissions in the scheme year in tonnes of carbon dioxide equivalent x £10 per tonne x an inflation factor) + £5,000. See proposal 3 below for further information on the proposed amended inflation factor.

The Authority does not intend to remove the additional sum of £5,000 the regulators may apply as part of the Article 56 penalty. It may be appropriate for regulators to apply this in certain circumstances, such as where an HSE has benefitted financially as a result of a breach.

The proposal will mean a more proportionate approach is taken by regulators for penalties given in association with Article 56.

Question 2: Do you agree with the recommended proposals to ensure a more proportionate penalty is given to hospitals and small emitters in relation to Article 56?

3. Amendments to the Article 52 inflation factor calculation

Penalties given under Article 52, Article 53 (Failure to transfer or surrender allowances where underreporting discovered after transfer) and the proposed penalty in Article 56, refer to an inflation factor which is currently calculated as follows:

The inflation factor is $(CPI_2 - CPI_1) / CPI_1$ or 1, whichever is greater, where –

- CPI_2 is the consumer prices index for the most recent March for which the consumer prices index is published when the penalty notice is given. Currently, CPI_2 for the 12-month period following March 2023 is 128.9.
- CPI_1 is the consumer prices index for March 2021, which has a value of 109.4. This base figure is used as the first CPI published after the scheme came into force.

The latest consumer price index publication can be located [here](#), along with previous consumer price indexes.

The UK ETS Authority is proposing two changes to the above inflation factor calculation.

1. A technical change to correct the inflation factor calculation to ' CPI_2 / CPI_1 or 1, whichever is greater'. This will enable the inflation factor to function as intended, so that penalties change accurately in line with inflation and remain proportionate.
2. To amend the definition of CPI_2 to the consumer prices index for the most recent March for which the consumer price index is published when the breach occurred, not when the penalty notice is given. This will ensure that the appropriate and most fair rate of inflation is used in cases where a penalty notice is given in a different year to the breach.

<p>Question 3: Do you agree with the proposed amendments to Article 52 to ensure that the inflation factor is correctly applied and is based on the CPI up to the date of the breach occurred?</p>

4. Amendment to the Article 53 penalty to align under-surrender penalties whether the under-surrender is discovered before or after a permit transfer.

In the [Developing the UK ETS Authority response](#), the Authority set out its intention to introduce a deficit notice, issued where an operator or aircraft operator fails to surrender allowances to cover its reportable or aviation emissions by the relevant deadline. Failure to comply with a deficit notice would result in a penalty consisting of a proportionate mandatory penalty and a daily penalty that may be applied by regulators. Currently, the Article 53 penalty (for failure to transfer or surrender allowances where under-reporting of allowances is discovered after a permit transfer) is different to the proposed deficit penalty and contains no daily penalty element. The UK ETS Authority is therefore proposing to amend Article 53, when the deficit notice penalty is introduced, to align the deficit penalty and the Article 53 penalty.

The proposal will mean a more consistent approach is taken by regulators for all penalties given in association with under-surrender.

Question 4: Do you agree with the recommended proposals to ensure the upcoming Deficit Notice provisions and penalties apply in both non-transferring and transferring scenarios?

How to provide your views:

The UK ETS Authority is seeking views on the above proposals to ensure civil penalty values are comparable to penalties of a similar nature and are proportionate to the type of breach. If you have any feedback, please respond at emissions.trading@energysecurity.gov.uk by 08/03/2024.

The UK ETS Authority