

# The future of UK carbon trading

The UK will leave the EU Emissions Trading Scheme (EU ETS) at the end of this year, when the Brexit transition period comes to an end. That will leave a big gap in the mechanisms needed to achieve net zero carbon emissions by 2050, and consequently a consultation exercise was held in 2019 on the future of carbon pricing in the UK. Now the Department for Business, Energy & Industrial Strategy and the devolved administrations have published their response to the consultation and their proposals for replacing the EU ETS with a UK 'cap and trade' scheme.

The plan is that the new UK ETS will take over from the EU ETS in January 2021, and that it will be very similar in most respects to Phase IV of the EU scheme which starts on the same date. Depending on the outcome of the trade agreement negotiations with the EU, it could even be linked to the EU ETS, with compatible carbon allowances. Like that scheme, it will cover energy intensive industries, power generation and

certain aviation routes, and participants will have to obtain most of their allowances via auctions, although some will continue to be allocated for free to new entrants and where necessary to prevent carbon leakage. But additional sectors could well be included within a few years.

One key difference between the EU ETS and the proposed UK scheme is that the number of allowances issued will initially be capped at only 95% of what the UK's notional share of the EU ETS cap would have been, in order to show "greater climate ambition from the start". The cap for Phase I, which runs until 2030, will be adjusted in the future to provide a trajectory to net zero. In addition, there will be an Auction Reserve Price of £15 in the early years to provide a minimum carbon price, irrespective of the demand for allowances.

Despite publishing these proposals, the government is still hedging its bets by working on a potential carbon emission tax that would be an alternative to a UK ETS. A consultation paper on such a tax is expected later this year.

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