

Section 95 and Schedule 12: carbon emissions tax; Section 96: charge for allocating allowances under emissions reduction trading scheme

The UK is considering two main options to maintain carbon pricing in line with its commitments to reach net-zero emissions by 2050 in case it leaves the EU with no deal. These two options are aimed at allowing as smooth as possible a transition out of the EU Emissions Trading Scheme (EU ETS),¹ which is the EU's main climate policy instrument. The first option is to introduce a UK ETS that could, if both parties agree, be linked to the EU ETS.² The second option is to replace the UK participation in the EU ETS by a carbon emissions tax.³ The UK Government and the devolved administrations have expressed their preference for a UK ETS.⁴ Nevertheless, both options remain on the table. This “twin-track approach” has been justified as a way to “ensure that, whatever the circumstances, the UK will have an effective carbon pricing regime in place”.⁵ Consequently, provisions are being introduced to support the establishment of either a UK ETS or a carbon emissions tax.

Sections 69 to 78 of the Finance Act 2019 (FA 2019) introduced the main design features of the carbon emissions tax.⁶ Section 95 of and Schedule 12 to the Finance Act 2020 (FA 2020) include amendments to some of these provisions in order to make the carbon emissions tax operational as of 1 January 2021, if need be.⁷ Moreover, section 96 FA 2020 provides the legal basis for the introduction

¹ Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a system for greenhouse gas emission allowance trading within the Union and amending Council Directive 96/61/EC [2003] OJ L275/32 (25 October 2003), as amended.

² European Commission, Task Force for the Preparation and Conduct of the Negotiations with the United Kingdom under Article 50 TEU, *Revised text of the Political Declaration setting out the framework for the future relationship between the European Union and the United Kingdom as agreed at negotiators' level on 17 October 2019*, para.70. See also HM Government, *The Future Relationship with the EU: The UK's Approach to Negotiations* (February 2020, CP211), 22, Pt 2, para.14.

³ HM Treasury, *Budget 2018* (October 2018), 47. See also HMRC, Policy paper, *Carbon Emissions Tax* (29 October 2018), available at: <https://www.gov.uk/government/publications/carbon-emissions-tax/carbon-emissions-tax> [Accessed 23 September 2020].

⁴ UK Government, press release, *New Emissions Trading System proposal would see UK go further in tackling climate change* (1 June 2020), available at: <https://www.gov.uk/government/news/new-emissions-trading-system-proposal-would-see-uk-go-further-in-tackling-climate-change> [Accessed 23 September 2020]; Department for Business, Energy & Industrial Strategy, The Scottish Government, Welsh Government, and Department of Agriculture, Environment and Rural Affairs (Northern Ireland), *The future of UK carbon pricing: UK Government and Devolved Administrations' response* (June 2020), available at: <https://www.gov.uk/government/consultations/the-future-of-uk-carbon-pricing> [Accessed 23 September 2020]. See also Vivid Economics, *The Future of Carbon Pricing in the UK: Report prepared for the Committee on Climate Change: Final Report* (August 2019), 101. This report presents the UK carbon tax as a “fallback option”.

⁵ Second Reading of the Finance Bill, *Hansard*, HC, Vol 675, cols 129–130 (27 April 2020), comment by The Financial Secretary to the Treasury (Jesse Norman), available at: <https://hansard.parliament.uk/commons/2020-04-27/debates/C37146D2-C2C0-4146-A015-E038C1E439DA/FinanceBill#contribution-D4645A63-BC79-477E-96C7-4E812F836290> [Accessed 23 September 2020].

⁶ See also HMRC, Policy paper, *Changes to tax provisions for Carbon Emissions Tax* (11 March 2020), available at: <https://www.gov.uk/government/publications/changes-to-tax-provisions-for-carbon-emissions-tax/changes-to-tax-provisions-for-carbon-emissions-tax> [Accessed 23 September 2020].

⁷ See HM Treasury, *Finance Bill Explanatory Notes* (Explanatory Notes) (19 March 2020), available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/873637/Finance_Bill_2020_Explanatory_Notes.pdf [Accessed 2 September 2020], cl.92, Sch.11, Resolution 52, para.1, 170. See also letter of 4 June 2020 from the Financial Secretary to the Treasury to the Public Bill Committee, available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/890311/FST_Letter_to_PBC_Chairs_-_delegated_powers.pdf [Accessed 23 September 2020], regarding the clauses that introduce the power to make secondary legislation.

of a UK ETS. It authorises HM Treasury to make regulations which provide for the auctioning of allowances and the introduction of market stability mechanisms to limit price volatility.⁸

This short note first briefly describes the main features of the carbon emissions tax. Secondly, it highlights that the carbon emissions tax would mimic many design features of an ETS, which blurs the line between carbon taxation and emission trading. Thirdly, it discusses how such a carbon emissions tax could be the first step towards a simplified approach to carbon pricing in the UK. Finally, it concludes.

1. The main design features of the carbon emissions tax

The UK carbon emissions tax differs from traditional carbon taxes, which are usually designed as excise taxes levied on fuels by weight, volume or on actual emissions (the so-called “fuel approach”).⁹ The carbon emissions tax relies on an alternative approach, which is based on the measurement of the actual emissions of installations (the so-called “direct emissions approach”).¹⁰ The carbon emissions tax is an annual tax, which is charged, in relation to regulated installations, “if the amount of reported carbon emissions for a reporting period exceeds the emissions allowance for the period”.¹¹ In many ways, its design mimics the approach of the EU ETS, under which installations are required to surrender allowances to cover their total annual emissions. Under the EU ETS, most of the allowances are allocated through an auctioning system but some are allocated for free. In particular, the energy-intensive sectors at risk of carbon leakage benefit from free allowances.¹² The carbon emissions tax can be compared to the EU ETS in terms of its scope, its approach to carbon leakage and its carbon price.

First, installations to be subject to the carbon emissions tax should be broadly the same as those that are currently part of the EU ETS, with two main exceptions.¹³ First, power generators located in Northern Ireland would, in principle, remain part of the EU ETS.¹⁴ Secondly, the carbon emissions tax would not cover the aviation sector. This is not surprising given the legal limits that apply to the taxation of this sector under international law.¹⁵ Therefore, in order to meet the UK’s commitment to tackle the emissions of the aviation sector, additional ad hoc measures would need to be established.¹⁶

⁸ The Explanatory Notes, above fn.7 (Finance Bill 2020 cl.93, Resolution 53, para.12, 174) indicate that such a charging clause is necessary given that “Paragraph 5 of Schedule 2 of the Climate Change Act 2008 does not permit regulations made under section 44(1) to provide for allowances to be allocated in return for consideration”.

⁹ See the draft chapter on the design of a carbon tax for the *United Nations Handbook on Carbon Taxation*: United Nations, Committee of Experts on International Cooperation in Tax Matters, Twentieth session, Ch.3, “Designing a Carbon Tax – Carbon Taxation Handbook” (21 April 2020, E/C.18/2020/CRP.17), 16.

¹⁰ *United Nations Handbook on Carbon Taxation*, above fn.9, 26–27.

¹¹ FA 2019 s.70(1).

¹² See the consolidated text of Directive 2003/87/EC, above fn.1, Art.10b (as inserted by Directive (EU) 2018/410 of the European Parliament and of the Council of 14 March 2018 amending Directive 2003/87/EC to enhance cost-effective emission reductions and low-carbon investments and Decision (EU) 2015/1814 [2018] OJ L76 (19 March 2018).

¹³ FA 2019 s.77(1); HM Treasury, *Finance (No. 3) Bill Explanatory Notes* (7 November 2018), cl.68, para.5, 211.

¹⁴ The Single Electricity Market would remain operational in Northern Ireland as provided for in the Ireland/Northern Ireland Protocol. See Department for Business, Energy & Industrial Strategy, *Guidance, Meeting climate change requirements from 1 January 2021* (updated 9 September 2020), available at: <https://www.gov.uk/government/publications/meeting-climate-change-requirements-if-theres-no-brexite-deal/meeting-climate-change-requirements-if-theres-no-brexite-deal> [Accessed 23 September 2020].

¹⁵ See the provisions on the exemptions of aviation fuel on board an aircraft in the Convention on International Civil Aviation done at Chicago, 7 December 1944 (‘Chicago Convention’) (Art.24) and the similar provisions that are included in bilateral air transport agreements.

¹⁶ In the hypothesis of a UK ETS, the aviation sector would be included in the scheme (see *The future of UK carbon pricing: UK Government and Devolved Administrations’ response*, above fn.4, Ch.3).

For the installations subject to the carbon emissions tax, current reporting requirements for installations should be maintained and be based on existing emissions reporting arrangements.¹⁷

Secondly, the threshold for the determination of the taxable emissions—the so-called “emissions allowance”—should play a similar role to that of the allowances that are allocated for free under the EU ETS.¹⁸ Its objective is to allow “the government to maintain similar arrangements to the EU ETS for industrial installations deemed to be exposed to significant risk of carbon leakage, to support their competitiveness”.¹⁹ The “emissions allowance” for the carbon emissions tax remains to be defined. The Finance Act 2019 provides that the “emissions allowance” should be determined by reference to an amount of emissions to be “specified by or under, or determined in accordance with, regulations made by the Commissioners for Her Majesty’s Revenue and Customs”.²⁰ Setting the threshold of emissions subject to the tax or the EU ETS at the “right” level is key under both mechanisms. Under an ETS, if the allocation of free allowances is too generous, installations might be able to benefit from windfall profits without having to reduce the amount of carbon emissions that they generate. Similarly, under a carbon emissions tax, if the threshold of “emissions allowance” is set too “high”, very few installations would end up being subject to the tax, which would make it ineffective (no emissions would be taxable).

To the extent that the method used to determine the threshold of taxable emissions is comparable to the methods used under the EU ETS to set out the levels of free allowances, the two mechanisms will achieve comparable outcomes for the installations with reported emissions higher than their allocated free allowances or “emissions allowance” threshold. However, for the installations with lower reported emissions, the mechanisms could lead to different outcomes. Under an ETS, these firms would, in principle, be rewarded: they would be incentivised to cut their emissions further in order to be able to sell their excessive free allowances. In comparison, a carbon emissions tax would not have this incentive effect, given that the tax would not be “credited or repaid” if the “emission allowances were unused”.²¹ To compensate for the absence of such an incentive effect, the Government is now considering the introduction of a payments system to “reward decarbonization from main scheme installations” as well as special arrangements for small emitters.²²

Thirdly, the tax rate of the carbon emissions tax has been set at £16 per tonne of carbon dioxide equivalent²³ in order to “maintain a stable carbon price for the installations that were subject to the EU ETS” and “replace the revenue lost from the auctioning of EU allowances”.²⁴ This tax rate was established in 2018 on the basis of an average of the carbon price under the ETS over a period of six months and a forecast for the next six months.²⁵ The tax rate has not been updated since 2018, which is problematic given the high volatility of carbon prices under the EU ETS. At the very least, the tax rate should have been updated in FA 2020 to better reflect the higher average carbon price under the EU ETS in 2019 in comparison to 2018 prices.²⁶ Moreover, if the carbon emissions tax is introduced and maintained, its tax rate should be reassessed in the coming years, independently of the EU ETS carbon

¹⁷ FA 2019 ss.71 and 72.

¹⁸ HMRC and HM Treasury, *Carbon Emissions Tax: Consultation* (21 July 2020), 11, point 2.22.

¹⁹ *Finance (No. 3) Bill Explanatory Notes*, above fn.14, cl.68, para.5, 211.

²⁰ FA 2019 s.73.

²¹ HMRC, *Technical Note - Carbon Emissions Tax* (published 29 October 2018; last updated 3 September 2019), available at: <https://www.gov.uk/government/publications/carbon-emissions-tax-technical-note> [Accessed 23 September 2020], (in particular Ch.3, 6). Please note that this publication was withdrawn on 8 June 2020. A new technical note should be published before January 2021.

²² See *Carbon Emissions Tax: Consultation*, above fn.19, 17, points 2.45–2.50.

²³ FA 2019 s.70(3).

²⁴ HMRC, Policy paper, *Changes to tax provisions for Carbon Emissions tax* (11 March 2020), available at: <https://www.gov.uk/government/publications/changes-to-tax-provisions-for-carbon-emissions-tax/changes-to-tax-provisions-for-carbon-emissions-tax> [Accessed 23 September 2020] (see under the section on “policy objective”).

²⁵ See House of Lords, Select Committee on the European Union, Sub-Committee on Energy and Environment, *Corrected oral evidence: Post-Brexit carbon pricing* (27 February 2019) (see R. Jenrick’s answers to questions 25 and 29).

price. The UK should aim for a carbon price sufficiently high to meet its commitment to reach a net-zero emissions target by 2050 and the proposed £16 does not seem to meet this objective.²⁷ If the objective is to encourage investments in low carbon technologies, it is key that it is sufficiently credible that the carbon price will increase and remain high.

FA 2020 contains several amendments to FA 2019. Some of these amendments are just minor technical corrections and updates to FA 2019 but some others are substantial. For example, FA 2020 provides the Treasury with the power to exclude certain installations from the carbon emissions tax,²⁸ such as power generators located in Northern Ireland.²⁹ Moreover, FA 2020 extends the power of HMRC to make further provision about the carbon emissions tax, such as the power to make provision for “the imposition of civil penalties” in case of non-compliance.³⁰ It also adds a penalty for failure to make payments on time.³¹

2. A carbon emissions tax versus a standalone UK emissions trading scheme

The UK’s twin-track approach raises the question of the advantages and disadvantages of a carbon emissions tax in comparison to a standalone UK ETS. This section highlights that the general arguments usually put forward in favour of either of these instruments might not apply to the UK’s proposals. Given their common objective of ensuring a stable carbon price in case the EU ETS no longer applies in the UK as of January 2021, the two options differ less from each other than they generally do.

The general advantages and disadvantages of carbon pricing in comparison with emissions trading are well known.³² First, the design and administration of carbon taxes is usually considered to be relatively simple in comparison to emissions trading.³³ Secondly, carbon taxation and emissions trading are considered to provide different levels of certainty in terms of price and emission targets. Carbon taxes provide certainty with regard to the abatement cost of carbon emissions. Under a carbon tax, the tax rate defines the abatement cost whereas, for emissions trading, the cost of permits is defined by the market on the condition that it is competitive. In contrast, emissions trading schemes provide certainty with regard to the reduction in emissions levels that can be achieved: the total emissions generated on a yearly basis should correspond to the amount of emissions allowances that have been allocated by the authority, either for free or through auctioning. Thirdly, emissions trading

²⁶ Questions on whether the tax rate would be reviewed have been asked to the Ministers of State at the Department for Business, Energy and Industrial Strategy. See House of Lords, letter of 4 September 2019 from Lord Teverson to The Rt Hon Kwasi Kwarteng MP (“Post-Brexit carbon pricing and implications of a ‘no deal’ Brexit”), available at: <https://www.parliament.uk/documents/lords-committees/eu-energy-environment-subcommittee/no-deal/LTtoKK-carbonpricingandnodeal-040919.pdf> [Accessed XXX]; House of Lords, letter of 15 May 2019 from Lord Teverson to the Rt Hon Claire Perry MP (“Post-Brexit carbon pricing”), available at: <https://www.parliament.uk/documents/lords-committees/eu-energy-environment-subcommittee/post-brexit-carbon-pricing/LTtoCP-carbon%20pricing-15.05.19.pdf> [Accessed XXX].

²⁷ The carbon price support (CPS) should be added on top of the carbon emissions tax to determine the total carbon price but, even then, the rate seems insufficient to meet the UK’s climate commitments. See J. Burke, R. Byrnes and S. Fankhauser, Policy report, *How to price carbon to reach net-zero emissions in the UK* (May 2019), available at: http://www.lse.ac.uk/GranthamInstitute/wp-content/uploads/2019/05/GRI_POLICY-REPORT_How-to-price-carbon-to-reach-net-zero-emissions-in-the-UK.pdf [Accessed 23 September 2020]. This report indicates that “a shadow price consistent with a net-zero target would start at £50 per tonne of carbon dioxide (tCO₂) (with a range of £40–100) in 2020” (4).

²⁸ FA 2020 Sch.12, para.3.

²⁹ Finance Bill, Eighth Sitting, col 209 (16 June 2020). For power generators located in Northern Ireland, see fn.15.

³⁰ FA 2020 Sch.12, para.4(2).

³¹ FA 2020 Sch.12, para.9.

³² This entire paragraph is based on D. Fullerton, A. Leicester and S. Smith, Ch.5, “Environmental Taxes” in S. Adam, et al. (eds), *Dimensions of Tax Design: The Mirrlees Review* (Oxford: OUP, 2010), s.5.2.4., 436–439.

³³ This point is mentioned in Vivid Economics, above fn.4, 4–5.

systems are considered more cost-efficient because they allow for an efficient allocation of emissions abatement between firms under the condition that a competitive carbon market is in place.³⁴ Fourthly, both mechanisms differ with regard to the institutional provisions that apply to their adoption and implementation. For example, at the EU level, unanimity is required for the adoption of taxes, but qualified majority voting requirements apply to the adoption of environmental regulation, including the emissions trading scheme. In the UK, a carbon emissions tax would be a reserved matter for the UK Government, which has raised some concerns in Wales and Scotland.³⁵

Aside from the institutional aspects, the differences that generally distinguish carbon taxes from emissions trading schemes do not fully apply to the UK proposals for a carbon emissions tax or a standalone UK ETS. First, although most carbon taxes are generally simpler to administer than emissions trading schemes, it might not hold true for a carbon emissions tax. Indeed, the “direct emissions approach” that underlies the carbon emissions tax is characterised by an administrative complexity similar to that which characterises emissions trading.³⁶ Secondly, both a carbon emissions tax and a standalone UK ETS could provide for some level of certainty both in respect to the level of carbon price and emissions reduction. Under a well-designed carbon tax, the tax rate could be modified to achieve the desirable emissions reduction levels in case the initial tax rate was too low to achieve it. Similarly, a well-designed standalone ETS could include an “auction reserve price” ensuring a “minimum carbon price signal” or other mechanisms allowing for adjustments to be made to the supply of allowances in case the price level is considered too low.³⁷ Thirdly, the alleged advantage of emissions trading systems in terms of cost-efficiency might not apply to a standalone UK ETS. Such advantage is conditional upon the existence of a competitive market and the UK market for carbon emissions might be too small for that.³⁸ Finally, the two UK proposals for carbon pricing present additional differences due to their specific design features. In particular, their scope would be slightly different: a UK standalone ETS would include the aviation sector, which would be excluded under the carbon emissions tax.

The choice to be made between the carbon emissions tax and the standalone UK ETS should be informed by their distinguishing features, which do not always match the textbook example of carbon taxes and emissions trading. Although the two mechanisms differ on several grounds, the carbon emissions tax differs less from a standalone UK ETS than would a traditional carbon tax based on a “fuel approach”. Therefore, the decision on which of these two instruments should prevail in the case of a no-deal Brexit might not be as crucial as the decision on how to reform the UK carbon pricing policy in the long run. This question is analysed in the next section.

³⁴ Fullerton, Leicester and Smith, above fn.33, 438.

³⁵ Welsh Government, press release, *EU Emissions Trading System (EU ETS)* (15 October 2018), available at: <https://gov.wales/eu-emissions-trading-system-eu-ets> [Accessed 23 September 2020]. See also House of Lords, Select Committee on the European Union, Sub-Committee on Energy and Environment, *Corrected oral evidence: Post-Brexit carbon pricing*, above fn.26, question 31.

³⁶ *United Nations Handbook on Carbon Taxation*, above fn.9, 26–27 and 33.

³⁷ The Explanatory Notes, above fn.7, (cl.93, Resolution 53, para.13, 174) indicate that Finance Bill 2020 cl.93 allows for the implementation of such “market stability mechanisms”, which could “include a Cost Containment Mechanism (CCM) to respond to any significant short-term price spikes and an Auction Reserve Price (ARP)”. See also the observation on “supply adjustment mechanisms” in Vivid Economics, above fn.4, 89–90. See also F. Flues and K. van Dender, “Carbon pricing design: Effectiveness, efficiency and feasibility: An investment perspective” (2020) OECD Taxation Working Papers No.48.

³⁸ See the observations regarding market stability, competitiveness, exposure to shocks and carbon market liquidity in Vivid Economics, above fn.4, 3–4. See also J. Burke, B. Doda, L. Taschini and L. Mattauch, *The future of carbon pricing: A joint submission to the UK Government by the Grantham Research Institute on Climate Change and the Environment, the Institute for New Economic Thinking at the Oxford Martin School, and the Environmental Change Institute* (August 2019), available at: http://www.lse.ac.uk/GranthamInstitute/wp-content/uploads/2019/07/GRI_Consultation-response-on-the-future-of-carbon-pricing.pdf [Accessed 23 September 2020].

3. Brexit: a way to simplify the UK's carbon pricing policy?

The UK's approach to carbon pricing has been based on a complex "set of interlocking mechanisms", including taxes and emissions trading instruments.³⁹ In addition to the EU ETS, a carbon tax is levied on electricity generation (the so-called "carbon price support" (CPS) rate introduced by Schedule 32 to the Finance Act 2012. Moreover, other taxes are imposed on the use of energy. For example, the climate change levy (CCL), introduced in 2001, is also imposed on the non-domestic use of electricity, gas, liquefied petroleum gas and solid fuels.⁴⁰

As a member of the EU, the UK had to comply with EU law requirements and could not easily change the design of the EU ETS. In this context, its complex and multi-layered approach to carbon pricing might have been justified.⁴¹ The CPS has been adopted on top of the EU ETS in order to guarantee a sufficiently high carbon price (referred to as the "carbon price floor") against the background of a "too low" carbon price under the EU ETS.⁴² Although the CPS has added complexity to the UK's carbon pricing policy, it has played a key role in sustaining a relatively high carbon price in relation to electricity in the UK, which has allowed for a boost in "low-carbon investments".⁴³

The introduction of either a standalone UK ETS or a carbon emissions tax will not necessarily lead to a simplification of the UK's complex carbon pricing policy. However, the opportunity for such a simplified approach should be taken seriously if the UK's climate policy becomes independent from the EU ETS.⁴⁴

If the UK chooses to adopt a standalone UK ETS as of January 2021, the CPS could be abandoned. The UK would be able to design its ETS independently of the EU. This standalone ETS could include a supply adjustment mechanism that would provide for a minimum carbon price and, thus, fulfil the same role as the CPS.⁴⁵ Such a design would simplify the UK's carbon pricing policy by integrating two of its key instruments that apply to emissions from non-domestic energy use. Carbon taxes could nevertheless remain a relevant tool for carbon pricing, for example to cover emissions that are traditionally left out of the scope of an ETS, such as the emissions related to domestic energy use (for example, those linked to heating) or the emissions generated by small and medium-sized businesses.

³⁹ S. Smith and J. Swierzbinski, "Assessing the performance of the UK Emissions Trading Scheme" (2007) 37 *Environmental and Resource Economics* 131, 133. See also J. Mirrlees, et al., Ch.11, "Tax and Climate Change" in J. Mirrlees, et al. (eds), *Tax by Design: The Mirrlees Review* (Oxford: OUP, 2011).

⁴⁰ FA 2000 s.30 and Sch.6.

⁴¹ Pollitt and Chyong explain that "[f]rustration with the lack of tightness of the EU ETS prompted the UK to introduce an additional carbon tax on fossil fuels for electricity production in 2013 (the carbon price floor)": see M.G. Pollitt and K. Chyong, *Brexit and its implications for British and EU Energy and Climate Policy*, Project Report, Centre on Regulation in Europe (22 November 2017), 41.

⁴² On the CPS and carbon price floor, see D. Hirst, *Carbon Price Floor (CPF) and the price support mechanism*, House of Commons Library, Briefing Paper No.05927 (8 January 2018).

⁴³ On the effects of the CPS, see Vivid Economics, above fn.4, 39, referring to G. Perino, R.A. Ritz and A. van Benthem, "Understanding Overlapping Policies: Internal Carbon Leakage and the Punctured Waterbad" (2019) EBER Working Paper No.25643. See also A. Varma, "UK's climate change levy: cost effectiveness, competitiveness and environmental impacts" (2003) 31 *Energy Policy* 60.

⁴⁴ Hepburn and Teytelboym have also suggested that the UK carbon pricing policy might become stronger after Brexit: "...action on climate change in Britain is more likely to be weaker than stronger. The exception, perhaps, might be carbon pricing": see C. Hepburn and A. Teytelboym, "Climate change policy after Brexit" (2017) 33(1) *Oxford Review of Economic Policy* 144, 145. Similarly, Sorrell has described Brexit as "an opportunity (a policy window) for radical policy change in this area" (see S. Sorrell, *Is Brexit an opportunity to rethink UK carbon pricing?* (20 September 2016, Centre on Innovation and Energy Demand), available at: <http://www.cied.ac.uk/blog/is-brexit-an-opportunity-to-rethink-uk-carbon-pricing/> [Accessed 23 September 2020]).

⁴⁵ It has also been suggested that the CCL might no longer be necessary if the scope of the standalone ETS is sufficiently broad. See Vivid Economics, above fn.4, 77.

Based on the hypothesis that the carbon emissions tax is to be introduced in January 2021, carbon pricing in the UK would no longer include a mix of emissions trading and tax instruments but would rely only on tax instruments. Such a system of carbon pricing would still be complex, including as it would a carbon emissions tax, a CPS and other taxes on energy use. Therefore, over the longer term, the UK could consider integrating its different carbon taxes and taxes on energy use into a simpler environmental tax on energy.⁴⁶ The CPS and the carbon emission tax could be merged into either a carbon emissions tax with a higher tax rate or into a broad carbon tax based on a “fuel approach”. Given that the latter option is relatively simple in comparison to the former, a reform in favour of a broad-based carbon tax on energy use based on a “fuel approach” would have the highest potential for simplifying the UK’s carbon pricing policy.

Conclusion

The UK has been a frontrunner of carbon pricing with the adoption of a UK emissions trading scheme in the early 2000s in anticipation of the introduction of the EU ETS. One objective of this early move was to provide UK businesses with a first-mover advantage. Twenty years later, the UK is anticipating the reverse situation, namely a potential abrupt end of the EU ETS in the case of a no-deal scenario. The UK has adopted a precautionary approach with two main proposals. However, a choice between these two proposals should be made to avoid additional confusion regarding the future of the UK’s carbon pricing policy. Moreover, many aspects of the two proposals need to be clarified. There are a few months left for the UK to make these two proposals operational. It might be better to concentrate on the details of one or other of these two options rather than come up with two blurry proposals. Finally, in the case of a no-deal, the UK will not just need to prepare for the transition out of the EU ETS but it will also have to anticipate how new European proposals on carbon pricing, including border carbon adjustments, might affect its climate change policy.⁴⁷

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⁴⁶ See Vivid Economics, above fn.4, 4 and 77. Hepburn and Teytelboym, above fn.45, 149, have suggested that one way forward would be to “simply transition the Carbon Price Floor into a carbon tax”. Note that legal limits apply to the taxation of the aviation sector. It might be easier to internalise the emissions of the aviation sector through a non-fiscal instrument.

⁴⁷ On the interaction between the EU Green deal and the UK’s climate policy, see House of Lords, Select Committee on the European Union, Sub-Committee on Energy and Environment, *Corrected oral evidence: EU Green Deal* (4 March 2020), available at: <https://committees.parliament.uk/oralevidence/118/default/> [Accessed 23 September 2020]. See also Lords Select Committee, News, *What does the EU’s carbon border adjustment mean for the UK?* (26 February 2020), available at: <https://committees.parliament.uk/committee/335/eu-energy-and-environment-subcommittee/news/111614/what-does-the-eus-carbon-border-adjustment-mean-for-the-uk/> [Accessed 30 September 2020].

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