Dear Cabinet Secretary

EU ETS – EU Exit Regulations

Thank you for your letter of 2 October regarding the EU ETS – EU Exit Regulations.

The Committee looks forward to discussing this with you on 24 October. In advance of that meeting the Committee would find it helpful to have a response to the questions set out in the annex to this letter. Given the short timescales we are working to we request the response by Friday 12 October.

Yours sincerely

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Convener
Environment, Climate Change and Land Reform Committee
NOTIFICATION TO CONSENT - EU EMISSIONS TRADING SCHEME

Questions for the Scottish Government

Timing

• The notification records that the 28 days for Scottish Parliament scrutiny referred to in the agreed protocol have not been given. Since the UK Government does not intend to lay this SI until 14 November, can the Scottish Government advise why consent is required by 29 October?
• What would be the consequences of the Scottish Parliament failing to report to the Scottish Government by 29 October?
• What would be the consequences of the Scottish Government failing to report to the UK Government by 29 October?

Identification of legislation with deficiencies

• The notification states that the EU ETS is established by over 54 pieces of legislation. The only piece of UK legislation mentioned in the notification is the UK Greenhouse Gas Regulations 2012. Is that the only piece of legislation which the proposed SI will change? If there are others, please specify them.

Identification of deficiencies

• Has the Scottish Government seen a draft of the proposed SI and, if so, could the Scottish Government let the Committee see this?
• Can the Scottish Government provide more detail (including examples) on the type of deficiency which will be corrected by the proposed SI and what specific amendments are proposed?

Stakeholder engagement/consultation

• The notification mentions that stakeholders' views have not focused on no-deal scenario arrangements. What stakeholder engagement/consultation have the Scottish and UK Governments undertaken on this proposed SI?
• What were stakeholders' views and how have they been taken into account?
• Do the detailed options papers developed by the UK Emissions Trading Group (ETG) include options in the event of a no deal scenario? Can more detail of these papers be shared with the Committee now?

Continued monitoring and reporting requirements

• Can the Scottish Government provide more detail on which monitoring, reporting and enforcement requirements are proposed to be retained under the proposed SI?
• Will the proposed SI result in any changes to the monitoring, reporting and enforcement requirements referred to in the notification, including:
  o Which bodies or authorities traded sector participants will be accountable to?
Who will be responsible for enforcement after EU exit?
Will the role of SEPA remain exactly as it currently is?
The timing for monitoring and reporting?
The way in which reported information is published (including how it is made available to the public)?

- What would be the impact of not monitoring and reporting emissions according to the current technical rules as a set out in EU regulations?

**Legal basis for membership of the EU ETS**

- What is the precise legal basis for the UK’s membership of the EU ETS?
- Do the European Commission and UK Government consider membership of the EU ETS to be tied to membership of the Single Market?
- Does the Scottish Government share that view?
- What precedents are there for non-EU membership of the EU ETS?

**Timing of Regulations with regard to trading phases and annual cycles**

- Is it the UK Government’s intention for the proposed SI to come into force on 29th March 2019 i.e. immediately following the UK exiting the EU?
- What implications does the timing of the SI have for the participation in annual cycles of the EU ETS, regarding purchasing and surrendering allowances?
- Is it the case that the ‘compliance cycle’ for the ETS means that the UK will have left the EU before its businesses are required to report their annual 2018 emissions (31 March 2019) or to surrender the appropriate number of allowances (30 April 2019)?
- If companies have allowances that could be traded are they prevented from doing so?
- The EU ETS is in the middle of its third trading phase which runs until the end of 2020. Has the Scottish Government explored the possibility with the UK Government of UK participants remaining in the scheme until the end of Phase 3?

**Implications for businesses**

- A number of institutions participate in the EU ETS for commodity trading purposes, such as banks and hedge funds. Has the Scottish Government undertaken any assessment of the levels of participation of the financial sector in Scotland in the EU ETS and the impact of leaving the EU in a no deal scenario?
- What would the financial implications be for industrial users of the EU ETS e.g. Ineos at Grangemouth?
- What would the cost of rising emissions as a result of leaving the EU ETS be?

**Implications of the Commission Regulation of 12 February 2018**

- It is the Committee’s understanding that as a result of the Commission Regulation of 12 February 2018 in preparation for the UK’s potential departure from the EU ETS, UK-issued allowances (previously entirely fungible with other allowances across the scheme) are now geographically
denominated. What assessment has the Scottish or UK Government made of the impact of this change on Scottish participants?

- Are allowances held by UK participants already at risk of becoming devalued?

**UK Government Technical Note relating to the EU ETS**

- Is the Scottish Government in discussions with the UK Government regarding when this Technical Note will be published?
- Does the Scottish Government expect to have reviewed this Note and agreed its content before it is published?
- When does the Scottish Government expect this to be published?

**Commitment to environmental standards**

- Both the Scottish and UK Governments have committed to maintaining environmental standards after Brexit. Can this commitment be met if there is no replacement or equivalent mechanism in place (including an interim mechanism) by 29th March 2019?
- The notification states that “The EU ETS is predicated on the polluter pays principle by requiring the traded sector to account for their CO2 emissions. The approach in the UK SI ensures that the traded sector remains accountable in the event of no-deal, by continuing to monitor and report their emissions.” Given that the notification recognises that the key delivery mechanism of the EU ETS (i.e. the purchasing and surrendering of allowances) will cease as a result of the proposed changes, how will continued monitoring and reporting of emissions alone ensure that the traded sector remains accountable for their emissions as required by the polluter-pays principle?

**Assessment of options for an EU ETS replacement (including interim arrangements)**

- What is the Scottish Government’s policy preference regarding the continuation of the emissions trading?
- Does the Scottish Government have a view, in the event of a no deal scenario, on whether the relevant Scottish and UK authorities have the capacity to mirror the workings of the EU ETS?
- If continued membership of the EU ETS is not a viable option following the UK’s exit from the EU, what options are available to replicate its functions?
- Can the Scottish Government provide more detail on why its policy preference is to continue with UK wide arrangements?
- What are the benefits and risks of developing a replacement scheme at a UK level rather than pursuing a domestic scheme?
- has the Scottish Government explored the possibility of Scottish participants seeking their own arrangements e.g. to continue membership of the EU ETS on their own and why has a domestic scheme been discounted?
- How does the Scottish Government plan to engage the Scottish Parliament, stakeholders and the general public in developing a replacement mechanism in the event of the UK leaving the EU ETS in March 2019?
• Have interim arrangements been explored with EU ETS participants which would maintain the carbon price even in the event of no deal?
• Does the Scottish Government have a view, assuming the UK leaves the EU ETS in March 2019 under a no deal scenario, on the likely timescales for introducing a new mechanism (or pilot mechanism) that will deliver the equivalent level of environmental protection?

Implications for GHG emissions targets and low carbon investment

• The notification states that The Climate Change Plan (Report on Policies and Proposals covering 2018-32) considers that participation in the EU ETS would contribute 17% towards our targets, and it is not clear what the approach set out in the UK SI would mean for the rate of decarbonisation from the traded sector. What assessment has the Scottish Government undertaken of the potential short, medium and long-term implications of a period of non-membership of the EU ETS for Scotland’s progress towards its statutory climate targets?
• Has the Scottish or UK Government requested or received advice from the Committee on Climate Change, or other advisory bodies on the potential impacts of the UK leaving the EU ETS on national progress towards GHG emission reduction targets?
• The ETS Directive requires a proportion of revenues from auctions to be spent on a defined list of options. The Committee understands that under this requirement the UK Government has allocated funding to low carbon schemes such as the renewable heat incentive. Has the Scottish Government undertaken any assessment of the potential risks of loss of Government revenue from auctions of allowances on funding available for low carbon investment in Scotland?
• Given the notification states that the proposed SI will reduce costs for Scottish participants given they no longer require EU ETS emissions allowances, has the Scottish Government considered whether this will create a competitive advantage for carbon-intensive industries, and whether this may result in knock on environmental or economic impacts (including on non-participants)?
• How does the SI relate to the provisions in the Climate Change (Emissions Reduction Targets) (Scotland) Bill on the emissions accounting (Part 2)? As there will be no carbon credits, is the effect of this that there is nothing to account for the purposes of assessing progress to targets?
• What are the implications for delivery of the Climate Change Plan 2018-2032?
• What are stakeholders views on this?
• What is the effect for companies which are incorporated elsewhere in the EU but which emit greenhouse gases in Scotland?