# Improving the Integrity of the CRC through Allowance Transfers

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The CRC Energy Efficiency Scheme (formerly known as the Carbon Reduction Commitment) is a regulatory mechanism that aims to improve energy efficiency in large public and private sector organisations and to reduce greenhouse gas emissions from the UK.

However, the design of the CRC – in particular its relationship with the EU Emissions Trading Scheme (EU ETS), Europe's flagship greenhouse gas abatement mechanism, means that while it may encourage energy efficiency it is fundamentally flawed as a scheme for reducing greenhouse gas emissions. The government has recently announced a review of the scheme.

So, what's the problem? The problem stems from the fact that most of the emissions covered by the scheme are caused by the generation of electricity in plants already regulated by the EU ETS. Power generators hold EU ETS allowances to cover their expected emissions, so when a power user improves efficiency or reduces electricity consumption by other means (perhaps through the installation of on-site generation), the power company is left with surplus emissions allowances that it can use – either to sell to companies that want to emit more, or to allow it to produce power with cheaper, higher carbon fuels such as coal. The "downstream" greenhouse gas benefits of efficiency or local generation are therefore negated by the surplus of "upstream" allowances.

This problem applies to all downstream electricity saving measures within the EU, including measures to encourage local renewable generation.

One solution to this problem would be to allow participants to claim the surplus allowances arising from efficiency (and possibly other abatement measures) from their power providers, and to sell these back to the national authorities responsible for issuing / auctioning the EU ETS allowances to the power generators. These allowances would then be retired, so as to take them out of circulation.

A process for allowance transfer would have several positive effects:

- It would provide an additional financial incentive for electricity users to actively monitor, manage and reduce their electricity use in a way that produces demonstrable reductions in emissions;
- The price of carbon would become much more apparent and consistent throughout the economy;
- It would turn the CRC from an energy efficiency scheme to an energy efficiency AND greenhouse gas abatement scheme;
- It would help tighten the oversupply of allowances within the EU ETS.

Allowance transfer would enable some interesting developments:

- The government would become a buyer and a seller of EU allowances. At present it sells some allowances and others are "grandfathered" – issued free. There is a question of what the government should do with revenues from allowance auctions. The re-purchase and retiral of surplus allowances through a transfer mechanism is an obvious use with readily quantified greenhouse gas impacts;
- The fact that electricity users would have a strong financial incentive to participate may make compulsive participation in the CRC unnecessary. This could substantially reduce the administrative burden;
- The fact that electricity users would be claiming allowances from their power providers would mean that the government would act as a facilitator or arbitrator of terms rather than pushing energy efficiency advice on sometimes deaf ears;
- Over time it may be possible to extend the scheme to incorporate emission reductions from other activities not covered by the EU ETS, for example emissions from transport, waste disposal, agriculture and forestry. It would clearly be necessary to adjust the allocation process in line with such developments but this does provide a way of bringing a wide range of sectors within the scope of the trading mechanism in a controlled and incremental manner.

For further information about the potential impacts of allowance transfers on greenhouse gas mitigation and accounting, please contact:

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