

# The New UK Carbon Reduction Scheme

## Energy Alert

April 30, 2010

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On April 1, 2010, the new mandatory CRC (formerly known as the Carbon Reduction Commitment) energy efficiency emissions trading scheme came into force in the UK.

The aim of the CRC Energy Efficiency Scheme (CRC) is to reduce CO<sub>2</sub> emissions and increase the energy efficiency of those large businesses and public sector organizations that the UK government believes are responsible for an estimated 10 percent of the UK's overall greenhouse gas emissions. It is expected that the implementation of the CRC, through the CRC Energy Efficiency Scheme Order 2010, will contribute significantly towards achieving the UK's target, under the Climate Change Act 2008, of reducing its greenhouse gas emissions by 80 percent before 2050 (compared to 1990 levels). This, in turn, will assist the UK in achieving its international targets under the Kyoto Protocol and other EU CO<sub>2</sub> reduction targets and is aimed at putting the UK at the forefront of the green technology revolution on the international stage. The CRC runs alongside, and is intended to conform with, the EU Emissions Trading Scheme—the former dealing with large non-energy intensive businesses and public sector organizations on a UK national level, while the latter deals with energy intensive industries (such as manufacturing and refining) on an EU-wide basis.

The CRC is divided into seven Phases beginning on April 1, 2010, each of which lasts for approximately seven years (except for the first Phase, which will last three years and be known as the Introductory Phase). There is also a deliberate two-year overlap between each Phase at the beginning and the end of each Phase. Each of the seven Phases is further divided into “Compliance Years,” which run from April 1 to March 31. During the Introductory Phase, the UK government will sell an unlimited number of Allowances at a fixed price of £12 per ton of CO<sub>2</sub>, while, in subsequent Phases, the UK government will auction a limited number of Allowances annually to encourage participants to reduce their CO<sub>2</sub> emissions. The Allowances may also be bought and sold by participants in the secondary market. Participants will be required to buy in advance the amount of Allowances that they expect to require to cover their emissions in any relevant Compliance Year and ultimately to surrender those Allowances to the Environment Agency, the administrator of the CRC.

An incentivization mechanism has been incorporated into the CRC whereby, inter alia, a portion of revenues from the CRC will be recycled back to the participants of the CRC as a bonus after six months. In this way, those participants whose energy efficiency improves each year will receive a larger payment than those participants whose energy efficiency worsens or does not improve.

The UK government anticipates that approximately 5,000 organizations will fall within the ambit of the CRC, primarily those whose annual electricity bills will amount to £500,000 or over. In addition, it is



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likely that an additional 20,000 organizations (though not formally participating in the CRC) will nevertheless be required to submit information to the Environment Agency regarding their energy efficiency. These organizations are expected to include large retailers, hotel chains, large offices, utility companies, hospitals, educational establishments, government departments, joint ventures, partnerships, private equity funds and franchises; they may also cover overseas companies that have operations in the UK.

Penalties for individuals failing to comply with the new CRC are potentially severe and can include a maximum of two years' imprisonment and unlimited fines.

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