
CARBON REDUCTION COMMITMENT – ENERGY EFFICIENCY SCHEME

**Responsible Cabinet Members –
Councillor Nick Wallis,
Sustainable Environment & Climate Change Portfolio
Councillor Chris McEwan, Efficiency & Resources Portfolio**

**Responsible Directors
Richard Alty, Assistant Chief Executive (Regeneration)
Paul Wildsmith, Director of Corporate Services**

SUMMARY REPORT

Purpose of the Report

1. The purpose of this report is to give Cabinet a brief outline of the new Carbon Reduction Commitment Energy Efficiency Scheme (CRC) and to seek delegated powers for the Director of Corporate Services to take the necessary actions to manage the scheme.

Summary

2. The CRC is a new mandatory emissions trading scheme for the UK that comes into force from April 2010 and aims to reduce carbon dioxide emissions through energy efficiency.
3. The scheme requires each participant member to purchase allowances for energy consumed. Income generated from the sale of allowances is then recycled to participants through a payment based on their position within the schemes league table, which can result in net cost of net gain to individual participating organisations. This provides an incentive to member organisations to reduce their energy consumption. The net cost or gain to the Council cannot be meaningfully estimated at this stage, though the range of potential implications can be accommodated within the medium term financial plan.

Recommendation

4. It is recommended that:
 - (a) Cabinet note the content of this report.
 - (b) That the Scheme of Delegation to officers be amended to include a power for the Director of Corporate Services under A Financial Matters as a new item 17, as follows:
To buy and sell allowances under the Carbon Reduction Commitment Scheme.

Reasons

5. The recommendations are supported by the following reasons:

- (a) To ensure that Darlington Borough Council comply with the new CRC Energy Efficiency Scheme.
- (b) To maximise the benefits of trading by allowing quick decisions to be made in line with day to day changing market conditions.

Richard Alty
Assistant Chief Executive, Regeneration

Paul Wildsmith
Director of Corporate Services

Background Papers

Department for Energy Efficiency and Climate Change – Consultation on the draft order to implement the Carbon Reduction Commitment.

Brett Nielsen 2907
Kelvin McDade 2441

S17 Crime and Disorder	This report has no implications for crime and disorder
Health and Wellbeing	There are no issues which this report needs to address
Sustainability	The introduction of the Carbon Reduction Commitment scheme encourages all participants to improve their energy efficiency and therefore reduce consumption. This fits in with the Council's agreed policies on energy efficiency and contributes towards the Council's 10:10 campaign.
Diversity	There are no issues which this report needs to address
Wards Affected	No direct implications
Groups Affected	No direct implications
Budget and Policy Framework	This report does not recommend a change to the budget or policy framework
Key Decision	The proposals do not represent a key decision
Urgent Decision	No
One Darlington: Perfectly Placed	There are no issues which this report needs to address
Efficiency	No direct implications. However, projects aimed at reducing energy consumption will contribute to reduced costs

MAIN REPORT

Introduction

6. The CRC is a new mandatory emissions trading scheme for the UK that aims to reduce carbon dioxide emissions through energy efficiency.
7. Organisations will have to monitor their energy use and purchase allowances. The more an organisation emits the more allowances it has to purchase providing a direct incentive to reduce energy use emissions.
8. A council's energy consumption will cover all sites the Authority occupies or owns including schools, although housing stock is excluded. There are still a number of issues to be resolved with regard to exactly what properties are included within our portfolio, which will either require a local decision or confirmation in final Government guidance.
9. The Environment Agency will undertake the role of scheme administrator. It will be responsible for registration, running the on-line registry, selling allowances on behalf of the government, auditing participants and taking enforcement action for non-compliance.
10. Final debates in Parliament are expected to be completed during the winter with legislation coming into force in March 2010.

Timeline

11. The scheme starts in April 2010 and is divided into set time periods known as 'phases'. Phase 1 is the introductory phase, which runs from 1 April 2010 until 31 March 2013. Subsequent phases last for seven years. The first two years of these phases are preparatory, and overlap with the preceding phase.
12. Each phase has:
 - (a) A qualification period, where organisations must assess whether or not they qualify for participating in the scheme, or need to make an information disclosure.
 - (b) A registration period, during which organisations that are required to take action under the scheme must either submit their information disclosure or register as a participant. The registration is required with the first 6 months of year one in each phase.
 - (c) A footprint year, where participants must monitor their total emissions from energy use and work out what emissions must be included in the scheme. This is year one of each phase and must be reported in a Footprint Report.
 - (d) A series of annual reporting years, which run from April to March. In the introductory phase each of the three years in the phase is an annual reporting year. In subsequent phases the reporting years run from year 2 onwards.

Initial Registration

13. The Environment Agency will send a letter inviting organisations to register. Registration opens on 1 April 2010 and ends on September 2010. Failure to register in time will incur a fine of £5,000, with a further fine of £500 per working day until registration is complete. Before organisations can complete the registration process participants need to pay a registration charge of £950 to cover the administration and data validation needed to activate a compliance account.
14. Once registered, participants will pay an annual subsistence charge of £1,290.
15. To prevent unauthorised access the CRC on-line registration will be underpinned by the Government Gateway security arrangements.
16. The following is an overview of activities required to complete registration.
 - (a) A number of individuals will need to be appointed to act as points of contact. Some of these contacts will need to communicate with each other, use the registry and may have to answer questions from the Environment Agency relating to registration. The EA will need to validate business contact details of some of these contacts to ensure they are authorised to act for the registering organisation. This validation may take some time.
 - (b) As part of the process of determining qualification to the scheme: a list of settled half hourly meters (MPAN numbers) and the amount of half hourly electricity supplied to the organisation must be submitted.
 - (c) Detailed information about this organisation will also need to be submitted.
17. Registration packs are due to be received prior to the end of this financial year. The process of registration is a lengthy procedure that will require significant resources to ensure that the submission is kept within the required tolerances and therefore does not attract penalty. The Department of Energy and Climate Change (DECC) quotes “Do not underestimate this task. For large organisations this is at least a six month task, with only a 5% margin before fines kick in”. All submissions will require verification of data within the deadlines, therefore time must also be built in for this process.

Individuals Involved with Registration

18. The registrant – Any person can enter the registration information onto the on-line registry. This person has restricted access to the CRC Registry i.e. although they can enter the registration information, they will not be able to finish the registration process. Only the primary or secondary contact (see below) can complete registration.
 - (a) A senior officer contact. This must be a director of the organisation or person of equivalent status who exercises management control to act for the organisation. The EA will check official sources to validate the appointment of this officer

- (b) A primary contact and a secondary contact. These will be the contacts that the EA are in touch with day-to-day. Either the primary or secondary contact can be the senior officer contact. Only the primary or secondary contact can complete registration.
- (c) The registrant may nominate themselves as the primary or secondary contact, or as the senior officers. However, they will need to provide additional information to be validated by the EA.
- (d) An invoice contact. This contact will be send invoices for the annual subsistence charge.

Financial Aspects of the scheme

- 19. The CRC scheme has been introduced by the Government in response to reducing the amount of energy consumed by large organisations. The scheme aims to do this by financial incentives/disincentives, however overall the scheme is intended to be cost neutral at a national level, although better performing organisations will benefit at the cost of those whose performance is weaker.
- 20. The scheme runs in an introductory phase from the 1st April 2010 for three years, the first year of the scheme (2010/11) is a footprint year with no financial activity, in that there is no purchase of allowances or recycling payment. Following this introductory phase a capped period will commence from April 2013. **Appendix 1** details the time line for the project.
- 21. At this point the two known key financial aspects of the scheme are the purchase of allowances and the receipt of recycling payments.

Purchase of Allowances

- 22. Each April the Government will hold a sale of allowances to give participants the ability to purchase allowances to cover their expected carbon emissions for that year. Although there is no requirement to buy allowances at this point, one allowance will be required for each tonne of carbon emitted, therefore at this sale point an estimate of expected emissions for the coming year should be known.
- 23. In the introductory phase the sale of allowances will be set at a fixed price of £12 per allowance and there will be no limit on the number of allowances that can be purchased. The first sale will take place in April 2011 for emissions made during 2011/12.
- 24. After the Government sale, allowances can be purchased or sold on the secondary market (based on market forces) and additionally there will also be a facility to purchase through a Government “safety valve”. This safety valve is designed to protect against the price of allowances being too high. Price will be based on European Trading Scheme price (ETS), however the price of allowances purchased from this mechanism will always be at least at the Government auction price plus broker and handling fees. This is intended to encourage accurate energy use forecasting.
- 25. Each July each participant must report their emissions for the previous year end (failure to do so results in financial penalties) and at this point surrender sufficient allowances to cover

emissions for the same period. This gives participants four months from the end of the reporting period to purchase additional allowances on the secondary market if required, allowances surrendered must be from the previous year's auction or secondary purchases, no allowances from the last sale period can be used. Failure to surrender enough allowances results in a fine of £40 per each missing allowance and in addition outstanding allowances will still need to be purchased and surrendered. Any unused allowances can be rolled forward to the next year, however no allowances bought in the introductory phase can be rolled forward at the end of the third year.

26. Based on the latest emissions data available for the Council (2008/09 outturn) the number of allowances that would need to be purchased would be 13,243 tonnes, which at £12 per tonne would mean the Council would pay £158,916. This is a ball park figure of the initial cost to the Council; the actual purchase cost in April 2011 will be dependent on estimated requirements for that year. The Council would later receive a recycling payment, which may be more or less than the initial cost (see the following paragraphs on Recycling Payments).
27. From April 2013 the next phase of the scheme commences with the start of the first five year capped phase (capped phases actually run for seven years, although the first two years will be the final two years of the previous phase). In the capped phase there will be a restriction on the number of allowances for sale in the Government sales based previous year's requirements less targeted decreases in emissions. At these auctions restrictions will be placed on percentage of the allowances that can be bought by single parties to stop any participants monopolising purchase of allowances and creating an inflated secondary market. The price of allowances in this phase will be set based on demand, following the receipt of sealed bids from participants. This price, "the clearing price" will then be offered to participants on the allocations they have bid for.

Recycling Payments

28. As the scheme is intended to be revenue neutral to the Government all revenues collected from the auctions in April will be recycled to scheme participants in the following October. This leaves a six month cash flow delay between purchase of allowances and receipt of repayment.
29. The amount of recycled payment to a participant will depend upon two elements. The first element will be based on the organisations percentage of the first year (phase one 2010/11) total consumption. The second element will be an adjustment of bonus/penalty based on position within the league table of each member of the scheme. The bonus/penalty payment will rise in 10% increments from year 2 (at 10%) to 50% in year 6. The 2010/11 base year will be used for all years recycling payments during the introductory phase. For all other phases the first year of that phase will be used as the base year (i.e. the penultimate year of the previous phase).
30. The following example shows a recycling payment in year three of the scheme with payment been made in October 2012, recycling total sales of allowances purchased in April 2012 for use in the year 2012/13. (The example includes no adjustment for metrics):

Organisation	Number of Allowances Purchased	Value £ (@ £12 per allowance)	Base Year (2010/11) CRC emissions	Actual Emissions (11/12)	League position (2011/12 data)	Bonus/ Penalty	Recycling Score	% of total recycling score	Recycling payment £	Net Cost or Gain £
A	800	9,600	1,000	750	1	+20%	1,200	56%	16,800	+7,200
B	1,700	20,400	1,200	2,000	2	-20%	960	44%	13,200	-7,200
Total	2,500	30,000	2,200	2,750			2,160	100%	30,000	Nil

31. League tables will be published annually based on the data submitted in July, using three weighting metrics as follows,

- (a) Absolute Metric – The percentage change in emissions over a rolling five year programme.
- (b) Early Action Metric – Actions taken before the scheme commenced e.g. gaining Carbon Trust status and installing automatic meter reading (AMR).
- (c) Growth Metric – Comparison of consumption against growth/decline of the business over a five year rolling programme.

32. In the first year as no data will be held for the growth or absolute metric only the early action metric will be used. (The growth and absolute metrics will be based on the number of years data available in years 2 to 5 until five years of data is collected).

33. The metric weightings will apply as per the following table

Metric	Year 2	Year 3	Year 4	Year 4 to 9
Early Action	100%	40%	20%	0%
Absolute	0%	45%	60%	75%
Growth	0%	15%	20%	25%

Other Costs

34. In addition to the purchase of allowances, various fees are payable by the Council with regard to the scheme. Fees charged include scheme registration, annual participation, safety valve requests (charged at £300 each time) and in addition to penalties associated with having insufficient allowances, there are also penalties for failure to register, late submission of reporting data, errors in data and failure to keep adequate records.

35. Each year a sample of participants will be audited with a tolerance level of 5% on the data submitted. Any errors in excess of this amount will be subject to a fine of £40 per tonne of incorrectly identified emissions. At this time it is expected that none of these supplementary costs will be recycled to scheme participants.

Financial Implications and Decisions

36. The above paragraphs give an outline to the key financial elements of the scheme. At present a full financial picture to this Council can not be ascertained (i.e. how much money will be received back in recycle payment) as it is not know what our league table position will be or the how many allowances will be purchased across the whole scheme. There will be a number elements that will need to be considered with regard to how the Council takes forward a strategy for CRC with various decisions having to be made.
37. Officers have considered the practical implications of the scheme and taken a number of decisions on the internal workings. These are detailed below:
- (a) Management of resources to ensure that the registration is completed accurately and within tolerances will be undertaken by the Assistant Director Resources (Corporate Services Department).
 - (b) Systems to collect and forecast emissions data will be lead by the Energy Management Officer in the Estates Team in conjunction with relevant departmental leads.
 - (c) As schools account for a large percentage of the Authority's total consumption, schools will need to be influenced to reduce emissions without direct control of delegated budgets. This will be lead by the Assistant Director Planning & Resources (Children's Services).
 - (d) Costs for initial registration to the scheme will be covered by existing resources within the Estates budget.
 - (e) At present it is unknown if the Council will make a surplus, deficit or break-even in the first round of the CRC sales. Therefore, in the first year of the scheme recycling payments shortfalls or surpluses will be borne centrally by the Council (rather than allocated departmentally) either by requesting additional resources or through a contribution to reserves. A clearer picture of this Councils position should become available once the first set of league tables are produced which should allow future financial implications to become clearer.
 - (f) There will be a six month delay between purchase of allowances and receipt of recycling payments. It is proposed that the cash flow implications be managed through the Councils Treasury Management section, with any financing costs being borne by the central budget.
 - (g) In order to improve this Councils position within the league table, decisions will need to be made over what actions can make the most impact from the resources employed (i.e. give the best value for money). Where improvements can be made at a small cost it is agreed that these decisions be made by individual building budget managers in line with advice from the Energy Management section. Where improvements are proposed that have significant financial implications these be fed through CMT for approval (after consulting Energy Management) with onward referral to Cabinet as necessary.
 - (h) At present schools and a number of the tenanted properties benefit from lower energy costs through the Councils block energy contracts, however, as a result of this they are included in the Council's CRC consumption figures. These buildings will continue to benefit from this in the first year of the CRC scheme, with a review taking place at the end of this year to see what impact this has on the overall position of the Council, the result of which will be reported to CMT/Cabinet.

38. In addition to the internal decisions made in paragraph 37 there are a number specific issues with regard to financial management that need to be addressed to implement the CRC scheme in Darlington. With regard to the purchase and sale of allowances, the Council will need to make a decision on what policy it wishes to follow in order to maximise benefit or reduce risk to the Authority. There are a number of options that can be undertaken with regard to purchase of allowances for example, buy what we need, buy with a buffer (to give certainty and then sell/bank the excess, buy additional allowances to try and sell on at a profit. All of these options require decision making as the benefit of each will be influenced by the market conditions at that particular time. It is proposed therefore that in order to facilitate quick day to day decision making that Cabinet approve the delegation of the policy decisions with regard to buying and selling of allowances to the Director of Corporate Services and that the Director of Corporate Services also be given delegated powers to undertake the buying and selling of CRC allowances at each sale period in line with the Councils financial position and CRC market conditions to gain the best of course of action for the Council.

Outcome of Consultation

39. There has been no external consultation regarding this report.