

Huw Irranca-Davies AS/MS
Y Dirprwy Brif Weinidog ac Ysgrifennydd y Cabinet dros
Newid Hinsawdd a Materion Gwledig
Deputy First Minister and Cabinet Secretary for Climate
Change and Rural Affairs



Llywodraeth Cymru
Welsh Government

Ein cyf/Our ref: MA/HIDCC/5924/24

Llŷr Gruffydd MS
Chair
Climate Change, Environment and Infrastructure Committee
Welsh Parliament
Cardiff Bay
Cardiff
CF99 1SN

26 September 2024

Dear Llŷr,

I am writing to inform you that the UK Emissions Trading Scheme (ETS) Authority (formed of Welsh Government, UK Government, Scottish Government, and Northern Ireland Executive), has today contacted ETS scheme participants to seek views on moving the start of the scheme's second free allocation period from 2026 to 2027.

A key role of the UK ETS Authority is to align the Scheme to net zero targets, ensure it is functioning as intended, and supports decarbonisation in ways which maintain business competitiveness. One way of maintaining market competitiveness is the free allocation of UK ETS allowances. Free allocations aim to protect trade-exposed industry in the UK from global competitors which are not subject to carbon pricing (carbon leakage).

To provide UK ETS participants with certainty over their future free allocations, the Authority consulted on a review of the process of assessing free allocations, which was published in December 2023¹. This review is particularly key for Wales as some of our industries, are very trade exposed and harder to decarbonise.

Welsh industry currently receives high levels of support through free allocations. It is important we do not disadvantage Welsh industry, as this would result in these industries relocating to countries that do not have the same climate ambitions, risking increased global emissions and an unfair transition to net zero as a result.

¹ [UK Emissions Trading Scheme: free allocation review - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/uk-emissions-trading-scheme-free-allocation-review)

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Rydym yn croesawu derbyn gohebiaeth yn Gymraeg. Byddwn yn ateb gohebiaeth a dderbynnir yn Gymraeg yn Gymraeg ac ni fydd gohebu yn Gymraeg yn arwain at oedi.

We welcome receiving correspondence in Welsh. Any correspondence received in Welsh will be answered in Welsh and corresponding in Welsh will not lead to a delay in responding.

Following the Free Allocation Review, the second free allocation period, originally planned for 2026, will be used to implement any changes. Moving the scheme's second free allocation period to 2027 would mean any changes from the review are implemented a year later than previously planned. However, it would enable us to align changes to the UK ETS free allocation policy with the UK Government's plans to introduce a UK Carbon Border Adjustment Mechanism (CBAM) in 2027, which is in itself a carbon leakage mitigation measure. The Authority received a significant number of responses to the Free Allocation Review consultation earlier this year indicating a preference for alignment to ensure a consistent approach to carbon leakage mitigation. The move to 2027 will also provide additional time for careful consideration of stakeholder views and policy development in what is a complex and challenging area.

The Authority will be engaging directly with affected stakeholders, the consultation will be open for two weeks and the UK ETS Authority will respond as quickly as possible to give scheme participants certainty over their free allocations in the 2026 scheme year. The consultation will not be translated as affected stakeholders have already expressed their language preference in English.

I will of course write to you again when the Authority Response to the consultation on the Free Allocation Review is published. The information gathered will aid us in refining the scheme and enable us to create more robust mechanisms that will incentivise innovation, drive emission reductions, and secure a resilient, sustainable future for Wales.

I am copying this letter to Mike Hedges MS, Chair of Legislation, Justice and Constitution Committee.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Huw Irranca-Davies', written in a cursive style.

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