



UK Emissions Trading Scheme: Future Markets Policy

Consultation response from Shell U.K. Limited

11 March 2024

By email to: ukets.consultationresponses@energysecurity.gov.uk

Shell U.K. Limited (“Shell UK”)¹ welcomes the opportunity to respond to the UK Government’s consultation on the UK Emissions Trading Scheme: Future Markets Policy.

For many years, Shell UK has advocated that countries put a direct price on carbon emissions. Shell UK believes that Carbon Pricing Mechanisms (CPM) should be a part of a broader policy framework to achieve net-zero emissions, applying to as many sectors of the economy as possible and increasing over time.

Shell UK also believes that government and policymakers should promote the use of low-carbon products through policies that create demand and encourage supply of low-carbon energy in industry such as fiscal support, government mandates, public procurement and green certificates, as well as to accelerate policies to encourage the development of carbon capture, utilisation and storage (CCUS) for industry

If you have any queries regarding this submission, please contact:

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Questions and responses

1. Do you agree with the key risks we have identified? (Yes/No). Please provide any supporting evidence in your response.

No answer

2. Are there any alternative risks to those listed above that the Authority should consider? (Yes/No). Please provide any supporting evidence in your response.

No answer

3. Do you believe that the UK ETS would benefit from the introduction of a supply adjustment mechanism to address demand shift with long-term impacts risk? (Yes/ No). Please explain the reasons for your response.

Yes. Given the size of the UK ETS, it has a higher degree of volatility than the EU ETS. Large scale decarbonisation is unlikely to be linear, and with the materiality of certain sectors and individual installations within the UK ETS, there is a high risk of non-linear reductions in UK emissions in a

¹ In this response the words “Shell UK”, “we”, “us” and “our” are used to refer to Shell U.K. Limited and its subsidiaries in general or to those who work for them.



particular year, that could lead to an oversupply in the market, and a depressive impact on the UK ETS price. Although the reducing cap seeks to incentivise such reductions in emissions, a supply adjustment mechanism (SAM) would maintain the long-term price signal required for decarbonisation and would permit the market to respond to supply events that occur. Towards the end of the phase, future scarcity can be managed by the SAM while remaining consistent with the Net Zero cap.

4. If so, do you have a preference for a) a quantity-triggered supply adjustment mechanism or b) a price-triggered supply adjustment mechanism, as the best means of addressing this risk? Please give your reasons for your preference and response.

The objective of the supply adjustment mechanism is to effectively manage the supply of allowances in the system, therefore a quantity-triggered SAM better aligns with this objective. Although a quantity based SAM typically provides an annual adjustment, and therefore is not designed for short-term market adjustments, its effectiveness will be highly dependent on the threshold levels for intake and withdrawal into the SAM.

We believe that it is not suitable to align the thresholds of the UK ETS with the EU ETS, as the UK ETS is a smaller market and would be vulnerable to significant fluctuations when adjustments are made. As we approach the end of the decade, the SAM will need to allow for more generous withdrawals to accommodate a tighter market. Additionally, the EU's Market Stability Reserve (MSR) will also need to be reviewed in 2026, as it is generally expected to be less effective towards the end of the decade. Therefore, the UK's SAM should not replicate the EU ETS MSR at this time.

Towards the end of the decade, the SAM may need to provide for more generous withdrawals as the market is generally expected to tighten.

5. Do you agree with the Authority's minded-to position on the introduction of a quantity-triggered SAM? (Yes/ No). Please give your reasons for your response.

Yes, for the reasons outlined in the response to question 4.

6. Do you agree with the proposed approach for calculating the UK ETS TNAC? (Yes/ No) Please give your reasons for your response.

Yes. We agree with the definition of the TNAC = Supply (Free Allocation to date + Auction volume to date) – Demand (annual verified emissions to date).

7. If you disagree with the proposed approach, please suggest an alternative approach and your rationale for this?

No answer

8. What is your view on what level of surplus constitutes a) an optimum level of surplus in the scheme, that would allow for effective functioning of the market and b) how could this be assessed including in terms of methodology? Please give your reasons and evidence you may have for your response.

We encourage the authority to run a technical stakeholder process to discuss and analyse detailed designed elements of the Supply Adjustment Mechanism such as the threshold level and the intake and withdrawal rates. In general, it should be ensured that the SAM does not return a large quantity of allowances back into supply before the end of the decade .



This workgroup should also consider the integration of GGRs into the UK ETS.

9. Do you have a view on what level a) the upper quantity trigger threshold and b) the lower quantity trigger threshold should be in a UK ETS SAM? (Yes/ No). Please give your reasons and any evidence to support your response.

See response to question 4.

10. How reactive should the upper and lower thresholds be, for example should each threshold have a sliding scale of supply adjustment? Please give your reasons and any evidence to support your response.

See responses to questions 4 and 5.

11. Has the Authority identified all types of triggers that should be considered; or are there any other types of trigger thresholds that should be considered? Please give your reasons for your response.

No answer

12. Do you agree that relative trigger thresholds would be more appropriate than absolute static thresholds? (Yes/ No). Please give your reasons for your response.

Yes – as the UK ETS evolves, a dynamic trigger that is relative to the UK ETS would be appropriate.

13. If you agree, what is your preference – relative trigger threshold values a) as a proportion of the annual UK ETS cap or b) relative to annual auction volume.

We believe the threshold is best calculated using the TNAC definition.

14. What is your view on what the appropriate level of auction volume adjustment should be? Please give your reasons and any evidence for your response.

No answer

15. Do you have a preference for this adjustment to be a percentage of annual auction volume, or other fixed amount, a combination of both or any other metric? Please give your reasons for your response.

No answer

16. Do you agree with the proposed TNAC publication timing of post compliance in spring? (Yes/ No). If not, please explain your reasons.

Yes. The publication of the TNAC post compliance in spring would seem sensible if the TNAC requires verified emissions data. However any timing should fit into the timetable that reflects any changes which occur as a result of changes following the UK ETS Free Allocation review consultation.

17. What is your view on auction supply adjustment timings if the SAM is activated? Please give details of your preferred timings and rationale for this.

No answer

18. Should auction volume require adjustment due to SAM activation, do you agree that the Authority should endeavour to preserve approximate equal auction volume distribution in the time period affected by this adjustment? (Yes/ No). Please give your reasons for your response.



Yes

19. In your view, when, in terms of scheme year, should any quantity-triggered SAM be implemented into the UK ETS, meaning the SAM would begin operating the following year post compliance period? Please explain your reasons for your response.

While implementation in the following year post compliance period may be suitable, the UK ETS has already been able to adjust the auction volumes in year previously when auctions haven't cleared, and therefore, consideration should be given whether a more responsive SAM would be possible without delaying to the following year.

20. Do you have any views on the interactions between any quantity-triggered SAM and the ARP and CCM? Please give your reasons and any evidence for your response.

Each of these instruments serves a different purpose therefore we do not believe the activation of one mechanism should impact the activation of another. That said, from a CCM perspective, we propose the terms for discretion in decision making should be clearly set out, or as a minimum, examples of in what circumstance the UK ETS authority may choose to exercise its discretion in not making any adjustments – for example where there is a Supplier of Last Resort event, or any similar supplier failure.

21. Do you agree with the Authority's assessment of each of the options considered? (Yes/No). Please provide any evidence in support of your answer.

No answer

22. Are there any alternative options to those listed above that could be implemented by the Authority to address the risk of a sudden, sustained and significant price decrease in the UK ETS market? If so, please describe how the mechanism functions.

If auctioned allowances fail to be purchased above the ARP, even when distributed across the following four auctions, allowances could be allocated to the SAM.

If allowances are expected to be tight in later years then these allowances could then be released from the SAM at a later point while remaining consistent with the Net Zero cap.

23. Do you agree with the Authority's minded to position to retain the ARP? (Yes/No). Please provide any evidence in support of your answer.

Yes.

24. Do you think that an alternative policy option, such as any of the options previously discussed in this chapter, should be implemented in conjunction with the ARP? (Yes/No). If so, please elaborate.

No answer

25. Do you think the ARP trigger level should be changed? (Yes/No). What level do you think the ARP should be set at? Please provide a rationale for your answer.

Shell believes that Carbon Pricing should apply to as many sectors of the economy as possible and increase over time. While we note the auction price has been consistently above the ARP since the UK ETS inception one way of ensuring this could be to increase the ARP in line with inflation, such as is done in the California scheme for example.



26. Do you think the ARP trigger level should remain static or should it evolve over time? If you think it should evolve, how do you think the Authority should design this evolution? Please provide a rationale for your answer.

No answer

27. Do you think the Authority should alter the way an ARP trigger affects auction supply? If so, please explain how you think this should be changed.

No answer

28. Are there any other ways the Authority could alter an ARP to make it more effective? If so, please explain these alterations.

No answer

29. Do you agree with the Authority's assessment of each of the options considered? (Yes/No). Please provide any evidence in support of your answer.

No answer

30. Are there any alternative options to those listed above that could be implemented by the Authority to address the risk of a sudden, sustained and significant price increase? If so, please describe how the mechanism functions.

No answer

31. Do you believe the CCM should be retained with no adjustments? (Yes/No). Please provide any supporting evidence in your response.

The CCM has an important role to play in the event of any extreme shocks to the UK ETS. It would be beneficial if the UK ETS authority provided more information on how discretion may be used, this could include outlining cases where an intervention may or may not be made, should the CCM trigger threshold be met – for example the previous supplier crisis that led to short-term purchasing spike.

32. Do you believe the current CCM thresholds should remain? (Yes/No). Please provide any supporting evidence.

No answer

33. If no, should the CCM thresholds be made more reactive by changing the multiplier, trigger period and/or reference period? Please provide any supporting evidence.

No answer

34. Do you believe the CCM trigger methodology should be based on historical comparisons or a fixed price? Please provide any supporting evidence.

No answer

35. Are there alternative methods we should consider when setting the CCM trigger price? Please provide any supporting evidence.

No answer



36. Do you believe that the CCM should retain discretion in its decision-making process? (Yes/No). Please provide any supporting evidence.

Yes, however it would be beneficial if the UK ETS authority provided more information on how discretion may be used, this could include outlining cases where an intervention may or may not be made, should the CCM trigger threshold be met – for example the previous supplier crisis that led to short-term purchasing spike. In future, an exemption could be made when there is a Supplier of Last Resort process.

37. If no, do you believe the CCM should have a fully or partially automated response following a trigger? If so, please describe how this could function.

We do not support automated release of allowances upon a CCM trigger.

38. Are there any other design changes not listed above that would improve the effectiveness of the CCM?

No answer

39. Do you have any views on the approach to reserve allowances in the UK ETS or anything you would like the Authority to consider when making decisions on its size and structure?

Should the UK ETS change its approach to reserve allowances or other design features on size and structure, these should be subject to formal consultation ahead of any intervention.