

European Scrutiny Committee

House of Commons London SW1A 0AA

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From: Sir William Cash MP

1 December 2021

Rt Hon. Greg Hands MP

Minister for Energy, Clean Growth and Climate Change

Department for Business, Energy & Industrial Strategy

1 Victoria Street

London SW1H 0ET

10871/21: Proposal for a Regulation establishing a carbon border adjustment mechanism (41916)

We considered your Explanatory Memorandum on the above proposal at our meeting of 1 December 2021.

We take note of comments by European Commissioners, the WTO Director General and a UK Government Minister that, ideally, a global system of carbon pricing would be developed rather than a series of unilateral carbon border adjustment measures. Would you agree that a multilateral approach to avoiding, and where necessary tackling, carbon leakage is the most desirable one and, if so, what action is the Government taking to pursue that approach?

Being mindful that a multilateral approach could nevertheless take some time to develop, unilateral approaches appear inevitable. Now that the EU has proposed the first fully-developed carbon border adjustment mechanism, with potentially significant implications for the UK, it is welcome that the UK has engaged in bilateral dialogue on the proposal through some of the specialised meetings convened under the UK-EU Trade and Cooperation Agreement as well as the Joint Consultative Working Group established under the Withdrawal Agreement. We note from the Minutes of the 4 October Trade Specialised Committee on Goods that the UK and EU agreed to hold further informal technical discussions on EU CBAM. Please could you provide us with more detail on the timing and nature of those discussions and how you intend to communicate progress given the informal nature of the dialogue?

It is notable that the third countries excluded from the EU CBAM are either part of the EU ETS or have an arrangement linking to the EU ETS. The easiest way to mitigate the impact of EU CBAM on the UK would therefore be to agree to link the UK and EU Emissions Trading Systems. Given that the EU and UK agreed in the Trade and Cooperation Agreement to consider linking their

respective emissions trading systems, could you tell us what progress has been made to that end?

A second avenue to mitigate the impact on the UK would be for the UK and EU to explore the provision in the draft Regulation for the EU to conclude agreements with third countries to take account of carbon pricing mechanisms in these countries. From the Minutes of the Trade Specialised Committee on Goods, we note the EU's commitment that domestic decarbonising efforts of third countries would be taken into account by the EU CBAM. Has the Government had any discussions with the Commission yet about any agreement on how CBAM's operation could take into account the UK ETS?

At the heart of the potential impact of CBAM on the UK is the possible addition of the adopted Regulation to the list of legislation with which Northern Ireland must align under the current terms of the Northern Ireland Protocol. Clearly, the operation of the Protocol is under negotiation at the moment and the Government has understandably not clarified whether it agrees with the contention that the Regulation, once adopted, should be added to the Protocol. We would nevertheless expect the Government to be operating for the moment on the basis that the Regulation might be applied in Northern Ireland. Are you undertaking analysis to understand the draft Regulation's implications for Northern Ireland—including trade with Great Britain—and to identify any issues of concern which might be raised with the Commission without prejudicing the final decision on adding the Regulation to the Protocol? Is any further discussion on the proposal expected within the Joint Consultative Working Group?

We noted with the interest the Government's assessment that EU CBAM's impact on UK businesses would be proportionate to the relevant industrial concentration within UK regions, and presumably nations and that this was of particular interest to the Welsh Government. We ask that you keep us updated on your assessment of EU CBAM's impact.

We have taken note of the technical issues concerning the EU CBAM's compliance with international trade law, as well as the potential difficulties of how any NI alignment with EU CBAM would practically interact with NI's participation in the UK ETS rather than the EU ETS (aside from electricity generation). We will monitor these issues as discussions progress within the EU institutions on the design of the Mechanisms.

We look forward to a response within ten working days.

I am copying this letter to Darren Jones MP, Chair of the Business, Energy and Industrial Strategy Committee and Rebecca Davies, Clerk of that Committee; to Rt Hon. Philip Dunne MP, Chair of the Environmental Audit Committee and Martyn Atkins, Clerk of that Committee; to Angus Brendan MacNeil MP, Chair of the International Trade Committee and Eligio Cerval-Pena, Clerk of that Committee; to Simon Hoare MP, Chair of the Northern Ireland Affairs Committee and Stephen Habberley, Clerk of that Committee; to Pete Wishart MP, Chair of the Scottish Affairs Committee and Leoni Kurt, Clerk of that Committee; to Rt Hon. Mel Stride MP and Kenneth Fox, Clerk to that Committee; to Rt Hon. Stephen Crabb MP, Chair of the Welsh Affairs Committee and Dr Adam Evans, Clerk of that Committee; to Lord Kinnoull, Chair of the House of Lords European Affairs Committee, and to Nick Boorer, that Committee's Clerk; to the Parliamentary Scrutiny team in your Department; and to Les Saunders in the Cabinet Office.

CHAIR