

# CRC - WHEN AN INCENTIVE BECOMES A TAX AND WHAT TO DO ABOUT IT...



*"In the Spending Review a fundamental change was made to the way in which the Carbon Reduction Commitment (CRC) will operate. What was designed as a revenue-neutral incentive to cut carbon emissions has become a green 'stealth tax' which will result in all affected organisations paying 8-9% of their energy costs to Government. Organisations should quickly implement practical carbon reduction measures to reduce their future liability."*

## **Matt Fulford**

Head of Sustainability

## Executive Summary

- The Carbon Reduction Commitment (CRC) is changing
- It has evolved from an incentive to a green 'stealth tax'
- All affected organisations will have to pay £12 per tonne on their carbon
- On average £200,000 per organisation per year will have to be paid to the Treasury but the variance will be great
- Organisations in the health, local government, education, retail and CRE sectors are likely to feel the biggest impact.

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**Buried deep inside the Spending Review was one short but very significant paragraph for organisations and their carbon reduction plans.**

*"The CRC Energy Efficiency scheme will be simplified to reduce the burden on businesses, with the first allowance sales for 2011-12 emissions now taking place in 2012 rather than 2011. Revenues from allowance sales totalling £1 billion a year by 2014-15 will be used to support the public finances, including spending on the environment, **rather than recycled to participants.**"*

This means that participants in the scheme will no longer receive any money back from the Government - changing the CRC from an incentive to a tax overnight.

When it was first designed, CRC was meant to be largely revenue-neutral for participants and the Treasury. Under the previous model, organisations that were impacted would pay out at a certain level but receive money back six months later, depending on their carbon reduction performance (ranked in league tables). Effectively this meant the maximum an organisation could lose in the first year was £1.20/tonne and by year five was £6.00/tonne.

Many organisations would have gained by a similar amount and the vast majority would have experienced little overall gain or loss. Now all organisations in the scheme - likely to be between 3000 and 5000 - will have to pay £12/tonne on all their carbon, regardless of how well they perform in the league table.

It is likely to impact organisations of medium-sized energy use (those spending over £500,000 on electricity in a year) but will not affect big polluters which fall under The European Union Emissions Trading Scheme (EUETS) or small organisations with limited energy use.

## **What is the financial impact?**

The CRC has become a carbon tax and will add on 8-9% to all gas and electricity costs from April 2012. Organisations should budget for this cost now, in addition to the forecasted increase in utility costs, as it will be unavoidable.

Overall the Treasury expect to raise £715 million in 2011-12 rising to £1.02 billion by 2014-2015. Given the number of participants within the scheme this means that on average an additional £200,000 per organisation per year will have to be paid to the Treasury. However, the variance of cost between the organisations will be significant, with many larger organisations paying much more than this. The sectors likely to feel the biggest impact are:

### **Health**

CRC is likely to cost the NHS £38 million per year in total. The average trust will pay £160,000 a year with the largest trust having to pay £1.12 million annually.

## Local Government

For one London Borough, the annual cost is estimated to run to £224,000, of this £113,000 is due to the carbon emissions from its schools estate and only £60,000 from its corporate office space. For a Unitary Council the total cost is approximately £162,000 with £120,000 from schools. Local authorities are therefore likely to pass on the costs of CRC directly to schools as the reduced complexity means the CRC liability is easily transferable.

## Education

We estimate that if a local authority decides to pass on the costs to its schools, the cost for a primary school will be £1,500 annually, whilst an average secondary school will pay £4,500 annually. HE and FE providers are likely to be hit hard too.

## Retail

For a leading high street retailer the CRC liability will cost approximately £260,000 per year, this will be considerably more for the biggest retailers.

## CRE

Consideration will have to be made within landlord and tenant agreements to establish who will be finally responsible for the cost.

The issue about who pays is at the heart of service charge administration and the RICS Code. The landlord has the ability to pass on some charges that change within an accounting period to the tenant - e.g. imposed tax rises from a budget announcement - however the landlord cannot unilaterally increase other costs once the budget for a period has been agreed in all cases. It is not black and white; both the specific wording of the lease and the professional codes and customs will determine who bears the resulting cost. Any occupier needs to be aware of the change and take action based on informed advice accordingly.

Organisations in the hotel, transport, industry, defence and leisure sectors will also all be affected.

## What you need to do...

Previous advice to organisations responding to the CRC has been around taking the relevant quick wins to improve their position on the league table. The main elements of this were to install automatic meters and gain the Carbon Trust Standard. However, the league table no longer applies and will become a reputational driver only (if it is still produced).

The Carbon Trust Standard now has little value under the new model but Automatic Metering Reading will still greatly help with administering the scheme and provide an excellent tool for carbon reduction. Organisations should continue with plans in this area although should review the value of installing them in small energy-use buildings.

The key action organisations should now take is a focused drive on carbon reduction to reduce the amount of tonnes of carbon they emit and therefore the amount they will have to pay. To gain the full benefit of carbon reduction in reducing CRC the steps should be taken prior to April 2011, but reductions at anytime will help. The CRC will have the effect of improving the payback periods on any investment made in 'greening' built-assets.

## Five steps to reduce your liability:

We find that most organisations can save 20-30% of carbon through a series of carefully designed reduction measures which payback in under 5 years. There are also a handful of measures which payback in less than 2 years and increasingly there are funding methods available to finance these improvements, so capital expenditure is not needed. To establish the best strategy to reduce their liability, organisations should follow these five steps:

- 1 Establish whether you are eligible for the scheme.
- 2 Undertake an estate audit to assess current emissions and what your future liability under CRC would be (if no action was taken).
- 3 Identify if any preparations have already been made for CRC in its previous form.
- 4 Develop (or re-develop) your strategy to minimise its impact on your organisation.
- 5 Implement the strategy, starting with practical carbon reduction measures.

## Client Success



### A leading high street retailer

We have reduced the carbon emissions of a leading high street retailer by over 20% in under three years through a series of supported baseline and improvement recommendations.



### A major NHS Trust

We are currently working with a leading NHS Acute trust to implement a strategy that will reduce its carbon emissions by over 50% in a four year plan that will be cost neutral in five years.

To find out more information on CRC, its potential impact on your organisation and how to reduce your liability, contact:

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