



## **CRC – the introduction of a stealth tax? The implications for Participants and landlord and tenant**

On 20 October 2010, the Chancellor of the Exchequer set out the government's four-year public spending plans in the Spending Review 2010. This included two changes to the CRC Energy Efficiency Scheme which fundamentally alter the nature of the scheme.

- The first sale of allowances for 2011/12 emissions will now take place in 2012 rather than 2011.
- Revenue from the sale of Allowance sales will be used to support the public finances (including spending on the environment), rather than recycled back to Participants in the scheme.

The adaptation of the scheme to become revenue raising changes the scheme fundamentally and raises questions as to how the scheme will operate. The government has yet to set out in full its plans but it has suggested that the new proposals will simplify the scheme and reduce the burden on businesses.

### **Sales of allowances**

The first Allowance sales for 2011-2012 emissions will take place in 2012 rather than 2011, giving Participants a further year to budget for the costs of the CRC. Although not yet clear, it appears that the need to buy allowances in advance and to predict future energy consumption has also been removed. It may be that the Government's assertion that this will simplify the scheme may prove correct.

However, given that Participants will still need to collate and report data, arguably the burden on Participants is exactly the same from a day to day management perspective and more significant from a financial perspective.

### **Recycling payments**

The Government seems to have realised that it has missed a trick at a time when it is looking to maximise its revenue and reduce its expenditure. The scheme is no longer going to be "revenue neutral" with the net costs of allowances being recycled to Participants. Instead the revenue generated from the sale of allowances will be retained by the Government, which is estimated to total £1billion a year by 2014-2015.

As each allowance will initially cost £12 and an allowance is needed for each tonne of carbon consumed, the costs of CRC will increase significantly for each Participant. Given that Participants are already making provision for this scheme, there is pressure on the Government to provide more information.

In the meantime any landlord Participant that had decided not to deal with CRC in its leases because of the relatively low costs involved might want to reconsider.

### **The impact on landlords and tenants of cancelling revenue recycling**

If a landlord is a Participant in the CRC and the energy contract is in the landlord's name, the landlord will have to account for the emissions even though the energy has been used by its tenants. Consequently, the landlord will have to report on, and surrender Allowances for, the associated carbon emissions of its tenant(s).

A considerable amount of time and energy has been devoted by the property industry over the past two years in considering whether existing leases give landlords the ability to pass through to their tenants the costs they incur under the CRC. The general consensus was against incorporating CRC provisions within leases given the complex nature of the scheme, the administrative burden of allocating costs and the relatively low costs of compliance. However, now that the CRC has become a cost to all Participants (i.e. there is no possibility of receiving a recycling payment that might exceed the costs of participating in the scheme) landlords will be more inclined to pass on these charges to their tenants.

If the landlord procures and pays for the energy supplied only to the common parts of the building or estate, the landlord would be advised to include the costs within a service charge or a separate CRC charge. Where

#### **LIVERPOOL**

Horton House, Exchange Flags, Liverpool L2 3YL  
0151 600 3000

#### **MANCHESTER**

55 King Street, Manchester M2 4LQ  
0161 836 8800

#### **PRESTON**

7-8 Chapel Street, Preston PR1 8AN  
01772 823921



the landlord's obligations extend to providing a supply of energy to the entire building, not only will this have to be dealt with in the terms of the lease but landlord will likely require greater monitoring of the tenants' energy consumption. Tenants will need to co-operate with landlords to provide them with up to date and accurate reports of their energy consumption and forecast requirements. Landlords will also need to exert some degree of control over tenants in their energy use to avoid consumption rising above the landlords' budgeted allowance. In recouping the costs of the CRC, landlords will need to be transparent in their method of allocating such costs to each and every tenant as the CRC operates on an organisation basis and not building by building.

The changes to the CRC may incentivise landlords to require tenants to procure and pay for their own energy use. In this way, the lease can remain silent and non-Participant tenants will avoid paying a premium for their energy use and the landlord will no longer be responsible for the CRC costs of the building.

### Next steps?

In terms of what this means for Participants going forward, the withdrawal of recycling payments will come as a blow to organisations which had understood that CRC to be revenue neutral. Further, the one year postponement of the need to purchase CRC allowances is little compensation since allowances will still have to be purchased in respect of 2011 - 2012 emissions, albeit only in 2012, so this is simply a timing issue.

Businesses which had begun to come to terms with CRC (and have already incurred costs, for example in achieving accreditation to the Carbon Trust Standard) will now have to adjust their strategies in the light of these changes, and for landlords and tenants, life has not become any easier.

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The Commercial Property department in the Manchester office is commended in the Legal 500 as an 'excellent' practice for industrial and logistics work with national coverage which provides 'a great balance between technical ability and commerciality' and 'excellent personal service'. The team is led by Tony Fitzmaurice who is described as 'commercially aware' in the 2010 edition of The Legal 500, which noted that Fitzmaurice's reputation enhances a well-respected team, which provides 'a great balance between technical ability and commerciality' and 'excellent personal service'. Matthew O'Brien, an Associate in the team is described as 'an excellent junior lawyer, old beyond his years.'

### Contact Details

For more information about the Logistics team and the service they provide please contact:



**Matthew O'Brien**  
Associate  
0161 836 8862  
[matthew.obrien@brabnerscs.com](mailto:matthew.obrien@brabnerscs.com)



**Claire Gregory**  
Associate  
Head of Environment and Regulatory  
0161 836 8858  
[claire.gregory@brabnerscs.com](mailto:claire.gregory@brabnerscs.com)

If you no longer wish to receive these bulletins please let us know by e-mail to [helen.calvert@brabnerscs.com](mailto:helen.calvert@brabnerscs.com)

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**LIVERPOOL**  
Horton House, Exchange Flags, Liverpool L2 3YL  
0151 600 3000

**MANCHESTER**  
55 King Street, Manchester M2 4LQ  
0161 836 8800

**PRESTON**  
7-8 Chapel Street, Preston PR1 8AN  
01772 823921

email: [law@brabnerscs.com](mailto:law@brabnerscs.com) [www.brabnerschaffestreet.com](http://www.brabnerschaffestreet.com)