

# UK ETS: Broken, but fixable

Secret subsidies: Many airlines received millions in subsidies last year via the UK ETS

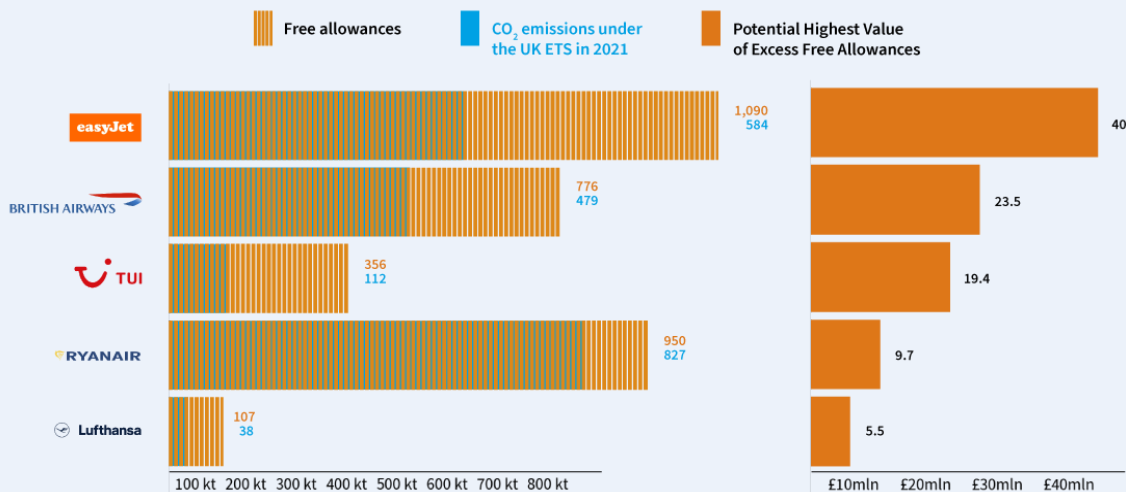
June 2022

## Executive Summary

In 2021, UK airlines received more free UK ETS allowances (i.e free pollution permits) from the Government than they were required to submit. In effect, this meant that the industry as a whole received a direct subsidy from the British taxpayer. In total, 4.4 million allowances were handed out for free: using the average 2021 UK ETS price of £55.59, these allowances were worth £242 million.

However, only 3.4 million allowances were required to be submitted to cover for airline emissions. This meant that on top of receiving free allowances to cover their ETS costs, airlines could sell the 'excess' allowances on the ETS secondary market and financially profit. If airlines sold at the height of the market (£79.20 per allowance), these excess allowances equalled a potential direct subsidy from the British taxpayer to the airline industry of £72 million.

## Top Five Airlines By Excess Free Allowances



EasyJet, Ryanair and British Airways received the most free allowances, and since all received more free allowances than they were required to submit, they were all directly subsidised. For example, easyJet received 506,000 more free allowances than they were required to submit. If easyJet chose to sell these excess allowances on to the secondary market, it would have received up to £40 million.

In theory, free allowances are handed out to prevent carbon leakage. In practice, the risk of carbon leakage in the aviation industry is minimal, and, so far under the UK ETS, free allowances have effectively acted as a direct transfer of money from the British taxpayer to the airline industry.

The UK has a golden chance to ‘fix’ the shortcomings of the UK ETS. Awarding free allowances to airlines should be completely withdrawn from 2024, and the scheme should be applied to all departing flights, regardless of destination.

## 1. Overview of the UK ETS

The UK Emissions Trading Scheme (ETS) is a cap and trade scheme that started on the 1st January 2021, following the UK’s exit from the EU ETS. Under the scheme, one tonne of carbon equals one allowance. To provide stability to the companies that participate in the scheme, the initial period of the UK ETS intentionally mirrors the EU ETS, and runs till 1st January 2024. However, after this time the Government has stated that it wants the UK ETS to be “[net zero consistent](#)”, and is therefore [consulting](#) on the best way to do so.

Whilst most aspects of the current scheme mirror the EU ETS, two climate friendly policies were introduced. Firstly, the total size of the cap is 5% lower than the UK’s previous share of the EU ETS, and secondly, an auction reserve price of £22 per allowance was introduced. This statement of intent clearly shows that the UK is determined to use the UK ETS as a major tool in reducing the UK’s emissions.

Aviation is included in the scheme, and airlines are obliged to surrender allowances for the carbon they produce from all UK-departing flights to other UK destinations, the European Economic Area, and Gibraltar.

### 1.1. Unjustified free allowances

Currently, the UK ETS also mirrors the EU ETS in awarding free allowances to airlines, in theory to mitigate against “carbon leakage”. Carbon leakage refers to a situation where production of a product may be moved abroad due to the increased costs that carbon policies impose. For physical products, like steel, this would mean a company relocating a factory from the UK to a country that does not have many, or any, carbon policies. For airlines, the core product is the transport of passengers from A to B, and therefore the risk of carbon leakage is almost non-existent (in addition, a domestic flight cannot be operated by a third country airline, given air traffic rights are determined by air service agreements).

The European Court of Auditors [also highlighted](#) that free allowances to aviation “support carbon-intensive air travel to the detriment of rail transport”. Furthermore, the European Commission [highlighted](#) that “a significant risk for carbon leakage for aviation due to the ETS has not been substantiated due to its very nature (difficulties or even impossibility to change/divert route due to the very nature of the traffic)”. This “undermines the effectiveness of the carbon price signal thereby removing incentives for aircraft operators to decarbonise their activities”.

[T&E published research in January 2022 that proved that the risk of carbon leakage \(under the EU ETS\) was low](#). This was then backed up by [UK specific research published in February 2022 by Frontier Economics](#) (which was jointly commissioned by the Department for Transport and Department for Business, Energy and Industrial Strategy) which found that “there is minimal risk of a trade-off between strengthening abatement incentives and reducing carbon leakage”: i.e that there was a minimal risk of carbon leakage under the UK ETS.

In conclusion, free allowances to airlines are being awarded for no economic or environmental reason.

## **2. Secret subsidies**

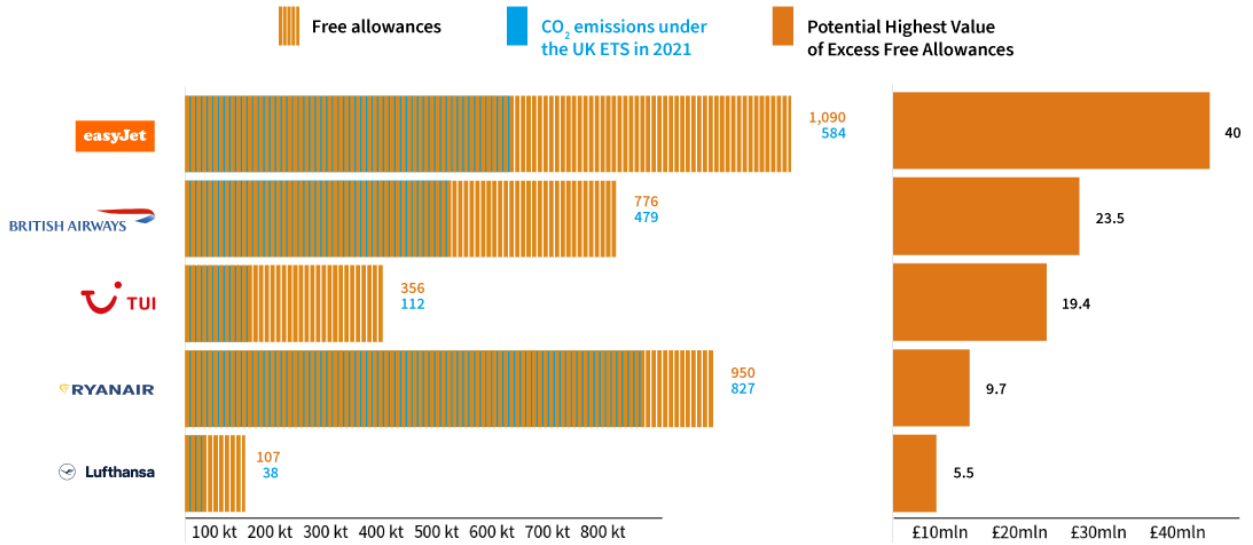
In 2021, the Government [distributed 4.4 million free allowances to airlines](#), but [the industry only emitted 3.4 million tonnes of carbon on flights under the scheme](#). This meant that - in direct contradiction of the polluter pays principle - the industry as a whole simply did not have to pay for any of the carbon emissions they released. At the average 2021 UK ETS price of £55.59 per allowance, these 4.4 million allowances were worth £242 million. 3.4 million allowances had to be returned, meaning that 0.9<sup>1</sup> million have been retained or sold back onto the UK ETS secondary market. Had the latter happened, airlines could have received up to £72 million. This money is, in effect, a direct subsidy from the British taxpayer to the airline industry.

This subsidy was not evenly distributed amongst individual airlines, and some airlines clearly benefited more than others. The table below shows the airlines that benefited from the first year of the UK ETS the most.

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<sup>1</sup> Discrepancy in figures due to rounding errors.

## Top Five Airlines By Excess Free Allowances



### Top Five Airlines By Excess Free Allowances

Airline <sup>2</sup>	Free allowances received (thousand)	Value of free allowances at average 2021 price (£million)	Allowances required to be submitted (thousand)	'Excess' allowances (thousand)	Value of excess allowances at highest 2021 UK ETS price (£million)	Value of excess allowances at lowest 2021 UK ETS price (£million)
easyJet	1,090	60.6	584	506	40.0	21.4
British Airways	776	43.1	479	297	23.5	12.6
TUI	356	19.8	112	245	19.4	10.4
Ryanair	950	52.8	827	123	9.7	5.2
Lufthansa	107	6.0	38	69	5.5	2.9

Source: T&E calculations, using a minimum 2021 UK ETS price of £42.40, and a maximum price of £79.20, based on the reported ETS price in the period 19/5/21 - 1/1/22. (ETS Price source: [Ember](https://ember.com))

<sup>2</sup> Grouped by parent organisation: see appendix

## 2.1. Highlights from the table

As can be seen, easyJet were the biggest winners, receiving nearly double the number of allowances for free than they had to submit. These ‘excess’ free allowances could either have been banked for use in future years, or sold on the secondary market. If easyJet chose the latter, then these free allowances equalled a direct subsidy from the UK Government of at least £21 million, and potentially up to £40 million. British Airways also received a direct subsidy of at least £13 million, and potentially up to £24 million, whilst TUI and Ryanair received subsidies of up to £19 million and £10 million respectively.

Not all airlines received ‘excess’ free allowances. Freight company DHL was required to buy the most allowances from the secondary market (possibly linked to current growth rates in freight transport). It received 49,700 allowances for free, but emitted 133,979 tonnes of carbon, so had to buy an additional 84,279 allowances. This still meant that DHL received £2.8 million worth of allowances for free,<sup>3</sup> and then had to spend a further £4.7 million to cover the cost of its emissions.

## 2.2. Most emissions come from long-haul and should no longer be ignored

Whilst a lot of attention is currently focussed on the UK ETS, it should be remembered that most carbon emissions from UK departing flights come from long haul flights: i.e. those flights not covered by the scheme. The UK ETS puts a price on carbon emissions on departing flights from the UK to other UK airports, the European Economic Area (EEA) and Gibraltar only. Whilst exact 2021 data is not available on total global emissions per airline, [data for 2019 is](#). That data indeed proved that collectively airlines do not pay for most of their pollution, although there were wide discrepancies between airlines. Only 14% of British Airways’ emissions were covered by pricing policies, meaning most of their flights and therefore emissions were exempt from carbon taxes. Conversely, 86% of Ryanair’s emissions were covered by carbon pricing measures, although both airlines received free allowances.

Nor can ICAO’s flawed carbon offsetting scheme (Corsia) be relied on to solve aviation’s climate problem on long haul routes, as highlighted by a [previous study conducted for the EU](#). In the EU, the European Parliament is looking to fully apply the polluter pays principle by integrating long haul routes into its ETS. It [recently voted](#) to apply the EU ETS to all flights departing the EEA, regardless of destination. Other measures agreed by MEPs include not distributing free allowances from 2025, and to start monitoring non-CO2 impacts.

Furthermore, the majority of aviation’s climate impact comes from the non-CO2 effects that planes cause. [Over 100 years carbon only accounts for one third of the climate impact planes cause, with the other two thirds coming from the non-CO2 climate impacts: principally from NOX emissions and contrail formation.](#)

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<sup>3</sup> Using the average 2021 UK ETS price of £55.59

### 3. Conclusions

The UK inherited a flawed ETS system from the EU, but is now consulting on exactly how to make the UK's version "net zero aligned". Clearly awarding free allowances to airlines is environmentally absurd. Doing so does not solve the non-existent problem of carbon leakage. Instead, it simply allows the Government to avoid implementing the polluter pays principle, and airlines to duck the responsibility of their climate impact.

The UK Government now has a golden opportunity to correct the mistakes from the first year of the UK ETS operation. Its own analysis says that there is minimal risk of carbon leakage, and the above analysis shows that free allowances have simply been subsidising an increasingly polluting industry. The UK Government aspires to be a climate leader, and therefore awarding free allowances to airlines should be completely stopped from 2024.

Furthermore, the European Parliament has proposed to apply the ETS to all departing flights from the EEA, which according to [analysis could save up to 53% more CO2 emissions than the EU's initial plans](#). This addresses the unfairness of the current scope of the ETS limited to intra-EU flights. This initiative makes sense from an environmental and economic point of view, and the UK should follow this lead.

In conclusion, the UK Government should:

- Completely stop awarding free allowances from 1st January 2024
- Extend the scope of the UK ETS to all departing flights, regardless of destination.

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## Appendix 1 - Parent Companies

Some airlines have multiple accounts in the ETS reporting system. These have been grouped by parent company, as seen in the table below

<b>Airline ALIAS</b>	<b>Identifiers in ETS log</b>
Aegean Airlines	AEGEAN AIRLINES S.A.
	AEGEAN AIRLINES SA
Aer Lingus	AER LINGUS LIMITED
	Aer Lingus Ltd
Air Malta	AIR MALTA P.L.C
	AIR Malta PLC
Alitalia	ALITALIA - SOCIETA' AEREA ITALIANA S.P.A. IN A.S. ITALY
	Alitalia Societa Aerea Italiana S.p.A
American Airlines	AMERICAN AIRLINES, INC.
ASL	27011.ASL Airlines Belgium
	ASL Airlines (Hungary) K.
	ASL Airlines (Ireland) Limited
	ASL Airlines Belgium
	ASL AIRLINES FRANCE S.A.
	ASL AIRLINES FRANCE SA
	ASL AIRLINES UK LTD
	Farnair Switzerland
Austrian Airlines	Austrian Airlines AG
BH Air Ltd	BH Air Ltd

	BH AIR OOD
Blue Air	BLUE AIR AVIATION S.A.
British Airways	BA CITYFLYER LIMITED
	BA CITYFLYER LTD
	British Airways PLC
Brussels Airlines	Brussels Airlines N.V. / S.A.
	BRUSSELS AIRLINES NV/SA
Bulgaria Air	Bulgaria Air
	BULGARIA AIR AD
Croatia Airlines	CROATIA AIRLINES D.D.
	Croatia Airlines Hrvatska Zrakoplovna Tvrtka d.d.
Delta	DELTA AIR LINES, INC.
DHL	DHL Air Limited
	DHL Air Ltd
	European Air Transport Leipzig GmbH
EasyJet	easyJet Europe Airline GMBH
	easyJet Switzerland SA
	EASYJET UK LIMITED
Etihad Airways	Etihad Airways
Eurowings	Eurowings GmbH
	GERMANWINGS GMBH
	Handelskonto der Germanwings GmbH
FedEx	11102.FedEx Express Corporate Aviation



	FEDERAL EXPRESS
	FEDERAL EXPRESS CORPORATION
Finnair Oyj	Finnair Oyj
Flexjet	FLEXJET OPERATIONS LIMITED
	FLEXJET, LLC
HiFly	HI FLY - TRANSPORTES AÉREOS S.A.
	HI FLY LIMITED
	Hi Fly, Transportes Aéreos, S.A.
Iberia	Iberia Express, S.A.
	IBERIA LAE SA OPERADORA SU
	IBERIA LINEAS AEREAS DE ESPANA SA OPERADORA
	IBERIA, Líneas Aéreas de España, S.A., Operadora
Icelandair	ICELANDAIR EHF.
	Icelandair ehf.
Jet2	JET2.COM LIMITED
KLM	KLM CITYHOPPER B.V.
	KONINKLIJKE LUCHTVAART MAATSCHAPPIJ N.V.
	Koninklijke Luchtvaart maatschappij NV
	Societe Air France
Loganair	Loganair Limited
	LOGANAIR LTD
Lufthansa	Deutsche Lufthansa AG
	DEUTSCHE LUFTHANSA AKTIENGESELLSCHAFT

	Lufthansa Cargo AG
	LUFTHANSA CARGO AKTIENGESELLSCHAFT
	LUFTHANSA TECHNIK AG
Norwegian	Norwegian Air (UK) Limited
	Norwegian Air International Limited AOHA
	Norwegian Air Shuttle AOC
	NORWEGIAN AIR SHUTTLE AOC AS
	Norwegian Air Sweden AOC AB
	Norwegian Air UK
	NORWEGIAN AIRSHUTTLE ASA
Qantas	QANTAS AIRWAYS LIMITED
Qatar Airways	QATAR AIRWAYS (Q.C.S.C.)
	QATAR AIRWAYS GROUP Q.C.S.C.
	QATAR AMIRI FLIGHT
	QATAR EXECUTIVE W.L.L.
Russian Airlines	AEROFLOT - RUSSIAN AIRLINES
Ryanair	Ryanair DAC
	RYANAIR DESIGNATED ACTIVITY COMPANY
	RYANAIR SUN S. A.
	Ryanair Sun S.A.
	Ryanair UK Limited
Scandinavian Airlines	Scandinavian Airlines
	Scandinavian Airlines – Ireland Limited

	SCANDINAVIAN AIRLINES SYSTEM DENMARK-NORWAY-SWEDEN
Smartwings	Smartwings AS
	SMARTWINGS, A.S.
Swissair	Swiss International Air Lines AG
Transavia	Transavia Airlines
	TRANSAVIA AIRLINES C.V.
	TRANSAVIA FRANCE
TUI	30011.TUI AIRLINES BELGIUM
	Handelskonto TUIfly GmbH
	Thomson Airways Limited
	TUI AIRLINES BELGIUM
	TUI Airlines Belgium N.V.
	TUI AIRLINES NEDERLAND B.V.
	TUI Airlines Nederland BV
	TUI AIRWAYS LIMITED
	TUIfly GmbH
	TUIfly Nordic AB
Turkish Airlines	TURKISH AIRLINES INCORPORATION
Virgin Atlantic	VIRGIN ATLANTIC AIRWAYS LTD
VistaJet	VistaJet Limited
Vueling	VUELING AIRLINES, S.A.
Wizz Air	WIZZ AIR HUNGARY LTD

WIZZ AIR UK LIMITED