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China Releases Carbon Allowance Trading Regulations

By Hui Xu, Paul A. Davies, Jean-Philippe Brisson and Qingyi Pan*

In this article, the authors discuss new regulations that aim to provide a legal framework for China's carbon allowance trading market by strengthening requirements and designating responsibilities.

Earlier this year, Chinese Premier Li Qiang signed a decree of the State Council, introducing the Regulations on the Administration of Carbon Allowance Trading (the Regulations). Effective from May 1, 2024, the Regulations provide a legal framework for the operation of China's emissions trading scheme (ETS), which initially commenced operations in July 2021 under ministry-level management rules without a higher-level legal foundation. The Regulations fill in the regulatory vacuum that has existed since 2021.

Together with the Chinese Certified Emission Reduction (CCER) Scheme, which was restarted on October 19, 2023, the development and strengthening of the China ETS reaffirms China's objectives to limit the growth of carbon dioxide emissions by 2030 and achieve carbon neutrality by 2060.[1]

PRIMARY RESPONSIBLE AUTHORITIES

Under the Regulations, the Ministry of Environment and Ecology (MEE) will be the primary agency responsible for supervising carbon allowance trading and related activities. The MEE is delegated to set out the thresholds of Covered Entities (see the definition below), also known as Key Emission Units, set up the annual cap of carbon allowances and the allocation plan for free allowances, as well as formulate technical specifications of the emissions report. Some other agencies (collectively, Other Relevant Agencies) will share certain responsibilities according to their respective duties and expertise, including the following:

- The State Administration for Market Regulation of China (SAMR), the People's Bank of China (PBOC), and the National Financial Regulator Administration of China (NFRA) will help supervise the national carbon allowance tracking system and trading exchange.

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[1] Xi Jingping's speech at the General Debate of the 76th Session of the UN General Assembly (Sept. 21, 2021), see https://www.fmprc.gov.cn/mfa_eng/wjb_663304/zzjg_663340/gjs_665170/gjsxw_665172/202109/t20210923_9580159.html (last visited on Feb. 18, 2024).

- The National Development and Reform Commission of China (NDRC) will help set up greenhouse gas (GHG) categories and industry scopes.
- Local MEEs will take charge of monitoring local carbon allowance trading and related activities, including compiling the annual list of covered entities, allocating free allowances, verifying annual emissions reports, and conducting on-site examinations of Covered Entities and technical service institutions.

The Regulations authorize the establishment of a national allowance tracking system and a trading exchange. The tracking system will enable participants of the national ETS to register and settle carbon allowance transactions. The trading exchange will provide a unified and centralized platform for participants to trade carbon allowances. Both the national carbon allowance tracking system and the exchange will include risk management and information disclosure mechanisms to reduce market manipulation risks.

In addition, technical service institutions may also be established to help Covered Entities conduct GHG testing and prepare the annual emissions report, or to help local MEEs conduct technical reviews on the annual emissions report, though they cannot serve both sides in the same province due to conflict of interests.

PARTICIPANT ELIGIBILITY AND TRADING SCOPE

Under the Regulations, Covered Entities and qualifying voluntary participants can participate in carbon allowance trading either by agreements or in auctions. Under the previous ministry-level management rules, which came into force on February 1, 2021, a "Covered Entity" was defined as an entity operating within a specific industry scope of the China ETS with annual GHG emissions equivalent to 26,000 tons of carbon dioxide or more. The Regulations have not changed the threshold; instead, they leave it to the MEE's discretion. The Regulations have not provided rules or requirements for qualifying voluntary participants.

The staff of the MEE, Other Relevant Agencies, the national carbon emission tracking system and trading exchange, and technical service institutions are all prohibited from carbon allowance transacting allowances, including spot transactions and other tradable products approved and to be approved by the State Council.

OTHER PRIMARY FEATURES

Data Quality Control

Under the Regulations, Covered Entities must ensure the authenticity, completeness, and accuracy of their emissions accounting data and annual emissions reports. They must also disclose the emissions inventory, emissions facilities, and accounting methods and other information in their annual emissions reports.

The original records and management accounts of the data involved must be kept for at least five years. Technical service institutions entrusted to conduct GHG testing, prepare annual emissions reports, and conduct technical reviews will be responsible for the corresponding reports and opinions. Tampering with or falsifying data, or using fake data is prohibited.

Penalty Level

The Regulations adopt a series of multi-dimensional administrative penalties and stress the importance of data veracity, as shown in Table 1.

Table 1

Types of violations Relevant subjects	Data fabrication	Non-performance (Failure to surrender allowances)	Other administrative violations
Covered entities	• Confiscation of illicit earnings • Fine of five to 10 times the illicit earnings • Reduction of free allowances between 50% and 100% for the next compliance period • Suspension of business The directly responsible persons may face a fine of up to RMB200,000 (approximately US$27,780).	• Fine calculated at five to 10 times the average market price of the previous month of the compliance deadline • Reduction of free allowances equivalent to such non-performance for the next compliance period • Suspension of business	If a Covered Entity fails to comply with its data quality control plan, file emissions accounting data or annual emissions reports, disclose certain key information in annual reports, or keep the original records and management accounts, it may face: • A fine between RMB50,000 and RMB500,000 (approximately US$6,945 to US$69,450); and/or • A suspension of its business.
Technical service institutions	• Confiscation of illicit earnings • Fine of five to 10 times the illicit earnings • Permanent revocation of the business license The directly responsible persons may face a fine of up to RMB200,000 (approximately US$27,780), and a five-year/permanent ban from practice.	N/A	N/A
Voluntary participants	Not explicitly provided by the Regulations.		

The Regulations also impose administrative penalties on market manipulation and disruption. Any entities or individuals that manipulate or disrupt the national ETS may face confiscation of illicit earnings, and a fine of one to 10 times such earnings. The directly responsible persons of such entities may face a warning, and a fine of up to RMB1,000,000 (approximately US$138,900). Resistance to or obstruction of the MEE's supervision may result in a fine between RMB20,000 and RMB200,000 (approximately US$2,778 to US$27,780). The above penalties will be recorded in the national credit system and disclosed to the public. Criminal liability may also be imposed and enforced to the extent that the violation constitutes a crime.

Unlike the ministry-level management rules, the Regulations enhance MEE's supervision capacity and increase penalties. Under the ministry-level management rules, data fabrication of covered entities may result in a fine of RMB10,000 to RMB30,000 (approximately US$1,389 to US$4,167), and/or a reduction of free allowances. Non-performance of surrendering allowances of covered entities may result in a fine of RMB20,000 to RMB30,000 (approximately US$2,778 to US$4,167), and/or a reduction of free allowances.

Regional Carbon Allowance Trading Market

Parallel to the national ETS, China has been running eight regional pilot carbon markets – Beijing, Tianjin, Shanghai, Chongqing, Guangdong, Hubei, Shenzhen, and Fujian ETS – each with its own trading rules. While allowing a dual-track system of both national and regional carbon allowance trading markets, the Regulations clarify that no new regional carbon allowance trading market will be further established in the future. Covered Entities under the national ETS will no longer participate in the regional pilot carbon markets of the same GHG category and in the same industry.

Covered Entities should prepare for the stricter compliance requirements and enhanced penalties for non-compliance effective on May 1, 2024, under the Regulations. Along with designating clear responsibilities to various authorities, establishing a national allowance tracking system and trading exchange, and possibly setting up technical service institutions to assist Covered Entities, these measures underscore China's move toward its short- and long-term emissions and environmental goals.

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