

UK CRC Energy Efficiency Scheme

The UK CRC Energy Efficiency Scheme will require some private equity firms with controlling stakes in portfolio companies that have UK operations to register with the UK Environment Agency.

The UK CRC Energy Efficiency Scheme comes into effect on 1 April 2010. Private equity firms with controlling stakes in portfolio companies with UK operations may be required to register with the UK Environment Agency by 30 June 2010.

What is the UK's Carbon Reduction Scheme?

The UK Carbon Reduction Commitment Energy Efficiency Scheme ("CRC") is a mandatory climate change and energy saving scheme that is being introduced as part of the UK's strategy to control carbon dioxide (CO₂) emissions. The CRC operates on a "cap and trade" basis. The government will sell CRC allowances (carbon credits) each year, in units representing the right to emit one tonne of CO₂. Participants can then trade allowances between themselves at a free market price, creating a financial incentive to reduce CO₂ emissions and sell surplus allowances. At the end of each year, participants must surrender sufficient allowances to cover their carbon emissions for that year.

Am I Affected?

Any private equity firm whose portfolio included, on 31 December 2008, a controlling stake in a company with UK operations must consider whether it is required to register with the UK Environment Agency as a CRC participant. Any UK-based business that had, during 2008, a "settled half-hourly" electricity meter (an "HHM") is required to comply with the CRC in some way. The level of participation required is determined by annual electricity consumption.

An organisation that fails to register is potentially liable to a fine of up to £45,000, and may also be "named and shamed." In addition, the Environment Agency may serve an enforcement notice requiring the organisation to register for the scheme. Failure to comply with an enforcement notice is a criminal offence for which a company's officers may be prosecuted personally.

Group Participation

Organisations are required to participate in the CRC on a group-wide basis. Only UK energy consumption is counted for the purposes of the CRC, both when assessing the level of participation required and when reporting annual usage and surrendering allowances, but all members of the group, even non-UK members, are jointly and severally liable for CRC compliance. In particular, the highest parent entity within a structure has additional administrative responsibilities.

Membership of a group is determined for CRC purposes by applying the same tests used for determining an accounting group, as set out in the UK Companies Act 2006. There is some legal uncertainty surrounding the application of these tests to limited partnership structures. However, the Environment Agency has indicated that it will be applying the following basic principles when assessing compliance by private equity funds:

- A majority-owned portfolio company will be treated as a subsidiary of, and therefore will be grouped with, the private equity fund that owns it.
- The private equity fund will be treated as a subsidiary of, and therefore will be grouped with, its general partner, such that:
 - All parallel funds with the same general partner (and their respective portfolio companies) will be treated as part of the same group.
 - If a number of general partner vehicles are under common ownership, all those general partners, the funds of which they are general partners and the majority-owned portfolio companies of those funds will form a single CRC group under the ultimate parent.

The Environment Agency has acknowledged that there are variations between structures, but any private equity organisation that does not register on this basis will be expected to demonstrate, based on appropriate legal advice, the justification for taking an alternative approach.

Steps to Take

The first step is to establish whether your organisation falls within the qualification criteria for the scheme:

1. Determine your group structure as at 31 December 2008.
2. Determine whether the UK-based operations of any portfolio company forming part of that group had, at any time during 2008, an HHM. If not, your group is not within the CRC and no further action is required.
3. If any member of the group had an HHM, it is necessary to assess the group's aggregate half-hourly metered UK electricity consumption for the calendar year 2008, calculated on the basis set out in the CRC legislation.
 - a) If the total is less than 3,000 MWh, you must provide to the Environment Agency, through an online registration system, details of the group's HHMs and contact details for your organisation.
 - b) If the total is between 3,000 MWh and 6,000 MWh, you must additionally provide details of the total electricity consumption for 2008.
 - c) If the total is 6,000 MWh or more, the group will be a full CRC participant and must register online for the carbon allowances trading scheme.

Registration opens on 1 April 2010. The deadline for registration is 30 June 2010 if you intend to "disaggregate" those parts of the group that would qualify for participation in their own right, and 30 September 2010 for all other participants.

By default, the entity with responsibility for registration will be the highest parent entity within the group. However, if this is a non-UK entity, the highest parent must nominate a UK-based member of the group to be the CRC Account Holder, with responsibility for administering the scheme on behalf of the group, and private equity firms will need to consider which entity should undertake this role.

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