

LENNARD DE KLERK OFFERS SOME PERSPECTIVES ON PROLONGING CARBON TRADE IN UKRAINE AND RUSSIA POST 2012

Bridging the gap

Given the complexities of UN climate change negotiations, the chances of a new global deal being reached this year in Cancun, or even in 2011 in South Africa, are slim. Should a new international accord be adopted in 2012, a ratification process of a couple of years will be needed. Therefore, it is unlikely that any agreement will enter into force before 2015 or 2016.

The EU will continue the region's emissions trading scheme (ETS) into a third phase (2013–2020), despite the lack of progress internationally. Furthermore, the EU has committed to reduce its greenhouse gas (GHG) emissions 20 per cent below 1990 levels – possibly to 30 per cent – by 2020.

It cannot be expected that Ukraine and Russia – non-EU members – will take on stringent targets after 2012. Emissions in both countries fell after the Soviet Union collapsed and the economies are expected to grow and recover in the coming decade.

Industrial installations in Ukraine and Russia have no cap on their GHG emissions, as no ETS or carbon tax exists. In Ukraine, in recent years, several draft laws have been proposed to introduce an ETS, but none have been adopted.

Ukraine's draft ETS law

On 23 September, a draft law was submitted to Ukraine's parliament proposing an emissions trading scheme (ETS). The main elements of the draft are:

- 2011–2012: Setting-up an emissions monitoring system at the installation level;
- 2013–2016: Collecting emissions data at the installation level;
- 2017–2018: First phase of trading with “no lose” targets (no penalties);
- 2019–2020: Second phase of trading with penalties;
- Allocation of allowances for the first phase will be based on grandfathering;
- There will be a carbon-neutral growth reserve for installations that increase production, but reduce specific emissions;
- Provisions to link the Ukraine ETS with other trading schemes; and
- Provisions to allow joint implementation projects in conjunction with the Ukraine ETS.

On 23 September, a new draft was published calling for the introduction of a cap-and-trade scheme, but which will only get a cap in 2017 (see box).

Given the above developments, there will be no incentive to reduce emissions in Ukraine and Russia in the immediate post-2012 period. Investors in joint implementation (JI) – one of Kyoto's project-based flexible mechanisms – will be also reluctant to look at new projects in the two countries, as the return on the investment is unsure.

The only way to promote new investments and new technologies is to implement temporary measures to “bridge the gap” between 31 December 2012 and a domestic ETS and/or a new international agreement. Given many people believe the existing Kyoto framework should be preserved, several ‘gap’ measures are being discussed, both at UN and EU level.

Here I propose some gap measures specifically for Ukraine and Russia, which could also be applied to other Annex I – industrialised – countries, such as Belarus or developing countries that may become Annex I.

In order to incentivise market participants to invest in new technologies to reduce emissions, two criteria should be met. First, emission reductions post 2012 should be issued with carbon credits that can be transferred, and, second, the credits should be eligible for use under compliance regimes. Only then will the reductions have meaningful value.

First “gap” measure: continued issuance until the end of the true-up period. After 31 December 2012, a compliance procedure will start to assess whether a Kyoto party is in compliance with the protocol's first commitment period (2008–2012). The process comprises a review of the last GHG inventory of 2012 and the amount of Kyoto units the country holds. These units are AAUs, certified emissions reductions (CERs – credits from the clean development mechanism) and emissions reduction units (ERUs – JI credits).

Following the conclusion of an expert review, a party has an additional 100 days to trade AAUs, CERs/ERUs. This time is also referred to as the “true-up” period and is expected to end in mid-2015. It provides an opportunity to verify reductions generated in 2013 and 2014 and issue ERUs respectively. The ERUs will be used for compliance during the first commitment period. Therefore, the first gap measure can be implemented under the existing framework of Kyoto.

The JI guidelines do allow for post-2012 issuance as long



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as the country hosting the project approves the extension of the crediting period beyond the first commitment period. This is the most straightforward gap measure that countries, such as Ukraine and Russia, could implement.

Second gap measure: bilateral agreements between Ukraine/Russia and the EU. The EU ETS is the only multilateral carbon compliance regime that is certain to operate beyond 2012. From 2013, more EU allowances will be allocated by auctions and the overall cap will be 21 per cent below 2005 levels, assuming a 20 per cent target against 1990 for the whole of the EU – or 34 per cent if the target becomes 30 per cent.

In the second phase of the ETS (2008–2012), CERs and ERUs are eligible for compliance, albeit with some qualitative and quantitative restrictions. The third phase of the ETS also allows for the usage of CERs and ERUs, although in absence of an international agreement, at a limited scale.

However, the EU emissions trading directive hints at expanding the usage of ERUs through the conclusion of bilateral or multilateral agreements. “In the event of the conclusion of an international agreement on climate change being delayed, the possibility should be provided for to use credits from high-quality projects in the community scheme through agreements with third countries. Such agreements, which may be bilateral or multilateral, could enable projects that generated ERUs until 2012, but are no longer able to do so under the Kyoto framework, to continue to be recognised in the community scheme” it says.

Similar language exists for bilateral or multilateral agreements for CDM projects with non-Annex I countries. But bilateral agreements with Russia and Ukraine have a strategic dimension beyond the climate discussion.

Russia is a supplier of energy to Europe. Ukraine is the main transit country of natural gas to Europe. It is of strategic importance to Europe that both countries invest in energy efficiency to support energy security in Europe. Only

if Russia reduces its energy consumption significantly will enough energy supply remain for the next generation. Only if Ukraine reduces the energy intensity of its industry can the country afford to pay market prices for natural gas and avoid “gas wars” with Russia.

Furthermore, European industry has the opportunity to increase exports of new technology. A bilateral agreement will also strengthen the ties between the EU and a potential future member state, such as Ukraine.

In the context of EU climate policy, the bloc aims to promote regional cap-and-trade schemes and link with them. Ukraine made the first steps in the latest draft ETS law. Such a scheme will not be up-and-running soon, but a bilateral agreement could bridge the gap and fit with EU policy goals, as well as ensure the continuation of JI.

Bilateral agreements will have to outline what JI credits will be allowed in the EU ETS. For example, how to register new projects after 2012 and how will “high-quality” be interpreted? The infrastructure created by the JI supervisory committee – the UN panel that administers the scheme – can play an important role by recognising its approved verifications as the compliance unit replacing the ERU.

With the first 15 JI projects approved in Russia recently and a second tender launched in September, there is renewed interest in the mechanism. Not only have Russia and Ukraine a large untapped reduction potential, the countries are close to the EU and are of strategic interest to the region.

The EU took the first steps by including the option for bilateral agreements in the emissions trading directive. Given the delay in achieving a new global treaty, now is the time for the EU, Russia and Ukraine to bridge the gap. ●

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