SKPI Legal Primer
Introduction Presentation

Project SKPI Workshop

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Presentation Overview

• Introduction to project team member Hogan & Hartson
• Concept of Legal Primer
• Key Chapters of Legal Primer
  • Types of Certificates and Transactions
  • KP Registry System
  • Role of National Legislation
Introduction – Who is Hogan & Hartson?

- Hogan & Hartson is a **global law firm** with offices all over the world and over 1,100 lawyers.

- Hogan & Hartson is **part of the implementation team** for the project “Support to Kyoto Protocol Implementation (SKPI)”, funded by the European Union, together with **ICF** and **TÜV Rheinland**.

- Hogan & Hartson has a preeminent **Climate Change Practice** with global reach. Experience in field of Kyoto Protocol implementation/CDM includes:
  - Role as carbon manager for **MCCF**, a multilateral carbon credit fund (approx. 195 Mio. € commitment) for EBRD/EIB, in a consortium with ICF.
  - Advise to the **Russian Federation** in the implementation of Kyoto Protocol, especially on registry and inventory issues (EU TACIS project), in a consortium with ICF.
  - Advise with regard to numerous CDM and JI projects and AAU trades, involving credits (CERs, ERUs, and AAUs) with current fair market value of over $500 million.
Legal Primer Presentation
Concept of the Legal Primer

The Concept of the SKPI Legal Primer is:

To enhance participation in the KP Flexible Mechanisms...

... by providing a basic legal guide comprehensible for non-lawyers...

... which can serve as a basis for more specific support by legal advisors.
The Legal Primer focuses on three areas:

- Most important KP emission credit and transaction types
- KP Registry System
- Role of national legislation in KP implementation and carbon transactions
Legal Primer Presentation
Carbon Transactions: KP Flexible Mechanisms

• Legal Primer centers around three **KP flexible mechanisms**:
  
  – **International Emissions Trading** (IET) allows sale and purchase of Assigned Amount Units (**AAUs**) and other units (Removal Units - RMUs, CERs, and ERUs) between Annex 1 countries
  
  – **Joint Implementation** (JI): Annex 1 countries or legal entities from such countries implement emission reduction projects in other Annex 1 countries to generate Emission Reduction Units (**ERUs**) 
  
  – **Clean Development Mechanism** (CDM): Annex 1 countries or legal entities from such countries get involved in emission reduction projects in non-Annex 1 countries to generate Certified Emission Reductions (**CERs**) 

• Legal perspective is important, as **emission credits are “legal creatures”**

• **Legal Primer** looks at each mechanism and **analyzes**:
  
  – **Nature** of unit type (AAU, CER, ERU)
  
  – **Generation** of unit type 
  
  – **Trading** of unit type
Legal Primer Presentation
Units and Transaction Types

**AAUs**
- Represent Party's assigned amount under KP
- Not generated, but assigned
- Trading between Annex 1 states as well as "authorized entities"

**CERs**
- Represent emission reductions achieved by CDM project
- Generated through CDM project
- Trading between member states and private entities

**ERUs**
- Represent emission reductions achieved by JI project
- Converted from AAUs
- Trading between member states and private entities
For each emission credit type, the Legal Primer outlines...

- **Generation mechanism** (for CERs and ERUs)
  - Important legal provisions
  - Project cycles
- **Trade types** (primary and secondary purchases) and **trade parties**
  (sovereign and private buyer groups)
- Characteristics of **trade agreements**
  - ERPA for CERs and ERUs
  - AAU-PA for AAUs (including Green Investment Scheme)
Legal Primer Presentation
Registry System

- As KP emission certificates have no physical existence, they only exist within systems which can record their existence.

- Such systems are referred to as KP Registry System.

- Emission certificate trades take place in various forms (individual, over-the-counter, exchanges), but must all be settled in KP Registries.

- Different registries form KP Registry System:
  - National Registries (only for Annex I states)
  - CDM Registry at UNFCCC
  - International Transaction Log (ITL) to connect all National Registries and CDM Registries
  - Within EU: EU-wide registry (CITL) to record EU Emission Trading Scheme transaction, also connected to ITL.
Legal Primer Presentation
KP Registry System

(Source: http://unfccc.int/kyoto_protocol/registry_systems/items/2723.php)
Legal Primer Presentation
Role of National Legislation

- KP and its flexible mechanisms must be implemented by national laws
  - Registry creation (for Annex I countries)
  - National framework for participation in JI and CDM
- Apart from direct implementation, questions arise regarding national legal treatment of KP Units
  - “Legal nature”
  - Property rights and transfer of property
  - Contract law
  - Financial services regulation
  - Taxation
  - Accounting treatment under national and international standards,
  - State aid, competition and international trade law
- Relationship between international and national laws often leads to problems
Legal Primer Presentation
Examples of National Legislation

- Legal Primer provides for **examples** of national **implementation in large EU economies**
  - **Advanced KP implementation**
  - Important emission credit **buyer countries**
  - **Examples** can help to shape **own legislation**

- Legal Primer **assesses legislation in**
  - EU (applicable for all EU member states)
  - Germany
  - United Kingdom
  - France

- Focus on examples which are most **“universal” for all jurisdictions:**
  - Means of **KP flexible mechanism implementation** (translated national laws as annexes)
  - **Regulation** of emissions trading
JI and CDM: Requirements and Project Cycle
• JI and CDM can only be supplementary to domestic emission reduction efforts of Annex 1 countries (cap in EU states!)

• Their objective is to allow for the most cost-effective ways of emission reductions

• JI and CDM allow for the involvement of private entities in emission reduction efforts

• EC Linking Directive enables private entities to use ERUs and CERs to meet their compliance targets under the European Emissions Trade Scheme (EU ETS)

• Renewable Projects can be eligible as JI/CDM, and generated credits therefore be used as financing tool
## Legal Primer Presentation
### Background: Differences between JI and CDM

<table>
<thead>
<tr>
<th>JI</th>
<th>CDM</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transfer of carbon credits between Annex 1 countries</td>
<td>Creation of additional carbon credits</td>
</tr>
</tbody>
</table>
| Two verification procedures  
  - Host Country satisfies only minimum requirements: **Track 2** procedure under the rules and supervision of the JI Supervisory Committee (JISC)  
  - Host Country satisfies additional requirements: **Track 1** procedure set up by and supervised by Host Country | Single verification procedure  
  - Under the rules and supervision of the CDM Executive Board (EB)  
  - Special provisions for small scale projects |
| ERUs cannot be used in the first phase of EU ETS | CERs can be used in the first EU ETS phase |
Legal Primer Presentation
Background: Overview CDM Key Features

- **Objective** of the CDM mechanism is to allow for the most cost-effective way to achieve emission reductions.

- CDM allows for the involvement of **private entities** in emission reduction efforts.

- Use of Credits for CDM (CERs) can only be **supplementary** to domestic emission reduction efforts of Annex 1 countries (cap in EU states!)

- EU “**Linking Directive**” enables private entities to use CERs to meet their compliance targets under the European Emissions Trade Scheme (EU ETS): Up to date most important demand factor.
## Legal Primer Presentation
### Background: CDM Participants

<table>
<thead>
<tr>
<th>Host Country</th>
<th>Investor Country (Annex 1)</th>
<th>Project Participants</th>
</tr>
</thead>
</table>
| - Party to the KP  
- Not Annex 1 Party  
- Voluntary participation  
- Designated National Authority shall be in place | - Party to the KP  
- Voluntary participation  
- Designated National Authority shall be in place  
- National registry in place  
- Assigned Amount established  
- Required inventory submitted | - Private entities must be authorized by a Party to participate  
- The authorizing Party must be eligible for participation |
Legal Primer Presentation
Background: CDM Project Requirements

• The project assists the Host Country to achieve **sustainable development**

• The project provides real, measurable, and long-term benefits related to the **mitigation of climate change**

• The project delivers reductions in emissions that are **additional** to any that would occur in the absence of the project activity ("**Additionality Criterion**")

• The type of project is **eligible** for CDM registration: Project Methodology must be accepted by CDM Executive Board
Project Idea Note

Provided by Project Participants

- No legal requirement
- Contains indicative project information including estimation of reductions
- Allows advance check of Kyoto compliance
Legal Primer Presentation
Background: CDM Project Cycle

**Project Idea Note**

**Project Design Document**

- General description of project activity
- Application of a baseline methodology
- Starting date and duration of the project activity/Crediting period
- Application of a monitoring methodology and plan
- Estimation of GHG emissions by source
- Environmental impacts
- Stakeholder Comments

Completed by **Project Participants** in the form required by the EB
The LoA states that:
- The Party has ratified the KP
- The participation in the project is voluntary
- The proposed project contributes to sustainable development (only in the case of Host Party)
Legal Primer Presentation
Background: CDM Project Cycle

Project Idea Note

Project Design Document

Letter of Approval

Validation

By Designated Operational Entity (DOE)

Independent evaluation of the project by a DOE regarding:
- Participation requirements
- Baseline and Additonality
- Monitoring plan
- Environmental impact and stakeholder comments

Following a successful validation, the validation report will be presented to the EB for registration.
Registration is the formal acceptance by the EB of a validated project as a CDM project.

- Prerequisite for the verification, certification and issuance of CERs.
- Occurs automatically within 8 weeks unless a review is requested.
Implementation of Monitoring Plan set out in PDD requires:

- Collection and archiving of all data necessary for estimation of emissions and determination the baseline
- Data for assessment of environmental impacts
- Quality assurance of monitoring process

The results are to be provided to the DOE in Monitoring Reports.
Verification = periodic review by DOE of monitored reductions resulting from project

Certification = assurance by the DOE to the EB that project actually achieved verified reductions and request for issuance of CERs

Cannot be carried out by Validation DOE

Certification Report constitutes request for issuance of CERs to EB, to the verified amount of reductions
By EB

- Considered final 15 days after date of receipt of request for issuance, unless review is requested
- After deduction of 2% of the total CERs to cover administrative costs, CDM registry will forward remaining CERs to registry accounts of Parties and/or project participants involved
### Background: JI Eligibility Requirements

<table>
<thead>
<tr>
<th>Track 1</th>
<th>Track 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>(full eligibility requirements)</td>
<td>(minimum requirements)</td>
</tr>
<tr>
<td>• Host Country is a Party to the KP</td>
<td>• Host Country is a Party to the KP</td>
</tr>
<tr>
<td>• Its assigned amount has been calculated and recorded</td>
<td>• Its assigned amount has been calculated and recorded</td>
</tr>
<tr>
<td>• It has a national registry in place</td>
<td>• It has a national registry in place</td>
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<tr>
<td>• It has in place a national system for the estimation emissions</td>
<td></td>
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<tr>
<td>• It has submitted annually the most recent required national inventory of emissions</td>
<td></td>
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<tr>
<td>• It has submitted supplementary information on its assigned amount and has made the accurate additions to, and subtractions from, its assigned amount</td>
<td></td>
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Legal Primer Presentation
Background: JI Project Cycle Track 1

Project Idea Note
By Project Participants
No legal requirement

Project Design Document
Completed by Project Participants as required by JISC

Letter of Approval
Issued by the Host and Investor Country

Validation
By Accredited Independent Entity (AIE)
- AIEs are accredited by JISC
- Validation is made publicly available

Issuance ERUs
by Host Country
(ERUs are transformed AAUs or RMUs of the Host Country)

Review
by JISC
Only if requested within 15 days

Verification
by AIE
Verification is made publicly available (including a justification)

Monitoring
by Project Participants
Monitoring Reports are to be submitted to AIE

Review
by JISC
Only if requested within 45 days of the publication of the Validation
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