



**CLIMATE**FOCUS

Carbon Offsetting in  
Europe Post 2012  
Kyoto Protocol, EU  
ETS, and Effort Sharing

This report has been funded by the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety. The views expressed are those of the authors and do not necessarily reflect the views of the German Government or of KfW Bankengruppe.

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4 April 2011

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Version 2.0

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## Executive Summary

The difficulties faced by international negotiations in finalizing an agreed framework for post-2012 international greenhouse gas (GHG) emission regulation have left the rules relating to carbon offsetting in limbo. Though neither the Kyoto Protocol nor its component structures and mechanisms will cease to exist after 2012 in the absence of a further agreement, a gap in which no quantified emission reduction commitments are in force would create significant uncertainty regarding the continuity of various activities relating to the flexible-mechanisms under the Protocol. Given the various political and logistical challenges of having a subsequent commitment period or new agreement enter into force before 1 January 2013, such a gap appears likely. Moreover, though specific provisions in new EU legislation relating to offset trading provide for the avoidance of many such uncertainties, the EU framework contains uncertainty of its own in the event of a gap.

Though in terms of project activities the Clean Development Mechanism (CDM) remains the dominant flexible mechanism under the Kyoto Protocol, upward trends in Joint Implementation (JI) project activities and JI's arguably greater suitability as a model for future crediting mechanisms make it curious that greater attention has not been paid to the future of the mechanism itself. Indeed, its intrinsic connection with emission targets and assigned amounts under the Protocol (the QUELROs) makes uncertainty with regard to JI somewhat more worrying.

### JI under the Kyoto Protocol

There is general agreement that the absence of a commitment period does not directly affect the existence of JI or its institutional set-up. Moreover, the Joint Implementation Supervisory Committee (JISC) has indicated that such an absence would not affect Parties' eligibility to engage in JI, a view that appears well-founded, at least up to the end of the true-up period. It also appears relatively settled that Parties can issue emission reductions post 2012 in respect of reductions taking place up to the end of that year, and can trade ERUs until the end of the true-up period.

However, there is less consensus regarding the question whether post 2012 emission reductions (gap period ERUs) from either existing or from new projects can qualify for ERU issuance from the CP I AAU contingent. A convincing argument can be made that the continuation of operations includes emission reduction activities after 2012 and the generation of credits, as long as the exclusive relationship to CP I is guaranteed. Though initially opposed to this view, the UNFCCC Secretariat has recently stepped away from its previous stance, indicating that JI activities relating to CP I can continue until the end of the true-up period. It has, however, continued to express doubts over the basis upon which ERUs can be issued, and on the whole appears to believe that guidance from the CMP is required on the matter. The JISC, for its part, has demonstrated a similarly ambivalent stance on the matter, and has expressly called for CMP clarification. The two most feasible conclusions are, thus, that either the current regulatory framework allows for the continued issuance of ERUs for post 2012 emission reductions, or that there is a regulatory void requiring CMP guidance.



The CMP failed to address the matter in Cancun in December 2010, leaving the seventh session of the CMP in Durban later this year as the next available opportunity to clarify matters. Though sensitivities in the negotiations concerning the future of the Kyoto Protocol and the carryover of AAUs create uncertainty as to whether the CMP will address the issue, there remain several negotiating sessions throughout 2011 at which positive signals can be sent to national policy makers and investors. If no agreement is reached by the end of 2012, parties may decide to bilaterally continue projects based on their own interpretations of the current rules. Depending on the eventual view taken by the JISC, this could potentially lead to Tracks 1 and 2 taking diverging paths.

Whether JI can continue beyond the true-up period essentially depends on whether subsequent commitments are agreed to under the Kyoto Protocol or an alternative agreement and, if they are, when they will be ratified and enter into force. As the current rules imply ratification acts of more than 140 State Parties, it may well happen that the Kyoto gap continues beyond 2015. Several technical and political solutions have so far been discussed to tackle this situation, most of which, however, fail to overcome the express ratification threshold set by the Protocol.

#### JI, Article 11 (a), (b) and Article 24a EU ETS

Recent EU legislation extending and renewing the EU ETS and creating a new framework covering the majority of non-EU ETS emissions (the Effort Sharing Decision, or ESD) has introduced a new potential offset mechanism distinct from and independent of the Kyoto framework, in the form of Article 24a EU ETS. The need for implementing provisions (through comitology procedures) means, however, that it is at present difficult to predict the relationship of this mechanism with pre-existing mechanisms such as JI. Indeed, whether such a mechanism will be created at all is at present uncertain, and is likely to depend to a large degree on dynamics between the EU Commission and certain Member States during the course of 2011.

The fate of JI itself, moreover, is subject to significant uncertainty with regards both the EU ETS and the ESD. In relation to the EU ETS the question is twofold. First, how does the EU ETS treat JI projects and credits in the post-2012 scenarios (with and without a second commitment period)? Second, what is the status of intra-Member-State JI, i.e. of JI projects hosted by any EU Member State? The first question is problematic only insofar as there is a gap. Where a second commitment or a new agreement enters into force, the future of JI is guaranteed. Where there is a gap, uncertainty stems from statements in the recitals of both the revised EU ETS Directive and the ESD that JI cannot continue post 2012 in the absence of an international agreement. Despite this, however, the substantive text of both pieces of legislation appears to indicate that, should ERUs be available for post-2012 emissions, they will be accepted into the EU schemes.

The issue of intra-Member-State JI is more contentious. Various paragraphs in the recitals of both instruments raise the question of whether they consider JI a third-country mechanism only. As projects registered after 2012 are restricted to those recognised pursuant to agreements with third countries or in countries that have ratified a global agreement the question of intra-Member States JI in practical terms only relates to pre-2013 registered (determined) projects.

The strongest argument against the recognition of ERUs generated by pre-2013 projects in Member-States from 2013 is systematic and relates to double-counting. Phase III of the EU ETS sets out a strict approach towards double-counting, whereby a project cannot happen wherever it



would, directly or indirectly, affect an EU ETS installation. This does not in itself ban JI projects hosted in EU Member States altogether, though, since projects would remain conceivable in all non-ETS sectors which have no (indirect) repercussion on ETS installations. The ESD, in turn, which sets the framework for non-EU ETS sectors, is substantially unclear with regard to its treatment of double-counting of ERUs. While the Decision explicitly provides for the adjustment of Assigned Emission Amounts (AEAs) to account for any credits issued pursuant to an Article 24a EU ETS mechanism, there is no cognate provision for ERUs. Any JI project in an EU Member State then could produce ERU credits, while the Member State's AEA would remain unaffected. It is doubtful that this instance of double-counting was intended by the legislator. On the other hand, given the large number of JI projects currently registered in EU Member-States, it is equally doubtful that their *ex-nunc* ban was only implicitly declared.

This undecided state leaves pre-2012-registered JI projects in limbo, and seems somewhat out of step with the general EU support of JI. It may thus be that the legislator has simply made a mistake in omitting provisions on double-counting of ERUs. Potential solutions to such an equivocation may be available through conversion of existing projects or expansive interpretation of the ESD's double-counting provisions, though in the latter case rules of legal interpretation must be closely followed.

If JI projects are to be converted into Article 24a projects, it is highly desirable that such a mechanism be in place before 1 January 2013, in order that any gap be avoided. As the adoption of implementing measures and the establishment of a new institutional structure will take some time, the utilization of significant elements of the JI framework offers an attractive means of ensuring a smooth transition. As the EU is itself a Party to the Kyoto Protocol, and international treaties form an "integral part" of the *acquis communautaire*, the question arises whether the existing framework could indeed be utilized in part or *in toto* without further measures.

It remains questionable, however, whether decisions of treaty bodies become part of the *acquis* without further measures. Both legal reasoning and the practice of the EU indicate that implementing measures are required to bring such provisions within the scope of EU law. Nonetheless, Article 11b (5) EU ETS arguably does so, creating a good case that CMP decisions relating to JI are part of EU law. This conclusion, however, appears of little practical consequence, as all such decisions refer specifically to JI and the Kyoto Protocol architecture; to seek to use these as a basis for an alternative scheme outwith that architecture would be both practically cumbersome and legally questionable.

There is, nonetheless, significant scope for incorporating the JI architecture within the design of a new mechanism in order to ensure a smooth transition in 2013. Many of the most time consuming elements of operationalising an offset mechanism can be relatively easily co-opted, and the Chair of the JISC has indicated that that body may be utilized as a "service provider" for other offset mechanisms.

## Other Offsetting Instruments

The current uncertainty inevitably leads one to ask whether, in addition to Article 24a EU ETS and under the current legal framework, other offsetting mechanisms are conceivable. National offsetting schemes generating tradable emissions reductions, in principle, are in line with European rules and the Kyoto Protocol. Though they have no direct effect thereon, they do have



an indirect effect through reducing actual emissions and thus releasing tradable units. Both statements are, moreover, broadly true with regards bilateral or multilateral schemes among Member-States. Though it is also conceivable that Member-States could consider handing out EU ETS to offset project developers, the new rules on auctioning in the third phase of the scheme will not allow this.

Both the EU ETS and the ESD are specific in the types of *credits* they accept, and there is thus strictly no room for alternative offset credits in those schemes. However, the ESD creates a new type of trade, namely trade in AEA. Though, it is not itself project-based, it in many ways it resembles the trade in Assigned Amount Units (AAUs) under the Kyoto Protocol which, due to concerns over the large surpluses of AAUs available to some States, has led to the propagation of Green Investment Schemes (GISs) in an attempt to ensure AAU sales are linked to actual emission reductions. Given that considerable surpluses are likely to be available to some Member-States under the ESD, with others experiencing significant demand for AEA, the basis for AEA-*cum*-GIS transactions is there.

That being said, the AEA quotas today are not yet tradable, and while implementing legislation is under development, it cannot yet be assessed when and under what conditions the inter-Member-State trading will happen. Several policy decisions, namely whether the Union changes from its 20% commitment to a 30% commitment, will have a substantial effect on demand and prices. Similarly, it is not yet clear to what extent private individuals can participate in such trade. Private entities have come to play an increasing role in trade of AAUs of late, and the concept of GIS may certainly inspire the way country-to-country deals will be performed.

## Prospects

With important decisions pending, certainty on many elements of carbon offsetting in Europe post 2012 remains elusive. However, preparations for the time after 2012 must be made, by policy-makers and market participants alike. EU governments and policy-makers must make day-to-day decisions, as well as short and medium term policy choices, without a complete knowledge of how the regulatory frameworks will look in two, five and eight years time. This report on the regulatory certainties, voids and expectations of carbon offsetting in Europe will help policy-makers assess the current legal situation relating to offsetting in Europe after 2012, along with the policy options available and the legal avenues through which they can be achieved. Though the EU governments can only do so much to facilitate international negotiations, they can act independently to bring clarity into the EU regulatory framework by adopting a mechanism under Article 24a EU ETS which could serve as either a temporary or longer-term replacement for intra-EU JI. Such decisions will be crucial in shaping the role for project mechanisms in Europe in the coming years.

From the perspective of governmental market participants, this report will also assist in assessing the global risk situation and informing strategies for developing sustainable carbon portfolios beyond 2012.

In its conclusion, it summarises the key findings that will serve to inform the difficult yet crucial decisions that must be made in the current climate of uncertainty.



## Preface

The regulatory imponderables in the run-up to 2012 concerning the fate of international carbon offsetting, in general, and Joint Implementation (JI), in particular, are numerous. Many carbon developers and investors, especially from the private sector, will move out of the business, or not enter it in the first place. But others will stay on and prepare for investment and development post 2013 on the basis that uncertainty holds both risks and opportunities and that a high-risk investment strategy may ultimately be rewarded by preferential commercial conditions and market leadership. Others still may design and implement pioneer projects while minimizing risks as much as possible.

Governments, international organizations, and international and national development banks such as the World Bank, EBRD and KfW will play a leading role in this situation as their mandate exceeds the narrow boundaries of commercial investments and project risk assessment.

The present report, commissioned by KfW on behalf of the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety under the ongoing CDM/JI Initiative, provides an analysis of the regulatory situation post 2012 for JI and offsetting in and for the European Union. It aims at identifying where uncertainties lie but also where certainties exist, where further policy measures are required and where the existing framework remains adequate. The ultimate aim is to enable policy-makers and investors to gain detailed insight into the prospective situation for offsetting in Europe upon approaching the end of the first commitment period under the Kyoto Protocol and the start of the Third Trading Period under the EU ETS, and to present policy options that will facilitate decision-making in a climate of uncertainty.

Following a brief overview of the legal questions surrounding JI and offsetting under the Kyoto Protocol, the EU ETS Directive and the Effort Sharing Decision (chapter 1—Introduction), we will first describe the current rules regarding JI and other forms of offsetting in the EU (chapter 2) and then turn to an analysis of the *gap* and the role for JI after 2012 (chapter 3). From here we will turn to the European legislative framework and discuss the reception of the JI mechanism by both the Directive and the Effort Sharing Decision from 2013, including the interaction with the European instrument Article 24a EU ETS (chapter 4). This analysis will be followed by a legal option assessment regarding other offsetting instruments admissible or encouraged by the European regulatory framework (chapter 5). The concluding chapter will be dedicated to a summary of findings and a list of recommendations for carbon investors to go about after 2012 (chapter 6—Conclusion).





# 1. Introduction: The Unclear Role of JI and Domestic Offsetting

In international negotiations on the Kyoto Protocol's flexible mechanisms, the Clean Development Mechanism (CDM) receives most of the attention. The other two, i.e. Joint Implementation (JI) and International Emissions Trading (IET), remain somewhat in the shadow. This is only partly explained by differences in size. It is true the CDM is the biggest mechanism of all; it assembles a lot more projects than the others (around 5,600 CDM projects are in the pipeline compared to around 350 JI projects)<sup>1</sup> and the credits generated by the different mechanisms to date easily confirm the lead positions for the CDM (440 million Certified Emission Reductions or CERs compared to a mere 20-25 million Emission Reduction Units or ERUs and around 250 million traded Assigned Amount Units or AAUs).<sup>2</sup> However, looking at the whole commitment period 2008-12 (Commitment Period or CP I), the picture evens out. The expected CDM output up until 2012 has shrunk to less than 1 billion CERs, while the latest JI forecast sets the ERU figure for 2012 in the range of 500 million ERUs.<sup>3</sup> This maintains the lead position of the CDM over JI, but all circumstances considered—in particular the late start of JI and the fact that there are four times more countries eligible to host CDM projects than those eligible for JI—the JI figures may eventually be judged the more impressive ones.

In addition, JI may be considered the more appropriate model for future crediting mechanism in developing countries, in particular where those move from a project to a national accounting scale. Sectoral crediting, no-lose targets, NAMA crediting, and REDD—the crediting instruments discussed may all learn from the JI experience, in particular where they integrate various levels of accounting: net emission reductions of a project within the context of national crediting and accounting frameworks.<sup>4</sup>

It is surprising, therefore, that there are almost no discussions on the future of the very mechanism itself. The Joint Implementation Supervisory Committee (JISC), the body established by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP) to administer the international JI track, observes that “[currently] *JI does not appear to be considered a major influence among decision makers in governments or business*”.<sup>5</sup> This does not only concern international negotiators. In its option analysis to move beyond the EU 20% reduction target for 2020, while making multiple references to the CDM, the EU Commission

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<sup>1</sup> IET is not a project-based but a transaction-only instrument, so a project pipeline strictu sensu does not exist; in practice, however, it is often linked to project-style Green Investment Schemes (GIS); there may have been around 40 IET-cum-GIS transactions thus far.

<sup>2</sup> For the figures on CDM and JI see the November 2010 figures of UNEP Risoe (<http://cdmpipeline.org/>) and Point Carbon of 1 October 2010 (quoting a report from Vertis Environmental Finance); the ERU issuance figure relate to 80 projects in 11 countries (track 1 and track 2 combined); for the figures on AAU trading under IET see Point Carbon [...]

<sup>3</sup> According to UNEP Risoe, November 2010; the JISC, in its Report on Experience with the Verification Procedure under the Joint Implementation Supervisory Committee and Possible Improvements in the Future Operation of Joint Implementation, 23<sup>rd</sup> Meeting of the JISC, October 2010, calculates for JI Track 2 alone a contingent of 300 million ERUs up until 2012.

<sup>4</sup> The model character also resonates in the deliberations of the JISC in its 2010 Report (see above), paragraph 89: “Whereas JI is currently explicitly linked to the use of ERUs for compliance purposes under the Kyoto Protocol, this approach could in principle be applied within any domestic or regional emissions trading scheme or to any international system of quantitative targets.”

<sup>5</sup> JISC, 2010 Report, paragraph 91.



does not mention JI once.<sup>6</sup> The private sector, for its part, scores a little better. The International Emissions Trading Agency (IETA), a not-for-profit advocacy group, lists 73 JI-related documents on its website (compared to about 350 CDM-related). However, for most parts, JI is still seen as a niche mechanism for both policy makers and the private sector. The only pressure group with a dedicated JI focus, the JI Action Group, has merely half a dozen members.

Whether this situation will change largely depends on the regulatory fate of JI after 2012—under international treaty law and under European legislation. As far as international treaty law is concerned: It is impossible to foresee if and when a second commitment period under the Kyoto Protocol (CP II) will be agreed upon, or if and when a comprehensive international agreement will be concluded to set, inter alia, legally binding targets for a number of countries. Until there is clarity on this, the existing Kyoto Protocol framework, with its CP I, remains the exclusive legal regime under which JI may or may not happen after 2012. Even if international negotiations prove successful in the run-up to 2012, it will take time for State Parties to go through the necessary ratification process to allow for a future treaty entering into force.<sup>7</sup> The closer we approach the end of CP I, the less likely it is that this process could be completed before 2013. This opens a regulatory gap as of 1 January 2013—*hiatus*, as the French speaking community has come to refer to it—and the regulatory status, or possibility, of JI during the gap is unclear.

The European regulatory setting purportedly seeks to avoid the gap. The newly amended directive establishing a scheme for greenhouse gas emission allowance trading within the European Union (EU ETS) contains a comprehensive regime for the time after 2012 (it covers the third EU ETS trading phase reaching from 2013 to 2020). It also addresses the project based mechanisms of the Kyoto Protocol, CDM and JI during that period. However, while contemplating two scenarios—the conclusion and entry into force of an international agreement and the absence, or delay, of such an agreement—the new directive does not make detailed reference to the regulatory consequences of the *Kyoto gap* after 2012. It observes, at a rather **remote place in its recitals, that the “Kyoto framework” would not “enable ERUs to be created from 2013 onwards without new quantified emission targets being in place for host countries” (the generation of CDM credits, it is added, could “potentially” continue). However, other than** that it contents itself, in a not fully consistent manner, to making references either to both post-2012 CERs and ERUs (notably in the important provision Article 11a(3)) or simply to post-2012 “credits” (cf. Article 11a (5)). The failure to comprehensively deal with this issue means that the new legislation may create as many questions as it answers.

In addition to the cumbersome interaction between the international and the European regulatory frameworks, the EU ETS creates an ambiguity, if not a void, of its own. With or without an international agreement that allows the continuation of JI, it is not clear whether the EU ETS would tolerate JI project activities after 2012 hosted in EU Member States, or even accept ERUs from such activities for EU ETS compliance purposes. The competing mechanism of choice in this respect may be a genuine EU-wide offsetting instrument as foreseen under Article 24a EU ETS of the amended EU ETS directive. The directive, however, is not explicit on whether an Article 24a instrument, if ever adopted, replaces or simply supplements national and international offsetting schemes.

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<sup>6</sup> Communication from the Commission: Analysis of options to move beyond 20% greenhouse gas emission reductions and assessing the risk of carbon leakage, COM(2010) 265 final, 26 May 2010.

<sup>7</sup> The ratification process for the Kyoto Protocol took from 1997 to 2005.



The third legal regime which comes into place is the Effort Sharing Decision of 2009 (ESD),<sup>8</sup> a government-to-government agreement to cap Member State emissions from a wide range of greenhouse gas (GHG) sensitive activities not covered by the EU ETS by the year 2020. The activities range from transport (cars, trucks) to buildings, services, small industrial installations, agriculture and waste, which together represent about 60% of total GHG emissions in the EU.<sup>9</sup> The ESD, in its calculation of the national quota, the so called Annual Emission Allocation (AEA), makes reference to Article 24a EU ETS but not to JI hosted by EU Member States. This puts the intra-Member-State JI after 2012 once again into question.

Both the EU ETS Directive and the ESD may indeed reach beyond the instruments Article 24a EU ETS and CDM/JI. Under the Directive, national Governments may set aside certain quota of EU allowances to compensate for emission reduction activities in sectors not covered by the EU ETS. Under the ESD a form of European emissions trading, modelled on International Emissions Trading (IET) under Article 17 of the Kyoto Protocol, may be established under the existing rules. As the ESD allows for the setting and measurement of the national quota, on the one hand, and the trading of parts of the quota between Member States on the other, it could link a transfer of a percentage of its AEA to transnational emission reduction projects.

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<sup>8</sup> Decision No 406/2009/EC of the European Parliament and of the Council of 23 April 2009 on the effort of Member States to reduce their greenhouse gas emissions to meet the Community's greenhouse gas emission reduction commitments up to 2020.

<sup>9</sup> See Annex II of the Effort Sharing Decision for the covered sectors; for the size see European Commission, Questions and Answers on the Effort Sharing Decision, [http://ec.europa.eu/clima/policies/effort/docs/q\\_a.pdf](http://ec.europa.eu/clima/policies/effort/docs/q_a.pdf).



## 2. Offsetting in Europe under the Kyoto Protocol and the current EU ETS

Joint Implementation is the international mechanism allowing the transfer of project-based emission reductions among European countries. There have been several experiments in countries such as France, the United Kingdom, Belgium, and Italy to create domestic emission crediting regimes including tradable credits (called *white certificates* or other); but JI and its credit unit, the ERU, to date remain the exclusive project-based instrument recognized by both the Kyoto Protocol and the European emissions trading scheme, the EU ETS, where the emission reductions may be transferred within the EU.

The basis for JI in the Kyoto Protocol is Article 6 which reads (paragraphs 1 and 3):

*For the purpose of meeting its commitments under Article 3, any Party included in Annex I may transfer to, or acquire from, any other such Party emission reduction units resulting from projects aimed at reducing anthropogenic emissions by sources or enhancing anthropogenic removals by sinks of greenhouse gases in any sector of the economy*

*[...]*

*A Party included in Annex I may authorize legal entities to participate, under its responsibility, in actions leading to the generation, transfer or acquisition under this Article of emission reduction units.*

JI has two tracks; track 1 refers to a unilateral project cycle in which the project host country determines the project according to a domestic set of rules, track 2 refers to an international project cycle in which projects are determined according to the determination rules laid down in **the JI Guidelines, Decision 9 CMP 1, and subsequent decisions by the JISC as the mechanism's governing body**. For both tracks the issuance of ERUs falls into the responsibility of the project host country and the issuance can only occur on the basis of an international transaction (ERUs must transgress borders changing national registries).<sup>10</sup>

The EU ETS recognizes ERUs from either track. Article 11a ("Use of CERs and ERUs from project activities in the Community scheme") of the Directive 2004/101/EC ("Linking Directive")<sup>11</sup> reads (paragraph 1):

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<sup>10</sup> Note that some countries, including France, accept transactions in which only a portion of the ERUs issued is transferred into a foreign registry; the rest may stay within the country, see for France Art. L. 229-20 Code de l'Environnement; Article 6 Décret n° 2006-622 du 29 mai 2006 ; Art. 15(1) Arrêté du 2 mars 2007 : « La délivrance des URE [ERUs] intervient à la demande du titulaire de l'agrément... Cette demande... précise la répartition des unités de réduction des émissions sur les comptes de chaque participant au projet. L'un au moins des comptes crédités doit être ouvert dans le registre d'un État tiers qui a ratifié le protocole de Kyoto et figure à son annexe B. La première demande de délivrance est accompagnée de la lettre officielle d'agrément de l'activité de projet délivrée par l'Etat responsable du registre national des émissions dans lequel le ou les participants étrangers détiennent leur(s) compte(s). »

<sup>11</sup> Directive 2004/101/EC of the European Parliament and of the Council of 27 October 2004 amending Directive 2003/87/EC establishing a scheme for greenhouse gas emission allowance trading within the Community, in respect of the Kyoto Protocol's project mechanisms.

*[...] Member States may allow operators to use CERs and ERUs from project activities in the Community scheme up to a percentage of the allocation of allowances to each installation, to be specified by each Member State in its national allocation plan for that period. This shall take place through the issue and immediate surrender of one allowance by the Member State in exchange for one CER or ERU held by the operator in the national registry of its Member State.*

## JI Projects Hosted by EU Member States

It is up to each EU Member State to decide whether it wishes to engage in hosting JI projects, or not. If positive, the general requirements of Article 6 Kyoto Protocol and Decision 9 CMP 1 need to be met (mainly JI eligibility criteria and national approval procedures), before the country in question can host JI projects. The following EU countries have met the requirements and have had at least one project registered on their territory:<sup>12</sup>

**Table 1:** Number of JI projects registered in EU Member States and their reduction potential.

| EU Country     | JI Track 1 | JI Track 2 | Reduction potential (ERU/year) |
|----------------|------------|------------|--------------------------------|
| Bulgaria       | 26         | 1          | 2,566                          |
| Czech Republic | 44         | 0          | 1,222                          |
| Estonia        | 11         | 0          | 386                            |
| Finland        | 3          | 0          | 607                            |
| France         | 16         | 0          | 3,641                          |
| Germany        | 21         | 0          | 4,436                          |
| Hungary        | 11         | 0          | 1,778                          |
| Lithuania      | 0          | 9          | 1,802                          |
| Poland         | 15         | 0          | 2,670                          |
| Romania        | 10         | 1          | 2,879                          |
| Spain          | 3          | 0          | 164                            |
| <b>Total</b>   | <b>160</b> | <b>11</b>  | <b>22,152</b>                  |

The aggregate ERU amount expected from registered JI projects in EU Member States is about 22 million per year.<sup>13</sup> The prevalent project types are N2O destruction, renewables (including biomass and biogas), energy efficiency and fuel switch.<sup>14</sup> The issue of direct and indirect double-counting towards the EU ETS and (banned) cross-funding through government subsidy programs reduce the scope for JI projects considerably. However, the trend for JI over recent years both inside and outside the EU has been decidedly upwards (see Figure 1 on expected growth below).

<sup>12</sup> UNEP Risoe, February 2011.

<sup>13</sup> UNEP Risoe, *ibid*.

<sup>14</sup> For a recent overview of JI project types across Annex I countries see Rob Elsworth and Bryony Worthington, E R Who? Joint Implementation and the EU Emissions Trading System, Sandbag October 2010.

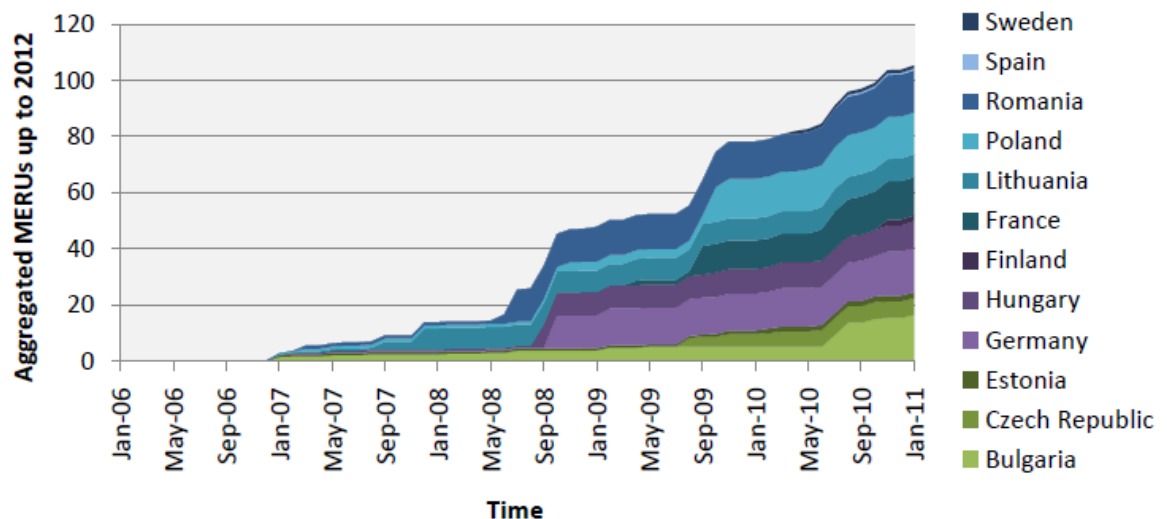


Moreover, there are fresh initiatives to develop or explore the potential for JI projects in those countries that have thus far not had a domestic JI practice (Ireland, Denmark).<sup>15</sup>

While JI projects may co-exist with the EU ETS, the Linking Directive regulates JI projects hosted by EU Member States. In the context of double-counting—a project generates emission reduction credits and, at the same time, leads to a reduction of emissions from installations covered by the EU ETS, thereby freeing up EU allowances—the Directive lays down that (Article 11 b (2):

*Member States hosting project activities shall ensure that no ERUs or CERs are issued for reductions or limitations of greenhouse gas emissions from installations falling within the scope of this Directive.*

The subsequent paragraphs 3 and 4 then contain exceptions, or remedies, to the general ban on double-counting.



**Figure 1:** Growth in ERUs expected up to 2012 from all JI projects under or beyond determination in EU countries.<sup>16</sup>

### Crediting Period of JI Projects

Unlike the modalities and procedures for the CDM,<sup>17</sup> the JI guidelines do not specify criteria for the required duration of project crediting periods. The only JISC guidance available is the following:<sup>18</sup>

<sup>15</sup> Both countries recently launched tenders for studies on designing a national JI program.

<sup>16</sup> Source: UNEP Risoe, JI Pipeline, February 2011.

<sup>17</sup> Paragraph 49 of the “Modalities and Procedures” for the CDM specifies that project participants shall select a crediting period that is (a) a maximum of seven years which may be renewed up to two times or (b) a maximum of ten years, non-renewable. See UNFCCC, Decision 3/CMP.1, UN Doc. FCCC/KP/CMP/2005/8/Add.1 (30 March 2006).

<sup>18</sup> Guidance on criteria for baseline setting and monitoring, JISC 18, Annex 2, paragraph 19.



*The crediting period can extend beyond 2012 subject to the approval by the host Party. The status of emission reductions or enhancements of net removals generated by JI projects after the end of the first commitment period may be determined by any relevant agreement under the UNFCCC.*

This has left the determination of crediting periods' duration largely at the discretion of the Parties hosting individual projects.

In practice, the vast majority of projects have specified periods beginning at a date after 1 January 2008 and ending on 31 December 2012. This includes many projects which have expected lifetimes far greater than the crediting period provided for, perhaps indicating an implicit assumption on behalf of the parties involved that crediting periods may not extend past 2012.<sup>19</sup> Many such projects are also made subject to the proviso that project approval beyond 2012 is conditional upon the continuation of JI on the basis of a decision to be adopted by the Conference of the Parties (COP),<sup>20</sup> or that emissions reductions generated after the crediting period may be used in accordance with an appropriate mechanism under the UNFCCC or other international instrument.<sup>21</sup>

However, there have been notable exceptions to this general practice. A project implemented by the Netherlands and Ukraine in July 2008 specifies two crediting periods: 2008-2012 and 2013-2017.<sup>22</sup> A Switzerland-Ukraine project operational in 2006 provides for, in addition to “[f]irst stage obligation crediting under Kyoto Protocol” from 2008-2012 and early crediting in 2006-2007, fully twenty-four years of late crediting, up to 2036.<sup>23</sup> Neither of the above projects is made subject to any explicit provisos, though a third project, specifying a crediting period of ten years up to 2017, is made subject to a subsequent COP decision.<sup>24</sup> A fourth, somewhat unclear, refers to a crediting period extending up to 2012 which “[i]f after the first period of obligations under Kyoto Protocol its validity is not prolonged” can be “shortened” to 31 December 2017, making a total crediting period of thirteen years.<sup>25</sup>

In the national JI procedures for the approval of projects, one will often find an explicit reference to 2012 as an end date to crediting.<sup>26</sup> However, outside the EU, Ukraine's JI procedural rules provide for project installation owners to apply to the national authority to deposit AAUs “with

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<sup>19</sup> See, e.g., PDD for project UA1000189, at 25, which sets out the expected operational lifetime of the project as extending to 2028, but the crediting period only so far as 31 December 2012.

<<http://ji.unfccc.int/UserManagement/FileStorage/GPTQV219YFW4CDAHR00ELZS5X7B8UJ>>  
<sup>20</sup> This proviso is regularly inserted by Germany in its Letter of Approval. See, e.g., LoA for project 0194 at 2 <  
<http://ji.unfccc.int/UserManagement/FileStorage/NTM9G8AL003B4R15ECQUJIFZSVWD2X>>.

<sup>21</sup> PDD for project UA1000181, at 19

<<http://ji.unfccc.int/UserManagement/FileStorage/Z81N619X30KBTE7SL2JWYGMOPARQ5V>>.

<sup>22</sup> PDD for project UA1000100, at 35

<<http://ji.unfccc.int/UserManagement/FileStorage/3XLZ4ERP8KW2NJDAM09B6CIFT7GY1Q>>.

<sup>23</sup> PDD for project UA1000185, at 24

<<http://ji.unfccc.int/UserManagement/FileStorage/R3JO5FZ12XYSMP6TADL97BG0VW8E4K>>.

<sup>24</sup> This project involves Germany, and as such is made subject to the general proviso of that party's LoA, as per note 19, *supra*. See Germany's LoA for project UA1000156, at 2 <

<http://ji.unfccc.int/UserManagement/FileStorage/NIB37QZCP2UF1GMHYDAL04SVO86XRJ>>.

<sup>25</sup> PDD for project UA1000175, at 26.

<http://ji.unfccc.int/UserManagement/FileStorage/BXUCMA108ELW6SYTIZNPH9GRFK205>>.

<sup>26</sup> See for Germany § 5(3) Projekt-Mechanismen-Gesetz: “Die Zustimmung wird entsprechend der vom Projektträger beantragten Laufzeit befristet. Die Laufzeit darf nicht über den 31. Dezember 2012 hinausgehen”; in France the crediting limitation is made in the Letter of Approval.



*the purpose to carry over them to the next commitment period of the Kyoto Protocol*.<sup>27</sup> Though the seemingly rough translation of the guidelines leaves it somewhat unclear what the exact consequence of this provision is, it would appear that it allows for emissions reductions generated beyond CP I to be converted into ERUs beyond that commitment period based on banked CP I AAs. These would presumably be created in a CP II, though it is also conceivable that they are intended to be generated even in the absence of a CP II on the basis of AAs retained from CP I.

The temporal limitation to 2012 is not necessarily echoed by the current EU ETS (Directive 2003/87/EC) and the Linking Directive (on the Kyoto regulatory framework, see below). Rather, the directives allow the recognition of ERUs “during each period referred to in Article 11(2)” (Linking Directive), i.e. during “the five-year period beginning 1 January 2008, and for each subsequent five-year period” (Article 11 (2) of Directive 2003/87/EC). However, since the new EU ETS Directive (29/2009/EC) has been adopted, this is no longer of relevance. The new directive introduces a new Article 11a EU ETS, applicable as of 2013, which leaves the previous regulatory framework as laid out by the Linking Directive valid only until 31 December 2012. To what extent there are any restrictions, if any, on JI projects and ERU issuance after 2012 needs to be assessed in the context of the new EU ETS Directive 29/2009/EC.

### Conclusion

JI is to-date the only project-based mechanism recognised by both the Kyoto Protocol and the EU ETS where the emission reductions can be transferred within the EU. While the issue of double-counting with respect to the EU ETS significantly restricts the scope for JI within the EU, the use of this mechanism has been the subject of decidedly upward trends over recent years, and both “new” and “old” Member States have hosted significant numbers of JI projects. Most of these projects have crediting periods taking place between 1 January 2008 and 31 December 2012, i.e. within CP I. There have been notable exceptions, however, indicating an expectation of some Parties that crediting may continue after 2012.

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<sup>27</sup> Cabinet of Ministers of Ukraine, *Decree on Approval of the Procedure of Drafting, Review, Approval and Implementation of Projects Aimed at Reduction of Anthropogenic Emissions of Greenhouse Gases*, Decree No. 206 of 22 February 2006 (as amended), paragraph 6. <  
<http://ji.unfccc.int/UserManagement/FileStorage/OVYPM9FQNK4D0GWUHI7X512RSETACZ>>.





### 3. The Kyoto Protocol after 2012: The Long Good-Bye for JI?

Whether or not the Kyoto Parties will decide on a second commitment period before the end of the first commitment period in 2012, in practice it will be virtually impossible to have an uninterrupted switch from CP I to CP II on 1 January 2013. Article 3 (9) of the Kyoto Protocol subjects the establishment of commitments for subsequent periods to formal amendment procedures in accordance with Article 20 and 21 (7) of the Protocol. Following these provisions, the new commitments are adopted by the CMP, while a vote can only be cast provided the draft text has been communicated to all Parties at least six months before the meeting. Once there is a vote and the amendment has been adopted, the amended text is circulated among Parties for their acceptance. Acceptance under international law is a process to which, *mutatis mutandis*, the rules of ratification apply (Article 14 Vienna Convention on the Law of Treaties of 1969, henceforth “Vienna Convention”).

According to Article 20(4) Kyoto Protocol, three quarters of all State Parties to the Protocol need to accept the adopted amendment text. This means that 145 Parties need to go through a ratification process in order to have the amendment enter into force. Each country decides for itself the nature of this process; however, in most cases their constitutions provide for ratification with mandatory involvement of the national legislator.

This is not only challenging from a political point of view—having 145 Parties (including, in many cases, national parliaments) agree with a new set of commitments—but also from an organizational and logistical point of view: It will take time for dozens and dozens of countries to push the amendment through the national legislators, finalize the ratification decision (usually done through the signature of the head of state) and deposit the acceptance note with the relevant UNFCCC institution (the UN Secretary General, according to Article 23 of the Kyoto Protocol). In addition, there is a 90 day grace period from the deposit of the 145<sup>th</sup> acceptance note to the entry into force of the amendment.

All odds considered, a CP II amendment of the Kyoto Protocol will not enter into force prior to **any date in 2013**. This leaves the Kyoto Protocol with what is generally referred to as the “**gap scenario**”: **The Kyoto Protocol will continue to be effective; however, one of its key features and design components—quantified emission limitation and reduction commitments (QUELROs)—will disappear, for a shorter period, a longer period, or for good.**

This puts the flexible mechanisms, and notably JI, in a dilemma. While questions of a similar nature arise regarding the survival of both the CDM and JI, it appears that from a legal and technical standpoint the uncertainty regarding JI is slightly more worrying due to its intrinsic connection with emission targets and assigned amounts under the Protocol (the QUELROs). The following sections will elaborate on the implications of this connection.

#### JI: Continuity within Uncertainty

As the Kyoto Protocol continues to be effective, there is general agreement among international legal practitioners that there is nothing in Article 6 or elsewhere in the Kyoto Protocol, or in subsequent CMP decisions which indicates an end-point to the life of JI and its institutional set-up. In the relevant Marrakesh Decision (Decision 9 CMP 1), the JI governing body, the JISC, is



explicitly called upon to assume certain tasks after the expiration of the first commitment period (sec 8). Echoing the common understanding, in a recently released paper (Gap Analysis), the UNFCCC Secretariat confirmed the non-limited nature of the JISC and the operations of JI by **stating that “Decisions taken by the Conference of the Parties (COP) and the CMP relating to the institutional framework of joint implementation (JI), in particular the Joint Implementation Supervisory Committee are not expressly conditioned on the existence of a commitment period.”**<sup>28</sup>

Similarly, in its October 2010 Report to the CMP, the JISC notes that JI eligibility (as defined by Decision 9 CMP 1, paragraphs 21, 22) will be maintained after 2012 and JI determination activities (paragraph 23, 24) continued:

*It is the understanding of the JISC that the eligibility requirements adopted for JI by the CMP would not restrict Parties, or legal entities authorized by them, from continuing to have projects determined or emission reductions and removal enhancements verified beyond 2012.*<sup>29</sup>

This view appears to be well founded. According to paragraphs 21 and 24 of the annex to Decision 9 CMP 1, the core eligibility criteria for host Parties are:

- It is a Party to the Kyoto Protocol;
- Its assigned amount pursuant to Article 3 (7) and (8) of the Kyoto Protocol (KP), has been calculated and recorded in accordance with decision 13 CMP 1; and
- It has in place a national registry in accordance with Article 7 (4) KP and the requirements in the guidelines decided thereunder.<sup>30</sup>

The first and third requirements are clearly not contingent on the existence of a compliance period. In relation to the continuation of the Kyoto Protocol, since there are no specific provisions on its termination, it will continue in operation until such time as the parties agree to its termination or replacement.<sup>31</sup> In relation to the registry requirement, this is not tied to any specific commitment period, but it persists as a general obligation of Annex I parties.

The second requirement is arguably more contentious. Parties thus far have assigned amounts only in relation to CP I. It could thus be argued that after 2012, when CP I ends, and in the absence of a CP II, parties cease to have an assigned amount for the purposes of this requirement. However, reference is made to a party's assigned amount “pursuant to Article 3, paragraphs 7 and 8”. Article 3 (7) KP provides for the calculation of assigned amounts specifically for CP I. Thus, it can be argued that the assigned amount calculation requirement is a milestone requirement, as opposed to a continuity requirement (such as the first and the third requirement)

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<sup>28</sup> FCCC/KP/AWG/2010/10 for 13<sup>th</sup> session of AWG-KP, Legal Considerations Relating to a Possible Gap Between the First and Subsequent Commitment Periods, paragraph 42.

<sup>29</sup> See also the JI Frequently Asked Questions (FAQ) list prepared by the UNFCCC Secretariat,

<http://ji.unfccc.int/FAQ/index.html>: “JI exists as part of the Kyoto Protocol, an agreement that established a legal framework for an indefinite period. Although the emission targets of Annex I Parties are negotiated on a commitment period by commitment period basis, JI itself is a long-term mechanism that continues from one period to the next, and is not tied to specific commitment periods. This continuity applies to all aspects of JI, including the determination of projects, issuance of emission reduction units (ERUs), and accreditation of independent entities.”

<sup>30</sup> Article 21 contains six requirements that must be met if a party wishes to engage in ‘Track 1’ JI. However, according to Article 24, only the above three requirements must be met for the party to engage in ‘Track 2’ JI.

<sup>31</sup> Vienna Convention, Articles 54b and 59 (1).



and that in the absence of an amendment to Article 3 and Annex B (which contains the specific assigned amounts for each party) any party that has had its assigned amount for CP I calculated meets the criteria of this requirement. It would follow that JI eligibility, once established under CP I, continues and remains contingent on the necessity alone for a country to remain Kyoto Party and to maintain a registry.

Alternatively, it can be argued that this interpretation is overly formalistic, and that the assigned amount calculation requirement is in fact a continuity requirement. This argument relies on a purposive interpretation, taking the purpose of the requirement as the insurance that each party has a clearly defined assigned amount from which ERUs can be drawn. As in the absence of new commitments having entered into force parties will no longer have effective emission reduction commitments, the passing of the true-up period could thus be seen to render the calculation of an assigned amount for CP I redundant. In this view, the fact that Article 3 (7) provides only for the calculation of assigned amounts for CP 1 is incidental, as the Parties had intended that this would be amended along with Annex B when a second period was adopted, in accordance with Article 3 (9).

If this view is adopted, however, it must still be remembered that parties have until mid 2015 to fulfil their CP 1 commitments.<sup>32</sup> Thus, at least until the end of the true-up period, it is unlikely that the purpose of the assigned amount calculation requirement can be said to be frustrated.<sup>33</sup>

The significance of the foregoing is that the framework for JI continues to exist so long as the Kyoto Protocol is in force and no amendments or CMP decisions are made to the contrary. Though its effective operation will depend on other factors, such as the existence of valid AAs, the framework remains, and any *hiatus* in operation may be ended by the entry into force of a new commitment period. The following sections thus seek to identify whether such a *hiatus* is likely in the period immediately following 2012.

#### Emission Reductions Generated Before 2013 but Issued after 2012

Another point of certainty relates to the right of countries to acquire and transfer first commitment period (CP I) ERUs, that is ERUs issued in relation to emissions reductions achieved between 1 January 2008 and 31 December 2012, after 2012 up until the end of the so called ‘true-up’ period. The formal name for the true-up period is the “additional period for fulfilling commitments”, as defined in Decision 27 CMP 1 (XIII) and referred to in numerous decisions of the Marrakesh Accords.<sup>34</sup> The definition reads:

*For the purpose of fulfilling commitments under Article 3, paragraph 1, of the Protocol, a Party may, until the hundredth day after the date set by the Conference of the Parties serving as the meeting of the Parties to the Protocol for the completion of the expert review process under Article 8 of the Protocol for the last year of the commitment period, continue to acquire, and other Parties may transfer to such Party, emission reduction units, certified emission*

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<sup>32</sup> Decision 27 CMP 1, Part XIII. See following section.

<sup>33</sup> It might be noted here, however, that though a party may continue to retain AAs, the Secretariat has noted that parties will have no *assigned amount* during a gap period. See Gap Analysis, *supra* note 27, paragraph 35.

<sup>34</sup> See Decision 5 CMP 1 (Annex, paragraph 59); Decision 11 CMP 1 (Annex, paragraph 8); Decision 13 CMP 1 (paragraph 3, 5 and Annex, paragraph 11, 12, 14, 15); Decision 22 CMP 1 (Annex, paragraph 86 and 89, 90 and 94).

*reductions, assigned amount units and removal units under Articles 6, 12 and 17 of the Protocol, from the preceding commitment period, provided the eligibility of any such Party has not been suspended...*

As the annual reports containing the inventory for the last year of the first commitment period (2012) will be submitted in 2014 and given that the Article 8 Kyoto Protocol review process cannot close before then, the timeline for the end of review and the grace period of 100 days suggests that the end date for the additional (true-up) period will fall somewhere in mid 2015. For a graphic overview see Figure 2.

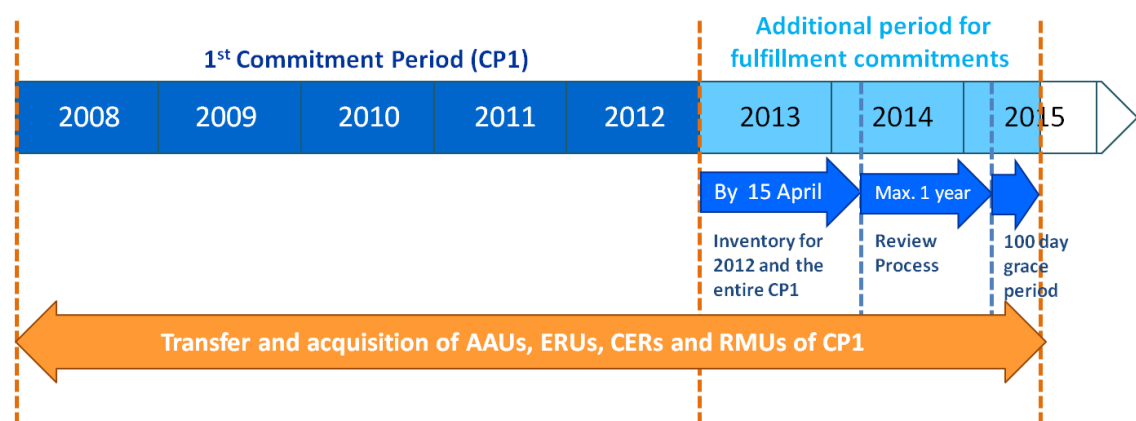


Figure 2: CP 1 Timeline, including the true-up period.

The possibility of issuing ERUs that relate to emissions reductions achieved between 1 January 2008 and 31 December 2012, up until the end of the true-up period is also made clear by the CMP, at the least in respect to JI emission removals projects (i.e., projects related to land use and forestry activities, also referred to as LULUCF). Decision 13 CMP 1 stipulates that, for those Annex I countries accounting for LULUCF activities under articles 3.3 and 3.4 of the Kyoto Protocol on a commitment period basis, issuance of RMUs (and, hence, also the conversion of RMUs into ERUs) can only take place after the end of the relevant commitment period.

Considering the points mentioned above, it seems logical to conclude that issuance of ERUs in the true-up period for emission reductions achieved before 31 December 2012 (i.e., projects other than LULUCF projects) before the end of the true-up period is also possible. The Secretariat seems to share the opinion, although it observes that, for JI track 2, the CMP may need to establish a deadline for requesting the issuance of CP I ERUs.<sup>35</sup>

In conclusion: it appears non-contentious that ERUs relating to emissions reductions achieved between 1 January 2008 and 31 December 2012, can be transferred, acquired and/or issued up until the end of the true-up period. If such ERUs are not used for compliance with the first commitment period emission targets, they can either be carried-over for use in a potential second commitment period or they can be cancelled.

## Emission Reductions Generated Post 2012 and Before the Entry into Force of a CP II

<sup>35</sup> "Frequently Asked Questions (FAQ)" concerning JI, <http://ji.unfccc.int/FAQ/index.html>.



However, there is less consensus regarding the question whether post 2012 emission reductions (gap period ERUs) from either existing or from new projects can qualify for ERU issuance from the CP I AAU contingent.

The UNFCCC Secretariat, in a commentary issued on their website,<sup>36</sup> stated that

*ERUs may be used by Annex I Parties in complying with their emission targets for the first commitment period, as long as they have been issued for emission reductions or removals taking place up to the end of 2012.*

The JISC, for its part, has found that “[a project’s] crediting period can extend beyond 2012 subject to the approval by the host Party” but that “[the] status of emission reductions or enhancements of net removals generated by JI projects after the end of the first commitment period may be determined by any relevant agreement under the UNFCCC.”

Both remarks seem to suggest that in the absence of any decision or clarification from Parties or the CMP, emission reductions generated after 2012 cannot qualify for ERUs from the CP I AAU contingent.

The value of both statements, though, seems limited. The Secretariat (whose interpretations have no legal authority per se) does not provide any reasons for its interpretation, while the finding of the JISC does not negate post 2012 ERUs but rather submits their future function to further determination by the Contracting Parties—itsself an accurate statement on the decision-making powers in international institutions and the temporality of past agreements.

An arguably more fitting authority for the present case is the Gap Analysis—in which the Secretariat argues the different options and legal positions. Among the unambiguous findings of this memorandum is that JI, for the purposes of its continuity, has the end of the true-up period as its relevant milestone, not the 31 December 2012:<sup>37</sup>

*[One needs to distinguish] between processes and institutions that will continue beyond 2012 because of the activities relating to the true-up period, and those that will continue for purposes that do not relate to the first commitment period.*

Only where activities no longer relate to the first commitment period, i.e. as of some point in 2015, the fate of JI becomes unclear. Until then, the argument runs, JI continues as an operating mechanism. Nonetheless, the Secretariat continues to express some doubt as to the basis upon which ERUs can be issued (para 44).

It can convincingly be argued that the continuation of operations includes emission reduction activities after 2012 and the generation of credits, as long as the exclusive relationship to CP I is guaranteed. *First*, it would seem artificial to isolate some operations (verification) of JI from others (credit generation), while the true-up period is ongoing. *Second*, as pointed out above, Decision 9 CMP 1 does not set a temporal limitation for JI operations. As long as a host country is JI eligible, there does not appear to be any provision preventing it from verifying *and* issuing the appropriate quantity of ERUs in accordance with Decision 13 CMP 1 (Decision 9 CMP 1, paragraphs 23 and 24). Decision 13 CMP 1, for its part, makes explicit reference to the true-up

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<sup>36</sup> *Ibid.*

<sup>37</sup> Gap Analysis, *supra* note 27, paragraph 32.



period,<sup>38</sup> during which normal unit/credit operations with reference to CP 1 units/credits continue. In response to the Secretariat's doubt over the basis upon which ERUs can be issued during a gap that, as parties will continue to hold CP 1 AAUs in their national registry up until the end of the true-up period, there is nothing to prevent them using these for ERU creation. *Third*, taking a systematic interpretation the similarities in the wording in section XIII of CMP Decision 27 CMP 1 and Article 6 (1) Kyoto Protocol could be seen as instructive:

*“For the purpose of fulfilling commitments under Article 3, paragraph 1, of the Protocol, a Party may ... continue to acquire and other Parties may transfer to such Party, emission reduction units...”*

As Article 6 is commonly understood to authorize not just the trade with ERUs, but the establishment and operation of JI projects, the parallel wording in section XIII of Decision 27 CMP 1, could indicate that it similarly authorizes such activities during the true-up period. As long as these projects operate in relation to the first commitment period, hence, the generation of credits after 2012 and before the end of the true-up period would remain admissible (“late crediting”).<sup>39</sup> Such late crediting may be compared with the early crediting practised before 2008: while not backed by any particular provisions in the Kyoto Protocol or decision of the CMP, parties agreed to transfer AAUs for pre-2008 emission reductions generated by approved JI projects. Similarly to the early crediting, late crediting constitutes a net environmental benefit over naked AAU trades.

It is not entirely clear whether, in its recent report, the JISC stands entirely behind this view or not. On one hand, it confirms that all aspects of JI are to continue beyond CP 1, observing that:<sup>40</sup>

*JI is designed as a long-term mechanism that continuous from one period to the next, and is not tied to specific commitment periods. This continuity applies to all aspects of JI including the determination of projects, issuance of ERUs, and accreditation of independent entities. (Emphasis added)*

On the other hand, the JISC appears to take the position that CP 1 ERUs cannot be issued after 31 December 2012, proffering that:<sup>41</sup> “ERUs issued for the first commitment period are to relate to emission reductions or removal enhancements that occur from 1 January 2008 to 31 December 2012.”

Thus, the JISC seems to repudiate the interpretation made above under which the current legal framework allows for crediting emission reductions achieved after 2012. Nevertheless, noting a need for clarification,<sup>42</sup> the JISC refers the matter to CMP with the recommendation to allow

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<sup>38</sup> Decision 13 CMP 1, paragraph 3, and annex, paragraph 11, 12, 14, 15, 34, 36, 49, and 62.

<sup>39</sup> Contrary to this view, however, it may equally be argued that, taking a textual interpretation, the specific referral to transfer and acquisition of units post-2012 without provision for their generation excludes the latter possibility. In this regard it may be noted that Article 6 goes on to provide for the creation of further modalities for its implementation, whereas Decision 27 does not elaborate further on the above provision.

<sup>40</sup> Report on Experience with the Verification Procedure under the Joint Implementation Supervisory Committee and Possible Improvements in the Future Operation of Joint Implementation, 23<sup>rd</sup> Meeting of the JISC, October 2010, paragraph 78.

<sup>41</sup> *Ibid.*, paragraph 85.

<sup>42</sup> *Ibid.*, paragraph 83: “...Under these circumstances, while the projects themselves would be able to continue unimpeded, it needs to be clarified whether the issuance of ERUs can occur before the Parties’ targets for a period beyond 2012 enter into force.”



ERUs to be issued from CP 1 AAUs in respect of emission reductions achieved between 1 January 2013 and the end of the true-up period.<sup>43</sup>

The UNFCCC Secretariat, for its part, in a presentation during the 23<sup>rd</sup> meeting of the JISC in October 2010, furthered the withdrawal from its earlier stance in the above mentioned Q&As, **noting that there was no “perfect legal clarity” and “no specific reference [in the Kyoto Protocol and related CMP guidance] allowing or disallowing such ERU issuance”**.<sup>44</sup> The matter, the Secretariat concludes “is ultimately political rather than legal”.

This leads to the following conclusions. One may argue that the existing regulatory framework (status quo) allows for generating and issuing credits for post 2012 emission reductions under CP I (position 1). A second position would be that there is a legal void which needs to be filled by new guidance from CMP; CMP may decide that JI continue along the lines described (position 2, as per the JISC and the Secretariat). By contrast, a flat rejection of the possibility for JI to continue in the discussed way seems to find little support.

During the 13<sup>th</sup> session of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP) in Bonn 2010, the feedback of State Parties to the Gap Analysis was mixed and inconclusive. China, Saudi-Arabia and the African Group argued that the gap question would not need to be addressed as long as there is a chance that a second commitment period could be implemented in time.<sup>45</sup> Australia and maybe Switzerland were of the opinion that both CDM and JI should continue through a gap.<sup>46</sup> The EU emphasized that it was up to the Kyoto Parties to decide whether the mechanisms would continue.<sup>47</sup>

In Cancun, the recommendation of the JISC failed to resonate vibrantly with the Parties to the Kyoto Protocol. While some important decisions were taken on JI, the matter of the gap was only **briskly touched upon, with the CMP merely “tak[ing] note of the view of the Joint Implementation Supervisory Committee ... on the need for a future operation of joint implementation after the first commitment period.”**

The failure to issue substantive guidance is most likely the result of competing priorities of Parties at the conference, as well as the delicate political sensitivities surrounding any discussion on further commitment periods under the Kyoto Protocol. The consequence, however, is that the matter will remain undecided until, at the earliest, the next meeting of the CMP in Durban in November/December this year.

Whether the JISC recommendation will eventually find resonance in Durban, moreover, remains subject to a range of factors. Aside from its clear link to the adoption of further commitment periods under the Kyoto Protocol, the issue may ultimately be interpreted as touching on the question to what extent there should be a carry-over of AAUs into subsequent commitment periods. The current rules of the Kyoto Protocol (Article 3(13)) allow full carry-over. Yet, in the ongoing negotiations, this matter belongs to the most contentious issues discussed.

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<sup>43</sup> Ibid., paragraph 123.

<sup>44</sup> Presentation is with the author.

<sup>45</sup> TWN, Mandate of the AWG-KP contact group on legal matters in dispute, 6 October 2010.

<sup>46</sup> IISD, *Earth Negotiations Bulletin*, ‘Summary of the Bonn Climate Talks, 2-6 August 2010’ Vol 12 No 478, 09/08/10; IISD, *Earth Negotiations Bulletin*, ‘AWG-LCA 11 and AWG-KP 13 Highlights: Thursday, 5 August 2010’ Vol 12 No 477.

<sup>47</sup> Ibid.





A CP I prolongation of JI, in this context, could be seen as an anticipation of a carry-over deal. However, it should be noted that the general assumption behind the above is the strict reference to CP I. One could equally argue, thus, that the post 2012 usage of credits would refer back to 2008-12 and thereby reduce the amount of units/credits that could potentially be carried over into a subsequent commitment period.

The continued irresolution of this issue leaves a number of courses of action for both investors and policy-makers in the coming year. On one hand, both may find continued investment (of financial and political capital) unacceptably risky. On the other hand, individual host countries may choose to adopt the conclusion that the existing framework allows for the continued issuance of ERUs in respect of post-2012 emissions, and issue ERUs for Track 1 projects on that basis. This would lead to continuation of Track 1 JI, but could lead to Track 1 and Track 2 following different paths, particularly if the JISC decides to adopt the more conservative approach. How this would be reflected by the International Transaction Log (ITL) is not too clear. In addition, CMP may at a later stage decide that such issuance is invalid; this would in turn create another regulatory limbo. However, the consensus rule in the UNFCCC makes it unlikely that any such decision could be adopted where some states had already made a contrary interpretation.

While the next opportunity for full clarification by the CMP does not arise until Durban, there remain opportunities for sending positive signals in the meantime. The AWG-KP will undertake its first meeting of 2011 in Bangkok from 3-8 April, and will continue to meet throughout the year. If broad agreement, or at least substantial support, can be reached on the principle of true-up period ERU issuance, this may give stakeholders the confidence they need to continue engaging with JI in the immediate future.

## Beyond 2015

It was noted above that the legal framework underlying JI will remain in existence until contrary provision is made. It has further been noted that the effective operation of JI is largely dependent on whether Parties continue to meet the relevant eligibility criteria and whether there is a valid supply of AAUs from which ERUs can be issued. With the option to use CP I AAUs for this purpose only extending up to the end of the true-up period, then, whether JI can continue beyond this date is inextricably tied to whether further commitments are agreed to under the Kyoto Protocol or an alternative agreement and when ratification, i.e. entry into force, of such further commitments occurs.

Reliable predictions are not currently possible. Various solutions have, however, been proposed in order to break the current impasse and reach compromise solutions that would allow the Kyoto Protocol, or at least part thereof, to continue. One option is to continue the flexible mechanisms while allowing each Annex I Party to select their own emission targets.<sup>48</sup> Another is to continue with a multi-speed process, whereby some Parties would sign on to further commitment periods, while others would work under more flexible regimes until the timing becomes right for adopting more formal commitments.<sup>49</sup>

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<sup>48</sup> Alister Doyle, Analysis: Governments to Debate Kyoto Climate Dilemma, Reuters, 17 February 2011.

<sup>49</sup> *Ibid.*





The Gap Analysis also considered several legal options for overcoming the barriers to the adoption of a CP II presented by the entry into force requirements for amendments to the Kyoto Protocol. Among the solutions considered was an **“opt-out” or tacit acceptance procedure**, whereby an amendment would enter into force after the expiration of a certain time period for all Parties who had not explicitly rejected it. Along with this, the Analysis also considered cognate solutions, including an opt-in procedure with a lower entry into force threshold, and an adjustment procedure which would allow adjustments to be made to annexes by decision of the CMP.<sup>50</sup>

As the Secretariat ultimately concluded, however, such options would require amendment to the Kyoto Protocol, which would itself be subject to the 145 ratification requirement. They are not by themselves therefore likely to avoid the issues created by this requirement.

Perhaps a more workable solution is another suggested by the Gap Analysis: provisional application of amendments under Article 25 of the Vienna Convention on the Law of Treaties. In this case, amendments providing for a CP II would specify that they are to apply provisionally upon adoption by the CMP with respect to all Parties who have not notified the others of their intent not to ratify the amendment.<sup>51</sup> **In theory, it may then be possible to issue “provisional” AAUs for the purpose of allowing the flexible mechanisms to continue.** However, this would be subject to the danger that Parties later notify of their intention not to ratify, thus making any **ERUs issued on the basis of their “provisional” AAUs invalid.**

Alternatively, Parties could engage in **“early crediting” before the entry into force** of the relevant amendment. As was done before the beginning of CP I, Parties would here agree to transfer AAUs after the beginning of a CP II on the basis of emission reductions occurring before this date. This would not necessarily need to be sanctioned by a decision of the CMP, though this could perhaps accommodate its operation more effectively. The danger again here is that if amendments providing for a CP II do not ultimately enter into force, such reductions will be unable to be credited. While this eventuality could be provided for in relevant contracts with host states or project developers, this may present a risk many investors are not willing to take.

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<sup>50</sup> Gap Analysis, *supra* note 27, paragraph 8.

<sup>51</sup> *Ibid.*, paragraphs 15-22.



## Conclusion

Prevailing legal and political conditions indicate that a gap in international regulation is likely after 2012. Though the legal and institutional framework for JI will continue to operate in this period, and parties will most likely remain eligible to participate—at least until the end of the true-up period—the issuance of ERUs is subject to less certainty.

On one hand, it appears relatively non-contentious that ERUs relating to pre-2013 emissions can be issued and transferred until the end of the true-up period. With regard to post-2012 reductions, there are strong arguments supporting the view that ERUs can be issued for such reductions from CP I AAs during the true-up period. There is, however, little certainty on this matter, and neither the views of the JISC nor the Secretariat have been entirely clear. The failure of the CMP to settle the question in Cancun means the next opportunity to do so is in Durban later this year, though there are opportunities to send positive signals in the meantime. Failing decisive resolution by that body, JI activity may ebb, or Parties may decide to continue bilaterally, leading to potential deviation between Tracks 1 and 2.

Whether JI can continue beyond the true-up period essentially depends on whether subsequent commitments are agreed to under the Kyoto Protocol or an alternative agreement and, if they are, when they will be ratified and enter into force. As the current rules imply ratification acts of more than 140 State Parties, it may well happen that the Kyoto gap continues beyond 2015. Several technical and political solutions have so far been discussed to tackle this situation, most of which, however, fail to overcome the express ratification threshold set by the Protocol.



## 4. New European Order: Article 24a EU ETS and Projects under the Effort Sharing Decision

The EU Emissions Trading Scheme (EU ETS) in its current form covers about 40% of EU-wide GHG emissions. Although targeted by various national and EU policies and measures, 60%—or 3 billion tCO<sub>2</sub>e—of EU emissions are not subject to caps at installation or emitter level.<sup>52</sup> Even though recent figures<sup>53</sup> suggest that the EU is well on track to achieve its emission reduction target of at least -20% by 2020 compared to 1990,<sup>54</sup> both capped and uncapped sectors must **contribute to the EU's total reduction efforts. The Union's 'Climate action and renewable energy package' of April 2009**<sup>55</sup> contains a set of comprehensive measures to target emissions inside and outside the existing EU ETS. As part of the package legislation, the European trading scheme was extended in scope to include new industries (e.g. aluminium and ammonia producers) and two new gases (nitrous oxide and perfluorocarbons).

The package also added another layer of cap and trade to its climate policy. The Effort Sharing Decision<sup>56</sup> introduced emissions targets for Member States for almost all sectors not covered by the EU ETS: small scale emitters in transport (cars and trucks), buildings (in particular heating), services, small industrial installations, agriculture, waste and others, together amounting to some 60% of total GHG emissions in the EU.<sup>57</sup> Each EU Member State has been set a cap on its respective emissions in these sectors. The individual targets vary, with Luxembourg, Denmark and Ireland having a reduction commitment of -20% and Romania and Bulgaria a target of +20% over 2005 levels. The average target will be approximately -10% throughout the EU, which together with the reduction achieved by the EU ETS (-21% over 2005 levels) equals an overall reduction of -20% over 1990 levels.

An element that cuts across the new EU ETS Directive and the Effort Sharing Decision is the option to establish an EU offsetting instrument that is distinct from the offsetting framework of

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<sup>52</sup> The 'Annual European Community greenhouse gas inventory 1990–2007 and inventory report 2009' from 27 May 2009 reports 5045 million tonnes of CO<sub>2</sub> equivalents (MtCO<sub>2</sub>e) in 2007.

<sup>53</sup> European Environment Agency, Tracking Progress Towards Kyoto and 2020 Targets in Europe, EEA Report No 7/2010, October 2010.

<sup>54</sup> 30% in the event of a sufficiently ambitious international agreement, cf. most recently the statement of the EU 28 **January 2010 regarding the Copenhagen Accord: "As part of a global and comprehensive agreement** for the period beyond 2012, the EU reiterates its conditional offer to move to a 30% reduction by 2020 compared to 1990 levels, provided that other developed countries commit themselves to comparable emission reductions and that developing countries **contribute adequately according to their responsibilities and respective capabilities."**

<sup>55</sup> See Regulation (EC) No 443/2009 of the European Parliament and of the Council of 23 April 2009 (performance standards for passenger cars); Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 (renewable energy); Directive 2009/29/EC of the European Parliament and of the Council of 23 April 2009 amending Directive 2003/87/EC (EU ETS Directive); and Directive 2009/30/EC of the European Parliament and of the Council of 23 April 2009 amending Directive 98/70/EC and Council Directive 1999/32/EC; Directive 2009/31/EC of the European Parliament and of the Council of 23 April 2009 (Carbon Capture and Storage); and Decision No 406/2009/EC of the European Parliament and of the Council of 23 April 2009 (Effort Sharing Decision); all acts published at OJ L140/52 of 12 June 2009.

<sup>56</sup> Decision No 406/2009/EC of the European Parliament and of the Council of 23 April 2009 on the effort of Member States to **reduce their greenhouse gas emissions to meet the Community's greenhouse gas emission reduction commitments up to 2020.**

<sup>57</sup> Note that the land-use, land-use change and forestry (LULUCF) is not covered by the Effort Sharing Decision, see Article 3 (1) in conjunction with Article 2 (1) and annex I.



the Kyoto Protocol (see Figure 3 on the different regulatory layers). The basis for the instrument can be found in the Directive, in its Article 24a (“Harmonised rules for projects that reduce emissions”) which foresees the

*issuing [of] allowances or credits in respect of projects administered by Member States that reduce greenhouse gas emissions not covered by the Community scheme.*

Article 24a is a subsidiary provision to Article 24 EU ETS, which authorizes the unilateral inclusion of additional activities and gases (beyond what is already covered by the EU ETS) in the European trading scheme. Thus, measures under Article 24a “shall only be adopted where inclusion is not possible in accordance with Article 24”.

Article 24a requires the adoption of delegated legislation (“implementing measures”) to become effective. Through comitology procedures—the Commission adopts rules approved by Member State representatives and, in certain instances, by the EU Parliament—the mechanism’s details, such as project areas, criteria for eligibility, project definition, participation, crediting principles, and credit title, remain to be defined. These implementing measures, as explicitly provided in Article 24a (1) need to ensure that double-counting of emission reductions is prevented and the implementation of “other policy measures to reduce emissions” is not impeded.

According to Article 24a (3) a Member State can unilaterally refuse certain project types for its territory. Whether a host Member State is authorized to define additional unilateral requirements is not entirely clear from the provision in Article 24a(3): “Such projects will be executed on the basis of the agreement of the Member State in which the project takes place.”

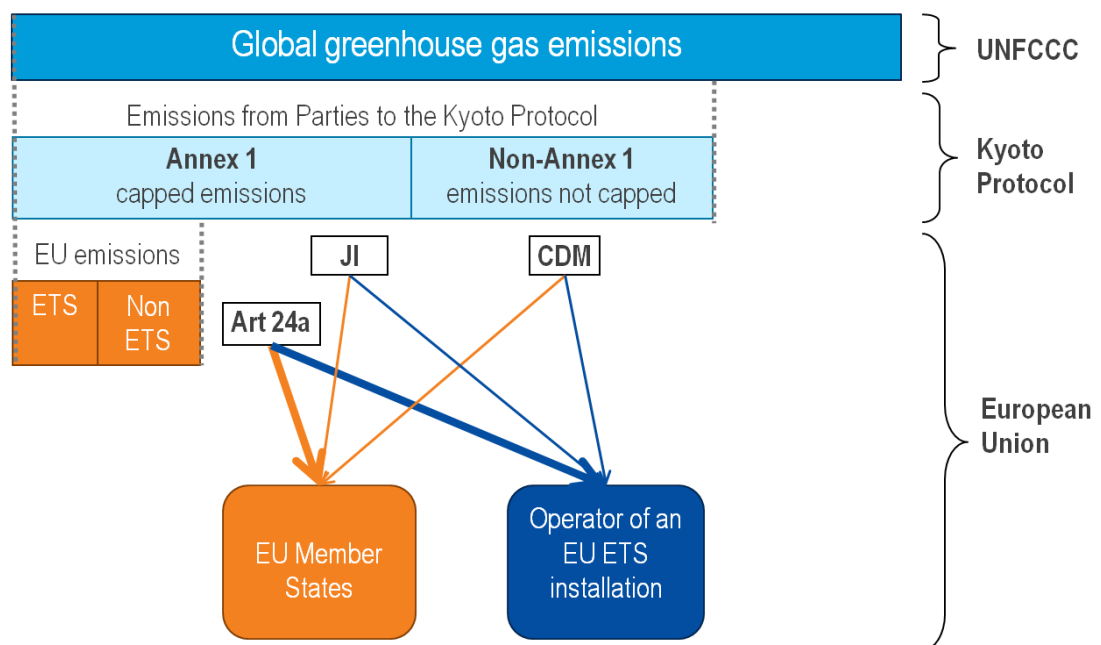


Figure 3: Offsetting mechanisms under the Kyoto Protocol and under the EU ETS



It should be noted that with the Article 24a mechanism the EU departs further from the strict rule under which an EU unit (to-date read: allowance) is shadowed by a Kyoto unit (AAU, CER, ERU). The new EU Registry Regulation 58, which, for most parts, applies from 1 January 2012 (Article 91), distinguishes Party accounts (referring to the Kyoto registries) and national accounts (referring to the EU ETS). Allowances issued by Member States are shadowed by an equal **quantity of AAUs which need to be transferred, from the Party account, to the “ETS AAU deposit account” (Article 39)**. Credits issued under Article 24a EU ETS do not fall under this rule and they are not shadowed by a Kyoto unit.

The offsetting mechanism under Article 24a EU ETS, thus, is de-linked from the Kyoto framework and stays intact with or without the **continuation of the Protocol’s commitment periods**.

Whether an offsetting mechanism will in fact be developed under Article 24a in the near future is not currently certain. In a conference held to discuss the future of offsetting in Europe in Paris in January 2011, numerous Member State representatives and carbon market participants expressed their support for the development of a new mechanism under Article 24a. A presentation **prepared by the EU Commission’s head of climate policy coordination, Peter Zapfel for the same conference, however, indicated that the matter was not high on the Commission’s priority list**, and that a process for drafting implementing measures would not be undertaken in the near future. Nonetheless, Member State representative resolved to draft a common position paper **with a view to driving the process forward and placing the matter on the Commission’s agenda**. Though the initiative for drafting measures ultimately rests with the Commission, Member States also have a role in the process, in particular through their representatives on the climate committee. How this dynamic will play out in the coming year will be of significant importance to the role of offsetting in Europe post-2012.

#### Article 11a and 11b EU ETS and JI

Uncertainty surrounds the status and fate of JI in relation to the EU ETS. The question is twofold. First, how does the EU ETS treat JI projects and credits in the post-2012 scenarios (with and without a second commitment period)? Second, what is the status of intra-Member-State JI, i.e. of JI projects hosted by any EU Member State?

The first question is problematic only in the scenario that there is no international agreement (or not yet one), nor a second commitment period under the Kyoto Protocol, respectively immediately succeeding CP 1. In the scenario of a continuation of subsequent commitment periods or of the entry into force of a new international agreement, there can be no doubt that JI continues to be accepted by the EU ETS Directive. Article 11b, which through 2012 and beyond remains largely in its previous form, makes explicit reference to ERUs as being recognized by the EU ETS. In addition, Article 28, introduced by the new EU ETS Directive, refers expressis verbis to the recognition of ERUs in the event of the conclusion of an international agreement on climate change (paragraph 3):

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<sup>58</sup> Commission Regulation (EU) No 920/2010 of 7 October 2010 for a standardized and secured system of registries pursuant to Directive 2003/87/EC of the European Parliament and of the Council and Decision 280/2004/EC of the European Parliament and of the Council, Official Journal L 270 of 14 October 2010.



*The proposal shall allow, as appropriate, operators to use, in addition to the credits provided for in this Directive, CERs, **ERUs** or other approved credits from third countries which have ratified the international agreement on climate change (emphasis added).*

Focusing then on the question regarding post 2012 JI in the scenario that there is no international agreement (or second commitment period), it may be of relevance to note the factual assumption that is made in one of the Directives recitals (No 15):

*Without an international agreement on climate change that determines the assigned amount for developed countries, Joint Implementation projects cannot continue after 2012.*

The same statement can be found in the Effort Sharing Decision to be discussed below.<sup>59</sup> However, in its provisions that relate to JI (and the CDM), the Directive appears to contradict this **assumption. Article 11a on, as the title has it, the “use of CERs and ERUs from project activities in the Community scheme before the entry into force of an international agreement on climate change” foresees (paragraph 3):**

*To the extent that the levels of CER and ERU use, allowed to operators or aircraft operators by Member States for the period from 2008 to 2012, have not been used up or an entitlement to use credits is granted under paragraph 8, competent authorities shall allow operators to exchange CER and **ERUs from projects that were registered before 2013 issued in respect of emission reductions from 2013 onwards** for allowances valid from 2013 onwards. (emphasis added)*

Article 11a, thus, explicitly refers to the scenario prior to a second commitment period of the Kyoto Protocol (or another international agreement of that sort), making the guarantee that ERUs from pre-2013 registered projects will be accepted in the EU ETS. New projects, i.e. projects with a registration date after 2012, on the other hand, do not fall under the JI continuation authorization of Article 11a (3) quoted above. They would be possible on the basis of third country agreements (Article 11a (5)):

*... credits from projects or other emission reducing activities may be used in the Community scheme in accordance with agreements concluded with third countries, specifying levels of use. In accordance with such agreements, operators shall be able to use credits from project activities in those third countries to comply with their obligations under the Community scheme.*

In the remaining paragraphs, Article 11a refers to the generic form “credit” encompassing all possible credit types, CERs, ERUs and third-country credits.

Thus, the provision Article 11a, as a whole, appears to make consistent use of the various credit types; it is significant then that reference is made to post 2012 ERUs—always in the absence of an international agreement. Clearly, the provision does not prescribe whether or not ERUs will exist or, as a matter of fact, can exist. It simply states that in the case that they do (even in the absence of an international agreement), they will be accepted by the EU ETS.

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<sup>59</sup> Decision 406/2009/EC, recital 15: “Without an international agreement on climate change that determines the assigned amount for developed countries, Joint Implementation (JI) projects cannot continue after 2012.”



Noting that a recital can only be used to interpret a directive where the provisions are *prima facie* ambiguous, it seems a fair assessment that the above mentioned recital 15 contains a (misleading or not) statement of facts which does not guide us in our interpretation of Article 11a.

### Intra-Member-State JI: Limitations for the Capped and the Uncapped Economy

The second question, by contrast, is more contentious. The new EU ETS Directive, at numerous occasions, leaves one to speculate whether it considers JI a third-country mechanism only. In its Recital 28, it states:

*Once there is an international agreement on climate change, additional use of CERs and ERUs should be provided for, from countries which have ratified that agreement.*

“Countries” in this context refers to third countries (Member States are just that: “Member States”). The recital then seems to imply that ERUs (just as CERs) can only come from third countries, i.e. non-EU-Member-States.

Similarly, in its recital 30, the Directive refers to JI projects that “*generated ERUs until 2012 but are no longer able to do so under the Kyoto framework*”; it foresees the possibility that “*agreements with third countries*” be concluded in order to ensure that those projects continue to be recognized in the Community scheme.

Considering this and that Article 11a (3) restricts the usage of ERUs to projects registered until 31 December 2012, while otherwise the recognition of ERUs depends on agreements with third countries or whether the third country in question has ratified a global agreement (see the above quoted Article 28(3))—the question of intra-Member State JI in practical terms then only relates to pre-2013 registered (determined) projects. Projects that are registered after this date would not be eligible for credit recognition under the EU ETS.

This does not mean, on the other hand, that all pre-2013 registered EU JI projects would continue to be recognized under the EU ETS.

### Pre-2013 Projects and the EU ETS

The strongest argument against the recognition of ERUs generated by pre-2013 projects under the EU ETS after 2013 is systematic and relates to double-counting. The above-mentioned Article 11b, in its second paragraph, reads:

*Except as provided for in paragraphs 3 and 4, Member States hosting project activities shall ensure that no ERUs or CERs are issued for reductions or limitations of greenhouse gas emissions from activities falling within the scope of this Directive.*

Paragraph 3 and 4 lay down remedies for instances of direct double counting (the EU ETS installation generates CDM/ERU credits) and indirect double-counting (the CDM/JI project



causes emission reductions at a EU ETS installation) which consist of the cancellation of allowances at different levels. These remedies, however, are limited in time; they are due to expire at the end of 2012.

This means for the Third Trading Phase as of 2013 that a strict approach towards double-counting applies: A project cannot happen wherever it would, directly or indirectly, affect an EU ETS installation.

This does not in itself ban JI projects hosted in EU Member States altogether, though, since projects would remain conceivable in all non-ETS sectors which have no (indirect) repercussion on ETS installations. For the non-ETS sectors, in turn, the ESD sets the framework.

### JI Projects and the Effort Sharing Decision

While the ESD integrates the Article 24a mechanism, it is unclear how it treats JI. That is, if and when Article 24a of the revised EU ETS Directive becomes operational as an EU-wide offsetting mechanism, its relationship with the ESD is straight forward. Article 10(b) ESD provides that the maximum quantity of emissions allowed to each Member State (its Annual Emissions Allocation, or AEA, as defined in Article 2 (2) ESD) shall be adjusted in accordance with the allowances or credits issued by that Member State pursuant to Articles 24 and 24a that relate to emissions covered by the Decision (which, as the ESD aims to cover most emissions not covered by the EU ETS, will likely amount to almost all such allowances/credits). In other words, for every credit that is issued by a Member State for a project in its territory, it must reduce its AEA by an equivalent amount. This guarantees that there is no instance of double-counting (a project generating EU allowances/credits under the EU ETS and, at the same time, freeing up AEA units under the Effort Sharing Decision). Though specific modalities will of course need to be worked out based upon how Article 24a EU ETS is to be implemented (if at all), the relationship is thus largely clear and unproblematic.

This statement is significantly less true with regard to JI projects. The ESD does not directly address the role of intra-Member State JI, and its provisions do not appear to provide any clear signal as to what this role, if any, might be. This is perhaps curious when it is considered that EU Member States have seen significant JI activity in their territories, with over 100 projects registered as of early 2010.<sup>60</sup> In line with the principle of double-counting, one would expect that **any credits generated by JI projects in Member States are deducted from that State's AEA just as Article 24a EU ETS allowances/credits are.**

The conclusion one could draw is that the ESD implicitly excludes the possibility that JI may take place in Member States post-2012. It is hard to see how a counter-argument based on the assumption that the ESD intends to privilege JI by not requiring the deduction from the AEA could be built. This would clearly produce questionable instances of double-counting: ERUs would be produced that could be transferred into both the EU ETS and the ESD, while the host countries would benefit from a non-adjusted AEA.

The conclusion—the exclusion of JI projects hosted by Member States—would be consistent with regard to new projects (registered after 2012) for which the new offsetting mechanism

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<sup>60</sup> See above, Chapter 2.





Article 24a, in theory, is available. However, it leaves the JI projects registered before 2013, whose continued recognition is guaranteed by Article 11a (3) and by the similar provision of Article 5 (1)(b) ESD, in limbo. Also, given the history and ongoing practice of JI in EU Member States and the generally affirmative view of the European legislation towards an international agreement including its mechanism, it would seem odd that both legislative frameworks, EU ETS and ESD, would make substantial limitations to the mechanism's application on implicit terms.

It is not the most improbable possibility that the legislator was unintentionally oblivious when adopting the ESD and that the omission of JI related credits in the provision on AEA adjustment (Article 10) was equally not intended.

A solution could consist in the automatic transferral of pre-2013 JI projects into Article 24a EU ETS projects. Another one may be to apply, *mutatis mutandis*, Article 10 ESD to intra-Member-State JI. However, the limits of legal interpretation as defined by the European Court of Justice (ECJ) need to be respected.

It is hard to draw a clear conclusion from the findings. Certainty is limited to the fact that (i) both the EU ETS and the ESD accept Joint Implementation as a mechanism under a future international agreement, and (ii) that EU hosted projects registered after 2012 can only do so under the Article 24a EU ETS mechanism. Other than that, there is probably sufficient ground to assume that both legislative frameworks would recognize certain post 2012 ERUs in the absence of an international agreement, as long as they are generated in line with the Kyoto Protocol.

However, regarding the question whether (pre-2013) JI projects hosted by EU Member States will be able to continue after 2012, there is little legal certainty. Sufficient clarity exists only with regard to the EU ETS. Following Article 11b EU ETS, JI projects that would cause direct or indirect double-counting are excluded. For the non-EU ETS sectors, however, there is an apparent legal void. The ESD does not hold a double-counting provision for JI projects. This could be interpreted as implying that also non-EU ETS sector JI projects in EU Member States are excluded. However, that would result in a complete ban on JI for EU Member States—something which is hard to reconcile with the general affirmation of both the EU ETS and the ESD of JI as an international offset mechanism. An unintentional legislative omission may have occurred. A solution within the existing legal framework would consist in an automatic transferral of existing JI projects into Article 24a EU ETS projects or in a JI-compatible interpretation of Article 10 ESD.

## Article 24a and JI

Whether as a mechanism to replace JI for the purposes of the EU or to run parallel thereto, the implementation and operationalisation of an Article 24a mechanism before 1 January 2013 would provide substantial certainty to policy-makers and investors by ensuring that JI projects in the EU will be able to re-register as Article 24a projects and so continue to produce emission reductions and corresponding credits. Yet, the establishment of the procedures and institutional structure such a mechanism will take some time and, as noted above, whether implementing measures will be developed in the near future remains uncertain.

This leads to the question of whether the procedures and institutional structure can be co-opted or used by a European instrument as a provisional (or perhaps longer term) measure to ensure a smooth transition in 2013. JI has developed increasingly sophisticated operating mechanisms in



the past number of years, and, though most agree on the need for improvements, its use could provide an adequate and appropriate basis upon which Article 24a could begin to operate. Determining how such an interaction could proceed requires an analysis of various legal and practical questions, the former of which will be dealt with first.

The European Union is a Party to the Kyoto Protocol.<sup>61</sup> Pursuant to Article 216 (2) of the Treaty on the Functioning of the European Union, agreements concluded by the Union are binding upon the institutions and the Member States. The ECJ, in turn, has held in the *Haegeman* decision and consistently since that agreements to which the EU is a party form an “integral part” of EU law.<sup>62</sup> The question may thus be asked whether the CMP decisions adopted under the authority of the Kyoto Protocol that provide the operating structure for JI already form part of the *acquis communautaire* and, consequently, whether they can be used for the purpose of an EU instrument without further measures being adopted.

**Despite international agreements being an “integral part” of EU law, it is not entirely clear whether such agreements become part of the *acquis* immediately upon ratification. Whether decisions of treaty bodies operating under agreements to which the EU is a party automatically form part of EU law is perhaps even more uncertain. Moreover, the operation of JI would generally appear to be within the competences of the Member States, rather than the EU. It is they who issue Letters of Approval authorising private entities to participate in projects and who ultimately remain responsible retaining their eligibility.**

However, the CMP decisions relating to JI are nonetheless arguably transposed into EU law by Article 11b (5) EU ETS, which reads:

*A Member State that authorises private or public entities to participate in project activities shall remain responsible for the fulfillment of its obligations under the UNFCCC and the Kyoto Protocol and shall ensure that such participation is consistent with the relevant guidelines, modalities and procedures adopted pursuant to the UNFCCC or the Kyoto Protocol.*

There is thus a strong case for arguing that the various CMP decisions pertaining to JI (and the CDM) are currently part of the *acquis communautaire*.

Despite this, the relevant guidelines being part of the *acquis* may not be of significant value in seeking to use the JI machinery for purposes of Article 24a. In the first instance, most of the guidelines refer specifically to Article 6 KP, AAUs, ERUs and other elements that are specific to JI. Unless a new mechanism was designed so similarly to JI that all its elements, including emission units, were identically named and organised, the transposition of guidelines designed for another mechanism operating within another legal framework would be unlikely to be legally operable. Secondly, even if the mechanism and the European legal framework were reorganised in this way, to utilise Article 11b (5) in this way would most certainly amount to the subversion of

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<sup>61</sup> The Kyoto Protocol was approved on behalf of the European Community by Council Decision 2002/358/EC of 25 April 2002, which was deposited with the United Nations Secretary-General on 31 May 2002. By Communication from the EU Council on 8 March 2010, the EU notified the Secretary General that the European Community has been replaced by the European Union in respect of all Agreements deposited with the UN to which it is a Party.

<sup>62</sup> Case 181/73 *Haegeman* [1974] ECR 449, para 5. See also Paul Craig Grainne De Búrca, *EU Law* (4<sup>th</sup> Ed., 2007), p.202.



the intention of the legislator, *en casu* to ensure compliance with the guidelines in the use of the JI mechanism, and would thus be of questionable legal validity.

This is not to say, however, that substantial elements of the JI machinery cannot be used to provide for the quick start of Article 24a. Elements such as existing Accredited Independent Entities, national approval procedures, verification procedures, and various elements of the JISC/Track 1 processes are amongst those that are most time consuming to establish, and these can relatively easily be co-opted for use under a new mechanism with little alteration. It is necessary, however, that new regulations/guidelines be adopted explicitly incorporating these elements.

In addition, the Chair of the JISC, Benoît Leguet **has recently referred to the JISC as a “service provider”, which could potentially provide** international credibility and recognition to any offset scheme.<sup>63</sup> With measures based largely on the existing JI framework, and a cooperation agreement with the JISC providing that it would operate its Track 2 procedure in relation to Article 24a, a new mechanism could be established and initially operational in relatively little time, at which point legislators could concentrate on making necessary improvements.

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<sup>63</sup> Benoît Leguet, Joint Implementation: Lessons Learned, Presentation at “Project Mechanisms in Europe after 2012” Conference, Paris, 21 January 2011, p. 8, available at <http://climatefocus.com/downloads/Paris/11-01-21%20JISC%20Chair%20Projects%20in%20Europe%20Workshop.pdf>.

## Conclusion

The 2009 Climate and Energy Package has answered some questions concerning the future of offsetting in Europe, yet created others. Certainty appears to be largely limited to the fact that (i) both the EU ETS and the ESD accept Joint Implementation as a mechanism under a future international agreement, and (ii) that EU hosted projects registered after 2012 can only do so under the Article 24a EU ETS mechanism. Other than that, there is probably sufficient ground to assume that both legislative frameworks would recognize certain post 2012 ERUs in the absence of an international agreement, as long as they are generated in line with the Kyoto Protocol.

However, regarding the question whether (pre-2013) JI projects hosted by EU Member States will be able to continue after 2012, there is little legal certainty. Sufficient clarity exists only with regard to the EU ETS. Following Article 11b EU ETS, JI projects that would cause direct or indirect double-counting are excluded. For the non-EU ETS sectors, however, there is an apparent legal void. The ESD does not hold a double-counting provision for JI projects. This could be interpreted as implying that also non-EU ETS sector JI projects in EU Member States are excluded. However, that would result in a complete ban on JI for EU Member States—something which is hard to reconcile with the general affirmation of both the EU ETS and the ESD of JI as an international offset mechanism. It thus appears to be possible that an unintentional legislative omission may have occurred.

A solution within the existing legal framework would consist in an automatic transferral of existing JI projects into Article 24a EU ETS projects. This of course depends on whether such a mechanism is in fact created. Recent signs from the Commission indicate that implementing measures will not soon be forthcoming, though new initiatives by Member States may lead to further consideration. If such an approach is followed, significant elements of JI may be utilized to ensure a smooth transition to a new mechanism. As the existing JI framework would not be compatible with the operation of a new mechanism, implementing measures must however explicitly incorporate its elements in order to ensure both legal permissibility and practical utility.

A second solution could consist in a JI-compatible interpretation of Article 10 ESD, though it is not entirely clear whether such an interpretation would be compatible with the relevant rules and principles as defined by the ECJ.



## 5. Other Ways of Investment: Offsetting and Trading under the Effort Sharing Decision

We have seen above that Article 24a EU ETS provides an offsetting mechanism beyond the Kyoto Protocol and any international agreement supplementing or replacing the Kyoto Protocol. We have also seen that the status of Joint Implementation after 2012 holds a number of imponderables, namely (i) the open negotiations on a second commitment period and the post 2012 international climate change regime; (ii) the question whether CMP, in Durban or later, will decide in favour or against (or not at all on) the continuation of JI during the Kyoto gap; and (iii) the possibility of JI projects—assuming JI does continue after 2012—hosted by EU Member States.

This leads one to ask whether, in addition to Article 24a EU ETS and under the current legal framework, other offsetting mechanisms are conceivable. The question has three dimensions: first, the national context; second, the bilateral or multilateral context among EU Member States; and third, the EU context proper.

### National Offsetting Schemes

National offsetting schemes of the sort that certain national economic sectors, at the municipal, regional or federal/national level, could generate emission reductions from projects which would translate into tradable credits are in conformity with both the (existing) international framework (UNFCCC, Kyoto Protocol) and the European climate and energy package. More to the point: there is nothing in these regulatory regimes that would impede such activities; from a European law perspective, however, any such scheme needs to respect the EU rules on competition and state subsidies.

A national offsetting scheme and any emission credit it produces, while being in line with the Kyoto and European frameworks, would be of no direct relevance for these regimes. The emission reductions achieved would neither trade for an EU allowance nor translate into a credit that were recognized by the Effort Sharing Decision and the national targets on the non-EU ETS sectors.

Nevertheless, the schemes would have an indirect effect on the cap-and-trade schemes in question, as they would reduce actual emissions and thus release tradable units.

Member States may consider a variation of such schemes which could nonetheless involve the transfer of tradable units. It would consist of handing out EU allowances to offset project developers. However, the precondition for any such EU allowance driven offsetting scheme would be that Member States maintain an allowance reserve from which hand-outs could be provided. Such reserves will not exist after 2012. Article 10 (1) of the new EU ETS Directive requires that all allowances be auctioned except for those reserved for specific purposes listed in Article 10a and 10c:

*From 2013 onwards, Member States shall auction all allowances which are not allocated free of charge in accordance with Article 10a and 10c.*



Emission reduction activities do not fall under the Articles 10a and 10c.

### Bilateral and Multilateral Schemes among Member States

Provided that such schemes and offsetting models are in conformity with EU law, in particular with the EU provisions on competition and state subsidies, Member States are free to cooperate including with respect to cross-border emission reduction crediting schemes.

For the effect on the international regulatory framework (if existent) or the European one, EU ETS and ESD, the situation is the same as above. Any such schemes and credit types cannot trade into the international and supranational regimes but they have indirect effects through the factual reduction of GHG emissions.

### The European Framework

Both the EU ETS and the ESD apply a strict *nomenclatura*. For the purposes of trade and compliance of project-based credits; they accept CERs (from the CDM), ERUs (from JI), Article 24a EU ETS allowances/credits and international credits (as negotiated at the global, multilateral or bilateral level with third countries). Other project credit forms will be ignored (under current rules).

There is, nonetheless, another trade form which is not project-based per se but may still be coupled with emission reduction activities. Under Article 3 (4) of the Effort Sharing Decision, Member States are allowed to trade their annual emission allocation (AEA):

*A Member State may transfer up to 5 % of its annual emission allocation for a given year to other Member States. A receiving Member State may use this quantity for the implementation of its obligation under this Article for the given year or any subsequent years until 2020.*

The AEA transactions resemble International Emissions Trading under Article 17 of the Kyoto Protocol. In theory these are naked sales, i.e. sales that do not relate to individual emission reductions. However, initially in response to critique that had been voiced regarding large AAU surpluses in some Annex I countries, an IET practice has taken shape under which the transfer of **AAUs is backed by a 'green investment' or a so called Green Investment Scheme (GIS)**.<sup>64</sup> A GIS may consist of a JI-style emission reduction project but is by no means limited to projects in this sense. A variety of subsidy programmes, especially in the field of energy efficiency and residential buildings, have been set up as part of GIS in the past;<sup>65</sup> and, more generally, all kinds of policies and measures financed by AAU revenues may be considered a GIS. Given the broadness of the concept and the flexible governance structure, there are large discrepancies in quality, measurement and performance. However, AAU-cum-GIS transactions have triggered several hundred million EUR green investments so far and the transaction trend points upwards.

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<sup>64</sup> Cf. Moritz von Unger, AAU Sales and Green Investment Schemes: Perspectives for 2012 and After, Climate Focus Commentary, November 2010, [www.climatefocus.com](http://www.climatefocus.com).

<sup>65</sup> For an overview see Andreas Tuerk et al., Green Investment Schemes: First Experiences and Lessons Learnt (Working Paper), Joanneum, Graz 2010.

AEA transactions may trigger similar investments under the ESD. While the tradable amounts are capped at 5% of the annual quota and while available price projections calculate a relatively low amount (4 EUR per unit in the 20% reduction scenario; however, 30 EUR per unit in the 30% scenario),<sup>66</sup> the basis for AEA-*cum*-GIS transactions is there. Several Member States may exceed their annual AEA by considerable margins; according to recent figures countries such as Spain, Italy, Austria, Denmark, Ireland, and Luxembourg are struggling with relatively large spreads between baseline projects and targets, while ten countries, Central and Eastern European countries plus Greece and Portugal in particular, are expected to have considerable surpluses (see Figure 4). With the 5% cap, tradable surpluses in these ten countries could still equal 18 million AEAs per year. Though demand is expected to be quite low in the 20% scenario, the 30% scenario has been predicted to dramatically increase liquidity in the prospective AEA market.<sup>67</sup>

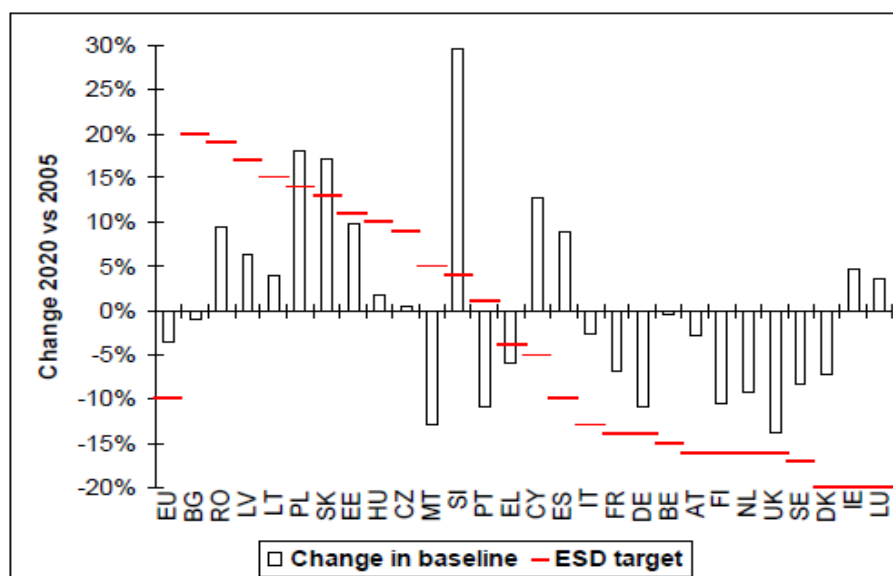


Figure 4: Projected levels of non-EU ETS emissions in EU Member States in 2020 compared to their ESD targets.<sup>68</sup>

Furthermore, a GIS that produces actual emission reductions is an incentive to trade as it will free up additional AEA units in subsequent years. Lastly, unlike under the Kyoto Protocol, enforcement is not questioned in the EU context, i.e. countries that miss their AEA targets face rigorous corrective actions (Article 7 ESD); in order to avoid these, countries will be inclined to buy AEA units; and both sides, not least for reasons of public expectations, will aim at selling and buying greening schemes rather than simply 'hot air'.

<sup>66</sup> EU Commission Staff Working Document accompanying the Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Analysis of Options to Move Beyond 20% Greenhouse Gas Emission Reductions and Assessing the Risk of Carbon Leakage, Background Information and Analysis, Part II, SEC(2010) 650, 26 May 2010 (page 43).

<sup>67</sup> M. Kruppa, New EU Market Could Create Huge CER Demand: Analysts, Point Carbon, 23 November 2010.

<sup>68</sup> Source: EU Commission Staff Working Document accompanying the Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Analysis of Options to Move Beyond 20% Greenhouse Gas Emission Reductions and Assessing the Risk of Carbon Leakage, Background Information and Analysis, Part II, SEC(2010) 650, 26 May 2010 (page 32).



This being said, the AEA quotas today are not yet tradable, and while implementing legislation is under development, it cannot yet be assessed when and under what conditions the inter-Member-State trading will happen.

Similarly, it is not yet clear to what extent private individuals can participate in such trade. While private entities are not under compliance obligations, they may still be given the right to hold and transfer AEA units. The IET practice has shown an increasing involvement of private parties in AAU transaction. They can act as buyers in back-to-back transactions or, as in the Japanese cap-and-trade example, as end-users. There are further options, too. In JI transactions in New Zealand, AAUs are offered as collateral; and Australia recently saw its first time AAU deal involving a forestry project in Western Australia led by a private developer that received AAUs in return for emission reductions and resold them on the international markets.<sup>69</sup> It remains to be seen how the implementing legislator, the European Commission, structures the trade with AEA before one can explore the various trade constellations that will exist. Yet, the concept of GIS may certainly inspire the way country-to-country deals will be performed.

### Conclusion

The project mechanisms of the Kyoto Protocol have created a wealth of knowledge and experience in the field of offsetting. Though they are likely to continue to lead the sector, additional project-based schemes are possible, and indeed some are already getting underway.

Aside from a potential mechanism under Article 24a EU ETS, there is scope for national, bilateral or multilateral offsetting schemes within the EU. These are consistent with the Kyoto Protocol and EU climate legislation, though they must be designed within the boundaries of EU competition law. While credits created under such schemes would not be traded under the EU ETS or ESD, they would have an indirect effect on these schemes by reducing emissions and thus releasing tradable units. There may also be scope for Member States to award ETS allowances to project developers, though this will not be possible after 2012.

The prospective AEA market also presents new opportunities. With many Member States expected to have significant margins between targets and baseline emissions, and others foreseeing surpluses, public expectations and concerns regarding environmental integrity of AEA sales may create fertile ground for the development of Green Investment Schemes. This is particularly likely if the EU increases its 2020 commitment to 30%, a scenario in which considerable liquidity is expected in the AEA market. With the design of the AEA trading market yet to be realised, however, it remains to be seen how its structure will influence the operation of such schemes, and to what extent the involvement of the private sector will be permitted.

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<sup>69</sup> Moritz von Unger, AAU Sales and Green Investment Schemes: Perspectives for 2012 and After, Climate Focus Commentary, November 2010, [www.climatefocus.com](http://www.climatefocus.com).





## 6. Conclusion: How to Operationalise Offsetting in the EU: Governance and Project Perspectives

Important decisions are pending—on CP II, on the Kyoto Protocol and the international climate change regime as a whole, on the continuation of JI during the gap, on the EU move from the 20% to the 30% target, on the implementation of Article 24a and the trade rules for AEA units, in particular—and yet preparations for the time after 2012 have to be made. EU governments and policy-makers must make day-to-day decisions, as well as short and medium term policy choices, without a complete knowledge of how the regulatory frameworks will look in two, five and eight years time. JI project developers and project investors in ongoing projects either have to plan continuing operations, hoping for a regulatory framework that allows that their projects continue from 2013 or start closing down activities. New developers and investors are weighing the risks that go hand in hand with the current stalemate in international negotiations and the regulatory uncertainty on the European plane.

This report on the regulatory certainties, voids and expectations of carbon offsetting in Europe, commissioned by KfW on behalf of German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety under the ongoing CDM/JI Initiative, will help policy-makers assess the current legal situation relating to offsetting in Europe after 2012, along with the policy options available and the legal avenues through which they can be achieved. From the perspective of governmental market participants it will assist in assessing the global risk situation and informing strategies for developing sustainable carbon portfolios beyond 2012.

Ongoing projects that span the time prior to 31 December 2012 and thereafter such as the two JI PoA projects of Polish BOS Bank and KfW (Boiler Modernization Programme and Building Energy Efficiency Programme) face particular challenges. The two projects are scheduled to be registered (determined) in 2011. With respect to the present common understanding of the legal situation only emission reductions until end of 2012 can generate ERUs. However, the majority of the emission reductions under the two projects will be achieved after 2012. So the present legal uncertainty risk to undermine the proper implementation of the two projects as the planned revenues from ERUs generated after 2012 are necessary for their implementation.

The findings of the present report are summarized in the following:

### International (non-EU) JI during the True-Up Period

For the short term, 2013-2015 at least, a positive decision of the CMP could bring sufficient clarity. The failure to do this in Cancun has extended the period of uncertainty considerably. However, positive signals in 2011 sessions of the AWG-KP and a decisive pronouncement in Durban will secure the continuation of JI until 2015, and provided that Annex I Parties agree to extend Letters of Approval, existing projects will be operational for a few more years. However, the limitation of demand from the most important credit buyer, the EU market, must be noted. Only JI projects that are registered (determined) prior to 31 December 2012 will be recognized as ERU source by the EU ETS (and the ESD). The 31 December 2012 milestone, thus, is decisive for all who are currently (or prior to 2013) in the JI project development phase.



## International (non-EU) JI after the True-Up Period

The long-term planning for JI depends on the entry into force of a second commitment period and/or the conclusion of a comprehensive international agreement on climate change. With no progress on this issue in Cancun, reliable forecasts in this respect cannot be made. However, at least from a European perspective, the continuation of a JI-type offsetting mechanism, on the bilateral, multilateral or global level, is a policy priority and there are signs that provided an environmentally robust project is developed it will be recognized by future crediting schemes that are linked to the EU ETS. While there is not yet a clear roadmap and certainty that, and when, any such offsetting schemes will be developed, investors may still find the existing risks acceptable to go ahead with any projects in countries such as Russia, Ukraine, Belarus, Kazakhstan, and elsewhere.

## Projects within the EU

For the European offsetting market proper, the situation, in some ways, is even less predictable than the JI market in other JI countries. This is because both the EU ETS and the ESD failed to clarify whether JI projects may or may not be hosted by EU Member States after 2012. However, a number of conclusions have been drawn from the analysis above. First, JI, if at all, could occur only in the non-EU ETS sectors, i.e. the strict ban on double-counting will exclude all projects that have a direct or indirect effect on EU ETS installations. Second, JI projects in the non-EU ETS sectors will only be admissible if they fit into the structure of the ESD. Double-counting, again, is the decisive element in this respect. As the current rules do not foresee that ESD figures (AEAs) are adjusted by any crediting under JI, ensuring that credits from JI projects can be recognised under the ESD while avoiding double-counting issues would require that the (delegated) legislator become active by **adding "ERUs" to the list of credits whose issuance necessitates adjustments of AAUs**, having JI treated as credits from the new European offsetting mechanism, Article 24a EU ETS, or transferring all non-ETS sector JI into the Article 24a EU ETS framework. Either way, post 2012 JI hosted in EU Member States will become operational only once legislative provisions have been made.

Third, Article 24a EU ETS avoids many of the problems of JI, and may ultimately substitute it for the purposes of the EU ETS and the ESD. As the instrumentalisation of the article depends on the adoption of implementing legislation through comitology, special attention should be given to the planning of European policy-makers. If the decision is made to substitute EU JI projects for Article 24a projects, securing an uninterrupted continuation from the Second to the Third Trading Phase (2013-2020) and giving project developers and investors a minimum amount of time for project planning will require legislation to be proposed and processed through comitology as soon as possible.

Utilizing the existing JI framework for the purposes of a new mechanism under Article 24a without further (delegated) legislation is neither legally permissible nor practicable. However, implementing measures could be drafted so as to utilize many of the key JI components to ensure a smooth transition to a new mechanism in 2013. In addition, the JISC may be seen as a **"service provider" that could add legitimacy and recognition to a new mechanism both in the short and medium term.**



Beyond Article 24a and the continuation of JI, Member States may draw up national and bilateral/multilateral offsetting schemes in line with European legislation on, inter alia, state subsidies. However, credits of such schemes, if generable, will not be recognized by either the EU ETS or the ESD.

The trade with emissions quota between Member States, however, does allow the duplication of International Emissions Trading and Green Investment Schemes. The AEA trade—whose details are yet to be established—may also serve as Government guarantee (collateral) for project development after 2012.