

NewMarket Mechanism

Will Kazakhstan be the next country to establish a carbon emissions trading scheme?

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Kazakhstan is among the few countries without access to international compliance carbon markets. But this may change now that the country has adopted legislation to implement an emissions trading scheme (ETS).

Kazakhstan has a unique position under the Kyoto Protocol. It is considered an Annex I party (developed country) to the UN Framework Convention on Climate Change, but has not yet been included in the protocol's Annex B (has an emissions target).

Therefore, the country has not been allocated Assigned Amount Units, and is neither eligible to

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participate in the Clean Development Mechanism (CDM) nor in Joint Implementation (JI), the protocol's project-based flexible mechanisms.

While access to international carbon markets remains elusive, on 3 December 2011 President Nursultan Nazarbayev signed legislation for the implementation of an ETS. Throughout 2012, the adoption of secondary legislation has been lending shape to the scheme. Some of the design elements of the Kazakhstan cap-and-trade system resemble those of the EU ETS.

The Kazakhstan ETS will cover 177 companies, with a total cap set at 146 million tonnes of carbon dioxide equivalent (Mt CO₂e). The legislation foresees that the scheme will start with a one-year trial period in January, followed by a seven-year trading period from 2014 till 2020.

Emission allowances are to be allocated based on participants' 2010 emission levels. The Ministry of Environmental Protection (MEP) is considering free allocation of allowances for the 2013 trial period. The current legislation provides for auctioning in the years after 2013. Banking from the first to second trading period is not permitted.

Regulation of the system will be undertaken by the MEP. The legislation further defines:

- trade of emission units through designated trading platforms;
- a national emissions registry and accreditation of validators of monitoring plans and verifiers of emission reports;
- the information participants must provide in their application for an allocation. This includes a list of installations, monitoring plans and an overview of plans to reduce emissions and comply with the scheme's targets; and
- modalities for offset projects in non-ETS sectors, credits from which can be used for compliance purposes under the ETS. Offset projects will apply basic principles from the CDM.

However, several doubts remain. Implementation of the ETS in 2013 – or even in 2014 – remains subject to political uncertainty, despite legislation and other key structures being in place. Also many design elements remain outstanding.

The uncertainties include:

- the compatibility of the ETS with Kazakhstan's economic growth plans is being questioned by key business associations and energy producers. They have expressed concern that the scheme will adversely impact the country's ability to reach its growth targets;
- the first National Allocation Plan (NAP) for the period 2013–2020 has been drafted, but has yet to be adopted;
- a decision needs to be made on whether to cover

Comparing the Kazakhstan ETS with the EU ETS

ETS design element	Kazakhstan	EU (2012–2020)
Sector coverage	Oil and gas production, energy, mining and metallurgy, chemical industry, agriculture and transport	Energy, cement, steel, pulp and paper, glass, lime, aluminium, chemical industry, aviation, refineries
Entities/installations covered	177 entities; number of installations still undetermined	Over 12,000 installations
Emission coverage	Over 50% of Kazakhstan's greenhouse gas (GHG) emissions	Approximately 45% of EU GHG emissions
Gases covered	Carbon dioxide (CO ₂) and methane (CH ₄), but a final decision on inclusion of CH ₄ is pending	CO ₂ , N ₂ O, perfluorocarbons.
Threshold for inclusion	20,000 t of CO ₂ e/year	25,000 t CO ₂ e/year for installations whose inclusion threshold is defined by their emission level
Offsetting allowed	From domestic projects on coal-mine methane, waste management, renewable energy, energy efficiency, or in agriculture and land use, land-use change and forestry (LULUCF)	From CDM, JI and article 24a projects. The latter is dependent on implementing legislation that has yet to be adopted.
Trading periods	Pilot phase in 2013, second phase from 2014–2020.	2005–2007, 2008–2012, 2013–2020.
Targets	Overall objective is a 15% reduction by 2020 compared with 1992 emission level. Sectoral target in the energy sector is a 3% reduction by 2015 compared with 2012 level	21% reduction by 2020 compared with 2005 level

- CO₂ alone or to include methane (CH₄) also;
- the historical data underlying the first NAP has not been verified by independent third parties; and
- the establishment of a national emissions registry remains incomplete.

Kazakhstan has used the EU ETS as the basis for the design of its own programme. Similarities between the two schemes can be found in the approach and methods for allocation and in the monitoring, reporting and verification system employed. There are important differences, however (see table).

One difference is the coverage. The Kazakhstan ETS reflects high ambitions in terms of greenhouse gases and sectors. The scheme covers future emissions of CO₂ and CH₄, while the EU system initially only applied to emissions of CO₂.

Sector coverage is also broader, with transport and agriculture included. However, the small size of the majority of installations in those two sectors, coupled with low political will to include some entities, such as airlines and railroad companies, means that most installations in the sectors are not likely to be covered during the first and second trading periods.

A further difference is that the Kazakhstan ETS applies to companies rather than installations, at least during the first trading period. This is a legacy from previous environmental legislation, which was also at the company level.

Finally, unlike the EU ETS, the Kazakhstan system does not allow for the use of offsets from CDM or JI projects. Offsets from projects within Kazakhstan, on the other hand, are permitted, while in the EU ETS implementing provisions for the use of domestic offsets under Article 24a of the emissions trading directive are yet to be adopted.

If implemented as planned, the Kazakhstan ETS will open a range of opportunities for companies within the country and abroad. These include:

- providing additional capacity for the validation of

monitoring plans and the annual verification of monitoring reports;

- responding to demand for energy efficient technologies created by the scheme's emission reduction incentives;
 - offering dedicated financial services to ETS participants;
 - providing legal services to ETS participants, brokers, verifiers and engineering companies to support with the trade of allowances or with contracting of service providers; and
 - providing access to carbon market information.
- ETS development in Kazakhstan can benefit from

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the experience of people operating in cap-and-trade schemes in other countries. More importantly, international cooperation on ETS development is needed to harmonise the design of carbon markets and, thereby, keep prospects open for linking and integration in the future. ●

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