



## CONTINUED ISSUANCE OF ERU POST-2012 UNDER THE KP

### QUESTIONS AND ANSWERS

16 NOVEMBER 2010

#### 1. INTRODUCTION

The JISC at its recent meeting in October 2010 as part of its report<sup>1</sup> to the CMP suggested Parties to provide clarity on the continued issuance of ERUs post-2012. The rules of the Kyoto Protocol were designed assuming a second commitment period would directly follow the end of the first commitment period. Due to a delay in reaching a new international agreement, a new situation has arisen in which a GAP period will appear. In this context a *crucial* observation was made by the JISC:

*78. JI is part of the Kyoto Protocol, and although the emission targets of Annex I Parties are negotiated on a commitment period by commitment period basis, JI is designed as 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 ERUs, and accreditation of independent entities.*

In this context the JISC have made the following recommendation to the CMP:

*123. Recommendation: The JISC recommends that the CMP, with regard to the continuation of activities under Track 2 procedure in the immediate period beyond 2012:*

- a) Clarify that these activities may continue*
- b) Allow emission reductions and removal enhancements, achieved by existing and new JI projects between 1 January 2013 and the end of the .true-up. period, or the entry into force of new commitments, whichever is the sooner, to be issued by host Parties as ERUs by converting AAUs or RMUs from the first commitment period.*

As the only project-based offsetting mechanism available to Parties and the private sector in Annex I countries, the JI mechanism has become an important stimulus to investments in energy efficiency, renewable energy and other GHG reductions. Continued ERU crediting should be seen as a GAP measure to avoid an abrupt discontinuity in such investments. The continued issuance of ERUs will furthermore be able to maintain the JI regulatory framework in place today during a gap period without compromising the environmental integrity of CP1 commitments. Without such, or similar, gap measure a new mechanism would have to be established from scratch in a post-2012 agreement.

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<sup>1</sup> Report on experience with the verification procedure under the Joint Implementation Supervisory Committee and possible improvements in the future operation of Joint Implementation

Below are key questions related to continued ERU crediting addressed to inform and provide facts to Parties in their further consideration of the measure.

## 2. QUESTIONS AND ANSWERS

*1. Will continued ERU crediting lead to borrowing from future commitment periods and thereby undermine the integrity of the KP commitments?*

ERUs are created by converting AAUs that have already been issued by a Party into its national registry (Decision 13/CMP.1, annex, para 29). If a Party does not hold AAUs in its registry, no ERUs can therefore be issued. As the Kyoto Protocol does not allow for borrowing of AAUs from future commitment periods, and AAUs can only be issued after a party's assigned amount has been calculated and the commitment period has begun, only AAUs from the first commitment period will be available from which to issue ERUs during a gap period. Therefore, continued ERU crediting will not lead to borrowing from future commitment periods.

*2. Will the continuation of JI after 2012 weaken the targets of CP1?*

As the issuance of one CP1 ERU is done by cancelling one CP1 AAU those credits cancel each other out and there are no extra compliance units available under CP1. The targets are not weakened; on the contrary, since AAUs maintain their CP 1 compliance capacity up until the end of the true-up period, their conversion into ERUs guarantees that Kyoto units translate into meaningful mitigation action.

*3. Is continued ERU crediting inconsistent with the accounting rules under the KP?*

No, there are no provisions of the Marrakesh Accords or elsewhere in decisions under the Kyoto Protocol, which have to be amended to continue issuance of ERUs during the true-up period.

The Kyoto Protocol was intended to have sequential commitment periods, where CP2 would follow immediately after CP1, and intended to have ERUs issued post 2012 on the basis of CP2 AAUs.

While the Marrakesh Accords did not envisage a gap period where a CP2 would not follow immediately after CP1, the continued conversion of CP1 AAUs during a gap period is actually fully consistent with all relevant decisions and does not require any amendments to said decisions. The relevant rules includes, in particular, decision 9/CMP.1 on Guidelines for the implementation of Article 6 of the Kyoto Protocol, and 13/CMP.1 on modalities for the accounting of assigned amounts under Article 7, paragraph 4, of the Kyoto Protocol.

To ensure that no CP1 ERUs can be issued after a CP2 have entered into force, and to avoid any potential inconsistency with the accounting rules, the recommendation by the JISC specifically limits the continued issuance of ERUs on basis of CP1 AAUs to a period from 1 January 2013 to the end of the true-up period or the entry into force of new commitments, whichever occurs first.

*4. Could continued ERU crediting lead to double-counting issues arising under the Effort Sharing Decision?*

Concerns over double-counting under the Effort Sharing Decision (ESD) arise from the lack of express provision for deductions from Member States' Assigned Emissions Amounts (AEA) in respect of ERUs issued for JI projects within Member States' territories. This leads to the possibility that Member States could sell ERUs for reductions made and still count those reductions towards their commitments under the Decision.

Note that this issue concerns JI projects hosted by EU Member States alone and that it relates to Community legislation, not the Kyoto framework. The same concerns would arise in the absence of the gap, i.e. under CP2.

If EU Member States continue to engage in JI on their territories, any concerns regarding double-counting under the ESD can effectively be excluded by, for instance, acknowledging ERU crediting under Article 24a of the revised EU ETS Directive. Article 10(b) of the ESD would then foresee the deduction of the relevant amounts from the country AEA's.

*5. Will continued ERU crediting legitimize or imply any official acceptance of AAU surpluses?*

There are several reasons why continued ERU crediting is not of significance in relation to the issue of AAU surpluses:

- (a) An AAU surplus will occur when a Party is holding a volume of AAUs larger than is needed to comply with CP1 commitments. During the true-up period it remains undisputed that Parties may continue to transfer AAUs. Converting a portion of AAUs to ERUs in respect of actual and verified emission reductions and having such ERUs transferred will thus have the same impact on an AAU surplus as would direct transfer of the AAUs. Moreover ERUs issued in respect of emission reductions occurring during the true-up period will, contrary to reductions pre-2013, not free up any AAUs and thus not add to a surplus.
- (b) The continued issuance of ERUs will stimulate investments in energy efficiency, renewable energy and other GHG reductions which are real and verified under JI guidelines. As such it will represent a robust alternative to AAU transactions of any sort after 2012.
- (c) The expected volume of additional ERUs to be issued under continued ERU crediting will in any case be insignificant compared to the overall volume of surplus AAUs.

*6. Will continued ERU crediting reduce the quality of compliance instruments in CP1 of the KP?*

On the contrary continued ERU crediting can be said to improve the quality of compliance instruments available for Parties to fulfill commitments under CP1 of the KP.

ERUs are issued by cancelling an equivalent number of AAUs in respect of emission reductions verified in accordance with decision 9/CMP.1 and relevant guidelines issued on that basis. There is thus an immediate link between emission reductions achieved and ERUs, which is not necessarily implied by an AAU and the quality can thus be said to be improved.

AAUs are not eligible as compliance instrument under the EU ETS. The quality of compliance tools available to ETS operators will however neither degrade in as so far that there is an absolute cap on the

number of credits operators can use for compliance and the cap can be filled with CERs in absence of ERUs.

### *7. Will continued ERU crediting flood the EU ETS market?*

Continued ERU issuance for the period during the true-up period will not flood the ETS.

Under Article 11a(8) of the EU ETS the amount of offset credits operators can use towards meeting their commitments - CERs, ERUs or other international credits - is capped. The exact limits for each operator are to be set by the Commission in comitology proceedings. As this cap applies to all permitted credits in aggregate, disallowing ERUs would simply allow for more CERs and/or credits issued pursuant to agreements with third countries under Article 11a(5). Similarly, Article 5(1)(b) of the Effort Sharing Decision cap Member States use of ERUs and CERs at 3% of their total assigned annual emissions. As such, continued ERU crediting will have no affect on the amount of credits permitted in the EU ETS.

Moreover, from a practical standpoint the level of ERUs entering the EU ETS market is and is likely to remain low.

### **3. ABOUT THE JOINT IMPLEMENTATION ACTION GROUP**

The Joint Implementation (JI) mechanism under the Kyoto Protocol has developed a project pipeline that is expected to generate 409 million tons of greenhouse gas (GHG) emission reductions in the period 2008-2012. Its central principle has proved simple and effective: countries under the Kyoto Protocol with capped emissions can trade project credits and reduce their total emission profile. The JI mechanism delivers low transaction costs, substantial benefits, and should be expanded in the next climate framework.

The Joint Implementation Action Group (JIAG) was formed in March 2008 to support the post-2012 negotiations with hands-on experience from market participants. The consortium of carbon market pioneers representing over 100 millions of tonnes of greenhouse gas emission reductions through JI projects constantly interacts with policy-makers and interest groups to communicate its views. The JIAG believes it is essential that JI is enhanced in the next climate agreement, maximizes its potential as a project finance mechanism, creating incentives to reduce GHG emission in a wide range of sectors and among a broad range of actors.

On the web-site [www.jiactiongroup.com](http://www.jiactiongroup.com) you will find an overview of the JIAG's activities, its publications, policy papers, legal papers, information on how the JIAG works and how entities can support its activities by becoming a JIAG member. On the website a Legal Opinion on the continued issuance of ERU can be found.

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