ADMINISTRATIVE UNIT OF THE RUSSIAN FEDERATION ON KYOTO FIELD

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At present, Russia is active in preparation for ratification of Kyoto Protocol. This is testified by development of legislative, regulatory and methodological frameworks, works on *greenhouse gas* (GHG) emissions accounting, accumulation and analysis of GHG emissions reduction projects preparation and implementation, elaboration of specialized documentation for such projects.
Buyers of Russian emission reductions have become more active too: increasing number of western companies, with operations in various industries, express their interest in cooperation with Russian enterprises and start looking for potential investment projects; increasing number of countries carry out regular international emissions reduction projects tenders. Now, there is no need to prove, as two years ago, that carbon finance is not a myth, and even not a tale. In the light of forthcoming ratification by Russia and, consequently, Kyoto Protocol coming into effect, we are facing another issues: projects in what Administrative Units of the Russian Federation (RFAUs) will be first in a queue for carbon investments; how the Russian Federation Government will distribute assigned amount among RFAUs; what rules and procedures of projects preparation and implementation will be in place at the national level.
In this article, falling for temptation to glance in the future, we will try to imagine possible algorithm of both RFAUs and enterprises actions within the project preparation.
In general, in regulation of carbon field economic relations the Government should provide three sets of conditions.

a) The carbon market should be flexible. Its openness for participation should be ensured by the absence of high administrative barriers. Its transparency should be achieved by high quality of both actual information about the market legal rules, GHG emissions levels, changes in its assigned amount for the Russian Federation and compliance with national commitments, and, as well, by specialized analytical information about market participants, carbon projects and transactions, about the role of carbon investments in social and economic development of regions. Universality of the carbon market must ensure uniform rules for maximum number of its participants.

b) At the same time, stability of the carbon market must be ensured, i. e. the most effective compliance with GHG emissions stabilization commitments. The system of the developing market relationships should not become a decorative “rattle” which demonstrates once more “marketness” of Russian economy. That means that a maximum admissible share of Russian assigned amount should be in circulation. On the other hand, we must ensure commitments compliance and avoid excess sales of our emissions allowances. The latter is very important aspect of “carbon safety” of the Russian Federation, and advisable in economic terms – excess supply will decrease price for our emissions at the international market. In order to make the carbon market sustainable, the legislator may choose “soft” or “hard” scenario of regulation. The “soft” scenario envisages a predominant use of RFAUs reservation to insure and guarantee commitments compliance. The ”hard” one represents development of system of restrictions, sanctions and penalties at GHG emissions transactions.

c) Control over the carbon market participants must be ensured, here "soft" or "hard" measures are envisaged as well. The first group of measures includes permissive procedures providing access to emissions transactions (licensing, certification, accreditation, registration). The second group relates to control itself, and includes the system of audits, evaluations, tenders between both market participants and separate categories of investment projects.

The above mentioned system of measures should be implemented in all spheres of state regulation of GHG emissions reduction. The most important thing is to fix the status of GHG emissions and determine methods of this sphere regulation in the relevant branch of law. Today, the predominant position among experts is to use civil instead environmental law that corresponds with the Kyoto Protocol spirit at greater extent.

Accordingly, it is necessary to determine regulations related to carbon resource taxation and its reflection in accounting reports. In this connection, we should have in place the systems of GHG emissions accounting and monitoring systems, state cadastre, i. e. the system of right-establishing documents.

Simultaneously, another system, that of investment projects registration should exist in order to provide projects with the status of Joint Implementation projects.

At the same time, the regulatory framework for carbon market itself should be developed and put into action to regulate relations between buyers and sellers. The system of licensing of various types of activities and certification of products and services at the carbon market should be also in operation.

One more important issue is the mechanism of Russia's assigned amount allocation between RFAUs. There is understanding that Russia's commitments on GHG emissions stabilization represent the sum of regional commitments, i. e. emission permits should be distributed in proportion to commitments.

We can often hear suggestions that since the Kyoto Protocol establishes the 1990 as the base level, it is advisable to make allocations in accordance with 1990 levels of emissions in RFAUs. It seems to be the simplest solution, but it's wrong.

The most substantial argument against such way of allocation is that it would not ensure uniform system of assigned amount reservation with the purpose of guarantee compliance with national commitments. Anyway, a part of the assigned amount should be reserved by federal government for these purposes.

Besides, such an allocation would be unfair towards the most actively developing regions with increased emissions levels due to rapid social-economic development and slower rates of energy efficiency improvement. At the same time, those RFAUs, where social-economic recession took the lead over energy efficiency decrease, may get unjustified rewards in the form of excess carbon resource. These are the worst cases, extremes, they show inefficiency of such approach to GHG emission permits allocations between RFAUs.

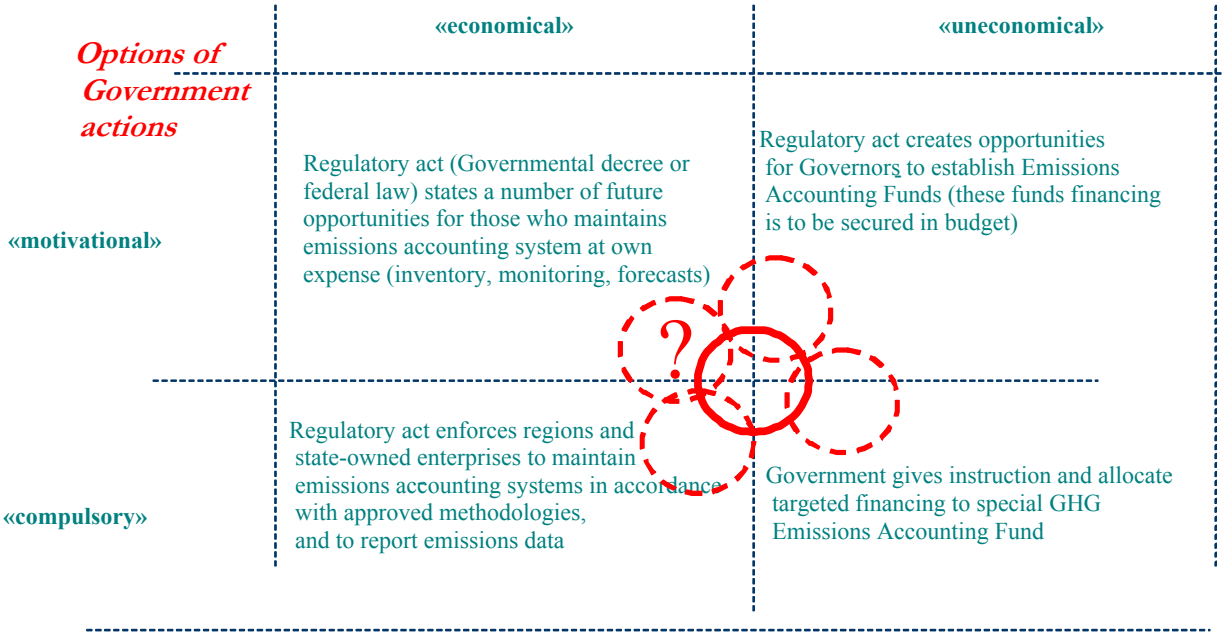
The most preferable approach is the following: allocation of emissions level in proportion to specific GHG emissions levels per product unit of RFAUs and their dynamics since 1990. This would enable not only to reward the regions with energy efficiency growth, but give actual incentives for energy saving to enterprises in lagging regions as well.

Whatever the case, it is obvious that all the RFAUs should implement GHG emissions inventories from 1990 onwards in the context of specific emission sources. Those inventories should be based on uniform methodology.

This is serious and large-scale work requiring both financial and human resources. Execution of this work can be either motivational or compulsory, and at the same time economical or uneconomical.

Introduction of GHG emissions accounting system

GHG emissions inventory and monitoring systems are the basis for national carbon market infrastructure



Motivational/economical option implies coming into affect of a regulatory act setting a number of advantages for RFAUs which will, at their own expense, introduce emission accounting system, including inventory, monitoring and forecasting components. Such advantages may be: giving priority to GHG emissions reduction projects, inclusion of projects into federal portfolio, top-priority allocation of GHG emissions, participation in the system of federal guarantees for carbon investments, etc.

Motivational/uneconomical option can be realized through providing governors of RFAUs with opportunity to establish specialized GHG emissions accounting funds financed from the budget.

Compulsory/economical option may see life through adoption of governmental decree enforcing RFAUs to introduce emissions accounting system in accordance with federal methodologies, and report their emissions data. The regions will be free in choosing sources of financing and methods of this work implementation herewith.

Finally, compulsory/uneconomical option relates to allocation in federal budget of earmarked financing for GHG emissions accounting funds, and their control from federal level.

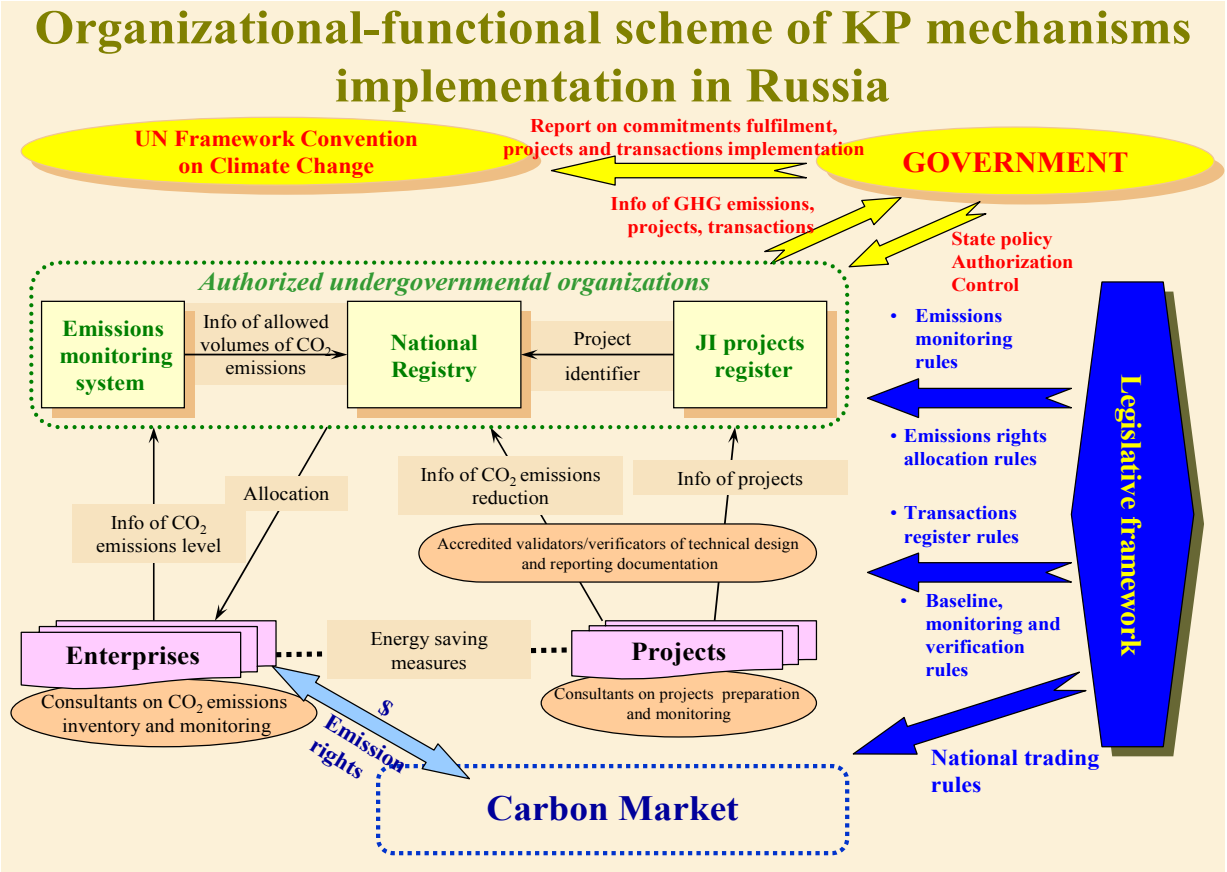


Fig.1 Organizational-functional scheme of KP mechanisms

So, the full-value and effective participation of RFAU in drawing financial resources to energy efficiency projects needs a certain number of measures.

First, it needs to implement inventory of GHG emissions under uniform methodology in accordance with international requirements, introduce regional system of GHG emissions monitoring in accordance with the Kyoto Protocol provisions, get international certification of this system, and verify actual emissions data.

Second, in accordance with regional inventory data, each RFAU should assert its volume within Russia's assigned amount under the process of emissions permits allocation among regions. Thus, RFAU will create their own carbon resource to ensure participation in GHG market and project financing.

It should be also taken into account that a regional regulatory framework may need more accurate definitions with a view to make possible GHG emissions allocations and transactions.

Projects financing at a regional level may be arranged as follows: preparation of the list of energy saving and energy efficiency projects and measures leading to GHG emissions reduction, preliminary calculations of potential reduction and its cost; selection of priority projects will enable to construct RFAU's project portfolio for presentation to potential investors.

The further activities on the pre-design, design and implementation of GHG emissions reduction projects and measures mayan be financed by investors. Herewith, the portfolio-based management would allow balancing project risks.

Sales of emissions reductions generated from early-stage projects will facilitate initiating of further mechanism of revolving financing for energy efficiency projects.

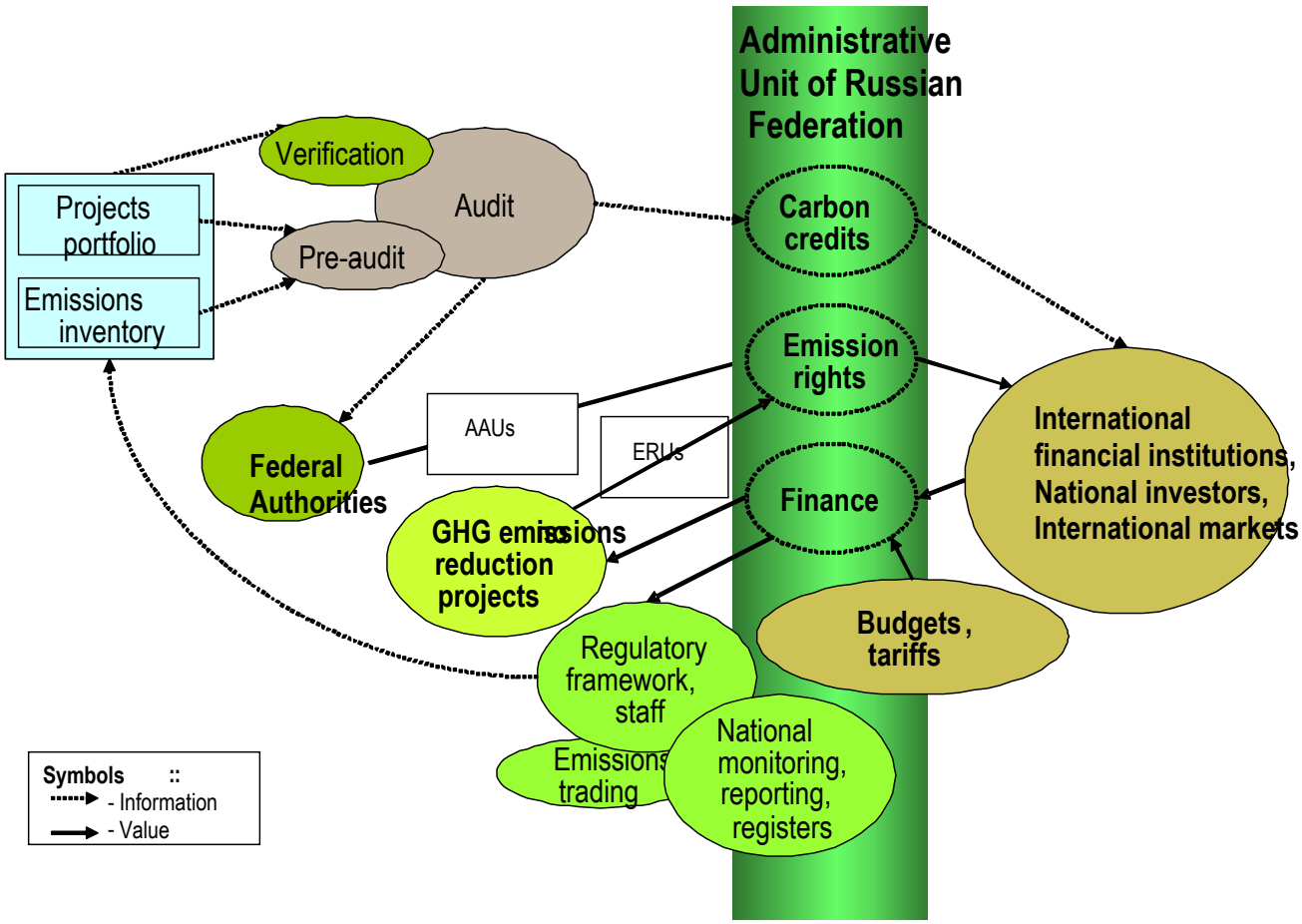


Fig.2 Procedures of enterprise participation in the carbon market operations

This scheme provides clear procedures of enterprises participation in the carbon market operations.

One of the governmental authorities should be assigned with responsibility for national scale emissions inventory. It may be Committee of the Russian Federation for Hydrometeorology (Roshydromet) since it is responsible for submission of statistical data on emissions to Secretariat of UN Framework Convention on Climate Change. However, this task can be entrusted to the Ministry of Natural Resources and Environmental Protection (MNR), taking into account the wide network of regional branches.

An enterprise, independently of its ownership, submits application claiming its willingness to implement emissions inventory to the assigned Coordinating Authority. This authority conducts a tender among companies which have licenses for execution of inventories. The licenses are issued by Coordinating Authority in accordance with the scheme similar to licensing of energy audit execution.

The company-winner executes inventory. However, the enterprise can do it itself in case it uses the certified methodology and has relevant license. Inventory results are submitted to Coordinating Authority for review by itself or by means of specialized organizations or competent international agencies. Upon conclusions of this review, the enterprise gets the inventory certificate.

The inventory certificate provides enterprises with one-year registration title in the national GHG emissions monitoring system. Within this system, for no less than one year, enterprise should submit on a quarterly basis its emissions data collected through monitoring system directly or through company with monitoring and inventory license. After independent audit, such an enterprise gets the Certificate of participation in monitoring system.

These certificates, in accordance with the Governmental decree, are issued by Coordinating Authority, which also appoints a registrator for keeping emissions cadastre and carrying out a selective check-up of licensed organizations.

Besides, a licensed organization should make GHG emission forecasts up to 2012 for enterprises-participants of the monitoring system, using the certified methodology.

Inventory certificates or certificates of participation in the monitoring system, as well as emissions forecast, provide enterprises with the right to get a portion of the national assigned amount corresponding to enterprise's actual emissions for previous year, as property for inclusion into balance but with limitation of the right for its further transfer. Such an enterprise is registered in the national system of GHG emissions trading and gets the right to participate in tenders for assigned amount allocation for free disposal.

The Government provides the Ministry of Economic Development and Trade with the responsibility for development, introduction and control of rules for accounting within the national emissions trading system, including emission rights register and transactions register. The same ministry conducts regular tenders on allocation of unused assigned amount.

Tenders of type I. Participants are enterprises with monitoring or inventory certificates, and emissions forecasts, and thus having licenses for emissions rights reserves. In this case, we can see a simplified scheme of emissions rights allocation in the requested volume that corresponds to the expected volume of emissions reduction through internal measures or joint projects. However, this requested volume should not exceed 90% of 1990 level (10% or more should be reserved for insurance purposes).

Tenders of type II. Participants are enterprises with inventory certificated for the previous year, provided non-exceeding of 1990 emissions, which have registered JI projects in the established order and have feasibility studies in place. In this case, an enterprise can get no more than 100% of estimated emissions reductions from the projects, but with the right for immediate transfer to investor of no more than 50%.

Tenders of type III. Participants are enterprises at various stages of registration in the national systems of monitoring and inventory, without any certificates, but with registered JI projects and feasibility studies. In this case, provided reliable projects' support (risks insurance, bank guarantee, etc) emissions rights can be allocated in the volume not exceeding 50% of the estimated emissions reductions from the projects, but with the right for immediate transfer to investor of no more than 25%.

The main condition for an enterprise to get a portion of the assigned amount at its own disposal is to undertake the commitment to have sufficient volume of GHG emission rights in the first commitment period (2008-2012) to cover its actual emissions in this period.