



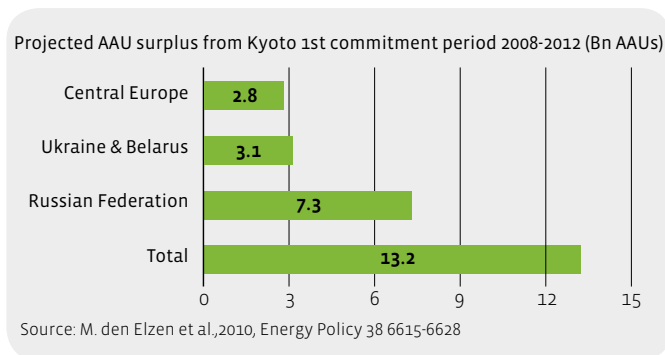
## Executive Summary

With less than six months left of the first commitment period of the international climate regime, the Kyoto Protocol, there still is no agreement between Parties on the 'AAU surplus issue'. We explain why resolving this issue - which is currently being negotiated under the United Nations Framework Convention on Climate Change (UNFCCC) - is vital to the viability of any future climate regime.

Assigned Amount Units (AAUs) were introduced under the Kyoto Protocol. One AAU allows a country to emit 1 tonne of CO<sub>2</sub>e. Each country with an emissions reduction commitment under the Kyoto Protocol's first commitment period received AAUs equivalent to the number of tonnes it is allowed to emit during that first 5-year commitment period.

Kyoto Protocol rules allow countries to carry over unused AAUs into the next commitment period. A number of countries, such as Russia, Ukraine and Poland, have very large amounts of surplus AAUs. By the end of 2012, up to 13 billion surplus AAUs could be carried over into the Kyoto Protocol's next commitment period. This is almost three times the annual emissions of the European Union or more than twice those of the United States.

This surplus threatens the viability and effectiveness of international climate policy regimes. If no restrictions are placed on the AAUs surplus, these pledges could lead to no additional emissions reductions compared to business-as-usual emissions projections by 2020. This holds true even if the Russian surplus is excluded.<sup>1</sup> Allowing the full AAU surplus to be carried over could eliminate the chances of avoiding dangerous climate change by overshooting the +2°C limit.<sup>2</sup>



Parties are also allowed to carry over emission reduction credits from the Clean Development Mechanism (CDM) and Joint Implementation (JI). The carry-over of CDM credits (CERs) and JI credits (ERUs) is limited to up to 2.5% each of the total amount of AAUs a country received for the first commitment period. Carry-over from these offsetting mechanisms could lower actual emission reductions by 2020 by roughly 6%.

If a solution to these surpluses is not found, it will significantly weaken the environmental integrity of a second commitment period under the Kyoto Protocol. A new climate deal will likely build on parts of the Kyoto Protocol's framework. Having a second Kyoto commitment period that is significantly weakened by low targets and participation, and large loopholes such as a massive AAU surplus carry-over would not bode

<sup>1</sup> den Elzen M., Meinshausen M., Hof A. (2012). The impact of surplus units from the first Kyoto period on achieving the reduction pledges of the Cancún Agreements Climatic Change. DOI: 10.1007/s10584-012-0530-5

<sup>2</sup> UNEP, November 2011, "Bridging the Emissions Gap - The Emissions Gap - an update"

well for the new global climate deal called for by the Durban Platform. This new climate regime is supposed to come into effect in 2020 and needs to be agreed on by 2015.

It is therefore essential to find and then agree on a solution that addresses the surplus at the 18th Conference of the Parties (COP) in Qatar at the end of 2012.

Solutions that would eliminate or greatly reduce the impact of the surplus include:

- not allowing any carry over, or allow a limited carry-over of AAU surplus and offset credits between the first and second commitment periods
- allowing the carry-over of surplus but severely restricting the use of the carried-over AAUs and offset credits
- excluding Parties not committing to binding targets beyond 2012 from trading AAUs.

Various proposals have been tabled at the UNFCCC climate negotiations. The proposals by the Africa Group and AOSIS in particular are promising with regard to safeguarding the environmental integrity of the Kyoto Protocol post 2012.

Key players in this debate such as the G77, the EU and Russia need to act now, to successfully resolve the surplus issue at COP 18 in December:

### G77

A joint G77 supported proposal that builds on the elements of the AOSIS and Africa Group proposal would add significant political weight and as a consequence put more pressure on Parties such as the EU and Russia to engage more constructively and urgently in this debate. We recommend that the G77 decide on a proposal by the next UNFCCC inter-sessional which takes place in Bangkok at the end of August 2012.

### The Russian Federation

The Russian Federation has not signed up to a binding target under the second commitment period of the Kyoto Protocol. Nonetheless, it expects to be able to sell its surplus. But with the vast AAU surplus it owns, it seems unlikely that other Parties would allow Russia to do so without committing to a target under the second commitment period. Russia should commit to meaningful and binding emissions cuts and also accept a significant discount on AAUs.<sup>3</sup> Such policy choices would likely lead to financial benefits for Russia because creating more scarcity in a heavily over-supplied AAU trading market would increase the value of each AAU. Whereas, the business-as-usual scenario, in which the full surplus is carried over and relatively weak targets remain for the second commitment period of the Kyoto Protocol would likely lead to a AAU price collapse after 2012, rendering surpluses almost worthless.

### The European Union

The EU has a contradictory stance on the AAU surplus: on the one hand, the European Union has been very vocal in calling for meaningful mitigation actions. The EU has also made its participation under a second Kyoto commitment period conditional on improving the environmental integrity of the Kyoto Protocol. This includes solving the surplus issue. At the UNFCCC negotiations on the other hand, the EU has remained

<sup>3</sup> Furthermore, it is paramount to ensure that those AAUs are not "laundered" in a way that a substantial amount of AAUs would be swapped into non-additional ERU credits and then weaken second commitment period ambitions indirectly



silent due to internal disagreement among EU Member States on how to address the surplus. If the EU ratified a second commitment period without addressing the surplus issue it could be considered to be passively complicit in damaging the environmental integrity of future climate regimes.

The EU needs to find an intra-European solution so it is able to take a clear position at the UNFCCC negotiations. However, debates on this issue within the EU are difficult due to the position of some Eastern European Member States, namely Poland, who prefer the default ('i.e. full carry-over') outcome. An internal solution must be found and agreed on by the next Environmental Minister's Council in October of 2012. The potential inconsistencies between the EU's domestic legislation (in particular the EU-ETS) and restrictions on the surplus carry-over could be resolved by committing to a higher reduction target for 2020.

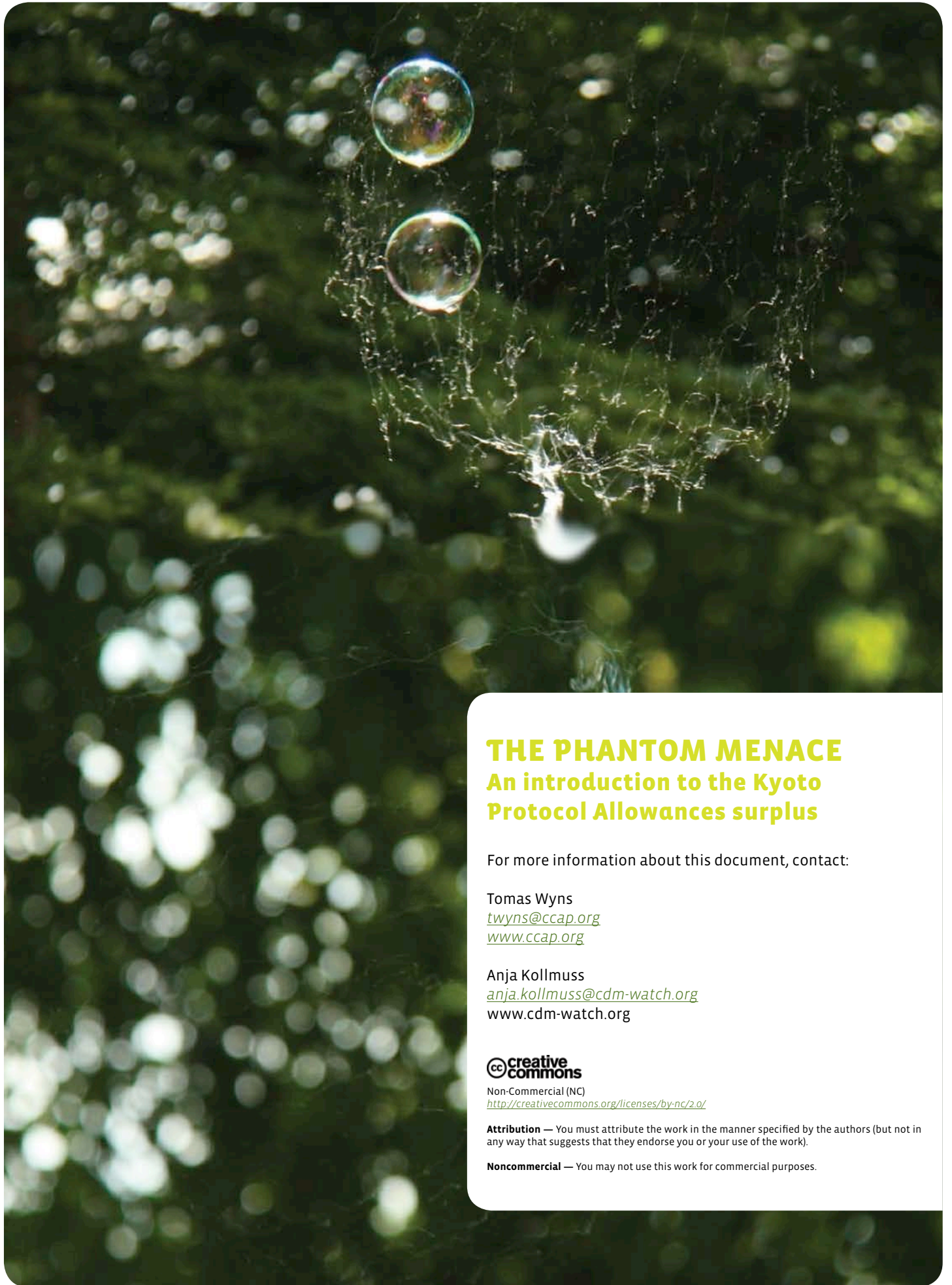
The EU has shown in Durban that it can still leverage positive outcomes at the UNFCCC negotiations by being the driving force behind the agreement for a new climate accord by 2015. If the EU wants to maintain its constructive and proactive role in the climate mitigation arena it needs to follow up with clear and strong positions on elements that could threaten the environmental integrity of a future global climate regime.

If the EU and the G77 put their diplomatic weight behind a joint position, it would greatly increase the chances of addressing the AAU surplus to strengthen the environmental integrity of a second commitment period and a new climate treaty to be agreed by 2015.



*Courtesy zwali/flickr*





## THE PHANTOM MENACE

### An introduction to the Kyoto Protocol Allowances surplus

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