

Carbon trading: key legal and tax issues

Dominique Tissot, Partner, CMS

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Legal mechanisms of the Kyoto protocol

CDM vs. JI vs. Emissions trading

- Clean Development Mechanism (CDM)
 - Art. 12 of the Protocol
 - Not regulated by the Russian legislation in force
 - Basic principles
 - allowing a country with an emission-reduction or emission-limitation commitment under the Protocol (Annex B Party) to implement an emission-reduction project in developing countries
 - allowing to earn saleable certified emission reduction (CER) credits which can be counted towards meeting Kyoto targets
- Joint Implementation (JI)
 - Art. 6 of the Protocol
 - Allowing an investor to earn Emission Reduction Units (ERUs) from an emission reduction project in a host country
 - Only legal mechanism possible in Russia so far
- Green Investment Schemes (GIS) / Emissions trading (the “carbon market”)
 - Art. 17 of the Kyoto Protocol
 - Regulatory framework under way
 - Basic principle: allowing a country having excess capacity (emission units permitted to it but not “used”) to sell it to countries that are over their Kyoto targets

JI projects (1/4)

General rules and prospects of ERUs trading in Russia

- Basic principles
 - End buyer – Russian company (investor)
 - Commodity – ERUs
- Eligibility and approval
 - Less than 2 years left (by 01/01/12) to valid a project and get tradable ERUs
 - Difficulties within the framework of an standard EPC project to obtain and trade new ERUs
 - Detailed procedure involving Sberbank and the Ministry of Economic Development (RF Government Decree No. 883 and MED Decree No. 485)
- Trading of existing ERUs
 - Tax and legal treatment depending on the qualification of ERUs in Russia

JI projects (2/4)

Legal treatment of ERUs trading in Russia

- JI projects are investment projects implemented in accordance with applicable legislation (RF Government Decree No. 883)
- Most appropriate contractual instrument – investment agreement
- Title to the results of a JI project is obtained by an investor directly
- Qualification of ERUs
 - Legal uncertainties (tradable commodity, right, quasi-license, etc.)
 - Conservative vs. aggressive approach
- Contractual framework
 - ERPA or others?
 - Russian vs. foreign law

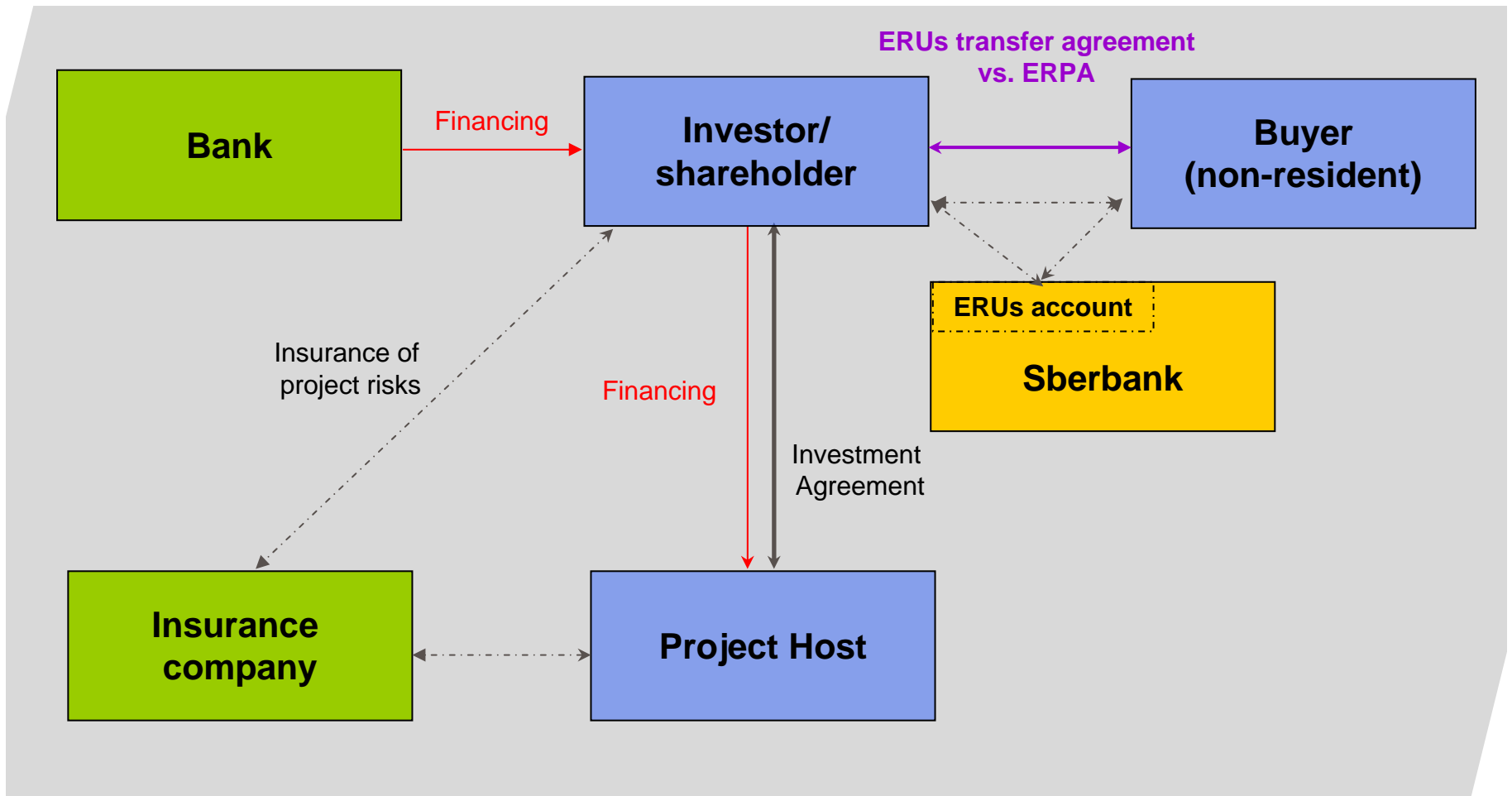
JI projects (3/4)

Tax treatment of ERUs trading in Russia

- Taxation regime depends on
 - Legal qualification of ERUs
 - Legal qualification and terms of the ERUs transfer agreement (ERPA?)
 - Localization of the investor and buyer of ERUs
- Profits tax
 - Income: payment received for ERUs (recognition in the realization period
→ not possible before registration of ERUs)
 - Expenses
 - On application for the JI project approval (recognition in the period of application)
 - On realization of the JI project (recognition depending on the qualification of expenses)
- VAT
 - Parties both in Russia: VAT applicable
 - Buyer outside of Russia: arguably no VAT notwithstanding the approach (conservative vs. aggressive)

JI projects (4/4)

Contractual structure between a project host and an investor



Thanks for your attention!

CMS, Russia
Gogolevsky Blvd. 11, 119019 Moscow

Email: Dominique.Tissot@cmslegal.ru

Tel.: +7 495 786 3088

Fax: +7 495 786 4001