Appraisal Environmental and Social Review Summary

Appraisal Stage

(ESRS Appraisal Stage)

Date Prepared/Updated: 06/30/2022 | Report No: ESRSA02270

BASIC INFORMATION

A. Basic Project Data

Country	Region	Project ID	Parent Project ID (if any)
Kazakhstan	EUROPE AND CENTRAL ASIA	P177785	
Project Name	Partnership for Market Implementation		
Practice Area (Lead)	Financing Instrument	Estimated Appraisal Date	Estimated Board Date
Environment, Natural Resources & the Blue Economy	Investment Project Financing		7/29/2022
Borrower(s)	Implementing Agency(ies)		
Ministry of Ecology, Geology and Natural Resources	Zhasyl Damu JSC under Ministry of Ecology, Geology and Natural Resources		

Proposed Development Objective

To strengthen the effectiveness of Emission Trading Scheme and support carbon pricing expansion to contribute to the updated 2030 Nationally Determined Contribution targets and 2060 carbon neutrality goals of Kazakhstan.

Financing (in USD Million)	Amount
Total Project Cost	5.00

B. Is the project being prepared in a Situation of Urgent Need of Assistance or Capacity Constraints, as per Bank IPF Policy, para. 12?

No

C. Summary Description of Proposed Project [including overview of Country, Sectoral & Institutional Contexts and Relationship to CPF]

Kazakhstan has been the economic success story of Central Asia, transitioning from lower-middle-income to upper-middle-income status in less than two decades. Kazakhstan is a mineral and fossil rich middle income country of 18.5 million people, strategically located Central Asian country with Russia to the north and China to its south-east. Kazakhstan has signed on to ambitious Nationally Determined Contribution (NDC) targets under the Paris Agreement - to reduce GHG emissions from the benchmark 1990 level by 15 percent (unconditionally) and 25 percent (conditional upon international support) by 2030. Energy production and consumption are responsible for 84 percent of

Kazakhstan's GHG emissions. Thus, achieving a low carbon path to development will require strong actions, starting with reducing its reliance on coal for power and heating. Kazakhstan has indicated its desire to continue to strengthen its capacity to pursue lower carbon growth and effective adaptation. Kazakhstan already regulates its GHG emissions through the national Emission Trading Scheme (ETS) which is enshrined in its Environment Code. The President of the Republic of Kazakhstan pledged to achieve carbon neutrality by 2060 at the 'Climate Ambition Summit' on December 12, 2020.

Carbon pricing can play a key role in supporting Kazakhstan to meet its NDC targets by 2030 and carbon neutrality goal by 2060. The PMR study highlighted the importance of introducing carbon taxes for emitters not covered by the ETS as one instrument to achieve this. From January 1, 2023 of the "Carbon Border Adjustment Mechanism" (CBAM) in the European Union and other countries will make it more difficult for manufactured goods and products produced energy-inefficiently to find export markets. In other words, it will become increasingly difficult over time, for Kazakhstan to ignore the effects of global decarbonization, and hence preparing its economy for a greener future is at the heart of remaining competitive and attaining the national goal of becoming a high ranking developed economy. Kazakhstan is actively involved in the international process of combating climate change.
The PMI program is a continuation of the PMR completed in Feb. 2021. Based on the various analytical assessments, modeling exercises, and stakeholder consultations that PMR has supported since Kazakhstan joined the PMR as a technical partner in 2014, it was concluded that the country is behind in meeting its existing NDC targets and may not be able to meet future targets unless urgent regulatory actions are taken and required investments are materialized.

This PMI project is a follow-up support to the completed PMR support to Kazakhstan on carbon pricing and will be client-executed. It will support the following components, which are subject to adjustment when the full PMI proposal is finalized based on comments received from the PMI Management Unit in the Bank and the appraisal/approval review:

Component 1: ETS Improvement (US$ 3,200,000)
Component 2: Expanding Carbon Pricing (US$ 950,000)
Component 3: Stakeholder Engagement and Just Transition (US$ 350,000)
Component 4: Project Management and M&E (US$ 500,000)

The proposed project is aligned with and directly contributes to the Country Partnership Framework FY2020-2025. Namely, project objectives are a part of the Focus Area 3 (Securing Sustainable, Resilient, and Low Carbon Growth), and Objective 7 of Preserving and Restoring Natural Capital. Explicit carbon pricing instruments, such as an ETS and carbon taxes provide an incentive for sectors to move towards decarbonization by adopting low-carbon technologies. While an ETS provides an emission certainty to industry, taxes provide a price certainty necessary for enterprises to shift practices. These price signals can therefore support Kazakhstan's energy sector transformation and green transition.

D. Environmental and Social Overview

D.1. Detailed project location(s) and salient physical characteristics relevant to the E&S assessment [geographic, environmental, social]

Kazakhstan is a mineral and fossil-rich middle-income country of 18.5 million people. It is the largest per-capita greenhouse gas (GHG) emitter in Europe and Central Asia and ranked 20th globally in 2020. More than 80% of GHG emissions in Kazakhstan are associated with the extraction, processing, transportation, storage, and combustion of fuels in all sectors of the economy from stationary and mobile sources. The annual total national emissions (without LULUCF) amounted to 385 and 355 MtCO2e in 1990 and 2019 respectively (GOK, Inventory submitted to UNFCCC in 2021). Kazakhstan has signed on to ambitious Nationally Determined Contribution (NDC) targets under the Paris Agreement - to reduce GHG emissions from the benchmark 1990 level by 15 percent (unconditionally) and 25 percent (conditional upon international support) by 2030. Kazakhstan regulates its domestic CO2 emissions through the national Emission Trading Scheme (ETS), which was introduced in 2011 and has been in operation since 2013 with several updates. However, the ETS system and relevant supporting policies need further improvement to achieve carbon neutrality by 2060, as pledged by the President at the "Climate Ambition Summit" in December 2020. This current project only supports TA type activities based on the country's strong commitment to tackling climate change and its aims include inter alia tightening the ETS caps and introducing carbon taxes, implementing carbon offset mechanisms, and allowance allocation, strengthening monitoring, reporting a, and verification (MRV) of the GHG emissions under the ETS; introducing taxes in the non-ETS GHG emitter sectors, implementation of allowance allocation. No physical works are planned under this TA project. The project activities will be mostly consulting services such as conducting assessment studies, training, developing implementation plans, and other advisory support. In component 1, upgrading IT infrastructure (electronic devices) necessary for the operation of the domestic offset program including the technical upgrades to the registry's software is expected to involve only software upgrades. The client has confirmed that any hardware (electronic equipment) replacement is not expected for the moment. The geographic scope of the project is nationwide.

D. 2. Borrower's Institutional Capacity

This project will be implemented by the Ministry of Ecology, Geology, and NatuResourcesurce (MEGNR). A Project Implementation Unit (PIU) will be set up in the office of the Operator of the carbon units trading systems ("ETS operator") under MEGNR. Component 2 and Component 3 will be also led and implemented by MEGNR and ETS Operators, but involve the Ministry of National Economy (the MNE) and Ministry of Finance (MoF) to consult the activities. Other key parties in implementation of the grant include the Ministry of Energy (MOE) and the Ministry of Industry and Infrastructure Development (MIID). A Steering Committee led by the Vice Minister of MEGNR will be established to provide oversight and guidance for the implementation of the project and ensure effective coordination and collaboration among the key parties and other stakeholders. Environmental and social impact management of all project activities will be processed and managed by the PIU under the supervision of the ETS operator and MEGNR following the Bank's environmental and social framework (ESF). However, MEGNR and ETS operator do not have any previous experience in implementing Bank-financed projects and applying Bank's ESF. Given that situation, a training program to develop and expand professional skills and capacity in ESF issues including labor, stakeholder engagement, and grievance redress for staff involved in the project will be included in the Environmental and Social Commitment Plan (ESCP) and implemented.

II. SUMMARY OF ENVIRONMENTAL AND SOCIAL (ES) RISKS AND IMPACTS

A. Environmental and Social Risk Classification (ESRC)

Moderate

Environmental Risk Rating Low

The environmental risk from the project activities is expected to be low. The project is a technical assistance program funded by a recipient executed trust fund (RETF) grant. There are no physical works or equipment replacement/rehabilitation planned under the project that could have the potential to cause potential adverse impacts and or risks on the biophysical environment, human health and safety, and/or valued environmental assets. The outputs of the project are likely to have indirect positive environmental impacts by providing technical assistance in establishing the system and enabling conditions that incentivize reducing both GHG emissions and air pollution. Only the activity that might involve physical activity would be related to upgrading IT infrastructure necessary i) for the operation of the domestic offset program including the technical upgrades to the registry's software and improvements in the current regulatory documentation and ii) for running the auctions of allowance allocation under Component 1. However, the client has confirmed that this activity will involve only software upgrades and any hardware updates (i.e., electronic device purchase or replacement) are not anticipated for the moment. Thus, no risk related to electronic waste disposal is envisaged in the current scope of the project.

Social Risk Rating Moderate

The project is not expected to involve physical works which could cause land acquisition or resettlements impacts, labor influx risks, community health and safety risks, or impacts on cultural heritage. The Project is mainly focused on promoting policies on decarbonization measures targeted at increasing modernization and competitiveness of industry, growth of GDP, and fostering investments in green technologies. However, the downstream impacts arising from the implementation of the policies cannot be overlooked, which could have adverse impacts on poor and venerable households as a result of higher energy prices. Furthermore, the likelihood of job losses and related loss of income which could result from a focus on modernization in investment in green technology will require appropriate measures to be in place to minimize such impacts. A strong focus on skill diversification, retraining, and growth of new and greener industries should be a part of the overall package of measures that the government considers minimizing impacts on individuals as a result of sectoral reform. The project will also hire consultants to further strengthen the PIU for the implementation of the project. To ensure a deeper understanding of the long-term social impacts and to inform initiatives to address the effects on vulnerable and poor households and communities, a details social impact assessment will be undertaken during the project implementation. The project will also require stakeholder engagement and information disclosure, which will require the establishment of a robust GM system for project beneficiaries and direct or indirect stakeholders. The overall social risk rating of the project is moderate.

B. Environment and Social Standards (ESSs) that Apply to the Activities Being Considered

B.1. General Assessment

ESS1 Assessment and Management of Environmental and Social Risks and Impacts

Overview of the relevance of the Standard for the Project:

The project supports analysis, technical studies, training, and information technology infrastructure to improve ETS of the Republic of Kazakhstan, including reporting forms on greenhouse gas emissions, development of a methodology for calculating benchmarks, developing benchmarks for certain types of products, enhancing the draft Rules for trading carbon units, the development of proposals for amendments and additions to the national exchange

legislation for the possibility of holding primary auctions in the most suitable format, and assessing the feasibility of integrating carbon pricing with air pollution taxes.
The project has no physical dimensions and does not include actions with any material manifestations that could cause negative environmental impact. However, the outputs of the project are likely to have indirect positive environmental impacts by providing technical assistance in establishing the system and enabling conditions that incentivize reducing both GHG emissions and air pollution. There are, though, potential social impacts and risks mainly pertaining to SEA/SH as a result of the project capacity building and training initiatives. Furthermore, the downstream impacts of the project which could derive from the policies which will be informed by the project could result in higher energy prices which will have an impact on poor and vulnerable households.
As the project is a TA with no physical work, the project will not prepare free-standing environmental instruments. However, to further assess the potential social impacts of the large-scale transition to a low carbon economy and sectoral reforms, the project will undertake a detailed social impact assessment to better understand these impacts. Considering there are no significant social impacts anticipated under the project such as land acquisition, labor influx, or impacts on cultural heritage. However, the project should promote transparency through extensive stakeholder participation and public information disclosure. This can be achieved through inclusive planning which will provide a platform to promote broader stakeholder engagement and participation through strategic planning initiatives such as focus groups, engagement of academia, private sector, relevant government entities, and expert panels discussions on project activities during implementation as part of the project environmental and social commitment plan (ESCP). The commitment detailed in the ESCP has been agreed upon with the client.

ESS10 Stakeholder Engagement and Information Disclosure

The project has developed a Stakeholder engagement plan (SEP) which includes a Grievance Mechanism (GM) and communication strategy with the relevant stakeholders such Ministry of Ecology, Geology and Natural Resources, Ministry of Finance, Ministry of National Economy, Ministry of Energy, Ministry of Industry and Infrastructure Development, academia, large GHG emitters, and other key stakeholders/industries related to the ETS and carbon taxes. The SEP will be consulted upon, cleared, and disclosed by end of July 2022. The SEP will also address the timing and methodology for meaningful and participatory consultation, including arrangements for information disclosure to all stakeholders. The SEP is considered a living document that will be updated throughout the project life cycle. The project will also include measures to strengthen social accountability and citizen engagement. This will include: (i) effective consultations, (ii) establishing a functional grievance mechanism (GM), and most importantly a social impact assessment during the project implementation. Furthermore, the client Ministry will need to agree on institutional arrangements for complaint resolution and the required physical infrastructure for complaint management and registration to ensure there is sufficient capacity and resources in place to ensure the proposed GRM system will be able to respond to project-related complaints in a timely manner.

B.2. Specific Risks and Impacts

A brief description of the potential environmental and social risks and impacts relevant to the Project.

ESS2 Labor and Working Conditions

This standard is relevant as the project's TA activities will be delivered by the PIU, and possibly individual consultant experts to be engaged under the project. The TA beneficiaries are likely to be government civil servants, government agencies and large Greenhouse Gas (GHG) emitters, and other key stakeholders/industries related to the Emission Trading Scheme (ETS), and other agencies. There may be labor-related risks, such as SEA and SH risks. But the risk level is considered low among its teams given the TA nature and types of activities to be supported under the project. The project teams will remain subject to the terms and conditions of their existing public sector employment agreements and arrangements. The requirements of a labor-management procedure have been reflected in the ESCP.

ESS3 Resource Efficiency and Pollution Prevention and Management

This standard is not relevant. Use of natural resources, generation of emissions and waste, and significant GHG production are not anticipated.

ESS4 Community Health and Safety

This standard is not relevant. No community health and safety issues are expected through project activities; nor will activities affect ecosystem services.

ESS5 Land Acquisition, Restrictions on Land Use and Involuntary Resettlement

This standard is not relevant, because the project doesn't involve any physical work which may cause land acquisition or involuntary resettlement.

ESS6 Biodiversity Conservation and Sustainable Management of Living Natural Resources

This standard is not relevant. The project will not impact biodiversity or living natural resources.

ESS7 Indigenous Peoples/Sub-Saharan African Historically Underserved Traditional Local Communities

This standard is not relevant as there are no Indigenous Peoples in the project area.

ESS8 Cultural Heritage

This standard is not relevant. The project will not impact tangible or intangible cultural resources.

ESS9 Financial Intermediaries

This standard is not relevant. The project will not include any financial intermediaries.

B.3 Other Relevant Project Risks

None

C. Legal Operational Policies that Apply

OP 7.50 Projects on International Waterways	No
OP 7.60 Projects in Disputed Areas	No

B.3. Reliance on Borrower's policy, legal and institutional framework, relevant to the Project risks and impacts

Is this project being prepared for use of Borrower Framework? No

Areas where "Use of Borrower Framework" is being considered:

The Borrower's Framework is/ will not be considered.

IV. CONTACT POINTS

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Borrower/Client/Recipient

Borrower: Ministry of Ecology, Geology and Natural Resources

Implementing Agency(ies)

Implementing Agency: Zhasyl Damu JSC under Ministry of Ecology, Geology and Natural Resources

V. FOR MORE INFORMATION CONTACT

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VI. APPROVAL

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