

Malaysia's Future Carbon Trading Laws and Legislation - Lessons from Sarawak (Part 1/2)

In April 2024, it was announced that the Federal Government had agreed to enact National legislation related to carbon regulation and trading ("**Federal Carbon Legislation**"), and that such Federal Carbon Legislation would be based upon existing carbon trading laws in the State of Sarawak.

Sarawak is the only State in Malaysia that presently has a standalone carbon trading legislation, namely the Environment (Reduction Of Greenhouse Gases Emission) Ordinance, 2023 ("**Sarawak Carbon Legislation**"), which came into force on 1st March 2024.

Whilst the actual formulation and operation of the future Federal Carbon Legislation will only be known upon release of the Draft Federal Bill, the fact that the Federal Government has indicated an intention to incorporate provisions of the Sarawak Carbon Legislation into a Federal Carbon Legislation shows that the Sarawak Carbon Legislation may act as a good reference point as to what may come at a National

level. The Sarawak Carbon Legislation will be considered below accordingly.

The Sarawak Carbon Legislation broadly has 2 categories of provisions, i.e.:

(i) **Scheduled Economic Sectors**

specific provisions related to high carbon emission sectors identified in Schedule 1 to the Sarawak Carbon Legislation ("**Scheduled Economic Sectors**") to reduce their carbon emissions. This is done via the imposition of carbon emission thresholds and reporting obligations, whereby there will be specific restrictions on the amount of carbon that may be emitted and any emissions above such amount will be penalised accordingly; and

(ii) **All Economic Sectors**

general provisions which apply to all economic sectors ("**All Economic Sectors**") which wish to engage in activities to reduce, mitigate, capture, store or abate carbon and in the process, generate carbon credits. This is done via the imposition of rules, restrictions and requirements for which carbon credits may be generated and sold from

activities that seek to reduce, mitigate, capture, store or abate carbon.

This Article is the first of 2 parts. This **Part 1** will explore the regulatory framework with regard to Scheduled Economic Sectors and emission thresholds and **Part 2** will explore the regulatory framework with regard to All Economic Sectors and carbon trading.

Note: In the Sarawakian context, various functions and responsibilities are undertaken by the State Administration including the Controller of Environmental Quality (“Controller**”), the State Natural Resources and Environment Board (“**Board**”) and the State Government Executive Council (Majlis Mesyuarat Kerajaan Negeri) (“**State Exco**”). It remains to be seen who will undertake these relevant functions in the Federal Carbon Legislation context.*

(1) Scheduled Economic Sectors

At the date of writing, the Scheduled Economic Sectors under Schedule 1 to the Sarawak Carbon Legislation are the:

- (i) **Oil & Gas Sector** (exploration, production and processing of

petroleum or gas whether onshore or offshore Sarawak and all activities related to carbon capture and storage); and

- (ii) **Energy Sector** (generation, production and transmission of electricity)

Under the same Schedule 1, the State Exco retains the discretion to schedule any other sectors as Scheduled Economic Sectors by publication in the *Gazette*. This is relevant as it gives the State Exco the wide discretion to add new sectors into the Schedule, as time progresses.

(2) Carbon Emission Threshold

The State Exco by notification published in the *Gazette* will determine a threshold for the amount of carbon that an entity in a Scheduled Economic Sector may legally emit / release into the atmosphere (“**Carbon Emission Threshold**”).

(3) Registration for Scheduled Economic Sectors

Statutory Requirement:

Any person or business undertaking activities in a Scheduled Economic Sector is required to register with the Controller within 90 days of the coming into force of the Sarawak Carbon Legislation.

Non-Compliance Penalty:

Fine up to RM 50,000 | Imprisonment up to 1 year

(4) Reporting Obligations for Scheduled Economic Sectors

Statutory Requirement:

Economic activities on land, water and forest areas under the Scheduled Economic Activities must submit a report to the Controller on the carbon equivalent of emissions resulting from the economic activities undertaken, in a “**Carbon Emission Report**”.

The Carbon Emission Report must comply with:

(i) the standards in the

Greenhouse Gas Protocol published by the World Business Council for Sustainable Development and World Resources Institute; or

(ii) any other standards approved by the Controller; and

(iii) the scope of reporting of greenhouse gas emission levels is to be determined by Board.

The Carbon Emission Report must contain:

(i) greenhouse gas emission levels of the entity based upon the scope determined by the Board, as at the date of the Report;

(ii) how the entity is applying and adapting low carbon solutions to reduce emission levels to the Carbon Emission Threshold;

(iii) if greenhouse gases have been captured and stored, the volume captured and stored; and

(iv) other information, data or document which the

Controller deems necessary.

Non-Compliance Penalty:

Fine up to RM 50,000 | Imprisonment up to 1 year

(5) Annual Reporting Obligations for Scheduled Economic Sectors

Statutory Requirement:

Subsequent to the first Carbon Emission Report above, subsequent Carbon Emission Reports must be submitted to the Controller for each subsequent calendar year ending 31st of December.

These annual Carbon Emission Reports must be submitted to the Controller on or before the 28th of February of each year.

Non-Compliance Penalty:

Fine up to RM 50,000 | Imprisonment up to 1 year

(6) Effect of Carbon Emission Report on Scheduled Economic Sectors

If a business' Carbon Emission Report shows that that business' emissions exceed the Carbon

Emission Threshold set by the State Exco, the Controller may:

- (i) direct the business to submit a carbon reduction and abatement plan, approved by an accredited external auditor, to reduce emissions to the Carbon Emission Threshold within a specified time; and
- (ii) in the event such plan as approved by the State Exco when implemented, fails to reduce emissions to the Carbon Emission Threshold, the business will be legally required to capture and store greenhouse gases as per the Sarawak Carbon Legislation or any other written law relating to capture and storage of greenhouse gases in Sarawak.

If the business cannot or will not meet the Carbon Emission Threshold, it will be liable to pay a carbon levy.

(7) Carbon Levy

If a business's carbon emissions exceed the Carbon Emission Threshold set by the State Exco and the business fails or

refuses to reduce emissions, a penalty in the nature of a carbon levy will be imposed upon that business.

The levy amount is calculated using the formula $A \times B$, where:

- **A** is the total carbon dioxide equivalent of greenhouse gas emissions (in metric tonnes) recorded in the Carbon Emission Report.
- **B** is the carbon levy rate set by the State Exco by notification in Gazette.

The carbon levy becomes a liability at the end of the reporting period and must be paid by the business in accordance with the Sarawak Carbon Legislation. However, if the business has an approved carbon reduction plan from the Controller, it will not incur the levy during the plan's implementation period (provided the conditions of the carbon reduction plan are complied with).

(8) Assessment of Carbon Levy

Upon receiving the Carbon Emission Report, the Controller shall, within 30 days:

- (i) Determine the amount of carbon levy the business must pay, and
- (ii) Calculate the number of Carbon Credit Units the business needs to surrender to cover the levy or part of it. (Carbon Credit Units shall be covered in **Part 2** of this Article).

Following this assessment, the Controller will issue a notice of assessment ("**Assessment**") to the registered business entity.

(9) Appeal on Carbon Levy

A person dissatisfied with an Assessment made by the Controller can appeal to a Tribunal constituted to hear appeals of such nature, within 21 days of receiving the Assessment.

Regardless of the appeal, the carbon levy must be paid by the due date. If the Assessment is later cancelled, changed, or reduced, the adjusted amount or any overpaid levy will be refunded to the appellant.

(10) Payment of Carbon Levy

Payment on the Assessment must be made within 30 days and can be paid for by retiring Carbon Credit Units held by the business or such other manner determined by the Controller (in the event there are insufficient Carbon Credit Units held by the business to pay the assessment accordingly).

If the entity fails to pay the carbon levy within the specified period:

- (i) A financial penalty of 8% of the unpaid levy, or another amount set by the State Exco, will be imposed;
- (ii) The Controller will issue a written demand for payment of the levy and penalty, which must be settled within 30 days; and
- (iii) If payment is not made within this period, the unpaid levy and penalty may be recovered as a civil debt by the State Government, which may pursue legal action to collect the amounts owed, including costs on an indemnity basis.

Conclusion

The foregoing make clear that strict regulations exist in the State of Sarawak to regulate and control the carbon emissions of high emission sectors. How these measures may translate into a Federal Carbon Legislation remain to be seen but these provisions (with modification) may lend an insight as to what's to come for Malaysia in the future. The legal framework on carbon trading in Sarawak and how that may translate at a national level, will be covered in Part 2 of this article.

This article was written by ASL's strategic alliance partner, Abhilaash Subramaniam from Abhilaash Subramaniam & Co. It contains general information only. It does not constitute legal advice or an expression of legal opinion and should not be relied upon as such.