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Blueprint of “CCS Business Act” by Japanese Government

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One of the Japanese media has recently reported that the bill named as “CCS Business Act” is expected to be submitted to the regular Diet’s session of Japan next year 2024. As you may know, the Japanese government has discussing commercialization of carbon capture and storage (“CCS”) projects over these several years with a view to achievement of the goal of ‘carbon neutral’. In this newsletter, we provide some of our thoughts regarding the concept of the “CCS Business Act” based on the already published government documents and announcements available so far.

1. Introduction

As you are aware, CCS is a technology whereby the CO₂ emitted is to be separated and captured, and then be stored in a certain reservoir underground or under the seabed. The current Sixth Strategic Energy Plan formulated by the Japanese government in 2021 sets out CCS as a new technology which is a key function in the context of materializing the goal of the “carbon neutrality”

by the year of 2050. As per this direction, a long-term roadmap for materializing the CCS projects has been formulated by the Ministry of Economy, Trade and Industry (“**METI**”), and then it will consider improving the business environment for the commercialization of CCS.

As part of such movement, the Japanese government organized a study group inside METI in January 2022 to discuss the feasibility of the CCS projects and any other matters related thereto. The final report prepared by such study group of METI was made public on March 10, 2023. As an attachment to such final report, a blueprint document titled “Discussion on the Concept of ‘CCS Business Act’ (**title as tentative**)” (hereinafter, the “**Blueprint Document**”).

We hereby note some of our thoughts about the concept of the “CCS Business Act”.

2. Concept of the “CCS Business Act” in the Blueprint Document

2.1. Concept of “CO₂ Storage Right” – Differences with Mining Rights under the Mining Act

In the first place, the Blueprint Document assumes the new concept named as a “CO₂ Storage Right” as one of the fundamental concepts under the “CCS Business Act”. The “CO₂ Storage Right” will be defined as the right to conduct a storage business of CO₂ as a part of CCS project. The Blueprint Document indicates that this “CO₂ Storage Right” should be subject to a legal system which is similar to that of the existing mining rights under the Mining Act. In our view, this approach looks reasonable when looking at the precedents in the foreign countries where the CCS projects are active or developed, such as EU.

On the other hand, the Blueprint Document states that: *“the “CO₂ Storage Right” under discussion will be granted based on the relevant national policy, and it should be subject to various regulatory provisions and the relevant public obligations. In this sense, a “CO₂ Storage Right” will not be a pure private right, but instead it should be treated as kind of a public right.”* Looking at this statement in the Blueprint Document, it seems that the concept of the “CO₂ Storage Right” will have to be considered from the viewpoints different than the mining rights under the Mining Act, although the basic structure of the “CO₂ Storage Right” will be similar to that of the existing system of the Mining Act. In our view, specifically the following matters (however, not limited to the below) should be discussed in the course of legislation of the “CCS Business Act”:

- (a) The current Mining Act requires the holder of a mining right be a Japanese national or a Japanese corporation. When it comes to the “CO₂ Storage Right” under discussion, we believe that it is necessary to consider if this kind of “nationality” requirement which may be applicable to the “CO₂ Storage Right” would be appropriate, specifically from the perspective of the “public” nature of CCS business as indicated in the Blueprint Document.

- (b) The duration period of a “CO₂ Storage Right” should also be carefully discussed. The duration period of a prospecting right for oil and natural gas under the current Mining Act is four (4) years plus another four (4) years (if extended twice); being eight (8) years at maximum. The prospecting right (“*Shi-kutsu-ken*”) for CO₂ storage business may have the same time limitation of eight (8) years, as indicated in the Blueprint Document. On the other hand, the duration period of the “Storage Right” which is to be the absolute right to “store” CO₂ after prospecting will need another consideration. There is no limited duration period of a digging right (“*Sai-kutsu-ken*”) under the Mining Act, in that a digging right (“*Sai-kutsu-ken*”) is an absolute right to mine the resources after prospecting under the Mining Act. However, CCS project does not assume the extraction of minerals unlike the mining rights under the Mining Act, and accordingly, it is arguable if the indefinite duration period should be appropriate for the “Storage Right” under discussion. Also, the Blueprint Document discusses whether the responsibility for a long-term security and monitoring will be transferred to the government after the storage of CO₂ as per the “Storage Right”. It should be carefully discussed whether or not the duration of the “Storage Right” after prospecting should be indefinite.
- (c) In respect of the criteria for grant/approval of the “CO₂ Storage Right”, the Blueprint Document indicates that the applicant for the “CO₂ Storage Right” must demonstrate that it has sufficient financial and technical expertise to undertake reasonable development of CCS. In this regard, again the “public” nature of the “CO₂ Storage Right” will have to be taken into account. Specifically, it would be arguable if the relevant documents such as the financial statements of the applicant should be required for the purpose of demonstrating the financial capacity of the applicant for a “CO₂ Storage Right” in consideration of such “public” nature of CCS project.
- (d) Regarding the implementation phase of a “CO₂ Storage Right” upon the grant of the same, it seems that consideration will be needed on what aspects of the CCS project are different from those of mining rights (i.e., prospecting right and digging right). For example, under the current Mining Act, a mining right holder must commence the mining activity within six (6) months after the grant of the right. When it comes to a “CO₂ Storage Right” now under discussion, it would be necessary to set out the appropriate deadline for commencement of the prospecting work or storage work under the “CO₂ Storage Right”, especially by taking into account the public nature of the CCS project.
- (e) In respect of the responsibility for mine pollution, Article 109 of the current Mining Act provides a strict liability to be imposed on a mining operator if and when any mine pollution occurs. However, it is arguable whether this theory of a strict liability for mine pollution should also be applicable to a “CO₂ Storage Right,” although the Blueprint Document indicates that the principle of strict liability of an operator should be adopted for CCS project. It is notable that the Blueprint Document also directs the concentration of responsibility onto the CCS operator in respect of the risk around the CCS project. In consideration of the “public” nature the CCS business as mentioned above, we see that further discussion would be needed in

respect of the share of responsibilities among the stakeholders who participate in CCS projects.

As such, basically we see it reasonable that CCS projects, and the designing of a “CO₂ Storage Right” for that purpose, will be similar to the current mining right system under the Mining Act. Nonetheless, we believe that it will also be necessary to make appropriate arrangements by taking account the above-mentioned “public” nature of CCS projects. As a separate note, a proper business model of CCS projects including governmental subsidies will have to be further discussed.

Additionally, the Blueprint Document assumes that exploration activity to locate a suitable site for CCS projects must be subject to approval by METI. Under the current Mining Act, only the method of exploration by artificial earthquake requires the approval by METI if conducted in a terrestrial area. No other exploration activities, such as magnetic surveys on site, require approval by METI. At the time when the Mining Act was amended in 2012 whereby such permission system for exploration by artificial earthquake method was introduced, the government’s official announcement stated that *“Exploration for mineral resources is essential for mining, however it requires occupying a certain area for a certain period of time. Therefore, there is a risk that it will hinder the uses of the occupied area by others, or it will harm the interests of other industries. For this reason, when a person conducts a large-scale exploration that involves a certain level of occupancy of the area, it must be carefully considered if there is any impact on activities of other industries in the same area, and also, the government should consider whether the exploration activity will or will not hinder the proper management of the mineral resources.”* We believe that further discussion would be necessary to see if the same concern applies to the exploration of suitable sites for the purpose of the CCS business.

2.2. Project Finance for CCS projects – “CO₂ Storage Right” as Real Property, and Creation of “CCS business foundation”

In the Blueprint Document, it is discussed that a “CO₂ Storage Right” shall be deemed as a “real property”. If this idea is adopted, the CCS operators will be entitled to eliminate any third party who interferes with the operation of the CCS business. Moreover, the operators of a CCS business will be able to transfer or otherwise dispose of the “CO₂ Storage Right”, which means that, in particular, it would enable the CCS operators to create a mortgage over the “CO₂ Storage Right” as a real property. We see that this method to materialize the potential value of the project as “real property” is similar to the concession rights in PFI projects which was introduced in the 2011 as per the amendment to the PFI Act of Japan. As such, we think that of the past discussion regarding PFI projects would be informative for the purpose of considering how to secure a project finance for CCS projects (if bankable).

In addition to the deemed “real property” idea as for the “CO₂ Storage Right”, the Blueprint Document discusses an idea of creating a so-called “CCS business foundation” system, whereby the land and structures, and also the equipment and other ancillary assets all together, in addition

to the “CO₂ Storage Right”, will constitute a single “foundation” as a possible subject of mortgages. Although this idea is promising from the viewpoint of project finance for CCS project, probably it may be difficult to treat assets that are frequently replaced during the operation of the CCS business. It seems necessary to continue the discussion on what type of system should be structured in this regard.

2.3. Other Considerations

In addition to the storage business of CO₂, CCS-related business also includes the separation and capture of CO₂, and transportation of CO₂. Regarding these businesses (other than storage of CO₂), the regulatory framework is discussed by the government, which will be more clear once the bill for the “CCS Business Act” is formulated.

Also, the Blueprint Document suggests that it be appropriate to treat CO₂ as valuable instead of a waste. As such, some consideration is to be given to the owners of CO₂ itself. It is our understanding that this discussion in the Blueprint Document is based on the prospect that CO₂ will be somehow a manageable object as a result of storage thereof underground. Additionally, in the context of sale of CO₂ being captured, it is being discussed what kind of measurements would be suitable to regulate the sale of CO₂ so captured. The commercial feasibility of CCS projects depends on whether any appropriate business models can be formulated. Accordingly, the most efficient way should be discussed how to monetize the project by use of stored CO₂ as valuable, as well as CCS operators’ obtaining some carbon credits as one possible solution, in respect of operation of the CCS projects.

3. Final Remarks

In this newsletter, we have provided our preliminary view over the concept of the said “CCS Business Act,” and made certain considerations. However, it looks that there are still a lot of matters that need to be further considered in order to formulate the bill of the “CCS Business Act”, and we will continue to watch out for the direction of the discussion by the government.

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- This newsletter is published as a general service to clients and friends and does not constitute legal advice. Should you wish to receive further information or advice, please contact the authors as follows:

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