

Members of the CDM Executive Board
UNFCCC Secretariat
Martin-Luther-King-Strasse 8
D 53153 Bonn
Germany

To cdm-info@unfccc.int
From rachel.child@pd-forum.net
Date 21 May 2014
Page 1/6
Subject **Call for input on "Issues included in the annotated agenda of the seventy ninth meeting of the CDM Executive Board and its annexes"**

Project Developer Forum Ltd.
100 New Bridge Street
UK London EC4V 6JA

Europe: +44 20 7121 6100
Asia: +65 6578 9286
office@pd-forum.net
www.pd-forum.net

CHAIRPERSON:
Gareth Phillips
gareth.phillips@pd-forum.net

CO VICE CHAIRPERSONS:
Sven Kolmetz
sven.kolmetz@pd-forum.net
Rachel Child
Rachel.child@pd-forum.net

Honorable Members of the CDM Executive Board,

The Project Developer Forum (PD Forum) welcomes the publication of the annotated agenda for EB79 and would like to provide the following input on the agenda and other issues.

Annex 5 - Concept note: Role and structure of the panels and working groups under the CDM Executive Board

The PD Forum welcomes the discussion on possible alternative structures for panels and working groups, particularly in light of continued poor market conditions and subsequent reduced workload for the EB support structure. We suggest that the most appropriate structure in light of these market conditions is a core panel of CDM and methodological experts, drawing on technical expertise as and when necessary. This structure, we believe, will help to ensure consistency across methodologies, as well as being a cost-effective means of ensuring appropriate expertise is available as and when necessary. In addition to this, the PD Forum supports the use of electronic means where possible to discuss issues and make decisions in a cost-effective, efficient and environmentally responsible way.

Annex 13 - Draft Package of documents on application of E- policy in investment analysis for additionality demonstration and selection of baseline scenario

The PD Forum welcomes the EB's attention dedicated to this important topic and recognizes the conceptual progress which has been made by defining and analysing different options as presented by Annex 13.

Before entering a detailed discussion, the PD Forum would like to reiterate the importance of this topic to recognize and foster ambition of all parties and to develop concepts that allow the interaction of national and international policies as a key element of the future climate regime. In the current bottom-up process, the CDM stands out as the only tool which can offer solid MRV principles and procedures and thus is important for the development of globally comparable and consistent carbon pricing mechanisms. Moreover we understand that the concepts of CMP 5, "*Further guidance relating to the clean development mechanism*", paragraph 10 and 11, continue to be a central guidance as they allow us to extract the fundamental principles for the definition of any rule on the treatment of national policies under the CDM:

- *Respect sovereign prerogative to decide on the design and implementation of most effective, locally adapted and economically sustainable policies*
- *Avoid that countries are discouraged to adopt or continue efforts and policies that promote the achievement of the ultimate objective of the Convention and thus avoid that early mover countries are penalized*
- *Avoid distortions which favor / penalize certain policy types or technologies.*

With these important considerations in mind we would like to comment first on the content of the "Cover Note" and subsequently on Appendix 1

Comments on the Cover Note:

As expressed in our comments on the annotated agenda of EB 75, the PD Forum commends the EB decision that any rule and procedure for the treatment of E- policies will be of voluntary nature, and that the decision that the treatment of E- policies shall be consistent for additionality and baseline as any other approach would question a fundamental concept of the CDM.

In relation to the options which are being discussed and the impact analysis which has been conducted as described in the cover note, we would like to provide some comments and recommendations:

1) **Avoiding distortive effects on policies and technologies:**

It is important that the revised rules are able to treat different kinds of E- policies and technologies in an adequate manner and without creating any distortions between countries, policy options and technologies. This fundamental objective is readily addressed by Options B (2B and 4B), as they adhere to the financial principle that the investment decision is based on the evaluation of the complete assessment period. Only if this economic principle is observed can all policy and technology specific features be summarized in one valid and unequivocal financial indicator as is the NPV or the IRR. In line with this economic fundamental principle, the results presented by paragraph 21 (c), show that:

"Option B always results in a lower NPV compared to Options 2A and 4A."

As well as (f), this concludes that:

"For short-term subsidies, the NPV results are very likely to be the same for all options (2A, 4A and B). If the project activities start during the defined seven-year "E- policy benefit period", the subsidies would likely occur during the period rather than before or after the period; therefore the impacts from all options would be the same."

Therefore the analysis clearly shows that Option 2A and 2B penalize long term subsidies and therefore represent distortive rules. This is of special concern as long term incentives are more sustainable for the host countries, especially those with financial constraints.

In addition to that finding we would like to add some aspects to illustrate that there is also a risk of technology distortion which was not captured by the analysis:

Some projects and technologies, especially capital intensive infrastructure investments, imply long construction times of up to 5 or more years and if incentives are related to the cash flow (such as tax exemption or feed in tariffs), then option 2A and 2B penalize these projects in a way that was not captured by the results presented, shortening their benefit period to two years or less. This is of special concern as these capital intensive long term investments are most important to support transformational clean economic growth of developing countries and to avoid further fossil fuel lock-in.

Based on this discussion we conclude that Options B are preferable to Options A as:

- a) Any distortive effect between "*short-term or one time subsidies*" or on "*long-term subsidies*" is avoided and the "*prerogative of the host country to decide on the design and implementation of policies to promote or give competitive advantage to low greenhouse gas emitting fuels or technologies*" as defined by Decision 2/CMP 5, paragraph 10 is respected. This is important as a policy which would favour "*short-term or one time subsidies*" over "*long-term subsidies*" would penalize poor countries which need to attract investors with long term incentives to protect their governmental budgets.
- b) Options B avoid that projects with low investment requirement and rapid payback period are favoured over investments which are capital intensive and require a long period of investment amortisation. Conversely Option A would mean that Host Countries are left alone with important

but difficult capital intensive projects while low hanging fruits with quick payback would have an increased advantage under the CDM.

- c) In addition to the arguments above, we understand that Options B are a straightforward way to avoid any perverse incentive for countries to abandon or change, substitute or adapt their policies and thus is an adequate solution to satisfy the provision of Decision 2/CMP5, paragraph 11.

- 2) The importance not to penalize early mover projects and countries:

As expressed before, it is most important that early mover projects and countries are not penalized and thus we welcome that all options (2A; 2B; 4A; 4B) consider that the "seven-year benefit period" for countries that have enacted or implemented E- policies before 1 January 2014 would start as of this date.

Unfortunately the scenarios that have been presented in paragraph 20, as well as the result mentioned in paragraph 21 (e) cast some doubt on the interpretation of this concept. We would understand that scenario (a) and (b) are equivalent as both projects are early mover projects, but the fact that these two scenarios have been defined indicates that a different treatment is being applied and possibly that the benefit period would not be considered for the first years of the investment analysis, i.e. the years before January 2014. To avoid any confusion, we would suggest amending the respective paragraphs as follows:

*The seven year benefit period starts [on the policy implementation date][when the policy enters into force in the host Party]or on 1 January 2014, whichever is later. **If policies have been implemented before 1 January 2014, the benefit period shall be extended back to the original [policy implementation date][date the policy entered into force in the host Party] in order to recognize and reward early action of host countries.***

With this clarification, the benefit period for early mover projects would effectively be extended by the time span of anticipation in relation to 1 January 2014.

- 3) Trade-offs between the project submission vs the Project Start Date for definition of eligibility
The Project Start Date is a clearly defined concept and is validated for each project and therefore offers concise and reliable criteria to define if a project is eligible. If, as currently suggested in all options, the date of "project submission" is used to define the eligibility to the rule this is not in line with economic rationale and it will lead to some gaming by PPs which will seek to submit projects in accordance with their needs, as described in the second half of paragraph 21 (b). Moreover it will lead to an undesirable rush at the end of 2020 when the benefit period for all early mover projects will expire.

In addition we would like to highlight a possible problem with the definition of scenarios (d) and (e) as their Project Start Date is before the policy implementation date, which would mean that the E- incentive was not available at the time of investment decision. Considering the fundamental concept that additionality is to be assessed according to the circumstances and views as applicable at the Project Starting Date these are questionable scenarios, unless a PP would demonstrate that he anticipated the implementation of the regulation, but this would not represent a valid element of a standardized discussion.

- 4) The importance of setting an unequivocal start date of the benefit period.

We further appreciate that the detrimental aspects of options 2 which consider the start date of the benefit period to be the date when a policy enters into force, versus option 4, which considers the start date to be the one when a policy is fully implemented have been captured by the discussion.

As recognized by the EB there is sometimes long delay between the date that a policy enters into force and the date it is fully regulated, operational and effective ("the policy implementation date") and therefore we urge the EB to favour Option 4. In addition, and to avoid the difficulty of defining and

validating the date when effective policy implementation was reached we suggest amending the definition of "implementation" with the underlined section as follows:

*"Implementation": means that for the E- policy all necessary implementing regulations have entered into force in the host Party and the E- policy is available to project participants, **as demonstrated by the Project Start Date of the first registered CDM project which had benefited by the policy.***

By adding this clear criterion for qualification and validation we understand that a solid, meaningful and verifiable criterion is established. In fact the effectiveness of a policy scheme is best demonstrated and clearly recognized by possible investors on the basis of an effective investment decision (Project Start Date). Moreover all data about such projects are available to the UNFCCC and thus to the validating DOE.

In conclusion we believe that Option 4B, amended as follows would represent an adequate definition which avoids distortions, penalizing of early movers and which will promote further action and ambition of host parties:

*The seven-year benefit period starts on the policy implementation date or 1 January 2014, whichever is later. **If policies have been implemented before 1 January 2014, the benefit period shall be extended back to the original policy implementation date in order to recognize and reward early action of host countries.***

*For each project **with a Project Start Date** submitted for registration during the defined seven-year benefit period, all the comparative advantages received by the project can be disregarded for the entire assessment period of the investment analysis (say, 21 years).*

Comments on Appendix 1:

In fact it seems that the results of the discussion as presented in the Cover Note has not yet been transferred to the Draft guideline on "Application of E- policy in investment analysis for additionality demonstration and selection of baseline scenario" and therefore we just urge the EB and the secretariat to make sure that the document is developed with care and diligence to make sure that undue distortions or perverse incentives for project developers and host countries are avoided.

Conclusions:

With the Option 4B as discussed above, we believe that the EB has the opportunity to solve this important discussion with efficient and straightforward guidance for the treatment of additionality and the setting of baselines. This guidance will help to foster ambition and investment for GHG mitigation in the critical seven years until the end of 2020, after which the parties have agreed to implement a new legally binding framework. In effect, the period between now and 2020 is critical for two complementary reasons: As highlighted by the International Energy Agency (World Energy Outlook, 2011) early GHG mitigation is crucial to minimize future cost for all parties and to avoid that the door to limit climate change to a maximum of 2 degrees is closed by locking in future GHG emissions by continued expansion of fossil fuelled energy infrastructure in developing countries. Any early action and national mitigation policy by developing countries therefore has to be recognized, supported and enhanced.

In addition to this, the coming years will be important to further construct and develop the conceptual elements and building blocks of the future climate regime, with the overall objective to promote the establishment of a globally comparable and consistent carbon pricing mechanisms. With this objective in mind we understand that the synergy between the CDM and national support and climate policies is an important fundament due to the following arguments and evolutions:

1. Developing countries such as Mexico, China, South Korea have established or are discussing (South Africa, Chile) internal carbon market and tax regimes which allow the direct or indirect use of CERs to meet national, regional or sectoral emission reduction targets and other

countries are evaluating this approach. As long as CERs, issued under the rules of the UNFCCC, are used this will assure global comparability and consistency and allow indirect linking of markets, but if the CDM is not compatible with the national support policies this positive evolution will be interrupted.

2. In the absence of international demand many host countries are seeking to create domestic demand for CERs and to make use of the CDM and its infrastructure to facilitate the implementation to flexibilize domestic policies such as cap & trade or carbon tax.
3. There are experiences where countries have established national support policies to promote GHG mitigation projects while the government decided to keep a share of the Certified Emission Reductions and this concept of a Host Country Share of Proceeds is another option to promote and quantify tangible emission reductions in developing countries.
4. The CDM today is the only UN recognized standard for baseline setting and MRV and its system with numerous DOEs and host DNAs is a fundamental complement to offer the necessary project based MRV to the evolving NAMAs and the embedded sectoral mechanisms. This synergy has to be fostered in order to facilitate and catalyse the evolution and integration of these tools.
5. The sophisticated rationale of the CDM will help to understand and evaluate the effectiveness of national policies and though the host countries are respected in their sovereign right to develop the policies best suited to their reality, the resulting transparency and consistent MRV will allow exchange and competition of concepts.
6. By integrating the CDM into national policies these countries are given an important tool to reduce and monitor domestic emissions as well as to complement and enhance their national mechanisms, procedures and competences. Based on the institutional learning it will only be another step to complement the CDM with regional and sectoral Cap and Trade schemes and the ultimate solution would be to combine the CDM with a national emission Cap, a scenario which will allow generating CERs which are backed by Assigned Amount Units as it is the case of JI.
7. Last but not least we want to emphasize again that the complementarity of the CDM with multilateral financing of development banks, as well as the future Green Climate Fund is another important element, especially for less and least developing countries. To account for this fact we again propose that rules and procedures equivalent to the E- regulation are being adopted for such multilateral support policies.

In conclusion we would like to make reference again to our extensive input provided by our letter from 8th May 2013, as well as by our input on the annotated agenda to EB 74 from 16 July 2013 and our input the annotated agenda to EB 75 from 23 September 2013

Annex 15 - Concept note: General simplification in the validation process - Delay in validation of monitoring plan (3/CMP.9 – Paragraph 10)

The PD Forum welcomes consideration of delaying the validation of the monitoring plan as this is something we have been calling for for several years. As outlined in the concept note, it is generally impractical to tightly define the monitoring plan at validation stage when the project activity is usually still at planning or construction stage. And this leads to subsequent delays in issuance if the monitoring plan needs to be revised.

We therefore support proposals to increase flexibility in the timing of the monitoring plan. We further suggest that, given that there are advantages and disadvantages to all three scenarios presented in the concept note¹, an element of flexibility is introduced whereby PPs can decide when the monitoring plan is validated. Some PPs may wish to continue with the current situation whereby the monitoring plan is validated at validation stage, thereby reducing risk later on; whereas others may prefer to delay this until post registration but before the first verification to avoid any potential delays in issuance; and others

¹ i.e. validation of MP at validation stage (current situation), validation of MP post validation but before first verification and validation of MP at first verification

may prefer to wait until the first verification to avoid increased costs associated with an additional DOE site visit.

Annex 16 - Concept note: General simplification in the validation process (3/CMP.9 – Paragraph 18)

The PD Forum also welcomes all efforts to simplify the validation process and reduce transaction costs for PPs, particularly given the current market conditions. We support proposals for a 'streamlined' validation process for PAs/ PoAs that use positive lists and indeed hope that these simplified additionality procedures can themselves be extended. While we support the development of a simplified template for PAs/ PoAs that use the streamlined validation process, we suggest that given current market conditions and the volume of projects/ programmes in the pipeline, development of meth specific templates might not be an efficient use of resources at this point in time.

We thank you for the opportunity to provide our comments on the annotated agenda and annexes and would be very happy to discuss them with you further,

Kind regards,



Rachel Child
Co Vice Chair, Project Developer Forum