

The World Bank

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street N.W.
Washington, D.C. 20433
U.S.A.

(202) 473-1000
Cable Address: INTBAFRAD
Cable Address: INDEVAS

May 4, 2009

CDM Executive Board
c/o UNFCCC Secretariat
P.O. Box 260124
D-53153 Bonn
Germany

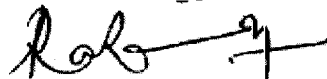
Sub: Submission of inputs on efficiency in the operation of the CDM and opportunities for improvement

Honorable Members of the CDM Executive Board,

We appreciate the CDM Executive Board's call for public inputs on the subject of **efficiency in the operation of the CDM and opportunities for improvement** and welcome the opportunity to contribute suggestions for enhancing transparency, consistency and overall efficiency of the CDM. The enclosed inputs are presented for consideration of the CDM Executive Board.

We would be happy to provide clarifications and contribute to further discussion on the subject if the Executive Board finds this helpful.

With kind regards,



Rama Chandra Reddy
Acting Team Leader
Policy and Methodology Team
Carbon Finance Unit, The World Bank

Efficiency in the operation of the CDM and opportunities for improvement

The CDM has made impressive strides and the key to the continued success of CDM is to achieve the goal of greater efficiency in registering GHG mitigation projects and programs without compromising environmental integrity. The following inputs of the World Bank are based on its experience as a multilateral institution that has participated in the CDM for several years. The key issues in the context of decision 2/CMP.4 are highlighted and the suggestions for improvement to enhance the efficiency of the CDM are presented for consideration of the CDM Executive Board.

Issue 1. Transparency and Consistency in EB Decisions

Effects of Issue 1	Suggestions for improvement
<p>1) Catalogue of EB decisions, though available, does not enable identification of EB decisions across project types or for specific requirements. This results in unclear and repeated submissions of documentation that may not necessarily comply with the rulings of the EB. This situation often puts small project entities with fewer resources at disadvantage as they have to devote significant time and resources to go through the entire body of guidance and decisions and still not be able to access the relevant decisions.</p>	<ul style="list-style-type: none"> • Advanced tracking tools and electronic search capabilities that identify and differentiate decisions from generic guidance in the reports of EB meetings should be implemented. This is necessary especially considering the increase in volume of information and growth of annexes to EB meeting reports over time. • Categorization of decisions and generic guidance by sector scopes (e.g waste management, agriculture etc), project types, methodologies and specific issues would improve the access to relevant information. • Decisions of the EB from the meeting report should be extracted and summarized at the end of each meeting, and categorized in the context of earlier decisions to link the EB decisions over time so as improve the access to decisions and information.
<p>2) Unclear hierarchy of decisions and guidelines and differences in interpretation by different documents and lack of guidance as to which decision/document supersedes the others.</p>	<ul style="list-style-type: none"> • Adopt a system that uniquely identifies the CDM decisions and the documentation should be classified to provide a hierarchical system for decisions and guidance. This will improve the clarity in the application of CDM requirements emanating from EB decisions, procedures, VVM, glossary of terms and other guidance.
<p>3). Despite clear guidance for distinction between small-scale and large-scale projects and programs, there is continued imposition/interpretation of</p>	<ul style="list-style-type: none"> • Reinforce the distinction between small and large scale projects and provide suitable guidance to clarify applicability of the simplified procedures for small-scale

<p>the requirement of investment analysis for <i>all</i> projects, irrespective of scale, although investment analysis is not a mandatory for small-scale CDM activities as per the simplified modalities and procedures.</p>	<p>projects to avoid selective interpretation of VVM guidance by DOEs that is contradictory to the spirit of simplified procedures</p>
<p>4) Due to delays in EB decision making some draft guidance is implemented in advance of its EB approval and in anticipation of an expected EB approval decision.</p> <p>Guidance such as the “Enhanced barrier analysis” was prepared by the Secretariat as draft document, but DOEs have started applying these in order to be conservative. This lack of clarity of when to implement the guidance causes uncertainty and delays.</p>	<ul style="list-style-type: none"> • There is a need for clear guidance to DOEs that draft guidelines and documents should not be applied to validation, verification and requests for reviews until final decisions/guidance on the relevant aspects are approved by the EB.
<p>5) There is a lack of clarity concerning documentation requirements at the stage of submitting a request for registration. This situation contributes to significant delays.</p>	<ul style="list-style-type: none"> • The completeness check template/checklist should be prominently displayed at the UNFCCC website so that PPs can be requested to use the checklist to compile and submit all the documentation required for the registration of a project. The completeness check template/ checklist utilized by the Secretariat should be comprehensive and cover all the documentation required for registration of a project and should clearly be referenced in case of a request for review.
<p>6) There are no EB approved procedures for surveys and sampling for projects (small scale and large scale) and programs when methodologies do not provide the relevant guidance.</p> <p>The issues related to surveys, sample size and statistical significance to achieve the accuracy desired in methodologies come up frequently for projects and programs that are implemented in multiple dispersed locations. However, the approved guidance is very generic and often the</p>	<ul style="list-style-type: none"> • It is suggested that EB approve a guidance tool on survey and sampling that covers all aspects of statistical procedures to be followed when applying all methodologies so that guidance in the tool complements the requirements of the methodologies. This tool could be excel or web-based tool allowing PPs to input project specific information. • It is suggested that EB approve a robust guidance on surveys, sample size and statistical procedures, including the indicative sample sizes acceptable and could rationalize the monitoring costs of

<p>decisions of the project proponents are not agreeable to DOEs resulting in costly repetitions of survey and data analysis. EB has also placed some projects under review at verification citing the reasons of lack of representativeness of the sampling procedures verified by the DOEs resulting in the withholding of issuance of credits.</p>	<p>projects and programs implemented over wide geographic regions and often remote areas in developing country contexts. Such guidance will facilitate the DOEs to assess the project in an objective manner without the need for DOE level multiple interpretations of procedures.</p>
<p>7). Procedure for assessment of baseline for renewal of crediting period for projects is not clear. Several early start projects adopting 7-year renewable crediting period are completing their crediting period.</p>	<ul style="list-style-type: none"> • The approved guidelines for baseline assessment for renewal of crediting period need to be updated to facilitate the renewal of crediting period without incurring additional delays and transaction costs.

Issue 2. Accountability of Regulatory Bodies (EB, Panels/Working Groups and DOEs)

Effects of Issue 2	Suggestions for improvement
<p>1) Questions of governance are important to ensure the accountability of regulatory bodies. In most regulatory institutions, the right to appeal against a regulatory action exists. Ensuring such due process contributes to enhancing confidence and trust in a regulatory bodies. In the case of the CDM, when a PP has a concern or aggrieved by a regulatory action, there is no opportunity for appeal. The only option available under the current procedures is to submit a letter directly to the EB as an unsolicited communication as per Annex 37 of EB31 decision. It is not always transparent how such a letter (or a submission to a call for inputs) is considered and processed within the CDM. In most situations, the PPs/other appealing entities do not receive communication on the follow-up to the representation.</p>	<ul style="list-style-type: none"> • Undertake an examination of the CDM governance and its processes to ensure due process • Define effective process where PPs can alert EB and panels of situations of likely conflict of interest. • Establish the institution of ombudsman to handle and compile feedback of project proponents/other appealing entities regarding the assessments of projects. The Ombudsmen institution should be independent of the CDM EB and panels and have power to review the EB decisions and should be mandated to report to COP/MOP on the decisions of the EB to preserve sense of fairness of regulatory actions. • The Ombudsman institution would also serve as a channel of communication to COP/MOP in situations where EB does not have mandate to make regulatory decisions.
<p>2). The existing structure of CDM Executive Board with members and alternates with 2 year tenures and half of the Board replacing each year may</p>	<ul style="list-style-type: none"> • Considering the growth in number of projects and compliance needs, there is a significant need for real time decision making in the Executive Board as opposed

<p>not provide adequate time for members to contribute to decision making considering the Board meets 5 to 6 times a year.</p>	<p>to the current practice of decision making at periodic meetings during the year. This calls for professional and permanent CDM Executive Board and panels with members appointed with longer tenures.</p> <ul style="list-style-type: none"> • To ensure the continuity of decision making, small proportion, e.g., one-third or one-fourth of Board members may be replaced each year instead of the current practice of replacing one-half of the Board members. • To ensure the independence of the EB/Panels, the tenure of EB/Panel members may be limited to 1 to 2 terms with restrictions on subsequent reappointment to regulatory bodies under the convention.
<p>3) Cases where similar projects or project bundles are not treated the same due to changes in methodologies or interpretations. This results in significant uncertainty as the project proponents would have already committed significant investments to projects. Several such instances have been observed and reported reflecting the uncertainty associated with regulatory process and consequent loss of confidence in the CDM. Example: Out of bundles of biogas projects in a country, two bundles were registered and subsequent bundles were not accepted. Such cases reflect the loss of faith of the project proponents and poor communities/households in the regulatory process.</p>	<ul style="list-style-type: none"> • A process that allows a project proponent to seek clarification or to appeal against a specific decision would greatly improve trust in the process.
<p>4) Working groups and DOEs may interpret methodology applicability, revision/deviation requirements of a methodology, documentation related to additionality or the EB decisions differently causing expensive delays in the registration of projects or issuance of credits resulting in serious financial losses for PPs. However, there exists no redressal or compensatory mechanism for improper application of</p>	<ul style="list-style-type: none"> • Systems for timely redressal of issues emanating from interpretation of rules and procedures by regulatory agencies should be established to ensure the confidence of stakeholders in the regulatory process.

rules or conflicting guidance by regulatory bodies.	
---	--

Issue 3. Improving Procedures for Processing Methodology & Project Submissions

Effects of Issue 3	Suggestions for improvement
<p>1) The process for submission of new methodologies, revisions, clarifications and deviation to existing methodologies needs to be simplified and streamlined and should be more user-friendly and predictable.</p> <p>For example, some industrial, transport and power sector methodologies were rejected by the methodology panel without adequate feedback for rejection. In certain cases, methodologies were rejected on the grounds that lack of scientific consensus on the methodology topic. The time and uncertainties associated with the process lead to high transaction costs.</p>	<ul style="list-style-type: none"> • Adoption of procedures that would streamline methodology review and facilitate guidance and communication should be established. • The communication of the SSC-WG with the project entities during methodology review facilitated several technical clarifications on the application of small scale methodologies, Similar procedures could be institutionalized for large scale methodologies, which are often complex and could benefit from communication with project proponents thereby reducing time spent on written requests.
<p>2) Lack of clarity around methodology parameter requirements, calculations and monitoring occur due in part because they are presented as paper based tools.</p>	<ul style="list-style-type: none"> • Web and spreadsheet-based tools could support the application of methodologies and guidance tools and help simplify the monitoring, calculation and reporting.
<p>3) In the recent past, delays in methodology reviews were caused due to inability to find sector experts.</p>	<ul style="list-style-type: none"> • The pool of expert consultants associated with CDM is limited. The UNFCCC Secretariat and the methodology panels should formally engage leading industrial research institutions and industry associations to provide inputs and not rely solely on individual consultants. Recognized industrial research institutions and industry associations have the benefit of their outputs vetted by a broader set of community as opposed to a single consultant engaged by the EB.
<p>4) Changes in versions of methodologies or tools delay submissions during the period that a proposed CDM project has started</p>	<ul style="list-style-type: none"> • Increase the grace period for the use of old versions of methodologies and changes to tools (e.g. additionality tool) from 8 months to 12 months.

<p>validation/registration process. A constantly moving target makes it difficult to integrate the CDM contribution into a project. It creates delays and difficult to manage uncertainties.</p>	<ul style="list-style-type: none"> Projects that completed the global stakeholder process should be exempt from future changes in the versions of the methodology or tools.
<p>5) The workload in terms of the issues raised, discussed and decisions made make it difficult to process projects in timely and efficient manner.</p>	<ul style="list-style-type: none"> Constitution of full time panels with provisions for regional/decentralized and virtual meetings would help ensure timely response to issues raised.
<p>6) The number of review cases reflects to a large degree the EB's concerns about ensuring the quality of DOE inputs in validation and verification reports. Thus the review process is an expensive process that requires deployment of scarce resources of the Secretariat.</p>	<ul style="list-style-type: none"> Evaluate other steps that could be implemented early in the process to ensure the submission of quality of documentation from project proponents and DOEs to avoid delays in project registration or issuance of credits.
<p>7) The EB decisions become effective as soon as they are approved. However, there may be delays in incorporating the EB decisions into methodologies.</p>	<ul style="list-style-type: none"> There should be guidance on the application of EB decisions to projects when methodology versions do not cover the latest EB decisions.

Issue 4. Improvements in the Application and Coverage of Methodologies

Effects of Issue 4	Suggestions for improvement
<p>1), In several methodologies, there is no clarity on the treatment of uncertainty. As a consequence, there is pressure from regulatory agencies to adopt conservative parameters that may not be relevant for the project context. There is also no guidance on application of conservative parameters and the ways in which issues of materiality need to be reconciled.</p>	<ul style="list-style-type: none"> There is a need for guidance on circumstances in which conservative parameter values could be used. There is a need for guidance on treatment of materiality that allows for a certain degree of imprecision in situations where differences in expected results have no significant impact on CERs, particularly in case of differences between monitoring practice at verification compared with the monitoring plan of the registered PDD. If the differences do not lead to significant impact on CERs then they should be considered insignificant and noted in the verification report of the DOE
<p>2). Insufficient representation of project types such as:</p> <ul style="list-style-type: none"> Energy efficiency 	<p>To encourage submissions of methodologies in the under represented sector scopes, we recommend:</p>

<ul style="list-style-type: none"> • Transport • Construction • Agriculture 	<ul style="list-style-type: none"> • Baseline and monitoring procedures to be developed in close alignment to the specific sector (e.g., use of baseline metrics such as specific energy consumption), • Develop default values for emission reductions based sector practices. • Consider sector specific automatic additionality based on a set of criteria (e.g., benchmarks), positive list of technologies etc. • Consider adjustment factors for internalizing issues such as rebound effect, • Consider eliminating the consideration of grey energy in transport projects
<p>3). Addressing risks of perverse incentives is important for the credibility of the CDM as a whole</p>	<ul style="list-style-type: none"> • Similar to an 'A' list, consider a sector specific 'B' list of technologies or project types to be restricted to either "greenfield" or "brownfield" applications

Issue 5. Need to re-visit Additionality Assessment

Effects of Issue 5	Suggestions for improvement
<p>1) Investment analysis and the interpretation that "profitable projects" per se not additional has resulted in many requests for review by the EB.</p> <p>While the EB has developed useful tools, additionality seems to be influenced by the regulatory views on appropriateness of underlying assumptions. There is also a trend towards reliance on investment analysis in comparison to the barrier analysis for assessing additionality of projects.</p> <p>The increasingly narrow interpretation of additionality often does not reflect the changes in real world business variables such as prices (e.g., recent oil price spikes of 200 to 300% over a short term) and decline in demand for goods and services due to recessionary trends.</p>	<ul style="list-style-type: none"> • Clear guidance on the use of parameters, (e.g., which parameters should be current and which from the time of investment decision) will assist in clarifying consistency of investment analysis. • Establishment of a set of criteria for assessing technologies that can be considered 'automatically' additional helps in improving the transparency of assessment. • Definition of benchmark additionality based on energy performance, market penetration or other parameters. • Assessment of baselines using econometric trend analysis could help in situations where historical data on the baseline is available.

Issue 6. Regional Representation of CDM Projects

Effect of Issue 6	Suggestions for improvement
<p>1) Poor representation of LDCs in Africa and other regions reflects the constraints to business development and information on CDM regulatory process</p>	<ul style="list-style-type: none"> • Identification of sectors and technologies that are automatically considered additional for one or more commitment periods in the LDCs to encourage CDM consideration in the investment decisions of projects.
<p>2) Poor financial capacity or lack of awareness regarding a specific issue is self-evident in most LDCs and it is quite difficult to get “documentary evidence” in support of such assertions.</p>	<ul style="list-style-type: none"> • Identify simplified approaches to account for the baselines in the LDC contexts. • Regulatory requirements should take into account the limitations of technology and data availability • Simplified procedures (sampling, site visits, automatic additionality, requirement for documentary evidence etc) should be adopted so as to reduce the transaction costs of regulatory compliance. • The use of sector-level research documentation should be permitted for assessment of additionality. For example: if international research publications document the lack of funding for small hydro power plants in a country, this should suffice as evidence of financing barrier. • The methodology requirements and : baselines need not be limited to existing energy use as production levels are expected to grow in developing countries translating the increase in energy services over time.
<p>3). Lack of capacity, absence of awareness and lack of information on regulatory changes limit the uptake of CDM.</p>	<ul style="list-style-type: none"> • There is a significant need to build capacity at the DNA, sub-national and industry/sector levels. For example, improved funding from bilateral agencies, multilateral agencies and private sector to capacity development initiatives such as Nairobi framework could improve the capacity of countries.
<p>4). Issuance of temporary credits has acted as a deterrent for the uptake of Afforestation and Reforestation projects, which contribute to sustainable development through conservation of land and water resources, supply of biomass resources for fuelwood, fodder, timber and non-timber products and provision of employment and carbon sequestration benefits to rural poor in</p>	<ul style="list-style-type: none"> • There is a strong need to remedy the issue of temporary credits for AR projects by adopting suitable measures that ensure permanence of AR credits and contribute to the greater uptake of AR projects.

LDCs	
5) Considering the capacity and financial constraints, few project types can sustain the monitoring burden of methodologies	<ul style="list-style-type: none"> • There is a need to identify the project types that can benefit from methodologies with low monitoring burden by complying with a set of performance criteria and default factors for issuance of credits.

Issue 7. Scaling up the CDM

Effect of Issue 7	Suggestions for improvement
1) Program of Activities	<ul style="list-style-type: none"> • The issue of liability described by the DOEs has been taken up in recent discussions of the EB and needs to be urgently addressed. • With regard to the start date of the CPA not precede that of the PoA, it is important to show that the PoA was the driver behind the establishment of CPAs. However, the enforcement of a requirement based on start dates may not be realistic. The results of the current requirement as discussed by the EB would look as follows: <ul style="list-style-type: none"> • A program is launched (databases created, managers hired, stakeholder consultation, EIA completed – as per validation requirement). At this stage, all financial resources (grant, soft loan, and other funds) will have been secured. • The first CPA is identified and implemented (to document the performance of a typical CPA). • The Program will stop, awaiting registration of the POA. <p>To avoid this scenario, the EB should permit project proponents to justify the start of the CPA prior to registration of a PoA based on a set of criteria (e.g., documentary evidence linking the implementation/investment decision for CPA with the POA).</p> • Grace period for early mover PoAs should be provided. The lack of validation of PoAs due to lack of DOE action was outside the PP's control and was brought to the attention of the EB during early 2008.
2) Sector/multi-project baselines	<ul style="list-style-type: none"> • Appoint a consultative group to provide recommendations and develop initial data

	<p>databases for the establishment of sector based benchmarks.</p> <ul style="list-style-type: none">• Based on this work the EB could submit informed recommendations and action plan to the CMP for approval and oversight.• Build on the learning-by-doing and complement the process by drawing upon the experience with CDM and providing some top-down guidance,
3) Constraints on DOE resources are the factors contributing to delays in validation and verification of projects.	<ul style="list-style-type: none">• There is a need to strengthen DOE capabilities and to ensure that the DOEs deploy right competence for regulatory tasks.
