

Dear Mr. Eduardo Calvo, Chair of the Executive Board

REF: CDM LOAN SCHEME – Challenges faced and constructive inputs

The PD Forum welcomes the planned activities of the CDM Executive Board (the Board) as part of the 2016 work plan with regards to the CDM loan scheme including an independent evaluation.¹ To this effect, the PD Forum has noted that a survey was sent out to CDM loan participants, participants were also requested to submit a detailed status update on their loan activities and explicit reminders were delivered with regards to the repayment conditions of the loan. The PD Forum understands that results from the evaluation shall be presented at EB91.

The PD-Forum feels it important to initially frame this communication within the context of the original grounds for the establishment of the CDM Loan scheme, a rationale that is clearly set out in each of the loan agreements -

<http://cdmloanscheme.org/sites/default/files/Loan-Agreement.pdf>. The fifth session of the CMP through decision 2/CMP.5, paragraph 49, requested the CDM Executive Board to allocate financial resources from the interest accrued on the principal of the trust fund for the CDM, as well as any voluntary contributions from donors, in order to provide loans to support certain activities relating to the CDM in countries with fewer than ten registered CDM project activities (as of 1 January of the year of the submission of the loan application). The sixth session of the CMP through decision 3/CMP.6, established the modalities and procedures for the operationalization of a Loan Scheme to support the development of CDM project activities in countries with fewer than ten registered CDM project activities.

Furthermore the PD-Forum would like to initially recognise that the CDM loan scheme has potentially played an important role in offsetting transaction costs associated with the development of CDM projects, this is particularly pertinent given the focus on assisting initiatives in underrepresented regions (less than 10 registered CDM projects). With over 70 CDM loans approved, it is evident that the scheme has made a noteworthy contribution to the global efforts undertaken to de-risk the up front costs associated with the CDM registration and issuance process within the context of a challenging carbon market environment.

Against this backdrop, the PD-Forum believes that as critical efforts continue with regards to positioning the CDM within the Post Paris Agreement landscape the loan scheme could have a significant role to play in supporting the development of internationally recognised climate mitigation actions. Given the changed playing field the CDM loan would in addition need to respond and evolve to maintain relevance.

¹ See EB 88 A01 –INFO CDM Executive Board Work plan 2016

The PD-Forum therefore would like to contribute to the ongoing efforts of the Board with regards to the Loan Scheme and highlight both challenges faced by Project developers with the existing scheme in addition to providing constructive and hopefully timely input to any future developments.

1. Loan repayment terms

Current CDM loan agreements stipulate that projects are required to pay back loans within one year of the first issuance of CERs or alternatively the final scheduled date for Repayment of the total disbursed funds is 30 September 2018. In addition the Loan Funds are to be used for expenditures incurred no later than 31 December 2017. However, given the current market circumstances, projects without an ERPA will face challenges to repay the CDM loan based on the sales of CERs. UNOPS, the administrator, has indicated that projects are expected to repay the loan even if issued CERs remain unsold. Beyond the current CDM Loan scheme contract also contains provisions for UNOPS to request UNFCCC to withhold CERs issued but not yet distributed to defaulting Loan Scheme recipients. This is putting an additional financial burden on projects and in effect going against the *raison d'etre* of the CDM, i.e. to overcome financial barriers as opposed to creating them in regions/countries where the support has been identified as most needed.

Constructive input: Update the CDM Loan Scheme modalities for existing loans in order to reflect current and future carbon market realities, based on a potential timeframe for significantly increased demand under the Paris Agreement being post 2020. Options could be explored to convert the loans into grants, or as a minimum extend the terms of the re-payment period beyond 2020.

2. Systemic level requirements beyond the direct control of the developer affecting loan disbursements

CDM loans are disbursed according to pre agreed milestones inline with the CDM project cycle, in most cases determined by the performance of the developer and associated consultant. However in some cases there are systemic level requirements that sit beyond the direct control of the developer that affect loan disbursement. This is even the case even when disbursements are to be made to a third party such as DOEs for example, that need to be compensated for their work. An example situation is where the project participant is unable to secure a letter of approval from the host country DNA for reasons beyond their control. A second example is a Force Majeure such as a political crisis or arising conflict, which currently only results in loan cancellation, with disbursed amounts still to be repaid. In such situations, the project is unable to achieve CDM registration hence will not meet a critical payment milestone. The project participant is left to pay off outstanding bills from the CDM consultant and the validating DOE even when control does not lie directly with them.

Constructive input: The governance body of the Loan scheme is encouraged to give clear rulings for the current CDM pipeline in cases where systemic level issues beyond the direct control of the developer and consultant have resulted in the indefinite stalling of a project within the CDM cycle. Allowances could be afforded to these activities in terms of the loan disbursed received prior to the unforeseen and uncontrollable barrier.

3. Diversification of CER financing

Access to scaled up climate finance is fundamental to the implementation of the Paris Agreement, with various methods for fund disbursement emerging with market and non-market approaches leading to diversification and fragmentation of climate finance sources. These tendencies are equally reflected in the application of the CDM toolbox through a range of financing mechanisms from traditional compliance markets and voluntary offsets, through to innovative approaches such as Results Based Financing and Green Bonds. The generation of sophisticated financial modeling means that the CDM Loan scheme repayment model being based on the assumption of CER issuance resulting in a market-based sale is outdated.

Constructive input: Redesign a Post Paris Agreement CDM loan scheme to facilitate application for accessing a broad range of climate finance through the CDM with the modalities reflecting the financing mechanisms that may be applied to projects.

We would be available to discuss further any of the above suggestions if the EB or the Secretariat requires.

Best regards,