

The Future of the CDM

Ten reasons to use its full potential

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by

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Coal Mine Methane utilisation and abatement in China. Photo: Sindicatum Sustainable Resources

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Do you believe it is acceptable to dump your waste in the sea?

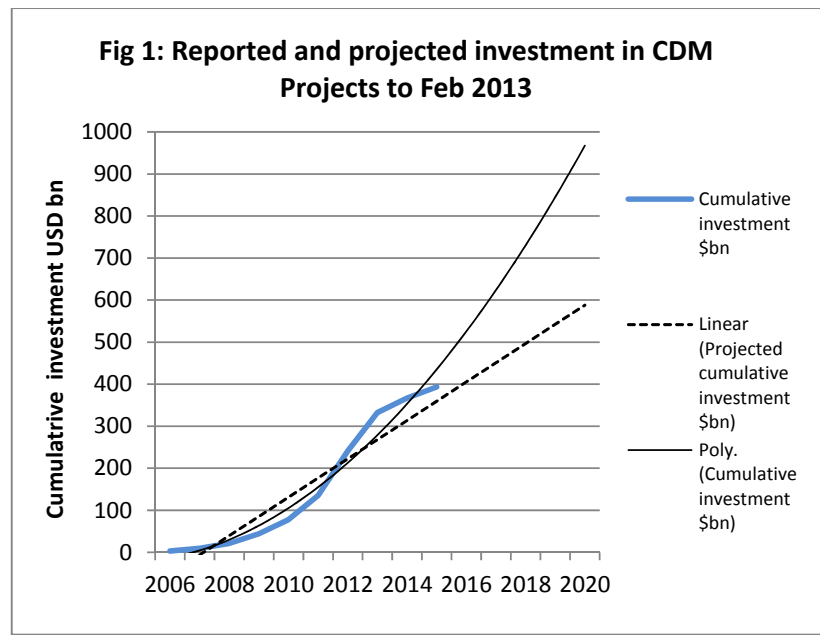
No?

Then why do you think it is ok to dump your CO₂ in the air?

KEY POINTS

- The High Level Panel on the CDM Policy Dialogue last year concluded that “*nations must intervene forcefully to address the immediate crisis and substantially increase their mitigation ambition*”.

- **The CDM was on track to deliver somewhere between USD 600 billion and USD 1 trillion of investment into clean energy projects in developing countries by 2020** (Figure 1). This represents investment that helps to move developing countries onto a low carbon development path and away from the lock-in of high carbon technologies. The CDM is currently the only success story in the international climate change negotiations. It has delivered countless benefits and has the potential to deliver substantially more.



- **The CDM's potential should be used to the fullest by:**
 - 1. Creating demand for CERs**
 - China, India and other Advanced Developing Parties can use CERs to help meet targets
 - ICAO and IMO can use CERs to offset their carbon footprint, after setting targets
 - The international community can create a fund to purchase emission reductions and retire them as a contribution towards global mitigation
 - Cities should follow Sao Paulo's example and use emission reductions to meet targets
 - International organisations like the UN should offset all their emissions.
 - 2. Ensuring that the CDM is a key part of the international climate change political framework going forward.**
 - 3. Using the current review of the CDM Modalities and Procedures to further improve the CDM as a mechanism which delivers CERs that Parties and stakeholders continue to want to buy.**

SECTION 1: *Five challenges for the CDM*

Over the past 14 years, the CDM has emerged as the world's largest carbon finance mechanism and has driven \$215-450bn in investments into renewable energy and low carbon projects. These investments have been concentrated in major emerging economies, where emissions growth most needs to be slowed, and in renewable energy, which is critical for decarbonising the global power sector. Nevertheless there remain some challenges.

1) There is an alarming lack of ambition amongst the Parties.

Despite increasingly alarming reports from climate scientists and an obvious increase in climate related disasters, there is an alarming lack of ambition amongst the Parties. Weak targets and over-allocation combined with a prolonged economic slow-down has resulted in an oversupply of all kinds of carbon units, including CERs, the price of which has fallen to below USD 0.30 per unit. There is no sign of increased demand from the EU ETS, other developing ETS or Annex 1 Parties. As a result, *new* projected CDM driven investment in clean energy and low carbon projects till 2020 has fallen from its potential of USD 600 - 750bn, to around zero.

2) Stakeholders repeat the claim that a significant proportion of CDM projects are not additional.

These claims continue to undermine confidence in the CDM, yet they are unjustified. The High Level Panel on the CDM Policy Dialogue did not find any evidence to support these claims. The fact is that every single registered CDM project has been individually tested against, and passed, the additionality criteria that were current at the time of registration.

There is a fundamental mistake in this assessment. Critics of the CDM are applying today's standards of additionality and today's interpretation of those standards to yesterday's projects. However, projects were registered and investments were made against the standards and interpretation of those standards that were current at that time.

Rules and standards in the CDM have been improved continuously in a learning-by-doing environment, so that going forward, projects get better. This constant quest to achieve the highest

standards is inherent in the mechanism's very nature. As a consequence of learning-by-doing, today's projects should be better than yesterday's projects, but that does not mean that yesterday's projects are not valuable to society and the environment or not additional.



Waves threaten New York City during Hurricane Sandy

3) Stakeholders continue to claim that carbon finance has not been channelled to the "right" kinds of activities.

Contribution to sustainable development is a sovereign issue, however, industrial gas projects, waste heat recovery projects and large scale hydro projects are amongst some of the technologies which have attracted criticism. Some Annex 1 Parties (some of whom have issued Letters of Approval to these projects) have since taken unilateral measures to implement qualitative restrictions and/or additional eligibility criteria to address their concerns. Whilst regulation by the CDM EB would be preferable to ensure that there is one common standard for CDM projects and not a range of standards, CDM developers and investors have been forced to adjust their business models to take these measures into account.

The CDM has very effectively identified the **least cost abatement opportunities** which the mechanism was designed to exploit, and at the same time provided significant sustainable

development benefits such as renewable energy, long-term employment and technologies to use sustainably sourced biomass . The CDM has also shown itself to be highly responsive to the likes and dislikes of the marketplace, adapting via “learning by doing” such that many of today’s projects specifically address buyers’ desires . Besides, these low-cost abatement opportunities were heavily taxed in some of the host countries, such as China, and this tax revenue has been and continues to be used to further the country’s climate change policies. This is a typical example of how best to use the CDM and the possibilities for individual adjustments according to local voters’ preferences on both the supply and demand side, are numerous.

It is a fact that the CDM is, or was greatly supporting sustainable development in poor and rural communities, in Least Developing Countries and in Africa, whilst at the same time contributing to the decarbonisation of the energy sector in advanced developing countries and **mitigating more GHG emissions than the rest of the world’s efforts put together.**

4) The CDM is perceived as an “offset only” mechanism which does not contribute to the host country’s mitigation.

The CDM was created, amongst other things, to help Annex 1 Parties meet their commitments under the Kyoto Protocol, so it should come as no surprise that CERs from CDM projects are used to offset excess emissions. Furthermore, it has been extremely successful in doing so and has rapidly identified and extinguished some of the most polluting sources of CO₂ and long-lived GHG emissions, delivering least cost abatement consistent with market principles.

CDM methodologies have considerable conservative safeguards built into them to ensure that there is no over-issuance and one consequence of this is that CDM projects only claim a proportion of their actual emission reductions. This conservativeness has to date not been quantified and hence cannot be presented as evidence of host

country mitigation but it is nevertheless real and the CDM is thus delivering net emission reductions.

That being said, there are close to 0.5 bn CERs which have been generated, verified and issued, which have not yet been surrendered against compliance obligations and if the current market conditions continue, a significant number are unlikely to ever be surrendered. Under the current circumstances, the CDM is in fact the only global mechanism which has both helped Annex 1 Parties meet targets and **delivered real permanent emission reductions in developing countries paid for largely by the private sector.**

CDM projects further contribute to mitigation by introducing new technology which leads to technology transfer and uptake of that technology outside registered CDM projects, for example, novel waste heat recovery technologies and wind power. The CDM also builds projects that will continue to operate and reduce emissions beyond the crediting period of the project.

Should the Parties so wish there are several significant steps that could be taken to increase and transparently quantify the mitigation benefits of CDM projects. The PD Forum has proposed a Host Country Mitigation Share of Proceeds, described in a separate paper available at www.pd-forum.net.

5) The CDM is perceived as being slow, bureaucratic, inconsistent and complex with high transaction barriers.

This was true but significant improvements have been made by the CDM Executive Board and the Secretariat over the last few years, and with over 6,000 projects registered and 1.2 billion CERs issued, the transaction barriers are clearly not insurmountable. There is, or at least there was, a significant body of companies who understood the rules and after 10 years of engagement could navigate the process with greater certainty. However, that is not to say that there is no scope for improvement.



Biomass for biogas production at cassava based ethanol plant, Indonesia.

SECTION 2: *10 reasons to use its full potential*

The CDM has, to date, had a positive impact on global climate change mitigation. In developing countries, the CDM introduced explicit carbon pricing, and built the networks and institutions required to monitor, report and verify greenhouse gas emissions. On a global level, the CDM has developed the norms, processes and infrastructure required for future mitigation initiatives, including New Market Mechanisms and the Green Climate Fund. For the private sector, the CDM has offered a risk mitigation mechanism which has led to, for example, US pension funds investing in Chinese coal mine methane utilisation and abatement.

1) Every one of the challenges listed above is either a non-issue or is being addressed.

Criticism of the CDM is a fashionable reaction to what needs to be a long term policy. Stakeholders have made 171 recommendations to the EB as to how to improve the CDM through the current revision of the CDM Modalities & Procedures. The High Level Panel came up with 52 recommendations. These recommendations can address all of the above issues if the Parties are able to take them forward at CMP19 in Warsaw.

2) Framework for Various Approaches and the New Market-Based Mechanism will face the same challenges.

Baselines, additionality, monitoring, reporting and verification cannot be disguised or avoided. Environmental integrity is not easy to deliver and

there are no shortcuts (or at least, we have not found them yet).

3) There will always be significant sectors of every economy where it is impossible to implement sectoral cap and trade, regulations, incentives, taxes etc.

The challenges for Government departments and institutions to monitor and verify activity levels or emissions arising from unregulated industries, throughout Least Developed Economies or in dispersed and variable activities at a household or cottage industry level are insurmountable. On the other hand, project-based activities including the CDM have already demonstrated an ability to take private sector money, at scale, into areas where public funds and infrastructure are unable to reach.

4) CDM brings not only finance but also technology.

Private sector firms develop and own technology; less so Governments. The CDM allows the private sector to bring the benefits of such new technology into the investment decision-making process.

5) The CDM, a Public-Private Partnership, has been strongly endorsed by the private sector, as evidenced by the flow of funds it has mobilised.

The Host Country Letter of Approval, issued to emission reduction projects under the CDM, provides investors with the certainty they need. Following issuance of this Letter of Approval, any CERs generated by the project can be transferred into an Annex 1 Registry account from where they can be sold. Of course, no one anticipated that the resulting CERs would currently be almost valueless. However, no other mechanism proposed to date offers this certainty and without it, the Private Sector will not engage enthusiastically or at the required scale.

6) The CDM enables project developers to identify and develop assets that require carbon finance.

The additionality tool rigorously tests whether projects need carbon finance and only those which are found to be unattractive without carbon finance can be registered as CDM Projects. The CDM works with asset-specific accuracy to improve resource use efficiency. No other program can do that.

7) The CDM has delivered massive sustainable development benefits.

Some may be harder to identify and quantify but there is no mistaking the benefits of on- or off-grid renewable energy to developing economies. Renewable electricity projects constructed under the CDM have to date delivered over 300 TWh: **about as much as the annual electricity consumption of the UK, Spain or Italy.** CDM projects have improved the quality of life for

countless people in 84 countries, delivered to host Governments in return for the right to export CERs.

8) The CDM is the most successful means of channelling low carbon investment in developing countries.

Even if all the OECD countries stopped emitting GHGs tomorrow we would still be unable to reach the 2°C target. We need to help Non-Annex 1 countries transition onto low carbon development pathways. There is a general expectation that the money for this will come from the private sector, but how will the private sector be compensated for the additional risks associated with deploying new technologies and investing in developing countries? The CDM is a proven successful risk mitigation mechanism.

9) Capped economies or sectors will need offsets in times when allowances are in short supply.

It seems unlikely now, but sometime in the future, we do expect caps to bite and start constraining economic activity. **As Governments and economies work to break the link between growth in output and growth in emissions, they will need access to additional emission reductions to provide short term flexibility.** Caps are the only way to drive global emissions down, but they require a flexibility mechanism in order to minimise their impact on economic competitiveness.

10) We need to act now to mitigate GHG emissions because if we delay, the costs of adaptation will be much greater.

The CDM is currently (though somewhat unintentionally) a successful mitigation instrument. With some minor changes, it can remain a strong mitigation instrument whilst at the same time helping Annex 1 countries and, in due course, selected developing countries implement policies which will ultimately result in lower costs of adaptation and at least a chance of avoiding run-away climate change.



Geothermal Installation Indonesia.

SECTION 3: *Three steps to use the CDM even more efficiently*

The rules of the CDM have been refined and strengthened over time. The additionality tool is the strictest of any offset mechanism, and has grown increasingly robust. In addition the CDM has placed unprecedented scrutiny on stakeholder consultation, and implemented steps to enhance monitoring, reporting and verification. Much has been achieved but the current review of the CDM Modalities and Procedures presents a once in a decade opportunity to address persistent problems and set the mechanism on track to play a very significant role in our efforts to combat climate change in the future.

1) Create and increase demand for CERs.

Parties must declare much greater ambition and translate that ambition into demand for emission reductions. China, India and other Advanced Developing Economies should use CERs to meet targets. ICAO, IMO, existing and developing ETS should similarly use CERs to meet targets.

A fund should be created to purchase emission reductions and retire them as a contribution towards global mitigation. Such a fund could be established by the World Bank, the Global Environment Facility, the Green Climate Fund or the Adaptation Fund – or a combination.

Major cities around the world can follow Sao Paulo's lead and implement emission targets to reduce costs and where necessary use emission reductions to help meet targets.

International organisations, starting with the UN themselves, should offset all of their emissions.

Allowing all Parties to use CERs would immediately increase the use of the CDM.

2) Parties must work to ensure that the CDM fits within the current and developing framework for combating climate change.

New market-based mechanisms and the Framework for Various Approaches offer to inject new momentum into the negotiations, but this must not be at the expense of the CDM. **The CDM is the only functioning mechanism which we have** and it touches significant parts of the global economy that NMBM and FVA cannot hope to reach any time soon.

3) Parties must use the review of the CDM Modalities and Procedures to change the CDM into an instrument which delivers the kinds of emission reductions that Parties want to buy.

For example:

- Institute a transparent host country mitigation procedure (see www.pd-forum.net).
- Provide clearer direction as to the kinds of projects they want to see by developing positive lists of technologies which are considered automatically additional.
- Redefine the relationship between E- policies (policies that encourage low emission technologies) and the CDM.
- Simplify the CDM by removing artificial barriers such as the concept of micro and small scale projects.

Gallery of CDM Projects



Biogas project, Brazil



Hydro Power Project, China



Landfill gas utilisation and flaring in Thailand



Avoided gas flaring in Indonesia



Host Country Mitigation Share of Proceeds

A CDM Reform proposal by the PD Forum

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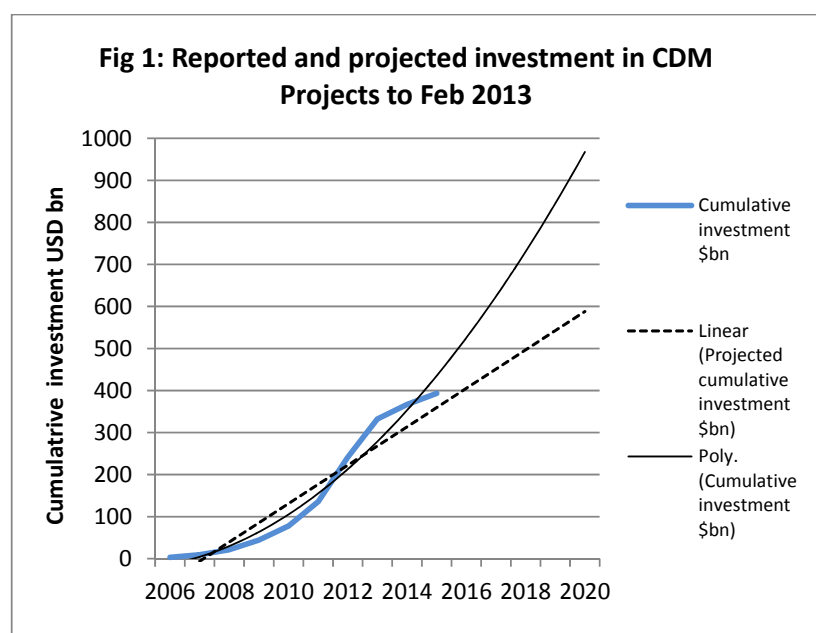
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Host Country Mitigation Share of Proceeds

A CDM reform proposal from the PD Forum

Introduction

The Parties are facing many challenges over how to move forward with the climate negotiations. While it has been reconfirmed that the CDM continues (several times), the future of the CDM is one of those challenges. The CDM has delivered more than USD215bn of investment in clean energy and emission reductions in host countries and was on target for between USD600bn and USD 1 trillion by 2020 (see Figure 1).



SOURCE: UNEP RISOE CDM Pipeline February 2013. Cumulative investment is the sum of investments reported for projects at validation, requesting registration and registered.

However, the CDM has struggled to fulfil stakeholders' expectations. It is criticized for financing projects that would have happened anyway and only helping to offset emissions in Annex 1 countries. The CDM is both a market based mechanism to find least cost abatement opportunities and a sustainable development tool. Balancing these twin objectives has proved challenging, and recently a third objective has been injected – an expectation that CDM projects will contribute to host country mitigation.

Stakeholders in the CDM have responded to these objectives in various ways including the imposition by buying Parties of qualitative restrictions on market access for CERs, positive discrimination in favour of projects from least developed countries, promotion by the CDM Executive Board of tools such as specific procedures and guidelines for micro scale projects and PoAs to encourage development of projects in rural areas and the scale up of dispersed community level project activities which are considered to promote sustainable development. As evidence of the mechanism's contribution to mitigation, Project Developers have pointed to the conservative nature of CDM methodologies. Project Developers and investors have also demonstrated great flexibility in the kinds of projects they have developed, responding to the learning-by-doing environment.

However, the future of the CDM remains unclear as proposals for New Market Based Mechanisms and the Framework for Various Approaches are developed. One suggestion is that **the CDM could act as an open source of methodologies, modalities and procedures, effectively act as an MRV service provider to other mechanisms, whilst contributing to and facilitating localized development of low carbon investments and an element of host country mitigation.**

How could this work?

The PD Forum proposes the establishment of an optional Host Country Mitigation Share of a CDM project's emission reductions.

The CDM community is already familiar with the concept of a Share of Proceeds (SOP). CDM projects already pay a cash SOP on the issuance of CERs towards the administration costs of the CDM and a CER SOP towards the Adaptation Fund. The Host Country Mitigation Share could be implemented as a Mitigation SOP (MSOP).

It is proposed that infrastructure to support an additional optional share of proceeds is established with the following objectives:

- The Host Country Mitigation Share of Proceeds will be collected at the point of issuance of CERs from CDM projects and transferred into a Host Country Mitigation Account in the CDM Registry, in a transparent manner.
- CERs held in the Host Country Mitigation Account may only be used to surrender against that Host Country's targets or voluntary pledges and reported in the next national communication or national inventor; or converted into allowances for use in the Host Country's domestic emission trading scheme.
- Like Host Country Approval of a CDM Project Activity, the level of Host Country Mitigation Share of Proceeds would be a sovereign decision, communicated periodically by the Host Country DNA to the UNFCCC and advertised on the UNFCCC webpage. Once a project receives its LoA, confirming the application of the advertised MSOP, the MSOP would be fixed for the crediting period of the project in question.
- The level of MSOP within and between Host Countries may be varied by technology, project location and time¹ (age of the project) depending on the host's own support, such as through feed in tariffs or subsidies; or to encourage or relatively discourage CDM investment in sectors and locations; to encourage investment into strongly additional technologies and discourage investment into technologies that are going to happen anyway; to facilitate the integration of CDM projects with current and future host country E-² and GHG management policies; and to guarantee net mitigation.
- Existing CDM projects could voluntarily apply for a revised Host Country LoA containing an updated MSOP in order to meet buyers' expectations of contribution to mitigation.

There would be no change in the volume of CERs issued, but the net result would be either no change in the number of CERs available in the market (in the case of a zero rated MSOP, for example in an LDC) or a decrease in CERs in the market where DNAs set a higher MSOP. However, the transparent demonstration of the contribution to host country mitigation would increase the quality and value of CERs to buying Parties and lead to the transparent accounting of the full climate benefits of the project.

¹ The size of the MSOP may vary (increase) during the crediting period, but such steps would need to be carefully considered against the costs for project operators to maintain the project performance and MRV infrastructure.

² E- policies are policies which encourage low emission technologies and practices.

It would be expected that Advanced Developing Countries would set higher mitigation shares of proceeds compared to Least Developed Countries and Host Countries could also vary the MSOP to reflect contribution to sustainable development; degree of additionality³; and interaction with existing E- policies. This variation would reflect the fact that the investment risks in advanced developing countries are significantly different from the risks in LDCs. Table 1 below gives an illustration of how Host Country Mitigation Shares of Proceeds might vary in different types of countries and by different types of projects:

Table 1: Examples of Host Country Mitigation SoP by development status. Proposed figures are for illustration purposes only.

Project Type	Host Country Mitigation Share of Proceeds expressed as a % of CERs at issuance		
	Advanced Developing Country ⁴	Developing Country	Least Developed county
Low contribution to sustainable development for example projects within an industrial complex	30%	20%	10%
Medium contribution for example renewable energy	20%	10%	5%
High contribution for example biomass cook stoves	10%	5%	0%

In addition, DNAs may introduce further variation by region within the country to highlight the different levels of economic development in different regions and they may vary the MSOP over time to, for example, reflect the future implementation of domestic policies such as ETS, taxes or performance standards or the degree of additionality. This would be equivalent to varying the duration of the crediting period but at a region / technology level rather than for example a country level.

Implementing a domestic ETS

As an alternative to cancelling the MSOP against existing pledges, and in particular as part of possible future commitments under the Durban Platform, Host Parties may use the MSOP to create allowances for use within a domestic ETS or allow CERs to be used directly in their ETS⁵. Capped schemes benefit from a source of supply of additional emission reductions and therefore Host Parties may turn to (their own) CDM projects to supply these emission reductions. Since a Non-Annex 1 ETS would be a voluntary action, using CERs to offset emissions within a cap would also amount to a voluntary cancellation and would therefore have the same mitigation impact as the MSOP.

Considering the benefits of ETS as an efficient and effective means of reducing emissions, this is a highly desirable step and it would move host parties considerably closer to the goal of global emission management.

³ For example, pure abatement projects with no other sources of revenues are strongly additional whilst renewable energy project range from strongly additional to “going to happen anyway” in which case the CDM may serve to advance their implementation by a few years.

⁴ A suitable classification system is required to distinguish a 3rd group of countries between advanced developed countries and least developed countries.

⁵ See our submission on the Carbon Market Architecture for a detailed discussion on domestic ETS implementation, under the New Market-based Mechanism.

What would be the benefits of such a scheme?

- 1) Host Countries will be able to use the CDM as a very powerful incentive mechanism to direct investment to GHG reduction projects.**

Giving DNAs a means to direct investment into different sectors would immediately increase their importance within host country government and ensure that not only Environment and Energy Ministries take notice, but also Ministries of Economy and Finance. The role of the CDM would change from being an opportunity for external investors to participate and invest in a host country's clean development whilst producing CERs to a becoming a mechanism which host countries can use to actively stimulate investment into specific areas of their economy in order to deliver particular sustainable development objectives, promote the development of technologies which are strongly additional, mitigate host country emissions whilst generating high quality emission reductions for consumption in other countries.

Active participation from host countries to direct investment towards specifically under-developed sectors will allow Governments to attract investors towards areas of the economy where investment is not taking place, where development of projects is not business as usual and where projects would be strongly additional.

- 2) By creating a transparent mitigation mechanism, the Parties would convert the CDM from an offset-only mechanism with claims of mitigation, into a powerful development mechanism with transparent and quantified mitigation benefits.**

The CDM is often seen as a purely offsetting mechanism: all the emission reductions generated by registered project activities are in theory destined to offset emissions beyond caps in Annex 1 countries⁶. However in practice, the CDM is first and foremost a mechanism to generate certified emission reductions and report them in a transparent way. It is the use of the emission reductions by consumers which makes it an offset mechanism and this is why it is possible to insert a mitigation function into the CDM in a simple and transparent manner.

Some Parties have criticized the CDM as possibly deterring the transition to net mitigation by Non-Annex I countries. At the same time, Non-Annex I countries have claimed that Annex I countries take the "cheapest" emission reductions in their countries leaving them with potentially more expensive options to mitigate climate change in the future. The Host Country Mitigation SOP would be a way to overcome both criticisms, giving incentives for Non-Annex I countries to engage with domestic mitigation plans in a cost effective manner.

- 3) The Host Country Mitigation SOP would promote accurate and transparent accounting of GHG emissions and remission reductions.**

CDM methodologies have been designed to be conservative in order to ensure that excess emission reductions are not issued, and this conservativeness has also been used to explain that CDM projects do contribute to Host Country mitigation. Neither claim is adequate because the extent of the conservativeness is not quantified and varies between different methodologies whilst claims of inherent mitigation are un-reported and un-recognized.

By defining a general approach to conservativeness which can be applied throughout methodologies, it will be possible to quantify the amount of emissions cancelled/not issued to ensure conservativeness. By adding the Host Country Mitigation Share of Proceeds in a transparent manner, all of the emission reductions generated by

⁶ It is possible to argue, however, that CDM is not a pure offsetting mechanism but a net mitigation one: 1) conservative accounting regimes mean that probably about 10% of actual emission reductions are not credited; 2) hundreds of millions of CERs have been generated and not yet used; and 3) recently with the creation of the voluntary cancellation accounts in the CDM Registry, some organizations have started to cancel CERs voluntarily.

a project are identified and transparently accounted for, and both conservativeness and host country mitigation can be clearly quantified.

Host Country Mitigation SOP CERs may only be used for cancellation against a Host Party's pledges or targets, and reported in its next National Communication.

4) The Host Country Mitigation SOP is a bridge between CDM and FVA / NMBM.

CDM projects generating emission reductions for sale to capped entities in other jurisdictions are effectively acting in isolation of Host Country policies. By introducing a self-defined Host Country Mitigation SOP, CDM projects start to link with Host Country policies. For instance, when a Host Country sets an SOP for a given sector of its economy, a gateway to the FVA is created. At the pre-defined time, for example at end of its crediting period, the project activity could become fully integrated into policies implemented under the FVA. This is important because it provides a mechanism through which the host country can indicate in advance, when and how it expects facilities to start to contribute fully to host country mitigation actions rather than assisting other Parties and entities in the transition towards low carbon status.

In transitioning from a CDM project to becoming part of a host country FVA or NMBM policy, the existing CDM building blocks can continue to be used, particularly the MRV component. This kind of mechanism would provide transparency and certainty to investors and would encourage the continuation of Private Sector interest in clean development.

Examples of setting the MSOP

The MSOP may be determined by a number of factors including the following:

Host country development status and pledges / targets. Some developing and advanced developing countries have already made pledges or set targets to reduce GHG emissions or GHG emission intensity. These economies are often relatively developed and the risks for investors are considerably lower than the risks of investing in less developed economies. Host Governments may decide that an MSOP is a reasonable price to charge in return for granting permission to export CERs, and that the MSOP can be used to contribute to the host Party's pledge or target.

Other forms of financial support for the implementation of the technology from the host country including E-policies. For example a feed in tariff or renewable energy credits may provide an additional source of revenue working alongside the revenue from CERs to encourage investment in renewable energy. Whilst both streams of additional revenue are necessary for the investment to proceed (if not the project would not be additional), the host government may consider that the host economy is already contributing to the project and that a share of CERs is warranted in return. On the other hand, in a host country where there is no such support, the investors are likely to need to full share of CERs to manage the risk of investment.

Host Governments may plan to introduce other policies and measures in the future which will supersede the CDM status and issuance of CERs – for example, if the country were to introduce a national or region ETS covering the power sector, then renewable energy facilities might be included and either issued with allowances for free, zero rated for carbon emissions or lose their CERs and receive the same number of allowances. Such plans can be communicated and implemented transparently via the MSOP.

Conversely, Parties may wish to encourage investment into relatively under-developed sectors of the economy and they may decide to apply relatively lower MSOP and/or longer crediting periods in order attract investment

into these technologies, sectors or regions. For example, Host Governments are unlikely to be able to regulate domestic emissions from cookstoves whilst CDM Project developers have had significant success in developing such projects. Host Governments may decide that encouraging investment into this sector is attractive whilst investment into the renewable energy sector can be addressed through measures such as an ETS or renewable portfolio standards or feed in tariffs. Accordingly, the Government would set a low MSOP for the cookstove sector and a higher MSOP for the renewable energy sector.

Implementation measures

Host Country DNA

- Give DNAs the authority to set Host Country Mitigation SoP which could vary by technology, geography and throughout the crediting period (although all these variations should be fixed *ex ante*)
- To be communicated to UNFCCC and displayed on the UNFCCC website
- To be inscribed in the Host Country LoA and to be fixed for the duration of the crediting period
- Host Country DNAs to re-issue LoAs to existing CDM projects which voluntarily apply, so that an MSOP can be included.

CDM Executive Board

Registry

- Create Host Country Mitigation Accounts for each country defining a Host Country Mitigation SoP.
- Deduct the Host Country Mitigation Share of Proceeds at issuance
- CERs in the Host Country Mitigation Account may be cancelled against that Host Country's pledges or future targets.

For more information visit www.pd-forum.net or email gareth.phillips@pd-forum.net

About the Project Developer Forum

The Project Developer Forum (PD-Forum) is a collective voice to represent the interests of companies developing greenhouse gas (GHG) emission reduction projects in international markets under the Clean Development Mechanism (CDM), Joint Implementation (JI) and other carbon emission reduction schemes and programs.

The PD Forum's primary aims are to:

- improve the efficiency, legitimacy and functioning of the regulatory systems governing the development and use of emission reduction projects,
- influence policy developments and regulatory standards related to emissions trading and emission reduction projects,
- update and support independent standards and codes of conduct in order to further improve the integrity of the industry.

The PD-Forum is active in communicating with regulators at national, supranational and international levels and other project developers about the rules and regulations governing emissions trading and emissions reductions projects.

