

February 6, 2009

**Ad Hoc Working Group on Further Commitments
for Annex I Parties to the Kyoto Protocol**

UNFCCC Secretariat
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Dear Mr. Dovland,

IETA is writing to you to respond to the call for input concerning the issues identified in para 5 (c) (iv) of the Work Programme for 2009 of the AWG-KP, namely improvements to emissions trading and the project-based mechanisms. In our submission, which is included in an annex to this letter, IETA has directly addressed the issues noted in Annex I of document FCCC/KP/AWG/2008/INF.3 in exactly the order of that document. We hope that this facilitates your ability to take our comments into consideration. IETA appreciates the opportunity to comment, and looks forward to further developments within the AWG-KP.

Sincerely,



Henry Derwent
President, IETA

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ANNEX

IETA input on “Possible improvements to emissions trading and the project-based mechanisms under the Kyoto Protocol”

You will find below the IETA position in reference to each of the “possible improvements” included in the AWG-KP document FCCC/KP/AWG/2008/INF.3, “Elaboration of possible improvements to emissions trading and the project-based mechanisms under the Kyoto Protocol. Note by the Chair.” Each “possible improvement” is listed in bold as a heading, with the IETA position in relation to that idea in regular type directly below it.

I. Clean Development Mechanism

“A. Include other Land use, land-use change and forestry activities:”

IETA believes that if the CDM is to provide meaningful benefits to most developing countries in the short to medium term, it must include crediting for all rural land use that increases carbon stocks. Most developing countries and most of their populations are dependent on agriculture and cannot reduce overall emissions significantly without incentives for sustainable agriculture, horticulture, agroforestry and improved livestock management. The current approved methodologies for LULUCF and rules adopted in Marrakech make it impossible for such activities to benefit from the CDM and contribute to meeting the global challenge of climate change. IETA believes that the Marrakech Accords with respect to LULUCF should be replaced with simplified rules that, while maintaining environmental integrity, result in reasonably low transaction costs and the fullest possible use of the CDM. We understand, however, the concerns about impermanence that accompany many LULUCF activities. Rather than allowing these concerns to continue to delay emission reductions in these areas, however, IETA encourages the Parties and the CDM Executive Board to examine innovative approaches to dealing with these concerns. In particular, robust and reliable methods of dealing with permanence have recently been developed in the voluntary market, including the use of insurance and buffer zones, as in the Voluntary Carbon Standard. IETA urges the Parties to take advantage of these new methods to fully integrate this important sector into the CDM.

“B. Introduce a cap for newly eligible land use, land-use change and forestry activities:”

IETA opposes the introduction of a cap for newly eligible land use, land-use change and forestry activities. IETA believes that there is no longer any justification for a cap on LULUCF CDM credits, as it is clear that LULUCF projects are not sufficiently low-cost as to usher in a flood of new credits to the market. They should be treated equally with all other CDM credits.

“C. Include carbon dioxide capture and storage:”

In IETA’s view, CCS meets the objectives and criteria of the CDM and supports the ability of developing countries to contribute towards the UNFCCC’s ultimate objective of stabilizing atmospheric GHG concentrations. Many Parties agree, and have begun to use their domestic cap-and-trade schemes to incentivize the demonstration of CCS. For example, in 2008, the EU passed legislation to include CCS within the EU ETS. Under the EU ETS post 2012, CO₂ that is injected and stored according to the rules laid down in the EU’s CCS Directive will be regarded as not emitted.

IETA believes that the CDM is capable of incentivizing critical, cost-effective CCS opportunities that reduce the CO₂ emissions arising from some forms of power generation and a wide range of industrial processes (e.g. ammonia, cement production, gas processing – including liquefied natural gas production for export markets).



Various technological, methodological and legal concerns have been expressed in relation to the potential inclusion of CCS in the CDM. IETA has previously addressed these concerns in a submission to the SBSTA and hopes to contribute further to the debate in the future.

“D. Include Nuclear Activities:”

IETA believes that tackling the challenge of climate change requires such significant efforts that the widest possible range of technologies for emission reduction should be made available to the market. As such, on principle, IETA does not believe that proven mitigation technologies or techniques should be excluded from the CDM, given that environmental and public safety is protected and other forms of support they receive worldwide are taken into account.

General comments on E– G below, Relating to the development of new flexible mechanisms or sectoral CDM:

First, IETA believes that while the development and implementation of future mechanisms must build on the experiences gained in the operation of the CDM and JI, the Parties should not shy away from the development of institutional arrangements that vary significantly from them. Indeed, IETA believes that new market-based mechanisms could conceivably entail the implementation of innovative financial and regulatory regimes that, where appropriate, go far beyond the current UN mechanisms and might even contain non-UN based elements. A purely illustrative example is a mechanism entailing a non-UN external regulatory board comprised of public and private participants.

Second, IETA would like to emphasize that much work is yet to be done on how to bring the proposals conceived so far to a level of development that explains crucial details concerning timelines, data availability and collection, and market design. In particular, there seems to be no proposal explaining how economic entities will be able to generate and trade emission reduction credits within the mechanisms proposed. Going forward, such work must also include a serious consideration for the potential effects that the possibly large number of credits generated by such mechanisms could have on the global market price for carbon. IETA is doing work internally on these issues and looks forward to working with the Parties and other stakeholders to further develop proposals that incentivize private capital to meet the UNFCCC’s environmental objectives.

“E. Introduce Sectoral CDM for emission reductions below a baseline defined at a sectoral level:”

IETA supports any move toward increased standardization within the Clean Development Mechanism, as long as such moves widen the possibilities for emission reductions, lower transaction costs, and bring more predictability to the system. If the Parties agree to move forward with sectoral CDM, IETA urges the Parties to carefully consider the data availability and increased management requirements of such an enhancement to the CDM, and to plan well in advance for any new data management and governance structure requirements. In particular, IETA is very concerned about the ability of the CDM Executive Board, its supporting panels, working groups, and UNFCCC Secretariat staff to manage such a system, given the constraints of the current governance structure.

“F. Introduce sectoral crediting of emission reductions below a previously established no-lose target:”

IETA recognizes that the idea of a move to sectoral (or economy-wide) no-lose targets for some developing countries has become increasingly referenced in submissions and proposals, both from the Parties and non-governmental organizations. IETA is not opposed to the creation of



such a mechanism for some developing countries, but believes that those countries **not** involved in such a mechanism should continue to be able to access project-based and programmatic CDM.

Furthermore, IETA believes that a no-lose sectoral crediting mechanism would entail a much more complex management system, including significantly greater levels of data collection and monitoring, and, therefore, would require an approach to regulatory oversight very different from the current Clean Development Mechanism. IETA therefore believes that, if created, such a mechanism should be supervised by a dedicated body constituted by the CMP and operating under its authority, not the CDM Executive Board.

In addition, it is IETA's view that the introduction of sectoral no-lose targets with crediting below a pre-established baseline would best incentivize emission reductions if credits issued were fully fungible with AAUs, CERs, and ERUs, and if issuance of such credits were devolved to the level of economic entity, rather than issued and traded at the government level.

Finally, IETA also believes that the introduction of such credits into the international market could possibly have significant consequences on the balance of supply and demand, and therefore for the global carbon price. IETA urges the Parties to take this into consideration when designing a Post-2012 framework and hopes to contribute to the discussion on this issue more in the near future.

“G. Introduce crediting on the basis of nationally appropriate mitigation actions (NAMAs):”

In general, IETA supports the creation of market-based tools to incentivize emission reductions. We would, therefore, be interested in the development of crediting based on nationally appropriate mitigation actions, particularly if those actions occur in sectors that do not seem very suited to a project-based, programmatic, or sectoral crediting mechanism. Indeed, in the event that Parties were to create a crediting mechanism designed to compensate developing countries for the implementation of NAMAs, IETA believes that such a system should be designed to serve as a **complement**, not a replacement, for those other mechanisms.

It is also the view of IETA that a NAMAs crediting mechanism would entail a great deal of subjective decision-making as well as significantly more complex data collection and monitoring than the current CDM. It would, therefore, require the type of “hands-on” approach to governance that IETA believes that the CDM Executive Board should be avoiding now and will certainly be able to avoid once standardization reforms are implemented. For that reason, the type of regulatory oversight required for a NAMAs crediting mechanism will be very different from the current Clean Development Mechanism. IETA therefore believes that, if created, such a mechanism should be supervised by a dedicated body constituted by the CMP and operating under its authority, not the CDM Executive Board.

“H. Ensure environmental integrity and assess additionality through the development of standardized, multi-project baselines:”

IETA strongly supports the idea that the CDM Executive Board should direct the Methodology Panel or designate a new panel to define conservative standardized baselines for specific types of project activities under the CDM by pre-approving parameters and procedures for use in baseline methodologies for project types where doing so is deemed possible and where doing so will simplify and streamline the registration and issuance process for those project types. IETA believes that the current approach to establishing baselines causes insurmountable difficulties for many project types and in countries with low levels of data availability; raises



costs unnecessarily for all projects; and results in fewer projects developed and less equitable regional distribution.

In the course of the development of parameters and procedures, IETA believes that the panel undertaking this task should work closely with experienced project developers through, for example, workshops convened for the purpose of defining and designing such parameters and procedures.

IETA supports the idea that project developers should have the choice to forgo the use of a standardized, more-conservative baseline, if they prefer to undertake the additional work and bear the additional cost of establishing a unique baseline for their project activity. IETA also believes that existing projects should be able to choose whether they prefer to continue using their unique baseline or switch to a newly-established standardized baseline for their project type after the end of their current crediting period.

“1. Ensure environmental integrity and assess additionality through the development of positive and negative lists of project activity types:”

IETA strongly advocates for the integration of positive lists as a means to automatically assess the additionality of some project activities. It is IETA’s view that ensuring environmental integrity will be a simpler process, and will entail fewer transaction costs for all entities involved, if positive lists are created for some project activities. Indeed, IETA believes that the development of such lists should be made a priority by the Parties as soon as possible. Like with the introduction of standardized baselines, IETA believes that the current approach to assessing additionality causes insurmountable difficulties for many project types and in countries with low levels of data availability, and it raises costs unnecessarily for all projects. Due to project eligibility uncertainty, the current approach also results in fewer projects developed and less equitable regional distribution, as investors and project developers become increasingly less willing to risk time and money on the development of projects that may ultimately not be approved for registration.

Criteria for the creation of positive lists could be based on (1) the primary technology employed in the project activity, (2) the host Party of the project activity (due to certain technologies being common practice in some countries and not in others), or (3) the scale of the project activity (small-scale or large-scale). IETA believes that, given general direction by the Parties, the SBSTA, the CDM Executive Board, or a body of experts created solely for that purpose should be tasked with defining the specific criteria for categories of project activities for inclusion in a positive list. The entity chosen should also be tasked with deciding an appropriate procedure for the necessary periodic review of these lists over time.

IETA, supported by its many member companies, would gladly contribute to the work required for list development and review. IETA believes that registered project activities for which the project type is removed from the list should be allowed to complete the full number of crediting periods allowed, in line with the idea that retroactive decision-making should not affect the eligibility of previously registered projects.

For those project types that do not lend themselves to placement on a positive list, IETA urges the Parties and the CDM Executive Board to consider the creation of a two-step process whereby project developers may apply for and receive a CDM registration eligibility determination in advance of significant investment.



In line with IETA's view that meeting the challenge of climate change calls for the widest possible range of emission reducing technologies to remain available to the market, IETA does not call for the creation of negative lists for the CDM. If project developers choose to do the work of proving additionality and establishing a crediting baseline for a project type not included on a positive list, IETA believes that their submission should continue to be considered for registration.

“J. Differentiate the eligibility of Parties through the use of indicators:”

IETA does not advocate restricting the eligibility of Annex I Parties to the use of CERs issued through the CDM for the purpose of compliance with commitments under the Kyoto Protocol beyond the current rules and regulations.

IETA does not advocate the differentiation of non-Annex I country eligibility as such, but rather encourages the Parties to make decisions on differentiation based on the movement of Parties or sectors from one market-based mechanism to another. For example, some developing country Parties, or some sectors in some developing country Parties, may be made ineligible for the CDM as a factor of being shifted to a new market-based mechanism (such as, a sectoral no-lose target with crediting below a pre-established baseline). IETA strongly advocates against disqualification from the CDM of sectors or host Parties not covered in such an alternate scheme, however. Moreover, IETA calls for the establishment of a grace period between the decision to transition a country or sector to a new mechanism and the end of eligibility for CDM projects based in that sector or country. Such a grace period is necessary for those projects that have already been commissioned or are under development at the time that the decision is made for such a move.

“K. Improve access to clean development mechanism project activities by specified host countries:”

Rather than advocate for further special provisions for certain host countries or project activities as a means to enhance regional distribution of CDM project activities, IETA strongly urges the Parties to direct the CDM Executive Board to strengthen and consistently enforce the distinction between small-scale and large-scale projects, where small-scale baselines and monitoring do not require extensive historical data or expensive monitoring. Small businesses, government entities, and organizations in LDCs have serious difficulties obtaining data and undertaking extensive monitoring, for reason of cost and availability, yet IETA has observed that the current approach to assessing small-scale methodologies and projects does not consistently take this into account. IETA believes, therefore, that the Parties should move to adequately implement the already existent special provisions before moving to expand those to other countries or project types.

Along a similar line of thought, IETA also believes that the Parties should focus on quickly addressing the multiple barriers currently facing the development of Programmes of Activities rather than adding additional measures to try to expand CDM activities into under-utilized host countries. In a multi-page submission to the EB after a call for public input issued at EB41, IETA has outlined these barriers and proposed clear solutions to them. Adopting the solutions provided in that response will unleash the high potential for PoAs to contribute to the sustainable development of host countries that have not been a good fit for more traditional CDM project activities so far.

IETA also understands the challenges that smaller and less wealthy host countries face in setting up and resourcing DNAs, and the impact that has on the ability of project developers to move forward with viable projects in those host countries. For that reason, IETA recommends



that the CDM Executive Board work to further strengthen the DNA Forum, and examine the potential of providing increased services, including training, to smaller and poorly resourced DNAs. The aim of such services would be the establishment of well functioning DNAs so that project approvals can be provided in a timely and consistent manner.

Finally, it is IETA's view that the most effective and least-disruptive method of directing investment in CDM projects to under-utilized host countries would be to move towards the use of standardized baselines and positive lists. Doing so would lower transaction costs and project eligibility risk substantially for project developers and investors, enabling them to move into countries and project types previously thought too expensive or too risky.

Due to a concern for the environmental integrity of the CDM, IETA does not believe that it would be appropriate for projects from a select group of host countries to be exempt from the requirement to demonstrate additionality, apart from those project types specifically included in positive lists.

“L. Include co-benefits as criteria for the registration of project activities:”

IETA does not support the inclusion of co-benefits as criteria for the registration of project activities, as doing so would be likely to add additional costs and uncertainties into the project development process, further pushing project developers and investors from an already uncertain market. Moreover, the determination of which co-benefits to consider and how to measure them has been discussed before and rejected by the Parties. For these reasons, IETA supports the decision that the determination of sustainable development benefit criteria remain under the authority of the host country.

That being said, it is clear to IETA that there is a need for DNAs to take appropriate action regarding the determination of sustainable development benefit as outlined by the mandate given by the Parties. IETA would propose, therefore, that the DNA forum take a more active approach in discussing the practical implementation of this duty. In addition, IETA suggests that a joint workshop be held where DNAs and industry representatives can discuss ways that the DNAs could assess the sustainable development benefit of project activities to their country without alienating the private sector.

“M. Introduce multiplication factors to increase or decrease the certified emission reductions issued for specific project activity types:”

On principle, IETA does not advocate the use of multiplication factors to increase or decrease CERs issued for specific project activity types.

II. Joint Implementation

“A. Introduce modalities for treatment of clean development mechanism project activities upon graduation of host Parties:”

IETA believes that where a Party becomes eligible to host joint implementation (JI) projects, any registered CDM project activities hosted by that Party should continue as CDM project activities until the end of their current crediting period and that a quantity of assigned amount units (AAUs) equal to the CERs issued from this time onwards should be cancelled. This is important for the security of private sector investments and to provide for a smooth transition from one mechanism to the other. However, IETA also believes that, at the end of its crediting period the CDM project should be able to qualify for conversion into a JI project, providing that it meets the JI provisions. Such conversion should be limited to those projects that have elected to have



3 crediting periods of 7 years or are a Programme of Activities. IETA does not see a need to have specific provisions for Afforestation and Reforestation project activities.

“B. Include Nuclear Activities:”

IETA believes that tackling the challenge of climate change requires such significant efforts that the widest possible range of technologies for emission reduction should be made available to the market. As such, on principle, IETA does not believe that proven mitigation technologies or techniques should be excluded from JI, given that environmental and public safety is protected and other forms of support they receive worldwide are taken into account.

“C. Include projects that reduce greenhouse gas emissions from deforestation and forest degradation:”

IETA believes that JI should include projects that reduce greenhouse gas emissions from deforestation and forest degradation. Such credits, although likely to be limited in scale due to climatic differences, can make a significant contribution to climate mitigation and adaptation.

“D. Ensure environmental integrity and assess additionality through the development of positive or negative lists of project types:”

Although IETA is not directly opposed to the idea of positive lists for JI, we believe that the increased flexibility of JI in comparison to CDM, and the increased involvement of the host country Party, means that taking such a step to improve the predictability, consistency, and efficiency of the system is not necessary. IETA does not support the idea of negative lists for JI.

“E. Include co-benefits as criteria for the final determination for projects:”

As with the CDM, IETA does not support the inclusion of co-benefits as criteria for the registration of project activities, as doing so would be likely to add additional costs and uncertainties into the project development process, further pushing project developers and investors from a JI market that has yet to result in a significant volume of reductions. IETA does, however, advocate that host countries exercise their responsibility to ensure that projects result in sustainable development benefits for their country.

F. [Additional Issue of Concern]

The need for a determination and verification manual:

IETA believes that the Joint Implementation Supervisory Committee (JISC) should develop a determination and verification manual (DVM). IETA would like to work together with the JISC to assure that a DVM is developed in a professional and expeditious manner.

IETA notes that there are some important differences between the CDM and JI when it comes to Validation and Verification activities. One of these concerns the responsibility of Entities under JI to examine and approve methodologies when an approved CDM methodology is not being used (or where there are variations in the use of an approved CDM methodology). The skill set of an Entity that is required to assess and evaluate the suitability and appropriateness of a variation to a methodology or a new methodology is substantially different to the skill set required to check that a project is designed or operating in line with an approved methodology. It will be important for any DVM to recognize this issue, and ensure that appropriate guidance on the assessment and evaluation of new methodologies or variations to methodologies is included.

IETA believes that ISO 14064 provides a suitable framework from which the DVM could be developed. The way the ISO standard requires validators and verifiers to ask project developers questions when assessing projects as well as integrates the concept of materiality and level of



assurance could be of particular convenience when developing a DVM. Recognizing that the JISC may not have the time and resources to quickly prepare a determination and verification manual, IETA has offered to form a group that would help draft the manual and hopes to work closely with the JISC on this proposed initiative.

III. Emissions trading

[Additional Issues of Concern]

Disclosure of information on transactions of Assigned Amount Units (AAU)

IETA is mindful of the fact that some countries might be tempted, particularly in the current economic situation, to sell AAUs with very limited greening measures (i.e. “soft greening”) or without greening whatsoever (also referred to as trading “hot air”) due to the fact that greening adds to transaction costs. Insufficient monitoring and verification, however, threatens the environmental integrity and credibility of international emissions trading under the Kyoto Protocol and as a result weakens the discussion of a truly global post-2012 climate agreement. Most importantly, hot air trading will not reduce GHG emissions and will not provide any benefit in terms of addressing climate change.

IETA believes that transparency is vital to maintain the environmental integrity of the Kyoto Protocol when transacting Assigned Amount Units. As stated above, due to the AAU supply/demand balance during the first commitment period it is possible that Kyoto compliance could be achieved by Parties that have not made valuable efforts to combat climate change. IETA therefore considers that all information pertaining to AAU transactions should be publically disclosed. Transaction size, unit costs and the process by which AAUs are to be “greened” should be outlined on the UNFCCC’s website.

IV. Cross-cutting issues

“A. Relax or eliminate carry-over (banking) restrictions on Kyoto units:”

IETA does not advocate restrictions on the carry-over of Kyoto units to a subsequent commitment period as a rule. IETA does believe, however, that given the very significant impact that very large surpluses from this first crediting period could have on environmental and market outcomes in the future, the surplus must be taken into consideration when considering appropriate targets for subsequent periods.

“B. Change the limit on the retirement of temporary certified emission reductions and long-term certified emission reductions:”

IETA believes, and domestic and regional carbon markets confirm, that tCER and ICER credits are not acceptable as compliance units equivalent to other forms of carbon assets. Unfortunately, IETA believes that continuing the use of tCERs and ICERs is very likely to lead to a continuation of the lack of interest in these carbon assets as compliance units in the domestic and regional markets which underpin current CDM & JI project activities.

IETA believes, however, that it is critical that A/R project activities be incentivised and driven by the carbon market, and it is IETA's preference that CERs from LULUCF and REDD be fungible with other CERs in the future, thus leveraging the existing and future demand in the market. Robust and reliable methods of dealing with permanence have recently been developed in the voluntary market including the use of buffer zones and insurance, as in the Voluntary Carbon Standard. IETA encourages the Parties and the CDM Executive Board to examine alternative



approaches to dealing with these particular aspects of A/R project activities. IETA is very eager to support this work in any way that we can.

“C. Introduce borrowing of assigned amount from future commitment periods:”

IETA does not advocate the introduction of borrowing AAUs from future commitment periods, as doing so might create uncertainty in the market about the level of demand. In place of allowing Parties to borrow AAUs from future commitment periods, IETA urges the Parties to consider the establishment of longer commitment periods as a means of giving economic entities more flexibility in planning for and meeting their compliance obligations.

Concluding Note

Many of the proposals discussed above represent a real challenge for the AWG–KP and for the negotiations, which IETA hopes very much can be concluded in Copenhagen. Many of the paragraphs above are necessarily general, but there is an urgent need now to become specific, and to deal with the details of them in the near future. Many of the proposals need to be examined from the perspective of the financial sector, if there is to be any chance of the substantial private sector investment and contribution that the Parties, the UNFCCC Secretariat and other stakeholders are all looking for. IETA’s members have helped turn the CDM into a major success. They are very keen, and very well placed, to ensure that the expansion of the CDM, and the design of possible additional instruments, is effective and attracts maximum private interest. We will be working on the AWG–KP’s agenda throughout 2009 and hope that we will be able to engage with you in doing so.