PROJECT
DEVELOPER
FORUM

Submission to Subsidiary Body for Implementation

Possible changes to the modalities and procedures for the Clean Development Mechanism

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Summary

The PD Forum recommends that the Parties make significant changes to the CDM Modalities and Procedures in order to address the shortcomings identified and to create a reformed and solid market mechanism which is capable of:

- identifying and promoting material and cost effective emission reductions in countries, regions and sectors which are not, or not yet, covered by cap and trade systems;
- contributing to sustainable development;
- promoting private sector investment; and
- promoting enhanced ambition for GHG mitigation by developed and developing nations as requested by parties and COP18.

The PD Forum's suggestions to promote these objectives through the reform of the CDM Modalities and Procedures are summarized below and detailed in Annex 1.

PD Forum envisages three possible development pathways for the CDM, each leading to a role of different relevance in the international climate policy architecture:

i) the CDM becoming a voluntary tool and a means of verifying mitigation outcomes for payments by results, effectively an MRV service provider for other mechanisms and approaches;
ii) the CDM being used as the basis for host country emission reduction projects to supply credits to domestic ETS; or
iii) continued and enhanced use of the CDM as a universal project based mechanism to link uncapped environments and sectors to the existing and emerging emission trading schemes in developing and developed economies. In this role the CDM will effectively play an important role to indirectly link the different emission trading schemes as suggested by the International Energy Agency[1].

We believe that a reformed and efficient CDM controlled by a regulatory body is capable to play each of these three roles in the future. This,together with significantly increased ambition by Parties –will allow the CDM to play a significant role in future efforts to combat climate change, and to pave the way to a more comprehensive and efficient climate architecture with enhanced ambition by all parties. Please see Annex 2 for a discussion of how we see the international architecture evolving. To fulfill these roles, significant changes to the Modalities and Procedures are required.

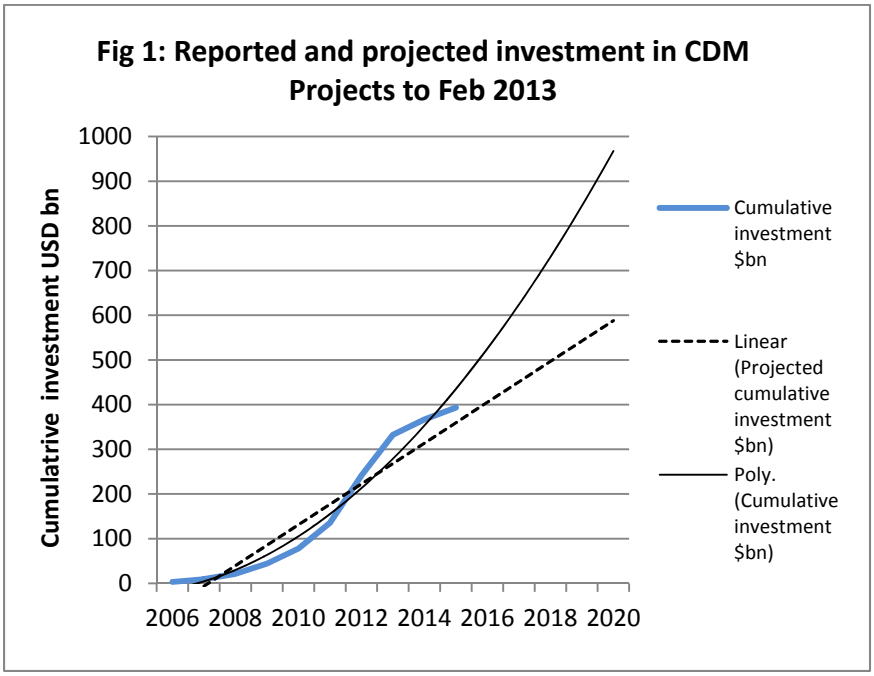
[1] According to the World Energy Outlook 2011 a 450 ppm policy scenario implies that carbon prices in OECD shall rise to about 120 USD/tCO2 by 2035 while other major economies will see prices rising from 20 USD/t in 2020 to 90 USD in 2035. In this Scenario indirect linking with adequate offsets is needed to warrant cost effectiveness.

Overview of recommended changes to the CDM M&P

- Make the CDM available to all Parties as well as the international transport markets covered by ICAO and IMO.
- Change the Executive Board's responsibilities to be Supervisory. Increase membership and eliminate the concept of alternate members, and at the same time, renaming the Executive Board "the Board" .
- Define procedures based on the principles of the "rule of law", such as independent control and the right to appeal, which are essential to attract investors.
- Allow Non Annex I countries to use CERs in their own sectoral or regional Emission Trading Schemes or implement Host Country Mitigation Share of Proceeds as appropriate. See annex 3 for a description of the Host Country Mitigation Share of Proceeds.
- Request the CDM Board to develop principles for the management of conservativeness in CDM methodologies such that conservative factors are not compounded within methodologies but rather are defined consistently and accounted for in a transparent manner, and that conservativeness is spread fairly across all methodologies according to rational principles.
- Request the Board to quantify the total conservativeness in requests for issuance, and report annually to the Parties, the total number of CERs which have been held back under the auspices of conservativeness.
- Define the responsibilities of DNAs and significantly strengthen them, in preparation for future involvement in FVA and NMBM.
- Continue to strengthen the environmental integrity of the mechanism by conducting a review of the duration of crediting periods and in particular, seeking inputs from stakeholders to better understand the impact of the duration of the crediting period on investment and operational decisions, creating automatic additionality lists and further developing standardized baselines.
- Abandon the concept of small scale projects as these are no easier than "large scale" "" CDM projects.
- Recognize that the CDM is capable of identifying least cost abatement opportunities and contributing to their economic viability, but that other policies such as access to adequate financing are needed to assure their effective implementation.
- Warrant the synergy of the CDM with host country mitigation (NAMA) policies as well as with the financial policies and instruments of Multilateral and National Development Banks as well as with the future Green Climate Fund.
- Move PoA into a NAMA framework – without small scale barriers there is no barrier to scaling up activities
- Move afforestation and reforestation out of the CDM and into the REDD+ mechanism where they can be dealt with in a more appropriate way.
- Prepare the CDM 'infrastructure', including the methodologies, DOEs, DNAs as well as governance structure, such as the expert panels, to become a service provider to new approaches such as FVA and NMBM.

Background

The global carbon market has been highly successful. The CDM has mobilized investments of USD 215 billion in emission reductions[2], mostly from the private sector. The CDM was on track to generate to promote cumulative investments between USD 600 billion and USD 1 trillion into clean energy and low carbon technology by 2020 (Figure 1).[3]



As demand has fallen away, investment is declining to levels which threaten the existence of the CDM and the capabilities and capacities which have been created to operate it. Despite its success, Parties and stakeholders have indicated that they want to see changes to the CDM before demand is re-created. Accordingly the PD Forum agrees and believes that reforming the CDM must be the priority, and that the reform shall aim to ensure the CDM's compatibility with the principles and mechanisms defined by and developed under the ADP. Furthermore, the CDM must remain operational to bridge the gap until 2020 when – hopefully – a new global framework will enter into force. We therefore believe that a reformed CDM which is capable of generating additional and permanent emission reductions in a cost efficient and effective manner is a key element to progress towards enhanced ambition from developing and developed countries. A reformed CDM also represents the foundations for the development of New Market Based Mechanisms and for the establishment and the indirect linkage of emission trading schemes in developed and developing countries. This is essential not only to raise demand for CERs and therefore emission reductions in the short term, but also to prevent the

[2] 'Benefits of the CDM up to 2012', UNFCCC (2012), see http://cdm.unfccc.int/about/dev_ben/ABC_2012.pdf.
[3] UNEP RISOE CDM Pipeline February 2013. Cumulative investment is the sum of investments reported for projects at validation, requesting registration and registered.

technological lock-in which is taking place in developing countries and which threatens the viability of the objective to limit climate change to 2°C

It is therefore incumbent upon the Parties to take this once in a decade opportunity to reform the CDM substantially and significantly to address, once and for all, criticisms from stakeholders and Parties.

It is important to distinguish between changes or adaptations which can be made via the annual round of Guidance to the CDM EB and reforms which need to be addressed via the Modalities and Procedures.

The PD Forum believes that there are significant changes which need to be made via this review and we urge the Parties to do more than enough to clear the barriers which are obstructing the future of the CDM, rather than fail by doing too little.

Introduction

PD Forum foresees three potential non-exclusive but incremental roles for the further development of the CDM:

1) Unless significant reform of the CDM together with significant increase in ambition by all parties is demonstrated, the international community will move away from using the CDM as a step towards global carbon markets and as an indirect link between emissions trading schemes. As a result, policy makers will seek to establish different mechanisms which will still need to address the challenges faced by the CDM and precious time, experience and resources will be lost until alternatives are developed. National governments will pursue their own policies without any overarching framework for MRV, offsetting or indirect linking of emission trading schemes and important opportunities for meeting a common goal, benchmarking and institutional learning will be lost. Isolated emission trading schemes without access to international offsets will have to rely on price and supply control mechanisms such as funds which buy and sell allowances until politically driven decisions to link different ETS are accomplished in the future. Until excess allowances are worked out of the system, caps are unlikely to trigger real action. The CDM meanwhile will no longer be relevant to domestic ETS or internationally binding targets and may be used for voluntary action and as a means of paying for mitigation by results. We foresee little demand for voluntary CERs as the voluntary market is already thin and addressed by several existing schemes which in some stakeholders' eyes are superior to the CDM. The methodologies and validation / verification process is a good means of verifying delivery of emission reductions prior to payment, but is probably over-burdened by the EB and its panels to achieve this result. Donors may wish to add their own criteria and borrow from the CDM model rather than use it in its current format.

Under the Scenario, CDM has very little role in the future and an important opportunity to prevent the technological lock-in in developing countries will be lost by the time alternative policies have been developed and agreed from scratch.

2) A more comprehensive role for the CDM would be that it is taken up by host countries as a means of promoting domestic project activities to supply flexibility to their own emerging emission trading schemes. This is a sensible move because domestic ETS in developing countries will only be limited to regions and sectors which are mature enough while other mitigation opportunities in less developed parts of the country or sectors of the economy can be bound in with the CDM to implement low cost abatement opportunities. This approach will recognize that many parts of developing countries have achieved a reasonable level of economic development, but that there are still sectors (for example landfill gas, coal mine methane, waste water treatment and deployment of energy efficient devices) or regions (for example poor and under developed regions in China or Brazil) that are hard to regulate under an ETS. Low cost abatement opportunities mean that additional allowances (i.e. emission reduction units) can be supplied into an ETS to meet the aggregate emission reduction cap and broaden the mitigation activities beyond the scope of the ETS itself, but this implies that the offsets that are being used are real, additional and permanent, which are the key strengths of the CDM. However, as domestic entities take over from the CDM EB in administering the scheme such as is proposed in China's developing ETS, or develop their own voluntary schemes, it will be difficult to avoid the inevitable conflict of interest, where easier standards result in more cheaper offsets, further reducing the costs for industry to comply with the cap. This "race to the bottom" will result in projects with lower environmental integrity, weaker baselines and less international scrutiny which in turn will inflate caps and undermine the overall environmental goal whilst on paper, targets will be achieved. In addition to this, the opportunity for indirect linking of emission trading schemes as well as the foundation for "comparability of efforts" is lost.

Under this scenario, CDM will go through years of uncertainty until developing countries define their approach; there will be a real risk that it will lose its environmental integrity and transparency; and existing resources will be lost in the process.

3) The most comprehensive and promising role for the CDM, which comprises many of the elements above requires that all Parties continue to use the CDM as the main international project-based mechanism to provide flexibility to both domestic and international emission trading schemes[4]. As more and more countries develop domestic Emission Trading Schemes the indirect linkage which the CDM currently provides for the Kyoto Protocol, the EU ETS and the Australian CPL will be seen as a key benefit which will not only facilitate the establishment of new schemes, but also help to align criteria and principles which will facilitate future direct linking. In addition to this, the universal use of the CDM will safeguard the possibility to compare

[4] Joint implementation is the other project based mechanism which may be used between capped entities.

costs and efforts of different systems. A reformed CDM will continue to be the sole mechanism for some time but will act in synergy with NAMA policies and the emerging carbon financing policies of Multilateral and National Development Banks as well as the Green Climate Fund once active. This experience will give a conceptual boost to the development of New Market Based Mechanisms and represent a significant element of the Framework for Various approaches. To make the CDM fit for this role, the Parties need to make significant changes to its Modalities and Procedures in order to meet stakeholders' and buyers' expectations. Governance needs to be improved, environmental integrity strengthened and issues such as its contribution to host country sustainable development, NAMA policies and domestic mitigation ambitions as well as the management of Letters of Approval need to be addressed if the mechanism is to have a chance of meeting long term expectations.

Under this scenario, the CDM can be reformed and its operational resources on all levels can be safeguarded. Meaningful mitigation can be promoted in the critical years to come and technological lock-in can be minimized until other more comprehensive policies and mechanisms are in place. Under this scenario the CDM can promote ambition by all parties, pave the way for New Market Mechanisms and promote the increasing establishment and indirect linking of ETS which are crucial to progress towards an efficient global carbon market.

Today only the CDM is capable to take up this comprehensive role and offer a real chance to help the world meet its most demanding targets to significantly reduce emissions by 2050.

These scenarios and what they mean for the CDM / FVA "building blocks" are summarized in Table 1 below.

Table 1: Three non-exclusive development scenarios for the future of the CDM and some of the main implications of each role.

	Governance – EB, DNAs, appeals, transparency, transaction costs	Environmental Integrity – additionality, baselines	Independent verification and accreditation of verifiers	MRV – technical issues, methodologies, accuracy / uncertainty	Host country - Sustainable development (SD); host country mitigation; Letter of Approval (LoA)
1) Niche market for voluntary offsets and payment by results for funds and donors	Governance less important as efforts address voluntary markets, not compliance. Appeals less important; transaction costs less critical	Highly important for voluntary market; payments by result against donor specified criteria;	Important for payment by results and voluntary markets. Most voluntary schemes recognize CDM accreditation rather than run their own accreditation programmes	Already good; continued improvements available; may place more emphasis on dispersed / household level activities / PoA	SD on the basis of voluntary reporting template will substitute host country SD priorities and LoA procedures while mitigation result might be less relevant.
2) Supplier of offsets to unlinked domestic ETS	EB less important as host Parties may take responsibility for registration and issuance; DNAs assume greater responsibility Comparability of efforts is compromised	Remain important but likely to result in lowering of standards as host parties seek cheaper offsets to minimize costs of ETS for domestic industry	Important but will migrate to domestically accredited verifiers or move to international accreditation under ISO standards.	Standards should be maintained and built upon as they compliment host country ETS MRV requirements Comparability to be safeguarded.	Little incentive to maintain sustainable development and host country mitigation element as the process is internalized within host country boundaries; LoA becomes irrelevant.
3) Supplier of internationally fungible units to link sectoral / regional ETS of different economies Support NAMA and MDB carbon financing to promote GHG mitigation in uncapped environments.	Further improvements required, especially the role of EB (supervision versus executive function); appeals; transaction costs	Continued progress on improving environmental integrity required whilst reducing transaction costs	Remains central to the integrity of the mechanism and requires that the Board develops under the principles of "rules of law" including independent control and the right to appeal	Scope exists to continue to improve technical aspects, treatment of uncertainty, efficiency etc	More work required on confirming and demonstrating that projects deliver sustainable development benefits; steps to guarantee host country mitigation and better management of LoA.

Review of the CDM Modalities and Procedures

The PD Forum's recommendations for the review of the CDM have been organized broadly in line with the existing headings of the Marrakesh Accords. Our suggestions, together with justification for each recommendation and specific textual proposals against existing text are included in Annex 1.

The intention of these recommendations is to create a mechanism which delivers very high quality emission reductions units which:

a) Contribute to the host country's sustainable development;
b) Identify and implement cost effective GHG mitigation opportunities in uncapped environments to prevent the establishment of long term fossil fuel dependent infrastructure (lock-in) until more comprehensive mechanisms are established.
c) Help capped Parties and entities meet their targets in a cost effective manner; and
d) Facilitate the increase in mitigation ambition by developed and developing parties as recommended by the Decisions taken by COP 18

In addition, they aim to *inter alia*:

- Create a Board which is truly supervisory in function, and can respond to the international community's expectations of the CDM and accordingly, make rational decisions about the kinds of technologies which deliver CERs;
- Reform the CDM to be fit for its role as a foundation for the development of New Market Mechanisms as well as for its role in the Framework for Various Approaches to act in synergy with NAMA policies as well as financing mechanism implemented by Multilateral and National Development Banks as well as the Green Climate Fund;
- Make the CDM available also for Non Annex I country mitigation ambitions which might be related to sectoral or regional Cap an Trade systems which cover part of their economies or as a possibility for host countries to Monitor Verify and Report as well as bank the results of their NAMA policies by establishing Host Country Mitigation Share of Proceeds on their projects. Such measures create an opportunity for Host Parties to better control the sectors and regions as well as kinds of investments and technologies which should be covered by the CDM versus those which should be covered by more comprehensive mechanisms such as ETS. Such a mechanism will empower Host Parties to shape their mitigation policies whilst at the same time, retaining the CDM Board's centralized functions of standard setting, registration and issuance;
- Enhance the environmental integrity of the CDM, remove un-necessary barriers and restrictions, focus on the core function of registering emission reduction projects which can issue credits which the markets want to buy;
- Define the roles and responsibilities of DNAs;
- Enhance the efficiency of the mechanism and reduce costs for the Secretariat.

Recommendations in brief

Purpose

- Recognize the capability and value of the CDM to identify, promote as well as measure verify and report on additional emission reductions in sectors and regions not (yet) accessible to emission trading.
- Position the CDM as an indirect linking mechanism between different existing and emerging emission trading schemes.
- Broaden the scope of the CDM allowing all countries and international transport covered by ICAO and IMO to purchase and surrender CERs.
- Define a range of parameters to assess regional and sub-regional distribution including projects or CERs per head of population; per GDP and per MT GHG emissions.

Governance

- Redefine the Board's responsibilities to be supervisory with executive functions discharged via panels and the Secretariat. Consequently rename the CDM EB the Board. The Board "shall" establish committees rather than "may".
- Increase membership to 24 including 2 from civil society and 2 from the private sector.
- If alternate members remain, remove the provision that "terms as alternate members do count".
- Appoint an Executive Director of the CDM to ensure the Secretariat and Panels function efficiently and transparently.
- Develop procedures which warrant fairness, independent control and the right to appeals and other relevant principles of the rule of law[5] to make sure that the mechanisms is a solid foundation for investment decisions.

Environmental Integrity

- Review accreditation procedures for DOEs improving efficiency, addressing professional negligence and fraud, and defining insurable risks for DOEs who are responsible for significant deficiencies.
- Continue with the development of standardized baselines and develop lists of technologies which Parties consider to be automatically additional.
- Review the duration of crediting periods and call for input from stakeholders to better understand the impact of the duration of crediting periods on investment and operational decisions.

[5] An analysis of the gaps and reform opportunities has been prepared by Charlotte Streck and Jolene Lin in "Making Markets Work: A Review of CDM Performance and the Need for Reform", available from http://ejil.oxfordjournals.org/content/19/2/409.full

- Revise existing methodologies to determine the best estimate of emission reductions generated and then apply a transparent and reasonable adjustment factor as a basis for the issuance of a conservative volume of CERs. The Conservativeness factor shall be determined in a transparent manner following guiding principles defined by the Board such that conservative factors are not compounded within methodologies but rather are defined consistently and accounted for in a transparent manner, and that conservativeness is spread fairly across all methodologies according to rational principles. This shall allow transparently disclosing, quantifying and documenting the unaccredited net mitigation result of CDM projects.
- Annually, the Secretariat shall calculate the number of ERs which have not been issued as CERs (or retired in a separate conservativeness account) due to the application of the conservativeness factor and this shall be reported to the Parties.
- In the event that significant deficiencies are identified in the activities for DOEs, any over-issuance of CERs will be offset against the total Conservativeness factor for the period(s) in question. The offset will be transparently calculated and reported to the Parties.
- Revise all methodologies to include a single uncertainty threshold which the monitoring plan must not exceed. Remove references to arbitrary uncertainty criteria for specific metering devices.
- Build on the fact that the CDM can identify least cost mitigation opportunities and increase their economic attractiveness, but that other policies such as adequate financing facilities are needed to assure effective implementation. To achieve that the reformed CDM must warrant the synergy with national mitigation policies as well as the financing mechanism of Multilateral and National Development Banks and the future activities of the Green Climate Fund.

Monitoring, reporting and verification

- Allow the monitoring plan for a project to be elaborated either prior to validation or prior to the first verification, after the project has progressed in its design when a more accurate monitoring plan can be defined.

Host and Non-Host Country issues

- Define the role of Host and Non-Host Country DNAs
- DNAs shall provide criteria related to national regulations and legislation which projects must fulfill as required in order to gain and retain their Letter of Approval. DNAs shall elaborate transparent procedures for withdrawal of LoAs, but only as a measure of last resort and at the end of a crediting period and with procedures for appeal and following the rule of law.
- Host countries shall develop procedures for local stakeholder consultation and confirm in the Host Country LoA whether such procedures have been fulfilled
- Host Countries may define an optional Host Country Mitigation Share of Proceeds which will be deducted at the point of issuance and transferred into a newly created Host Country Mitigation Account which shall be used towards host country pledges or targets.

- In a further step to promote GHG mitigation in their economies Host Countries may use CERs from CDM projects as flexibility instruments for their own domestic ETS.
- Host Country DNA's shall prepare lists of E+ and E- policies which shall be taken into consideration during the validation of both additionality and baselines of CDM project activities.

Additional recommendations

- Remove the arbitrary classification of small scale projects as there is practically no difference between the validation and verification process for small and "large" scale CDM projects.
- When a NAMA framework is established, migrate PoA out of CDM and into NAMAs.
- Where CDM is applied in synergy with host national sectoral policies this can be developed into a sectoral mechanism.
- Migrate afforestation and reforestation activities out of the CDM and into REDD+.

Conclusion

The PD Forum believes that this package of proposals is sufficiently strong to alter the nature of the CDM such that buying Parties are willing to consider using the CDM once more. Failure to change the CDM sufficiently will mean that the mechanism is highly unlikely to play any significant role in international efforts to mitigate GHG emissions under a future agreement. Failure to reform the CDM and to boost demand for CERs in the short term will not only destroy the skills, infrastructure experiences and resources which have been built, but also contribute to the lock in of GHG emissions by continued fast expansion of fossil fuel intensive infrastructure in developing countries. To revert such a lock in the IEA estimates that each USD not invested today will require an investment of 4.5 USD in the period after 2020. For this reason the CDM is the key opportunity to contain the cost of GHG mitigation as we cannot wait for the establishment of new and alternative regulations.

Annex 1: Detailed proposals for review of the CDM Modalities and Procedures.

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
1	**Decision 3 CMP.1 Preamble** Bearing in mind that, in accordance with Article 12, the purpose of the CDM is to assist Parties not included in Annex I to the Convention in achieving sustainable development and in contributing to the ultimate objective of the convention, and to assist Parties included in Annex I in achieving compliance with their QELRCs under article 3 of the Kyoto Protocol. It is proposed that the CDM can also be used by Non-Annex I Parties to help achieve voluntary targets as the CDM offers access to least cost abatement opportunities with a high level of environmental integrity. Excluding non-Annex I Parties from the use of CERs penalizes them by making abatement more expensive or by lowering the standards of environmental integrity. Allowing them to use the CDM and CERs in complementation to national policies, targets and emission trading schemes provides them with an efficient tool to monitor, verify and report the results of their efforts will lay the fundament for the use of more comprehensive market mechanisms and ultimately reduce cost and increase their ambition. International emission sources arising from travel and under the auspices of ICAO and IMO shall be granted access to CERs for the purposes of offsetting emissions.The universal use of CERs as offsets by different countries and the international emission sources will safeguard comparability of efforts and the indirect linking will increase global cost efficiency, which is paramount in times of economic austerity.	*Bearing in mind that, in accordance with Article 12, the purpose of the CDM is to assist Parties not included in Annex I to the Convention in achieving sustainable development and in contributing to the ultimate objective of the convention, and to assist Parties included in Annex I in achieving compliance with their QELRCs under article 3 of the Kyoto Protocol <u>and to assist all Parties in implementing their NAMA policies and in achieving corresponding voluntary targets and pledges</u> . Entities generating sources of international emission from travel and under the auspices of ICAO and IMO shall be granted access to CERs for the purposes of offsetting emissions.*

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	Decision 3/CMP.1 Para 3 Invites the EB to review the simplified modalities, procedures and the definition of small-scale project activities referred to in Para 6 c) of decision 17/CP.7 and if necessary, make appropriate recommendations to the COP…. Small scale project activities under the CDM have become an unjustified restriction on the development of project activities that often deliver high levels of sustainable development to rural communities and an unnecessary burden on project developers and DOEs.. Validation of many small scale projects is now more demanding than validation of normal scale projects – the PDDs are almost identical except that the small scale PDD requires proof that the small scale project is not a debundled large scale project. The only advantages of small and micro scale projects is that some benefit from automatic additionality and they benefit from not needing to perform the common practice analysis. If automatic additionality is granted to technologies in regions which are under-represented then surely bigger projects would deliver bigger benefits to all. It is proposed to remove the arbitrary small scale classification and allow projects of any size to be developed, including those which deploy positive list technologies and benefit from automatic additionality. The Common Practice tool, which can be demanding to implement, should be waived for projects which are expected to deliver on average less than [50,000] CERs per annum. This will also reduce the transaction costs for the validation and verification process and reduce the complexity and workload for the Secretariat, Panels, Board and DOEs It is also worth noting that these steps will encourage more projects to use the positive technology list, technologies with automatic additionality and technologies with standardized baselines. As a result, the use of the additionlaity tool will reduce, which will in turn reduce transaction costs, administrative burden and much of the criticism about additionality within the CDM. Existing small scale methodologies should be reviewed for conversion to “normal” scale methodologies.	Delete preamble paragraph 3

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	Decision 3/CMP.1 Para 4 bis The CDM's role, as defined in option 3 in the introduction to this paper, foresees the need to ensure that the CDM is used as the main mechanism for linking current and future ETS implemented at international, national, domestic, regional and sectoral levels. Failure to do so will result in the proliferation of standards and emission reduction mechanisms and the resulting race to the bottom, losing environmental integrity and transparency on the way. At the same time, buying Parties want to see the CDM contributing to host country mitigation, which can be achieved by either the deduction of a Host country mitigation share of proceeds at issuance or the use of CDM projects for domestic ETS in non-capped economies. The CDM also needs to be able to work hand in hand with other national mitigation policies such as E-policies (eg feed in tariffs, renewable energy credits, etc) and the development policies of Multilateral and National Development Banks. Such a synergetic use of economic instruments is capable to generate structural change which will lead to significant additional and permanent emission reductions which can be monitored, verified and reported on the basis of the high universal standards established by the CDM.	*Decision 3/CMP.1 Para 4 bis invites the Executive board to take steps to enable the CDM to transparently contribute to mitigation beyond efforts in Annex 1 countries by ensuring that the CDM continues to be used as a basis for linking international and domestic emission trading schemes in both Annex 1 and Non-Annex 1 countries; allows for the optional implementation of a host country share of proceeds in Non-Annex 1 countries to be offset against pledges and future targets; allows for the use of CERs as offsets in domestic emission trading schemes to be established by developing countries, and that the CDM can be used in conjunction with other national mitigation policies, NAMAs, and financing mechanisms of Multilateral and National Development Banks and the future activities of the Green Climate Fund.*
	Annex Para 4c and 5h: The COP/MOP shall further…. Review the regional and subregional distribution of CDM project activities with a view to identifying systematic or systemic barriers to their equitable distribution and take appropriate decisions, based, inter alia, on a report by the EB Equitable distribution has never been defined and the interpretation of absolute number of projects or absolute number of emission reductions is inequitable. This has resulted in a desire to positively encourage the development of CDM project activities in some Parties and has influenced buying policies amongst other Parties. Ranking distribution by GDP, population or per capita emissions, for example, yields very different results, with neither China nor India being over-represented. The potential for GHG emissions reductions is closely linked to total GHG emissions from an economy. And since the CDM is a market based mechanism, it is not unreasonable that the market will produce project activities in proportion to availability. If Parties wish to see more projects in specific localities, they might utilize positive technology and geographic lists to promote specific technologies which are under-represented in certain countries. Where shortcomings and need for adjustment is identified the CDM shall be used in synergy with other tools such as Multilateral d=Development Bank Financing, support by the Green Climate Fund such as financing, sovereign guarantees, political risk insurance, as well as capacity building.	*Review the regional and subregional distribution of CDM project activities <u>against a range of denominators and define steps to encourage the development of CDM project activities involving desirable technologies and technologies which have application potential in under-represented regions.</u>* *<u>Where necessary and appropriate seek to combine the CDM with other Tools and Mechanisms which allow to overcome the applicable investment barriers..</u>*

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	Para 5. The Executive Board shall supervise the CDM under the authority and guidance of the COP/MOP. In this context the EB shall…. Sub-para a through p The EB is created to supervise the CDM however the tasks listed in a) through p) and particularly p) which leads on to paras 38, 41 and 65, take the EB well beyond supervision and into the realms of practical execution. Compared with the governing instrument of the Green Climate Fund, the EB has significantly more executive function than its supervisory role should permit; there is no clear delegation of executive function to the Secretariat; there is no Executive Director of the CDM (the Executive Secretary is responsible for all of the UNFCCC and cannot undertake this role for the CDM). Accordingly, the CDM EB should be renamed as the CDM Board (CDM Board or the Board) and the list of tasks for the CDM Board should be revised to ensure that they are either of a supervisory nature or if executive, then that executive function is limited to final approval of recommendations from the Secretariat, with the authority to intervene when they consider it necessary. Board members would gain executive responsibilities by Chairing panels, committees and working groups. So for example, the Board will not discuss the technical details of a new methodology. They will either accept or reject a recommendation on the basis of whether or not that methodology will contribute to the overall achievement of the objectives of the Framework Convention, The Board's responsibility shall extend to cover not only the supply of CERs from registered projects but also the demand from Parties to purchase emission reductions which are real, long term and permanent and which result in a beneficial distribution of carbon revenues for the promotion of sustainable development. The Board shall be aware that demand for CERs is influenced by public perceptions of the CDM's credibility and integrity and the Board shall take steps to ensure that the CERs produced by registered projects are universally accepted and not prone to additional qualitative restrictions. The Board shall form Panels chaired by Board members, with staff from the Secretariat and external experts who will prepare recommendations for the Board's approval. The Secretariat should be clearly tasked with the transparent and accountable execution of the CDM Board's guidance and the post of an Executive Director should be created. Looking to the future, the CDM Board may consider expanding its role to become the Board of the Flexibility Mechanisms (BFM) such that the BFM can guide the future development of the New Market Based Mechanism and the Framework of Various Approaches with the executive function provided by (an expanded) Secretariat and Executive Director.	*C. Board* *5. The Board shall supervise the CDM, under the authority and guidance of the COP/MOP, and be fully accountable to the COP/MOP. In this context the Board shall where necessary establish committees and panel to:* *a)* *b)* *c)* *d) remove reference to Appendix C* *e) remove* *f)* *g)* *h) Report to COP/MOP on regional and sub-regional distribution of CDM project activities and infrastructure and reduce barriers to under-representation* *i)* *j)* *k)* *l)* *m)* *n) Establish a panel to address issues relating to observance of modalities and procedures for the CDM by project participants and/pr operational entities and report on them to the COP/MOP* *o)* *p) Establish one or more panels to carry out other functions ascribed to it in decision 17/CP.7, the present annex and relevant decisions of the COP/MOP.* *q) Establish a panel and procedures to hear appeals from stakeholders concerning decisions of the Board.*

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	Para 7; Composition of the EB (now CDM Board) Reference is made to the Board of the Green Climate Fund. It is proposed that the CDM Board is expanded to have 24 members with no alternates. The Board will contain [two] representatives from each of Private Sector Organizations and Civil Society Organizations and representatives from other stakeholder groups as well as the Parties who are signatory to the Kyoto Protocol.	*The Board shall comprise 24 members from Parties to the Kyoto Protocol as follows….. including two representatives from each of Private Sector Organizations and Civil Society Organizations.*
	Para 8: Membership of the EB (now CDM Board) 8b) "terms as alternate members do not count". In the event that alternate members continue (contrary to our proposal in para 7 above), then this text should be deleted as it has allowed individuals to maintain a long term position on the Board, entrenching certain beliefs and excluding new participants from the Board. Attention is drawn to the significant time commitment, the expertise requirements and the conflict of interest provisions. EB members are elected for a two year term and should serve that term unless prevented by personal circumstances. Tagging of seats, whereby a different member takes over in the second year should not be permitted as this impacts upon the continuity of decision making and institutional knowledge; turnover of members is already addressed through the membership rules. To enhance the experience and understanding of Board and Secretariat staff, training programmes should be run involving site visit(s) and meetings with PPs and stakeholders to fully understand the scope of the CM activities on the ground. It is assumed that Board members will interact with DNAs and DOEs at roundtable events and DOE / DNA Forum meetings.	*8* *a)* *b) Delete "Terms as alternate members do not count"* *c)* *9 Delete*
	18. The Executive Board may establish committees…. At the moment the establishment of panels and committes is optional but this should be strengthened to "SHALL" in order to enhance the executive involvement of Board members in Panels	*18 The Board <u>shall</u> establish committees….*

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	Para 19 bis: Rule of law The Board shall work to develop procedures consistent with internationally accepted principles of "rule of law", including appeals, the right to be heard, the right to defend, non-retrospective application of rules and the creation of precedence. In particular, the Board will create an independent appeals process to hear appeals against positive and negative decisions by the Board. The Appeals process shall provide one single, fair, transparent and fact-based appeals procedure; where decisions by the appeals panel form persuasive and binding precedents for future decisions of the appeals panel and Board respectively; with the requisite checks and balances to ensure that the system is not abused; that costs of successful and unsuccessful appeals are fairly apportioned; which covers the decisions by the CDM Board; which is carried out by an Independent Appeals Panel made up of external experts and Secretariat staff as appropriate; and which ensures a form of direct communication through which the directly affected stakeholders can interact with the appeals panel.	*19 bis* *a) The Board shall work to develop or revise and implement rules and procedures which are consistent with internationally accepted principles of the" rule of law"* *b) The Board shall establish and operationalize an appeals process following guidance from the COP/MOP within one year of receipt of Guidance.* *c) The Board shall establish an Appeals Panel to implement the Appeals Procedures.* d) *The Board shall report to COP/MOP on the activities and decisions of the Appeal Panel.*

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	Section C bis: Designated National Authorities A new section shall be inserted providing direction for the establishment and responsibilities of Designated National Authorities. Host Country DNAs will, *inter alia*: • Develop and implement procedures for the timely issuance of Letters of Approval which shall include: o Confirmation that the proposed project activity contributes to host country sustainable development o That the local stakeholder consultation has been undertaken according to relevant guidelines o Any requirements to be fulfilled in addition to existing regulations and permitting requirements, failure of which may result in the temporary suspension or ultimate withdrawal of the Letter of Approval • Project assessment by the DNA shall occur on the basis of the conclusion of the Global Stakeholder Consultation and in parallel to the project validation. • Develop and implement procedures for the fair and transparent suspension or ultimate withdrawal of a Letter of Approval at the end of a crediting period (see PD Forum's submission to the EB on this subject at http://www.pd-forum.net/files/874f1e6114188653f3931f9ec0ce1c0c.pdf) • Develop and publish lists of E+ and E- policies which PP's may use in the establishment of baselines and additionality for CDM project activities • Develop and implement procedures for linking registered CDM project activities with registered NAMAs to avoid double counting • Procedures for the development and approval of standardized baselines to establish host country mitigation contributions from registered CDM projects, varied by technology, geographic region and project age if necessary, and publication thereof • Participation in regional DNA Forum activities • Etc. Non-Host Country DNAs will, inter alia: • Develop and implement procedures for the issuance of letters of Approval • Consider whether, in the Host Party's opinion, applicant projects contribute to the objectives of the Framework Convention • Undertake adequate due diligence to ensure that projects are genuine • Develop, and implement where necessary, procedures for the temporary suspension or withdrawal of an LoA. • Participate in regional DNA Forum activities Etc. With regard to optional procedures to establish host country mitigation contributions, it is proposed that host country DNAs are given the authority to set a share of proceeds by a combination of project type, location or age, in order to collect CERs as a contribution towards	Section C bis *Host Country DNAs shall, inter alia:* • *Develop and implement procedures for the timely issuance of Letters of Approval which shall include:* o *Confirmation that the proposed project activity contributes to host country sustainable development* o *That the local stakeholder consultation has been undertaken according to relevant guidelines* o *Any requirements to be fulfilled in addition to existing regulations and permitting requirements, failure of which may result in the temporary suspension or ultimate withdrawal of the Letter of Approval* • *Optionally, define and communicate to the UNFCCC Secretariat details of the Host Country Mitigation Share of Proceeds in accordance with Appendix E* • *Optionally, demonstrate how host country ETS is using CERs to contribute to the overall mitigation impact of the CDM.* • *Develop and implement procedures for the fair and transparent suspension or ultimate withdrawal of a Letter of Approval at the end of a crediting period* • *Develop and publish lists of E+ and E- policies which PP's may use in the establishment of baselines and additionality for CDM project activities* • *Develop and implement procedures for linking registered CDM project activities with registered NAMAs to avoid double counting* • *Procedures for the development and approval of standardized baselines to establish host country mitigation contributions from registered CDM projects, varied by technology, geographic region and project age if necessary, and publication thereof* • *Participation in regional DNA Forum activities* • *Etc.* *Non-Host Country DNAs will, inter alia:* • *Develop and implement procedures for the issuance of letters of Approval* • *Consider whether, in the Host Party's opinion, applicant projects contribute to the objectives of the Framework Convention* • *Undertake adequate due diligence to ensure that projects are genuine* • *Develop, and implement where necessary, procedures for the temporary suspension or withdrawal of an LoA.* • *Participate in regional DNA Forum activities* • *Etc*

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	Section D Accreditation and designation of operational entities Accreditation of DOEs has become a massive, costly and hugely inefficient process. DOEs are unable to apply any expert judgment without fear of sanction; the hesitation and wariness of DOEs causes delays and un-necessarily conservative interpretation of methodologies and guidance. The cost of continuous spot checks increases the costs of validation and verification. The issue of liability has not been resolved and the proposal to suspend DOEs has widespread and negative impacts upon project participants who are otherwise un-related to the case in question. Development of PoA has been badly held back because of challenges over sampling and liability (see proposals for PoA at the end of this submission). Some stakeholders have raised concerns over the relationship between PPs and DOEs on the basis that the PPs pay the DOEs even though formally the DOEs report to the Board. Project developers do not believe that this is a valid concern because third party auditors and inspectors are paid by the objects of their inspection in many commercial and regulatory settings, including, notably, financial auditors. The Accreditation Panel is responsible for ensuring that DOE are independent and a lack of independence has not been cited as a problem to date. It is proposed that the Board commission a review of the accreditation procedures in order to • Make better use of the ISO 14000 series of standards, particularly ISO 14065, 14066 and 14067 • Improve the consistency of the accreditation process so that all DOEs work to the same standards • Empower DOEs to apply their professional judgment on the basis of demonstrated competency • Critically evaluate the benefit of the spot check and site visit procedures in view of the transaction burden for DOEs and PPs compared to the benefits • Develop better training for DOEs, PPs and DNAs so that all participants in the project cycle share a common understanding of the rules Propose a means of addressing professional negligence and fraud amongst DOEs and PPsAllow and recognize the use of precedents as basis of DOE judgment	*20 bis The Board shall review the accreditation requirements in Appendix A in order to:* • *Make better use of the ISO 14000 series of standards, particularly ISO 14065, 14066 and 14067* • *Improve the consistency of the accreditation process so that all DOEs work to the same standards* • *Empower DOEs to apply their professional judgment on the basis of demonstrated competency* • *Critically evaluate the benefit of the spot check and site visit procedures in view of the transaction burden for DOEs and PPs compared to the benefits* • *Develop better training for DOEs, PPs and DNAs so that all participants in the project cycle share a common understanding of the rules* • *Propose a means of addressing professional negligence and fraud amongst DOEs and PPs* • *Allow and recognize the use of precedents as basis of DOE judgment*

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	Section F: Participation requirements Paras 31, 32 and 33 to be revised / removed The intention is that: 1) All Non-Annex B Parties should be eligible to host CDM projects and should create a Designated National Authority capable of issuing letters of Approval (and all that entails) 2) All Parties to the Kyoto Protocol (Annex B and Non Annex B) shall be eligible to acquire and transfer CERs from CDM projects 3) All Parties to the UNFCCC which are not Parties to the Kyoto Protocol shall be eligible to acquire and cancel CERs 4) The secretariat shall create registry procedures to allow this. The intention is that both non-Annex 1 and non-Kyoto Parties should have access to CERs for the purposes of offsetting emissions under various instruments such as Pledges, voluntary emission trading schemes etc. The justification for this is to avoid the proliferation of offset schemes generating units which are of a different and potentially lower standard of environmental integrity than CERs; it will encourage the use of the substantial infrastructure already in place; ensure that all offsets used for pledges and other forms of voluntary and mandatory commitments are of an equal standard; it will increase demand for CERs and increase investment in CDM projects, bringing more / better / assured sustainable development benefits to host countries; it will avoid double counting of GHG emission reductions and finally it will prepare the Parties for the adoption of NMBM and FVA and the implementation of the Durban Platform under which the distinction between Annex 1 and Non-Annex 1 will be less relevant. This solution also warrants that consistent MRV principles are being applied as a basis for comparability of efforts.	*31 b) Delete* *f) If it has an assigned amount, it submits the supplementary information….* *32 bis A Party not included in Annex 1 is eligible to use CERs if it is a party to the Kyoto Protocol.*

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	Section G Validation and registration Generally we wish to see changes to the validation and registration process consistent with other proposals above and also steps taken to improve the Environmental Integrity of the CDM, strengthen the local and global stakeholder consultation; reduce the transaction costs by application of positive lists, standardized baselines and materiality; fairer application of conservative principles; re-assessment of the duration of crediting periods; consolidation of the E+ and E- guidance to prevent perverse incentives as required by paragraph 11 of Decision 2/CMP.5 in order to assure that the CDM effectively supports developing countries in their efforts and policies for sustainable development and GHG mitigation and the development of baselines which ensure that projects increasingly contribute to host country mitigation actions. This also implies the development of explicit procedures for combining CDM Project Activities with other activities under the UNFCCC and outside of its scope such as NAMAs and FVA.	
	Para 37 (d) where projects use standardized or default baselines, there will be no requirement to validate the baseline other than the eligibility to use said baseline. This will result in a simplified validation procedure for projects using these categories of baselines. Similarly, projects which are considered to be automatically additional shall benefit from a simplified validation procedure. A simplified validation procedure shall be faster, cheaper and less demanding on PPs when compared against the standard validation procedure. (e) The baseline and monitoring methodologies comply…	e) The baseline and monitoring methodologies comply…*With consistent grace periods applied to the implementation of all tools, procedures and guidelines.*
	Para 40 (a) Prior to the submission, have received from the PP written approval of voluntary participation… achieving sustainable development. It is proposed to strengthen the Local Stakeholder Consultation process by requiring the host Party to confirm that the consultation has met host Party guidelines or procedures. In Doha, Parties already agreed to share best practices on local stakeholder consultation. The Secretariat may develop voluntary local stakeholder consultation guidelines which Parties may adopt if they wish, in the same way that the Secretariat has prepared voluntary sustainable development evaluation guidance.	40 a) … *including confirmation by the host Party that the project activity assists it in achieving sustainable development; that local stakeholder consultation procedures have been fulfilled; that the relevant advertised host country mitigation share of proceeds shall be applied for the duration of the crediting period (including confirmation of the share of proceeds); and referring to the published procedures for the suspension and ultimate withdrawal of Letters of Approval.*

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	(c) Receive, within 30 days, comments on validation requirements from Parties, stakeholders and UNFCCC Accredited NGOs and make them publicly available. It is proposed that steps are taken to exclude fake comments from non-genuine stakeholders. Despite guidance from the EB, DOEs still raise questions on "spam" comments. Spam comments may be identified using a simple checklist and email addresses and domain names which submit such comments on three occasions should be blacklisted from the stakeholder consultation process.	*40 c) Receive, within 30 days, comments on validation requirements from Parties, genuine stakeholders and UNFCCC Accredited NGOs and make them publicly available.* *c) bis Exclude "spam" comments from non-genuine stakeholders, identified as comments which come from fake email addresses, duplicated comments, comments which apply to other projects and comments which are generic and not specific to the project in question.*
	Para 40 (h) The validation process is very inefficient because, amongst other reasons, the entire process relies on the review of extensive written documentation which often contains, or creates, mistakes, inconsistencies and editorial errors through duplication of data/ text etc. There is considerable scope to remove much of this and reduce associated transaction costs by the development of a digital platform whereby data is entered once, automatically checked for consistency with the expected requirements at the time of entry and once "ticked" by the validator, is then "locked down" and only ever reproduced from the validated reference. It is proposed that the Secretariat once again takes up the development of a digital registration and issuance process.	*The Secretariat shall develop a digital validation and verification platform with the aim of reducing transaction costs and eliminating duplication of information and data and the associated errors.*

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	Para 41 Reduce the registration period and the delay in completing requests for review. Decisions on requests for review shall not wait to be taken at Board meetings but shall be approved electronically based on recommendation from the Secretariat. Considerable time and potential CDM benefits are lost by the artificial time restrictions around the submission of prior consideration and the need to wait for the project to be registered before creation of CERs can commence. In practice, the "pre-CDM" emission reductions are often verified as VERs and sold, representing a loss to society. If a project activity is successfully registered, then the activity is additional and the emission reductions generated before or after the date of registration have equal environmental value. Further, the PD Forum believes that the current registration process of multiple checks and reviews following submission of a request for registration or request for issuance is unnecessary and a considerable duplication of effort by the DOEs and Secretariat. In view of our comments above on DOEs, we propose that the DOEs are entrusted to carry out the validation and verification of projects and programmes and the 'completeness check' and 'information and reporting check' stages at request for registration and request for issuance are removed. Proposals for the random checking of DOE recommendations should be implemented rather than having the Secretariat check all DOE submissions.	*The registration by the Board shall be deemed final after two weeks….* *(b) It shall be finalized no later than four weeks after Project Participants have responded to the request for review.*

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	Para 43 A CDM project activity is additional if anthropogenic emissions of greenhouse gases by sources are reduced below those that would have occurred in the absence of the registered CDM project activity (3/CMP.1, Annex, paragraph 43). This paragraph introduced the concept of "environmental additionality", but it has gradually been substituted by a more narrow definition of financial additionality. The current rules as applied for CDM project validation focus on the question if the project would be profitable under baseline conditions and the premise is that profitable projects would be readily financed and implemented by "efficient capital markets" and therefore are not additional. Unfortunately the theoretical concept of efficient capital markets does not hold in practice and especially for developing countries. Consequently profitability alone does not warrant effective project implementation. Despite repeated requests by the CMP the CDM EB has failed to establish adequate rules and procedures which allow to effectively demonstrating additionality on the basis of alternative approaches which recognize the existence of the frequent market failures as observed in developing countries. For this reason we urge to retain the original definition of additionality. We also request to instruct the CDM EB to effectively establish rules and procedures which consider the economic reality of host countries and the existence of market failures as a basis for a definition of realistic business as usual baselines. Based on such realistic baselines the additionality of a project activity can be demonstrated on the basis of the measures and policies which were implemented and necessary to assure that the project is successfully implemented and capable to reduce emissions relative to the baseline	A CDM project activity is additional if anthropogenic emissions of GHG by sources are reduced below those that would have occurred in the absence of the registered project activity *43 bis In assessing whether or not a project is additional, host national policies which encourage low emission technologies (so-called E- policies) shall be recognized as essential elements to curb baseline emissions and shall therefore be excluded from the definition of the baselines and from the additionality discussion for a period of [10] years after the policy entered into force.* *43 ter A CDM Project Activity is additional if the project complies with criteria defined by the Board for automatic additionality.*
	Para 44 Would include strandardized baselines and baselines for positive list technologies, which would have methodologies establishing, for example, default baseline emissions	

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	Para 45 A baseline shall be established (b) In a transparent and conservative manner regarding the choices of approaches, assumptions, methodologies, parameters, data sources, key factors and additionality, and taking into account uncertainty Change conservative to consistent; methodologies shall specify the data to be used and rather than applying conservative factors throughout the methodology (which compound the impact of conservative decisions), the methodology shall demonstrate how, at the end of the baseline and project emission calculation, conservativeness is taken into consideration. The impact of the final conservativeness factor shall be quantified, recorded and reported annually to the COP	*45 a)delete* *b) In a transparent and consistent manner regarding the choices of approaches, assumptions, methodologies, parameters, data sources, key factors and additionality, and taking into account uncertainty.*
	c) On a project-specific basis Baselines for similar project activities should be transferrable within a reasonable period of time, for example for [2] years following the validation of a PDD, such that PPs can replicate projects without having to repeat the determination of the baseline in the same way that PoA procedures currently allow CPAs to be added to registered PoA DDs. This would enable PPs to replicate successful stand-alone projects of any size.	*On a project specific basis or by reference to another project applying the same methodology and technology in the same socio-economic region.*
	e) Delete	Delete
	f) Taking into account relevant national and/or sectoral policies and circumstances, such as sectoral reform initiatives, local fuel availability, power sector expansion plans, and the economic situation in the project sector The paragraph has been complemented by the E+/E- guidance as established by EB 16 and revised by EB 22, Annex 3 in 2005 which was designed to prevent that the rules for baseline setting and additionality demonstration represent a perverse incentive which could prevent Parties to implement policies which promote emission reducing technologies and to discourage Parties from adopting policies capable to artificially inflate emissions as a basis for artificially increased GHG abatement results. It can be assumed that this rule effectively deterred parties from the adoption of E+ policies, but only recently the rule for the treatment of E- policies gained attention on the background of the NAMA policies which were following COP 15 in Copenhagen. At the same conference the parties reiterated the central role of the E- concept by agreeing on the following principles (Decision 2/CMP.5): *10. Affirms that it is the prerogative of the host country to decide on the design and implementation of policies to promote or give competitive advantage to low*	*(e)Taking into account relevant national and/or sectoral policies and circumstances, such as sectoral reform initiatives, local fuel availability, power sector expansion plans, and the economic situation in the project sector. In order to promote policies which favor or give competitive advantage to low greenhouse gas emitting fuels or technologies, such policies shall be excluded from the determination of baselines for [10] years after the policy entered into force.*

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	greenhouse gas emitting fuels or technologies; *11. Requests the Executive Board to ensure that its rules and guidelines related to the introduction or implementation of the policies referred to in paragraph 10 above promote the achievement of the ultimate objective of the Convention and do not create perverse incentives for emission reduction efforts;* As a result the principle that the CDM shall promote GHG mitigation policies established by developing parties and avoid perverse incentives is now an important concept for the promotion of NAMAs as well as an opportunity for the adequate understanding and MRV of national GHG mitigation policies. As such this concept must be safeguarded and consolidated as an essential element of the reform of the CDM. To account for an evolution of the international climate regime, it is proposed that policies encouraging the use of low emission technologies (E-) are therefore further excluded from the baseline definition and the additionality assessment for a period of [10] year after the date of their implementation, after which they shall be taken into consideration .This gives host Parties a 10 year window to build infrastructure and capacity to implement policies with the support of CDM and then substitute this arrangement with solutions that are more adequate to the post 2020 regime as to be agreed on the basis of the ADP. See below for proposal to manage the baseline for technologies implemented under E- policies: Policies which favor increased GHG emissions (E+ policies) shall be excluded from the assessment of the additionality and determination of the baseline for the duration of the CDM (i.e. the treatment of these policies will remain unchanged). Due to the anticipated use of NAMAs to develop national policies and the potential for CDM to be used to finance such initiatives, the Secretariat shall provide for a linkage between CDM registered activities and the NAMA register in order to avoid double counting and help to demonstrate where projects are developed under E- policies. As mentioned above, DNAs shall be requested to provide lists of E+ and E- policies.	
	Para 46. Extend to include suppressed demand	

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	Para 48. Extend to include (d)standardized baselines (e)default baseline applied to a technology from the positive list.	*(d)standardized baselines* *(e)default baseline applied to a technology from the positive list.*
	Para 49. Selection of crediting periods. In Doha, the parties discussed reviewing the duration of crediting periods. The current crediting periods have been fixed and 10 years or 3 times 7 years. Any limitation of the length of the crediting period may not apply retroactively to projects which have already been registered. Therefore, this measure is unlikely to a significant impact upon the current supply of CERs. However, the impact of the duration on crediting periods on investment and operational decisions for different types of projects and technologies varies. Thus, we recommend that the Board undertake a review of crediting periods and in the process, stakeholders may be consulted to get a better understanding of how crediting periods for new projects could be defined.	*49 Project Participants shall apply the crediting period as defined by the Board.*
	Para 51 bis, ter	*51 bis A single conservativeness factor will be defined consistently, transparently and in accordance with agreed principles, in tools and methodologies and will be transparently applied to the final determination of emission reductions. The resulting deduction of CERs will be recorded by the Secretariat and reported annually to COP* *.51 ter In the event that significant deficiencies are identified in the activities for DOEs, any over-issuance of CERs will be offset against the total Conservativeness factor for the period(s) in question. The offset will be transparently calculated and reported to the Parties.*
	Section H Monitoring Generally, monitoring of CDM projects has been very successful and has contributed significant capacity building to host countries. Several small but significant changes can make the process significantly more streamlined. Uncertainty shall be managed by requiring all Montoring plans to include an uncertainty assessment which shall deliver and overall uncertainty below a defined and methodology specific uncertainty threshold. Thus renewable energy projects may be expected to monitor to within 0.5% uncertainty whilst cookstove projects may monitoring to within 5% uncertainty, and PPs can invest their resources of equipment and procedures which deliver the required level of uncertainty most cost efficiently.	

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	Para 53: project participants shall include, as part of the PDD, a monitoring plan that provides for a through g. Option to include in PDD The requirement to specify the monitoring plan in the PDD, often before the project is constructed, has created continuous problems for PPs and DOEs. Instead, it is proposed that PPs have the option to a) include the monitoring plan in the PDD (where it can be validated) or b) simply confirm which parameters the methodology requires to be monitored in the PDD and provide the monitoring plan prior to the first verification. Under option b), the detail in paras a through g should be provided in a stand-alone Monitoring Plan prepared prior to the start of the first monitoring period. During verification, the plan will be compared against the requirements of the methodology and changes in the plan to improve the accuracy or quality of the monitoring plan can be implemented on an on-going basis. The Monitoring Report, prepared for each verification shall be audited against the Monitoring Plan.	*53. Project participants shall include either as part of the PDD or as an annex to first verification report, a monitoring plan that provides for:* *a)…*
	Para 55 Delete	
	Para 56 PPs shall implement the monitoring plan contained in the registered PDD.	*PPs shall implement the defined monitoring plan either contained in the registered PDD or annexed to the first verification report.*
	Para 56 bis PPs shall calculate the overall uncertainty of the monitoring system and show that itdoes not exceed the methodology specific uncertainty threshold	*56 bis PPs shall calculate the overall uncertainty of the monitoring system and show that it does not exceed the methodology specific uncertainty threshold*
	Para 57 The DOE shall approve changes to the Monitoring Plan prior to periodic verification and may ask the verification team to confirm the PP's justification of changes during the next verification.	*57 ….. submitted for approval to a DOE prior to verification and may be assessed at verification.*
	Para 58, removed "registered"	

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	Para 59 bis…. In order to enhance the environmental credibility, projects' contribution to host country mitigation and transparently demonstrate conservativeness, two new deductions will be made from the CERs generated by CDM projects: A single deduction for conservative is meth specific and reflects one single adjustment factor for conservativeness applied at the end of the calculation of CERs, replacing arbitrary conservativeness factors which are applied to individual parameters in the calculation process and which can be compounded in the final calculation and which are non-transparent. A host country share of proceeds to contribute towards host country mitigation. This is proposed in preference to manipulation of baselines to create host country contribution, which would have a tendency to discourage investment in certain technologies across the board. Making the host country contribution technology, region and project age specific enables host countries to encourage investment in certain technologies in certain regions.	*59 bis The verification report will transparently show the baseline emissions, project emissions, leakage emissions if any and the resulting CERs. The following factors will be deducted from the resulting CERs and recorded in the CDM Registry:* *a) A single methodology specific conservativeness factor, the Conservativeness SoP* *b) The SOP Admin fee, at the current agreed level* c) *The SOP Host Country mitigation fee, at the level defined by the DNA considering the technology, location and age of the project activity.*
	Section I Verification and certification Generally, Verification should be streamlined such that second and subsequent verifications, where project implementation and monitoring have not changed, can be completed more quickly and simply, at significantly lower cost. The Secretariat shall develop procedures for on line verification of data for example from registered renewable energy projects and in such cases the DOE shall verify the integrity of the data collection and calculation systems and only sample data on site to ensure the systems are operating.	

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Issue No.	Issue to be addressed (including need for change)	Proposed change (including *proposed text in italics*, if applicable)
	Section J: Issuance of CERs Generally, issuance will be speeded up with the Board approving issuance one week of receipt of request for issuance and completing requests for review within two weeks of receipt of response from PPs. Board will approve Secretariat recommendations unless it has cause for concern. A new fee is introduced, collected in a manner similar to the adaptation fee, to reflect contribution to host country mitigation. DNAs are requested to set levels of the required host country contribution at fixed or variable rates, varying by technology, geographic location or age of project. Whilst the host country contribution is effectively a tax on project developers, it can also act as an incentive attracting investment to under-represented technologies and regions and discouraging investment in over-represented technologies and regions. The Host Country Contribution will be forwarded to an account in the name of the host country which they may use to meet current or future targets, pledges [or sell to raise capital for investment in climate mitigation and adaptation projects]. The registration and issuance fees at current market prices, make up a very large share of the market value of the reductions achieved through the CDM. We understand that an issuance fee is required to pay for the continuing administration of the CDM. The registration fees were necessary in the early years of the CDM to finance the mechanism at a time when few issuances occurred. However, as the CDM has now built up a large financial reserve, the upfront registration fees should no longer be necessary. The Board shall therefore reconsider the necessity of an upfront registration fee and review the level of issuance fees [annually] in line with current market prices.	
	Para 65; reduce issuance delay to 7 days b) Reduce review period to 15 days c) inform PP of the outcome within 7 days	*65. The issuance shall be considered final 7 days after the request for issuance…* *b) the Board shall complete its review within 15 days….* *c) the Board shall inform PPs of the outcome of the review within 7 days…*
	Section j bis: Funding The Board derives its funding from the registration and issuance fee and this should be made explicit in the Modalities and procedures, along with steps to change the level of fees charged	***Section j bis*** *67 The Board shall finance its operations through the levy of registration and issuance fees, and new methodology fees. The level of these fees shall be determined by the Board and reviewed periodically, taking into consideration market conditions and levels of existing finances.* *68 Registration fees for projects which are registered but not implemented and are subsequently withdrawn shall be refunded to PPs.*

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	Appendix A To be revised following completion of a review	
	Appendix B The PDD template should be substantially revised following a review using knowledge based on the validation and registration of over 5000 projects to date. For example, a revised PDD template should remove the complications that arise through editing and copy / pasting errors by reducing the need for text and moving towards a format which can be digitized and automatically checked at various stages of the process.	
	Appendix C The Board, drawing on experts in accordance with the modalities and procedures for a CDM, shall develop and recommend to the OP/COP Delete "develop" to remove the executive function of the Board.	*The Board, drawing on experts in accordance with the modalities and procedures for a CDM, shall recommend to the OP/COP*
	Appendix D	
	Appendix D bis **Procedures for the establishment and implementation of the Host Country Mitigation Share of Proceeds** **Please refer to Annex 3 to this submission**	**Appendix D bis** **Implementation measures to be transcribed into text** Host Country DNA a) Give DNAs the optional authority to set Host Country Mitigation SoP varied by technology, geography and duration b) To be communicated to UNFCCC and displayed on the UNFCCC website c) To be inscribed in the Host Country LoA and to be fixed for the duration of the crediting period Registry a) Create Host Country Mitigation Accounts for each country defining a Host Country Mitigation SoP. b) Deduct the Host Country Mitigation Share of Proceeds at issuance CERs in the Host Country Mitigation Account shall be cancelled against that Host Country's pledges or targets, or recorded in the next national communication or national inventory.
	Additional Proposals	

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	Afforestation and Reforestation Less than 1% of the registered CDM projects are afforestation and reforestation projects (currently there are 44 registered projects in scope 14). The introduction of temporary and long-term CER accounting rules and some Parties' purchasing policies have seriously impeded the demand for the resulting credits. In today's market there is no demand for these credits. It is proposed to take afforestation / reforestation activities out of the CDM and move them into REDD+ where accounting rules may be more beneficial to such projects and where investors may be driven by a different set of incentives.	

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	PoA PoA has potential to scale up certain types of activities and turn them from project specific activities into national or even international activities. In this respect, PoA is closer to the concept of NAMAs. On the other hand, we have seen how concerns around liability during validation and verification have hampered the development of PoA. It is proposed that as soon as NAMA frameworks are implemented, there should be a discussion about transferring the existing PoAs and register new PoAs under NAMA frameworks where Governments can take a greater role in the development of nationally appropriate actions. Changes to the CDM modalities and procedures described above can allow successful projects to scale up, specifically: • Removing the artificial distinction between small and "large" scale CDM projects so that if a project is considered by the host Party and the international buying community to be good, PPs are able to scale it up efficiently • Extending the concept of positive lists / automatic additionality to all CDM projects and not arbitrarily restricting it to small projects • Allowing PDDs to refer to validated baselines in registered projects which apply the same technology and methodology in similar socio-economic circumstances – effectively giving normal CDM projects one of the significant benefits afforded to PoA. In this way, the CDM can scale up beneficial projects using one set of simplified and streamlined rules whilst the very powerful concept of PoA can be freed from the constraints of the CDM process and allowed to develop under the more flexible concept of NAMAs. With regards to meaningful changes that are likely to have a big effect on registered PoAs and improve their issuance track record, following issue should be addressed: The need of verifying all CPAs included in a PoA within the same verification for one defined monitoring period should be removed. CMEs shall be flexible in determining the monitoring period of CPAs. The flexibility shall be given for different parallel verifications of a group of CPAs within the same PoA distinguished in length of the monitoring period. The nature of a CPA (i.e. size, technology, target group, fixed parameters etc.) determines the grouping and length of the monitoring period to minimize transaction costs and standardization of processes. If such flexibility is not given, newly included CPAs and small CPAs cannot be verified due to too high transaction costs relatively to the expected carbon revenues.	

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Issue No.	**Issue to be addressed (including need for change)**	**Proposed change (including *proposed text in italics*, if applicable)**
	Significant deficiencies The concept of significant deficiencies is not well defined and is proving difficult to implement. Proposals for insurance based protection for DOEs are expensive, will act to significantly increase transaction costs for PP and do not offer value for money on the basis that no significant deficiencies have been reported to date. It is proposed that any identified significant deficiencies are offset against the conservativeness factor and deducted in a transparent manner from the annual report of conservativeness to the COP. This is a rational means of making the system whole because an element of the risks of over-issuance which conservativeness factor guards against, is the possibility that a DOE makes a mistake and causes an over-issuance, or does not notice a mistake and does not stop an over-issuance.	Appendix D ter: In the event that a significant deficiency is identified according to agreed procedures, the DOE shall be penalized financially, in a manner against which they can insure themselves. This will act as a deterrent to DOEs. The quantity of CERs which has been over-issued will be offset in a transparent manner, against one or more annual conservativeness reports calculated from the sum of CERs deducted for conservativeness and reported to the COP annually.

Annex 2 Architecture paper

Carbon Market Architecture

CMIA and PD Forum joint submission to SBI, March 2013

Key points

- **Market-based mechanisms** are the most cost effective route to achieve the objective of the Convention;
- The global carbon market has been highly successful. The CDM has mobilized investments of **USD 215 billion** in emission reductions, mostly from the private sector. Registered CDM projects are estimated to achieve **850 million tCO2e reductions annually**, which is equivalent to more than 5% of non-Annex I CO2 emissions.
- Building on our previous proposal and the existing high-successful structure, **an over-arching carbon market architecture** is proposed, including each of the existing and newly proposed mechanisms, identifying common building blocks and providing fungibility between approaches.
- The proposed architecture consists of approaches of **increasing stringency** with regards to levels of emission reductions, monitoring and compliance, but also delivering increasing economic efficiency and reduced cost. Participation in the mechanisms would be voluntary: there is no mandatory migration through the mechanisms, but reduced transaction costs should make successive mechanisms more attractive and ambitious. Therefore, there is a **natural incentive for progression** towards more stringent commitments.
- **Each mechanism helps to build the technical capacity** and institutional infrastructure necessary for the next mechanism. **Transition through each mechanism may happen over a period of decades**, giving ambition, capacity and development time.
- This vision is dependent on three critical developments. First, **ambition has to dramatically increase** in the climate regime. If there is no demand for emission reductions, no approach will ever be attractive. Second, **investors must be rewarded** for their own achievements and not be penalised for others' failure. Third, a **continuing strong commitment to the carbon market** is necessary; if nations permit the CDM to disintegrate, the political consensus for truly global carbon markets may evaporate along with much of the world's developing country carbon market capacity, and thus the possibility of implementing this vision.

Introduction

CMIA has previously put forward an over-arching architecture for the management of GHG emissions in the global economy, with an increasing share of emissions covered over time. With new approaches having been proposed and defined, the detail of our proposed architecture has evolved, while still maintaining the overall philosophy of increasing coverage and graduation depending on capacity.

The original Kyoto architecture included two levels, (1) national targets with emissions trading, and (2) the two project-based mechanisms, one in a capped environment (JI), and one in a uncapped environment (CDM). The existing climate change policy architecture has already expanded beyond Kyoto's levels (EU emission trading schemes (ETS), POAs, NAMAs, and arguably CDM standardised baselines). First suggested in Bali, and then in Cancun, the COP defined a New Market-based Mechanism (NMM) and considers establishing a Framework for

Various Approaches (FVA), acknowledging that various approaches are being implemented by Parties. While both NMM and FVA are still scarcely defined, the carbon market architecture under the UNFCCC has expanded far beyond the original design.

At the same time as expanding the architecture, the Kyoto model is under review following the end of the first commitment period under Kyoto. Additionally, negotiations have already started for another potentially major overhaul with a new global agreement in 2015. Therefore, it is good to take stock of the architecture we already have and which we are currently designing, and ensure it is fit for purpose.

Taking stock

There are currently 4 mechanisms defined, International Emissions Trading (Article 17), Joint Implementation (Article 6), Clean Development Mechanism (Article 12), and a New Market-based Mechanism (Cancun). There are also a number of approaches that are applied within the UNFCCC, including POAs, NAMAs, benchmarks and standardised baselines, and outside the UNFCCC, including ETS. Further, the COP is considering whether to establish a framework to cover the various approaches (already) used (FVA).

There is also significant experience that should be taken into consideration when reviewing the overall architecture. The key messages are:

- The global carbon market has been highly successful. The CDM has mobilized investments of USD 215 billion in emission reductions[6], mostly from the private sector.
- Registered CDM projects are estimated to achieve 850 million tonnes of CO2e annually, which is equivalent to more than 5% of non-Annex I CO2 emissions. [7]
- Market-based mechanisms are the most cost effective route to achieve the objective of the Convention.
- A market-based approach is only ever as good as the target it is designed to meet. The main barrier to efficient operation of the carbon market, and achievement of emission reductions, is the current crisis of demand. 'Mitigation targets are so modest that they no longer create strong incentives for investment'.[8]
- The private sector needs demand for emission reductions (i.e. targets), fungibility of efforts (i.e. tradability) and confidence in the longevity of the UN process-backed market-based approaches in order to invest.
- Incentives need to be available directly to individual operators in order for market forces to work; rewards must be directly related to success (compliance) and failure (missing target) must be penalised. If individual operators are not directly rewarded for their own success (compliance), but are reliant on others in their sector, market forces will not deliver cost effective reductions; rather this would result in a tragedy of the commons: because no-one is rewarded for success, no-one is responsible for failure.

[6] 'Benefits of the CDM up to 2012', UNFCCC (2012), see http://cdm.unfccc.int/about/dev_ben/ABC_2012.pdf. The UNEP Risoe CDM Pipeline (March 2013) suggests that investments related to registered projects alone amount to over USD 350 bn.
[7] Annual reductions from registered CDM projects from UNEP Risoe CDM Pipeline (March 2013). The whole pipeline would result in 1.6 bn tCO2e reductions annually. 2010 non-Annex I CO2 emissions from IEA CO2 Emissions from Fuel Combustion (2012).
[8] "Climate Change, Carbon Markets and the CDM: A Call to Action", Report of the High-Level Panel on the CDM Policy Dialogue, 11 Sep 2012, see http://www.cdmpolicydialogue.org/report/rpt110912.pdf.

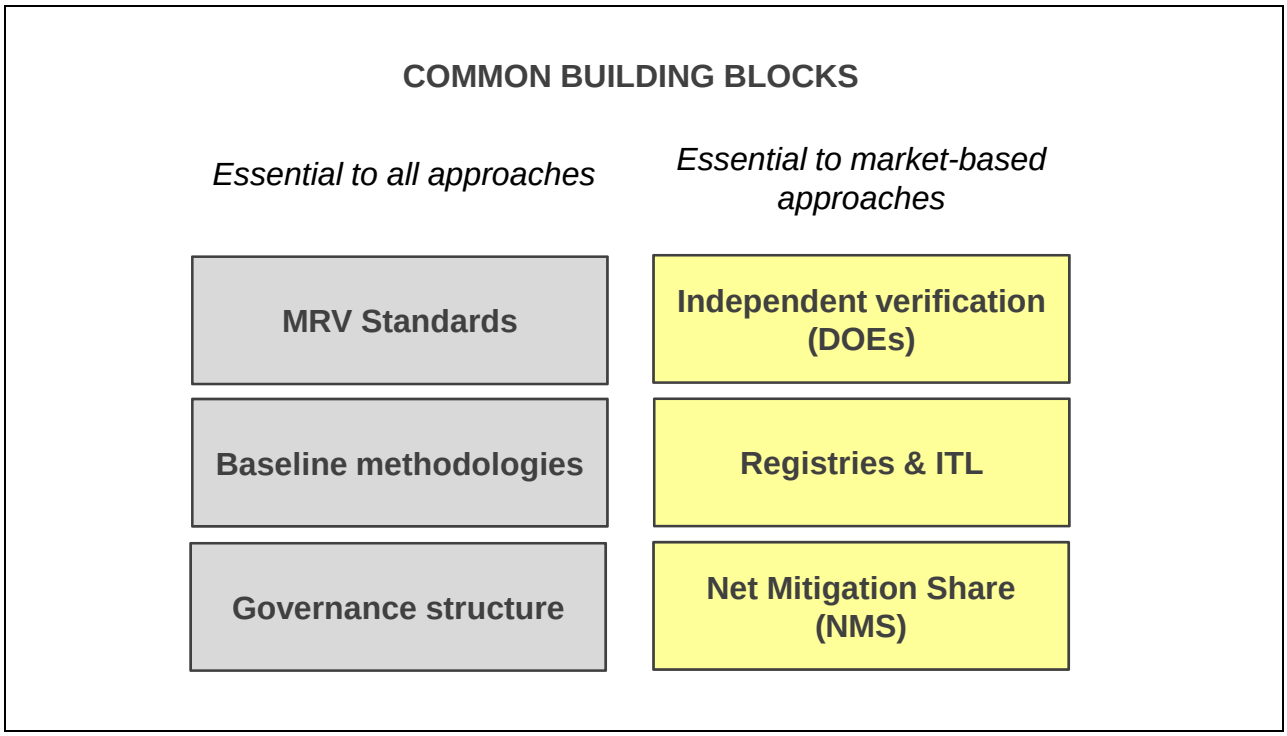
- The building blocks of the CDM, such as the MRV system, methodologies, and DOEs work. This existing market infrastructure needs to be preserved, and can be adjusted where necessary, for use under future approaches.
- The institutional and legal capacity required to implement a workable industrial emission trading scheme is enormous. A baseline and credit system is likely to be more appropriate for many constituencies.
- The land-use sector is very different from the main CDM, even delivering different credit types (tCERs or lCERs) which are not widely accepted. It is proposed that land-use projects are separated out from the CDM as soon as practicable, and merged with and grandfathered into a REDD+ mechanism.
- The programmatic approach is very different from the main CDM. It is proposed that programmatic approaches are separated out from the CDM as soon as practicable, and merged with and grandfathered into a (credited) NAMA mechanism.
- 'A strong CDM is necessary to support the political consensus essential for future progress [towards a truly global carbon market]. A robust CDM, furthermore, is necessary to bring the benefits of carbon markets to developing countries now. If nations permit the CDM market to disintegrate, the political consensus for truly global carbon markets may evaporate along with much of the world's developing country carbon market capacity. Developing countries and the private sector are unlikely to see sufficient benefits to justify aggressive emissions mitigation steps in those nations. The collapse of the CDM, in short, could seriously set back international climate cooperation, with potentially devastating consequences for all.' [9]

Building blocks

The guiding principles of the new approaches are similar to those of the existing mechanisms. The building blocks needed to operate the new approaches are also similar. The reason is that the existing mechanisms have proven to be efficient, but there is a desire to move beyond their boundaries. A thorough review and re-alignment of the existing mechanisms, in particular expanding their boundaries, could negate the need for the new approaches, but politically that seems to be difficult.

We propose guiding principles and the building blocks of the carbon market are seen as the framework for the approaches including the mechanisms. Some of the building blocks can be extracted from the CDM and JI, thus allowing the existing infrastructure, including institutional capacity, to continue and serve the new approaches without delay. The overarching architecture provides the common currency which gives the fungibility between the approaches and the global demand.

[9] Report of the High-Level Panel on the CDM Policy Dialogue.



Building blocks that may be part of the framework, and applied by all mechanisms, should include at least:

- **MRV system**
  The monitoring, reporting and verification system of the CDM is proven and has delivered over 1.2 bn tonnes of greenhouse gas emission reductions. Without transparent MRV it is not possible to account for all emission reductions. In addition, MRV allows incentives to be available direct to individual operators, without this market forces can not work effectively to deliver cost effective reductions.
- **Baseline methodologies and (emission reduction) accounting**
  The CDM has provided a wide range of credible baseline methodologies, nearly 200 methodologies covering almost every sector[10], providing the best resource for accurate carbon accounting for projects and approaches. It would be unnecessary in many cases the re-invent the wheel with new methodologies, as many sector-wide and/or standardized methodologies have already been developed or are under development. The JISC already adopts the same methodologies; it allows alternative approaches – but this is possible because the JI operates in a capped environment. Some further standardization and/or simplification may be needed to be applicable under other approaches, and greater host country commitments may allow for such simplification (as under JI).
- **Governance**
  We propose a single supervisory board for the mechanisms, with membership along the same lines as that of the Green Climate Fund, including representation from civil society NGOs and business. The Mechanisms Board should fulfill a supervisory role, with the executive functions delegated, probably to the UNFCCC secretariat, including an Executive Director. Expert Panels, chaired by and including representatives of the Board, would be responsible for much of the policy development/standard setting. The CDM

[10] As well as a number of A/R methodologies.

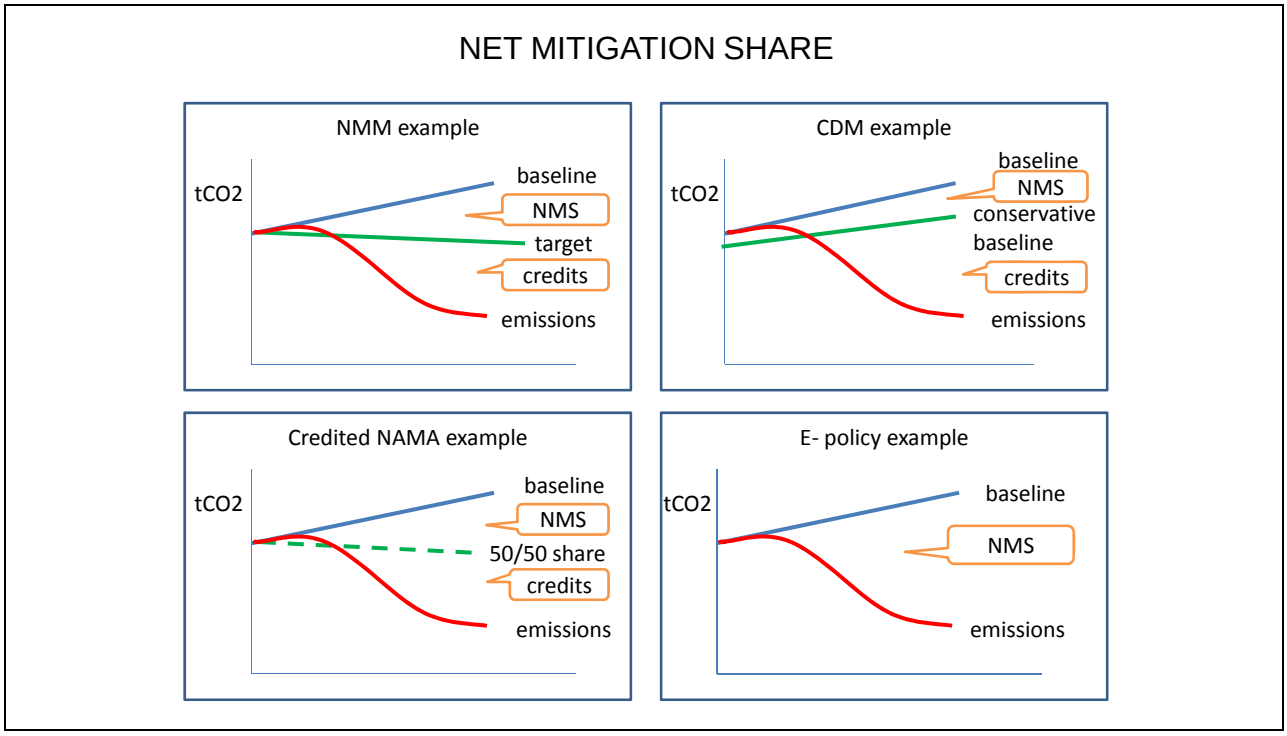
Executive Board and expert panels provide the basis for a prompt start of this governance structure, although the EB would need to be more supervisory and less executive. Also, the governance structure must include a satisfactory appeals process to guarantee due process for all participants. More detail is available in our submission on the Review of the CDM Modalities and Procedures.

- **DOEs and the accreditation (standard)**
  Both CDM and JI already use DOEs (AIEs under JI). Any approach would benefit from independent verification. And to ensure comparability of effort, and fungibility between approaches, they should all be subject to independent scrutiny. The JISC already adopts the CDM's DOEs; we propose the CDM accreditation standard is used throughout as the global standard.
- **Registries (and ITL)**
  Recording and tracking already exist though registries and the ITL and should be used to link all approaches. The open and transparent listing of projects, programmes, NAMAs etc., and allowing explicit multiple approaches, is the most effective way to eliminate double counting. There is no danger of double counting for a CDM project which is also explicitly stating that it's part of a NAMA; there *is* a danger where this information is deliberately held back and where there is a lack of transparent registry of approaches.

We propose to include an additional common building block:

- **Net Mitigation Share (NMS)**
  Enclosed is a separate paper with details, but the key points are summarized as follows and illustrated below:
  - In a component NMM (a sectoral scheme) it is expected that host countries would set a target for the sector below the baseline. Any reductions below the target would be credited and may be traded by the companies involved. The difference between the baseline and the target is the host country's own-effort, which is quantified in this manner and may be credited to the host country's account. See the illustration below. Therefore, the net mitigation share allows the own-effort of host countries to be fairly attributed to those host countries, while allowing the mechanisms to provide carbon financing to enable the actions.
  - It is accepted that the mitigation effort needs to be shared globally, taking into consideration different circumstances of developed and developing countries. It is expected that under the Durban Platform many countries will pledge some mitigation efforts. Such efforts will be made in part through policies that fall under the FVA, as they are designed to enhance the cost-effectiveness of, and to promote, mitigation actions. Therefore, host countries could introduce an own-effort share, with these reductions counted towards the host's pledged targets.
  - For example where host countries provide a feed-in tariff, or other support, the DNA may claim its own-effort share. This means that host countries could be credited for their E- policies, which would remove any perverse incentives currently perceived to exist. It may also simplify accounting of E+/E- policies, in particular if a database is established with E+/E- policies by each DNA. The host country NMS can be used in a similar way to allocate credited NAMAs (example shows 50% credited NAMA). See the illustration below.
  - It would be expected that Advanced Developed Countries would set higher rates, and LDCs lower rates. Rates may also vary over time, for example claiming higher own-effort after several years of crediting. With greater commitments of host countries, accounting may be simplified without jeopardizing the environmental integrity of the system.

- The ne mitigation share would guarantee that activities deliver net mitigation. This is relevant for all mechanisms, as it could also be applied by host countries under the CDM, but as a default it would be expected that the host country's NMS would be 0%.
- To improve accounting a single conservativeness factor should be introduced in methodologies, with this conservativeness retired in a special account, allowing a better appreciation of the net mitigation achieved through projects.[11] We believe that the best estimated reductions should be accounted for, even if then conservatively discounted with the conservativeness NMS and then retired. The introduction and quantification of this conservativeness provides an estimate of the net mitigation achieved. This would have no impact on the volume of credits that may be achieved by CDM projects, but calculates more fairly the best estimate of reductions achieved, and it provides for a standardized calculation among all approaches under the FVA umbrella. See illustration below.



Each of the former building blocks is necessary within each of the approaches. The MSOP would allow greater standardisation between all the various approaches and mechanisms – both NMM and FVA specify that they must lead to net mitigation. The CDM also leads to net mitigation by the application of its conservative approaches. Additionally, the Durban Platform should lead to commitments from developed and developing countries alike from 2020 onwards, and therefore there should be a way for these mechanisms and approaches to be used by each of the countries to contribute to their commitments.

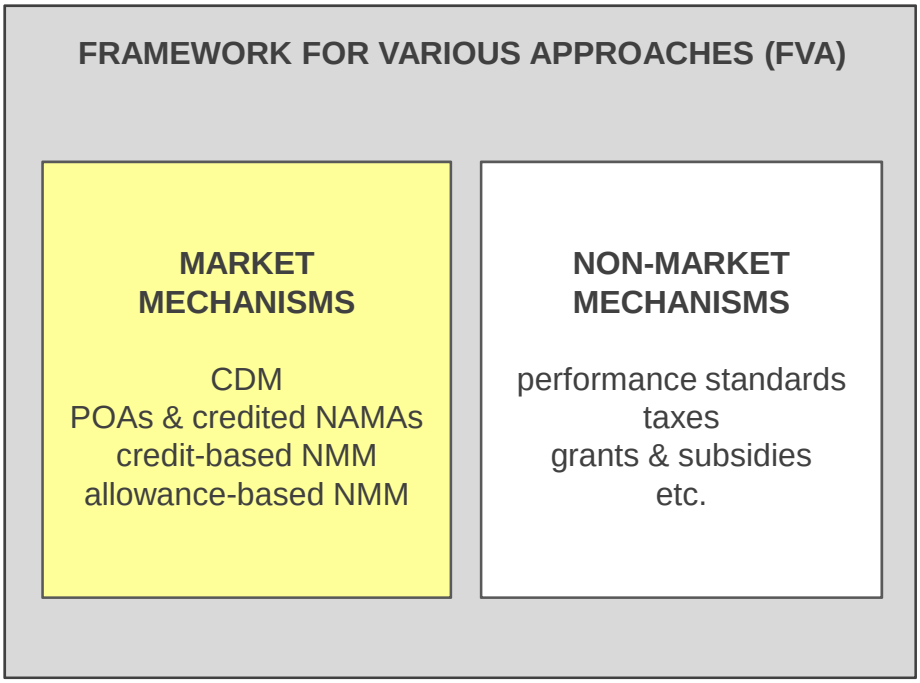
Framework for Various Approaches (FVA)

[11] For example, enclosed flares are normally more than 99.9% efficient in the destruction of methane, yet the methodology gives a default of only 90%; low enclosed flares are penalised with an additional 10% discount even if the efficiency is (accurately) measured. This may be conservative, but does not reflect reductions achieved by the underlying projects accurately.

FVA is still scarcely defined. We propose that the building blocks above provide the framework. Each of the existing project mechanisms, CDM and JI, as well as the NMM would then fall under the umbrella of the FVA. NAMA and other policies and measures may also fit in the framework. The use of the same building blocks (under the FVA) for all these approaches would aid comparability and fungibility between approaches, and prompt start, while avoiding duplication of work to design and operate the required regulatory and institutional infrastructure.

Where approaches qualify under FVA, reductions can be quantified clearly and accurately, in a manner that is comparable globally. Indeed, this approach may even be used to quantify the mitigation impact of for example ODA, or other donor support, host country policies, etc. Quantification is possible for all approaches under the FVA; crediting of the reductions would only occur in the mechanisms. The registry would ensure that double counting is avoided.

However, not all possible approaches, however laudable, would necessarily qualify or could be claimed under this FVA umbrella.



New Market-based Mechanism (NMM)

NMM is defined to enhance the cost-effectiveness of, and to promote, mitigation actions, bearing in mind different circumstances of developed and developing countries, and which may assist developed countries to meet part of their mitigation targets or commitments under the Convention. Therefore NMM needs crediting.

The COP's definition of NMM is still very broad. We understand that NMM are sector-based approaches using targets, benchmarks, standardised baselines or allowances. They key candidates for NMM should be large point sources or fossil fuel users, such as power plants, industrial sites, refineries, oil/gas flares, and possibly also planes and ships. Disaggregated or

under-developed sectors are not suitable for sectoral schemes, for example the agricultural sector, but can be effectively addressed through the project-based approach of the CDM.

The minimum eligibility criteria for a sector to participate in a market-based mechanism, involving credits is:

- National institutional capacity.
- Access to accurate and transparent sectoral (historical and current) data.
- Determination of a baseline/target/benchmark, including the definition of own-effort and/or additionality.
- Implementation of accurate and transparent monitoring, reporting and verification for all sector participants.
- A (national/sector) registry.

Where such information is not available at the sector-level projects are limited to CDM, with similar eligibility criteria applicable to the project. The advantage of a baseline-and-credit mechanism is that emission reductions are generated and verified before they are issued, creating a build-in performance guarantee. With the development of the various provincial emission trading schemes, the Chinese schemes could be prime candidates for each being component-NMM[12]. However, these are pilot phases, and are still only helping to build up the capacity we believe is required before a scheme could be NMM.

While a trading scheme based on allowances, such as the EU ETS, is more efficient than one based on baseline and credit, it also requires significantly greater institutional capacity. An allowance-based market mechanism would additionally require:

- Very strong institutional capacity to enable effective enforcement, policing of the scheme, with sufficiently high penalties etc.

Implementing an allowance-based ETS requires the distribution of state-owned assets (the allowances) either through (free) allocation or auctioning. Many states do not have the capacity to distribute such assets in a fair and transparent manner. Therefore, we propose that allowance-based schemes should probably only be used in Parties with national caps and eligible for using the mechanisms. (Then any problems occurring with the scheme would not affect the environmental integrity of the whole system, but only create difficulty for the Party to comply.)

In a component NMM (a sectoral scheme) it is expected that host countries would set a target for the sector below the baseline. Any reductions below the target would be credited and may be traded by the companies involved. The difference between the baseline and the target is the host country's own-effort, which is quantified in this manner and may be credited to the host country's account. See the illustration on MSOP above. Therefore, the mitigation share of proceeds allows the own-effort of host countries to be fairly attributed to those host countries, while allowing the mechanisms to provide carbon financing to enable the actions.

In principle, credits from other schemes could be allowed to be used as offsets within any of these schemes, creating a safety valve for the sector covered, fungibility across schemes, and a global carbon price.

[12] It is foreseen that NMM would be made up of various "component-NMM", each covering their own sector, or country/region, and each probably requiring acceptance within NMM.

While NMM is seen as a sectoral trading scheme, incentives and penalties need to be available directly to individual operators. If individual operators are not directly rewarded for their own success (compliance), but are reliant on others in their sector, this would result in a tragedy of the commons: because no-one is rewarded for success, no-one is responsible for failure.[13]

Overall architecture

The over-arching architecture for reducing global GHG emissions that we propose consists of five partially-overlapping levels of market-based mechanisms, building on the existing structure. The different levels have increasing stringency with regards to the level of emission reductions, monitoring and compliance, but also delivering increasing economic efficiency and reduced cost. Therefore, there is a natural incentive which can lead to a natural progression, graduation, towards (taking on) more stringent commitments, as will be required to achieve the objective of the Convention. Ultimately all emissions need to be effectively capped and reduced, both in developed and developing countries, but this will take time and effort, and the proposed architecture allows for achieving this step-by-step. Building on the existing mechanisms, and expanding from the current situation, the five levels of market mechanisms are:

1) Project-based mechanisms. Reformed project-based mechanisms CDM & JI, including the greater use of standardised baselines, but maintaining the flexibility for project-specific approaches. CDM would be operational in the uncapped environment, whereas JI would operate under caps (see level 6 below). With a mitigation share (of proceeds) being introduced, host parties could also account (voluntarily) for their own-effort.
2) Programme-based approaches POA and (credited) NAMA. POA would be split out from the CDM as soon as possible (but obviously grandfathered where already registered), and merged with NAMAs. POA is following a very different approach from the CDM, using different crediting periods etc. so we believe it would be more efficient to treat this as a different approach altogether. Under credited NAMAs part of the mitigation could be the host Party's own-effort, with the remainder credited, while non-credited NAMAs could be fully counted towards the host country's mitigation.
3) Land-use based approaches.[14] AR projects would be split out from the CDM as soon as possible (but obviously grandfathered where already registered), and merged with any new approach to REDD+. These are very different approaches from the CDM, receiving different credit types, using different crediting periods, traded in a different market, etc. so we believe it would be more efficient to treat this as a different approach.
4) a. New Market-based (credit) Mechanism (NMM). This would be primarily a benchmark- or baseline-and-credit approach, covering sectors, or larger parts of the economy. For example, the power sector could be one component-NMM. The sectoral approaches could potentially be derived from benchmarks or standardised baselines already used, in particular where a significant share of the sector is already taking part.
   b. New Market-based (allowance) Mechanism, i.e. cap-and-trade. Allowance-based NMM, providing even greater efficiency, should be limited to the capped environment or to constituencies with particularly strong enforcement capabilities. An example of an allowance-based NMM is a trading scheme such as the EU ETS. However, where the system operates under economy-wide targets or agreed (legally-binding) sectoral targets

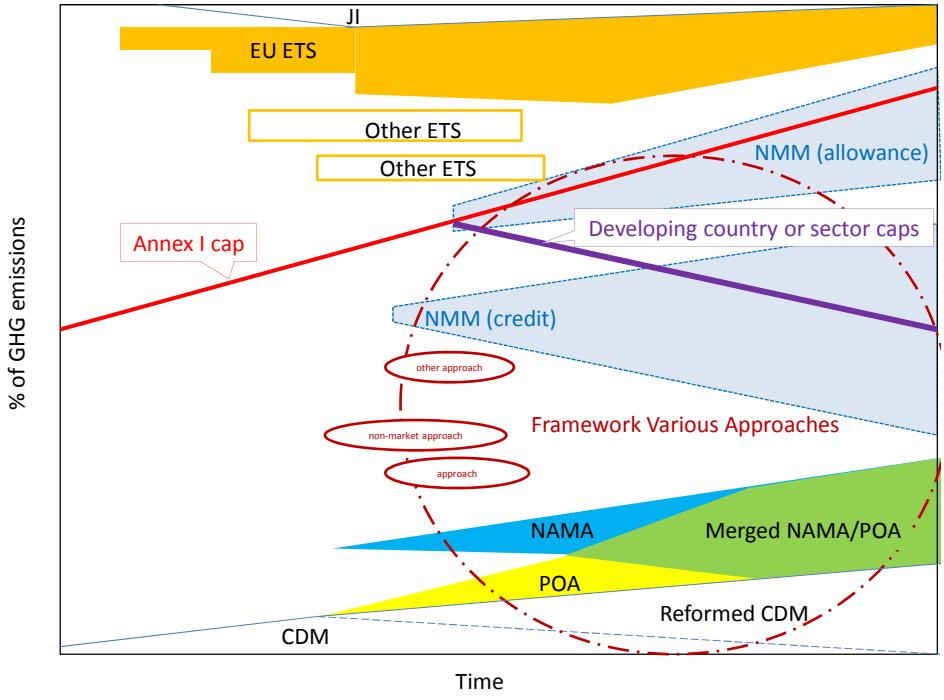
[13] A good rather than a bad outcome, "comedy of the commons", is only likely when the cost of the contribution is less than its value over time. If the targets set under the NMM require real effort, the costs are not 'much less than its value', and thus a good outcome is implausible. See: http://en.wikipedia.org/wiki/Comedy_of_the_commons.
[14] The various other levels of the carbon market are listed in progressive order, but the land-use based approaches should be seen more in parallel to the other 4 levels.

under the Durban Platform (see level 6 below), it would be unnecessary for this to be separately defined as NMM.

- *The levels 1, 2, (maybe 3) and 4 would be under the umbrella of Framework for Various Approaches (FVA), providing common building blocks, guaranteeing consistent accounting, comparability, fungibility, environmental integrity and avoiding doubling counting.*

5) Economy-wide targets (e.g. Kyoto targets), and agreed (legally-binding) sectoral targets under the Durban Platform. These targets would provide the regulatory environment for achieving reductions at the greatest economic efficiency, as they would provide maximum flexibility. International emissions trading (Kyoto Article 17) would be allowed under these caps. In principle each of the approaches above is possible under the economy-wide targets, for example the implementation of the EU ETS, as well track 1 of JI and a Green Investment Scheme. The host Party's responsibility to meet the agreed target provides the guarantee for the environmental integrity: any approach is as strong as the host Party's agreed target, and therefore doesn't need prior approval through the UN process. Therefore, there is a incentive which can lead to a natural progression, or graduation, towards (taking on) more stringent commitments, as will be required to achieve the objective of the Convention, and higher levels in the carbon market architecture.

The evolving Carbon Market Architecture



Notes: While Annex I emissions represented almost two-thirds of emissions in 1990, its share is less than half in 2010, and the share of Kyoto CP1 parties is only 25%. The Annex I cap, therefore, becomes a smaller share of global emissions over time (going right on the horizontal axis), hence the slope of the Annex I cap. However, the various mechanisms and approaches of the proposed Carbon Market Architecture should progressively cover a greater and greater share of world emissions (vertical axis).
The estimated annual emission reductions achieved through the CDM's registered projects is equivalent to almost 3% of world emissions, and more than 5% of non-Annex I emissions.

It is critical to note that to benefit from these various approaches, the market forces need to interact directly with the individual operators. These operators decide whether to invest in creating emission reductions, through new investments or behavioural or other changes. Therefore, they need to be rewarded directly for success (compliance / emission reductions) and penalised for failure (missing target / rising emissions). If individual operators are not directly rewarded, but are reliant on others before receiving their due reward, market forces will not deliver cost effective reductions; rather this would result in a tragedy of the commons: because no-one is rewarded for success, no-one is responsible for failure.

Over time, this proposed architecture could cover an increasing share of global GHG emissions through one of the mechanisms in order to be able to achieve the objective of the Convention.

Participation in one or more of these mechanisms or to adopt, for example, sector caps or an economy-wide cap is at the discretion of host Parties. Nevertheless, it would be envisaged that stringency, both in terms of limiting emissions and monitoring and verification of emissions/reductions, increases from CDM through to economy-wide targets, but that the economic efficiency of the mechanisms also increases. It is essential to appreciate that different mechanisms require diverse levels of technical and institutional capacity. Therefore greater capacity allows greater flexibility thus achieving greater economic efficiency.

While the participation in these mechanisms itself will build capacity in the country or sector to reach the next level through learning-by-doing as proven in the CDM, dedicated capacity building may further speed-up the expansion into the different levels. However, while sector-based approaches are more attractive in many respects, not all countries will be able to achieve the required additional capacity, nor is it necessarily the best route for all sectors; it has to be assumed that for many sectors the project-based approach will remain the most appropriate mechanism.

It is important that the development of the new approaches should not preclude the use of the existing mechanisms, for example CDM projects should not be forced to migrate to a new mechanism – but with lower transaction costs project participants may opt in voluntarily; also care needs to be taken so that projects/sectors are not refused the use of an existing mechanism before a new mechanisms is truly operational as that would jeopardise investments in the low carbon economy.

Conclusions

There is significant scope for a new market-based mechanism or mechanisms in conjunction with the ongoing reform/standardisation and expansion of the existing mechanisms. For this to materialise the current ambition, demand and vision to incentivise private entities to reduce emission will have to be clear, coherent and credible, with ambition significantly increased: without demand for the resulting reductions any new approaches would fail to deliver.

We have proposed the above over-arching architecture for reducing global GHG emissions that consists of five partially-overlapping levels of market-based mechanisms, building on the existing structure: first project-based mechanisms, then programmes, then NMM and finally caps, with land-use based approaches in parallel to the others. The different levels have increasing stringency with regards to the level of emission reductions, monitoring and compliance, but also delivering increasing economic efficiency and reduced cost. Therefore, there is a natural incentive which can lead to a natural progression, graduation, towards (taking on) more stringent commitments, as will be required to achieve the objective of the Convention.

Within this architecture, each mechanism helps to build the technical capacity and institutional infrastructure necessary for the next mechanism. Transition through each mechanism may happen over a period of decades, giving ambition, capacity and development time. Each successive mechanism is more powerful than the previous one, with the ability to attract more finance, deploy more technology, build greater capacity, have greater sustainable development benefits and contain a greater component of host country action.

Participation in the mechanisms would be voluntary: there is no mandatory migration through the mechanisms, but reduced transaction costs should make successive mechanisms more attractive and ambitious. The mechanisms are open to all sectors of the global economy, dependent only upon national circumstances, institutional infrastructure and ability to implement the mechanism. Once accepted within one mechanism, projects are grandfathered but may opt in into a new approach once that becomes operational, to ensure continuity and predictability for all stakeholders in these markets.

This vision is dependent on three critical developments. First, ambition in the climate regime has to dramatically increase. If there is no demand for emission reductions, no approach will ever be attractive. Second, investors must be rewarded for their own achievements and not be penalised for others' failure. Third, a continuing strong commitment to the carbon market is necessary; if nations permit the CDM to disintegrate, the political consensus for truly global carbon markets may evaporate along with much of the world's developing country carbon market capacity, and thus the possibility of implementing this vision.

The ultimate long-term objective is the adoption of ambitious binding caps on sectors and economies, which break the link between economic growth and growth in GHG emissions. Without this it is likely that the ultimate objective of the Convention will not be met.

About CMIA

The Climate Markets & Investment Association (CMIA) is an international trade association representing firms that finance, invest in, and provide enabling support to activities that reduce emissions. CMIA's membership accounted for 75 per cent of the global carbon market in 2010, valued at approximately USD 120 billion. See www.cmia.net.

About PD 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. PD Forum members account for almost 50% of all registered CDM projects and one third of all issued CERs. See www.pd-forum.net.

Insert CMIA PD Forum architecture paper

Annex 3 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[15]. 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, and/or alternatively that host countries use (their own) CERs as a flexibility instrument in domestic (voluntary) ETS.

[15] UNEP Risoe data, see Figure 1 in main text.

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 inventory.
- 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 time[16] 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 facilitate the integration of CDM projects with current and future host country E-[17] and GHG management policies and to guarantee net 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.

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 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

[16] 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.
[17] E- policies are policies which encourage low emission technologies and practices.

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.

	Host Country Mitigation Share of Proceeds expressed as a % of CERs at issuance		
Project Type	Advanced Developing Country[18]	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. 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 raising an MSOP, and in particular as part of possible future commitments under the Durban Platform, Host Parties may establish their own ETS within the more developed sectors or regions of the country.[19] 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.

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

[19] See our submission on the Carbon Market Architecture for a detailed discussion no 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, 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 already tend to be 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 countries[20]. 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.**

[20] 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.

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 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 County 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 though 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. According, 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

CDM Executive Board

Define an approach to conservativeness across methodologies which allows to transparently account the amount of emissions which are not issued to preserve it. Registry

- CERs in the Conservativeness Account may only be used to replace excess CERs issued as a result of significant deficiencies by DOEs.
- 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.