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Item 5 of the provisional agenda
Issues relating to the clean development mechanisms

**Annual report of the Executive Board of the clean development mechanism
to the Conference of the Parties serving as the meeting of the Parties
to the Kyoto Protocol**

Addendum

Summary

This addendum to the annual report (2005–2006) of the Executive Board of the clean development mechanism (CDM) to the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (COP/MOP) (FCCC/KP/CMP/2006/4) covers progress made towards the implementation of the CDM from 22 July to 1 November 2006.

Prominent developments during this period included the further registration of CDM project activities, issuance of certified emission reductions and approval of methodologies for baselines and monitoring. This addendum also includes several recommendations from the CDM Executive Board of the CDM to the COP/MOP for its consideration.

Mr. José Domingos Miguez, Chair of the Board, will highlight achievements and future challenges of the CDM in his presentation to the COP/MOP at its second session.

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I. Introduction

A. Scope of the report

1. This addendum to the annual report of the Executive Board of the clean development mechanism (CDM) to the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (COP/MOP) for the period 2005–2006¹ covers progress made towards implementation of the CDM between the cut-off date for that report (22 July 2006) and 1 November 2006. Apart from reporting the work undertaken by the Executive Board during this period, this addendum reflects the outcomes of the Board's twenty-sixth and twenty-seventh meetings and includes draft decisions recommended by the Board for adoption by the COP/MOP at its second session. As is the case for the parent document, this addendum needs to be read in conjunction with detailed information on operational and procedural matters available on the UNFCCC CDM website.²

2. The Chair of the Executive Board, Mr. José Domingos Miguez, will present the annual report and this addendum, as well as developments between 1 and 6 November 2006, to the COP/MOP at its second session.

B. Action to be taken by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol

3. The COP/MOP, at its second session, may wish to take the following actions, in addition to those identified in document FCCC/KP/CMP/2006/4:

- (a) Take note of this addendum to the annual report in accordance with the provisions of paragraphs 3 and 4 of the CDM modalities and procedures contained in the annex to decision of 3/CMP.1;
- (b) Designate the entities accredited and provisionally designated by the Board, as contained in annex I to this addendum;
- (c) Consider and adopt the recommendation for regional distribution of CDM project activities as contained in annex III to this addendum;
- (d) Confirm that given the operational nature of the CDM process, the Board may suspend/withdraw accreditation and re-instate/re-accredit a designated operational entity (DOE) between two sessions of the COP/MOP;
- (e) Provide guidance to the Board on:
 - (i) Whether carbon dioxide capture and storage (CCS) projects may be considered as CDM project activities taking into account issues relating to the project boundary, leakage and permanence, taking into account the recommendation provided by the Board and other inputs as requested by the COP/MOP at its first session;
 - (ii) Revised definitions for small-scale project activities;

¹ FCCC/KP/CMP/2006/4.

² This website serves as the central repository as it contains the reports of the meetings of the Executive Board, including documentation on all matters agreed by the Board, notably regarding the registration of CDM project activities, the approval of methodologies, the accreditation and provisional designation of operational entities, and the issuance of certified emission reductions. It also serves as the link to the CDM registry.

- (iii) A category for the calculation of emission reductions for small-scale project activities that propose the switch from non-renewable biomass to renewable biomass.

II. Work undertaken since the first session of the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol

A. Accreditation process for operational entities

4. In the period covered by this addendum, the Board accredited and provisionally designated three operational entities for validation (VAL) and one for verification/certification (VER) in specific sectors. Annex I to this addendum contains the list of entities accredited and provisionally designated by the Board and recommended for designation by the COP/MOP at its second session. The Board also decided to conduct spot-checks of three DOEs when considering requests for reviews. The assessment work on these three cases is under way.

5. In this period, four new applications for accreditation have been received, which brings the total number of applications to 39. There are currently 36 applications under consideration as three entities withdrew their applications. It may be noted that, of the last four applications received for accreditation, three are from entities located in Parties not included in Annex I to the Convention (non-Annex I Parties) and one is an entity in a Party with an economy in transition. Ten applications are from entities located in non-Annex I Parties.

6. The Board agreed to a further revision of the accreditation procedure. The procedures allow, for operational reasons, that the Board may suspend/withdraw accreditation and re-instate/re-accredit a DOE between two sessions of the COP/MOP. The procedure will enter into force if the COP/MOP confirms that the Board may do so.

7. The Board noted that the institutional set-up of the CDM relating the Board and the DOEs with the project participants, as defined in, inter alia, the provisions in the CDM modalities and procedures³, paragraphs 20, 26, 35, 36, 37, 61, 62, is based on the premise that the Board and DOEs act in a concerted manner, in particular when facing the high volume of activity the CDM has been able to attract.

8. The Board noted that while the DOEs provide the service to the Board of assessing the validity of project participants' proposed activities and establishing the amount of certified emission reductions (CERs) to be issued, they are in a contractual relationship with the project participants. The Board perceives that this may potentially compromise the important role of the DOEs in the regulatory set up.

9. The Board will continue to take measures to avoid deliverables of the DOEs being compromised by potential conflict of interest, such as through the establishment of the registration and issuance team, as well as through enhanced dialogue, the DOE forum and coordination workshops.

B. Methodologies for baselines and monitoring plans

Work on methodologies

10. During the reporting period covered by this addendum, the Board approved 10 additional methodologies for non-afforestation/reforestation project activities, one of which was a consolidation of two approved methodologies, bringing the number of approved methodologies to 46 and that of

³ Modalities and procedures for a clean development mechanism; annex to decision 3/CMP.1.

consolidated methodologies to 10. The full list of approved methodologies is available on the UNFCCC CDM website.⁴

11. The Board approved the first methodological “tool to determine methane emissions avoided from dumping waste at a solid waste disposal site”, which may be referred to in methodologies, in a similar fashion to referencing the “tool for assessment and demonstration of additionality” in approved methodologies.

12. The Board approved the second “methodological tool” to identify the baseline scenario and demonstrate additionality, referred to as the “combined tool”. This tool is applicable to project activities where all identified alternative baseline scenarios are under the control of project participants only. The development of the combined tool took into account the public comments received in response to calls for inputs on “new proposals to demonstrate additionality, including options to combine the selection of the baseline scenario and the demonstration of additionality”, “proposals to improve the tool for the demonstration and assessment of additionality” and an assessment of the application the current version of the additionality tool in a subset of registered project activities. The existing approved tool for the demonstration of additionality continues to be available to project participants. Furthermore, the Board shall provide further guidance in order to assist with the application of the additionality tool, in particular for the verification of additionality by DOEs. The Board therefore shall develop a brief manual to accompany the combined tool and the tool for demonstration of additionality.

Guidance to project developers

13. The Board provided guidance and clarifications on matters such as:

- (a) Double counting of emission reductions for situations concerning the consumption only as well as the consumption and production of biofuel within the same project boundary;
- (b) Broadening of methodologies the Board requested its Methodologies Panel (Meth Panel) to continue work on broadening methodologies in accordance with paragraphs 23 and 24 (a) and (b) of decision 7/CMP.1, by considering new methodologies that are clearly applicable to more than one project activity or can be consolidated with approved methodologies as a priority. Such proposed methodologies shall be clearly substantiated by the project proponents when submitting a proposal for new methodologies. It also requested the Meth Panel to limit the revision of approved methodologies to ensure that there is a minimum of six months between revisions, where possible. Taking into account all implications, the Chair of the Meth Panel may, however, recommend an earlier revision if it is deemed important. At the same time the Board called for inputs from the DOEs to propose revisions to approved methodologies. The call for inputs will be open for a period of two months;
- (c) Programme of activities in order to provide further guidance to operationalize decision 7/CMP.1, paragraph 20, on the consideration of project activities under a programme of activities as a single clean development mechanism project activity, the Board considered a proposal prepared by the Meth Panel, as required by the secretariat, on the definitions of a “programme of activities” and a “policy” as well as a draft proposal for structuring a “programme of activities” so that it could be registered as a single project activity. It requested the secretariat to prepare a revised proposal for consideration by the Executive Board at its twenty-eighth meeting, taking into account the inputs provided by the Board at its twenty-seventh meeting;

⁴ <<http://cdm.unfccc.int/methodologies>>.

- (d) Its recommendation on CCS as a CDM project activity, as requested by the COP/MOP at its first session. The recommendation is based on qualitative consideration of the proposed new methodology cases NM0167 and NM0168 for CCS as a CDM project activity and the small-scale methodology submission SSC_038. The recommendation is contained in annex II of this addendum;
- (e) Guidance on criteria for the consolidation and revision of methodologies.

Guidance required from the COP/MOP

14. The Board requests the COP/MOP to consider whether CCS project activities may be considered as CDM project activities, taking into account the Board's recommendation on the submission of proposed methodologies, the report on the workshop considering CCS as CDM project activities organized in conjunction with the twenty-fourth session of the Subsidiary Body for Scientific and Technological Advice and the submissions on the consideration of CCS as CDM project activities, taking into account issues relating to project boundary, leakage and permanence.

C. Afforestation and reforestation project activities

Work on methodologies

15. During the reporting period of this addendum, the Board approved one additional methodology for afforestation and reforestation (A/R) project activities, bringing the total number of approved methodologies for A/R project activities to four. The Board further revised one approved A/R methodology and the approved small-scale A/R methodology.

16. The Board continued to institute a number of measures to help streamline the A/R methodologies process, including by appointing two additional members to the A/R working group and thereby increasing the group's membership to eight.

Guidance to project developers

17. The Board, at its twenty-sixth and twenty-seventh meetings, provided guidance and clarifications on matters such as:

- (a) Accounting for emissions of N₂O from fertilizer application;
- (b) Revised guidance on the demonstration of the eligibility of lands for A/R project activities;
- (c) Revisions to guidelines and forms in order to further streamline the process of submission of new A/R methodologies and the introduction of new forms to facilitate the revision and submission of queries relating to approved A/R methodologies.

D. Simplified modalities and procedures for small-scale clean development mechanism project activities

18. During the reporting period covered by this addendum, the Board approved one methodology for small-scale project activities, bringing the total of approved methodologies for small-scale project activities to 20.

Guidance to project developers

19. The Board provided guidance and clarifications on matters such as:

- (a) The definition of "same technology/measure" in the CDM glossary of terms;

- (b) An eligibility limit in terms of aperture area for thermal applications of solar energy project activities.

Guidance required from the COP/MOP

20. In response to a request by the COP/MOP, at its first session, to review the simplified modalities, procedures and definitions of small-scale project activities and, if necessary, make appropriate recommendations, the Board proposed the following revisions to the definitions of small-scale project activities referred to in paragraph 6 (c) of decision 17/CP.7:

- (a) Type I project activities should remain the same, such that renewable energy project activities shall have a maximum output capacity of 15 MW (or an appropriate equivalent);
- (b) Type II project activities or those relating to improvements in energy efficiency which reduce energy consumption, on the supply and/or demand side, shall be limited to those with a maximum output of 60 GWh per year (or an appropriate equivalent);
- (c) Type III project activities, otherwise known as other project activities, shall be limited to those that result in emission reduction of less than or equal to 60 kt CO₂ equivalent (ktCO₂e) annually.

21. The Board noted that the threshold value of energy savings of 15 GWh per year may have been a barrier to the development of type II project activities. Furthermore, the Board considered that it was more appropriate to use a threshold based on emission reductions rather than one based on direct emissions for defining small-scale type III project activities.

22. In recommending these revisions, the Board took into account the need to make the definitions of the three types equivalent to each other. In doing so it decided to maintain the current definition of type I project activities. Furthermore, the Board proposed a revised definition of type II project activities based on the electrical energy generation capacity of a 15 MW power generating unit operating for 4000 hours a year, and revised the definition of type III project activities based on the emission reductions of currently registered type I project activities with the highest projected annual emission reductions.

23. Furthermore, regarding the interim measure as proposed by the Board at its twenty-fourth meeting, the Board clarified that for the simplified baseline and monitoring methodologies for type III small-scale projects, the 25 ktCO₂e limit is an applicability criteria. These approved methodologies are therefore applicable to project activities that demonstrate that the projected emission reductions are less than 25 ktCO₂e only. The phrase “the annual emission reduction for that particular year is capped at 25 ktCO₂e” should be interpreted in light of paragraph 8 of Annex II of decision 4/CMP.1, and while it may be possible that the emission reductions might, as an exception, exceed 25 ktCO₂e for some years during the crediting period, the emission reductions during these years will be capped at 25 ktCO₂e.

24. In response to a request by the COP/MOP at its first session, to develop, as a priority, a simplified methodology “for calculating emission reductions for small-scale project activities that propose the switch from non-renewable biomass to renewable biomass”, the Board considered the revised recommendations of two draft categories by the Small Scale Working group. These recommendations, which took into account that only A/R projects can be registered as project activities with emission reductions arising out of carbon stock changes under the CDM, proposed to use fossil fuels commonly used by local consumers for meeting similar thermal energy needs as the baseline. The discussions in the Board showed a divergence of opinions, stressing on the one hand the social and health benefits of such projects and concerns with establishing realistic baselines and, on the other hand, possible leakage effects and incentives for further deforestation, which could not be overcome by further revision of the proposed recommendations.

E. Matters relating to the registration of clean development mechanism project activities

Work relating to requests for registration of project activities

25. During the reporting period, 22 July 2006 to 1 November 2006, the following statistics relating to requests for registration were recorded:

- (a) 372 proposed project activities were submitted to DOEs for validation at an average rate of approximately 110 per month⁵;
- (b) 163 new requests for registration were received by the Board;
- (c) 139 (81 of the new requests and 58 requests submitted prior to the reporting period were dealt with);
- (d) 135 of these requests for registration were registered by the Board (78, or 58 per cent, were small scale) resulting in a total of 387 registered project activities⁶;
 - (i) 110 of the 135 registered project activities were registered automatically. This meant that fast-track registration occurred in 81 per cent of those cases;
 - (ii) 6 were registered following consideration by the Board of a request for review and additional submissions from the project participant and/or DOE;
 - (iii) 14 were registered with corrections being made following the consideration by the Board of a request for review;
 - (iv) 5 were registered after the Board had conducted a review to ensure that guidance and rules were implemented appropriately;
- (e) 4 project activities were rejected after reviews by the Board, resulting in the registration of 97 per cent of requests for registration that had final decisions made by the Board during the reporting period.

26. Thirteen requests for deviation were submitted to the Board during the reporting period. Of these, two related to deviations from approved methodologies discovered in the process of validation and 11 related to deviations from provisions for a registered project activity discovered in the process of verification. The Board provided a response to all of these requests⁷:

Work on procedures

27. The Board has facilitated and clarified tasks relating to the registration of proposed CDM project activities by issuing the following procedures and clarifications:⁸

- (a) Guidance on retroactive crediting – the Board agreed at its twenty-sixth meeting that, in order to operationalize paragraph 4 of decision 7/CMP.1, to clarify that project activities that started in the period between 1 January 2000 and 18 November 2004 that have either submitted a new methodology by 11 January 2006 or have requested validation by a DOE by 31 December 2005 can request retroactive credits if:

⁵ Details on proposed project activities are available for comment at <<http://cdm.unfccc.int/Projects/Validation>>.

⁶ A full list of registered CDM project activities is available at <<http://cdm.unfccc.int/Projects/registered.html>>.

⁷ For non-confidential cases the Board's guidance is available at <http://cdm.unfccc.int/Projects/Deviations>.

⁸ See <<http://cdm.unfccc.int/Reference/Procedures>> and <<http://cdm.unfccc.int/Reference/Guidclarif>>.

- (i) The request for registration of the project activity is submitted by the DOE through the electronic interface by 31 December 2006, midnight GMT;
 - (ii) Any required registration fee is received by the secretariat before 31 January 2007;
 - (iii) The request is complete and published on the UNFCCC CDM website by 15 February 2007;
- (b) Further clarification on procedures relating to retroactive crediting – the Board reiterated that only those project activities submitted for validation prior to 31 December 2005, whose project design documents (PDDs) were complete and suitable for publication for the global stakeholder consultation and which met all other requirements for prompt start CDM projects, would qualify to claim retroactive credits. The Board further clarified that these guidelines also apply to project activities which were submitted for validation prior to 31 December 2005 to one DOE and transferred at a later stage to another DOE;
- (c) Clarifications on the procedures for review referred to in paragraph 41 of the CDM modalities and procedures.

**F. Matters relating to the issuance of certified emission reductions
and the clean development mechanism registry**

Work relating to the issuance of certified emission reductions

28. During the reporting period, 6,288,357 CERs were issued as a result of 49 requests. Of these 49 requests, 44 were considered final 15 days after publication. In three cases, the Board instructed the CDM registry administrator to issue the requested CERs following the consideration of a request for review and clarifications provided by the DOE. In one case the Board instructed the CDM registry administrator to issue the requested CERs following the consideration of a review and clarifications provided by the DOE. In one case the Board instructed the CDM registry administrator to issue the requested CERs following corrections being made by the DOE and project participants in response to the outcome of a request for review. In three cases the Board is awaiting corrections to be made by the DOE and/or project participants following the consideration of a review.

29. During the reporting period the Board rejected two requests for issuance.

30. As at 1 November 2006, six requests for issuance remain within the 15-day period for requesting a review and a request for review of one request for issuance will be considered at the twenty-eighth meeting of the Executive Board.

31. As at 1 November 2006, 71 monitoring reports had been made public by DOEs and were awaiting a corresponding request for issuance as part of the verification process.

32. The more than 1,200 project activities for which PDDs were made public are expected to generate more than 1.4 billion CERs by the end of the first commitment period, assuming that none of the activities will request an extension of the crediting period. The 387 project activities already registered account for more than 660 million of the 1.4 billion CERs.

Work on procedures

33. In order to facilitate the preparation and consideration of requests for issuance, the Board adopted the following procedures and clarifications:⁹

- (a) Procedures for revising monitoring plans in accordance with paragraph 57 of the CDM modalities and procedures;
- (b) To instruct DOEs that, in performing verification;
 - (i) DOEs shall ensure that all of the monitoring parameters required by the registered monitoring plan are reported by the project participants at the pre-defined intervals. Project participants are advised that data should be provided in the monitoring report before a request for issuance is made to a DOE, and submitted to the secretariat in a format which allows for assessment by the Registration and Issuance Team (RIT) member appointed to conduct the appraisal;
 - (ii) When it is discovered that activity levels or non-activity parameters have not been monitored by the project participants in accordance with the registered monitoring plan, the DOE shall make the most conservative assumption theoretically possible in finalizing the verification report;
- (c) Clarifications to facilitate the implementation of the procedures for review referred to in paragraph 65 of the CDM modalities and procedures.

CDM registry

34. As at 1 November 2006, 32 holding accounts had been opened in the CDM registry, three of which are permanent, and 55 requests for forwarding had been processed by the CDM registry administrator.

35. The CDM registry will be used in November 2006 to conduct pilot testing of the international transaction log (ITL). Full initialization testing between the ITL and the CDM registry is scheduled to take place in January 2007 to allow the communication link between these by April 2007.

G. Relationship with designated national authorities

36. The first meeting of the designated national authorities (DNA) forum was held on 27–28 October 2006, in Bonn, Germany. The meeting was attended by 81 DNA representatives and national focal points from both Parties included in Annex I to the Convention and non-Annex I Parties. The DNA forum at its first formal meeting considered its rules of procedure and agreed to adopt them at its next meeting. The forum elected a committee of five representatives from five United Nations regions and elected two co-chairs from this committee. The forum identified several issues to further discuss and bring to the attention of the Board. The DNA representatives shared their experiences and a general exchange of views took place through a lively discussion. The participants expressed their appreciation for this opportunity and emphasized the need for frequent meetings and other means for exchanging views and sharing information.

37. The Board interacted with the DNA forum to share information on recent developments and hear the experiences of and issues faced by DNAs. The participants highlighted issues of mutual concern and stressed the need for the Board to take these issues into consideration in its role as the regulatory body

⁹ See <<http://cdm.unfccc.int/Reference/Procedures>> and <<http://cdm.unfccc.int/Reference/Guidclarif>>.

for the operationalization of the CDM. Participants from non-Annex I Parties, in particular, stressed the need for capacity-building in order to enhance the involvement of developing countries in the CDM.

38. The Board expressed its deep appreciation to the Government of Japan for funding the first meeting of the DNA forum. The Board agreed, due to the importance and the benefits of the DNA forum, to include the cost of two forum meetings per year in the CDM management plan.

39. In addition, an informal meeting of DNAs is planned to be held on 13 November 2006 in Nairobi, Kenya, in conjunction with the second session of the COP/MOP.

III. The clean development mechanism management plan¹⁰ and resources for work on the clean development mechanism

Management plan 2007–2008

40. The Board, at its twenty-seventh meeting, in accordance with paragraph 13 of decision 7/CMP.1, approved the first version of the CDM management plan (MAP) to cover activities in 2007 and 2008. The CDM MAP 2007, contained in document FCCC/KP/CMP/2006/4/Add.1 (Part II), is based on lessons learned in 2006 and presents the management plan in focal areas such as work on methodology, accreditation, registration and issuance.

41. The Executive Board, aware of the responsibility transferred to it by the provisions included in 7/CMP.1 on budgetary matters, invited the COP/MOP to take note of the CDM MAP. It further invited the COP/MOP to provide guidance or clarification, as appropriate, to the Board and to the secretariat on the implementation of subparagraph 13 (a) of decision 7/CMP.1 with a view to ensuring that the arrangements are satisfactory and to provide the necessary accountability.

42. With respect to the establishment of an Executive Committee of the Executive Board, the Board agreed to continue consideration of this issue at its twenty-eighth meeting.

Resources for the work on the CDM

43. Including the carry-over from 2005, and the income received by 1 November 2006¹² and assuming no further contributions from Parties in 2006, the total resources available in 2006 were USD 9.3 million. Based on expenditures so far, and planned expenditures for the remainder of 2006, it is expected that there will be a carry-over of USD 4.4 million for use in 2007. At expected rates of expenditure, and assuming no further income, these resources will be sufficient to support operations in the CDM-MAP until early in the second quarter of 2007.

44. In accordance with decision 7/CMP.1, income generated from share of proceeds (SOPs) and methodologies and registration fees are set aside to support the work of the CDM, which according to the decision was expected to become self-sufficient in January 2008. Current realistic, but conservative, estimates of income generated from fees and SOPs indicate that the operating cushion will actually be achieved towards the end of the second quarter of 2007. The expectation is that the CDM MAP could start to be fully financed from the accumulated fees and SOPs as of the end of the second quarter of 2007. Given the analysis in paragraph 43 above, however, there would be a period of 2 to 3 months during which activities would not be covered from the funding cushion, i.e. there would be a shortfall of resources of approximately USD 2.5 million until the CDM will start to be fully self-financed.

¹⁰ The CDM management plan is contained in FCCC/KP/CMP/2006/4/Add.1 (Part II).

¹² Including the contributions from Germany, Norway and Spain that are about to be credited onto the UNFCCC's account.

Therefore, the Board invited Parties that still have outstanding pledges to pay those pledges as soon as possible to cover this expected shortfall during the second quarter of 2007.

IV. Summary of decisions

45. The same provisions as indicated in the parent document apply.

Annex I

List of provisionally designated operational entities

Entities accredited and provisionally designated by the Board and recommended for designation by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol for validation (VAL) and verification/certification (VER) for specific sectoral scopes

Name of entity	Sectoral scopes	
	VAL	VER
TÜV SÜD Industrie Service GmbH	8,9	8,9
KPMG Sustainability B.V	13	
Lloyd's Register Quality Assurance Ltd	13	

Annex II**Recommendation on carbon dioxide capture and storage¹**

1. This recommendation by the Executive Board of the clean development mechanism (CDM) is based on the assessment of three proposed new methodologies for carbon dioxide capture and storage (CCS) project activities and identifies a number of related issues. The identification of issues is based on the qualitative assessment by the Executive Board, the Board's Methodologies Panel, and the desk reviews of proposed new methodologies NM0167, NM0168 and SSC_038.
2. The approaches and procedures suggested by the submitted methodologies do not address the methodological and accounting issues in an appropriate and adequate fashion, and thus cannot be approved in CDM methodologies in their current form. In addition, it is questionable whether some issues can be resolved without further guidance from the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol and/or a technical body on CCS.
3. Two categories of methodological issues have been identified: (1) methodological issues that are comparable in nature to those faced by other proposed CDM methodologies – identification of alternative scenarios and baseline selection, analysis of additionality and carbon dioxide leakage/seepage, calculation algorithms for baseline emissions, project emissions and emissions reductions, sub-national project boundary questions, etc; and (2) issues that go beyond the nature of other proposed CDM methodologies, i.e. issues that are at the frontier of scientific knowledge or engineering practice (site selection criteria, monitoring methods) or that present unique accounting or liability challenges (permanence, in other words the implications of accidental, unanticipated or intentional future releases of stored carbon dioxide (CO₂) from the reservoir).
4. Among the issues in the second category, it may be helpful to differentiate between policy or legal issues and issues of a largely technical nature (i.e. which require geological, petroleum engineering and other specific expertise in order to be addressed). Based on the assessment of the methodologies, the following issues have been identified:
 - (a) Policy or legal issues;
 - (i) Acceptable levels of long-term physical leakage (seepage) risk and uncertainty (e.g. less than X per cent seepage by year Y with a likelihood of Z per cent);
 - (ii) Project boundary issues (such as reservoirs in international waters, several projects using one reservoir, etc) and national boundaries (approval procedures for projects that cross national boundaries);
 - (iii) Long-term responsibility for monitoring the reservoir and any remediation measures that may be necessary after the end of the crediting period (i.e. liability);
 - (iv) Accounting options for any long-term seepage from reservoirs (e.g. new modalities and procedures such as those for land use, land use change and forestry (LULUCF));

¹ The executive summary only has been provided. For the basis that lead to the above recommendation, please refer to annex 13 of the twenty-sixth meeting of the Executive Board at <<http://cdm.unfccc.int/EB>>.

- (b) Issues of a largely technical and methodological nature:
- (i) The development of criteria and a step-wise guidance for the selection of suitable storage sites with respect to the release of greenhouse gases, and how this relates to applicability conditions for methodologies;
 - (ii) Guidance on the development of adequate and appropriate monitoring methodologies for physical leakage (seepage) from the storage site;
 - (iii) Guidance related to the operation of reservoirs (e.g. well sealing and abandonment procedures) and remediation measures, and how these may need to be addressed in baseline and monitoring methodologies.

5. It is important to emphasize that the resolution of these technical and methodological issues, in particular the suitability of storage sites, depends also upon guidance with respect to policy and legal issues, in particular on acceptable levels of long-term physical leakage (seepage) risk and uncertainty.

Summary of submitted projects methodologies

6. NM0167 (CDM project design document): The White Tiger Oil Field Carbon Capture and Storage project in Vietnam) addresses project activities that capture CO₂ from a power plant and transport it by pipeline for injection into geological reservoirs, including the use in enhanced oil recovery (EOR) operations. The project boundary includes capture, transport, injection, where relevant, EOR installations, and the storage reservoir, but excludes the power plant. Leakage is assumed to be negligible (the issue of whether the additional oil recovered may or may not affect global emissions is not discussed). The methodology proposes that if physical leakage (seepage) is below 0.1 per cent per annum², the emission reductions from the project activity are deemed permanent, and if seepage is higher, permanence is assumed to be insufficient in which case all CERs arising from the project activity are cancelled. Monitoring is carried out primarily by direct measurements at the injection point, and underground via 4D seismic analysis. The baseline is continued EOR with seawater. Site selection is done according to criteria provided in an IEA GHG R&D Programme publication on CCS³.

7. NM0168 (CDM project design document): The capture of the CO₂ from the liquefied natural gas (LNG) complex and its geological storage in the aquifer located in Malaysia) addresses project activities that capture a mixture of waste acid gases from natural gas processing plants and LNG plants and stores this gas mixture, which consists primarily of CO₂, in underground aquifers or abandoned oil/gas reservoirs. In order to sell the gas, the CO₂-rich acid gas must be separated and removed. Separation (capture) facilities are therefore not included in the project boundary, which consists of compression, transport and the storage reservoir. Physical leakage (seepage) is estimated based on monitoring procedures, which involve the monitoring of the CO₂ stream into the reservoir and the potential seepage paths identified through seismic measurements. The baseline is the incineration of the acid gas rather than the storage underground. For site selection criteria, the methodology refers to data from the Intergovernmental Panel on Climate Change Special Report on CCS, which has been incorrectly

² In the methodology, this is explained as follows: A figure of 1000-year permanence is the most commonly quoted in reports concerning CCS. This is equivalent to a seepage rate of 0.1 per cent/yr or 0.7 per cent for a seven-year crediting period. Projects in strict compliance with the applicability conditions of this methodology can claim “permanent storage of CO₂”. Note that, if we assume a seepage rate of 0.1 per cent per year, about 63 per cent of the CO₂ stored would be released after 1000 years.

³ IEA Greenhouse Gas R&D Programme. 2003. *Barriers to overcome in implementation of CO₂ capture and storage (2): Rules and standards for the transmission and storage of CO₂*. Report number: PH4/23.

interpreted as a performance norm. Permanence is accounted for by discounting certified emission reductions or seepage beyond the crediting period based on an ex-ante estimated seepage rate.

8. SSC_038 (Anthropogenic ocean sequestration by changing the alkalinity of ocean surface water (alkalinity shift)) addresses project activities that use CO₂ from power station flue gases and pump it through flowing seawater in which porous baskets containing limestone have been placed. The resulting reaction converts the CO₂ contained in the flue gas to bicarbonate. Only a fraction of the flue gases pumped in this way will be neutralized and remain in solution. This fraction varies but is expected to be about 50 per cent. The project boundary is the physical boundary of the power station and cooling water channel, and extends into the sea, where the boundary is delineated by a 20 km radius from the cooling water discharge point. Leakage may occur through the use of additional electricity to achieve a constant flow rate past the limestone baskets. Monitoring comprises the measurement of pH, temperature and the estimation of dissolved organic carbon⁴.

⁴ Based on an unpublished manuscript of the United States Department of Energy (1994).

Annex III

Regional distribution of clean development mechanism project activities

I. Mandate

1. Taking into account the provisions of the Marrakesh Accords reflected in decisions 3/CMP.1, 4/CMP.1 and 7/CMP.1 especially the last in which paragraphs 3236 requested Parties to submit to the secretariat, by 31 May 2006, their views on systematic or systemic barriers to the equitable distribution of clean development mechanism (CDM) project activities and options to address these barriers, for consideration by Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol at its second session. Such submissions from Parties are contained in document FCCC/KP/CMP/2006/MISC 1.
2. By its decision 7/CMP.1 (paragraph 33), the COP/MOP also requested the Executive Board of the CDM to report to it, at its second session, information on systematic or systemic barriers to the equitable regional and subregional distribution of clean development mechanism project activities, and options to address these issues.
3. In addition, decision 29/CMP.1 on capacity-building relating to the implementation of the Kyoto Protocol in developing countries and decision 30/CMP.1 reaffirmed the framework for capacity-building and presented priority areas specifically for the implementation of the Kyoto Protocol. Subparagraphs (d) and (e) of decision 29/CMP.1 concern the provision of support for “broader participation” and “improving geographical distribution” respectively.

II. Principles

4. The Executive Board agrees that to further consider the issue of regional distribution of CDM project activities it must be kept in mind that:
 - (a) Each Party not included in Annex I to the Convention (non-Annex I Party) should have an opportunity to realize its full potential to access the opportunities offered by the CDM, especially and with particular attention to African countries and small island developing States;
 - (b) The term equitable distribution should not be taken to mean equal distribution of CDM project activities (e.g. the same number of projects in each country; preferences for small- or large-scale projects; an equal number of certified emission reductions (CERs) generated).

III. Progress to date

5. The following measures have been undertaken so far by the Board to alleviate some of the concerns on equitable geographic distribution:
 - (a) Simplified modalities and procedures for small-scale projects;
 - (b) Removal of the registration fee for projects with emission reductions below 15,000 tonnes per year;
 - (c) Lower amount of share of proceeds for the first 15,000 CERs issued per year;

- (d) Differentiation in the method of payment of the application fee for applicant entities from non-Annex I Parties;
- (e) Establishment of the Designated National Authorities Forum;
- (f) Participation in subregional and global capacity-building events or awareness raising activities;
- (g) The CDM Bazaar (under way).

IV. Barriers

6. The Executive Board acknowledged the existence of barriers at different levels and different stages and is cognizant of the fact that only a few of them can be addressed at the Board level, others can be addressed at the Party level and yet others by the public and private sectors in countries.

7. Considering the market-based nature of the CDM and that the private sector will naturally gravitate to low-risk, high opportunity locations and projects, some of the main obstacles are financial; insufficient access to funds for technical assistance and capacity-building and insufficient access to project finance and risk management tools.

8. The following are some of the other barriers:

- (a) Structural and institutional issues, such as weak institutional and administrative capacity relating to the development of CDM project activities;
- (b) CDM-specific capacity issues, such as lack of CDM-related awareness and experience in relevant sectors, investment conditions and small size of projects;
- (c) CDM process issues, such as facilities and procedures not being in place, complexity of processes and methodologies, insufficient guidance on bundling and size limit of bundles, and lack of clarity with regard to the relationship of official development assistance involvement in the project cycle;
- (d) Uncertainty of the role of CDM post 2012.

V. Recommendations

9. The Executive Board, taking into account the mandate received, agreed on the following recommendations to be submitted to the COP/MOP at its second session for its further consideration and guidance:

- (a) Financing and financial tools
 - (i) Encourage Annex I Parties to establish CDM financial facility(ies)¹ to help non-Annex I Parties, especially least developing countries (LDCs) and with particular attention to African countries and small island developing States with less CDM project activities, to cover the start-up costs relating to the development of CDM project activities, in particular by:

¹ More than one facility would be possible depending on how Annex I Parties choose to group or cooperate on this issue.

- providing seed funding for developing and implementing CDM project activities which could be reimbursed from the generation of CERs from such projects;
 - supporting the development of methodologies applicable to LDCs and other non-Annex I Parties with less CDM project activities;
 - organizing hands-on training for project developers, local experts, DNAs and other stakeholders, as necessary;
 - providing support to develop expertise for the development of project design documents (PDDs);
- (ii) Contributions by Annex I Parties to the above facility(ies) would be voluntary and reimbursable from the CERs generated by the project activities implemented through the facility;
- (iii) Noting that CDM is only complementary to other sources of funding for realizing a CDM project activity, encourage Annex I Parties to explore ways to develop financial tools to secure funding for the development of CDM project activities that can help developing countries and non-Annex I Parties with economies in transition with lack of access to financing, taking also into consideration activities of multilateral financial institutions which are investing in enhancing the capacity in those countries;
- (iv) Encourage financial institutions to provide seed funding to develop CDM project activities using CERs as collateral;
- (b) Capacity-building and training
- (i) Encourage Parties and United Nations organizations to focus on capacity-building areas that are specific for the development of CDM project activities, for example development of PDDs, assessing proposals, awareness-raising, financial engineering, information sharing and facilitating the application of applicant entities (AEs) from Africa and other non-Annex I Parties, and the development of methodologies;
- (ii) Encourage Parties and United Nations organizations to also focus on capacity-building activities that build the institutional capacity which can assist Parties in developing CDM project activities and DNAs, in particular in countries with low emissions and less projects;
- (iii) Support non-Annex I Parties to create an organized infrastructure which will facilitate capacity-building for the implementation of the Kyoto Protocol provisions, and namely to establish permanent CDM offices at the national level in non-Annex I Parties with a local expert team, which would develop a portfolio of CDM projects using experts from an established roster of experts in the field;
- (c) Co-operation
- (i) Encourage regional cooperation in order to facilitate the exchange of experience and information at all levels;

- (ii) Encourage Annex I Parties engaged in the CDM market to pay particular attention to a more equitable distribution of CDM project activities;
 - (iii) Encourage Parties to cooperate bilaterally in order to develop and implement CDM project activities;
 - (iv) Encourage co-operation between the DNAs of Annex I and non-Annex I Parties, in particular through the DNA forum;
- (d) Involvement of other stakeholders
- (i) Encourage designated operational entities, to establish offices and partnerships in African countries and small islands developing States in order to contribute to a more equitable distribution of CDM project activities;
 - (ii) Encourage a greater involvement of national industry associations and local banks in the CDM market;
 - (iii) Encourage the participation of regional banks in the development and promotion of CDM project activities;
 - (iv) Encourage synergy between all intergovernmental organizations in coordinating activities relating to capacity-building and technical and financial assistance;
- (e) Request the UNFCCC secretariat to develop a public awareness programme to facilitate the availability and sharing of information on the CDM process in non-Annex I Parties.
