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Second review of the Kyoto Protocol pursuant to its Article 9

Compilation and analysis of available information on the scope, effectiveness and functioning of the flexibility mechanisms under the Kyoto Protocol

Note by the secretariat

Summary

This note compiles and analyses available information in relation to the scope, effectiveness and functioning of the flexibility mechanisms under the Kyoto Protocol. The note focuses on the two project-based mechanisms under the Kyoto Protocol, namely the clean development mechanism (CDM) and joint implementation (JI). It considers possible improvements to institutional arrangements and governance in relation to the CDM Executive Board, the Joint Implementation Supervisory Committee (JISC), designated operational entities under the CDM and accredited independent entities under JI, as well as possible improvements to the rules and procedures for the two mechanisms, including technical issues such as additionality and methodologies.

The note draws on a number of information sources, including submissions by Parties, the work of the CDM Executive Board and the JISC, and issues for consideration in the current commitment period identified by Parties during the work of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol.

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I. Introduction

A. Mandate

1. The Subsidiary Body for Implementation (SBI), at its twenty-eighth session, continued the preparations for the second review of the Kyoto Protocol pursuant to its Article 9, which is to take place at the fourth session of the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP). In this context, the SBI requested the secretariat to prepare an information note to compile and analyse available information on ways and means to enhance equitable regional and subregional distribution of projects under the clean development mechanism (CDM) and the scope, effectiveness and functioning of the flexibility mechanisms under the Kyoto Protocol. It further requested the secretariat to make the note available to Parties prior to the pre-session workshop referred to in decision 4/CMP.3, paragraph 11.^{1, 2}

2. At the same session, the SBI invited Parties to submit to the secretariat, by 19 September 2008, for compilation and synthesis, their views on: (1) ways and means to enhance equitable regional and subregional distribution of CDM projects; and (2) how the current institutional arrangements, governance, rules and procedures of the CDM and joint implementation (JI) improved in the first commitment period in order to enhance their functioning and effectiveness.³ These submissions are contained in document FCCC/KP/CMP/2008/MISC.2.

B. Scope of the note

3. This note compiles and analyses information on the second part of the mandate mentioned in paragraph 1 above, namely in relation to the scope, effectiveness and functioning of the flexibility mechanisms under the Kyoto Protocol.⁴ The note focuses on the project-based mechanisms under the Kyoto Protocol: the CDM and JI.

4. Chapters II and III of the note consider possible improvements to institutional arrangements and governance in relation to the Executive Board of the CDM and designated operational entities (DOEs) under the CDM, respectively. Chapter IV considers possible improvements to the rules and procedures for the CDM, including technical issues such as additionality and methodologies. Finally, chapter V discusses the potential to apply possible improvements in JI.

5. Given the complexity and number of variations on the possible improvements to the flexibility mechanisms, the discussion in this note is neither exhaustive nor conclusive. The preparation of this note has focused on compiling suggested improvements and providing sufficient elaboration of them to give a sense of what they could mean in practice and how they may be applied. Many of the ideas discussed in this note would require more analysis and development if they were to be taken further.

6. This note does not discuss possible improvements to the mechanisms that could specifically address the issue of equitable regional and subregional distribution of CDM projects, although some of the possible improvements discussed in this note may have potential to enhance such distribution.

7. The note draws on the following information sources:

- (a) The submissions by Parties referred to in paragraph 2 above;

¹ FCCC/SBI/2008/8, paragraph 109 (d) (ii).

² The pre-session workshop is planned for 22–23 October 2008 in Athens, Greece.

³ FCCC/SBI/2008/8, paragraph 109 (d) (iii).

⁴ The first part of the mandate is addressed in document FCCC/KP/CMP/2008/INF.2.

- (b) Details of work undertaken in the context of the CDM Executive Board and the Joint Implementation Supervisory Committee (JISC);⁵
- (c) Issues relating to emissions trading and the project-based mechanisms under the Kyoto Protocol identified by Parties during the resumed fifth session of the Ad Hoc Working Group on Further Commitments for Annex I Parties under the Kyoto Protocol (AWG-KP) that may be considered for possible application within the current commitment period, as compiled by the Chair of the AWG-KP.⁶

**C. Possible action by the Conference of the Parties
serving as the meeting of the Parties to the Kyoto Protocol**

8. The CMP may wish to consider the compilation and analysis contained in this information note in undertaking the second review of the Kyoto Protocol.

II. Possible improvements to institutional arrangements and governance of the clean development mechanism in relation to the Executive Board

A. Delegation of technical decision-making

9. Some Parties wish the supervisory role of the CDM Executive Board to be enhanced by increasing its delegation of decision-making to the secretariat and/or committees and panels established under the Board (hereinafter referred to collectively as the support structure). Under this proposal, decisions would be taken by the support structure on the basis of clear guidance provided by the Executive Board. The Board itself would focus on strategic and policy issues and improvements to the CDM system, including through the definition of standards and tools. The Board would retain full accountability for the decisions taken by the support structure.

10. The rationale for this proposal centres on allowing the Executive Board to move away from case-by-case decision-making of a primarily technical nature. These technical activities would be undertaken by full-time professional staff working in the support structure. The intention would be both to enhance the overall efficiency of the system and to allow the Executive Board to play a greater strategic and policy role in its supervision of the CDM.

11. Areas where decision-making could be delegated to the support structure could include:

- (a) Approval of baseline and monitoring methodologies, development of methodologies using benchmarks and, where appropriate, assistance in developing methodologies in areas where none are being proposed;
- (b) Accreditation of designated operational entities (DOEs);
- (c) Registration of projects and issuance of certified emission reductions (CERs), including reviews of registration and issuances cases.

12. The delegation of decision-making to the support structure would need to take place in line with a clear and comprehensive set of rules and procedures for including appropriate standards and decision criteria that apply under various circumstances. This documentation would include criteria for which issues should be forwarded to the Executive Board for decision or further guidance. Decisions taken by the support structure would be only on matters included in the documentation, and issues not addressed in the documentation would be forwarded to the Executive Board. The documentation would need to be

⁵ The UNFCCC CDM and JI websites provide access to all the meeting reports of these bodies, annual reports by these bodies to the CMP and the documentation on which their decisions were based.

⁶ FCCC/KP/AWG/2008/3, annex III.

periodically updated to take account of new issues and processes. The Executive Board could follow a set of criteria defining the circumstances under which it should become involved and any action it should take.

13. The support structure would be accountable to the Executive Board and would need to provide regular and comprehensive reports to it. This reporting could include performance indicators to provide information on the decisions taken during the reporting period, issues forwarded to the Board for its decision or guidance, expenditure information, and indicators relating to how the CDM is fulfilling expectations placed on it by the CMP. The reporting could also include feedback and proposals to the Board.

14. The Executive Board has taken a number of steps to move in this direction. In particular, the secretariat now performs many duties in support of reviews of project registration and CER issuance, and several panels have been established by the Board to make recommendations to it on, for example, methodologies and the accreditation of DOEs. However, the proposal outlined in this document to transfer the responsibility for decision-making to the support structure goes further than the steps undertaken so far.

B. Consistency and transparency of decision-making

15. Some Parties propose that the consistency and transparency of decision-making by the CDM Executive Board should be enhanced in order to reduce any scope for value judgement and improve the understanding of the decisions by stakeholders. A key prerequisite for such enhancement is to ensure that a clear and comprehensive body of rules and procedures is in place for the CDM system, including appropriate standards and decision criteria. It would also be important that, when taking decisions, the Board should take into account previous relevant decisions, and highlight and justify any divergences from those decisions and the established decision-making process.

16. The following measures could be taken to enhance consistency and/or transparency:

- (a) All decisions taken could be classified, published and indexed separately;
- (b) A classification system for decisions could be introduced;
- (c) A formal hierarchy of decisions could be established to clarify how decisions are to be made in the event of any potential conflict between decision criteria;
- (d) Each decision could reference relevant previous decisions;
- (e) A clear process could be adopted for amending or replacing previous decisions;
- (f) All decisions and their rationales could be published.

17. The Executive Board has already acted, or is in the process of concluding actions, on some of these measures. For example, the Board maintains a catalogue of decisions on the UNFCCC CDM website, which it adjusts in the light of user feedback.

18. Striving for consistency in decision-making should not imply that poor decisions taken in the past would continue to be applied in similar cases in the future. For example, it would be important to allow the Executive Board (or its support structure) the flexibility to take decisions that differ from previous decisions on similar issues in order to, for example, improve a methodology or take into account lessons learned. In such cases, it would be important to balance the need to make appropriate decisions from that point onwards against the need to ensure equal treatment of stakeholders.

C. Process for reviews of projects and issuance of certified emission reductions

19. Some Parties call for a streamlining of the review process in order to reduce or avoid delays in registering CDM projects and to ensure that the process addresses only projects with substantial problems. One suggestion is to reconsider the way in which reviews are requested. However, specific proposals for how the review process should change have not been made. It may be possible to change the timeline for reviews, or to establish criteria for when a review may be triggered and for what should be considered in a review.

20. At present, the Executive Board takes all its decisions within the prescribed procedural timelines. Some delays have occurred as a result of, inter alia, resource constraints in the support structure and DOEs combined with unexpected peaks in the workload. The Board is addressing these delays.

D. Process for appeals

21. Several Parties propose the introduction of an appeals process for the CDM, for cases where project registration has been refused or the requested quantity of CERs has not been granted.

22. Designation of an appropriate body to hear appeals would depend on a number of factors, including whether decision-making had been delegated to the support structure under the Executive Board. For example:

- (a) If the Executive Board retains responsibility for case-by-case decisions regarding projects, appeals could be heard by a third body at a level between the Executive Board and the CMP. Alternatively, an appeals chamber could be established within the Executive Board composed of members with a legal background;
- (b) The Executive Board could itself consider appeals cases if decision-making had been delegated to the support structure.

23. Several issues would need to be considered if a new body were established, such as its composition, required competencies and required support structure; the support structure may need to be kept separate from the support provided to the day-to-day functions of the Executive Board.

24. It would also be important to decide whether appeals could be made only to determine whether due process had been followed or whether they could also be made to question technical issues regarding, for example, the number of CERs that may be issued for a project. It may be essential to determine criteria for what appeals may be brought and what actions the appeals body would be able to make.

25. Considering that the current procedure for review provides several opportunities to project participants and DOEs to clarify and provide further information to support their case before a final decision by the Executive Board is taken, necessary steps will have to be instituted to protect any appeals system from being misused.

E. Selection and role of members of constituted bodies

26. Some Parties propose that members of the CDM Executive Board should be selected in order to ensure that the Board possesses the expertise appropriate to its current and evolving role, and that the other activities of members should be declared, in particular with regard to any potential conflicts of interest.

27. Several specific measures have been suggested, including:
- (a) Establishment of specific terms of reference for members to clarify their role and identify any restrictions relating to Board membership. For example, the terms of reference could address the role of the Executive Board and its members, the fact that members act in their personal capacity, measures to avoid conflicts of interest (including resignation from other responsibilities), a required time commitment to the work of the Board, and minimum experience requirements;
 - (b) Publication of nominations to the Executive Board in the sessional period prior to the candidates' election, supported by written statements regarding the relevant qualifications and backgrounds of the candidates;
 - (c) Making the election of members to the Executive Board less political, for example by separating elections to the Board from elections to other constituted bodies under the Convention and its Kyoto Protocol;
 - (d) Direct election by the CMP of the Chair and Vice-Chair of the Executive Board to full-time positions. In addition to their work chairing the Executive Board, the Chair and Vice-Chair could act as ambassadors of the CDM and manage external relationships with stakeholders and the public. Other members of the Board could be elected to part-time positions;
 - (e) Establishment of a code of conduct for Executive Board members to ensure the quality of the work undertaken and assure the carbon market of the impartiality of the members of the Board. Members could be required to make public their curricula vitae and declare all their pecuniary and professional interests that may affect their impartiality to make decisions regarding CDM projects, including any roles they may have in their own countries. Members with government functions could be required to refrain from active participation in decision-making on CDM projects in which an organization of their government is involved. Breach of the code of conduct could lead to suspension or termination of their membership of the Executive Board.

F. Management of support to constituted bodies

28. Some Parties propose that the secretariat should enhance the management and transparency of its use of resources in support of the CDM Executive Board. In particular, it is suggested that the secretariat should more closely monitor the allocation of resources to its activities in support of the Executive Board and ensure that they are effectively focused on issues which are relevant to the facilitation of CDM projects. It may also be possible to consider ways of taking advantage of the similarities and synergy between the support structures put in place for the Executive Board and the JISC, while maintaining a separation in the accounting of costs for each mechanism.

III. Possible improvements to institutional arrangements and governance of the clean development mechanism in relation to designated operational entities

A. Accreditation process

29. Some Parties propose that the CDM Executive Board should further review the accreditation process and adopt a single standard for the accreditation of DOEs. The UNFCCC CDM validation and verification manual that is currently in preparation under the Executive Board could fulfil this need for a

single accreditation standard. In moving toward a single standard, the Executive Board could consider some specific areas, including:

- (a) Clarifying the roles of each element of the accreditation process – desk review, on-site assessment and witnessing;
- (b) Elaborating the purpose of spot checks and regular surveillance of DOEs;
- (c) Establishing indicative time lines for each stage in the accreditation process, including a deadline, after the start date of the project, for initiating validation activities or submitting a new methodology;
- (d) Addressing issues relating to the availability of projects for witnessing activities.

30. Several Parties suggest that a formal training programme should be run in parallel to the new standard. This would be mandatory for all experts working for DOEs, so that only staff who have successfully participated in the training may undertake validation and verification activities.

B. Guidance provided by constituted bodies

31. Some Parties note the need for the Executive Board to give more guidance to DOEs. To some extent, these concerns may be met by the validation and verification manual. There could be a need for the Executive Board to communicate more regularly with DOEs in order to keep them informed of the latest decisions by the Board and to help ensure the appropriate understanding and interpretation of those decisions. For example, there could be a debriefing for DOEs after each meeting of the Executive Board.

32. The Board is undertaking the following actions in this area:

- (a) Meeting the representatives of the DOE Forum at each Executive Board meeting;
- (b) Sending e-mail alerts after each Board meeting;
- (c) Involving DOEs in the development of procedures and guidance such as the validation and verification manual;
- (d) Providing substantive support to regional “calibration” meetings, which provide the opportunity for DOEs in the region to have staff interact on latest guidance and overall understanding.

C. Quality and consistency of assessments

33. Some Parties propose that the Executive Board should enforce higher standards in the results being produced by DOEs. A system could be established for non-compliance, which could lead to suspension or withdrawal of DOE accreditation, based on the number of reviews initiated, repeat errors, non-compliance with standards or proven misconduct. The Executive Board initiated work in 2007 on a policy framework to address non-compliance by DOEs in a systematic manner.

34. Some Parties also suggest that the Executive Board should publish statistics on DOE performance. This could be based on the established system and would help to guide project proponents in their choice of DOE.

35. A number of sanctions could be placed on DOEs in the event of poor performance. These could be of a financial nature or could involve restrictions on further work, such as suspension for a period of time or subjecting their submitted documentation to detailed reviews.

36. Some Parties also maintain that DOEs should report the outcomes of all their validation and verification assessments to the Executive Board, irrespective of whether results are positive or negative.

This would avoid situations in which another DOE is sought after a project was rejected by a first. The Executive Board could, in addition to publishing the status of each project for which a request for registration has been made (e.g. in process, withdrawn, rejected or completed) on the CDM website, also indicate the outcome of the validation process in case it does not result in a request for registration.

D. Selection and payment

37. Some Parties propose that options should be considered for having the Executive Board or the secretariat select and pay for the services that DOEs provide to projects. This could enhance the impartiality of DOEs and their independence from the project participants. For example, DOEs could be selected using a simple bidding procedure that takes into account both the cost and the previous performance of the DOEs. Project participants would still bear the direct cost for each project.

IV. Possible improvements to the rules and procedures of the clean development mechanism

A. Additionality and methodologies

38. Some Parties proposed that the assessment of additionality of CDM projects should generally be made more objective and, where possible, standardized. Specific options presented include:

- (a) Greater standardization in the use of financial benchmarks;
- (b) Use of more objective and quantitative criteria in the analysis of project barriers;
- (c) Greater use of emission benchmarks for demonstrating additionality.

39. In order to further enhance the objectivity and environmental integrity of the CDM, some Parties wish to consider further the use of sector- and subsector-specific benchmarks at a national level in determining the baseline emissions of CDM projects. These could also help to enhance the efficiency of the CDM process. These Parties therefore consider that the Executive Board should systematically assess approved methodologies for which benchmarks are appropriate and explore the use of benchmarks in these methodologies.

40. The Board is exploring the subject of benchmark and reference values. Most recently, it adopted a methodology that provides for the establishment of benchmarks to determine additionality and the baseline.

B. Programmes of activities

41. Some Parties propose that the approach to programmes of activities (PoAs) under the CDM be enhanced. Although the process of gathering and processing experience in the current approach to PoAs is still in its infancy,⁷ it is noted that there is likely to be further scope for enhancing the current rules for PoAs, including through allowing national policies as CDM projects.

V. Possible improvements in joint implementation

42. In principle, it would be possible to implement many of the possible improvements discussed in chapters II–IV above in the context of JI. However, given that there is less experience with JI than with the CDM, it is not yet clear in a number of cases that changes similar to those considered for the CDM

⁷ No PoA has yet been registered, although DOEs are currently validating five PoAs. The Executive Board has issued a public call for input to collect information on experiences and challenges with PoAs, and will consider options to address these at its 43rd meeting.

would be warranted in the context of JI. If changes were also to be applied in the context of JI, it would be important that these be tailored towards the specific modalities and circumstances of JI.

43. For example, it could be possible to enhance the supervisory role of the JISC in a manner similar to that described for the CDM Executive Board (see chapter II A above) and to delegate technical decision-making to the secretariat or to panels established under the JISC. Any such changes would apply only to the JI Track 2 procedure.⁸ However, the nature and procedures of JI Track 2 would imply differences in the scope of such delegation. For example, decisions to be delegated to the support structure of the JISC could include:

- (a) Accreditation of independent entities;
- (b) Appraisal and review of determinations.

44. It should be noted, however, that there are still fewer projects in the JI Track 2 pipeline than in the CDM pipeline and that there have not been the same calls to enhance the efficiency of the JI Track 2 process. The pressure to define and move to a new mode of work is therefore not as strong in the case of JI. The JISC has not initiated steps in this direction, as the CDM Executive Board has done already in the case of the CDM.

45. In relation to consistency and transparency of decision-making (see chapter II B above), it is important to note that fewer JI projects have received a final determination under JI Track 2 than have been registered under the CDM. As a result, issues of consistency have not yet arisen in the context of JI. Owing to the specific characteristics of JI Track 2, it may be more difficult to address the consistency of decision-making by applying the proposals in chapter II B above to the JISC than to the CDM Executive Board. In principle, however, it would be possible to apply some measures proposed for the CDM to JI Track 2.

⁸ The verification procedure under the JISC as defined in paragraphs 30–45 of the annex to decision 9/CMP.1.