

**CDM-MP71-A12**

## Concept note

---

Further elaboration on the proposed approach in expanding the application of existing combined tool

Version 01.0



**United Nations**  
Framework Convention on  
Climate Change

<b>TABLE OF CONTENTS</b>	<b>Page</b>
<b>1. PROCEDURAL BACKGROUND.....</b>	<b>3</b>
<b>2. PURPOSE .....</b>	<b>3</b>
<b>3. KEY ISSUES AND PROPOSED SOLUTIONS .....</b>	<b>3</b>
3.1. The proposal from the Meth Panel.....	3
3.2. Value addition of conducting the underlying work .....	4
3.2.1. Further clarify the applicability of approaches used for investment analysis.....	5
3.2.2. Strengthened additionality demonstration procedures .....	5
3.2.3. Improved consistency among different methodologies .....	6
3.3. Description of the newly introduced logical steps and their applications .....	7
3.4. Ways in which the most attractive alternative can be identified if only a benchmark analysis is applied .....	10
3.5. The relevance of the question in the flow diagram on whether the service or product can only be provided by the project developer .....	10
<b>4. IMPACTS.....</b>	<b>11</b>
<b>5. SUBSEQUENT WORK AND TIMELINES.....</b>	<b>11</b>
<b>6. RECOMMENDATIONS TO THE BOARD .....</b>	<b>11</b>

## **1. Procedural background**

1. At the ninetieth meeting, the Executive Board of the Clean Development Mechanism (hereinafter referred to as the Board) considered the concept note on the gap analysis to the application of the existing combined tool and agreed with the direction of the approach outlined in the concept note (Annex 18 of MP70). The Board also requested the Methodologies Panel (Meth Panel) and the secretariat to further work jointly on this issue based on the feedback provided, including:
  - (a) Value-added analysis of the work aimed at broadening the applicability of the combined tool;
  - (b) A clear description of the newly introduced logical steps and their applications presented in a flow diagram;
  - (c) Ways in which the most attractive alternative can be identified if only a benchmark analysis is applied; and
  - (d) The relevance of the question in the flow diagram on whether the service or product can only be provided by the project developer.

## **2. Purpose**

2. The objective of the concept note is to respond to the above mandate by providing further elaboration on the proposal from the Meth Panel and the secretariat in expanding the application of existing combined tool, in order to facilitate its consideration by the Board.

## **3. Key issues and proposed solutions**

### **3.1. The proposal from the Meth Panel**

3. The flowchart below illustrates the underlying proposal from the Meth Panel to expand the applicability of the existing combined tool as contained in the concept note considered at EB90 (Annex 18 of MP70), taking into account the Board's comment at EB90.



lessons learned, what could be further done etc. The Board requested the MP and where applicable, the SSC WG to broaden the application of the combined tool to cover as wide a scope as possible. In this way, the following benefits are expected to be realized:

### 3.2.1. Further clarify the applicability of approaches used for investment analysis

5. Three possible approaches have been provided for conducting investment analysis in both the additionality tool and the combined tool, i.e., simple cost analysis, investment comparison analysis and the benchmark analysis. While the applicability of the simple cost analysis is relatively clear, previous experience showed that the other two approaches had not been consistently applied, e.g., some projects mixed the situations for which the investment comparison analysis and the benchmark analysis are applicable. Therefore, there is still some room to further clarify the applicability of the investment comparison analysis versus the benchmark analysis. The proposed approach aims to improve this aspect by setting clear and objective criteria for the application of the investment comparison analysis and the benchmark analysis.

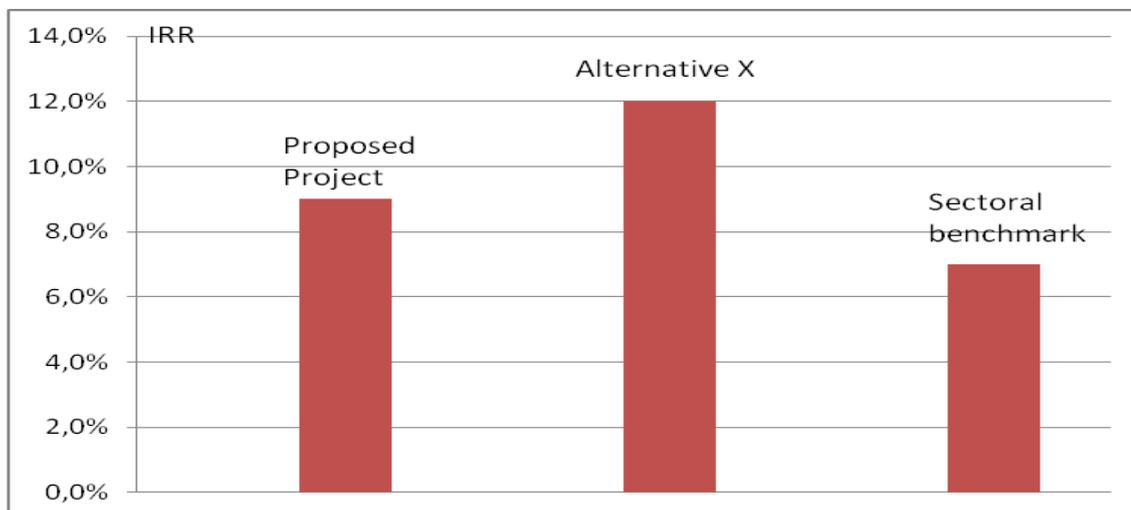
### 3.2.2. Strengthened additionality demonstration procedures

6. As seen in Table 1 below, additionality tool has been referred in 45 methodologies. A well-known weakness associated with the additionality tool is that it allows comparing the proposed project activity without CDM with any other available alternatives, leading to the questionable conclusion of additionality demonstration. The issue can be illustrated in the Figure 2 below. In this example, it may be possible to conclude that the proposed CDM project is additional by comparing the IRR of the proposed CDM project against the alternative X, whereas its IRR actually has also passed the sectoral financial benchmark indicating that it would likely be implemented anyway in the absence of the CDM.

**Table 1 Application of combined tool and additionality tool in Large Scale methodologies**

Tool referred	Combined Tool	Additionality Tool	Both	None
No. of methodologies	51	45	7	9

**Figure 2. Illustrative project activities for investment analysis**



7. In the new proposal from the Meth Panel, the above weakness is addressed by setting the clear criteria for circumstances in which applying the investment comparison analysis versus the benchmark analysis will be the most appropriate for demonstration of the additionality, by identifying which types of alternatives are relevant to the project: either other alternative investments by the project proponents or alternative investments by other actors in the market.

### 3.2.3. Improved consistency among different methodologies

8. As presented in the concept note at EB90, 112 large-scale methodologies have been approved by the Board to date (Table 1 below). Combined tool and additionality tool have currently been applied in an inconsistent manner. One important reason is that the current combined tool is supposed to be not applicable in some project scenarios, and thus additionality tool was referred with an aim to overcome the limitations of the combined tool. However, the Meth Panel is of the view that the underlying issues are still not fully addressed by merely referring to the additionality tool. The proposal in discussion from the Meth Panel will broaden the applicability of the existing combined tool to cover the limitations identified earlier, which will improve significantly the consistency across methodologies in the area of baseline identification and additionality demonstration.
9. In addition, the consistency of additionality, baseline and baseline scenario is also improved in the proposed approach. In principle, the baseline emissions calculation should correspond to the emission level of the identified baseline scenario. However, as found in the concept note considered in EB90, these two concept were decoupled in a number of methodologies (see para 15 of Annex 18 of MP70)<sup>1</sup>. In addition, according to paragraphs 43 and 44 of the CDM modalities and procedures, 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

<sup>1</sup> It was noticed in a number of large scale methodologies (e.g., AM0042 and AM0057) that the baseline emissions calculation does not exactly reflect the emission level of the identified baseline scenario (See details in the Annex 18 of MP70).

activity. In other words, a proposed CDM project activity is additional if emissions are reduced below those of its baseline. Therefore, at least conceptually, the question of whether a project activity is additional should be assessed against a given approach for determining its baseline scenario, and the requirements for the assessment of additionality should be consistent with the identification of the baseline scenario (also see section 3.3 of annex 06 to annotated agenda of EB85). The consistency of the underlying concepts is improved in the proposed approach from Meth Panel while expanding the applicability of the existing combined tool.

### 3.3. Description of the newly introduced logical steps and their applications

10. Further elaboration on the newly added logic steps can be found in the table below.

**Table 2 Elaboration on the newly added logic steps**

Logic step	Elaboration
<div style="border: 1px solid black; padding: 5px; width: fit-content; margin: 10px auto;">Step 2. Barrier analysis*</div>	<p>It is an existing step included in the current combined tool.</p> <p>Asterisk (*) to Step 2 in the above diagram indicates that Step 2 is not a mandatory step and that the PP may go to Step 3 investment analysis directly.</p>
<div style="border: 1px solid black; padding: 5px; width: fit-content; margin: 10px auto;">Is project without CDM the only alternative remaining?</div> <p style="text-align: center;">and</p> <div style="border: 1px solid black; padding: 5px; width: fit-content; margin: 10px auto;">Are there multiple alternatives remaining?</div>	<p>These two logic steps are not new concepts. In the current combined tool, “is only one alternative remaining” is questioned after the barrier analysis. Depending on the answer to this logic question, two different courses of subsequent actions are specified for further executing the barrier analysis (i.e., one is for scenario when the only remaining alternative is the project without CDM, while the other is for scenario when multiple alternatives remain, including or not the project without CDM).</p> <p>The possibility of streamlining the two scenarios was assessed by the Meth Panel. As a result, it was achieved by adding these two yellow-highlighted logic steps in the proposed approach, thereafter followed by a common course of actions for both these scenarios (i.e., moving to the logic step “can the service or product only be provided by the PP”).</p> <p>Conceptually, the expected outcome from these two newly added steps are the same as the steps in the current combined tool (page 12 of existing combined tool, clarifying box “Outcome of Step 2”):</p> <ul style="list-style-type: none"> <li>• When the only remaining alternative not prevented by any barrier is the proposed project without being registered as a CDM project, then it is not additional.</li> <li>• When the only remaining alternative not prevented by any barrier is <u>not</u> the proposed project activity without being registered as a CDM project, then proceed to step “can the</li> </ul>

	<p>service or product only be provided by the PP”.</p> <ul style="list-style-type: none"> <li>• If there is more than one alternative scenario that is not prevented by any barrier, then the following applies:             <ul style="list-style-type: none"> <li>a. If the alternative scenarios include the proposed project activity undertaken without being registered as a CDM project activity, proceed to the step “investment analysis”;</li> <li>b. If the alternative scenarios do not include the proposed project activity undertaken without being registered as a CDM project activity, PP defined the baseline scenario following further instructions.</li> </ul> </li> </ul>
<div style="border: 1px solid black; border-radius: 10px; padding: 5px; width: fit-content; margin: 10px auto;"> <p>Can the service or product only be provided by the PP?</p> </div>	<p>This step serves to decide on whether benchmark approach has to be applied. It is a critical step in the proposal.</p> <ol style="list-style-type: none"> <li>1) The underlying principle is that if the PP is not the only one who can provide the service/product, or someone else can also provide the same service/product (e.g., most electricity generation cases and probably most cases implying new capacity of production of a product/service supplied on the market), a benchmark approach has to be applied, e.g. a comparable product as that produced by the proposed CDM project can also be provided by different suppliers from the market. This is because it is difficult with high certainty to identify which is the exact 3<sup>rd</sup> party which the project service/product will displace, thus making the baseline identification challenging.</li> <li>2) Likewise, in order to move away from the benchmark analysis to the investment comparison analysis, the PP needs to provide proper justification to prove that the PP is the exclusive service/product provider, i.e., the alternatives supplying the same product/service are in the full control of the PP (e.g. most retrofit cases). In such a case, the alternative with the highest attractiveness as a result of the investment comparison analysis is deemed as the baseline.</li> <li>3) With the above approach, it is critical to identify the full list of alternatives which will be checked against the question “whether the product/service can only be provided by PP”. In this regard, if the above concept is agreed by the Board, the Meth Panel would also like to provide additional guidance to strengthen Step 1 for identification of alternative baseline scenarios. Among others, the following are being considered by the Meth Panel.             <ul style="list-style-type: none"> <li>• While providing the overview of the types of technologies or practices, among others, list the technologies deployed in the recent past (e.g., 3 years) in the applicable geographical area, and include technologies employed in other registered</li> </ul> </li> </ol>

	<p>CDM project activities;</p> <ul style="list-style-type: none"> <li>Services provided by a 3rd party (e.g., through a market or a power grid) shall always be included for further analysis, particularly for projects involving capacity addition (including Greenfield). Justification on why such an alternative is not relevant to the PP needs to be provided in order for it to be removed from the list.</li> </ul> <p>4) Furthermore, for the purpose of simplification, the Meth Panel is also of the view that the benchmark analysis (i.e., product/service is only to be provided by PP) shall also be applied in the case of the following two situations:</p> <ul style="list-style-type: none"> <li>In the situation when the project is developed as part of a portfolio of technologies delivering power to the grid;</li> <li>The PP is the only player to supply power to the grid in the country (i.e., monopoly)</li> </ul> <p>Detailed text to address the above cases will be proposed when it comes to the revision of the Combined Tool.</p>
<p>Benchmark analysis in IA</p> <p>and</p> <p>Investment comparison or simple cost analysis</p> <p>and</p> <p>Is the IA conclusive?</p>	<p>Different methods to conduct investment analysis, following the requirement/guidance in the existing combined tool (page 13). As discussed earlier, three possible approaches have been provided for conducting investment analysis in both the additionality tool and the combined tool, i.e., simple cost analysis, investment comparison analysis and the benchmark analysis. These steps explicitly specify the approach which shall be applied.</p>
<p>The baseline emission is the emission benchmark, or the emission of the most attractive alternative if required in the respective meth</p>	<p>This is a modified step compared with the version considered in EB90. It is related to one of the Board's input; please see the rationale in paragraph 11 below.</p> <p>This step is only applicable when a 3<sup>rd</sup> party can also provide the same service/product, due to which a definite baseline cannot be identified with certainty. In this case, the emission benchmark or the emission level of the most attractive scenario needs to be determined.</p> <p>Where applicable, procedure for the determination of emission benchmark has been provided in most (if not all) methodologies/tools for e.g., Greenfield projects.</p>

<p>Is emission level of the baseline scenario higher than that of the proposed project activity?</p>	<p>This is to ensure the level of GHG emissions from the project activity is less than the identified baseline. Otherwise, the proposed project will not be additional. Such a concept is also intended to align with the definition of additionality and baseline in paragraphs 43 and 44 of the CDM modalities and procedures, from which it may be deduced that a proposed CDM project activity is additional if emissions are reduced below those of its baseline (also refer to paragraph 9 above).</p>
--	--

### **3.4. Ways in which the most attractive alternative can be identified if only a benchmark analysis is applied**

11. The Meth Panel considered the issue raised by the Board, and agreed that the approach proposed by the MP70 may indeed require the PP to conduct both the benchmark analysis and the investment comparison analysis, which could be challenging in terms of data collection. The Meth Panel also acknowledge that emission benchmark will be sufficient for baseline emission determination in most cases and the situation for which the need to take the minimum between the emission benchmark and the emission of the most financially attractive alternative is rare. In such a context, the Meth Panel agreed to modify the earlier approach by only keeping the emission benchmark in the flowchart, with a view to provide additional guidance in the respective methodology in cases where the need to compare the emission benchmark and the emission of the most financially attractive alternative may be necessary.

### **3.5. The relevance of the question in the flow diagram on whether the service or product can only be provided by the project developer**

12. After reviewing the feedback from the Board on this issue, the Meth Panel would like to highlight that the following situations have been stipulated to apply the benchmark analysis and the following route in the proposed diagram:
  - (a) When the product/service can also be provided by some other parties e.g., from the market;
  - (b) When the proposed project activity is part of a portfolio;
  - (c) When the PP is the only player to supply power to the grid in the country (i.e., monopoly).
13. The Meth Panel also would like to bring Board's attention to the fact that in order to apply the investment comparison route as indicated by the proposed flowchart, the PP has to meet the following pre-conditions:
  - PP needs to justify it is the only product/service provider.

As mentioned earlier, the Meth Panel is proposing to strengthen this step, by requiring that services provided by a 3rd party (e.g., through a market or a power grid) shall always be included for further analysis, particularly for projects involving capacity addition (including Greenfield).

14. In such a context, the Meth Panel was of the view that it will not be easy for the proposed project in the example provided during the Board's discussion to be qualified

to go through the route of investment comparison analysis. In addition, the Meth Panel also agreed that while comparing different alternatives, the alternatives shall be those that are plausible to the PP for the same site as the proposed CDM project. Comparing the proposed project activity with an alternative of some specificities (e.g., cheaper coal power plant due to close to the coal pit in a country with an underdeveloped transmission network) in a different location does not seem to be appropriate. In conclusion, the Meth Panel agreed to maintain the recommendation as that in EB90 in this aspect for the Board's consideration.

## 4. Impacts

15. The proposal provided in this concept note will expand applicability of the combined tool, leading to the improved environmental integrity, as well as the consistency of methodological approaches for baseline identification and additionality demonstration.

## 5. Subsequent work and timelines

16. Based on the guidance from the Board, the Meth Panel will work on preparing the revised version of the combined tool in expanding its applicability condition at the next respective meetings and will recommend the draft revised tool for the consideration of the Board in 2017.

## 6. Recommendations to the Board

17. The Meth Panel recommend that the Board consider and approve the proposal contained in this document to expand the applicability of the combined tool; and to provide mandate to the Meth Panel to prepare the revised version of the tool taking into account any guidance from the Board.

-----

### Document information

<i>Version</i>	<i>Date</i>	<i>Description</i>
01.0	14 October 2016	MP 71, Annex 12 To be considered by the Board at EB92.

Decision Class: Regulatory

Document Type: Information note

Business Function: Methodological tool

Keywords: TOOL02, streamline, management of official documentation

---