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DET NORSKE VERITAS
DNV CERTIFICATION AS

Att: CDM Executive Board

Your ref.:
CDM Ref 1043

Our ref.:
MRSA/ETEL

Date:
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Response to request for review "Chumbagua Cogeneration Project" (1043)

Dear Members of the CDM Executive Board,

We refer to the requests for review raised by three Board members concerning DNV's request for registration of the "Chumbagua Cogeneration Project" (1043), and we would like to provide the following response to the issues raised by the requests for review.

Comment 1:

"Justification should be provided as to why a project IRR has been calculated for the benchmark analysis when the additionality tool requires where there is only one potential project developer (e.g. when the project activity upgrades an existing process), the IRR shall be calculated as an equity IRR."

DNV Response:

Given that the calculation of the IRR was based on cash flows after debt service (interest), the calculated IRR does correspond to an equity IRR (return to equity holders only). Furthermore, DNV acknowledges that private investment decisions for projects in developing countries (with high risk profile and not mature financial markets) like Honduras normally will require a minimum return on equity (ROE) that by far exceeds both local passive interest rates (the rate paid by financial intermediaries to those offering resources for the money raised) and local active rates (interest rate which financial intermediaries receive from borrowers for loans granted). In our opinion, the benchmark adopted by project participants thus conservatively represents the minimum required rate of return of the project to the shareholders of Energy Chumbagua S.A. de C.V. vis-à-vis the financial and business risks associated to the project.

Comment 2:

"Justification should be provided regarding why an annual maximum active interest rate has been used as a benchmark."

DNV Response:

According to argumentation of the project developer during the project validation stage, the previously adopted series of the highest observed active rates better represented the minimum required rate of return of the project for Energy Chumbagua S.A. de C.V. by the time the investment decision was made considering the high financial and business risks associated to the project. However, as a response to the above comment, the project participants decided to recalculate the IRR adopting the weighted average active loan rates as a benchmark as a conservative measure. Thus, the PDD and validation report will be amended accordingly. As the re-calculated project IRR is still lower than the adopted benchmark rate and also considering that the additionality argumentation was based on a barrier analysis, it is still deemed demonstrated that the project is not a likely baseline scenario.

Comment 3:

“The thermal firing capacity before and after the project activity should be clearly stated and it should be transparently justified how the requirement of scenario 14 of ACM0006 v4 that the project should “increase the power generation capacity, while the thermal firing capacity is maintained” has been met”

DNV Response:

DNV has verified that, as sugar-cane bagasse is a by-product of sugar production, all incremental biomass residue consumption and associated thermal energy generation during the project activity (in comparison with the baseline scenario) will be due to the company’s natural expansion of sugar production business as a response to the projected demand increase in sugar market. Thus, such increments can not be attributed to the implementation of the project activity as they would have also occurred in the absence of the project (baseline plant configuration).

It should be noted that the recently implemented baseline scenarios 18 and 19 of ACM0006 (scenarios implemented in version 5 of ACM0006 were not available by the time project was submitted for validation) indeed make a provision to increase the thermal firing capacity in projects resulting in improvement of energy efficiency by considering that “ (...) *in the absence of the project activity, the existing plant would also be retrofitted, but resulting in a lower efficiency of electricity generation than in the project case (e.g. by using a low-pressure boiler instead of a high-pressure boiler). The retrofitted plant in the baseline is referred to as “reference plant”.*” However, given that while scenarios 14, 18 and 19 adopt the same formula for estimation of the annual additional quantity of electricity generated as a result of the project implementation, the estimated GHG emission reductions would not change if scenario 18 or 19 were adopted as an alternative.

Finally, it should also be noted that, while registered as a CDM project activity, the project will generate certified emission reductions which will be verified based on the amount of excess electricity that the plant exports to the grid (monitoring parameter), not the estimated additional electricity.

Comment 4:

“Justification is required as to why the project participant used the environmental impact assessment and environmental license consultation process in the PDD instead of conducting a CDM project activity specific local stakeholder consultation process.”


DNV Response:

DNV was able to verify that apart of public consultation measures which were part of *the environmental impact assessment and environmental license processes, project participants also submitted letters to local stakeholders* at the Municipality of San Marcos inviting for comments regarding the implementation of the project as a CDM project activity. Letters were sent to the city hall and other local stakeholders within the local community. Copies of the letters as well as confirmation of receipt have been assessed by DNV. Two positive comments were received.

We sincerely hope that the Board accepts our above explanations.

Yours faithfully.

for DET NORSKE VERITAS CERTIFICATION AS



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