1289 Fuel switchover from higher carbon intensive fuels to Natural Gas (NG) at Indian Farmers Fertiliser Cooperative Ltd (IFFCO) in Phulpur Village, Allahabad, Uttar Pradesh by M/s Indian Farmers Fertiliser Cooperative Ltd (IFFCO)

Comment 1:

Further clarification is required as to how the DOE validated the investment analysis, particularly with respect to:

a) The treatment of depreciation, a non-cash item, in the NPV analysis;
b) The relevance of the CER price as a parameter for the sensitivity analysis; and
c) The exclusion of the cost differential between natural gas and naphtha, as the subsidy appears to be based on an assumed rather than actual production cost and therefore it is unclear whether the participant will indeed not benefit from actual fuel price differences.

Response by Project Participant:

a) The final NPV analysis was arrived at after a number of successive revisions. In the initial versions depreciation was not taken into account and Income tax concession on account of depreciation was not considered in the cash inflow. However, it seems that in the later versions, depreciation has been considered. We accept EB's review point and revised NPV analysis not considering the depreciation and please find attached revised NPV calculation sheet and associated changes have been carried out in the revised PDD.(Please refer step-1 of section B.5 of revised PDD).

b) As per the approved baseline and monitoring methodology ACM0009, the additionality of project has to be established by step 1 - Investment & sensitivity analysis. The project activity is financially unattractive (NPV is negative) and CDM revenue makes the project quite viable. Hence CDM revenue plays a vital role in the sustainability of the project.

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The price of Certified Emission Reduction (CER) is determined by market dynamics, and it has been observed in the recent past that CER price has varied significantly. However, the revenue from sale of CERs is a significant source of cash inflow and the most important factor that makes the project financially viable. Hence the project participant wished to analyze the impact of variation in carbon revenue due to variation in CER price on the financial viability of the project. Thus the CER price has been included as a parameter in the sensitivity analysis to ascertain the financial viability of the project activity.

However, as per the step-2 of additionality tool version 03, it needs to be demonstrated that the proposed project activity is economically or financially unattractive without the revenue from the sale of certified emission reductions (CERs). Thus sensitivity of the NPV to the CER price is although not required but it has been conducted to determine the CER price which tends to make the project activity economically viable.

We agree with review point raised by EB members and accordingly we have removed the sensitivity analysis of NPV considering variation in CER price. Please refer step-1 of section B.5 of revised PDD.

c) The project proponent reaffirms that the subsidy is based on actual production cost and not based on estimated value. The Govt. of India (GoI) has fixed production cost of Urea – which includes raw materials cost like Feed, Fuel and other cost like Marketing Cost, Fixed Cost, Return on Networth etc. for Urea plants based on the Group Concession Scheme (GCS). Under GCS the production cost of Urea is term as concession rate. The details of GCS is already explained in the PDD (please refer section B-5) and validation report (please refer CAR-2).

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In order to provide Urea to the farmers at affordable price, GoI has fixed the sales price of Urea and all companies have to sell Urea at this notified price. The difference between the actual production cost of Urea (concession rate) and notified sales price of Urea is borne by the GoI as subsidy.

The concession rate of Urea for the year 2003-04 was fixed by GoI, based on vintage and type of Feed/Fuel used, vide circular No.FICC/CE/22/2003/164 dated 28th May, 2003. In this circular it is clearly indicated that the rate for concession for Naphtha based Unit varies from Rs. 10,339 to Rs. 13,564 per tonne of Urea whereas the rate of concession for Natural Gas based unit varies from Rs. 4,754/- to Rs. 6,456 per tonne of Urea. This clearly indicates that the concession rate for Natural Gas based Urea plant are lower than the Naphtha based Urea plant (mainly due to the difference in the price of Naphtha and Natural Gas). This document is attached at **Annexure-1I.** Accordingly, the concession rate for **Phulpur-I** is Rs.11,194/- per tonne of Urea.

Since, the cost of raw materials like Feed, Fuel varies on yearly basis the concession rate of Urea is escalated/deescalated (revised) on yearly basis based on the actual cost of inputs like Feed, Fuel etc. On quarterly as well as Yearly basis, IFFCO submits the actual cost of inputs like Feed, Fuel etc. This submission is called as claim for escalation in concession rate. Please find attached a document to substantiate the annual escalation claim submitted by IFFCO to GoI vide letter No. HO/C&P/NF-121 dated 18th August, 2006 as **Annexure-2.** The actual cost of inputs is certified by third party financial auditor. GoI reviews the submitted statement of actual cost of inputs and accordingly increase/ decrease the concession rate of Urea.

Based on the escalation claim submitted by IFFCO for 2004-05, 2005-06 and first two quarters of 2006-07, GoI vide letter No. 12012/19/2006 (i)-FPP dated 12th November, 2007 have revised the concession rates (for

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Phulpur-I). This document is attached at **Annexure-3.** The document clearly depicts that the concession rate of **Phulpur-I** before the switchover from Naphtha to Natural Gas was Rs. 16,490/- per tonne of Urea (for the period April, 2005 to March, 2006) and after switchover to Natural Gas the concession rate get revised to Rs.9,969/- per tonne of Urea. Hence, the concession rate get reduced from Rs.16,490/- per tonne of Urea to Rs. 9,969/- per tonne Urea mainly due to Feed/ Fuel Switchover. Due to reduction in the concession rate the subsidy outgo of the GoI (concession rate less sale price of Urea) also get reduced and IFFCO is not getting benefited due to the differential price of Naphtha and Natural Gas.

Comment 2:

Further clarification is required as to how the prior consideration of the CDM was validated by the DOE as required by the guidelines for completing Sec. B.5 of the CDM-PDD.

Response by Project Participant:

IFFCO management took the decision of carrying out the project activity, considering the incentive or revenues from the CDM at various stages of the project planning and implementation. The project proponent was well aware of the possible benefits of CDM and risk involved with the implementation of the project activity.

The decision to implement the project activity was wholly based on the additional revenues from the CDM which is well substantiated by the following documents: The start date of the project activity is considered as 01/03/2006 (the date of completion of civil work related to the project activity) and attached as **Annexure-4.**

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Document No. 1 – Internal approval note (dated 20th December, 2004) by the senior management (Senior Executive Director and Managing Director of the company) apprising about CDM and associated benefits by implementing the project activity

IFFCO management was well aware that the project activity was economically not attractive and CDM revenues would make the project viable.

An internal approval note addressed to the Managing Director from the chief manager seeking his approval for the proposed project activity is attached as **Annexure-5**, which clearly demonstrates the importance of CDM in taking the decision to proceed with the project activity.

Document No. 2 – Copy of contract with CDM consultant (dated 19th April 2005) and related approval documents

IFFCO management was well aware that the project activity was economically not attractive and CDM revenues would make the project viable. Bearing this in mind, IFFCO initiated CDM process well before the implementation of the project activity. IFFCO started correspondence with CDM consultant and appointed M/s Ernst & Young as CDM consultant during the planning stage of the project. Please find attached following documents which clearly substantiates that CDM was considered before implementation of the project.

1. The internal approval documents of IFFCO for appointing M/s Ernst & Young as CDM consultant as **Annexure-6**
2. The Copy of Contract with CDM consultant is attached as **Annexure-7.**

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Document No. 3 – Copy of contract with DOE and related approval documents

IFFCO management seriously considered CDM before implementation of the project activity

Hence IFFCO proceeded with initiating actions for appointing validating agency (Designated operational entity) to establish the integrity of the CDM documentation before implementation of the project activity.

The following documents are attached for further reference, which clearly indicate that the process of CDM was started much before the actual start date of the project activity and that CDM was seriously considered before implementation of the project activity.

1. The internal approval document of IFFCO for appointing M/s DNV as DOE as **Annexure-8.**
2. The Copy of Contract with DOE dated 19 December 2005 (Ref. No. ES/6/8184/972).

The above documents clearly substantiate that the CDM was seriously considered by senior management of IFFCO in the decision to undertake the project activity.

The above information has also been included in the revised PDD under section B.5.

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