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Ref: Response to clarifications on issues associated with validation requirements for project activity under review "Jincheng Fengrun CMM Utilisation from Nine Mines in Jincheng City Shanxi Province China" (1928)

18 November 2008

UNFCCC Secretariat
Martin-Luther-King-Strasse 8
D-53153 Bonn
Germany

Attention: CDM Executive Board

Dear Sir or Madam,

We were informed that our project "Jincheng Fengrun CMM Utilisation from Nine Mines in Jincheng City Shanxi Province China" (1928) was requested for review by CDM Executive Board. As required by the Executive Board and on behalf of the project participants, we would like to answer the questions and clarify the issues raised in the requests for clarification as follows:

Question 1:

The DOE shall clarify how it has validated that CMM will be purchased at a fixed price of 0.15 RMB/m3 CH4. In doing so, the PP/DOE shall provide the documentary evidence based on the CMM purchase and supply agreements, actual invoices and payments made (if any). The DOE is requested to confirm whether the CMM price includes the costs of CMM extraction and supply.

PP's response:

In addition to the DOE's response, we would like to clarify the two issues pointed out, i.e. CMM is purchased at a fixed price; and the determination of CMM price.

- CMM is purchased at a fixed price

In order to encourage the CMM utilization and reduction in greenhouse gas emissions, the Jincheng City Government Price Administration Bureau published the Notice on CMM Price dated 24 November 2003. In both the PDD (page 16) and the DOE's validation report (page 15) it is stated that the price of 0.15 RMB/m^3 CH_4 was validated by checking it against this official document.

Further documents were provided to confirm that the same gas price was adopted by the project entity. These documents included CMM purchase and supply agreements.

Determination of CMM price

i. The price is regulated and determined by the government

Item 2 of the Notice Regarding CMM Pricing, Jincheng City Pricing Bureau (Document no. 301 of 2003), states that 'CMM price for the gas storage tank to the mine (gas source). The CMM price is determined based on the cost and benefit of CMM utilization and ultimate market consumer price. The unit price of CMM gas with 40% methane concentration is 0.15RMB/m^3. For every 5% increase of concentration, the price is to be added with 0.01RMB/m^3.' However, it was recognized by the project participants that it is not entirely transparent how the CMM price was determined by the Jincheng government.

Therefore it is not clear which aspects of the CMM extraction and supply are included in the fixed CMM price. The PDD discusses how prices are set in China and how this process is relevant to the consideration of the cost of CMM extraction and supply. According to the Price Law of the People's Republic of China Article 21 the government price shall be fixed according to the average cost and market supply, etc.

ii. The costs of CMM extraction and supply

We would hereby like to further clarify that the CMM extraction is usually included as a part of the investment borne by the coalmine owner as mandatory safety requirement. Such extraction system would be sufficient for venting of CMM. Once the mandatory safety extraction systems have been put in place, it has become a sunk cost and the running cost of venting the CMM from the coal mine into the atmosphere is relatively inexpensive. As this cost is not part of the project activity and continues to be governed by official safety requirements it should therefore not be considered in the context of the project activity. In addition as the safety system is mandatory it does not seem logical to include it in the setting of the gas price as the gas price should reflect the cost of providing the gas to the market and is unrelated to safety aspects. However we cannot say this definitively as the price setting is not entirely transparent.

In order to provide stable gas supply, additional extraction and supply costs are necessary to improve the efficiency of capturing the CMM through retrofitting the existing venting system, pre-treatment of captured CMM for utilization by power plant and construction of the pipeline from the coal mine to the point of delivery. Taking into account that the government issued price guidelines are not entirely transparent, the project participants checked that none of the additional costs associated with the extraction and supply were considered in the financial analysis. The DOE has verified this by checking the total investment breakdown the project's Feasibility Study Reports (FSRs) and the financial analysis of the PDD. The total investment includes mainly the construction costs for power plant facilities (the utilities building, office, walls, etc) and equipment (mainly the generator sets). Other costs included are design and site investigation costs etc. No costs for extraction and pipeline network are included.

This approach ensured that the financial analysis is conservative and avoids possible double-counting of the associated costs included in the fixed CMM price. This approach is further made conservative by the fact that the government takes broader considerations into account when setting prices and it is not possible to justify the price of CMM simply based on its extraction and supply costs alone (see validation report page 55).

Question 2:

The DOE is requested to provide reliable evidence that CDM was considered prior to the project start date and that continuing and real actions were taken to secure CDM status for the project activity in parallel with its implementation following the guidelines from paragraph 5, Annex 46, EB 41.

PP's response:

Besides DOE response we would like to add that in section B.5 of the PDD it is clearly described that CDM consideration prior to the project start date and supporting evidences available during the validation stage. In the validation report DOE has confirmed that the evidences be verified.

Dates	Key documents	Approval	Remarks
10/01/2005	Correspondence with the CNUDC regarding CDM	n/a	The project developer consulted the Jincheng Municipal CMM and Natural Gas Utilisation Development Committee (CNUDC) regarding its CDM development plan in January 2005. (Please refer to PDD page 14-15)
01/2005	FSR of 9 CMM projects	07/06/2005	The FSRs were conducted for the total installation of 24 MW in 9 project sites with CDM consideration. (Please refer to PDD page 14-15) The approval was granted by Jincheng Development Planning Committee.
20/04/2005	EIA of 9 CMM projects	28/12/2006	The Jincheng Environmental Protection Research Institute completed the EIA forms for the projects in April 2005. The Jincheng Environmental Protection Bureau issued the approvals.
02/08/2005	Construction contract	n/a	The earliest date of the signing of the construction contract was considered as the start of the project activity. The construction contracts have been submitted to DOE during the validation stage.
28/11/2005	Methodology ACM0008 version 1 approved at EB 22 meeting		*http://cdm.unfccc.int/UserManagement/FileStorage/CDMWF_ACM_XEC4J58XTB4NVRP9DNYDEQJL0ZECCS*
28/01/2006	Confidential agreement signed between the project developer and Buyers		An exclusive agreement for the negotiation for the CERs from the CMM utilization project for Fengrun project. This is a milestone that demonstrates the project owner has started actively meeting CER buyers.
25/11/2006	Term sheet signed		The project owner and Trading Emissions Plc signed the termsheet, in which stipulated the first payment of PDD development will be made only after ERPA signed.
16/05/2007	ERPA		The ERPA between the project owner and buyer signed on 2007/05/16.

23/05/2007	CDM PDD GSP		The English version finished on 10/05/2007 and started GSP http://www.dnv.com/focus/climate_change/Projects/ProjectDetails.asp?ProjectId=1222
03/06/2007	Host country application started		The Chinese version PDD finished and started for host country approval

Question 3

The DOE is requested to clarify how it has validated that:

(i) the CMM supplied to the project will not be supplied from sources other than that allowed by the methodology, considering that CMM is being purchased from near by mines, not owned by the PP, and that the methodology remains applicable to the project throughout the crediting period;

(ii) The CMM would have been vented to atmosphere and not sold in absence of the project activity;

And

(iii) There will be no double counting in claiming emission reductions due to venting of CMM to atmosphere (if any) in absence of the project activity by the owners of the mines and the PP.

PP's response:

(i) Each of the sites of the power plants is adjacent to the mine providing the gas. At each of the nine sites the pipeline runs directly from the mine to the powerhouse. The baseline of each mine has been described in the PDD and validated. During on site visit of the validation the auditor has verified that only one pipeline exists or under construction from the mine to the project site.

No additional gas will be sourced from additional mines which are not allowed in the methodology as each project is located adjacent to the mine which supplies it with gas already. There are no other mines in the immediate vicinity of any of the sites. All mines are active and will not be exhausted until well beyond the crediting period.

As piping the gas is expensive and technically challenging given the safety features required for CMM it is not easy or likely additional gas will be introduced from additional mines. The projects participants do however accept concern that in the future additional gas could theoretically be introduced from adjacent mines and therefore propose to amend the monitoring plan for the project to include checking of the project pipeline and source of the gas feeding the pipeline during verification. Given that the pipelines are short and they are all above ground, it will be relatively easy for the verifier to confirm the source of the gas.

(ii) Given that there is a price for gas it can be argued that there is therefore market demand for the gas and the baseline is possibly therefore not venting or flaring. In fact the price is set precisely because there is no market. The government sets the price to provide some form of transparency to the market as to what a fair price coal mine owners should seek. In the absence of an effective market for supply and demand of the gas, this price setting mechanism helps encourage a market by adding a value to the resource.

In the case of the mines, due to their location, the most practical solution is the use of the methane in engines to produce power. This is the project activity and it has been shown to be financially unattractive and would not proceed in the absence of CDM.

Each mine is located a significant distance from any large urban centre, such as Jincheng, which might have the demand and the required infrastructure in place to make use of the gas. Piping the gas significant distances is not cost effective and the PPs are not aware of any examples of this happening in the province where CDM incentive has not had a material impact. In addition the DOE verified that at each project site there is no reasonable alternative source of demand in close proximity to the sites.

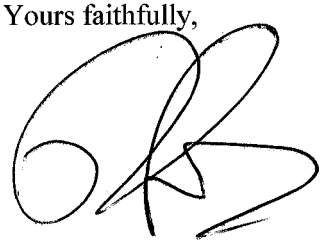
(iii) The final question raised is understood to be related to the risk of double counting if both the mine owner and the project owner were to claim the emission reductions related to reduced venting of the same CMM. This risk of double counting is mitigated by:

Emission reductions can only be generated when the CMM is destroyed, only the activities of capturing or selling the CMM gas cannot result in any emission reductions. For the proposed project activity, the emission reductions can only be archived by the project owner destroying the gas that purchased from the mines, and the destruction activity is carried out in the self-owned facilities within the validated project boundary. For the coalmines, it is unreasonable that to claim emission reductions by any external gas destruction activities, when there is no possession of gas ownership or destruction units.

In China, the CER ownership is shared by the project owner and the Government. The project has been approved by the local DNA who check whether any existing projects in the area already claim emission reductions for the same CMM. If the mine owners were to apply for CDM project registration, they would have to demonstrate the ownership of the gas and the possession of the destruction facilities. The destruction can only occur at one location for any given volume of gas.

- In order to prevent double counting of the emission reduction by both the coal mines and the project owner, the project proponent would like to propose the following approaches:
  - Precise coordinates of the location of each project site will be provided in the PDD;
  - Precise details of metering arrangements will be provided. This will make it clear which meters will be used for the project activity – only gas going to the gen sets of this project can claim CERs through this project. Should the mine owner decide to stop supplying the CMM to the project he could try to proceed with his own project. In such an instance, as the CMM would no longer go through the meters of the Project, the Project would then not be able to claim CERs.

Yours faithfully,



Philip Scales

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Note:

In case you have any further question or request during the review process, please do not hesitate to contact us by phone or e-mail to the person listed below:

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