

Mr. Rajesh Kumar Sethi
Chair, CDM Executive Board
UNFCCC Secretariat
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24th November 2008

Dear Mr. Sethi,

Re: Request for review of the request for registration for the CDM project activity 'Sichuan Pingshan Pingbian&Guanyintuo Hydropower Station' (Ref. No. 1897)

SGS has been informed that the request for registration for the proposed CDM project activity 'Sichuan Pingshan Pingbian&Guanyintuo Hydropower Station' (Ref. No. 1897) is under consideration for review because three requests for review have been received from members of the Board.

The requests for review are based on the reasons as outlined below. Through this letter, we would like to provide responses to the issues raised in the requests for review and provide additional information.

Requests for Review 1-3, Issue 1:

The DOE is requested to justify the suitability of the benchmark, in particular, appropriateness of a benchmark of year 1995 when assessing the additionality of a project activity with investment decision made in 2006.

SGS' Response to Issue 1:

As has been reported in Section 4.4 of the validation report, the benchmark IRR of 10% was used in the PDD which was referred from the Revision of Economic Evaluation Code for Small Hydropower Project (SL16-95). In Section 4.3 of this document (**Annex 1a**), it is indicated that the total investment IRR of the hydropower project with the installed capacity less than 25MW should not be lower than 10%.

According to number 2 under Section Water Resource Industry Standard in the "Bulletin of Valid Hydropower Technical Standard" issued in 2002 by the Ministry of Water Resources of the People's Republic of China, the Revision of Economic Evaluation Code for Small Hydropower Project (SL16-95) is still effective. (**Annex 1b**)

The proposed CDM project activity comprises of two hydropower stations, namely Pingbian Station and Guanyintuo Station. Each of the two stations has an installed capacity of 20 MW, meaning that the benchmark IRR of 10% applies to the two hydropower stations according to the Revision of Economic Evaluation Code for Small Hydropower Project (SL16-95).

The above mentioned information has been added in the revised validation report. (**Annex 1**)

Request for Review 1-3, Issue 2:

The DOE shall describe how the reliability of the input values used in the investment analysis has been validated in accordance with the guidance of EB38 paragraph 54

SGS' Response to Issue 2:

The PDR for a project is an official document prepared by an independent third party. Preliminary Design Report (PDR) will be checked by the relevant authorities before it is approved. As reported in Section 4.4 of the validation report (**Annex 1**), based on the data in the PDR, the project IRR without CDM revenues is 7.82 % (Pingbian Station) and 7.56% (Guanyintuo Station) which is lower than the benchmark 10%. In the revised PDD version 3.0 (**Annex 2**), in addition to the three parameters (Static total investment, Annual operational cost and Grid tariff) that were already used in the sensitivity analysis in the PDD version 2.2, the PP conducted the sensitivity analysis using Annual electricity supplied to the grid to demonstrate that the project faces significant commercial and financial barriers without CDM revenue. (**Annex 2a and 2b**) The PDRs of the project were approved by the local government on 01/06/2005 and 02/11/2005 respectively. (**Annex 2c**) The investment decision was made on 13/06/2006. In accordance with the guidance of EB38 paragraph 54(a), it has been validated that the period of time between the finalization of the PDR and the investment decision is sufficiently short for us to confirm that it is unlikely in the context of the underlying project activity that the input values would have materially changed.

As clarified in the response from the PP, all input values except for grid price used in the IRR calculation of the project in the PDD are cited from PDRs of Pingbian and Guanyintuo. The PDRs of the project were prepared by Chengdu Hydropower Investigation Design & Research Institute, which is an independent third party entity accredited by the relevant national authority to carry out feasibility studies for new projects. Accreditation certificate for Chengdu Hydropower Investigation Design & Research Institute has been validated. The grid price of 0.22Yuan RMB/kWh has been validated to be from the Power Connection Intent Agreement (PCIA) signed on 13/05/2005 and the Power Connection Agreement (PCA) signed on 30/06/2005. (**Annex 2d**) PCA is an official agreement and it is considered as a reliable data source. In accordance with the guidance of EB38 paragraph 54(b), it has been validated that the values used in the IRR calculation in the PDD are fully consistent with the PDR and the value of grid price used in the IRR calculation is appropriate.

In accordance with the guidance of EB38 paragraph 54(c), the following was done to confirm that the input values from the PDR are valid and applicable at the time of the investment decision:

- 1) The annual utilization hours of Pingbian and Guanyintuo used in the IRR calculation in the PDD are 4,705 and 4,580 respectively, both of which are calculated based on water resource data from 1966 to 2000. The possibility of dramatic variation of annual utilization hours during the crediting period from the estimation in the PDD is low.
- 2) The grid price used in the IRR calculation in the PDD has been validated to be from the Power Connection Intent Agreement (PCIA) signed on 13/05/2005 and the Power Connection Agreement (PCA) signed on 30/06/2005. PCA is an official agreement and it is considered as a reliable data source. (**Annex 2d**)
- 3) The value of total investment used in the IRR calculation in the PDD is 256,966,700 Yuan RMB. From the Investment for the Completed Projects of Pingbian & Guanyintuo Hydropower Stations (**Annex 2e**), the total investment of the completed partial projects cost by the project owner is 300,350,000 Yuan RMB, higher than the value of total investment used in the IRR calculation in the PDD.
- 4) The annual operational cost used in the IRR calculation in the PDD is 2,872,100 Yuan RMB (Pingbian) and 3,104,000 Yuan RMB (Guanyintuo). As has been clarified in the response from the PP, the total number of employees during the construction period (112) is bigger than the number in the PDRs (74) and this number will be close to 74 after the construction has been finished; the rate of overhaul cost (1%) has been validated to be consistent with value in the SL16-95 evaluation code; other cost used in the IRR calculation in the PDD (24Yuan RMB/kW) has been validated to be consistent with the value in the Interim Regulations of Hydropower Construction Project Financial Evaluation (**Annex 2f**); the welfare fund (14%) and the employee's insurance (26%) used in the IRR calculation has been validated to be in consistency with the values from the SL16-95 evaluation code and relevant regulations published by Chinese government (**Annex 2g**); the water charge of hydropower station used in the IRR calculation in the PDD (0.001Yuan RMB/kWh) has been validated to be lower than the corresponding value (0.0025~0.005Yuan RMB/kWh) in the Inform of Adjustment on Collection Standard of Water Charge (Doc.: Chuanbanhan [2005]110) in Sichuan Province published by local government (**Annex 2h**); the actual annual salary for the employees from the payroll records (18,000 Yuan RMB/Person, i.e., 1,500RMB/Person/Month as shown in the payroll records for October, 2008 (**Annex 2i**)) has been

validated to be higher than the numbers used in the IRR calculation in the PDD (8,000 Yuan RMB/Person for Pingbian and 10,000Yuan RMB/Person for Guanyintuo)

Request for Review 1-3, Issue 3:

The start date of the project activity should be as per the CDM glossary of terms.

SGS' Response to Issue 3:

The timeline of project has been provided in the response from the PP and the revised PDD. **(Annex 2):**

- Preliminary Design Reports (PDRs) of Pingbian and Guanyintuo hydropower station were completed in April, 2005;
- The Power Connection Intent Agreement (PCIA) with a grid tariff of 0.22Yuan RMB/kWh was signed between the project owner and the grid company on 13/05/2005;
- The Directorate decided to apply for CDM on 18/05/2005; **(This has been uploaded to website of the project on the UNFCCC website)**
- The Project owner entrusted an agency to find a proper cooperator on CDM application on 28/05/2005; **(Annex 3a)**
- PDR of Pingbian hydropower station was approved on 01/06/2005;
- The project owner trusted and confirmed Beijing Tianqing Power International CDM Consulting Co., Ltd to cooperate on CDM application of the project activity on 01/07/2005; **(Annex 3b)**
- Beijing Tianqing Power International CDM Consulting Co., Ltd signed a General Framework Agreement for the Development of CDM projects with Climate Expert Ltd. on 24/10/2005; **(Annex 3c)**
- PDR of Guanyintuo hydropower station was approved on 02/11/2005;
- ENEL signed a Letter of Intent (LoI) to Tianqing about the project on 24/11/2005; **(Annex 3d)**
- The project owner and Tianqing Power signed CDM PDD Cooperation Agreement on 16/01/2006; **(Annex 3e)**
- Approval of supporting CDM application was issued by local government on 12/05/2006; **(Annex 3f)**
- The project owner held a stakeholders' consultancy meeting about CDM application of the project on 17/05/2006;
- The project owner signed the Purchase Contracts of Turbines and Generators for Pingbian and Guanyintuo hydropower stations on 13/06/2006; **(Annex 3g)**

Following the clarification made at the EB41 meeting about the start date of a CDM project activity, which is the earliest date at which either the implementation or construction or real action of a project activity begins, the day (13/06/2006) on which the project owner signed the purchase contract of turbines and generators is considered as the start date of the project activity. As reported in Section 4.2 of the PDD, during the design period of the project, the incentive from CDM has been seriously considered and the relevant Board Meeting Minutes dated 18/05/2005 has been verified by SGS assessor.

- The CDM approval of the project was issued by Chinese DNA on 07/11/2006;
- Pingbian&Guanyintuo hydropower stations were approved to start construction on 18/12/2006; **(Annex 3h)**

The project participants have demonstrated that continuing and real actions were taken to secure CDM status for the project in parallel with its implementation by providing reliable evidences mentioned above.

The above mentioned information has been added in the revised PDD and validation report. **(Annex 1 and Annex 2)**



We apologize if the initial validation report was unclear and hope that this letter and the attached documents address the concerns of the Board. If further information is required, Joe Sun (Joe.Sun@sgs.com +86 13817041095) will be the contact person for the review process and is available to address questions from the Board during the consideration of the review in case the Executive Board wishes.

Yours sincerely,

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Encl:

Annex 1: Revised Validation Report

Annex 1a: the Revision of Economic Evaluation Code for Small Hydropower Project (SL16-95) available from <http://www.cws.net.cn/guifan/bz/SL16-95/>

Annex 1b: Bulletin of Valid Hydropower Technical Standard issued in 2002 by the Ministry of Water Resources of the People's Republic of China available from <http://www.cnhydro.com/techstandard/09.htm>

Annex 2: Revised PDD

Annex 2a: Revised IRR spreadsheet for Guanyintuo

Annex 2b: Revised IRR spreadsheet for Pingbian

Annex 2c: The approval for the PDRs of the project issued by the local government dated 01/06/2005 and 02/11/2005

Annex 2d: the Power Connection Agreement (PCA) signed on 30/06/2005 between the project company and the grid company

Annex 2e: the Investment for the Completed Projects of Pingbian&Guanyintuo Hydropower Stations dated 12/11/2008

Annex 2f :the Interim Regulations of Hydropower Construction Project Financial Evaluation

Annex 2g: relevant regulations published by Chinese government regarding employee insurance

Annex 2h: the Inform of Adjustment on Collection Standard of Water Charge (Doc.: Chuanbanhan [2005]110) in Sichuan Province published by local government

Annex 2i: the payroll records of the project for October, 2008

Annex 3a: CDM trust letter dated 28/05/2005

Annex 3b: CDM trust letter with Tianqin dated 01/07/2005

Annex 3c: General Framework Agreement signed between Beijing Tianqing Power International CDM Consulting Co., Ltd and Climate Expert Ltd.

Annex 3d: Letter of Intent (LoI) signed between Enel and Beijing Tianqing Power International CDM Consulting Co., Ltd dated 24/11/2005

Annex 3e: Cooperation Agreement signed between the project owner and Beijing Tianqing Power International CDM Consulting Co., Ltd dated 16/01/2006

Annex 3f: Approval of supporting CDM application issued by local government dated 12/05/2006

Annex 3g: Purchase Contracts of Turbines and Generators for Pingbian and Guanyintuo hydropower stations signed on 13/06/2006

Annex 3h: Approval for Pingbian&Guanyintuo hydropower stations to start construction issued by local government dated 18/12/2006