Subject: IETA response to the call for input on modalities and procedures for standardized baselines

22 March 2010

Office of the Executive Secretary
UNFCCC Secretariat
Martin Luther King Strasse 8
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Germany

Dear Mr. de Boer,

I am writing to you on behalf of the International Emissions Trading Association (IETA) in response to the invitation made in the document issued at COP/MOP 5 entitled "Further guidance relating to the Clean Development Mechanism" which asks for "Parties, intergovernmental organizations and admitted observer organizations to make submissions to the secretariat, by 22 March 2010, on their views on"… "modalities and procedures for the development of standardized baselines that are broadly applicable, while providing for a high level of environmental integrity and taking into account specific national circumstances".

IETA strongly supports the development of standardized baselines that take into account national circumstances and ensure a high level of environmental integrity. Indeed, IETA believes that this reform proposal is *vital* to enhancing the *efficiency, environmental integrity, and regional distribution* of the CDM. IETA's position paper entitled, "Multi-Project, Standardized Baselines: Explaining a Key Issue in the Reform of the Clean Development Mechanism," was developed for CMP negotiators and has been appended to the end of this letter. It both adds clarity to the discussion by explaining the concept of standardized baselines as well as providing a strong rationale for the integration of standardized baselines by explaining the many benefits of their greater utilization under the CDM.

As is explained it the appended position paper, IETA believes that the UNFCCC discussion to date has unnecessarily narrowed the focus of this reform item, however. There are three major steps in the CDM project cycle:

- the establishment of additionality,
- the determination of crediting baselines (or, baseline emissions), and
- the determination of ex-post project emissions.

IETA believes that the incorporation of standardized approaches into all of them would provide significant benefits by enhancing efficiency, increasing the objectivity of decision-making, and increasing accessibility to the CDM.

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Therefore, IETA believes that SBSTA's work on this issue should not be limited to the development of standardized baselines alone but rather should be expanded to consider the wider incorporation of standardized approaches, including the use of the following:

- Emissions intensity benchmarks: Set baseline emissions for project and program activities based on the GHG intensity per unit of production. The term "emissions intensity benchmarks" is often used interchangeably with "standardized baselines." Emissions intensity benchmarks can also be used to establish the additionality of a project in some cases.
- Positive lists: Replace the additionality test by determining eligibility for crediting for project activities that either (1) do not generate non-carbon revenue streams, or (2) experience high barriers to investment but which have faced significant challenges when trying to prove their additionality in the CDM to date (due to data availability, for example).
- Deemed- or per-unit values: Streamline the determination of the emission reductions of a project by allowing project participants to multiply a conservative estimate of the average emission savings of a given unit by the number of those units involved in the project activity, rather than carry out an extensive and costly monitoring plan.
- Default values: Streamline the process of gathering the necessary data for the determination of emission reductions by using conservative default values in place of actual measurements.
- Standardized barriers tests: Standardize tests used to establish the additionality of project activities for project types for which the entire additionality determination cannot be standardized

Taking Action

Standardized baselines as well as other standardized approaches are already possible under the CDM today, but they are extremely under-utilized. While the causes of this underutilization are multiple, the following play a large part in the current neglect of standardized approaches within the CDM:

- the opposition by some EB members to the increased usage of standardized approaches;
- the lack of a clear mandate from the Parties to increase their usage;
- the lack of clear CDM Guidance for project participants on the development of standardized approaches; and
- the difficulties faced by individual project participants in gathering the data needed to develop these standardized approaches on their own.

In order to reverse this underutilization, IETA suggests that SBSTA recommend that CMP 6 take a series of decisions:

1. The CMP should give directions for the use of top-down and bottom-up approaches for the development of standardized approaches for the determination of baseline emissions, the establishment of additionality, and the determination of ex-post project emissions.
2. Bottom-Up Approach: The CMP and the CDM EB should **invite** project developers and other market participants to develop and submit for approval to the EB methodologies and methodological revisions containing standardized approaches, including emissions intensity

benchmarks, default values, standardized barriers tests, and deemed values, as well as propose criteria for positive lists.

3. Top-down Approach:
    a. The EB should create a Stakeholder Advisory Panel for Standardized Approaches, with official standing, to support and advise the EB and Secretariat[1] as they take actions to facilitate the top-down development of standardized approaches. The Panel should be composed of CDM stakeholders; DNA representatives; and Industry experts, with additional experts, community representatives, and government stakeholders consulted when necessary. The Advisory Panel should fulfill two roles:
        i. Policy Role: Provide support in the drafting of new CDM Guidance for the development of standardized baselines and other standardized approaches.
        ii. Technical Role: Engage with and advise the EB and Secretariat as they develop top-down approaches.
    b. The EB should mandate regional multilateral organizations (such as, regional development banks) to coordinate efforts to gather necessary data and develop standardized baselines for final approval by the EB. It is important that this process be seen as impartial, transparent, credible and rooted in national and regional circumstances.

Learning Phase

IETA suggests that the work plan for the development of standardized baselines and other standardized approaches begin with a "learning phase" in order to gain the insight necessary to inform the drafting of new guidance for the development of standardized baselines and other standardized approaches. This learning phase should focus on the following:

1. **Improvement of Existing Methodologies:** For the first ~6 months, the EB, Secretariat, and Advisory Panel should place priority on analyzing existing methodologies (both those approved and submitted for approval) and identifying possibilities for the incorporation of standardized baselines and other standardized approaches. When determining which methodologies to focus on, the following general method of prioritization should apply:
    a. Methodologies judged to be applicable to countries with less than 10 CDM project activities
    b. Small-Scale Methodologies
    c. All other Methodologies.
2. **Review of Lessons Learned:** The Advisory Panel should review the lessons learned by this process and provide advice to the EB and Secretariat regarding:
    a. identification of gaps in existing CDM Guidance where revisions or new Guidance is required;
    b. provision of support in the drafting of required revisions and/or new Guidance; and
    c. provision of support in the drafting of a work plan for the second phase of activities to encourage and facilitate the development of standardized approaches for the CDM.

[1] IETA believes that additional, dedicated Secretariat staff will be required for the development of standardized approaches.

Quick Start

In order to jump-start the development of standardized approaches, IETA suggests that the Advisory Panel, in conjunction with the EB and Secretariat, consider undertaking the following "quick-start" activities concurrently with or immediately following the learning phase:

1. As the Methodologies Panel moves to develop top-down methodologies for project activities applicable in countries with less than 10 registered project activities, as requested by CMP 5, the Advisory Panel should be engaged to help develop methodologies that have as many standardized elements as possible.
2. The Advisory Panel should support the EB and Secretariat in the development of an initial positive list that is limited in scope, has clear criteria for eligibility, and has a pre-established date of expiry. In order to ease concerns that have arisen about the utilization of positive lists, this initial list could be followed by a pre-indicated review period to review the impact of the list on project registration and inform the development of subsequent lists.
3. The Working Group should develop a work program to aid countries in the calculation and publication of grid-emissions factor(s), with an initial focus on providing support to host countries with fewer than 10 registered project activities.

IETA greatly appreciates the opportunity to provide our input on the development of standardized baselines and other standardized approaches for incorporation into the CDM. We believe that this issue is one of the most critical elements of CDM reform under discussion today, and we look forward to engaging in the process of the development of standardized approaches in the near future. Please do not hesitate to contact me at derwent@ieta.org or Kim Carnahan at carnahan@ieta.org should you have any questions regarding this letter.

Sincerely,

Henry Derwent
President and CEO, IETA

Addendum:

Multi-Project, Standardized Baselines and Beyond: Explaining a Key Issue in the Reform of the Clean Development Mechanism

One reform proposal under discussion in the AWG-KP, which has now also been put on the agenda of the June 2010 SBSTA meeting, refers to "the development of standardized, multi-project baselines under the Clean Development Mechanism." This reform proposal is ***vital*** to enhancing the *efficiency, environmental integrity, and regional distribution* of the CDM. The concept itself lacks clarity, however, which is hindering the Parties' initiative to move forward. This document aims to inject renewed vigor in the discussion of CDM reform by answering the following questions:

- What exactly is a "multi-project, standardized baseline"?
- What are the benefits and perceived shortcomings of multi-project, standardized baselines and other standardization tools?
- What are some examples of how standardization tools can be applied to key project types?
- How can the Parties and the CDM Executive Board best facilitate the development of multi-project, standardized baselines and other tools for standardization?

All projects that aim to generate CERs under the CDM rules must meet essentially the same criteria and complete the same steps. This process is commonly known as the CDM project cycle. An initial step in the project cycle requires that project proponents undertake a lengthy eligibility exercise, including the justification of project *additionality* and identification of the *baseline scenario*, which is the level of emissions that would have occurred were it not for the CDM project. Streamlining and simplifying this process through the introduction of certain standardization tools decreases project costs and simplifies the very complicated process of CDM registration and issuance, thereby increasing access to the CDM and the transparency and predictability of the system.

What exactly is a "multi-project, standardized baseline"?

The key element in this concept is "standardization." Standardization refers to the adoption of generally accepted uniform procedures, and is used to enable objective comparison or judgment to simplify and add more predictability to decision-making. In the CDM, there can be standardized methods for:

1. the establishment of additionality,
2. the determination of baseline emissions of the project or program (i.e. the crediting baseline), and

3. the determination of actual project or program emissions after the project has been implemented in order to be able to request credit issuance.

While the current negotiating text implies a focus on the second point— standardized *crediting baselines*— methods for standardizing all three of these steps in the CDM project cycle can be developed and would benefit CDM stakeholders by simplifying the process of quantifying emissions reduction credits.

The following **tools of standardization**, whose use will differ based on the project type and country in question, have been developed to streamline these three steps in the CDM project cycle:

1. **Emissions intensity benchmarks:** Accomplish either of the following,
    a. **Set baseline emissions *and* establish additionality for project and program activities for which the business-as-usual GHG intensity per unit of production can be established.** Examples of project types that could use this type of benchmark include: cement production, aluminum production, nitric acid production, appliance efficiency, and vehicle emissions intensity.
    b. **Set baseline emissions levels in combination with a standardized additionality test based on a binary benchmark or positive list.** Examples of project types that could use this type of benchmark include: renewable power plants and avoided gas flaring at oil fields/refineries.

2. **Positive lists:** Streamline the process of establishing additionality for two types of activities:
    a. **Project or program activities that generate non-carbon revenue streams, but are generally observed to face high barriers to investment.** These lists are established based on a determination of eligibility for crediting made beforehand by policymakers, such as the COP/MOP, CDM EB, or another political body, and could streamline the eligibility determination for projects deploying technologies that the Parties clearly intended for the CDM to incentivize yet which face significant challenges when trying to prove their additionality. Prime candidates for positive lists include: electricity generation from solar, wind (in some countries), and small hydro; and residential or commercial building efficiency.

    b. **Project or program activities for which there is no real motivation for the activity if not for CDM revenues—including either no regulatory requirements or demonstrable non-enforcement of existing regulation**. In other words, for these project activities there would be a "binary benchmark" based around the question: "Are there revenues other than CDM revenues from the emission reduction activity?". If the answer is no, then the project is additional. Examples of project types that could use binary

benchmarks include: landfill gas and anaerobic digestion of agricultural wastewater.

3. **Deemed or Per-Unit Values:** Help determine the emission reductions of a project or program activity by allowing project participants to multiply a conservative estimate of the average emission savings of a given unit by the number of those units involved in the project activity, rather than carry out an extensive and costly monitoring plan. Examples of project types that could use deemed values include: solar lamps, high efficiency cook stoves, and high efficiency light bulbs.

4. **Default Values:** Help streamline the process of gathering the necessary data for the determination of emission reductions by using conservative default values in place of actual measurements. Default values are normally based on actual existing measurement data of similar, but not identical, conditions and are already used in many methodology types, particularly in countries where data is unavailable and/or costly to obtain. For example, ACM 0010 for manure management systems rely on many default values from the IPCC's 2006 Guidelines for National Greenhouse Gas Inventories in place for actual measurements for animal weight, biological oxygen demand, volatile solids, etc.

5. **Standardized Barriers Tests:** For project types where the entire additionality determination cannot be standardized, tools can also be devised to address each of the "barriers tests" currently used in the Tool for the Demonstration and Assessment of Additionality. Examples include: the assessment of, for example, market penetration rate. For instance, ACM 0005 includes a barrier test to determine whether or not the project qualifies as 'first-of-its-kind,' which requires the project to demonstrate that the market share of the technology used by the project activity is 5% or lower.

Many of these concepts are not new to the CDM; they are simply underused. For example, several examples of emissions intensity benchmarks can be found in approved methodologies being used in the CDM today:

- ACM 0013 for new grid-connected fossil fuel-fired power plants entails the use of an emissions intensity benchmark based on the performance of the top 15% of power plants that use the same fuel as the project plant and any technology available in the same geographical area. This benchmark is compared with the emission factor of the technology and fuel type that has been identified as the most likely baseline scenario, and the lower of the two is taken as the crediting baseline.

- ACM 0002 and AMS I.D for new grid-connected renewable power plants rely on a standardized baseline emission factor, known as the grid emission factor (GEF). Several other methodologies also use a GEF when producing electricity for on-site or

grid consumption. The means to calculate this factor are described in a so-called "methodological tool," which can be used for any host country. The emission factor differs country-by-country or even region-by-region within a country due to variations in each host country's existing power plants. Currently, the GEF must be calculated by each CDM project wishing to apply it. Its standardization can be achieved by having one central authority in each country/region responsible to calculate the grid factor each year.

There are only a few examples of the use of these standardization tools in the CDM today, however, despite the great promise they hold to simplify registration and issuance. Indeed, of all these approaches, the development and use of emissions intensity benchmarks has proven particularly difficult because of a lack of data available to individual project developers. A designated work program to gather such data at a level higher than individual project developers would substantially ease these constraints.

Sub-National, National, or Regional in Scope?

The concept of standardized baselines and, particularly, the idea of creating emissions intensity benchmarks received negative attention at last year's COP/MOP in Poznan because they were perceived as an attempt to force countries toward a common emissions intensity, and somehow place them on the road to binding emissions targets**. In the context of the CDM, this perception is completely inaccurate**.

Emissions intensity benchmarks would be determined country-by-country in all cases, unless it was more beneficial in terms of ease of measurement and monitoring to determine them regionally or globally. For example, it may prove less expensive and entirely appropriate to develop and use a single benchmark for several small countries in Africa that share a grid system as well as social and economic characteristics. Similarly, a common benchmark and default factors may prove very helpful in facilitating several types of programs of activities, in particular those distributing compact fluorescent light bulbs. On the other hand, in very large countries it may be necessary to have several benchmarks within the country to address significant differences between different areas.

What are the benefits and perceived shortcomings of multi-project, standardized baselines and other tools for standardization?

Standardization provides numerous benefits to the CDM along a number of parameters:

1. Regional and Sectoral Distribution: The uncertainty and costs related to determining crediting baselines, establishing additionality, and determining emission reductions ex-post on a case-by-case basis disproportionately impacts the economic viability of PoAs, small-scale projects, projects in LDCs, projects trying to break into new, untried sectors, and projects developed within small and medium-sized enterprises. Lowering these high transaction costs is absolutely key to incentivizing the flow of investment dollars into underrepresented host countries. Moreover, the work program created within the CDM to develop these approaches could be designed to specifically focus on the development of methodologies that would work particularly well in such countries.

2. Extensive Cost Reduction: The #1 cause of requests for review and reviews in the CDM stems directly from the current subjective determination of additionality under the CDM. The basic requirement to demonstrate that the project "would not have happened anyway" leads to endless questions and continuous distrust between the CDM EB and its Secretariat, DOEs and project participants. This not only causes massive delays in the system, it adds significant costs when the CDM EB and its Secretariat, in order to prove the additionality of the project, request additional data and expensive analyses, which require added work hours billed by consultants and the validating DOE. By reducing the cost of proving additionality, the use of benchmarks or positive lists directly affects the commercial viability of projects. The use of default factors or deemed value approaches will reduce the development costs even more, thereby further increasing the commercial viability of currently unprofitable projects.

3. Greater Predictability: Another factor directly impacting the willingness of private actors to invest in CDM projects in host countries with less favorable investment environments is the ability to predict whether or not the project in question will inevitably be registered by the CDM EB and eligible to receive emission reduction credits. For projects with relatively high likely profits, such as large projects in countries with good investment environment, the question of eligibility is less of a deterrent. For small countries, with a less favorable investment situation, the lack of assurance that a project will receive CER revenues, and the ability to accurately predict the flow of CER revenue, is critical.

4. Increased Simplicity and Accessibility: The CDM EB makes decisions on the additionality of project activities in closed sessions, for reasons that are often seen as vague and confusing, and claims have been made that decisions seem biased towards or against certain project types and host countries. Similarly, methodologies often require very complex calculations and monitoring to determine baseline and actual project emissions, which confuse even the most experienced methodology experts. Objectively establishing additionality and determining crediting baselines and project emissions through the use of

standardized procedures and data sets would simplify the project development process so that the CDM would be clearer and thereby more easily accessible to potential stakeholders.

5. Continuous GHG Improvements: Some emissions intensity benchmarks lead to direct environmental benefits by building in an incentive to continuously improve emissions intensity for that particular project type. For example, in ACM 0013, CDM projects are included in that calculation, so the benchmark will necessarily increase over time as more and more projects are undertaken in the area. Including CDM projects into the benchmark calculation is not appropriate for all technology types but it will incentivize continuous GHG efficiency improvements in those where it is.

Standardization does bring up some concerns, however. Some perceived shortcomings must be addressed:

1. **Ensuring that standardized methods for additionality and crediting baseline determination do not lead to over-crediting:** In order to preserve the environmental integrity of the CDM, the concept of conservativeness is key. The application of discount factors to account for uncertainty and the use of caps on output when the CDM could conceivably provide a perverse incentive to increase production unnecessarily ensure that the CDM is already very conservative. The principle of conservativeness will also need to be carefully applied when establishing emissions intensity benchmarks, deemed values, and default factors.

   Even so, the Parties will have to accept that some projects that would have happened anyway will be registered, and some projects will receive more credits than they deserve. **The nature of the mechanism, however, is that over-crediting or the registration of non-additional projects will be balanced out by a corresponding amount of under-crediting and the ineligibility of some truly additional projects.** In other words, the principle of conservativeness when applied to standardized baselines **will ensure additionality and appropriate crediting *on aggregate***, while making no direct claims on the additionality or crediting baselines of each individual project.

2. **Addressing the concern that conservativeness may rule out truly additional projects from eligibility**: By applying ambitious emissions intensity benchmarks and/or very conservative values when calculating per-unit emission reductions, the use of standardized baselines will inevitably cut out projects that are reducing emissions relative to their own project-specific business-as-usual situation. As explained above, this can simply be seen as a trade-off of the system—simplifying the process ensures that many more projects can be developed and registered but some projects that would have previously qualified for credits no longer will because they are not sufficiently ambitious. It might be noted that the Parties have the option to allow projects facing especially taxing barriers to forgo the use of these standardization tools and instead

use the existing methodological tools to establish additionality and baseline emissions. The Parties should exercise caution when creating such loopholes, however, in order to ensure that the trade-off between over and under crediting is maintained.

3. **Addressing concerns about "choosing winners"**: A common criticism of any technology policy always entails the question of whether or not government representatives should be choosing winners and losers by providing incentives for one technology type and not another. By placing certain technologies or project types on a positive list, however, the Parties are not precluding project developers from developing other projects using different technologies, they are simply easing the process by which they can develop projects on the list, which will in fact ease the registration and issuance process for all project types by cutting out a significant amount of extra work for the Secretariat, DOEs, and project participants. Moreover, in many cases, the process of placing a project type on a positive list will simply neutralize the unintentional, structural disincentives that technology was facing before.

4. **Addressing the political difficulty of agreeing on positive lists:** The question will also arise as to how any UNFCCC body— whether the COP/MOP itself, a sub-committee of it, or the EB— will be able to agree on the project types placed on a positive list, giving differing ideas of what should and should not be incentivized, in what countries they should be incentivized, and for how long they should stay on the list. Indeed, the Parties have attempted the creation of positive lists before, to no avail. Having now been able to witness the difficulties faced by certain project types— including, small scale renewables, end-use energy efficiency projects, and transport projects— the Parties may now be more prepared to give some technologies an extra push, especially if they begin with some of the most obviously beneficial and commercially uncompetitive technologies. If this is not the case, however, and the Parties cannot come to a consensus, then it may be time to consider putting such questions to a vote rather than waiting until consensus can be reached.

What are some examples of how standardization tools can be used with key project types?

Renewable-Energy Electricity

Projects generating electricity from renewable energy sources would be enabled further by implementing a positive list to determine additionality and a grid-specific GHG intensity benchmark for baseline emissions. The recommendation for placement on a positive list is based on the principal that even in Annex 1 countries, renewable power plant projects rely on subsidies, feed-in tariffs and/or an Emission Trading System in order to garner investment. The grid-specific GHG intensity benchmark could be adapted from the grid factor defined by the CDM in the *Tool to calculate the emission factor for an electricity system*; however, the grid factor should be determined annually by a central authority in each host country and validated

by a DOE one time, after which project developers should able to apply the result directly to their projects without an additional DOE validation.

Transport

Emission reductions projects in transport would benefit from regional GHG intensity benchmarks for baseline emissions and additionality. The transport sector is experiencing rapid growth in emissions but so far has not been affected by the availability of carbon finance because multiple factors influence transport-related emissions. For example, shipping companies must transport goods over various routes, using various types of vehicles, and different drivers and associated driving habits, which are all dependant on a range of economic and logistical conditions. Preparing project-specific additionality and baseline assessments and monitoring the emission reductions of the project requires very significant amounts of data, yet still can be fraught with uncertainty. Standardized benchmarks that set an appropriately low crediting level to ensure environmental integrity— such as establishing benchmark transportation emissions per kilometer travelled, per ton-kilometer of goods shipped, or per passenger-kilometer— will drastically reduce the associated uncertainty and cost for project developers.

High Efficiency Cook Stoves

Projects implementing household-level technologies with high sustainable development benefits could be encouraged via a positive list additionality test for chosen technologies, such as high efficiency cook-stoves. These projects could utilize country-specific emissions intensity benchmarks for baseline emissions. Default factors or deemed value approaches could also be used to determine the actual emissions level of the project activity. Using all three of these standardization methods together will dramatically increase the access to carbon finance for these projects, since the alternative of preparing individual, detailed additionality, baseline, and actual emission assessments for projects of such small size is currently untenable.

How can the Parties and the CDM Executive Board best facilitate the development of multi-project, standardized baselines?

Although some of these methods can technically be developed now, significant progress is unlikely without any new decisions being taken by the COP/MOP. A dedicated work-plan is need to facilitate their creation. Many issues mean that their development is moving much too slowly, including the following:

- time constraints within the Methodology Panel and Small-Scale Working Group,
- high costs of development relative to the budgets for projects in LDCs and for small-scale projects, and
- enduring concerns about how and by what bodies positive lists, in particular, should be determined
- unnecessary hesitation on the part of certain EB members to move forward with these methods.

To ensure that work on standardization methods begins immediately, the COP/MOP should do the following:

- *Provide* clear direction to the Executive Board to urgently facilitate and encourage the development of these standardization tools through the design of an ambitious work-plan to organize the necessary work.
- *Instruct* the Executive Board to engage closely with various CDM stakeholders, including local communities and experienced project developers, in the development of these standardization tools in order to ensure that they protect environmental integrity and constitute practical approaches for the individuals working on the ground.
- *Instruct* the Executive Board to include a few key technologies/project types in an initial positive list and request the Board to develop the necessary criteria.