January 5, 2011

Our Inputs on the Revised Draft "the Guidelines on the Assessment of Investment Analysis" (Version 04, Annex # to the EB 58 Report)

Japan Quality Assurance Organization

We would like to make two comments and three inquiries/clarifications as follows. We would be very pleased if the EB could respond to the following comments and inquiries/clarifications.

1. Paragraph 15/Appendix A

The second paragraph of **"Appendix A: Default values for the expected return on equity"** describes as follows:

"The risk free rate of return is calculated based on the long-term average returns of US treasury bonds. The US stock market is used as a proxy because it has the longest well recorded data for government bonds as well as stocks. A value of 3.0% is used."

We understand that the Non-Annex I Countries are usually lacking credible and well recorded data of risk free rate of return because of immaturity of their financial markets and regulation on/limitation to free, cross-border inflow and outflow of capital. Based on the above situation we cannot understand why the risk free rate of return based on the US long-term treasury bonds could be applied as respective risk free rate of return in these countries, of which financial markets, their structures or their market participants are different from the US financial market. We would ask the EB to provide us with the rationale why the risk free rate of return based on the US long-term treasury bonds could be applied as respective risk free rate of return in these countries. Even if we could apply the risk free rate of return based on the US long-term treasury bonds as respective risk free rate of return in these countries, we think that we should make all investment analysis for CDM project activities in these countries being denominated in not their currencies but US dollars in order to keep consistency and compatibility among the financial input data, assuming that free, cross-border arbitrage transaction of currencies and capital is ensured in these countries. In other words we think that we could not apply the risk free rate of return based on the US long-term treasury bonds as respective risk free rate of return in these countries unless the above condition or assumption is ensured.

The third paragraph of **"Appendix A: Default values for the expected return on equity"** describes as follows:

"The equity risk premium is derived from the long-term historical returns on equity in the US market relative to the return of bonds."

We would like to make the same comment as made on the second paragraph of the Appendix.

2. Paragraph 16

(a)
We would ask the EB to provide us with the definition of "registration issuance in the financial system and set-up in the market" and the reason why these are key parameters of the bond.

(Rationale)
We would ask the EB to clarify why "company specific interest rates are only relevant for projects with only one possible project developer," which we cannot understand the above phrase clearly.

3. Paragraph 17

(b) and the last sentence
We would ask the EB to provide us with the rationale why "50% debt and 50% equity financing may be assumed as a default" if the debt/equity finance structure is not available and the rationale why "50% debt and 50% equity financing may be assumed as a default" if the information on "the typical debt/equity financing structure observed in the sector of the country" is "not readily available."