April 14, 2010

Input for the Call:the draft "Tool to calculate the weighted average cost of capital (WACC)"

Japan Quality Assurance Organization

Step 4: Option 4A & 4B of the draft

Paragraph 111 (b) of the **"Clean Development Mechanism Validation and Verification Manual**"(Version 01.1, Annex 3 to the EB 51 Report) provides "(the DOE) Ensure that any risk premiums applied in determining the benchmark reflect the risks associated with the project type or activity." The Sub-step 2b (6) (a) of **"Tool for the demonstration and assessment of additionality"**(Version 05.2, Annex 10 to the EB 39 Report) refers to "a suitable risk premium to reflect private investment and/or the project type, as substantiated by an independent (financial) expert or documented by official publicly available financial data."

Option 4A (Use the average global expected equity return) and **Option 4B** (Use the country specific equity return) respectively recommend to use, as equity risk premium, the default values of 4.7% (**global equity risk premium**) and 4.1% (**general equity risk premium**), which are referred to in **"The worldwide equity premium: a smaller puzzle"** written by Elroy Dimson, Paul Marsh and Mike Stauntnun (from London Business School). This paper provides worldwide annual equity premiums for the period from 1900 through 2005 based on the stock indexes of the 17 developed countries. However, the equity risk premiums discussed in the Option 4A and 4B are the premiums in the Non-Annex I Parties that are not developed countries. We wonder whether or not the above "global equity risk premium" or "general equity risk premium" elaborated based on the relevant statistics in the developed countries is applicable as the default value of the equity risk premiums in the Non-Annex I Parties where it is not easy to get reliable or credible data or information on government bonds or stock markets. We would ask the CDM Executive Board to provide us with the rationale that we could apply the above "global equity risk premium" or "general equity risk premium" to the equity risk premiums in the Non-Annex I Parties as their default values. If we use the above premiums as the default values of the equity risk premiums in the Non-Annex I Parties, we further wonder whether or not those premiums reflect "the risks associated with the project type or activity"(Paragraph 111 (b) of the **"Clean Development Mechanism Validation and Verification Manua**l") or "private investment and/or the project type, as substantiated by an independent (financial) expert or documented by official publicly available financial data"(the Sub-step 2b (6) (a) of **"Tool for the demonstration and assessment of additionality").**

We would also ask the CDM Executive Board to clarify the difference between "global equity risk premium" and "general equity risk premium" because the draft did not provide any definitions of the above terms.