

How to further improve the
assessment of additionality

Additionality Tool

- 2 Options:
 - An alternative exists which would have been financially more attractive, e.g with a higher IRR (investment analysis)
 - The CDM project faces serious barriers, other than financial attractiveness (barrier analysis + Foik)
- Only barrier analysis requires to show how CDM alleviates the barrier
- Additionality Tool initially developed and proposed by the Netherlands, but experience shows that this concept is too much simplified and invites for creativity and free riders

Considerations on additionality

- CDM is a “zero-sum game”, since all CERs are used as offsets by Annex 1 countries
- After its introduction Additionality Tool (AT) was heavily criticized by PPs/IETA but later experience revealed creative use of this Tool → more guidance by Board
- Some critics tell us that 40-70% of all CDM credits are not credible (icing on the cake; not additional)
- Convinced it is not that bad, but Board should be open to discuss potential flaws in our system
- Despite several requests PPs never came forward with better way to assess additionality (are the huge financial revenues of CDM too important?)
- Now the Board should act, recognizing that any non-credible CER should be a concern to every Board member since environmental integrity is at the heart of CDM M&P

Concerns investment analysis

- In many cases difference in Project IRR versus Benchmark IRR is small (even when applying sensitivity analysis on input data)
- Small difference in IRR in such cases is not credible to support claim that only CDM is decisive for investment decision
 - other relevant elements are inter alia:
 - Strategic long term plans
 - Competitive position of company in the market
 - Product quality
 - Availability of resources (e.g. fuels, feedstock, cheap labor ect.)
 - Other local circumstances
 - Greenfield: comprehensive and optimized design
- Conclusion: only larger differences in IRR are credible for CDM claim
- Public sector:
 - not profit driven, so IRR often irrelevant
 - priority determined by demand for service or good and availability of capital

Flaws in additionality testing

- The following elements can be considered as flaws in the actual additionality testing:
 - A small difference between Project IRR and Benchmark IRR is no credible proof that project would not have been implemented without CDM
 - In addition, IRR calculations are still easy to manipulate
 - Many public sector projects would finally go ahead without CDM, perhaps some years later
 - Huge investments (> US\$ 50 – 100 million) with long lead times do not really depend and rely on the highly uncertain CDM
 - In addition: greenfield projects always optimized design
 - Excluding CDM projects for ever from the Common Practice check finally results in outdated technology still used as the reference

Potential solutions (1)

- For large (> US\$ 50 - 100 million) or for all private sector projects using investment analysis:
 - If Project IRR \geq Benchmark IRR:
 - not additional and no CERs can be claimed
 - If Project IRR is > [20]% (relative) lower than Benchmark IRR:
 - all CERs are considered clearly additional
 - For grey area where additionality is uncertain:
If Project IRR is between 0% and [20]% lower than Benchmark IRR:
 - factor in uncertainty, so CERs can be claimed pro rata only
 - Re-insert step 5 in AT for investment analysis: explain how CDM helps to overcome investment barrier

Potential solutions (2)

- Public sector may need another approach:
 - Is driven by urgent need for service or good, which may have been implemented without CDM a couple of years later anyhow
 - Large public sector projects (e.g mass rapid transport systems): max [7] [10] years crediting
 - Rate of return may be less relevant, so IRR may be wrong reference
 - CDM > x % of Operational Costs?
 - Accept trade-off between non-credible CERs and important SD impact (for LDCs only?)
 - Focus more on access to capital?
 - Other barriers?

Proposed other improvements

- Exclude LDCs and SIDS from proposed “20% rule”
- Any greenfield project can only use investment analysis or Foik (other barrier analysis not allowed)
- Clear technology step-changes in industry, requiring large investments (> US\$ 50-100 million) are not additional, since change in technology encompasses many other benefits (e.g. product quality, production rate and capacity) → huge cost savings, which are easy to hide in investment analysis.
- CDM projects are no more excluded from Common Practice test >[7] [10] years after their registration date

Proposed decisions + way forward

- Private sector projects:
 - Road test impact of introducing the (pro rata) 20% rule for private sector projects (LDCs/SIDS exempted)
 - Introduce step 5 in AT for investment analysis: how does CDM overcome investment barrier?
 - Exclude use of other barriers for all large greenfield projects
 - Ask Meth Panel advice on which step-change technologies should be excluded (= non-additional)
- Restrict exclusion of CDM projects from Common Practice test to only 10 years
- At EB66 secretariat presents draft revision of AT
- Assign consultant to elaborate on the public sector approach on additionality