

## THE CLEAN DEVELOPMENT MECHANISM

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### I INTRODUCTION

In March 2001 the Bush Administration officially announced that it was withdrawing its support for the *Kyoto Protocol to the United Nations Framework Convention on Climate Change* ('*Kyoto Protocol*').<sup>1</sup> One of the reasons cited was a unanimously approved Senate resolution that stated that both developed and developing countries must agree to emission reductions before the United States would ratify the *Kyoto Protocol*. According to the Bush Administration, the *Kyoto Protocol* is 'unfair' because it excludes developing nations from responsibility to reduce emissions.<sup>2</sup> It is true that developing countries are exempted from binding emission reduction targets in the first commitment period under the *Kyoto Protocol*. However, the Bush Administration's reasoning is based on a number of basic misunderstandings about the involvement of developing countries under the *United Nations Framework Convention on Climate Change* ('*UNFCCC*'),<sup>3</sup> and the mechanisms under the *Kyoto Protocol* to engage developing countries in climate change action.

### II BUILDING FINANCIAL AND TECHNOLOGICAL BRIDGES WITH DEVELOPING COUNTRIES

At a recent conference organised by the Pew Center for Climate Change,<sup>4</sup> Jan Pronk, President of Sixth Conference of the Parties to the *UNFCCC* ('COP 6'), took the opportunity to highlight a number of issues regarding the participation of developing countries in global climate change action. He noted

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1 Opened for signature 16 March 1998, 37 ILM 22.

2 See George W Bush, *Text of a Letter from the President to Senators Hagel, Helms, Craig and Roberts*, Press Release (13 March 2001) <<http://www.whitehouse.gov/news/releases/2001/03/20010314.html>> at 3 June 2001.

3 Opened for signature 4 June 1992, 31 ILM 849 (entered into force 21 March 1994).

4 Equity and Global Climate Change Conference, Washington DC, 17 April 2001.

that equity requires that developed countries start reducing their emissions now. Per capita emissions in developed countries are more than 20 times as high as per capita emissions in poor countries.<sup>5</sup> Moreover, historic emissions leading to current changes in climate are having a greater detrimental impact on developing countries than on developed countries.<sup>6</sup>

Pronk also pointed out that developing countries *do* have a number of commitments and obligations under the *UNFCCC*,<sup>7</sup> and that although they are exempted from specific quantitative targets and timetables in the first commitment period (2008-12) under the *Kyoto Protocol*, this delay is in line with the internationally accepted principle of common but differentiated responsibility. In order to be able to assume full responsibility for reducing emissions, developing countries must be assisted in their efforts by developed countries. And it is here that the *UNFCCC* and the *Kyoto Protocol* have an important role to play, setting up the framework for developed countries to provide the financial and technological assistance to developing countries to assist them in formulating sound domestic climate change policies and in adapting to the consequences of climate change.

The transfer of environmentally sound technologies and expertise to developing countries and support for capacity building are significant elements of developing country participation in climate change action.<sup>8</sup> The most equitable and effective means of involving developing countries is for developed countries to provide such assistance, whilst also taking the lead in reducing their emissions, particularly given that 'they are best placed, both economically and technologically, to make – and help others to make – the necessary changes'.<sup>9</sup> Indeed, art 4(5) of the *UNFCCC* obliges developed countries to promote, facilitate and finance the transfer of environmentally sound technologies to developing countries so as to enable them to implement the provisions of the *UNFCCC*. Similarly, art 4(7) notes that the extent to which developing countries will effectively implement their commitments will depend on the effective implementation by developed countries of their commitments in relation to financial resources and the transfer of environmentally sound technologies.

Building on these financial and technological commitments is the Clean Development Mechanism ('CDM'), established under art 12 of the *Kyoto Protocol*. Under the CDM, developed countries will be able to fund eligible

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5 Jan Pronk, (Speech presented at the Equity and Global Climate Change Conference, Washington DC, 17 April 2001) <<http://www.pewclimate.org/events/pronk.cfm>> at 3 June 2001.

6 Ibid.

7 See, eg, art 4(1)(b), which requires all Parties, including developing country Parties, to 'formulate, implement, publish and regularly update national ... programmes containing measures to mitigate climate change by addressing anthropogenic emissions by sources and removals by sinks' of greenhouse gases.

8 See art 2 of the *Kyoto Protocol*, as well as the informal negotiating proposals regarding developing country assistance put forward by the President of COP 6 in Jan Pronk, *Note by the President of COP 6* (23 November 2000) <<http://www.unfccc.int/resource/docs/cop6/dec1-cp6.pdf>> at 3 June 2001, and Jan Pronk, *New Proposals by the President of COP 6* (9 April 2001) <[http://www.unfccc.de/sessions/cop6\\_2/unfccc\\_np.pdf](http://www.unfccc.de/sessions/cop6_2/unfccc_np.pdf)> at 3 June 2001.

9 See Kofi Annan, (Speech presented at Fletcher School of Law and Diplomacy, Tufts University, Medford, 20 May 2001) <<http://www.unfccc.int/media/presse/sgspeech200501.pdf>> at 3 June 2001.

emission reduction projects in developing countries and use the resulting Certified Emissions Reductions ('CERs')<sup>10</sup> to offset part of their national reduction commitments. But the increasing interest in the CDM is not restricted to developed country anticipation of minimising the costs of compliance; developing countries view the CDM as a means for acquiring the financial assistance and technology transfers they require to implement their commitments under the *UNFCCC* while contributing to their sustainable development.

### III REQUIREMENTS FOR CDM PROJECTS

To be eligible to qualify as a CDM project activity and receive certification of emission reductions, a project activity must satisfy the criteria set out under art 12:

- the project activity must be undertaken by an Annex I Party in a developing country;
- the participation of both countries must be voluntary and approved by each country;
- the project activity must be of a type that results in emission reductions and contributes to the goal of sustainable developments by producing real, measurable and long-term benefits related to the mitigation of climate change; and
- the emission reductions must be additional to any emission reductions that would occur in the absence of the certified project activity – the requirement of 'environmental additionality'.

Significantly, unlike other flexibility mechanism projects,<sup>11</sup> emission reductions from the CDM can be generated from 1 January 2000 and banked for use in the first commitment period under the *Kyoto Protocol*. The CDM also allows the participation of corporate entities.<sup>12</sup>

CDM projects are particularly important as, like other technology transfer arrangements in international environmental agreements, they are designed to assist the flow of environmentally sound technologies into developing countries in circumstances where such flows would not otherwise occur. It will be up to the host country of the project to ensure that any project and investment for which CDM status is being pursued, is one that meets its goals of sustainable development, and which produces real long term climate change benefits. Assessing this will also involve testing the environmental additionality of a proposed project activity.<sup>13</sup>

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10 These are the 'credits' earned from CDM projects which are issued by the CDM Executive Board.

11 Joint implementation is another of the flexibility mechanisms and allows credits in the form of Emission Reduction Units ('ERUs') to be earned from emission reduction projects undertaken by one developed country in another developed country. However, as the current rules stand, ERUs can only be earned in the first *Kyoto Protocol* commitment period (2008-12) and not before.

12 See *Kyoto Protocol* art 12(9).

13 It may also involve testing for other additionality indicators such as financial additionality and technology additionality, depending on the outcome of negotiations of the CDM rules and guidelines.

#### IV THE PROJECT CYCLE

It is intended that CDM projects will be undertaken within a clear administrative framework with clear rules as to the establishment and role of the CDM Executive Board,<sup>14</sup> the types of eligible projects and the project cycle of registration, assessment and approval. Such clarity will be crucial to maximising private sector involvement in CDM projects. While the text of art 12 is necessarily brief in relation to such rules, the current negotiating texts regarding CDM projects are very detailed.<sup>15</sup> Despite lack of agreement at COP 6 in November 2000 regarding the rules for contentious issues such as sinks, supplementarity and compliance, broader consensus did appear to emerge in relation to the project cycle for the CDM.<sup>16</sup>

As the first step in the process of undertaking a CDM project, 'project participants'<sup>17</sup> will be required to complete a project design document that describes the project activity in detail, and to submit this document to an accredited operational entity for validation. The operational entity will then evaluate the project activity against the requirements of the CDM on the basis of the project design document, and make a determination as to whether, on the basis of the project design document and taking into account any public comments received, the project activity meets the eligibility, additionality and methodology requirements for validation.<sup>18</sup> At this stage, project participants will also need to provide a formal letter of approval from the designated national CDM authorities of the Parties involved, including confirmation that the project satisfies the sustainable development goals of the developing country hosting the project. If the proposed project activity is validated, the CDM Executive Board

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14 Article 12 of the *Kyoto Protocol* clearly envisages the establishment of a CDM Executive Board whose role will include formal approval of projects that are undertaken. In the absence of this Board, early projects are simply being structured along the existing CDM guidelines with the expectation that if given host country approval today, CDM Executive Board approval will be granted once the body is established. This may or may not be the case; the actual roles to be played by the CDM Executive Board and any other administrative bodies associated with it remain to be determined.

15 See the negotiating texts on art 12 of the *Kyoto Protocol* prepared by the President of COP 6: Jan Pronk, *Article 12 of the Kyoto Protocol, Note by the President*, UN Doc FCCC/CP/2000/CRP.2/Add.1 (24 November 2000) <<http://www.unfccc.int/resource/docs/cop6/crp02a01.pdf>> at 3 June 2001, and Jan Pronk, *Decisions concerning Mechanisms pursuant to Articles 6, 12 and 17 of the Kyoto Protocol*, UN Doc FCCC/CP/2001/2/Add.2 (11 June 2001) <<http://www.unfccc.int/resource/docs/cop6secpart/02a02.pdf>>; and that prepared by the UNFCCC Subsidiary Bodies: Subsidiary Body for Scientific and Technological Advice and Subsidiary Body for Implementation, *Modalities and Procedures for a Clean Development Mechanism*, UN Doc FCCC/SB/2000/CRP.20/Add.1 (18 November 2000) <<http://www.unfccc.int/resource/docs/2000/sb/crp20a01.pdf>> at 3 June 2001; as well as the informal negotiating proposals put forward by the President of COP 6: see above n 8.

16 The description of the project cycle in this article is based on the negotiating texts on art 12, with additional guidance taken from the informal negotiating proposals put forward by the President of COP 6: above n 15. No formal decisions have been taken by the Conference of the Parties in relation to these texts.

17 The term 'project participants' refers to the legal and corporate entities carrying on the CDM project, as opposed to the Parties themselves.

18 The Parties did not reach clear agreement on these more contentious requirements at COP 6.

will then register the CDM project activity. Only after such registration occurs will a project activity be eligible to be issued CERs.

Once the project activity has been validated and registered, the project participants will be required to implement a validated plan to monitor emission reductions flowing from the registered CDM project. These emission reductions will then need to be verified by an accredited independent operational entity. Once the operational entity is satisfied that the emission reductions are real, the operational entity will then complete a certification report, certifying that during the specific assessment period the project activity has achieved the additional emission reductions as verified.

The Executive Board will then issue CERs equal to the additional emission reductions as verified and contained in the certification report. Upon receiving authorisation from the Executive Board to issue CERs for a CDM project activity, the CDM Registry will issue and distribute the CERs to the national registries and accounts of the project participants and Parties specified in a distribution agreement. The CDM Registry will also be required to issue CERs amounting to the assessed share of proceeds from the CDM project activity into the account established to hold and manage the share of proceeds for administrative expenses and the developing country adaptation fund.

## **V FAST-TRACKING PROCEDURES FOR SMALL-SCALE RENEWABLES, ENERGY EFFICIENCY AND OTHER SMALL PROJECTS**

Special rules and guidelines have also been proposed to allow the 'fast-tracking' of small-scale emission reduction projects through the CDM project cycle. The fast track procedures for small scale projects are aimed at encouraging the investment in, and development of, CDM projects in developing countries that are otherwise unlikely to attract large-scale CDM projects, while the focus on renewable energy projects is aimed at prioritising these over other project types by also making them more attractive to private investors through simplified, and therefore more cost-effective, procedures.

The types of projects that are currently proposed include small-scale renewable energy production projects with a prescribed maximum output capacity,<sup>19</sup> and small-scale energy efficiency projects that are designed to reduce energy consumption by no more than a prescribed maximum.<sup>20</sup> The Executive Board will have the authority to review the definitions of these small-scale projects and to recommend measures through which such projects are to receive preferential treatment.

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19 The proposed maximum output capacities under current negotiating texts are 10, 15 or 50 megawatts: above n 15. The latest consolidated negotiating text and the informal negotiating proposals put forward by the President of COP 6 propose 15 megawatts: above n 15.

20 The proposed maximum energy consumption reductions under current negotiating texts are 1-5, 5 or 10 megawatts: above n 15. The latest consolidated negotiating text and the informal negotiating proposals put forward by the President of COP 6 propose 5 megawatts: above n 15.

Some of the areas where it is proposed that small-scale projects should receive preferential treatment during the CDM project cycle include deemed additionality and the ability to use standardised baselines, standardised crediting and simplified monitoring methodologies. In addition, small-scale projects are likely to be able to be bundled together so as to be subject to a single registration, rather than each being registered separately.

## VI CONCLUSION

If the CDM functions as it should, global emission reductions can be achieved with lower compliance costs, whilst developing countries can attract new, innovative, environmentally sound technology. In turn, such technology will place them in a better position to 'leapfrog' the greenhouse-intensive experiences of developed countries, and lead to their longer-term environmental sustainability. But without the financial and technological bridges between developed and developing countries, such as those commitments detailed in the *UNFCCC* and the CDM, any global climate change policy will struggle to succeed. Notwithstanding the fact that developing countries are exempted from shorter-term binding targets under the *Kyoto Protocol*, it cannot be disputed that their participation will be crucial in the longer-term given the projected significant rise in their emissions. Seeking the meaningful participation of developing countries now will not only enable them to fully participate in global climate change action in the future, but will assist also in decreasing the global costs of reducing greenhouse gas emissions.

Thus the focus of the current climate change debate, rather than criticising the short-term exclusion of developing countries from binding targets under the *Kyoto Protocol*, should be to build the financial resources and technology transfer bridges set out in the *UNFCCC* in order to engage developing countries and assist them in the implementation of these provisions. Even if the *Kyoto Protocol* does fall apart, it is hoped that – at the very least – Parties will recognise the importance of maintaining the CDM as a central means of global climate change abatement.