Enel-Endesa position on CDM qualitative restrictions

We are now approaching The Conference of the Parties of the UNFCCC to be held in Cancun in December. Among the key challenges for climate negotiators, the European electricity industry sees the expansion of the current role of offsets mechanisms as a key element for a global approach to curb carbon emissions. Offsets in the post-2012 framework are expected to lower overall mitigation costs and facilitate international technology transfer by encouraging financial flows from developed to developing countries.

The most promising option relies on the enhancement of the current CDM/JI, which, although requiring improvements, has proven its effectiveness in allowing for the implementation of emission reduction projects in developing countries through the mobilization of private capital. To encourage investments, however, regulatory stability and clarity over the "rules of the game" are paramount for the private sector.

We are aware that the European Commission is now working on a proposal to introduce qualitative restrictions on the use of credits from project-based mechanisms. This is already enshrined in the EU ETS Directive, and a formal proposal is expected before Cancun. The need for qualitative restrictions should be carefully assessed against the following potential risks:

- They would affect the supply of credits creating an artificial shortage in the market, in a moment in which no other alternative mechanism is yet in place or mature enough, leading to a potential increase in cost for compliance players.
- They would add additional uncertainty in the CDM/JI market as they question the validity of UNFCCC approved offset classes. The UNFCCC process has proven to be capable of properly addressing the key concerns on environmental integrity and sustainable development; setting stricter requirements would undermine the credibility of the process and the consequences should be carefully assessed under the perspective of future international climate negotiations
- They would set a dangerous precedent for all market operators: disqualifying a certain asset class would in fact pave the way to further restrictions on other asset groups in the future, thereby discouraging future investments.
- They would lead to market fragmentation, as different acceptance of CERs/ERUs under distinct jurisdictions will further undermine liquidity

and require market participants to create differentiated contracts for trading CERs/ERUs.

Given the high level of uncertainty currently associated with the future framework of international offsets (sectoral mechanisms, REDD, etc) any restriction applicable to existing projects would severely discourage investments flows in the global carbon market. Therefore, any qualitative restrictions should only be imposed on any CER/ERU asset class by ensuring that:

- Objective criteria are used to identify that asset class.
- An exhaustive definition is given, not subject to further refinements.
- No retroactive application of legislation is enacted.
- Any decisions should engage consultations with all stakeholders in a participatory way.

This is line with the position that the Council of the European Union took on this matter in its Conclusions on EU Position for the Copenhagen Climate Conference.

In trying to reach a position that preserves good market functioning as well as address the EC's desire to promote certain types of offset projects we would propose the following approach for CERs in their first crediting period:

- Qualitative restrictions should not have an impact on CERs/ERUs accrued by projects already registered at the time restrictions come in place during their 1st crediting period;
- Operators should be allowed to use for compliance during Phase 3 all CERs/ERUs issued from project activities already registered to the end of their first crediting period;
- No application of multipliers to CERs / ERUs issued from certain project activities should take place as this would increase market fragmentation.

This proposal would at the same time:

- be compatible with the CDM process;
- safeguard investors' vested rights and avoid legal and contractual problems;

- free up significant demand volumes, consistently with EC's priority to encourage certain types/technologies of offset projects, and to promote geographical diversification of CDM;
- Give enough time to work on the design of new crediting mechanisms, bridging the gap that would otherwise arise in case of abrupt application of QRs.

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