

PMR Project Implementation Status Report (ISR)

1. SUMMARY INFORMATION

Implementing Country:	Republic of Chile
Reporting Period:	From 09/05/2014 to 05/20/2015
Report Date:	05/20/2015
Implementing Agency:	Ministry of Energy
Contact Person:	Juan Pedro Searle, Sustainable Development Division, Ministry of Energy

Grant Executed By:	Recipient: Agencia de Cooperación Internacional, AGCI
Grant Effectiveness and Closing Dates:	09/05/2014 - 09/05/2017
Grant Amount (USD):	USD 3,000,000

2. OVERVIEW

The Grant became effective on September 2014; one and a half year after the PA endorsed Chile's MRP. Hence, no concrete progress can be informed at this stage regarding the technical activities and their relation to the Project's indicators (PDO and intermediary results). Nevertheless, as it is informed ahead in this report, the Coordination Team has been appointed in early May 2015, which is an important step under the MRP, since this Team will be in charge of moving the activities forward. The Work plan and TORs for each of the activities will be initiated shortly after their contracts have been signed.

3. IMPLEMENTATION REPORT BY COMPONENT

Differences between the Objectives/Activities in the Market Readiness Proposal and the Grant Agreement

Are there any important and material differences between the objectives/activities proposed in the Market Readiness Proposal and endorsed by the Partnership Assembly of the PMR and those agreed to in the Grant Agreement with the Delivery Partner and described in the Project's Results Framework?	<p><u>Yes</u>, in terms of the carbon pricing instrument chosen. This is a result of new developments in the country regarding economic instruments to tackle environmental problems.</p> <p><u>No</u>, regarding the MRV and Registry component of the MRP and the Stakeholders engagement and capacity building component.</p> <p>See explanation below.</p>
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In early April 2014—almost one year after the approval of Chile’s Market Readiness Proposal by the PA—the Administration of President Bachelet submitted to Congress draft legislation as part of its broad tax reform that includes, within the proposed green taxes, a carbon tax on large (greater than 50MW) stationary sources in the energy sector. The whole tax reform was finally passed on September 2014. Regarding green taxes (which also includes a tax on local pollutants), the Ministry of the Environment will be responsible of implementing and monitoring them. In consequence, the PMR activities will now provide support to the implementation of this carbon tax.

Although Chile has decided to implement a carbon tax as a major step in its long standing support for using economic instruments to tackle environmental related problems, the window of opportunity is still open to explore other economic instruments to tackle climate change. Although the green tax component would only enter into force in 2017, the Chilean Government expects that a great deal of analytical and preparatory work will be needed to support its implementation. Understanding the interaction (and impacts) of this carbon pricing instrument with existing policies and other carbon pricing instruments (such as an ETS) and its alignment with economic growth and with mid- to long-term mitigation and development goals —especially in the energy sector— would be crucial to support government as well as other stakeholders’ needs during this process.

Precisely, being part of the PMR community gives the country a great opportunity to explore what other instruments could be applied (either in conjunction with the carbon tax or as a second phase in this journey to reach a lower emissions development pathway) and certainly, an emissions trading system could be one of the tools that would provide more flexibility to the private sector, and as such, it will still be a major topic to be addressed under this PMR initiative. This PMR project therefore comes at a time of substantial political momentum. Using a phased approach, the project will support research and analysis as the government contemplates multiple approaches to carbon mitigation. Linking to other systems (including its regulatory, institutional and budgetary implications), the role of carbon pricing in fulfilling international climate change commitments, design options, MRV and Registry piloting, among others, will be part of the list of topics to be addressed through the PMR.

So the major change to the original MRP was the broadening of its scope (originally the focus was on ETS) and to refer now to “carbon pricing”. This change was captured in the Grant Agreement, where the main objectives of Chile’s MRP were drafted as “to provide technical assistance to the Beneficiary in the design and implementation of a Monitoring, Reporting and Verification (MRV) framework and registry, and the design and preparation of one or more carbon pricing instruments in the energy sector”. This change was also captured in the operational manual of the project, which is now referring to carbon pricing instruments that include both carbon tax and emissions trading scheme.

The PA was informed of this development during its 9th meeting held in Cologne in May 2014.

Implementation Progress by Component

A. Component 1: Regulatory, Economic and Institutional Analyses to assess the viability of one or more carbon pricing instruments for the energy sector	
Status:	Pending
Comments:	This component will be executed by a Technical Expert. The selection of this person was finalized on May 7, 2015. The contract is in process.
B. Component 2: Design and implementation of an MRV framework and registry	

Status:	Pending
Comments:	This component will be executed by a Technical Expert. The selection of this person was finalized on May 7, 2015. The contract is in process.
C. Component 3: Stakeholder engagement and communication strategy, and capacity building	
Status:	Pending
Comments:	This component will be executed by the Project Manager. The selection of this person was finalized on May 7, 2015. The contract is in process.
D. Component 4: PMR Implementation Coordination	
Status:	Ongoing The Project Coordination Team was selected in close coordination with the World Bank (i.e., Terms of Reference and selection of the project staff received the corresponding no-objection). The contracts for each Team member is being processed by the Grant's Recipient (<i>Agencia de Cooperación Internacional, AGCI</i>), with the aim of being signed by each member by the end of May 2015.
Comments:	The first coordination meeting with the Project Manager, the two technical experts for Components 1 and 2, and the Financial Assistant was held on May 18. The purpose was to explain contract details as well as specific tasks that will have to be performed by them. One of the initial tasks for all of them will be to prepare a detailed work plan during June, in order to start planning the project milestones, at least for the second semester of 2015. These work plans will be presented and discussed during a World Bank Mission, planned for July 2015.

4. PROGRESS, CHALLENGES, AND LESSONS LEARNED

<p>Important policy or regulatory developments related to the Grant's objectives and activities:</p> <p>Developments:</p> <p>At the same time when the signing of the Grant Agreement was being prepared and negotiated, the Government decided that a carbon tax would be a suitable instrument to put a price on carbon emissions coming from thermal power generation. This legislation was sent to congress on April 2014 and approved five months later (September 2014).</p> <p>As the Grant Agreement was being drafted during that same period, it was relatively simple to incorporate this new development in the respective objectives and activities described in it, since we envisaged that the MRV and Registry (core expected deliverable of the MRP), would not change as was originally thought (i.e., a system designed to register emissions and transactions of GHG from regulated entities). In doing so, the original approach of an ETS was broadened to refer now to carbon pricing instruments. By using a phased approach (starting with this carbon tax), the MRP is still looking into the future, where multiple approaches to carbon mitigation could be implemented in Chile.</p>

Challenges:

Possibly during the initial stages of the project, a potential challenge would be that of drawing the attention of stakeholders into a discussion of new carbon pricing instruments, in a situation where the country already has one and yet it needs to be implemented. The communication and engagement strategy will be key to minimize potential conflicts. In addition, the two studies that will be implemented under the (complementary) Upstream Policy Analysis initiative (both on the carbon tax and its impacts on the regulated sector and its coherence with other policies and regulations), would be relevant to support further discussions on this and other carbon pricing instruments, and probably, would ease the introduction of these issues among stakeholders.

Obviously, the transition from one carbon pricing to another will need regulatory changes but that would only be noticed/further addressed as the project develops.

Lessons learned:

At this stage, it is important to highlight that implementing countries can be subjected to major carbon pricing policy and regulatory changes while implementing their MRPs, and that those changes should be adequately reflected in and reported back to the Assembly in a timely manner. The PMR should remain as flexible as it has been, and facilitate these transitions (if, of course, they do not hinder or affect in any way the goals behind each of the MRPs, which is to support market readiness and implement carbon pricing instruments).

Important changes in the technical design or approach related to the Grant's activities:**Developments:**

As stated previously, the technical design or approach concerning the MRV and Registry System (a core non-regret outcome) remains the same as was stated in the MRP. The original functions will be kept unchanged (i.e., registry of emissions and GHG transactions). The Government is clear that this approach should serve purposes other than the MRV of a carbon tax, and so, it will be designed keeping in mind the functions of an ETS registry. For that, the current reporting system called the RETC (*Red de Emisiones y Transferencia de Contaminantes*) will be thoroughly revised and adjusted as necessary in order to nest such a GHG Registry.

Given the presence of the carbon tax, a few items have been added to the original activities under Component 1, which include the analysis of the role carbon pricing may have in supporting Chile's INDC and the regulatory, institutional and budgetary implications of linking to international systems.

Challenges:

One possible challenge would be to get the right technical and institutional design of the entire MRV system, including the registry. Choosing the right design and the proper institutional framework would be crucial. In-country visits would provide sound information and insights on how other countries or jurisdictions have made decisions on this regard. Then, the decision of what countries or jurisdictions to visit would be key.

Lessons learned:

NA

Key capacity issues (implementation, technical, financial management, procurement) related to the Grant's activities:
Developments:

After the approval of the MRP by the PA (March 2013), the Focal Point, in close coordination with the World Bank Team, embarked in a process of defining the local agency that would be in charge of receiving and managing the funds, in parallel to the drafting process of the Grant Agreement. The government decided on AGCI to be that Agency, based on its legal and technical capacity to administer funds on behalf of a third party. Even though the specific responsibilities of this Agency were captured in the Grant, as well as in the operational manual and subsidiary agreement between AGCI and the Ministry of Energy, respectively, it is appropriate to highlight here that this Agency will have to manage all the bidding processes and contracts derived from the procurement plan, apart from managing the specific accounting for the project. This means that the level of coordination, consistency and timings will be very interlinked and will require a full dedication of an expert in financial and accounting issues. Fortunately, the project conceived the hiring of such an expert, situation that has already been addressed.

Challenges:

Given the number of contracts that would need to be managed, this sole situation will imply a challenge to AGCI and to the Coordination Team. It is expected that the 3,000,000 USD grant will be spent in 2 years, rather the 3 years indicated in the Grant Agreement. This ambitious target will require close coordination among all tasks and experts. As the project implementation develops over time, corrections or adjustments will be applied accordingly.

Lessons learned:

NA

Coordination with other carbon pricing initiatives, including those funded by other donors:

Developments: The Forest Carbon Partnership facility (FCPF) project has already started in Chile. One of its objectives is to generate offsets from the LULUCF sector. We do not have or envisaged other carbon pricing initiatives for the energy sector, funded by other donors.

Challenges:

It will be interesting and at the same time, challenging, to explore the potential links of the offsetting system that is being supported through the Forestry Carbon Partnership Facility (FCPF), with the design of a carbon pricing instrument such as a future ETS for the energy sector. In addition, it would be relevant to evaluate possible new features to the carbon tax, as for instance, the consideration for regulated entities to use offsets as a flexible way of complying with the tax. This local offsetting system could provide these offsets. These are issues that might be looked at in the context of the MRP.

Lessons learned:

NA

Stakeholder engagement related to the Grant's activities:

Developments:

NA

Challenges: As previously stated, the discussion of carbon pricing options other than the tax could be counterproductive and so, potential conflicts will need to be averted by the Coordination Team and Focal Point. The stakeholder participation and engagement strategy would be essential to diminish or address any potential conflict.

Lessons learned:

NA

Other issues related to the Grant's activities

NA

5. ADDITIONAL INFORMATION

NA