



A PAY-FOR-PERFORMANCE AUCTION FACILITY FOR CLIMATE MITIGATION AND METHANE

AN INNOVATIVE RESULTS-BASED FUNDING MECHANISM

PARTNERSHIP FOR MARKET READINESS PA 8

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Carbon Finance
AT THE WORLD BANK

2012 G8 Request for Methane Finance Study Group



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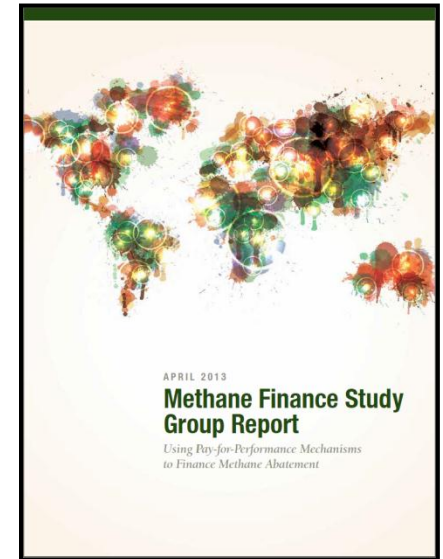
Fact Sheet: G-8 Action on Energy and Climate Change

At the Camp David Summit, G-8 Leaders recognized that the development of and universal access to environmentally safe, sustainable, secure, and affordable sources of energy is essential to global economic growth and to their overall efforts to address climate change. As such, they identified several actions for the G-8 to take together:

- Commission the World Bank to prepare a report on ways to integrate reduction of near-term climate pollution into their activities and ask the World Bank to bring together experts from interested countries to evaluate new approaches to financing projects to reduce methane, including through pay-for-performance mechanisms.

A “quick-win” proposal

- 1,200 “stranded” methane abatement projects in developing countries, representing 850 MtCO₂e in emission reductions between 2013 and 2020
- The projects and the infrastructure to verify their emission reductions are here - the incentive is missing
- Facility would support these projects by guaranteeing them a floor price for their future emission reductions
- This would be achieved by auctioning “put options”, i.e. a contract that gives the holder the right, but not the obligation, to sell its ERs to the facility at a given (“strike”) price
- Not a carbon market support facility but a climate finance pilot - if successful this pilot is easy to scale up and expand to other sectors.



A Methane Abatement Facility: Step-by-step overview

Steps to use CO₂e to Pay-for-Performance for Methane

Develop selection criteria and call for proposals



Pool donor resources to purchase tons of CO₂e from methane projects



List of criteria
E.g. country, technology, measurement standards, co-benefits etc.



Implement projects



Contract in hard currency helps implementer overcome financial and other barriers



Select and contract for methane reduction



Project implementers bid to purchase put option contracts from facility



Use auction to determine the winning bids



Sign put option contracts with winning bidders that permit the contracts to be transferred/sold

Verify & Pay-for-Performance



Monitor and verify tCO₂e using established GHG accounting standards



Should the market price be below the put option strike price contract holders exercise options and facility purchases tCO₂e

Attractive features of tradable put options and auctions

Attractive features of tradable put options

- **Tradability**
If an option holder cannot profitably deliver reductions, it would have an incentive to sell the option to another project owner who can abate methane at the same cost or more cheaply
- **Maximize Emission Reductions**
Owing to the tradability of the options the facility maximizes the likelihood of achieving emission reductions as contracts are economically redistributed from failing projects to successful ones
- **Recycling funds**
Should the options not be exercised b/c of an increase in carbon market prices, the contributors could recycle the funds to other climate finance projects

Attractive features of auctions

- **Ensures value for money**
Bidders with the lowest expected cost to deliver emission reductions will win, allowing the facility to catalyze the greatest number of reductions per dollar allocated
- **Price discovery**
Participants do not need to know the precise cost of emission reductions a priori; instead bidders bid based on their projected costs - thus “discovering” the minimum subsidy needed

Facility Design and Status Update

Issues being designed

- Auctions will encompass multiple countries to foster competition
- Auctions will be sector specific (starting with targeted methane sectors)
- Facility will consider opening to non-methane sectors in subsequent auction rounds
- Emission reductions purchased by facility will be retired and/or not resold into carbon market
- Facility will rely on rules and methodologies of existing carbon standards (CDM, VCS, CAR)
- Facility will test direct and reverse auction

Current status

- Facility proposal presented and discussed at series of recent climate meetings, including Ministerial meetings of the Climate and Clean Air Coalition
- Several potential donors have come forward to express interest to contribute
- The fund is targeting \$100 million
- Public launch expected in 2014; first auction round by end-2014
- Intended to inform future scaled-up flows of pay-for-performance climate finance, including through the Green Climate Fund

Thank you

Carbon Finance at the World Bank

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