

# Pilot Auction Facility for Methane and Climate Change Mitigation

The Pilot Auction Facility for Methane and Climate Change Mitigation (PAF) provides private investors with a financial incentive to fund projects that reduce greenhouse gas emissions. It uses existing carbon and capital market tools to pilot a model that is easy to scale up and expand to other sectors.

## A Pilot Auction to Catalyze Climate Finance

The PAF is an innovative instrument developed by the World Bank Group that supports projects which reduce greenhouse gas emissions by guaranteeing a floor price for future carbon credits. This is achieved by auctioning “put options”, i.e. a contract that gives the holders the right, but not the obligation, to sell their carbon credits to the facility at a pre-determined price. The put options will be auctioned in order to maximize cost effectiveness. Donors will provide backstop funding to pay the options should they be exercised. The emission reductions will be retired and not used as offsets for international compliance obligations.

The establishment of the facility was a recommendation of the 2013 Methane Finance Study Group to the G8 and its development has been discussed and supported by the partners of the Climate and Clean Air Coalition. The facility is open to contributions from governments, foundations and the private sector. The PAF has a total funding target of \$100 million.

## Quick Win

Technologies that reduce methane emissions are relatively inexpensive. But with the plunge in carbon prices since 2011, carbon revenues are not sufficient to make projects that use such technologies viable. As a result, about 1,200 methane-reduction projects have been identified in 2012 as dormant or incomplete. Brazil, India, Indonesia, Malaysia, Mexico and Thailand host most of these projects.

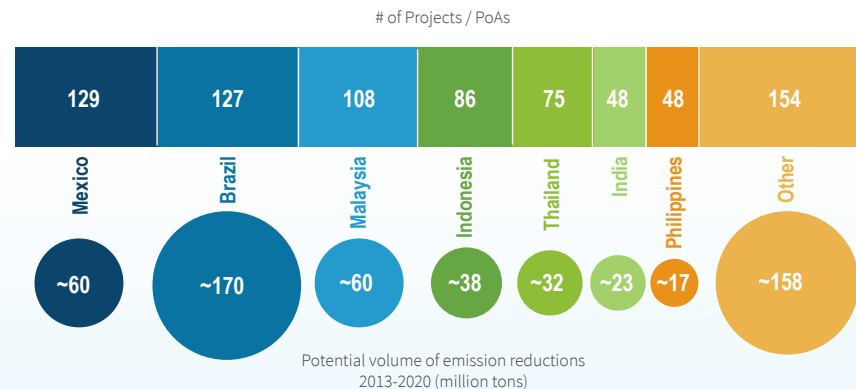
The additional revenue required to unlock these investments is often small. The various methane sectors could deliver as much as 8,200 million tons of emission reductions in developing countries by 2020 at less than \$10 per ton in incremental cost financing. The PAF will deliver quick impact by initially targeting methane reducing projects at risk of being decommissioned.

## Why Start with Methane?

By focusing initially on methane, a powerful short-lived climate pollutant, the facility will contribute to near-term climate change mitigation. Methane emissions caused by human activities are the second largest driver of climate change after carbon dioxide. Abating methane emissions will generate a large range of global and local air, health, and agricultural benefits. Methane is a precursor to tropospheric ozone, an air pollutant that is ubiquitous in the modern urban and rural environment. At high concentrations, ozone is harmful both to plants and humans, leading to crop loss, asthma and heart attacks.

Also, projects that reduce methane can deliver less pollution run-off, improved municipal solid waste management and wastewater collection, increased mine and landfill safety, and clean power generation.

## Project Potential



Since the lowest-cost opportunities are likely to be mostly found in middle-income economies, the PAF plans to allocate dedicated resources that will exclusively incentivize mitigation in lower-income countries. Data suggests 95 projects in low-income countries, representing ~30 million tons of potential reductions from methane in 32 countries.

## Scale-up

Green options piloted by the PAF test a new approach with the potential for significant scale-up. The PAF provides a blueprint for potential replication in the future, by the Green Climate Fund or others, to incentivize new greenhouse gas mitigation projects. In future phases, the PAF put options can also target other sectors and technologies.

## Step-by-Step Process

- Select and contract for emission reductions:**
  - Publicize auctions
  - Execute auction to determine the winning bids
  - Sign put option contracts with the winning bidders
- Achieve emission reductions:**
  - Put option contract in hard currency helps implementer overcome financial and other barriers
- Verify & pay-for-performance:**
  - Monitor and verify emission reductions using established GHG accounting standards
  - Should the market price be below the put option strike price, contract holders exercise options and the PAF purchases the carbon credits