

**International Rivers Comments on the CDM Project Design Document (PDD) for
La Yesca Large Hydroelectric Dam (Mexico)**

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La Yesca is a business-as-usual dam project that has already secured almost a billion dollars in project financing, is nearing the final stages of construction, and in no way requires – and has never been dependent upon – CDM income to be completed. It is therefore non-additional. It should not be validated for the CDM.

The project developer, the public utility CFE, has clearly long been aware of the possibility of obtaining CDM income for La Yesca and its other low carbon projects. As the PDD states, this potential income stream is mentioned in various project documents. However there is no evidence whatsoever that the potential for CDM income was key in securing financing for La Yesca or in CFE's decision to implement the project.

Non-Additionality

1) Investment Analysis

The PDD states that La Yesca is much less economically attractive than a natural gas combined cycle plant. No evidence is presented however showing that CDM income would come anywhere close to overcoming the large difference in the levelized costs between La Yesca and an NGCC plant. It is in fact extremely unlikely that CDM income would come near to closing this gap given that the PDD shows the levelized cost of electricity from La Yesca as being 60% more expensive than a NGCC and that CER income (of around \$10m/yr on a \$700m investment) would increase the IRR of Yesca by only 0.5%.

In any case decisions to build large dams are regularly made in Mexico and elsewhere despite them being economically unattractive. Reasons include the vested interests and political power of large construction and engineering companies and the bureaucratic power of dam-building interests within agencies such as CFE. To quote from the World Bank-sponsored World Commission on Dams:

“The decision to build a dam is influenced by many variables beyond immediate technical considerations. As a development choice, the selection of large dams often served as a focal point for the interests and aspirations of politicians, centralised government agencies, international aid donors and the dam-building industry, and did not provide for a comprehensive evaluation of available alternatives . . . In some cases, the opportunity for corruption provided by dams as large-scale infrastructure projects further distorted decision-making.”

It is not credible to believe that such pressures were not at play in the decision on La Yesca – and far more influential than any potential financial benefits from CER income - especially given the project’s extremely high costs relative to alternatives.

The cost difference between a NGCC plant and La Yesca may in fact be much greater than is claimed in the PDD. The PDD claims the investment cost of La Yesca as being \$701m. Yet the website of Vinson & Elkins, the law firm that closed the financing deal, claims that La Yesca raised \$990m in project finance in 2007 (a transaction that was named Project Finance International’s 2007 Power Deal of the Year (Americas)).¹ This greater cost for La Yesca would reduce to even less significance the potential income from CER sales in the decisions to build and finance the dam.

Furthermore La Yesca clearly is a project of major political importance. President Calderon inaugurated construction at the dam in January 2008. He stated that

“la Yesca es el proyecto de infraestructura hidroeléctrica más importante de su gobierno y que contribuirá a poner a México a la vanguardia de América Latina en materia de infraestructura. Afirmó que quiere ser el presidente de la infraestructura, con el objetivo de que México construya las obras que son necesarias para propiciar el desarrollo económico y promover la generación de empleos. Agregó que el proyecto hidroeléctrico La Yesca será un importante generador de electricidad a partir de una fuente renovable, que contribuye al cuidado del medio ambiente, a la vez de que su construcción será trascendente en la generación de empleos para los habitantes de la región, lo que redundará en una significativa derrama económica que beneficiará a la gente. Precisó que La Yesca representará una inversión de 8 mil millones de pesos, cuyo desarrollo permitirá generar más electricidad de manera competitiva y con mayor calidad en favor del aparato productivo nacional. La construcción de La Yesca viene acompañada de diversos proyectos sociales en materia de salud, educación, comunicaciones y reforestación que beneficiarán a los habitantes de estas comunidades.”²

Other dignitaries made similar comments at the ceremony:

“Por su parte, la Secretaria de Energía, Georgina Kessel, indicó que energía e infraestructura son piezas fundamentales para alcanzar el desarrollo que México requiere. Con La Yesca, puntualizó, el Gobierno de México lanza un mensaje importante de apoyo para el desarrollo de obras conjuntas con capital público y privado, que generen empleos bien remunerados. A su vez, el Director General de la Comisión Federal de Electricidad (CFE), Alfredo Elías, señaló que La Yesca es parte integral del enorme esfuerzo de construcción de infraestructura que ha emprendido el gobierno del Presidente Calderón, y que además muestra que en el sector energético es posible la unión de esfuerzos de los sectores público y privado. Con este proyecto, aseguró, México vuelve a pensar en grande para desarrollar importantes obras de clase mundial.”

¹ http://www.velaw.com/practices/practice_detail.aspx?id=18076&libID=18210#hydroelectric

² <http://saladeprensa.cfe.gob.mx/boletin/index.alia?docID=7993>

Given the political and economic importance of the project it is not credible that this almost billion dollar investment was made only because of the possibility of CDM income.

2) Common Practice Analysis

The PDD claims that La Yesca's additionality is also shown because "there are no similar hydroelectric power plants operating in Mexico." Obviously there are numerous very large hydro power plants operating in Mexico. The PDD itself lists 16 plants with a capacity of 100 MW or greater commissioned between 1959 and 2007. But the PDD claims that La Yesca is different as its construction started after the issuance of a 12% "social IRR" benchmark by the Government of Mexico in 2003.

But there is no evidence to suggest that the 12% benchmark has provided any significant barrier to the approval of new hydro projects. And indeed La Yesca is not the only hydro project of its type operating in Mexico as it is not due to start operation until 2012. CFE in fact intends to construct several other large hydro projects in the coming years: La Yesca is just one of six scheduled to be completed between 2012 and 2017 according to a September 2009 CFE Powerpoint presentation.³

It is significant that this powerpoint emphasizes the expense and complexity of applying for the CDM and the significant risks that projects will not get CDM registration. Barbara Haya's UC Berkeley PhD dissertation calculates that the combined impact of validation, registration, CER delivery and post-2012 risk reduces the value of predicted CERs by 52%.⁴ Project financiers and legal advisors are well aware of these risks. As Haya and other observers have shown, these risks mean that developers of projects like La Yesca ensure that their projects are non-additional (i.e. economically/financially and/or politically viable without CDM income) before reaching financial closure and starting construction.

In conclusion, this is a non-additional project that has received significant political support from the Mexican government and is not, and has never been, dependent on receiving income from the CDM.



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³ <http://www.ai.org.mx/.../Fuentes%20alternas%20de%20generacion%20electrica.pdf>

⁴ See Barbara Haya (2010) "Carbon Offsetting: An Efficient Way to Reduce Emissions or to Avoid Reducing Emissions?" p26. <http://bhaya.berkeley.edu/docs/HayaDissertation.pdf>

