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EXECUTIVE COMMITTEE OF
THE MULTILATERAL FUND FOR THE
IMPLEMENTATION OF THE MONTREAL PROTOCOL
Sixty-sixth Meeting
Montreal, 16-20 April 2012

REPORT OF THE SUB-GROUP ON THE PRODUCTION SECTOR

1. The Production Sector Sub-group was reconstituted at the 66th meeting of the Executive Committee. The Sub-group consisted of Argentina, Canada, China, Cuba, Japan, Jordan, the United Kingdom of Great Britain and Northern Ireland and the United States of America. Representatives of UNEP, UNIDO and the World Bank were also present as observers. Canada was the convener.

Agenda item 1: Adoption of the agenda

2. The Sub-group adopted the draft agenda as contained in Annex I.

Agenda item 2: Organization of work

3. The Meeting agreed to address the agenda as presented.

Agenda item 3: Implementation of decision 60/47 on the verification report on China's 2010 CFC production

4. The representative of the Secretariat introduced document UNEP/OzL.Pro/ExCom/66/SGP/2, stating that, as requested by the Executive Committee at its 65th meeting, the Secretariat had consulted with the World Bank to assess whether all the requirements of decision 60/47 had been met with respect to the information provided in the verification report on China's 2010 CFC production. The Bank had provided explanations regarding reporting and verification systems and the verification by the auditors of the information required in sub-paragraphs (b)(i)-(iii) and (b)(vi)-(ix) of the decision. It had also explained the discrepancy between the planned sales of the plant and the actual purchase of domestic MDI manufacturers and stated that the 2010 CFC production could not be considered as excessive as the amount was in line with the decision of the meeting of the Parties.

5. The Sub-group recommended that the Executive Committee take note of the verification report on the 2010 CFC production in China and the report on the implementation of decision 60/47.

Agenda item 4: Modification of China's CFC production sector phase-out plan to permit exemptions for the production of CFCs for essential uses approved for other Parties for 2012 (decision 65/49(b))

6. The representative of the Secretariat introduced document UNEP/OzL.Pro/ExCom/66/SGP/3, recalling that it was intended to assist the Executive Committee in assessing whether to allow 2012 CFC production in China for export of pharmaceutical-grade CFCs for essential uses of other countries. The document stated that the Russian Federation was seeking approval from the Executive Committee to source pharmaceutical-grade CFCs from China for its 2012 MDI production. The Government of China had confirmed that new production was needed to supply CFCs to the Russian Federation, as China needed its domestic stocks of pharmaceutical-grade CFCs for its essential use exemption needs.

7. In response to questions about the progress being made in introducing alternatives to CFCs in the manufacture of MDIs in the Russian Federation, the representative of the Secretariat informed the Sub-group that preparation of the GEF project to convert to non-CFC MDIs was practically finished. Implementation was due to start in 2012 and to be completed by the second half of 2013. The Government of the Russian Federation would submit a nomination for an essential use exemption for 2013 for the transition period. There were no more stocks available in the Russian Federation. The Russian Federation had traditionally sourced its pharmaceutical-grade CFCs from China because imports from other countries had required greater treatment upon receipt.

8. Given that decision 60/47 allowed the production for export of pharmaceutical-grade CFCs for the essential uses of other countries in 2010 only, there was a request for clarification regarding the source of the Russian Federation's pharmaceutical-grade CFCs in 2011. The representative of China stated that his country had exported pharmaceutical-grade CFCs to the Russian Federation; the amounts had been taken from his country's 2011 stockpiles.

9. There was some concern that the recommendation made by the Secretariat in document UNEP/OzL.Pro/ExCom/66/SGP/3 was too broad as it referred to the possibility of allowing 2012 CFC production in China for export of pharmaceutical-grade CFCs for essential uses of "other countries" rather than specifically to the Russian Federation. It was clarified that, as per decision XXIII/2, three countries other than the Russian Federation that had received essential-use authorizations for CFCs for MDIs for 2012.

10. The representative of China suggested that, given the Russian Federation was due to phase-out CFC use in the manufacture of MDIs in 2013, his country should be authorized to meet the Russian Federation's needs in that year too. Other members of the group pointed out that the Russian Federation had yet to submit an essential use nomination for 2013 and thus there was no corresponding decision by the meeting of the Parties authorizing them act.

11. One member stated his understanding that it was not possible to produce pharmaceutical-grade CFCs without also producing non-pharmaceutical grade CFCs. He therefore requested more information on the later be provided in China's verification report for 2012.

12. The Sub-group on the Production Sector recommended that the Executive Committee decide:

- (a) To modify the production sector Agreement for China to allow the production for export of pharmaceutical-grade CFCs in 2012, with an annual review, for purposes of meeting the 2012 essential use exemption for metered-dose inhalers (MDIs) authorized by the Parties in decision XXIII/2 for the other countries, provided the exporting country had reporting and verification systems in place and that the reporting and verification systems collected and reported on the following information:
 - (i) Documents from MDI manufacturers ordering pharmaceutical-grade CFCs;
 - (ii) Approvals from importing country governments for purchasing essential use pharmaceutical-grade CFCs;
 - (iii) Approvals received from governments of producing countries that order and the essential production authorized;
 - (iv) Raw materials consumed for production run;
 - (v) Amount of pharmaceutical-grade CFC produced;
 - (vi) Amount of non-pharmaceutical-grade CFC produced;
 - (vii) Documentation (transport, storage, disposal) verifying that the amount of non-pharmaceutical CFCs had been destroyed;
 - (viii) Export documentation from producers;
 - (ix) Invoices from MDI manufacturers; and
 - (x) Audit reports verifying all the above;

- (b) To request the World Bank, as the implementing agency for the CFC production phase-out plans for China to provide its services in carrying out the verification/audit and to submit reports to the Executive Committee on behalf of China on the understanding that:
 - (i) The World Bank verified that the producer had access to destroy the excess CFC produced using a destruction technique approved by the Parties;
 - (ii) The cost of verification would be approved in advance of the audit by the Executive Committee;
- (c) That:
 - (i) The Fund Secretariat, on behalf of the Executive Committee, would seek confirmation from the importing country of the actual quantities imported by that country;
 - (ii) The producing country agreed to limit the production of non-pharmaceutical specification grade CFCs to the extent possible and pay for their destruction; and
 - (iii) The Executive Committee would consider application of the penalty clause to any CFC production determined as being excessive by the verification reports.

Agenda item 5: Draft report of the Technical Audit of the HCFC Production Sector in China

13. The representative of the Secretariat introduced the draft report of the Technical Audit of the HCFC Production Sector in China. In his presentation, he outlined the Fund Secretariat's concerns relating to the draft report. As agreed with China, the World Bank had been provided a copy of the draft final report for its review and use in connection with the preparation of the HCFC Production Sector Plan. A peer review had been undertaken to address the apparent inconsistencies in the data noted in the Secretariat's initial review and to ensure that data provided in the technical audit were within the range of industry standards.

14. The Secretariat had provided the consultancy firm that had conducted the technical audit with detailed comments on the draft final report, the World Bank's comments and the peer review. Following a conversation with the consultancy firm, the Secretariat had concluded that the consultant had collected the information provided by the plants without fully vetting the data. The report could be used as a data collection effort rather than as a technical audit. The Secretariat had recommended to UNON that it should end the contract by mutual agreement on the understanding that the firm would provide the Fund Secretariat with all the data collected as part of the contract and satisfactorily answer all outstanding questions on the draft final report and that payment for the final report would be withheld. The UNON Contracts Office had agreed that, in light of the above, the Secretariat could discuss completing the contract with the firm that had provided the second lowest tender. That firm had stated that it was prepared to take the data collected by the first firm, the comments provided by the Secretariat and the peer reviewer and to complete the technical audit for presentation to the 67th meeting of the Executive Committee assuming that contractual arrangements were made in a timely manner.

15. In the ensuing discussion, members of the group said that they appreciated that the Secretariat had conducted the peer review and that it had brought the issue to the attention of the sub-group so soon. The presentation had raised a number of issues, such as: whether the data obtained by the first consultant was sufficient for the second consultant to conduct the kind of analysis required by the terms of reference; whether the deadline of submission to the 67th meeting gave the consultant sufficient time to prepare the report; whether more representative, 2011 data could be collected for use in the audit; what the cost

implications of the proposed way forward were; whether the methodology was being called into question along with the data; and whether, given the incomplete data, the report had been used by the World Bank and the Government of China to prepare the HCFC phase-out sector plan.

16. The representative of the Secretariat explained that collection of 2011 data had not been part of the original terms of reference. If 2011 data collection were to be required, a new call to tender would have to be issued with the related delays that that would entail. UNON was willing to expedite the process of the second lowest bidder of the initial tender taking over the end of the project and the consultant had stated on the basis of a preliminary, telephone conversation with the representative of the Secretariat that, he was confident that he could deal with at least 70% of the production sector with the size of the contract on offer; he would also have all the raw data at his disposal, would have the advantage of having the problematic areas already known and, in revisiting the data, may also be able to collect some 2011 data. Regarding, the overall cost of the process, the total payment to the two firms (US \$276,000) would be less than the second lowest original bid (US \$450,000).

17. The representative of the World Bank explained that, in producing the HCFC sector plan for China, his implementing agency and the Government of China had followed the same procedure as when preparing the CFC production phase-out plan, using the draft technical audit as a frame and using the compensation methodology that they had used for CFC phase-out. They had complemented the data in the audit with additional data, including from 2011, and verified it independently. Moreover, their knowledge of the industry and sector meant that they could find and resolve discrepancies more easily. The representative of China said that his country and the World Bank had worked hard on the HCFC sector plan and hoped that it would be considered by the Executive Committee regardless of the status of the final report on the technical audit.

18. The Sub-group on the Production Sector:

- (a) Took note of the draft final report, the peer review and the presentation by the Fund Secretariat on the technical audit of China's HCFC production sector;
- (b) Recommended that the Executive Committee:
 - (i) Take note that the Fund Secretariat intended to:
 - a. Request UNON to end the contract with the consultant contracted for the technical audit, by mutual agreement, ensuring payment for the work done to date, on the understanding that the consultant would provide to the Fund Secretariat all of the data collected as part of the contract and satisfactorily answer all outstanding questions on the draft final report;
 - b. Pursue completion of the technical audit with the next lowest price bidder, enabling the new consultant to submit the final technical audit to the Committee at its 67th meeting;
 - (ii) Note that the delayed submission of the final technical audit report would not prevent the Executive Committee from considering the project proposal for China;

- (iii) Request the members of the Production Sector Sub-group to submit comments relating to the final report to the Secretariat by 30 April 2012, on the understanding that any further work on the technical audit would, to the extent possible, address issues raised in their written or oral comments, as well as those made by the Secretariat, the peer reviewer and the World Bank, to the level of individual plants;
- (iv) Invite, through the Government of China, the plants to provide data that they had not provided to the original consultant, including on:
 - a. The book value for the facility relating directly to production of HCFCs for use in assessing residual plant value;
 - b. Trading price data for carbon emission reductions;
 - c. Incinerator costs; and
- (v) Request the Secretariat to review, for consideration at the 67th meeting, the project proposal for HCFC phase-out in the production sector in China, taking into account any available information from the technical audit as well as any other relevant sources of information.

Agenda item 6: HCFC production sector guidelines

19. Owing to lack of time, HCFC production sector guidelines were not discussed.

Agenda item 7: Other matters

20. The representative of China made a presentation on his country's HCFC production sector plan, giving members of the Sub-group to make comments and ask questions.

Annex I

DRAFT AGENDA

1. Adoption of the agenda.
2. Organization of work.
3. Implementation of decision 60/47 on the verification report on China's 2010 CFC production.
4. Modification of China's CFC production sector phase-out plan to permit exemptions for the production of CFCs for essential uses approved for other Parties for 2012 (decision 65/49(b)).
5. Draft report of the Technical Audit of the HCFC Production Sector in China.
6. HCFC production sector guidelines.
7. Other matters.
8. Adoption of the report.
9. Closure.
