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EXECUTIVE COMMITTEE OF
THE MULTILATERAL FUND FOR THE
IMPLEMENTATION OF THE MONTREAL PROTOCOL
Forty-seventh Meeting
Montreal, 21-25 November 2005

REPORT OF THE SUBGROUP ON THE PRODUCTION SECTOR

1. The Sub-Group of the Production Sector was convened by Canada, Chair of the Subgroup, during the 47th meeting of the Executive Committee and was attended by Brazil, Japan, the Syrian Arab Republic, Thailand, the United Kingdom of Great Britain and Northern Ireland, the United States of America and Zambia. Austria and The former Yugoslav Republic of Macedonia also participated as a result of the decision of the Executive Committee to expand the membership at the 47th Meeting. Representatives of the World Bank and UNIDO attended as observers.

2. The meeting was first briefed by the Chief Officer of the Secretariat on the 3 projects which had been submitted to the Subgroup, namely:

- (a) Sector plan for phase-out of ODS process agent applications (Phase II) and corresponding CTC production in China
- (b) Sector plan for methyl bromide production sector in China
- (c) Sector plan for ODS production sector in Romania

3. The Secretariat had reviewed these projects and formulated its recommendations in light of the policies of the Executive Committee regarding funding of ODS production phase out and the findings of the technical audits, where applicable. The Chief Officer also informed that Mr. Wakim, President of Wakim Consulting, had been invited to assist the deliberations of the Subgroup, if needed, since he conducted the technical audits for the Romanian ODS production sector and the China methyl bromide production sector.

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4. The Subgroup held several sessions at lunch time and in the evenings during the week of the Executive Committee meeting at which clarifications were sought from the Implementing Agencies and the Secretariat regarding the three projects.

5. The Subgroup had an extensive discussion on the project proposal of Romania to phase out the production capacities of CFC's, CTC, methyl bromide and TCA, especially with regard to the baseline level of CTC production for the calculation of compensation for closing down the production capacity. The Subgroup finally recommended that the Executive Committee approve a total of US\$ 6.3 million for closing down the production capacities for all the four ODS. The funding included expanding the CTC incineration capacity at the CTC plant to ensure the elimination of the entire CTC production in Romania including the CTC co-production.

6. The Subgroup reviewed the project proposal for phasing out the production of methyl bromide for controlled applications in China and had an extensive exchange of opinion on such issues as the number of years of the remaining life of the methyl bromide plants and the projected growth rate of methyl bromide production and consumption in China. The Subgroup recommended that the Executive Committee approve a total of US\$ 9,79 million to assist China in eliminating methyl bromide production for controlled uses according to the Montreal Protocol schedule.

7. The Sub-group had an extensive discussion on Phase II of the China CTC sector plan and tried to clarify the following issues related to:

- (a) the significant variance in the level of CTC being absorbed by the non-ODS chemicals between the original projection in the submission and the revised projection provided right before the 47th Meeting,
- (b) the implications of this variance on the amount of CTC for incineration.
- (c) the proposed cost of such applications as CPP/CEVA and MIC on the process agent part of the project.

8. The Subgroup finally reached a consensus on the level of funding for the China CTC Sector Plan (Phase II) at US\$46.5 million dollars.

9. As a result the Subgroup succeeded in completing its review of the three projects which were submitted for its consideration and wished to recommend that the Executive Committee:

- (a) Approves the Agreement for the Romania ODS production sector at a total level of funding of US\$ 6.3 million in principle, as contained in Annex I to this document, and the first tranche at US\$ 3,200,000.00 plus the support cost of US\$ 240,000.00 for UNIDO, with the understanding that the funding would eliminate the entire CTC production capacity including the capacity for CTC co-production.
- (b) Approves the Agreement for phasing out the methyl bromide production for controlled uses in China at a total level of funding of US\$ 9.79 million in

principle, as contained in Annex II to this document, and the first tranche at US\$3,000,000 plus the support cost of US\$225,000 for UNIDO.

- (c) Approves in principle the Sector Plan for Phase-out of ODS Process Agent Applications (Phase II) and Corresponding CTC Production in China at a total level of funding of US \$46,5 million plus agency support costs of US \$3,487,500 for the World Bank with the following provisos:
- (i) That approval was without prejudice to determination by the Parties of maximum residual levels of emissions for process agent applications by Article 5 Parties;
 - (ii) That China would reduce the residual emissions from the process agent applications for production of CSM, CPP and CEVA addressed in the Phase I and Phase II CTC sector plans to levels that might be agreed in future by the Parties without requesting additional assistance from the Multilateral Fund;
 - (iii) If, during the course of implementation of the Phase II CTC sector plan, or at any time thereafter, China discovers applications, tonnes of CTC, and/or uses, (including new process agent categories) of CTC not otherwise explicitly covered in the Phase II CTC phase-out sector plan, China commits to phase out these uses in a manner consistent with the phase out schedule included in the Agreement (to be submitted to the 48th meeting) at no additional cost to the Multilateral Fund;
 - (iv) China will report to the Ozone Secretariat any CTC applications additional to those addressed by this project as soon as they become known to the Government of China;
 - (v) Disposal of CTC by China will be undertaken in accordance with standards cited in applicable international convention.
- (d) To approve funding of US \$ 15 million plus support costs of US \$1,125 million for the World Bank for the first tranche of the project;
- (e) To note that the proposed funding of the second tranche would be worked out between the Secretariat and the World Bank and reflected in the draft Agreement to be submitted to the 48th Meeting.
- (f) To request the World Bank to submit a final draft agreement for the project to the 48th Meeting together with an annual implementation plan for 2006.

Annex I**DRAFT AGREEMENT FOR THE ROMANIA ODS PRODUCTION SECTOR**

1. The Executive Committee at its 47th Meeting decided to approve in principle a total of US \$ 6,300,000 in funding for the phased reduction and closure of the entire ODS production capacity in Romania consisting of 19,800 ODP tonnes of CTC, 90 ODP tonnes of Methyl Bromide and 4,750 ODP tonnes of CFC.

2. This is the total funding that would be available to the Government of Romania from the Multilateral Fund for the total permanent closure of all capacities for the production of the controlled substances in Group I Annex A and Group I Annex B (CFCs), Group II (carbon tetrachloride) and Group I Annex E (methyl bromide), dismantling of Methyl Bromide and CFC production facilities and/or development of capacity to produce alternatives to these ODSs.

3. The agreed level of funding would be paid out in instalments in the exact amounts specified in Table 1, and on the basis of the following understanding:

- (a) By this approval, the Government of Romania agrees that in exchange for the funding level specified in Table 1, it will reduce its total Group I Annex A and Group I Annex B (CFCs), Group II (carbon tetrachloride) and Group I Annex E (methyl bromide) production in accordance with the maximum allowable production in the same table:

Table 1

Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
Max. annual allowable Production of CFC (ODP tonnes)	0.0	0.0	0.0	0.0	0.0	0.0						
Max. annual allowable Production of CTC for controlled uses* (ODP tonnes)	170.0	170.0	170.0	0.0	0.0	0.0						
Max. annual allowable Production of methyl Bromide (ODP tonnes)	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Max. annual allowable Production of TCA (ODP tonnes)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
TOTAL MLF Grant (US\$'000)	3,440	968	1,075	1,290	0	0	0	0	0	0	0	6,773
Project cost (US\$ '000)	3,200	900	1,000	1,200	0	0	0	0	0	0	0	6,300
Agency fees (US\$ '000)	240	67.5	75	90	0	0	0	0	0	0	0	472.5

* - except for the uses exempted by a Decision of the Parties to Montreal Protocol

The Executive Committee has also agreed in principle that it will provide funds on the basis of annual programmes. Payments noted in this paragraph (other than the initial tranche for 2005) are conditioned upon completion of agreed production decreases noted in Table 1 being independently verified and maintained and the Government of Romania meeting the other requirements of this agreement.

The funds are to be approved at the second meeting each year, upon the submission by UNIDO and acceptance by the Executive Committee of the verification of the reduction target in the preceding year specified in Table 1, with the exception of the first tranche, which will be released upon approval of this agreement.

- (b) The Government of Romania agrees to ensure accurate monitoring of the phase out, and to report regularly, consistent with their obligations under the Protocol and this agreement. The Government of Romania also agrees to allow for independent technical audits administered by the implementing agency, and in addition, as may be directed by the Executive Committee to verify annual ODS production levels agreed in Table 1 and plant dismantling and/or retrofitting or destruction.
- (c) The Executive Committee wishes to provide to the Government of Romania with maximum flexibility in using the agreed funds to meet the reduction requirements agreed in Table 1. Accordingly, while Romania's country programme, sector strategy or other ancillary production related documentation discussed during the preparation of this agreement may have included estimates of specific funds that were thought to be needed for specific items, the Executive Committee is of the understanding that during implementation, as long as it is consistent with this agreement and the mode of implementation included in the Romania project proposal, the funds provided to the Government of Romania pursuant to this agreement may be used in any manner that the Government of Romania believes will achieve the smoothest ODS production phase out possible.
- (d) The Government of Romania agrees that the funds being agreed in principle by the Executive Committee at its 47th Meeting for complete closure of its ODS production capacity, is the total funding that will be available to it to enable its full compliance with the ODS production phase out requirements of the Montreal Protocol, and that no additional Multilateral Fund resources will be forthcoming for related activities including the development of infrastructure for the production of alternatives, the import of alternatives or the eventual closure of any HCFC facilities that use existing CFC infrastructure. It is also understood that aside from the agency fee referred to in paragraph (f) below and reflected in Table 1, the Government of Romania and the Multilateral Fund and its Implementing Agency will neither provide nor request further Multilateral Fund related funding for the accomplishment of the total phase out of ODS production in accordance with the schedule noted above and the terms of the strategy being approved. This includes but is not limited to funding for employee compensation and all technical assistance including training.

- (e) The Government of Romania understands that if the Executive Committee meets its obligations under this agreement, but the Government of Romania does not meet the reduction requirements outlined in paragraph (a), and the other requirements outlined in this document, the implementing agency and Multilateral Fund will withhold funding for the subsequent tranche of funding outlined in Table 1 until such time as the required reduction has been met or the required dismantling has been recorded. In addition, the Government of Romania understands that the Multilateral Fund will reduce the subsequent tranche and therefore, total funding for the ODS production closure on the basis of US \$1,000 per ODP tonne of reductions not achieved in any year of this agreement. It is clearly understood that the fulfilment of this agreement depends on satisfactory performance of its obligations by both the Government of Romania and the Executive Committee.
- (f) UNIDO has agreed to be the implementing agency for this project. The agency fee for the project will be at a fee of 7.5% of project costs, and released together with the annual tranches. As the implementing agency during that time period, UNIDO agrees to be responsible for:
- (i) Ensuring/providing independent verification to the Executive Committee that the phase out targets and associated activities have been met;
 - (ii) Ensuring that technical reviews arranged by UNIDO are undertaken by appropriate independent technical experts;
 - (iii) Assisting the Government of Romania in the development of its annual work programme, which incorporates achievements in previous annual programmes;
 - (iv) Carrying out supervision missions as required;
 - (v) Ensuring the presence of an effective operating mechanism to enable effective, transparent implementation of the programme and accurate, verified reporting of data;
 - (vi) Ensuring that disbursements are made to the Government of Romania based on agreed performance targets in the project, and the provisions of this agreement; and
 - (vii) Independently verifying for the Executive Committee that any dismantling of ODS production lines is done appropriately by ensuring that the reactor, distillation towers, receiver tanks for finished products, and control and monitoring equipment are dismantled and rendered unusable for future ODS production, and are disposed of.

- (g) The funding components of this agreement shall not be modified on the basis of future Executive Committee decisions that may affect the funding of the ODS production sector or any related activity.
- (h) All of the agreements set out in this agreement are undertaken solely within the context of the Montreal Protocol and as specified in this agreement. All terms used in this agreement have the meaning described to them in the Montreal Protocol unless otherwise defined herein.

Annex II

AGREEMENT FOR THE METHYL BROMIDE PRODUCTION SECTOR PLAN IN CHINA

1. The Executive Committee, at its 47th Meeting decided to approve in principle a total of US\$ 9,790,000 in funding for the phased reduction and closure of the entire methyl bromide production capacity for controlled applications in China.

2. This is the total funding that would be made available to China by the Multilateral Fund for the total permanent closure of all capacities for the production of controlled substances of Group I Annex E (methyl bromide) excluding the production for QPS, feedstock and critical uses if any, and/or development of capacity to produce alternatives to methyl bromide for controlled applications.

3. The agreed level of funding would be paid out in instalments in the exact amounts specified in Table 1 and on the basis of the following understanding:

(a) By this approval, the Government of China agrees that in exchange for the funding level specified in Table 1, it will reduce its controlled Group I Annex E (methyl bromide) production in accordance with the maximum allowable production in the same table:

Table 1.

(b)	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	
Max. annual allowable production of methyl bromide for controlled uses (ODP tonnes)	621.0	600.0	570.6	390.0	250.0	209.0	176.0	150.0	100.0	50.0	0.0*	-
Project cost (US\$ '000)	3,000	0	0	3,000	0	0	2,000	0	0	1,790	0	9,790
Agency fees (US\$ '000)	225	0	0	225	0	0	150	0	0	134	0	734
TOTAL MLF Grant (US\$ '000)	3,225	0	0	3,225	0	0	2,150	0	0	1,924	0	10,524

* save for QPS, feedstock and critical uses to be approved by Parties.

The Executive Committee has also agreed in principle that it will provide funds on the basis of progress reports submitted in accordance with the schedule indicated above. Payments noted in this paragraph (other than the initial tranche for 2005) are conditioned upon completion of agreed production decreases noted in Table 1 being independently verified and maintained and China meeting the other requirements of this agreement.

The funds are to be approved at the second meeting in the years indicated above, upon the submission by UNIDO and the acceptance by the Executive Committee of the verification of the reduction targets in the preceding years specified in Table 1, with the exception of the first tranche, which will be released upon approval of this agreement.

(b) The Government of China agrees to ensure accurate monitoring of the phase out, and to report regularly, consistent with their obligations under the Protocol and this agreement. China also agrees to allow for independent technical audits administered by the implementing agency, and in addition, as may be directed by the Executive Committee to verify annual controlled methyl bromide production levels agreed in Table.

(c) The Executive Committee wishes to provide the Government of China with maximum flexibility in using the agreed funds to meet the reduction requirements agreed in Table 1. Accordingly, while China's country programme, sector strategy or other ancillary production related documentation discussed during the preparation of this agreement may have included estimates of specific funds that were thought to be needed for specific items, the Executive Committee is of the understanding that during implementation, as long as it is consistent with this agreement and the mode of implementation included in the China project proposal, the funds provided to China pursuant to this agreement may be used in any manner that China believes will achieve the smoothest possible phase out of controlled methyl bromide production.

(d) The Government of China agrees that the funds being agreed in principle by the Executive Committee at its 47th Meeting for the complete closure of its methyl bromide production for controlled uses, is the total funding that will be available to enable its full compliance with the methyl bromide production phase-out requirements of the Montreal Protocol, and that no additional Multilateral Fund resources will be forthcoming for related activities, including the development of an infrastructure for the production and import of alternatives. It is also understood that, aside from the agency fee referred to in paragraph (f) below and reflected in Table 1, the Government of China and the Multilateral Fund and its Implementing Agency will neither provide nor request further Multilateral Fund related funding for the accomplishment of the total phase out of controlled methyl bromide production in accordance with the schedule noted above and the terms of the strategy being approved. This includes but is not limited to funding for employee compensation and all technical assistance including training.

(e) The Government of China understands that, if the Executive Committee meets its obligations under this agreement, but the Government of China does not meet the reduction requirements outlined in paragraph (a), and other requirements outlined in this document, UNIDO and the Multilateral Fund will withhold funding from the subsequent

tranche of the funding outlined in Table 1 until such time as the required reduction has been met. In addition, the Government of China understands that the Multilateral Fund will reduce the subsequent tranche and therefore, total funding for the methyl bromide production phase out on the basis of US \$ 5,000 per metric tonnes of reductions not achieved in any tranche of this agreement. It is clearly understood that the fulfilment of this agreement depends on the satisfactory performance of its obligations by both the Government of China, and the Executive Committee.

(f) UNIDO has agreed to be the implementing agency for this project. The agency fee for the project will be at a fee of 7.5% of project costs, and released together with the annual tranches. As the implementing agency during the project time, UNIDO is responsible for:

(i) Ensuring/providing independent verification to the Executive Committee that the phase-out targets and associated activities have been met;

(ii) Ensuring that technical reviews arranged by UNIDO are undertaken by appropriate independent technical experts;

(iii) Assisting the Government of China in the development of its annual work program, which incorporates achievements in programs in previous years;

(iv) Carrying out supervision missions as required;

(v) Ensuring the presence of an effective operating mechanism to enable an effective, transparent implementation of the programme and accurate, verified reporting of data;

(vi) Ensuring that disbursements are made to the Government of China based on agreed performance targets in the project, and the provisions of this agreement.

(g) The funding components of this agreement shall not be modified on the basis of future Executive Committee decisions that may affect the funding of the methyl bromide production sector or any related activity.

(h) All of the arrangements set out in this agreement are undertaken solely within the context of the Montreal Protocol and as specified in this agreement. All terms used in this agreement have the meaning ascribed to them in the Montreal Protocol unless otherwise defined herein.