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Privileges and immunities for individuals serving on constituted bodies under the Kyoto Protocol: report on the feasibility study on possible insurance for individuals serving on constituted bodies

Technical paper*

Summary

At the request of Parties and in response to decision 9/CMP.2, this paper was prepared to provide information on the feasibility of insurance for individuals serving on constituted bodies established under the Kyoto Protocol. The paper provides an analysis of the potential risks and their financial consequences for individuals serving on these constituted bodies, and provides an estimate of the cost of insurance against these risks. The paper also provides recommendations on ways to reduce the risk of claims against these individuals.

* This technical paper was prepared for the secretariat of the United Nations Framework Convention on Climate Change and its Kyoto Protocol by a risk analysis firm (Vanbreda Risk & Benefits).

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I. Executive Summary

1. This paper provides an overview of the activities of the members of the constituted bodies under the Kyoto Protocol, the risks involved and the feasibility of insuring these risks.

2. The decisions made by constituted bodies have a direct impact on investment decisions by the public and private sectors worldwide. The investment activities triggered by the mechanisms under the Kyoto Protocol constitute one of the successes of the mechanisms, but they also increase the risk, to the constituted bodies and their individual members, that the decisions made by these bodies could be contested.

3. Parties to the Kyoto Protocol are provided with some procedures to appeal the decisions of a constituted body which they perceive to infringe on their rights or interests. It is therefore unlikely – but nevertheless still possible – that Parties to the Kyoto Protocol would file claims in national courts against individuals serving on constituted bodies. On the other hand, private and/or public entities and individuals affected by decisions of a constituted body currently have no means or procedures to raise their complaints or concerns. This absence of procedures increases the risk that such entities and individuals will raise complaints, contest decisions or seek redress in national courts.

4. Since the constituted bodies have no legal personality, entities or individuals referred to in paragraph 3 above cannot file claims against these constituted bodies. This, however, is not the case for the individual members of the constituted bodies who serve in their personal capacities, thereby increasing their risk of enduring lawsuits. All of the activities of and responsibilities of the members of the constituted bodies could result in pure financial losses for these entities, increasing the 'professional liability' of these individuals. In addition to the professional liability, the potential material, physical and consequential damage to these entities during the undertaking of activities increases the 'public liability' of the members of the constituted bodies.

5. It is our opinion that, due to the considerable success and financial impact of the different mechanisms under the Kyoto Protocol, it will only be a matter of time before legal proceedings are brought against individual members of the constituted bodies. Furthermore, claims made against these individuals could amount to millions of euros.

6. In order to reduce liabilities and the risk of claims against individual members, commercial insurance could be purchased. A professional liability insurance policy will cover the liability of the insured for damage, including legal defence costs, caused to third parties, including their clients, arising out of wrongful acts committed during the provision of professional services by the insured to third parties. Classic public liability insurance covers the extra-contractual civil liability of the insured for damages caused to third parties as a result of prejudicial events occurring while conducting the activities described in the special conditions of the policy. Insurance quotes are expected to vary depending on the insurer.

7. It is also our opinion that the secretariat should consider an 'institutional' solution in order to further reduce the risk of claims. If such a solution were to be instituted, commercial insurance could be purchased in order to further contain the risk of legal proceedings, and the premium would likely be more affordable.

II. The constituted bodies

8. The Kyoto Protocol establishes three mechanisms that can be used by Parties to the Kyoto Protocol to help to achieve their commitments in order to contain and reduce emissions of greenhouse gases:

(a) Clean development mechanism (CDM);

(b) Joint implementation (JI);

(c) Emissions trading (ET).

9. The Parties to the Kyoto Protocol have established the following constituted bodies to manage these mechanisms, as well as to monitor, facilitate and enforce compliance:

(a) The CDM Executive Board and the Joint Implementation Supervisory Committee (JISC), which govern the CDM and JI, respectively;

(b) The expert review teams (ERTs), which monitor compliance;[1]

(c) The Compliance Committee, which facilitates and/or enforces compliance.

10. The CDM Executive Board, JISC and the facilitative and enforcement branches of the Compliance Committee all consist of 20 members/alternates each. The CDM Executive Board has also established five working groups, panels and teams consisting of 100 members. The JISC has created one additional panel consisting of eight members. This totals 168 members/alternates on these three bodies. The roster of experts serving on ERTs, on the other hand, consists of approximately 200 members.

11. The individual members of the different constituted bodies act in their personal capacity and on a voluntary basis. They do not receive a salary or remuneration but do get reimbursement for their expenses.

12. Parties can authorize private and/or public legal entities to participate in these mechanisms. There are approximately 7,000 private and/or public legal entities, including:

(a) Project participants – private and/or public legal entities authorized by a Party to participate in a CDM or JI project activity;

(b) Designated operational entities (DOEs) – domestic legal entities or international organizations accredited and designated by the CDM Executive Board on a provisional basis until confirmed by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP);

(c) Accredited independent entities – domestic legal entities or international organizations accredited by the JISC;

(d) Legal entities authorized to transfer and/or acquire emission reduction units (ERUs), certified emission reductions (CERs), assigned amount units (AAUs) or removal units (RMUs).

13. In addition to these specific private and/or public legal entities, there is a wide range of entities and individuals who do not have any direct dealings with the CDM Executive Board or JISC and are not listed as being officially involved in a CDM or JI project activity, but may still feel aggrieved by decisions made by constituted bodies. Such entities could include:

(a) Those directly involved in a CDM or JI project (but not in the project activity itself), such as project developers, financing institutions, equipment suppliers and land owners;

[1] Constituted bodies within the context of decision 9/CMP.2 include members of ERTs.

(b) Beneficiaries of the project, such as electricity consumers, employees of the project and their families, and communities benefiting from improvements to the local environment.

A. Executive Board of the clean development mechanism

14. The individual members of the CDM Executive Board could be held responsible by third parties with respect to the following tasks:

(a) Accreditation and designation of operational entities and reviews of such accreditation under specific standards;

(b) Formal registration of validated projects, including reconsiderations of such actions;

(c) Issuance of CERs, including review of any request for issuance.

15. The Executive Board reports to the CMP, which can reverse the Executive Board's decisions. The reality, however, is that most of the decisions of the Executive Board will not be disturbed by the CMP.

16. In other words, the CMP will usually act on information brought to it by the Executive Board and if a third party considers that such information violates its rights, the risk of claims against the members of the Executive Board who recommended such decisions or actions may increase.

1. Accreditation and designation of operational entities

17. The CDM Executive Board:

(a) Approves the accreditation of operational entities which meet the accreditation standards contained in decision 3/CMP.1, annex, appendix A;

(b) Recommends the designation of operational entities to the CMP;

(c) Reviews whether each DOE continues to comply with the accreditation standards and on this basis confirms whether to reaccredit each operational entity every three years;

(d) Conducts spot-checks and, on the basis of the results, decides to conduct the above-mentioned review, if warranted.

18. The Executive Board may recommend to the CMP to suspend or withdraw the designation of a DOE if it has carried out a review and found that the entity no longer meets the accreditation standards. The Executive Board may recommend the suspension or withdrawal of designation only after the DOE has had the possibility of a hearing. The suspension or withdrawal is with immediate effect, on a provisional basis, once the Executive Board has made a recommendation, and remains in effect pending a final decision by the CMP.

19. The affected entity is notified, immediately and in writing, once the Executive Board has recommended its suspension or withdrawal. The recommendation by the Executive Board and the decision by the CMP on such a case are made public.

20. Registered project activities are not affected by the suspension or withdrawal of the accreditation of a DOE unless significant deficiencies are identified in the relevant validation, verification or certification report for which the entity was responsible. In this case, the Executive Board decides whether a different DOE shall be appointed to review and, where appropriate, correct such deficiencies. If such an assessment reveals that excess CERs were issued, the DOE whose accreditation has been withdrawn or suspended must acquire and transfer, within 30 days of the end of review, an amount of

reduced tonnes of carbon dioxide equivalent (CO_2 eq) to the excess CERs issued, as determined by the Executive Board, to a cancellation account maintained in the CDM registry by the Executive Board.

21. These decisions of the Executive Board could lead to claims against its individual members by the DOEs that might feel wronged by the decisions.

2. Validation and registration

22. Validation is the process of independent evaluation of a project activity by a DOE.

23. Registration is the formal acceptance by the Executive Board of a validated project as a CDM project activity. Registration is the prerequisite for the verification, certification and issuance of CERs related to that project activity.

24. The participants in a CDM project select a DOE to validate a project activity (this is a contractual relationship). The DOE makes a determination as to whether the project activity should be validated and informs the project participants about this determination, whether it is positive or negative.

25. If a project gets validated, the operational entity submits the project to the Executive Board in order to obtain registration of the project.

26. The registration by the Executive Board is deemed final eight weeks after the date of receipt by the Executive Board of the request for registration, unless a Party involved in the project activity or at least three members of the Executive Board request a review of the proposed CDM project activity.

27. These decisions of the Executive Board could again entail claims against its members.

28. A proposed project activity that is not accepted may be reconsidered for validation and subsequent registration, after appropriate revisions, provided that it follows the procedures and meets the requirements for validation and registration.

3. Verification and certification

29. Verification is the periodic independent review and ex post facto determination by the DOE of the monitored reductions in anthropogenic emissions by sources of greenhouse gases that have occurred as a result of a registered CDM project activity during the verification period.

30. Certification is the written assurance by the DOE that, during a specified time period, a project activity achieved the reductions in anthropogenic emissions by sources of greenhouse gases, as verified.

4. Issuance of certified emission reductions

31. The certification report constitutes a request for issuance to the Executive Board of CERs equal to the verified amount of reductions of anthropogenic emissions by sources of greenhouse gases.

32. The issuance is considered final 15 days after the receipt of the request for issuance, unless a Party involved in the project activity or at least three members of the Executive Board request a review of the proposed issuance of CERs. Such a review is limited to issues of fraud, malfeasance or incompetence of the DOEs.

33. The decisions of the Executive Board could result in claims against its members, including claims by the operational entities.

5. Panels, working groups and teams

34. To assist in the performance of its functions, the Executive Board is entitled to establish panels, working groups and teams (e.g. Methodologies Panel, Afforestation and Reforestation working group, Small-scale CDM working group, etc.).

35. These experts do not take formal decisions but they undertake technical assessments (upon which decisions of the Executive Board are based) and also work on the development or elaboration/understanding of methodological standards (e.g. tools and methodologies).

36. Under normal circumstances, there would not be many claims filed against these experts since they do not take formal decisions and are not acting on the 'front line' as are the members of the Executive Board.

37. There might, however, be more of a risk if the identities of these experts are revealed to potential plaintiffs. Normally, the identity of the experts is considered confidential but a mistake may nevertheless occur and their identities be disclosed. In this case it would be possible for plaintiffs to raise claims against the members of the panels, working groups and teams, personally.

B. Joint Implementation Supervisory Committee

38. The members of the JISC could be held responsible by third parties with respect to the following tasks:

(a) Decision-making functions, including in circumstances defined in section E of the Article 6 guidelines, for example, to determine whether a project meets the required standards;

(b) The accreditation of independent entities in accordance with criteria set out in appendix A to the Article 6 guidelines and the suspension or withdrawal of such accreditation if it considers that the required standards are no longer met.

1. Determination of whether a project meets the required standards

39. The verification procedure is the determination by an independent entity, accredited pursuant to appendix A to the Article 6 guidelines, by the JISC, as to whether a project and the ensuing reductions of anthropogenic emissions by sinks meet the relevant requirements.

40. The determination by an accredited independent entity concerning a project is deemed final 45 days after the date on which the determination is made public, unless a Party involved in the project or three of the members of the JISC request a review by the JISC.

41. These final decisions of the JISC could result in claims against its members.

42. The accredited independent entity also makes a determination of the reductions in anthropogenic emissions reported by project participants in accordance with appendix B to the Article 6 guidelines. The determination is made publicly available together with an explanation of the reasons for the determination.

43. This determination is deemed final 15 days after the date on which the determination is made public, unless a Party involved in the project or three of the members of the JISC request a review by the JISC.

44. These final decisions of the JISC could again result in claims against its members.

2. Accreditation, suspension or withdrawal of independent entities

45. The JISC approves the accreditation of an independent entity and suspends or withdraws the accreditation if it has carried out a review and found that the entity no longer meets the accreditation standards.

46. The JISC may suspend or withdraw accreditation only after the accredited independent entity has had the opportunity for a hearing and depending on the outcome of the hearing. The suspension or withdrawal is with immediate effect. The affected entity is notified, immediately and in writing, once the JISC has decided upon its suspension or withdrawal. The decision by the JISC on such a case is made public.

47. Verified projects are not affected by the suspension or withdrawal of the accreditation of an independent entity unless significant deficiencies are identified. In this case, the JISC is appointed to assess and, where appropriate, correct such deficiencies. If such an assessment reveals that excess ERUs have been transferred as a result of the deficiencies, the independent entity whose accreditation has been withdrawn or suspended must acquire an equivalent amount of ERUs and place them in the holding account of the Party hosting the project within 30 days of the assessment mentioned above.

48. These decisions of the JISC could again lead to claims against its members by independent entities.

C. Expert review teams

49. The ERTs work directly with Parties listed in Annex B to the Kyoto Protocol to assess their progress in implementing the Kyoto Protocol.

50. One of the tasks of the ERTs is to provide input to the work of the Compliance Committee in the form of technical 'review reports'. These reports may contain 'questions of implementation'.

51. Based on the outcome of consideration of these 'questions of implementation' by the enforcement branch of the Compliance Committee, a Party may lose its eligibility to participate in the mechanisms under the Kyoto Protocol, or the enforcement branch could apply adjustments to its inventories under Article 5, paragraph 2, of the Kyoto Protocol.

52. The decisions of the Compliance Committee thus affect not only the Parties to the Kyoto Protocol, but also private and/or public legal entities participating in the mechanisms under the Kyoto Protocol as well as entities that do not have any direct dealings with the CDM Executive Board or JISC and are not listed as being officially involved in a CDM or JI project activity.

53. These private and/or public legal entities could potentially file claims against the members of the ERTs.

D. Compliance Committee

54. The Compliance Committee is made up of two branches: a facilitative branch and an enforcement branch. As their names suggest, the facilitative branch aims to provide advice and assistance to Parties in order to promote compliance whereas the enforcement branch has the responsibility to determine consequences for Parties that do not meet their commitments.

55. Through its branches, the Compliance Committee considers 'questions of implementation' which can be raised by ERTs, any Party with respect to itself, or any Party with respect to another Party.

56. The enforcement branch is responsible for determining whether a Party is in non-compliance with its emissions targets, the methodological and reporting requirements for greenhouse gas inventories, and the eligibility requirements under the mechanisms.

57. In case of disagreements between a Party and an ERT, the enforcement branch determines whether to apply adjustments to greenhouse gas inventories or to correct the compilation and accounting database for the accounting of assigned amounts.

58. The mandate of the facilitative branch is to provide advice and facilitation to Parties in implementing the Kyoto Protocol, and to promote compliance by Parties with their Kyoto commitments. Furthermore, the facilitative branch may provide an 'early warning' of potential non-compliance by Parties.

59. In the case of the enforcement branch, each type of non-compliance requires a specific course of action. For instance, where the enforcement branch has determined that a Party does not meet one or more eligibility requirements under Articles 6, 12 and 17 of the Kyoto Protocol, it will suspend the eligibility of that Party in accordance with relevant provisions under those Articles. In addition, it will require the Party to submit a compliance action plan.

60. The branches of the Compliance Committee base their deliberations on information provided by reports from ERTs, the CMP and subsidiary bodies, and Parties. Competent intergovernmental and non-governmental organizations may submit relevant factual and technical information to the relevant branch after the preliminary examination.

61. There are detailed procedures with specific timeframes for the enforcement branch, including the opportunity for a Party with a 'question of implementation' before the Compliance Committee to make formal written submissions and request a hearing where it can present its views and call on expert testimony. Members of ERTs can also be called upon to provide expert advice to the Compliance Committee.

62. Any Party that is found to be in non-compliance with its reporting requirements must develop a compliance action plan, and Parties that are found to not meet the criteria for participating in the mechanisms will have their eligibility suspended. In all cases, the enforcement branch will make a public declaration that the Party is in non-compliance and will also make public the consequences to be applied.

63. If a Party's eligibility is suspended, it may request, either through an ERT or directly to the enforcement branch, to have its eligibility restored if it believes it has rectified the problem and is again meeting the relevant criteria.

64. A Party whose eligibility has been suspended will normally try to get its eligibility restored as quickly as possible, which of course tends to limit the damage suffered by the Party but also the potential damages of participating private and/or public legal entities.

65. As a general rule, decisions taken by the two branches of the Compliance Committee cannot be appealed. The exception is a decision of the enforcement branch relating to emissions targets. Even then, a Party can only appeal a decision if it believes it has been denied due process. This appeal is brought before the CMP.

66. The decisions of the Compliance Committee may be contested before national courts and thus there is a risk of claims against its members.

III. Liability issues

67. As mentioned in paragraph 11 above, the individual members of constituted bodies act in their personal capacity.

68. Consequently, it is possible that claims could be filed against them personally in national courts, including claims for monetary damages, mainly from the private and public legal entities that are affected by the official functions and decisions of the members of the bodies, but also from Parties to the Kyoto Protocol and other third parties.

69. All of the activities and responsibilities of the members of the constituted bodies, as described in chapter II above, could result in pure financial losses for these parties and thus increase the 'professional liability' of the members of the constituted bodies.

70. In addition to this professional liability, it must also be noted that the members of some of the constituted bodies could also cause material, physical and consequential damage to third parties during the undertaking of activities. This refers to the 'public liability' of the members of the constituted bodies.

71. Since the professional liability represents by far the biggest risk for the members of the constituted bodies, it is essential to assess who could be the plaintiffs, what legal grounds the lawsuits could be based upon, what damages could be claimed, what the potential costs could be, and to provide an estimation on the probability of claims.

A. Plaintiffs

72. Not only could the private and/or public legal entities involved in a project activity feel aggrieved by the actions and decisions of the individuals serving on constituted bodies, but so could: (1) entities or individuals that do not have any direct dealings with the CDM Executive Board or JISC and are not listed as being officially involved in a CDM or JI project activity; (2) independent entities under the JI and the operational entities under the CDM; and (3) Parties to the Kyoto Protocol who may file claims against the members of the constituted bodies, although this is unlikely.

73. In short, anyone could file a claim against any of the members of the constituted bodies. Since there is no law prohibiting the raising of claims, it is basically sufficient that a person 'feels' aggrieved by an action of (a member of) a constituted body in order for this person to file a claim before a national court and to seek redress.

74. Obviously, the possibility of raising claims does not in itself guarantee that the lawsuits will also be successful. A judge will assess whether or not a claim is justified.

B. Legal grounds

75. Plaintiffs could file claims against the individuals serving on constituted bodies based on a number of legal grounds, such as:

(a) **Acting outside of the delegated authority** – that certain decisions taken by a constituted body are ultra vires, or beyond their authority;

(b) **Incompetence of the members of the established bodies**;

(c) **Substantially incorrect decisions** – decisions taken are based on factually incorrect technical or scientific conclusions;

(d) **Conflict of interest** – that individuals serving on a constituted body have a conflict of interest concerning decision-making;

(e) **Breach of confidentiality**;

(f) **Violation of procedural rights** – allegations that the conduct of a member of a constituted body is not in conformity with the operational policies, procedures and practices, which results in the violation of procedural rights of private and/or legal entities;

(g) **Violation of principles of due process**;

(h) **Lack of transparency** – allegations that there is inconsistency in the decisions concerning similar project activities;

(i) **Bias in decision-making** – accusations that the decisions, recommendations or other actions of the constituted body are biased or made improperly;

(j) **Lack of efficiency** – whenever a time limit (for instance, for a review by the CDM Executive Board) is not respected;

(k) **Wrongful comments allegedly harming the plaintiff** – for instance, if a member of a constituted body gives an interview and hints that a certain company or Party is causing environmental damage.

76. In order for a plaintiff to seek redress in a national court, the plaintiff will need to prove that the action undertaken by the individual member of a constituted body qualifies as a wrongful act (see chapter III C below) and that this action has caused damage to the plaintiff. If the plaintiff does not succeed in proving this, the claim will be dismissed by the court.

C. Damage

77. The market-based mechanisms established under the Kyoto Protocol are an enormous success and therefore the financial interests of those directly or indirectly involved in these mechanisms are huge. The CDM market, for instance, was worth more than EUR 5 billion in 2006.

78. The plaintiffs could file claims when they feel they have suffered damage. The concept of damage is very broad and will depend on the basis of the claim. Private and/or public legal entities involved in a project activity or in ET could, for instance, claim that, as a direct result of the actions taken by the members of constituted bodies, they:

(a) Missed investment or business opportunities;

(b) Were not able to participate in the lucrative mechanism of carbon trading;

(c) Suffered damaged reputation due to negative publicity;

(d) Were not able to attract credits;

(e) Had to dismiss employees;

(f) Were not able to respect their contractual obligations with other companies.

79. As regards entities or individuals that do not have any direct dealings with the CDM Executive Board or JISC, and are not listed as being officially involved in a CDM or JI project activity, they could, for instance, claim that as a direct result of the actions taken by the members of constituted bodies, they:

(a) Missed business opportunities or potential revenues;

(b) Lost their jobs;

(c) Had to make additional investments or remap their organization, resulting in extra costs;

(d) Suffered health damage since the project was not accepted (the level of emissions did not decrease and thus human health was negatively affected);

(e) Suffered damage since the anticipated improvement to the local environment did not materialize due to the failure to approve the registration of the project;

(f) Missed the opportunity to consume or deliver electricity (at a lower price).

80. Independent entities under the JI and operational entities under the CDM could, for instance, claim that, as a direct result of the actions of the members of constituted bodies, they:

(a) Suffered loss of business since they were not accredited, or their accreditation was suspended or withdrawn by the JISC or the CDM Executive Board;

(b) Suffered losses because they had to acquire amounts of ERUs and place them in the holding of the Party hosting the project (see para. 47 above);

(c) Suffered losses because they had to acquire and transfer CERs issued to a cancellation account maintained in the CDM registry by the CDM Executive Board (see para. 20 above);

(d) Suffered damaged reputation because of the review of the proposed issuance of CERs based on issues of fraud, malfeasance or incompetence of the operational entity (see para. 32 above).

81. The Parties to the Kyoto Protocol are provided with some procedures to defend themselves as well as to appeal the decisions of a constituted body which they deem to be flawed and/or unjustified. Though it is possible, it is less likely that Parties would file claims in national courts against individuals serving on constituted bodies.

82. If a claim is raised, Parties could, for instance, claim that they:

(a) Were not able to participate in the market-based mechanisms;

(b) Suffered damaged reputation;

(c) Had to address the claims of entities involved in a project activity and entities or individuals that are not involved in a project activity.

D. Costs

1. Compensation for monetary damages (pure financial loss)

83. The total amount which could be claimed depends strongly on the type of damage the entities claim to have suffered. It must be clear, however, that the maximum claims could be enormous and could amount to several million euros.[2]

[2] FCCC/KP/CMP/2007/2.

84. If an entity is, for instance, not able to participate in ET, this could lead to a huge claim. The current price for a tonne of CO_2 is approximately EUR 20. If, for example, we consider a carbon trade of 200,000 tonnes of CO_2, this results in a claim of EUR 4 million.

85. If an entity claims to have missed investment opportunities, this could also result in huge claims. The total amount of investment needed to set up a new production line could again be in the range of millions of euros.

86. The amount claimed because of damaged reputation could also be hundreds of thousands of euros.

87. If a private and/or public legal entity has to dismiss employees, or is not able to respect contractual obligations with other companies due to a decision taken by a constituted body, the amount of compensation claimed could also easily amount to hundreds of thousands of euros.

88. The total amount which could be claimed by individuals, as opposed to entities, looks to be somewhat smaller, but could still be significant.

89. If a group of individuals were to succeed, for instance, in proving that the non-acceptance of a project resulted in them having cancer, the claim would amount to millions of euros. This type of group claim could be made in countries where 'class actions' are allowed.

90. The total amount which could be claimed by entities, on the other hand, could also be significant. If an independent entity or operational entity does not get accredited, or if its accreditation is suspended or withdrawn, they suffer an important loss of business. The claims per lost project could amount to tens of thousands of euros or even hundreds of thousands of euros in the case of a very large project.

91. If an independent or operational entity has to acquire ERUs or CERs to cover any excess issuance of these credits, the claim could be much higher and could even amount to millions of euros.

92. If an operational entity suffers a loss of reputation, the claim would not only cover moral damages, but also the resulting loss of business, and could therefore amount to tens of thousands of euros.

93. If a Party files a claim, the total amount of damages could be enormous. If a Party is, for instance, not able to participate in ET, this could lead to a huge claim. As illustrated in paragraph 84 above, the cost of such a claim could amount to EUR 4 million.

94. When a Party to the Kyoto Protocol is, for instance, faced with complaints made by entities involved in a project activity, and whereby it is alleged that the Party did not manage its tasks appropriately, a claim could be raised by the Party against the members of the constituted bodies aiming to hold the Party harmless. As previously suggested in paragraph 83 above, the damage claim could be very high.

2. Estimated cost of legal process

95. The cost of the legal process is difficult to estimate as it will depend on a number of important criteria, such as:

(a) The duration of the legal proceedings;

(b) The necessity of retaining local counsel;

(c) The fees charged by the local counsel;

(d) The general costs of litigation;

(e) The country in which the claim was instituted;

(f) On some occasions, the total amount of damages claimed;

(g) The appeal procedures of different countries;

(h) The complexity of the case.

96. The cost of the legal process will therefore differ greatly from case to case and may, for instance, range from EUR 1,000 to EUR 200,000.

3. Examples

The following examples illustrate how legal costs could be calculated.

Example 1

97. A claim is raised by a Dutch legal entity before a Dutch national court against one of the members of the JISC. During the first session before the court, it appears that there is no legal possibility to raise a claim against the member of the JISC since there is no territorial link to the Dutch court, so the court has to declare itself incompetent to evaluate the claim.

98. The legal cost in this case would be quite low and could be estimated at EUR 1,500.

Example 2

99. A claim is raised by an American company against a member of the CDM Executive Board before its national court concerning a project activity in Senegal. The American judge declares himself competent to decide upon the claim and the total process duration ranges up to five years. The legal counsel costs USD 900 per hour and charges a total amount of 150 hours of work.

100. The legal cost in this case would be at least USD 135,000, not including expenses and costs of the trial itself, which can easily be estimated at an additional USD 30,000.

4. Cost of international mechanisms or arbitration processes

101. Though the possibility exists, for the moment there is no obligation for plaintiffs to utilize alternative dispute settlement mechanisms before, or in lieu of, filing claims in court.

102. In general, alternative dispute settlement mechanisms, such as arbitration, have some advantages over national courts. Most of the time they are more expeditious (thus reducing costs) and try to conciliate both parties to a legal claim.

103. Again, it is difficult to assess the cost of this kind of dispute settlement as it will depend on different criteria, such as:

(a) The length of the process;

(b) The cost of legal counsel;

(c) The cost imposed by the dispute settlement body;

(d) The costs associated with persuading the aggrieved Party to utilize alternative dispute settlement mechanisms;

(e) The country in which the dispute settlement body is based;

(f) The complexity of the case.

104. The cost of dispute settlement or arbitration will therefore differ greatly from case to case and may easily range from EUR 1,000 EUR to EUR 50,000 per case.

5. Examples

105. The following examples illustrate the possible cost of alternative dispute settlement mechanisms.

106. A dispute settlement body in Italy denies the claim of the plaintiff during its first session and the total cost to the body amounts to EUR 1,500.

107. An arbitration procedure in the United States takes up to six months to settle the claim and involves external experts to give their opinion on the case. The total cost amounts to USD 25,000.

108. A uniform procedure, on the other hand, which would impose on plaintiffs to submit their claims to one single dispute settlement mechanism in a specific country (for instance the headquarters of the secretariat in Bonn, Germany) would make things much easier and would also make it possible to present a more transparent and clear view of the legal costs.

6. Conclusion on costs

109. Every claim raised before a national court, whether it is justified or frivolous, will raise important costs associated with legal process/dispute settlement.

110. If, for instance, 15 claims are raised every year, the cost of legal process/dispute settlement could easily be estimated to range from EUR 250,000–400,000.

111. If, however, a plaintiff should succeed in obtaining redress from a national court, the cost of that claim alone could amount to millions of euros.

E. Estimation of probabilities

1. Clean development mechanism

112. Between 1 January 2001 and 5 February 2008, 3,344 projects were submitted to the validation system. The CDM Executive Board currently has no method of determining exactly how many projects do not get validated by the DOEs.

113. As of 5 February 2008, 117 requests for registration had been or were being reviewed by the Executive Board. The Executive Board currently has no method of determining exactly how many decisions of registration have been challenged or have been changed by the Executive Board.

114. The certification report by DOEs constitute a request for issuance to the Executive Board of CERs equal to the verified amount of reductions of anthropogenic emissions by sources of greenhouse gases. As of 5 February 2008, 22 requests for issuance had been or were being reviewed by the Executive Board. The Executive Board currently has no method of determining exactly how many requests for issuance have been challenged or have been changed by the Executive Board.

115. As of February 2008, there were 41 accredited operational entities. One application for accreditation was pending and three applications were withdrawn.

116. Reactions to the decisions of the Executive Board are normally received in the form of letters addressed to the Executive Board requesting clarifications and/or contesting such decisions. Between

October 2006 and August 2007, the Executive Secretary received 12 letters addressed to the Executive Board from legal entities expressing concern or raising issues regarding project activities under the CDM.

117. Some private legal entities stated that as a result of the decisions of the Executive Board, they had suffered losses amounting to several millions of euros. For two project activities, the private legal entities requested the Executive Board to revoke its decisions 'without prejudice to any other rights and remedies,' including the right to commence legal proceedings.

118. On behalf of the Executive Board, the secretariat sent letters to each private legal entity to clarify the decisions of the Executive Board, provide an update of actions taken by the Executive Board in response to the letter and/or recommend that the project activity be re-submitted for consideration by the Executive Board.

2. Joint implementation

119. Since the launch of the verification procedure under the JISC (JI 'track 2') in October 2006 until February 2008, only two projects submitted applications to the JISC. As of February 2008, one of the two submitted projects passed the verification procedure by an independent entity whilst the other one was still under review.

120. As of February 2008, no determinations of reductions of anthropogenic emissions were submitted since the crediting period only started as of 1 January 2008. Accordingly, no requests for review were submitted to the JISC.

121. As of February 2008, 15 applications for accreditation as independent entities were made. None of them have been accredited under JI but 13 are DOEs and are therefore able to operate provisionally under JI.

3. Expert review teams

122. Every year, the ERTs conduct reviews for Annex I Parties. Out of the initial reviews conducted in 2007, one 'question of implementation' was identified. Another was identified in April 2008.

123. Experts are invited to provide advice to the Compliance Committee whenever a 'question of implementation' is raised, which has happened once as of 15 May 2008.

124. As of 15 May 2008, no claims were filed against any members of the ERTs**.**

4. Compliance Committee

125. The Compliance Committee started operations in 2006 and since then, few decisions have been taken. As of 15 May 2008, the enforcement branch completed consideration of one 'question of implementation' and decided to proceed with another.

5. Conclusions on the current situation

126. As of 15 May 2008, no legal proceedings were filed against the members of the constituted bodies. It is our opinion, however, that it is only a matter of time before legal proceedings will commence.

127. The different mechanisms under the Kyoto Protocol have begun operating just recently and are having tremendous success, meaning that more and more projects will be submitted and thus the risk of litigation will increase.

128. The 12 letters sent to the Executive Secretary and addressed to the CDM Executive Board in less than a year's time, prove that the risk of litigation is growing larger by the day. The number of annual claims made against the members of constituted bodies could be significant.

129. Since the constituted bodies have no legal personality, plaintiffs can only file claims against the individual members of the constituted bodies. Whilst this is an enormous risk to the individuals, it may actually be an advantage considering the risk of legal proceedings. If, for instance, a private legal entity claims damages worth millions of euros, the entity may not to wish to start legal proceedings against the individual members of the constituted bodies, since they will be unable to pay these sums out of their own resources.

6. Recommendations for the future

130. In order to reduce the risk of claims and to minimize the cost of insurance, the institutional and procedural options set out below could be considered.

Due process rights

131. As mentioned in paragraph 81 above, Parties to the Kyoto Protocol are provided with some procedures to defend themselves as well as to appeal the decisions of a constituted body which they perceive to violate their rights.

132. This possibility, however, does not exist for other parties (private and/or public entities or others) affected by the decisions of a constituted body. For the time being, aggrieved entities or persons who may have suffered damage from decisions of constituted bodies have no right of recourse and essentially little, if any, due process rights.

133. In our opinion, this lack of procedural rights significantly increases the risk that claims will be filed against individual members of the constituted bodies. Plaintiffs will raise complaints, contest decisions or seek redress in national courts, simply because they do not have other options.

134. In order to substantially reduce the probability of claims (and hence the insurance premium) the secretariat has been strongly advised to incorporate mechanisms to promote procedural fairness for project participants and other parties. There is a clear necessity to provide parties with procedural rights of hearing and appealing the decisions of the constituted bodies.

135. Where rights of parties are affected by decisions of constituted bodies, they should be granted the right to be heard and the right to have a decision that they wish to contest reviewed by an independent body.[3]

Legal personality

136. In order to reduce the risk to the individual members of the constituted bodies, the option of providing the constituted bodies with legal personality may also be considered. This way, when an entity wants to file a claim, it will not be necessary to file the claim against the individual member. The entity will be able to contest the decisions of the constituted body as a whole.

137. Though this action may increase the risk of claims (see para. 129 above), it offers the benefit that the individuals will largely be free of risk.

[3] See FCCC/SBI/2006/21.

Hold harmless agreement

138. Another option could be to provide a 'hold harmless agreement' between the members of the constituted bodies and the constituted bodies themselves. Such 'agreement' would guarantee the individual members that, if a claim is raised against any of them, the constituted body will provide legal assistance and will hold the individuals harmless should they be required to pay damages to the plaintiffs.

139. In order to provide such 'agreement' it will not be strictly necessary to grant legal personality to the constituted bodies, thus again reducing the risk of claims.

140. In order to further minimize the risk of claims, the secretariat has been strongly advised that such 'hold harmless agreements' should not be made public in any way. If prospective plaintiffs realize that such agreement exists, the risk of claims would increase dramatically since the plaintiffs would then expect to be compensated for their damage by the constituted bodies.

Granting immunity

141. Currently, the members of the constituted bodies are only granted immunity for legal claims in Germany,[4] the host country of the secretariat. Outside Germany, however, the members of the bodies do not benefit from such immunity.

142. The immunity in Germany consists of a jurisdictional immunity. Plaintiffs can still file a claim against one of the members of a constituted body but cannot do this before a German court. Rather, they have to file their claims before an international dispute settlement body (which for the moment has not been established).

143. It would definitely be beneficial to grant immunity to all members of the constituted bodies. This kind of action would, however, entail a decision by the CMP and the creation of an international dispute settlement body which would then address all claims.

144. If immunity was to be granted to all individuals serving on constituted bodies, the claims filed before national courts would decrease dramatically, but the main benefit would be that the costs involved would become much more transparent and clear since all claims would have to be redirected to one international dispute settlement body.

145. The possibility would still exist that claims would be filed before national courts, but the defendant would have to focus only on explaining the principles of immunity in order for the national judge to dismiss the case, thus reducing the costs and insecurity (and the insurance premium – see chapter IV below).

International dispute settlement body

146. Obtaining written agreements with public and private entities:

(a) Document FCCC/SBI/2006/21 presents a comprehensive study of the consequences and resource implications of obtaining written agreements that claims will be filed before a dispute settlement body at the headquarters of the secretariat;

(b) This action would certainly have important benefits. Claims would still be filed against the members of the constituted bodies but would at least be redirected to a dispute settlement body, for instance, at the headquarters of the secretariat in Bonn, Germany;

[4] There is also immunity for acts during a conference or activity covered by a conference agreement with a host State.

(c) Plaintiffs would still be able to file claims before national courts but the defendant would have to focus only on the written agreements (condemning parties to file all claims before a dispute settlement organism) in order for the national judge to dismiss the case, thus dramatically reducing the costs and insecurity (and again, the insurance premium);

(d) The added benefit of this action would be that the estimation of costs resulting from filing claims before the dispute settlement body would become much more transparent and clear;

(e) A word of caution should be expressed, however, concerning the recommendations made in document FCCC/SBI/2006/21 since these kinds of agreements would be applicable only to parties who have effectively agreed upon the principle of submitting claims to one single dispute settlement body. These agreements would therefore not be applicable to other interested parties that did not (or did not have the opportunity to) sign the agreement. These parties would therefore still be able to seek redress before national courts.

IV. Insurance

A. Type of insurance

147. Professional liability presents the biggest risk to members of the constituted bodies. In order to insure the intellectual activities of the members of the different constituted bodies causing purely financial losses to third parties, there is need of professional liability insurance.

148. In order to insure the material, physical and consequential damages caused to third parties by members of the constituted bodies during the physical exercise of their jobs, there is need of public liability insurance.

149. Legal defence costs are part of both the professional and the public liability cover.

150. If, however, the secretariat considers the insurance premium for professional and/or public liability to be too high, it could consider coverage for legal defence costs only. The premium for legal defence costs will still be significant, however, because this frequently changes due to annual increases in lawyers' fees.

B. Analysis of common insurance terms and conditions

1. Professional liability insurance

151. A professional liability insurance policy will cover the liability of the insured for damage, including legal defence costs, caused to third parties, including their clients, arising out of wrongful acts committed during the provision of professional services by the insured to third parties.

152. In order to fully understand this principle it is necessary to provide some definitions:

(a) Insured: All individual members of the constituted bodies;

(b) Damages: Any amount that an insured shall be legally liable to pay to a third party in respect of judgements rendered against an insured, or for settlements negotiated by the insured with the written consent of the insurer;

(c) Professional services: The professional services of the individual members of the constituted bodies provided to third parties;

(d) Wrongful act: Any actual or alleged negligent act, error or omission committed whilst providing professional services.

Exclusions

153. The main exclusions of the policy that concern the individual members of the constituted bodies are:

(a) Damages arising out of, based upon or attributable to any intentional or criminal acts, or the non-compliance with prudence or safety rules, or with the law, regulations and practices specific to the insured's activities to such an extent that the indemnified consequences of this non-compliance was, according to the opinion of all persons that are normally competent in the subject, almost inevitable;

(b) Judicial, fiscal, administrative, disciplinary or economical fines, punitive and exemplary damages;

(c) Damages arising out of bodily injury or property damage, unless caused by a wrongful act. It is specified that this kind of policy does not cover claims in connection with damages that are covered under a classic public liability policy;

(d) Damages arising, based upon or attributable to any circumstance or wrongful act, that as of the inception of this policy, may reasonably have been expected by any insured party to give rise to a claim.

2. Public liability insurance

154. Classic public liability insurance covers the insured's extra-contractual civil liability for damages caused to third parties as a result of prejudicial events occurring while conducting the activities described in the special conditions of the policy.

155. As an extension to this, contractual liability is covered if it results from a factor which, by itself, is likely to provide extra-contractual liability.

Covered damages

156. The damages covered by this kind of insurance policy are:

(a) Physical and material damages suffered by third parties;

(b) Consequential financial damages from a physical and/or material damage suffered by third parties;

(c) Legal defence costs.

Exclusions

157. The main exclusions from coverage are:

(a) Damages caused deliberately by one of the insured;

(b) Damages caused by a serious fault committed by one of the insured. A serious fault is defined as follows:

(i) The non-compliance with prudence or safety rules, or with the law, regulations and practices specific to the insured's activities, to such an extent that the

indemnified consequences of this non-compliance was, according to the opinion of all persons that are normally competent in the subject, almost inevitable;

(ii) The repeated occurrence, by lack of precautions, of damages of the same origin;

(iii) Acceptance and performance of a task or a deal when the insured is aware of the fact that he does not have the competency, required techniques, material means or the adequate human resources to carry out this work or this deal, in order to fulfil his commitments in the respect of adequate safety conditions for third parties;

(iv) Judicial, transactional, administrative or economic fines, punitive or dissuasive damages (such as 'punitive damages' or 'exemplary damages' in some foreign legislations), as well as legal expenses of criminal proceedings.

3. Feasibility of one international policy versus several national/regional policies

158. It should be feasible to provide one single (master) insurance policy covering the individual members of the constituted bodies for their activities around the world.

159. All claims should be insured regardless of the country in which they are raised and irrespective of what system of law the claims would be based upon.

160. If the option to buy insurance is selected, the secretariat in Bonn, Germany should be named as policyholder. This way, the premium and all correspondence would be directed to the secretariat.

4. Identification of insurance companies worldwide that are able to provide coverage

161. Based on the risk analysis described above, the secretariat has been advised that an insurance solution could be a very important instrument to remove most of the liabilities mentioned, provided that the insurer can be convinced that there will be no abuse of the insurance policy. The main risk to the members of the constituted bodies is professional liability; therefore the insurer must be assured that purely political and business risks will not be covered under the policy.

162. Once the insurance company has been convinced, it will be possible to provide binding quotes such as those outlined in chapter IV B 5 below. Otherwise the insurer will not provide quotes, or the premium level would be much higher than the 'non-binding' quotes mentioned below.

163. Since the headquarters of the secretariat in Bonn would be named as policyholder, the secretariat has been advised to first contact German insurance companies specialized in covering professional liability, such as:

(a) HDI-Gerling;

(b) Allianz;

(c) Victoria (Ergo Group).

164. Second, the secretariat has been advised to consult internationally-based insurance companies such as:

(a) AIG;

(b) Liberty Insurance;

(c) ACE;

(d) Zurich;

(e) AXA Corporate Solutions;

(f) Chubb;

(g) XL Insurance;

(h) Lloyd's Syndicates;

(i) CNA.

5. Premium

165. Given the current situation as described in chapter III above, an estimation of the premium for public and professional liability insurance has been provided to the secretariat (see table 1).

Table 1. Premium for public and professional liability insurance[a]

(euros)

Limit of liability	Deductible	Premium	Deductible	Premium
2 500 000	50 000	122 500	100 000	110 000
5 000 000	50 000	197 000	100 000	175 500
10 000 000	50 000	325 000	100 000	295 000

[a] Taxes excluded.

166. As mentioned in paragraph 150 above, the secretariat may wish to select coverage for legal defence costs only. Table 2 provides an estimation of the premium for legal defence costs alone.

Table 2. Premium for legal defence costs only[a]

(euros)

Limit of liability	Deductible	Premium	Deductible	Premium
2 500 000	25 000	82 000	50 000	75 000
5 000 000	25 000	130 500	50 000	117 500
10 000 000	25 000	221 000	50 000	199 500

[a] Taxes excluded.

167. The premium could decrease if some of the recommendations identified in paragraphs 130–150 above are applied (for example, granting immunity to the individual members of the constituted bodies and obtaining written agreements from the project participants to file claims before a dispute settlement organism).

V. Conclusions

168. The individual members of the constituted bodies are, for the time being, exposed to a huge risk of legal procedures against them.

169. Plaintiffs could raise claims against any of the individual members before any national court worldwide, and the claims could amount to millions of euros.

170. Since the constituted bodies lack any legal personality, plaintiffs will have no other option but to sue the individual members of the constituted bodies serving in their personal capacity.

171. Owing to the enormous success and financial impact of the different mechanisms under the Kyoto Protocol, the secretariat has been advised that it will only be a matter of time before legal proceedings against the individual members commence.

172. In order to contain this risk to the individual members, commercial insurance could be purchased. Quotes are expected to vary from insurer to insurer. Some of them will follow the quotation approach in tables 1 and 2 and others will offer much higher premiums based upon their underwriting philosophy. Some insurers may decline providing a quote altogether if they believe that the risk is unquantifiable.

173. It may also be sound to take a more 'institutional' approach in order to reduce the risk of claims.

174. The options that should be considered include:

(a) Providing potential plaintiffs with more procedural rights;

(b) Granting legal personality to the constituted bodies;

(c) Signing 'hold harmless agreements' between the constituted bodies and their individual members;

(d) Granting immunity to the individual members; or

(e) Obtaining written agreements from project participants in order to redirect claims to an international dispute settlement body.

175. If such recommendations were to be instituted, commercial insurance could simply be purchased in order to further contain the risk of legal proceedings, and the premium would likely be more affordable.

176. Instead of selecting a full insurance solution, or protection by means of save harmless clauses, the secretariat could also opt for a combined solution (e.g. insurance with a limit of EUR 10 million and hold harmless clauses in excess).

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