2e. Flexibility on ERPA Arrangements

Background

- Several REDD+ Countries have expressed interest in options to access markets and increase the amount of finance mobilized to sustain their ER Programs and increase benefits to communities.

- Initial proposal for added flexibility shared in February 2024, followed by a presentation and response to CFP queries in March 2024.

- Initial proposal allowed countries to retain a limited number of ERs (‘Retained’ ERs) in a reporting period prior to fulfilling its Contract ER volume. This would enable the ‘frontloading’ of a small portion of their expected Excess ERs to pilot monetization of ERs CFPs expressed general support, but also concerns on demand-side integrity requirements, and proposed to discuss this at 28th CF Meeting.

- Based on more recent demands from REDD+ Countries, **FMT has developed a new, expanded, proposal for ERPA flexibility that would enable countries to propose contract ERs to be released as Excess ERs (‘released’ Excess ERs) that they could use in markets if desired**

Justification for additional flexibility

- Additional flexibility would enable countries that have the option to generate Excess ERs in the short term from 6 to 12 countries → equal opportunities to pilot markets
- Additional flexibility could enable up to 65 million ERs to be ‘released’ from ERPAs and potentially be made available to carbon markets.
- This is equivalent to $325m in Contract ER payments at $5/ton, which at projected market prices of $6-15 per unit, could represent a significant additional finance mobilization, potentially tripling amount of finance mobilized.
- Additional finance mobilization would result in:
  - Increased benefits flowing to stakeholders (including Indigenous Peoples and Local Communities)
  - Expansion and sustainability of mitigation action on the ground, and support for climate action
  - Long-term sustainability of ER Programs by being able to tap into carbon markets

Options for ERPA Flexibility

- Two options for ERPA flexibility could be used:

Option	Mechanism
Retained ERs	• Similar to February 2024 proposal. • Country is allowed to retain a certain volume of ERs for the purpose of monetizing them in the market. • Retained ER Volume to be proposed by the country and decided at the time of ERPA amendment. • The total Contract Volume would not be affected initially. • Explicit commitment to BSP adherence and demand-side integrity principles for Retained ER Volume. • Put Option as fail safe in case of failed monetization.
Floor price	• First piloted under the Initiative for Sustainable Forest Landscapes (ISFL) • Price offered by FCPF for Contract ERs effectively functions as a floor price. • Volume of Contract ERs available for monetization to be determined on case-by-case basis. • FCPF ERPAs provide for a ‘Third Party Offer’ (TPO) process. • TPO must comply with FCPF-approved demand-side principles, represents a robust and legally binding commitment, requires any TPO sale proceeds to be channeled through the BSP and reflects the Contract ER use modalities under the applicable FCPF ERPA. • FCPF CF retains a ‘Right of First Refusal’ • TPO sale volume would be reduced from Contract ER volume. • Put Option as fail safe in case of failed monetization.

Considerations

- **Disruption to REDD+ Countries**
  - Amendment of ERPAs could result in disruptions for REDD+ Countries that could affect the delivery of ERs.
  - However, ERPA amendments are required anyway to extend the ERPA term beyond 2025
  - Potential disruptions could be mitigated by only allowing REDD+ Countries that have received at least one payment from the FCPF, to benefit from the additional flexibility.
- **Tranche A and Tranche B**
  - If only one Tranche decides to allow additional flexibility in its ERPA, this would require CFPs to accept the Trustee to follow a ‘notional approach’ in the management of the pro-rata share of Tranche A and Tranche B.
- **Benefit sharing plan**
  - A REDD+ country requesting ERPA flexibility will be required to commit to channel any related revenue from the sale of such ERs in accordance with the BSP (similar to ISFL).
  - This requirement would be included in those amended ERPAs.

Considerations

- **Demand-side integrity**
  - The Bank actively supports a well-functioning and trusted global carbon market.
  - Demand-side integrity requirements **cannot be imposed on the monetization of Excess ERs that are not part of this proposal**, e.g., Excess ERs generated under current ERPAs.
  - FMT proposes the following actions:
    - **Agree on an FCPF CF position regarding demand-side best practices** for monetized ERs and make these publicly available
      - A draft set of best practices for CFP consideration is presented in Annex B of the FMT Note.
    - **Inclusion of requirements regarding demand-side integrity for monetization of Excess ERs generated as a result of additional flexibility**
      - Restrictions are likely to affect demand and pricing.
    - **Provide REDD+ countries with capacity building on demand-side integrity to support their monetization efforts**
      - This support is likely to include in-country workshops and technical assistance. These activities are closely linked to FMT Note 2024/2, *Enhancing Country Access to Finance.*

Options for CFP consideration

Option	Pros	Cons
1. Status quo	• No ERPA amendment. • Guaranteed payment for delivery of verified ERs	• No additional climate finance mobilization for the ER Programs and communities • Perceived unfairness since countries with ERPAs that already contain flexibility can access carbon markets • Lost opportunity to pilot carbon markets as part of FCPF. • Impact on long-term sustainability of ER Programs
2. ERPA Flexibility	• Additional climate finance mobilization for ER Programs and communities • More countries are able to pilot access to carbon markets early on. • FCPF can support actively country access to markets. • 'Exit strategy' for ER Programs beyond the FCPF Carbon Fund. • Newly uncommitted funds could be used to support programs that are not able to access markets or to increase the number of ER Programs that the FCPF CF (or SCALE) supports.	• ERPA amendment could cause disruption in countries (mitigated through the conditions on next slide) • Reputational risk linked to monetization of FCPF ERs in markets (mitigated through the conditions on next slide).

Conditions on ERPA Flexibility

- Should ERPA flexibility be approved by CFPs, REDD+ Countries would need to comply with the following criteria
  - The REDD+ country must have gone successfully through the first reporting, verification, and payment process;
  - Readiness for international carbon market transaction – existence of regulations (if necessary), or that the pilot would contribute to the development of regulations for international carbon market transactions, or that the lack thereof would not limit the pilot, existing legal opinion on ER title transfer also applies to any Excess ERs;
  - The REDD+ country explicitly acknowledges that the existing BSP will be applied to proceeds from the monetization of 'released' Excess ERs and this is included in the amended ERPA;
  - The REDD+ country accepts demand-side integrity principles recommended by the FCPF for sale of 'released' Excess ERs and this is included in the amended ERPA;
  - Granting ERPA flexibility is subject to World Bank acceptance.

Decision

- **FMT is requesting CFPs to support a change in the portfolio management strategy** by considering country requests for additional ERPA flexibility as outlined in the FMT Note
- The FMT is not requesting any country-specific action or ERPA amendment; any such action will continue requiring CFP approval following non-objection or double 2/3 majority vote (Sec. 12.4(b) of Charter)
- Upon this approval, FMT would explore country-specific ERPA flexibility options and propose to CFPs amendments on a country-by-country basis.
- Approval of a change in the strategy will require a general and unanimous support (not tranche-specific) by all CFPs that will be recorded in the Chair Summary.

END OF DAY