Forest Carbon Partnership Facility

3c. Action Plan

Organizational Meeting of the Carbon Fund

Barcelona, Spain

May 31, 2011

FOREST CARBON PARTNERSHIP FACILITY

Outline

1. Setting goals
2. Pricing/Valuation Approach
3. Methodological Framework
4. General ERPA Conditions




Outline

1. Setting goals
2. Pricing/Valuation Approach
3. Methodological Framework
4. General ERPA Conditions




6-Month Goals

- Carbon Fund Participants
  - Agree ER-PIN template
  - Agree Carbon Fund Rules of Procedure
- Participants Committee
  - Shares/discusses draft policy guidance on Valuation/Pricing Approach with PC
- Facility Management Team
  - Shares draft Methodological Framework with PC
  - Proposes Readiness Package outline to PC

1-Year Goals

- Participants Committee
  - Finalizes Readiness Package guidelines
  - Agrees policy guidance on Valuation/Pricing Approach
  - Agrees Methodological Framework
  - Agrees guidance for PC assessment of Readiness Package
  - Agrees General ERPA Conditions
- Facility Management Team / Trustee
  - Signs Participation Agreements with at least 2 additional private Participants (depends on developments in REDD+ regulatory framework)
  - Signs Letters of Intent for between 1 and 3 ER Programs

3-Year Goals

- Achieve current capitalization target of US$200 million
- Sign at least 3 ERPAs
- Review and revise FCPF framework as necessary (i.e., Methodological Framework, Valuation/Pricing Approach, etc)

Outline

1. Setting goals
2. Pricing/Valuation Approach
3. Methodological Framework
4. General ERPA Conditions




Principles for Pricing/Valuation Approach

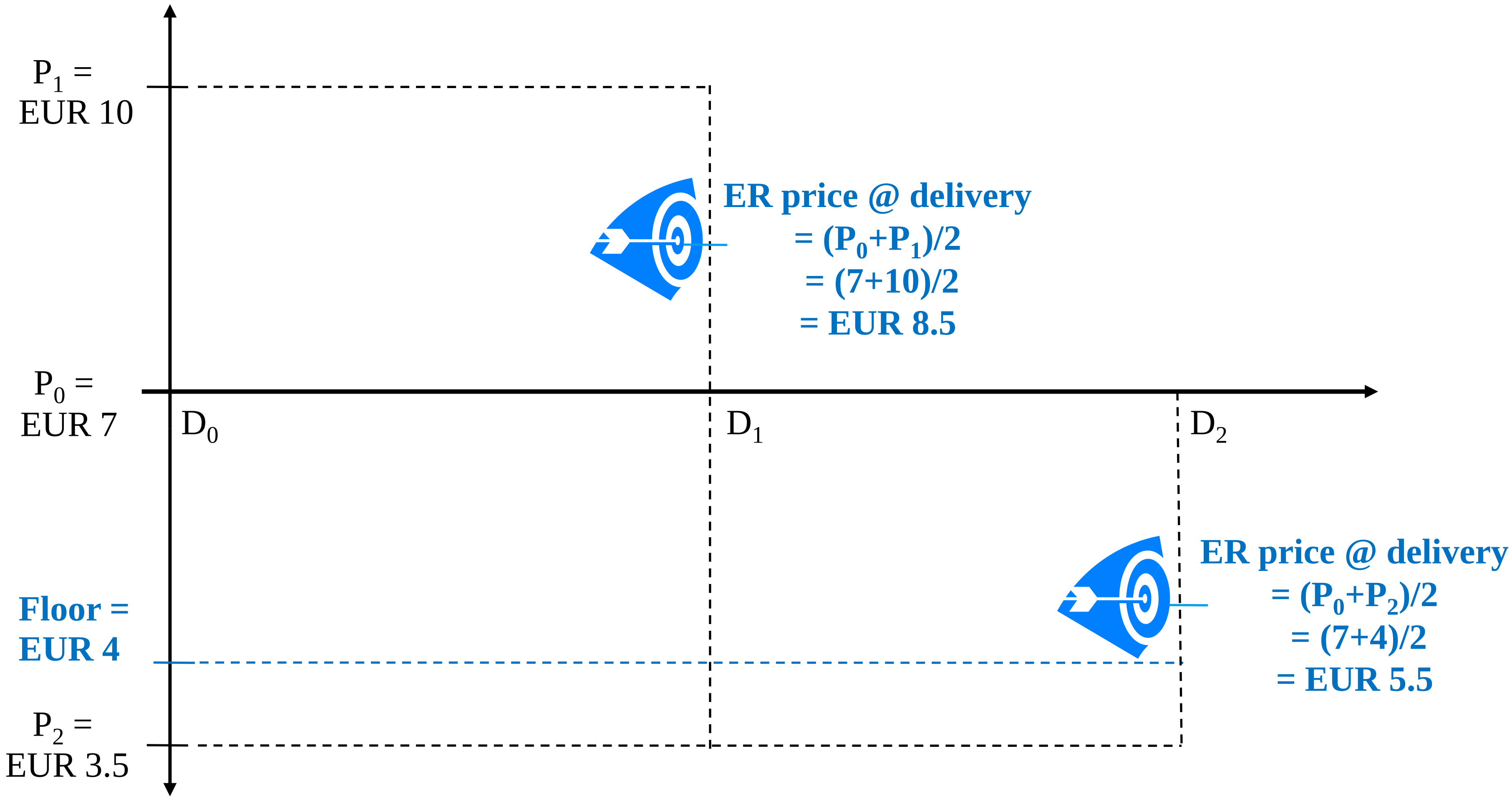
- The Pricing Approach should safeguard both buyers and sellers' interests in a reasonable manner
  - Should be transparent and reflect the transaction risk profile and the risk allocation between buyers and sellers in each transaction
- Should be simple (REDD+ is complex enough!)
- Choice between fixed or variable prices
  - May use both variable pricing components
    - Share some of the potential upside and downside in prices to reflect price fluctuations over time
  - Floor and ceiling prices can further reduce price fluctuation in the contract (upside and downside movements)
- Should include options for additional benefits (biodiversity, others)

Elements of Pricing/Valuation Approach

1. Identify Value Range or methods for fair value:
   - > Expected costs for achieving certain volume of Emission Reductions (sellers interest)
   - < opportunity costs for similar alternative Emission Reduction values (buyers interest)

2. Participants requested to have fair prices taking into account price development
   - Price Reference with Sharing of Upside and Downside
     - Select base price before first contract is signed
     - Seller and buyer share differences between base price and market price at time of delivery
   - Pros and Cons
     - *Pros:*
       - » Allows flexibility while limiting the exposure to price fluctuations
     - *Cons:*
       - » No guarantee against very large fluctuation
       - » Little predictability of fund flow

Example for upside/downside sharing



D0 = ERPA signature date **P0 = market price at ERPA signature**
D1, 2,… = delivery dates **P1, 2,… = market price each delivery date**

Pricing of Emission Reductions (1)

How is the reference price determined?

- Value identification can be either a market price (quotes or recent prices from similar programs) – preferred option
- In case there are no similar programs, auctioning of a part of the ERs might be a solution
  - If the ER Program is in the FCPF Carbon fund, FCPF participants are granted a discount
  - If the ER Program is outside the FCPF Carbon Fund, the auction clearing price serves as a market price indicator
- Value Determination:
  - Additional risk assessments based on quality of Program (likelihood of emission reduction)
  - Biodiversity and social additional values
    - Can be part of the FCPF price or paid by through other sources

Pricing of Emission Reductions (2)

- FMT circulates next draft version for Pricing /Valuation Approach
  - Peer review by ad hoc TAP and nominated experts
  - Open for public consultation
- Participants Committee: adopts policy guidance on pricing methodology
- FMT uses methodology for ERPAs:
  - FMT will interpret the policy guidance and propose price based
  - In terms of different views between buyers and sellers, FMT will arrange for a direct negotiation between seller and buyer

Outline

1. Setting goals
2. Pricing/Valuation Approach
3. **Methodological Framework**
4. General ERPA Conditions




Methodological Framework for Carbon Fund (1)

- Different types of ER programs can be submitted to the Carbon Fund
- Selection of ER Programs into the portfolio of the Carbon Fund will be based on selection criteria
- Use of a Standard can allow meaningful comparison between the different types of programs and helps to define quality
- But still the methodological framework should should allow enough room for testing and demonstration of country specific approaches according to national circumstances and priorities

Methodological Framework for Carbon Fund (2)

- Initially focusing on quantification of emission reductions, particularly:
  - Setting of reference emission level (REL) and/or reference level (RL)
  - Monitoring, Reporting and Verification of emission reductions
  - Minimization of the risk of displacement of emissions (leakage), reversals (non-permanence) and other relevant risks
- For other aspects, including safeguards, ER-Program is expected to comply with the World Bank’s applicable Operational Policies and Procedures.

Different Standards by Initiatives

UNFCCC

- SBSTA to develop modalities and procedures for REL / MRV
- SBSTA to develop guidance on risk of reversals and leakage
- Consideration at COP 17 in December 2011
- Based on IPCC good practice guidance and guidelines

California Cap-and-Trade Program

- Basic criteria for REDD programs defined in legislation
- Forest protocol available based on California Action Reserve (CAR) protocol, but only valid for activities in the US
- CAR is developing protocol with the state of Chiapas in Mexico

---

Governors' Climate and Forests Task Force

- Building a platform for state/provincial REDD programs
- Platform includes accounting and MRV
- Specific focus on links with the California system but the overall goal is that the platform can be used to build and enhance REDD+ programs that can access multiple market and non-market opportunities

---

Verified Carbon Standard (VCS)

- Developing new guidelines for Jurisdiction-Wide Accounting
- Balance the need for the VCS to set criteria with sovereign considerations of REDD+ design and implementation
- combination of developing best practices and/or procedural requirements along with minimum technical requirements

Proposed Use of Standards (1)

- Decision on a standard to be applied by the Carbon Fund will be needed
- Options: UNFCCC + the following:
  - Use one of the existing standards or initiatives
  - Develop a specific standard for the Carbon Fund (which could incorporate elements of other standards and initiatives)
- As part of this decision, Fund Participants and potential host countries of ER Programs might want to consider the objectives and scope of a Standard required for the Carbon Fund

Proposed Use of Standards (2)

- Standards can be stated as a set of principles which define the 'intent', and the desired outcome
- Once defined, principles can be translated into a set of criteria and/or indicators:
  - Criteria are the 'content' level of a standard that sets out the conditions which need to be met in order to deliver a principle
  - Indicators are quantitative or qualitative parameters that can be achieved and verified in relation to a criterion

Standards: Proposed Principles (1)

Completeness	Consistency
◆ Select the GHG sources and sinks, data, methods, criteria, and assumptions appropriate to the intended use of the reported information	◆ Use data, methods, criteria, and assumptions that allow meaningful and valid comparisons (both between programs and over time)
Accuracy	**Other principles?**
◆ Reduce bias and uncertainties as far as is practical ◆ The more accurate the estimate, the higher the potential value of carbon assets?	◆ Conservativeness ◆ Cost effectiveness ◆ Transparency ◆ Additional ◆ ……

Standards: Proposed Principles (2)

- Decide which aspects of the ER Programs are to be covered by Standards (limited to quantification of ERs only or should this be expanded to other activities, including quantification of other benefits?)
- What should be the principles that are the basis for the methodological framework for the Carbon Fund?
- Balance the need for harmonization vs the degree of flexibility to be allowed for testing and demonstrating different approaches
- Consider existing standards and initiatives where possible or should something specific for the Carbon Fund be developed and for what areas?
- Room for modifications of the framework as SBSTA work program on REDD+ evolves?
- Propose a process and timelines for development of a framework?

Outline

1. Setting goals
2. Pricing/Valuation Approach
3. Methodological Framework
4. General ERPA Conditions




General ERPA Conditions

- General Conditions for Emission Reductions Payment Agreements
  - Charter definition: a set of standard conditions applicable to all ERPAs, which sets out general rights and obligations of the parties to the ERPA
  - Section 11.1(g) of the Charter: PC approves the General Conditions
    - Types of ER's – tCERs, CERs, VERs?
    - Programmatic or project level?

THANK YOU!

www.forestcarbonpartnership.org