



## Forest Carbon Market Update

16 April 2009

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This is the second edition of TerraCarbon's Forest Carbon Market Update. The purpose of this report is to provide TerraCarbon's clients, partners, and colleagues with a short update each quarter on the key market developments in the rapidly evolving forest carbon sector. We appreciate your comments and suggestions.

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### U.S. Market Update

#### U.S. News- Waxman-Markey Bill Released

In late March, Reps. Waxman and Markey released a discussion draft of the much anticipated clean energy and climate change bill. The bill would establish a U.S. federal cap and trade program, and targets a 20% cut in U.S. emissions by 2020 and an 83% cut by 2050 (from 2005 levels). The cap would begin at 4.7 billion tons in 2012 and rise to 5.4 billion tons by 2016, as coverage increases from 68% to 85% of U.S. emissions. The bill would allow emitters to meet up to 30% of their initial compliance obligation with offset credits, of which 50% can come from domestic projects and 50% can come from international projects. However, as currently written, the bill would require emitters to submit 1.25 offset credits for each 1 ton of emissions (in effect, a 20% discount on offset credits).

In general, the bill is silent on the specific types of activities that would qualify for credits (to be determined by the EPA). However, credits from REDD activities would be explicitly allowed subject to certain conditions (e.g., bilateral or multilateral agreements with U.S. in place, measured against national baselines). In addition, REDD activities would be supported via an allowance set-aside (5% from 2012-2025, 3% from 2026-2030, and 2% from 2031-2050) designed to achieve supplemental emission reductions beyond those achieved under the cap. The set-aside could be used to support sub-national REDD activities for an initial period of 5 years, which would be subject to possible extension if the country is deemed to be making progress towards establishing a national baseline. The bill would also use proceeds from the strategic auction reserve (price containment mechanism) to support REDD activities.

Three other provisions of the bill are of interest to forest project developers. First, the bill's early action provision would require projects to start after 2001, and would allow credits only from Jan. 1, 2009 forward. Second, the early action provisions recognize only those projects verified against standards issued by U.S. states (e.g., RGGI and CCAR). Third, the bill calls for non-permanence to be managed through a risk-based reserve - similar to the VCS approach - with liability for intentional reversals.



## **Voluntary Market Update**

### **VCS Project Database and Registries Launched**

The VCS project database and registries are now operational, allowing registration and issuances of credits to the first VCS projects. At a conference in Washington D.C. on April 7, the VCS reported that 24 projects have been registered and almost 2 million tons of VCUs have been issued so far. As of April 7, the project database and registries showed that no forestry projects had been registered, although it may take several more weeks to work through the backlog of projects that are awaiting VCS registration.

### **ACR Forest Carbon Standard Issued**

The American Carbon Reserve (ACR) forest carbon project standard was issued in March. The standard was developed by Winrock International and seeks to build on other existing forestry standards by explicitly accepting methodologies and tools developed under the CDM, VCS, and CCAR as well as guidance issued by the IPCC and U.S. EPA. The standard covers AR, REDD, and IFM activities. Forestry projects can start as early as Jan. 1, 1990, provided other eligibility criteria are met. The ACR issues permanent credits to forest carbon projects, using a risk based buffer system like the VCS, but also permitting the set-aside of credits from non-forestry projects or insurance as alternatives.

## **International Market Update**

### **CDM Update: Two more AR projects registered**

The soil conservation project in Moldova and the Haryana small scale, reforestation project in India were registered under the CDM in the first quarter. These projects join the Pearl River Basin project in China as the only registered CDM AR projects. The Moldova project is expected to generate approximately 1.2 million temporary credits by 2012, while the Haryana project is expected to generate only 9,000 temporary credits by the same time. As mentioned previously, we expect the number of registered CDM AR projects to grow substantially this year, as more than forty projects remain in validation stage per the UNFCCC website.

### **EU ETS: Forestry Update**

The European Parliament voted in February to include forestry credits in the European Union's cap and trade system, the EU ETS. The vote called on the European Commission and European Council to consider market and non-market based mechanisms to fund forestry activities, and recommends developing pilot carbon markets for REDD projects. The European Commission has previously recommended that forestry credits be excluded from Phase II and III of the ETS. The European Commission has said that the EU position on forestry credits in future phases of the ETS will depend on the outcome of the post-2012 international negotiations. It is our view that provisions of a potential U.S. cap and trade legislation, which could permit forestry credits and place European companies at a competitive disadvantage to their U.S. peers, would place further pressure on the European Commission to review the EU's position.