Structuring PES Agreements

TRAINING COMMUNITY STAKEHOLDERS ON PAYMENT FOR ECOSYSTEM SERVICES (PES) IN UGANDA

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Presentation Outline

• Defining a Contract
• Major components of a Contract
• Major Considerations by the community
• The communities’ Obligations
• The potential legal obligations for land use changes
• Potential Risks with contract design
PART I:
FORMS OF AGREEMENTS

Defining a PES Agreement

PES Agreements are a form of business plans

• A formal statement of
  – a set of business goals
  – the reasons why they are believed attainable &
  – the plan for reaching those goals

• In this case, the business is to provide the ecosystem service that is the focus of the PES project
Defining an Agreement

- An Agreement:
  - An understanding between parties (individuals/groups) to follow a specific course of conduct/Actions

- The process of reaching an agreement
  - Actors: Number, level of homogeneity/heterogeneity
  - Opinion/action under consideration
    - Knowledge level for the actors
  - Duration over which the agreement holds

Types of Agreements

- ‘Handshake’ /Gentleman’s agreements
- Memorandum of Understanding (MoU) or Memorandum of Agreement (MoA)
- Legal contracts
- Customary law agreements
# Types of Agreements

## 1. A Gentlemen's Agreement
- An informal arrangement between two or more parties
- It may be written, oral, or simply understood as part of an unspoken agreement by convention or through mutually beneficial etiquette
- The essence is that it relies upon the honor of the parties for its fulfillment, rather than being in any way enforceable

## 2. A Memorandum of Agreement (MOA)/ Memorandum of Understanding (MoU)
- Written understanding of the agreement between parties to cooperatively work together
  - On an agreed upon project or meet an agreed objective
- It lays out the ground rules of a positive cooperative effort
- It is often used in cases where parties
  - either do not imply a legal commitment or
  - in situations where the parties cannot create a legally enforceable agreement
Types of Agreements

3. Legal Contracts
   – Engaging by written agreement/ Signing
   – A contract is a legally enforceable agreement between two or more parties with mutual obligations
     • enforceable in a court of law or
     • by binding arbitration

How does a contract look like?

• A few pages (5-15 )document
  – Depending on the extent of description of the different sections
• Commonly in a language well understood by the buyer and seller
  – Preferably translated in the local language for the benefit of the local communities
KEY CONTENTS OF A CONTRACT

- Date of Agreement
- Buyer details
- Seller details
- What the seller agrees to do
- What the buyer agrees to do
- Agreed upon definition of key terms
- Seller obligations
- Buyer obligations
- Payment conditions
- Verifications
- Seller’s Warranties
- Dispute Resolution
- Termination
- Variation
- Novation
- Risk & Uncertainty
- Signatories
- Schedules/Appendices
  - List of activities to undertake by the seller
  - Monitoring Requirements
  - Payment layouts
  - Declarations by the seller
  - Boundaries of the resource under consideration e.g., Land map
  - Monitoring requirements

PART II:
WHAT TO LOOK FOR IN A CONTRACT
What to look out for in Contract Design

- Document(s) for commitment
- Clarity of working terms/definitions
- The good/service to be traded
- The operational structure
- The Payment Structure = Fairness and Equity
- Monitoring, Reporting and Verification procedures
- Dispute resolution mechanisms
- Other Cross cutting considerations
  - Fairness - Equity
  - Flexibility - Pro-poor

Consideration 1: Type of Commitment

Form of Commitment

- Legally Unbinding
- Legally Binding

Between sellers = Association
- Lower chances to participate in formal markets

Between Buyers & Sellers = MoU
- Misunderstandings /Mistrust
- No mechanisms for enforcement

Between sellers = Contract
- High Clarity
- Reference points
- Co-benefits = capacity building

- Legal Counsel
- Time and Cost
Clarity of Key Terms Used

- Clarity on the terms used in the contract
  - Conservation measures
  - Carbon sequestration
  - Management practices
  - Monitoring requirements
    - Usually elaborated in appended lists = Schedules

Consideration 2: What is Traded?

- Ecosystem Service
- Environmental Service Provision e.g. Carbon sequestration, biodiversity conservation, watershed
- Land use/ Land use change e.g. Tree planting, forest protection, SFM

  - Risks to the supply the ES HIGH / LOW
  - Spatial extent of the ES provision points HIGH / LOW

  - Min carbon stock (tons/ha)
  - Level of species diversity
  - Management Practices
  - Regulated harvesting of Timber & NTFP
  - Soil conservation measures

  - Depend the market circumstances
  - Time lags BIG / SMALL

  - Min area (ha) planted
  - Forestry/Agroforestry
  - Management Practices
  - Rotation periods
  - Harvesting procedures

Fairness, Flexibility & Equity
Anticipated benefits/Associated costs
Consideration 3: The Operational Structure

Who are the Players?

Sellers
- One Sellers
- Several Sellers

Buyers
- One Buyer
- Several Buyers

WHO IS THE CONTRACTUAL BUYER AND SELLER? 

COMMUNITY MOBILISATION

For Aggregated sellers
- E.g. Private forest owners
- Different community forest owners’ associations

It will be of interest to clarify:
- Roles & Responsibilities of the individuals
- Management Structure
- Enforcement mechanisms
- Participation in monitoring
- Punitive measures for non-compliance within the seller category
Land-use Change Related Responsibilities & Obligations

1. Carbon Sequestration
   - Afforestation/reforestation on private land/degraded forest
     - Indigenous/Exotic spp
     - Land clearance
     - Planting
     - Re-planting/beating up
   - Afforestation/reforestation with trees that will have multiple benefits
     - Woodlots, agro-forestry & boundary planting
   - Appropriate management/silvicultural practices

Land-use Change Related Responsibilities & Obligations

1. Carbon Sequestration
   - Sustainable Management of Natural forests
     - Zoning/Management Plans
     - Avoided Deforestation/Degradation
       - Minimize activities
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1. Carbon Sequestration
   - Forest Management
     - Participate in monitoring of tree performance
     - Protect trees from fire, pests, disease, theft, sabotage, etc.
2. Biodiversity Conservation

- Protect the animals
- Protect the habitat
  - Living
  - Feeding
  - Reproduction

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Consideration 4: The Payment Structure

- Level of Payments/Contract price
  - Fixed vs Auctioned prices
  - For Aggregated sellers
    - Payment related to the levels of ES provision
      - Zoning/categorisation/stratification procedure
  - Who is negotiating the price (Market intermediary)
    - Ensure Openness, transparency and participation
      - Some individuals may consider the contract price as too low
      - Avail information of the market prices in the different markets e.g. Voluntary markets
      - Community members may attend some of the meetings of the buyers (if locally represented)
        » Better management of community expectations

Consideration 4: The Payment Structure

Form of Payment
- Cash/Direct financial payments (*currency?*)
  - Individual payments
- In-Kind Payments
  - Community infrastructural development
  - Recognition of rights
- Timing of Payments
  - After verification of monitoring targets at specified time periods
    - Milestone Payments
Consideration 4: The Payment Structure

- Management of payments for Aggregated sellers = CFOs, PFOs
  - Participatory benefit sharing arrangements
    - Cash benefits directed through microfinance schemes/Institutions
    - Decision criteria on who to pay how much
      - Incentives which are performance-linked
    - Reward for significant progress
  - Accounting Systems
    - Open accounts to manage funds
    - Preparing accounting, management & tracking systems for the project
    - Ensure clarity, transparency and accountability

Consideration 5: Monitoring, Reporting and Verification Procedures

- The set indicators
- Period of monitoring
- Consider:
  - Role players for enforcement, monitoring and reporting
    - Required skills = capacity building required
    - Tools and Equipment
  - Who does the verification
  - Associated costs
- Provision for adaptive
**Consid. 6: Re-negotiation of Contracts**

- **Supply Side:** Natural systems are dynamic
  - Uncertainties in forecasts *(associated costs and benefits)*
    - Quantities of the service to be provided
    - Response of the ES provision to the management activities undertaken
    - Community dynamics and other social/political factors

- **Demand Side:**
  - Price changes = economies/diseconomies of scale
  - Increases/decreases in market information asymmetry

**Consid. 6: Re-negotiation of Contracts**

- It is important to clarify the time and frequency

  **Realistically:**
  - Contracts should be for the first year’s commitment
  - Renegotiated at the end of YR 1 = multiple year contract
    - Pre-define renegotiation time points
Consideration 7: HOW TO HANDLE RISKS AND UNCERTAINTIES

- Outcomes due to e.g. fires, insect infestations, bad weather, landslides
- Strategies in place
  - Risk to be borne by a party better placed to manage it i.e.
    - A risk sharing format between sellers and buyers so that not all risk is borne by sellers & buyers
    - What are the Penalty provisions?
  - Where failure to deliver is due to acts of nature, war, Neither Buyer nor Seller shall be liable for any failure to perform its obligations

Consideration 8: Dispute Resolution & Termination of contract

- What happens at breach of contract (part of it)?
  - Dispute Resolution Committee
  - National legal system
    - Contractual disputes dealt with fairly and speedily
- What to do in case you want to end your contract before time = Termination
- What to do in case you want to re-do the contract = Novation
PART III:

POTENTIAL RISKS AND CO-BENEFITS OF CONTRACT DESIGNS

PES Contracts: Potential Risks

1. Confusion about what is being bought and sold
   - Marketing abstract ecosystem services
     • Asymmetric market information
   - Contrast cultural conceptions and economic models operating within traditional communities
     • Commoditization/Marketing of services that should not have a price tag attached
       – God (s) Given and Controlled = Spiritual attachments
       – Free for All
     • It is important to identify and consider these potential issues and “friction” points prior
2. Communities being tied into long and inflexible contracts
   • Hence, restricting their favoured land management practices
     – Need to speculate the potential future options that the sellers may wish to keep open

3. High Expectations
   – Confusion over resource and ecosystem service rights
     • PES projects DO NOT necessarily transfer resource rights

4. The Risk of Natural or Manmade hazards
   – E.g., fires, insect infestations, bad weather
   – Employ some type of insurance strategy
     • formal insurance
     • Informal procedures:

5. Levels of Participation
   • Participation in programmes/projects evolved to ensure that clients have a voice
     – and the information generated from activities is of use,
       • not only to managers/researchers, but also to clients/beneficiaries
PES Contracts: Potential Risks

9. Levels of Participation
   - Passive participation
   - Illicitive participation
   - Participation by consultation
   - Participation for material incentives
   - Functional Participation
   - Interactive Participation
   - Self mobilisation

Participation is concerned with:
   - Contribution
   - Involvement
   - Organization
   - Empowerment

Potential Co-benefits

1. Capacity building within the community
   - Training
   - Sharing of experiences in different fora

2. Increased group cohesion and collective decision making
   - Collective responsibility

3. Collective responsibility
   - Increased ownership and sustainability

4. Strengthening the rural peoples’ position in other resource-based negotiations
AGGREGATION AND PARTICIPATORY ARE THE KEY TO SUCCESS

THANK YOU