Contracting for Ecosystem Services

Slayde Hawkins
Forest Trends/Katoomba Group
Overview: Issues in PES Contracting

• Type of agreement
  o Purchase/sale of ecosystem service credits
  o Provision of ecosystem establishment, restoration or conservation services
  o Example: Trees for Global Benefits

• Finding the right level of formality and complexity

• Key elements of PES agreements

• Negotiating to get the best deal

• Special considerations for PES contracting
### Terminology

<table>
<thead>
<tr>
<th>Agreement ↔ Contract</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Parties</strong></td>
</tr>
<tr>
<td><strong>Rights</strong></td>
</tr>
<tr>
<td><strong>Obligations</strong></td>
</tr>
<tr>
<td><strong>Default</strong></td>
</tr>
</tbody>
</table>
• May structure PES contract as a purchase agreement or an agreement for the seller to provide services to support healthy ecosystems

usaha Purchase agreement – buyer pays for credits representing actual ecosystem benefits generated by seller’s project

usaha Services agreement – buyer pays for seller to take actions that are intended to lead to restoration, protection, or enhancement of ecosystem services
Purchase Contract for
Ecosystem Services Credits

• Purchase of **credits** for quantified ecosystem benefits that were actually generated:
  - VER (carbon)
  - Biodiversity offsets

• Payment depends upon proven, verified ecosystem outputs or results

• Used to **offset** buyer’s environmental impacts in concrete, quantifiable way
Contract for Services to Support Healthy Ecosystems

• Purchase of ecosystem conservation, restoration, maintenance services
  ß Tree planting
  ß Habitat protection
  ß Streamside restoration

• Payment depends upon verified provision of labor and/or raw materials (inputs)

• Suitable where contracted services are very likely to result in environmental benefits
Example: Trees for Global Benefits

- **Purpose:** removal of CO2 from the atmosphere
- **Mechanism/Activities:** Coordinated by ECOTRUST, 909 participants in Uganda’s Albertine Rift (1) plant trees, (2) implement agro-forestry, (3) practice improved forest management, (4) assist forest regeneration
- **Output:** CO2 credits, independently validated/verified by Plan Vivo & Rainforest Alliance, for up to 80,000 tons of CO2 per year

- **Validation** – Early assessment that project as designed is *likely to generate* claimed ecosystem benefits.
- **Verification** – Later confirmation that ecosystem benefits were *actually generated* by project activities

- **Buyers:** organizations or companies want to reduce carbon impacts for philanthropic or public relations purposes
The Contract: Level of Formality

- Ecosystem services agreements can vary widely in formality, length, and complexity

  - Formality generally increases: specificity, clarity, complexity, cost to negotiate and draft

  - Written agreements almost always required for PES
    - Important to minimize misunderstandings, reduce risk and overall costs
    - Absolutely necessary in well-established markets, as for carbon
Key Elements

• Clearly-defined rights & obligations
  - What is the ecosystem service?
  - What each party *must do, may do, may not do*

• Payment amounts, timing, based on:
  - Cost of providing services or creating offsets
  - Market prices
  - Risks for each party
  - Other costs allocated to each party

• Definition of and consequences for failure to perform
Negotiating the Contract

- Negotiation is a balancing act between getting the best deal and successfully coming to an agreement.
- PES negotiation issues and pitfalls:
  - Unequal bargaining power
  - Buyer’s lawyer represents the buyer, not both parties.
### Special Considerations

<table>
<thead>
<tr>
<th>Consideration</th>
<th>Potential Challenges</th>
</tr>
</thead>
<tbody>
<tr>
<td>Multiple sellers, community sellers</td>
<td>Coordination, benefit distribution, project governance</td>
</tr>
<tr>
<td>Monitoring</td>
<td>Balancing costs vs. need for accurate measurements and monitoring</td>
</tr>
<tr>
<td>Verification</td>
<td>Selecting the standards body, time, cost</td>
</tr>
<tr>
<td>Long-term obligations</td>
<td>Unforeseen ecosystem disruptions, sellers’ successors</td>
</tr>
<tr>
<td>Consequences of default</td>
<td>Small-scale seller inability to pay damages, buy replacement credits, etc.</td>
</tr>
<tr>
<td>Role of local, national government</td>
<td>Extensive state ownership/regulation of natural resources raises challenges for PES</td>
</tr>
</tbody>
</table>
Conclusions

1. Type of agreement
   a) Purchase agreement generally used for carbon, biodiversity PES – produces measurable outcomes that can offset other ecosystem impacts
   b) Services agreement may be suited to watershed PES, where certain upstream actions are almost certain to produce downstream benefits

2. PES agreement must be written

3. Basic elements of a PES contract are straightforward: (a) rights and obligations, (b) payment terms, (c) consequences of default

4. Yet, complexity arises because of:
   a) Complexity of underlying project and transaction – diverse costs and risks to be allocated between the parties through agreement terms
   b) Special considerations for PES projects, such as numerous participants, novelty of PES projects, and rapidly-evolving regulatory framework

For more information: www.katoombagroup.org/legal_contracts
THANK YOU!

Slayde Hawkins
shawkins@forest-trends.org