Contracting for Ecosystem Services

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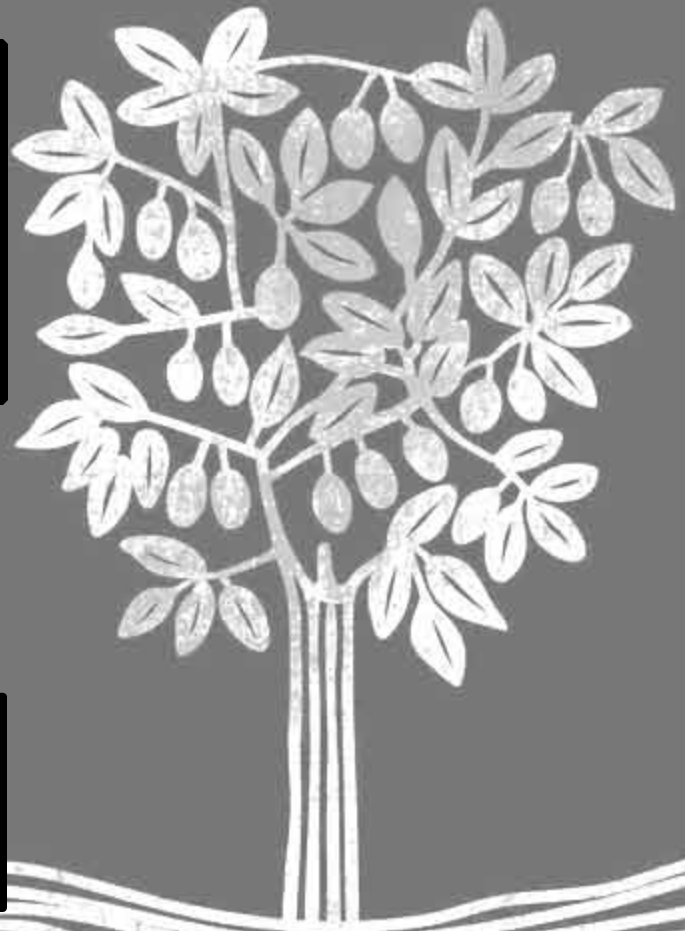


Overview: Issues in PES Contracting

- Type of agreement
  - Purchase/sale of ecosystem service credits
  - Provision of ecosystem establishment, restoration or conservation services
  - 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

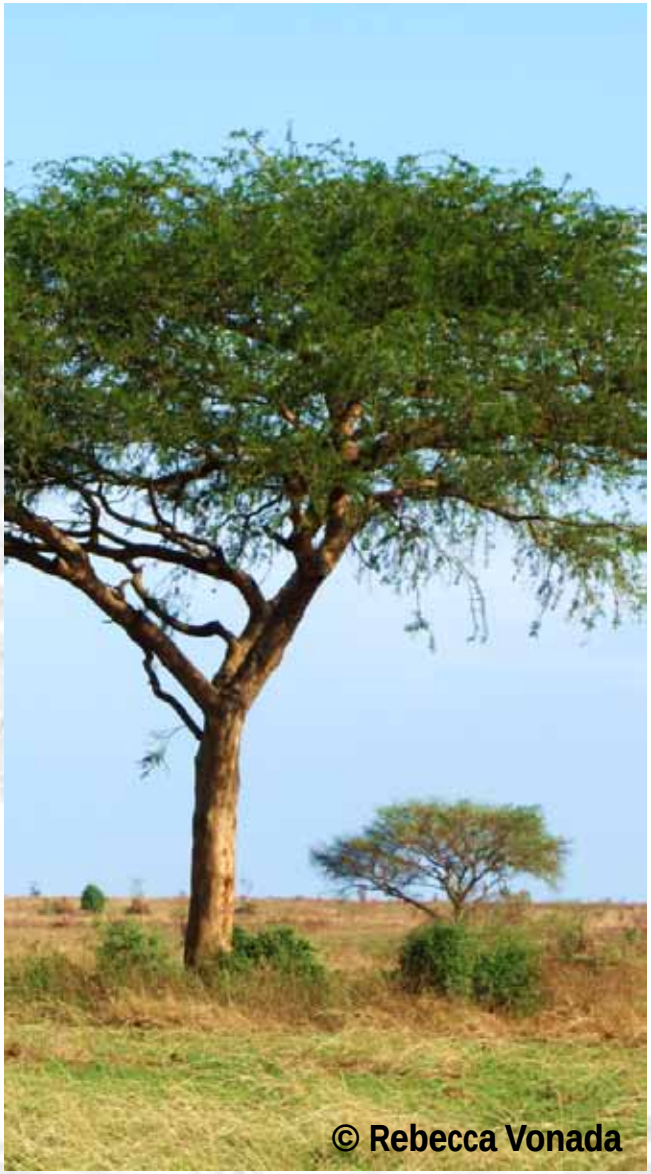
Terminology

Agreement ↔ Contract

Parties	The individuals or entities that agree to be bound by the contract terms by signing the contract
Rights	What an individual or organization signing the contract *may* do
Obligations	What an individual or organization signing the contract *must* or *must not* do
Default	Violation of the contract terms (usually defined in a written agreement)

Structuring the Agreement

- May structure PES contract as a *purchase agreement* or an agreement for the *seller to provide services* to support healthy ecosystems
  - **Purchase agreement** – buyer pays for credits representing actual ecosystem benefits generated by seller's project
  - **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**
  - § Tree planting
  - § Habitat protection
  - § Streamside restoration
- Payment depends upon <u>verified</u> 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

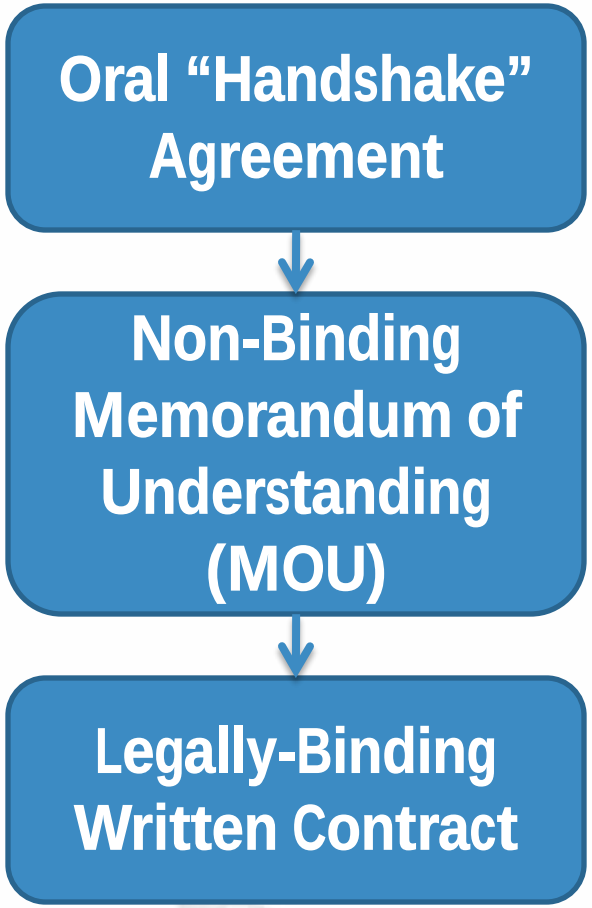
- **Purpose:** removal of CO2 from the atmosphere
- **Mechanism/Activities:** Coordinated by ECOTRUST, 909 participants in Uganda's Albertine Rift (1) plant trees, (2) implement agro-forestry, (3) practice improved forest management, (4) assist forest regeneration
- **Output:** CO2 credits, independently 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

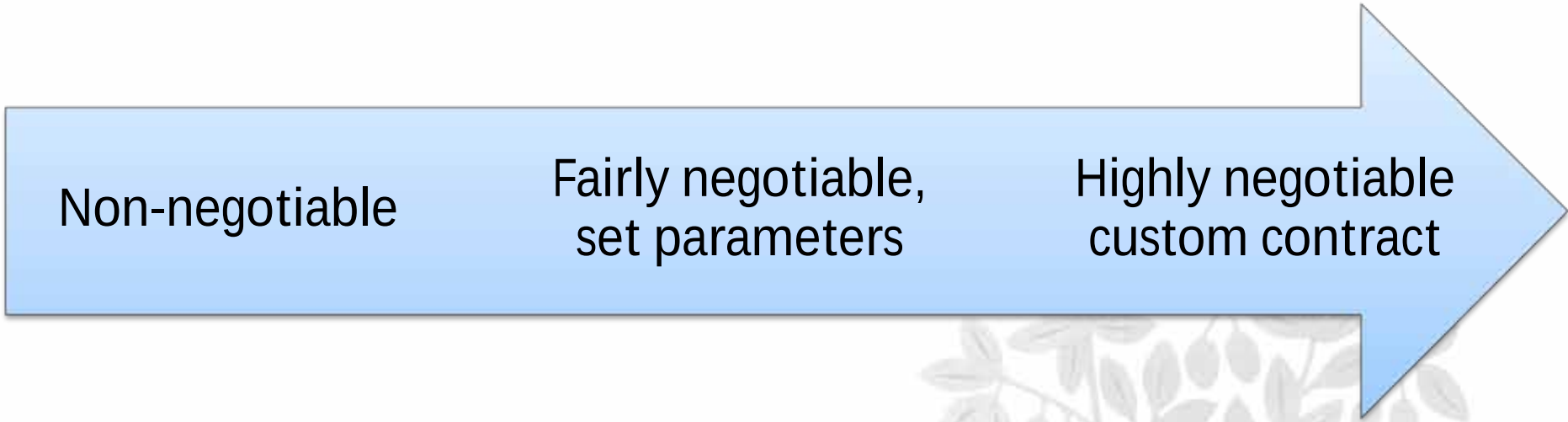


- Formality generally increases: specificity, clarity, complexity, cost to negotiate and draft
- Written agreements <u>almost always required</u> for PES
  - § Important to minimize misunderstandings, reduce risk and overall costs
  - § Absolutely necessary in well-established markets, as for carbon

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

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

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!

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