



## MEMORANDUM

**To:** Members of Working Group on Early Offsets Supply  
**From:** Nicholas Institute (Lydia Olander, David Cooley, Brian Murray, and Jan Mazurek)  
**Re:** Summary of discussion from the second call  
**Date:** 9/11/2009

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### **Summary of discussions from the second call**

#### *Cost Containment Uncertainty*

This issue was raised again on this call, because we didn't have enough time to discuss it sufficiently on the first call. The discussion centered on whether the amount of credits released from the strategic reserve should be increased if sufficient levels of offsets do not materialize. Most participants felt that this was not a necessary step to take and that adding another layer of complexity on how the reserve is administered would only add more uncertainty to the market. The point was also raised that increasing the release of credits from the reserve would require borrowing emissions reductions from future years, which could have near-term environmental consequences. Therefore, the participants felt that if this strategy is considered, it should only be used as a last resort, after all other cost containment strategies have been employed.

#### *Options for including additional pools of credits in early offsets projects*

The group discussed the potential for expanding the pools of credits available for offsets under RGGI and CAR before federal protocols are in place. The new CAR forestry protocols, issued on Sept. 1, 2009, include forest management and avoided conversion projects. Because these protocols are so new, however, their potential for supplying credits to the early offsets market is unclear. RGGI currently does not have protocols for avoided conversion or forest management. Neither RGGI nor CAR have protocols for agricultural soil sequestration projects.

Given the gaps in the existing registries an alternative approach for generating offsets during the transition to federal standards was discussed. The USDA could pay farmers directly for sequestration practices using offset credits. However, without an agreed upon



protocol for crediting practices this may still present uncertainty for participation and offsets until the agency or the Congress acts.

The group also discussed options for encouraging early investment in international offsets projects. Under Waxman-Markey, the United States must have a bilateral or multilateral agreement with the country where the project is located, which raised concern that it would take time to develop these agreements and slow the availability of CDM and REDD credits in the US market. Given that CDM is an internationally established and managed program, some suggested that CDM be allowed directly in the legislation, without the requirement for a bilateral or multilateral agreement. Others suggested that one MOU with the UNFCCC could satisfy the requirements and expedite the process, while still allowing for some control over the quality of credits allowed to be used in the US. It was also mentioned that direct linking of the US market to CDM may be complicated when it is unclear what CDM will look like after 2012 (in part because it reduces our negotiating options if this moves forward before Copenhagen).

The Working Group sees REDD as the most important early source of offsets. The approach in Waxman-Markey, in which baselines are established for each country or region, was seen as a good option, but it could take a lot of time to determine the baselines. Hurdles for early REDD offset credits in Waxman-Markey mentioned by the group included:

- the multi or bi-lateral agreements;
- the need for national or subnational baselines especially with 20 year targets for net deforestation;
- the 5 year limits on subnational and project based REDD; and
- country limits (which exclude major emitters<sup>1</sup>) from project based REDD.

Given that Brazil is the only country well positioned for national REDD baselines and it has been against selling these reductions for offsets, national crediting may take a while. Thus the group turned to project-based options for early offsets supply. One suggestion was to lengthen the crediting period to 8-10 years for project-based REDD to help with investment certainty. The possibility of removing country limits was also discussed since some are concerned about only high risk countries being eligible. However, looking at the list of ineligible countries (footnote 1), this may not be the case. (We will discuss more in our upcoming brief.)

Given the many potential hurdles for early REDD, an alternative was suggested. An early REDD pilot program similar to the proposal for domestic agricultural soil carbon, could be established. The EPA could buy REDD credits directly from countries for use in the US offsets market. These early credits purchased from investors could be held in reserve

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<sup>1</sup> Brazil, Indonesia, Malaysia, DRC, Myanmar (Burma), and Zambia. (Source WRI Climate Analysis Indicators Tool)



perhaps to help fill the strategic reserve and only released into the market if needed or they could be released directly. Again there is a question of where the early credits would come from. One possibility is that the EPA could take 1% from the 5% set-aside for the initial purchase of credits that could be repaid once the credits are sold in the offsets markets. (Again more discussion in upcoming brief.)

There was widespread agreement that the performance standards under Waxman-Markey would affect the supply of offsets from landfills and coal mines. These projects not only represent a significant pool of potential credits, but they are also among the highest quality offsets, in that additionality, leakage, and permanence are readily addressed. While it is possible that these sectors might still be able to generate offsets credits if they exceed the requirements of the performance standards, it was suggested that there would be little investment in projects before the standards are promulgated because of the uncertainty. Therefore, it was suggested that the performance standards could be delayed, and offsets projects from these sectors could be expressly allowed in the interim. It was suggested that a delay in promulgation of standards coupled with an early offsets pilot project could be a win-win in that offsets could be produced by sectors potentially covered by these standards in the early years of the cap-and-trade program, and EPA could use data generated by the offsets pilot program in determining how to set the standards.

### **Next steps**

Next week we will continue to research the ideas proposed in the first two calls and discuss possible topics for additional calls. We are currently considering a discussion of verifiers for early offsets and more in depth discussion of REDD. If you would like to propose an item for discussion regarding early offsets supply, please let us know. We are starting to draft a briefing paper based on these calls. Once we have a draft of that paper ready, we will distribute it to the working group, and we will convene another conference call to allow for discussion of the draft. We would like to schedule the next call for the week of Sept. 14<sup>th</sup>. Please let David Cooley ([david.cooley@duke.edu](mailto:david.cooley@duke.edu)) know your availability for the following times:

- Friday, September 18, 9:00-10:30am, eastern
- Friday, September 18, 11:00am-12:30pm, eastern

