

Forest Carbon Partnership Facility (FCPF) Term Sheet

DRAFT FOR DISCUSSION

Note: The Term Sheet lays out basic elements for establishing the FCPF. While the entire draft is open for discussion and subject to the Bank's internal approval, square brackets are used to indicate the need for more consideration or, in some cases, to show alternatives. Please note that a prospective participant should not rely on this draft Term Sheet for any decision to participate in the FCPF.

1. Objectives

The Forest Carbon Partnership Facility ("FCPF" or "the Facility") aims to assist developing countries in their efforts to reduce emissions from deforestation and degradation ("REDD") by piloting a system of policy approaches and positive incentives. The Facility would include two mechanisms:

- a "Readiness Mechanism" for providing technical assistance to the developing countries that participate in the Facility ("REDD Participant Countries") with the aim of building these countries' capacity to tap into a future system of incentives for the implementation of REDD programs of activities; and
- a "Carbon Finance Mechanism" for providing payments for emission reductions and associated benefits generated through emission reduction programs in selected REDD Participant Countries ("Pilot REDD Participant Countries").

2. Size

The Facility's two mechanisms referred to in section 1 are expected to be supported by two separate trust funds for which the International Bank for Reconstruction and Development ("IBRD" or "the Bank") will act as trustee.

The expected size of the trust fund for the Readiness Mechanism ("Readiness Fund") is US\$100 million with contributions expected from governments, public and private sector donors (together referred to as "Donors" or "Donor Participants").

The target size of the trust fund for the Carbon Finance Mechanism ("Carbon Fund") is US\$200 million. Contributions to the Carbon Fund are expected to come mainly from developed country governments, but also from other public and private entities (together referred to as "Buyers" or "Buyer Participants") acceptable to the IBRD. [As a condition for their participation, 2% of the contribution from Buyer Participants would be channeled to the Readiness Fund.]

The two funds would have opening, operational and closing dates. Once sufficient funding has been received for the Readiness Fund the Facility would become operational. It is expected that the minimum size for the Readiness Fund is US\$10 million and [US\$20 million] for the Carbon Fund. A Buyer which participates in the Carbon Fund [one year] after the fund is operational would make a catch-up payment [at the amount of X percentage of its Contribution.] Catch-up payment shall not be treated as part of the Buyer Participant's contribution to the Carbon Fund.

3. Operating Arrangements

- Once the Facility is declared open by the IBRD, the Readiness Fund and the Carbon Fund would start to accept participation from Donors and Buyers, respectively. After sufficient funding has been received for the Readiness Fund, the Facility would become operational, at which time the Facility would then be opened for participation by *Eligible REDD Countries* (Section 4).
- An *Eligible REDD Country* (Section 4) interested in participating in the Facility may submit to *the Secretariat of the Facility* (Section 5.5) a Readiness Plan Idea Note ("Readiness PIN") using a special template to be prepared by the Secretariat.
- Except for the *Interim Period* (Section 6), which follows a different process, *the Participants Committee of the Facility* (Section 5.2) would then review the Readiness PIN submitted and determine whether or not to accept the participation in accordance with the *Criteria for Selection of REDD Participant Countries* (Section 9). In case the Eligible REDD Country is accepted, the Secretariat, on the basis of the *Criteria for Budget Allocation for Readiness PIN and Readiness Plan* (Section 10) would allocate an appropriate budget from the Readiness Fund to the country in order to develop, on the basis of the Readiness PIN, a plan of action on REDD ("*Readiness Plan*") (Section 8). The country would then enter into a *Participation Agreement* (Section 15.2) with the Bank as Trustee for the Readiness Fund ("Trustee for the Readiness Fund"), and become a REDD Participant Country.
- After the Readiness Plan is prepared, the REDD Participant Country would submit such plan to the Participants Committee for approval. Upon approval, the Secretariat, in consultation with the Participants Committee, would then allocate budget for implementation of the plan.
- It is expected that the Secretariat would make arrangements to assist a REDD Participant Country to implement its Readiness Plan through working with the relevant entities of the Bank and other organizations.
- A REDD Participant Country would report to the Participants Committee through the Secretariat on the progress in implementing its Readiness Plan on a semi-annual basis or at any other frequency as necessary.

- Based on the reports, the Participants Committee would assess progress made on the implementation of the Readiness Plan. In the absence of guidance from the UNFCCC, the Participants Committee, upon request by a REDD Participant Country, on the basis of findings from an *ad hoc Technical Advisory Panel* (Section 5.4), would approve its reference scenarios, REDD strategy and monitoring plan.
- The REDD Participant Country may, at the time of submitting the Readiness Plan or during implementation of the plan, identify one or more potential Emission Reduction Programs (“Reduction Programs”) (Section 11) for the Carbon Finance Mechanism.
- The Reduction Programs would be reviewed by the Bank as the Trustee of the Carbon Fund (“Trustee of the Carbon Fund”) and forwarded to the *Buyer Participants Committee* (Section 5.3) under the Carbon Finance Mechanism for considerations.
- The Buyer Participants Committee may, based on the progress on implementing the Readiness Plan of the Reduction Programs in the REDD Participant Country, select one or more Reduction Programs from that country for a carbon purchase transaction, provided the reference scenarios and monitoring plan have been approved by the Participants Committee. The Buyer Participant Committee would then authorize the Trustee for the Carbon Fund to enter into an *Emission Reductions Purchase Agreement* (“ERPA”) (Section 15.3) either with the REDD Participant Country or with an entity approved by this country.
- Subject to independent verification, the Trustee for the Carbon Fund, would make payments to the party in the ERPA for the emission reductions (“ERs”) and other benefits generated by the Reduction Program. ERs would be delivered through the Trustee for the Carbon Fund, to the Buyer Participants on the pro rata basis.

4. Participants

The Participants in the Facility would be limited to:

- REDD Participant Countries (which (i) are Eligible REDD Countries; (ii) are selected by the Participants Committee or participate through the Interim Arrangement; and (iii) have entered into a Participation Agreement with the Trustee for the Readiness Fund. An Eligible REDD Country is defined as a Borrowing Member State of the IBRD or IDA that is located in sub-tropical or tropical region.)
- Donor Participants (which make at least the minimum contributions of US\$5 million to the Readiness Fund)
- Buyer Participants (which make at least the minimum contributions of US\$5 million to the REDD Carbon Fund and are acceptable by the Trustee of the REDD Carbon Fund)

5. Governance Structure

The governance structure for the Facility would include a Participants Meeting, a Participants Committee, a Buyers Participant Committee, and ad hoc Technical Advisory Panels established for specific tasks.

5.1 *Participants Meeting*

A meeting of all the Participants in the Facility would be held annually. The Eligible REDD countries that are in the process of preparing the Readiness PIN, the relevant international organizations, non-governmental organizations and private sector entities would be invited to participate as observers. The meeting would serve as a forum for exchange of information and experience.

At the meeting, the respective groups of the Participants would elect their representatives in the Participants Committee.

5.2 *Participants Committee (“PC”)*

Responsibilities:

The PC would be the Facility’s main decision-making body and would also provide guidance on policy issues on behalf of all the Participants. Specifically, it would:

- Select, in accordance with the Criteria of Selection of the REDD Participant Countries, an Eligible REDD Country to participate in the Facility by approving the Readiness PIN proposed by this country;
- Approve, on the basis of the findings of an ad hoc technical advisory panel that may be established by the PC for this purpose, the Readiness Plan submitted by a REDD Participant Country, and assess progress made in the implementation of the Readiness Plan;
- Advise the Secretariat on the budget allocation for implementing the Readiness Plan;
- Upon request by a REDD Participant Country which wishes to participate in carbon transaction and on the basis of the findings of the ad hoc Technical Advisory Panel, approve the reference scenario for its relevant Reduction Programs and monitoring plan;
- Prepare policy guidance on methodologies for price setting for ERPAs under the Carbon Finance Mechanism;

- In the absence of a mechanism from the UNFCCC, establish a list of independent verifiers for verifying ERs;
- Approve general conditions of the ERPA form; and
- Approve the annual budget proposed by the Secretariat for operation of the Facility (excluding the budget for Carbon Fund);

Composition:

[7] [6] members from REDD Participant Countries

[6] members from the Buyer Participants and Donor Participants

1 member from international organizations (IOs), 1 member of non-governmental organizations (NGOs) and 1 member from private sector entities would participate in the meetings as associate members but would not have voting rights. The respective groups of the IOs, NGOs and private sector entities would determine a process for selecting its representative as an associate member for participating in the meetings of the PC.

Decision making

Decisions by the Participants Committee would be taken by consensus, whenever possible. If all efforts at reaching a consensus have been exhausted and no agreement has been reached, decisions would be taken by [a simple majority] [a two thirds majority]. Each member of the PC would have one vote.

Recusals

A REDD Participant Country which is a PC member would recuse itself from taking part in any discussion and decision related to its own Readiness Plan and approval on its reference scenario.

5.3 *Buyer Participants Committee*

Responsibilities:

A Buyer Participants Committee would be established under the Carbon Finance Mechanism to make decisions on issues related to specific carbon purchase transactions. It would:

- Select Reduction Programs from a Pilot REDD Participant Country for a carbon transaction;
- Provide advice to the Trustee for the Carbon Fund on matters relating to carbon transactions and ERPA implementation;

- Determine the price for ERs generated from the selected Reduction Programs on the basis of the price setting guidelines provided by the Participants Committee; and
- Approve business plan and annual budgets for the Carbon Fund.

Composition

If the number of Buyer Participants is equal to or less than [seven], the Buyer Participant Committee would comprise all the Buyer Participants. If the number of the Buyers Participants exceeds [seven], the Buyer Participants Committee would comprise [five] members elected from among the Buyer Participants.

The REDD Country Participants and Donor Participants may elect a representative, respectively, as an observer to participate in the meetings without voting right.

Voting

US\$1,000,000 constitutes one vote and the decision is taken by majority

5.4 *Ad Hoc Technical Advisory Panel*

Ad Hoc Technical Panels would be established under the Facility for specific tasks in order to provide technical advice or information, including but not limited to: Readiness Plan, reference scenarios, monitoring plan, Reduction Programs, and social and environmental benefits.

5.5 *Secretariat*

Responsibilities:

The Facility would have a Secretariat to manage day-to-day operations of the Facility. The Secretariat would:

- Receive and screen Readiness PINs submitted by an Eligible REDD Country;
- Allocate, in accordance with the Criteria for Budget Allocation for preparing and implementation of Readiness Plan, the budget for a REDD Participant Country;
- Make arrangements for assisting the REDD Participant Countries implement their Readiness Plans;
- Provide Secretariat service to the Participants Committee and the Participants Meetings;

- Propose annual budgets for operation of the Readiness Fund and the costs for the Trustee of the Readiness Fund, activities undertaken by the Participant Meetings, Participants Committee and the cost of the Secretariat;

The IBRD would perform the Secretariat functions.

5.6 *Role of the Trustee*

The IBRD in its role as Trustee for the Readiness Fund would be responsible for administering the funds, providing financial reports, accepting participation in the Readiness Fund and managing contributions to the Readiness Fund.

The IBRD in its role as Trustee for the Carbon Fund would be responsible for managing the Carbon Fund, including administering the funds, providing financial reports, and accepting participation in the Carbon Fund, managing contributions to the Carbon Fund, facilitating the work of the Buyers Participant Committee, negotiating ERPAs, signing ERPAs, making payments under ERPAs, monitoring ERPA implementation and maintenance of ER registry.

The Fund Managers for the Readiness Fund and the Carbon Fund, respectively, and the Secretariat would be appointed by the IBRD. The Fund Managers would use the service of the Bank's Carbon Finance Unit and other units of the Bank for managing of the Facility.

6. Interim Arrangement

It is expected that a number of Eligible REDD Countries would participate in the Facility before the governance structure, in particular a Participants Committee, is put in place to perform the function of country selection. During the interim period, a Steering Committee consisting of Donor Participants, Buyer Participants, Eligible REDD Countries and other countries and entities invited by the Secretariat, would assess, in accordance with the Criteria for Selection of REDD Participant Countries, the eligibility of the REDD Eligible Countries which have expressed interest in participating in the Facility. To avoid conflict of interest, an Eligible REDD Country would not be invited to participate in any discussion or decision with respect to its participation in the Facility.

Once the REDD Participant Countries have reached [three] and at least there are [three] Donor Participants and Buyer Participants in the Facility, an organizational meeting of all the Participants in the Facility would be organized, at which the Participants Committee would be established and the Interim Arrangement would cease to operate.

7. Costs

Costs and expenses incurred in the administration of the Carbon Fund would be covered by the Carbon Fund. All other costs of the Facility would be equally shared between the Readiness Fund and the Carbon Fund.

8. Elements for Readiness Plan

A Readiness Plan would include:

- An assessment of historical emissions from deforestation and degradation;
- A projection into the future of emissions from deforestation and degradation based on a reference scenario;
- Design of a strategy to reduce emissions; and
- A monitoring system to observe emission reductions and identify any leakage.

9. Criteria for Selection of REDD Participant Countries

- [Being an Eligible REDD Country (Section 4)
- Relevance of the Eligible REDD Country (e.g. forest coverage, current and/or expected emissions from deforestation and degradation)
- Balance of three main biomes and geographic balance
- Ownership of national government of the Eligible REDD Country (including: (i) the Readiness PIN is submitted by the authorized representative of the national government; and (ii) an consultation process on the Readiness Plan has been conducted among key stakeholders.)
- Variety of approaches (e.g. testing of various methodologies to set reference scenarios and to provide incentives for reducing emissions from deforestation and degradation
- Availability of funding]

10. Criteria for Allocating Budget for Implementation of Readiness Plan

- The budget for implementation would be capped at US\$5 million but exceptions may be authorized by the Participants Committee based on justification by the Trustee for the Readiness Fund.

- The funding would be disbursed in accordance with milestones established in the Participation Agreement between the Trustee for the Readiness Fund and the REDD Participant Country.

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11. Emission Reduction Program (ER Program)

[ER Program is a set of measures, including policies and investments, selected by a REDD Participant Country to reduce emissions from deforestation and degradation.]

12. Limits on Liability and Indemnification

The IBRD and the staff members of the IBRD (collectively the “Indemnified Parties”) would be indemnified out of the Facility property against any loss, liability, cost, claim, action, demand or expense which any Indemnified Party may occur, except as may result from the Indemnified Party’s gross negligence or willful misconduct.

13. Trustee Withdrawal from Dispute or Claim

In order to avoid any potential conflict of interest between the IBRD and the IBRD acting as Trustees for the Carbon Fund, the Trustee for the Carbon Fund would not have any obligation to prosecute any default by a REDD Participant Country or the entity who is a party to the ERPA. In such case, the Trustee would seek to transfer of all or part of its rights and obligations to a third party acting on behalf of Buyer Participants in the Carbon Fund.

14. Duration of the Facility

The Facility would terminate on [December 31, 2020] unless otherwise decided by the Participants, subject to consent by the Executive Directors of the Bank.

The Facility would terminate upon resignation of the IBRD as Trustee for both Readiness Fund and Carbon Fund.

15. Legal Instruments

15.1 Charter for the Facility

The Facility would be governed by a Charter which would include, but not be limited to, all the elements described in this term sheet.

The Charter would also contain a number of annexes, such as

- Operating rules and procedures for the Readiness Fund
- Operating rules and procedures for the Carbon Fund
- Criteria for Selection of REDD Participant Countries
- Criteria for Allocating Budget for Implementation of REDD Action Plan by a REDD Participant Country

15.2 *Legal documents under the Readiness Fund*

- Participation Agreement between the Trustee for Readiness Fund and the REDD Participant Country, which includes:
 - Preparation of the Readiness Plan
 - Milestones for disbursement of funding
 - A timetable for implementation
 - The Trustee's remedies for fraud and corruption
- Participation Agreements with Donors
 - Contributions by the Donors in the form of the promissory notes
 - Reporting and auditing arrangements of the Trustee

15.3 *Legal documents under the REDD Carbon Fund*

- Participation Agreement between the Trustee for the Carbon Fund and the Buyer, including:
 - Contribution by the Buyer Participant in the form of promissory notes
 - Representation, Warranties and Covenants of the Buyer Participant
- ERPA (including General Conditions of the ERPA) between the Trustee for the Carbon Fund and a REDD Participant Country or an entity approved by the country ("Program Proponent"), including:
 - Program Proponent's obligation to deliver ERs and other benefits
 - Contract ER amount and delivery schedule
 - Conditions for payments
 - Default and remedies
 - Dispute settlement