Forest Carbon Partnership Facility

Carbon Fund: Pricing and Valuation Approach

Tenth Meeting of the Participants Committee (PC10)

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Carbon Fund Pricing approach and role of PC

- The FCPF Charter foresees in Section 11.1 (f) that the PC “adopts policy guidance on pricing methodologies for ERPAs”
- The goal set by the Carbon Fund Participants is that this would happen in June 2012
- This session presents some of the early thinking on the pricing approach although the end result might be different

Why is policy guidance on pricing required?

- REDD+ is new, few price references are available
- Voluntary forest carbon market has data, but generally small, project-based, transactions
- FCPF Carbon Fund is a different animal
  - Carbon Fund focus on a large scale e.g. administrative jurisdictions (national or sub-national) is an innovative approach and needs demonstration
  - Carbon Fund links ER Program implementation at sub-national level to national strategy and accounting systems
  - ER Programs can be a mix of policies and investments

Proposed steps in price formation

1 **Base Price**

- Determine Base Price (exogenous price reference)

2 **Adjustment**

- Determine any Price Adjustment (based on expected ER quality)

3 **Proposed ER Price**

- Compute proposed ER price

Price formation – Base Price

1 Base Price

- Based on external price references
  - Options
    - existing transactions, for example in voluntary market;
    - quotations by interested market players (e.g brokers);
    - auctioning?
- Can be based on price references at time of ERPA signing or at time of delivery of the emission reductions (or a combination)
  - Prices might differ over time, depending on progress of inclusion of REDD+ in different compliance regimes.
  - ERPA might have a variable model where the final base price is made up of the market price at different points in time
- Risks can be managed through price floors and price ceilings

Price formation – Adjustment

2

Adjustment

- Premium based on the quality of the emission reductions
- This quality could be determined through the application of the Carbon Fund methodological framework
- Can be a percentage or fixed amount

Price formation – Proposed ER Price

Compute proposed ER Price

Base Price

\+ Premium

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= Proposed ER Price

Price formation – hypothetical example (1)

1 **Base Price**

- Base price is set as the price reference at ERPA signing ($6)

2 **Adjustment**

- The quality of the emission reductions meets the minimum standards but no premium

3 **Proposed ER Price**

- Compute proposed ER Price = $6 + 0 = $6

Price formation – hypothetical example (2)

1 **Base Price**

- Base price is set as variable and is constructed as follows: 50% of price at ERPA signing ($6)+ 50% of price at ER delivery ($8)
- Base price therefore would be $7

2 **Adjustment**

- ER Program shows it is delivering high quality emission reductions which exceed the minimum requirements
- Premium is determined as 25%

3 **Proposed ER Price**

- Compute proposed ER Price = $7 + 25% = $8.75

Next steps

- Explore if the proposed approach is feasible or too complex
- Consider alternatives
- Determine how the approach would apply to different ER Programs
- Discuss how the different variables would be determined, for example how much should the premium be (if any)
- Working Group on methodology & valuation

THANK YOU!

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