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Submitted electronically to Jason.gray@arb.ca.gov and at http://www.arb.ca.gov/lispub/comm2/bcsubform.php?listname=sectorbased2015-ws&comm_period=1

RE: Next Steps for Evaluating the Role of Sector-Based Offset Credits Under the California Cap-and-Trade Program

Dear Mr. Gray:

On behalf of Friends of the Earth–US, this letter is respectfully submitted as a contribution to the development of socially just and environmentally effective climate policy in California. Our organization is grateful for the opportunity to submit this letter and the accompanying materials as documentation that will especially serve to identify and expose *inadequate risk analysis by state agencies* regarding potential establishment for new rules in the Cap-and-Trade Program. This material, as well as that which has been previously offered over the years in regards to the potential California adoption of a "Reduced Emissions from Deforestation and Degradation (REDD)" based offsets program, will serve ultimately to inform the development of truly just and effective climate policy for the State of California.

In brief, after assessment of the various types of risk associated with the potential role of International Forest Sector Based Offsets, or REDD, in the California Cap-and-Trade Program, it is clear that there exists an exceptionally high level of exposure of the program to a multitude of risk factors that will likely undermine the environmental and social effectiveness of the offsets program, and hence both the carbon market and the intended emissions reductions that are the primary objective of AB32. <u>It is also clear that the California Air Resources Board is not obligated or mandated in any way whatsoever to expose the residents of State of California to this risk.</u> In other words, there is no real viable *public interest* for which the State of California has to embark upon such a risky policy endeavor, especially when there

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are other more concrete and tangible means by which Californians and California industry can meet both mandated emissions reductions and stated tropical forest protection goals. It is particularly irresponsible to move forward with this policy proposal when unmanaged risk could result in severe implementation problems with, or even outright failure of, the offsets program, putting the entire Cap-and-Trade based climate policy of the State of California in jeopardy. *Considering the issues of risk as well as the complexities of rapidly evolving contextual dynamics in potential partner jurisdictions we consider that it is an imperative that there be a full and transparent discussion regarding the economic, social, and political contexts within which REDD based subnational jurisdictional linkages for offsets are proposed.*

Background

Friends of the Earth-US (FoE-US) is an environmental and social justice organization that maintains offices in Washington, D.C., and Berkeley, California, and which has members in all 50 states, including more than 70,000 members and activists in the State of California. FoE-US is a member of Friends of the Earth International, a global network representing more than 2 million activists in 75 nations. As an institution the organization has been an international leader in promoting innovative policy solutions for some of humanity's most pressing problems, including global climate change and tropical deforestation. As such we are honored to be engaged once again on this crucial issue regarding the future of California climate policy, and we are prepared to be involved as an informed stakeholder that can offer expertise and on the ground understanding as to what should be a robust and transparent debate regarding potential climate policy development. As the State of California searches for meaningful and effective means to meet our historic responsibility to respond to the challenges of the global climate crisis, our organization intends to be an integral part of that process. We believe our role is both as an expert stakeholder with experience and knowledge of the issues at hand, based on decades of work on international and domestic climate and forest policy issues, and as a government watchdog holding government officials and agencies accountable to the laws that guide the development of environmental policy and the rights to public participation in decision making.

Specifically, this letter offers comments on the State of California Air Resources Board (CARB) Staff White Paper *Scoping Next Steps for Evaluating the Potential Role of Sector-Based Offset Credits Under the California Cap-and-Trade Program, Including From Jurisdictional "Reducing Emissions From Deforestation and Forest Degradation" Programs* (hereafter White Paper). This brief letter also serves to provide insights and comments regarding the October 28, 2015 *Public Workshop to Discuss the Potential for Including International Sector-Based Offset Credits in the Cap-and-Trade Program* (hereafter Workshop), in which Friends of the Earth-US participated, both in person and remotely by webcast from San Cristóbal de las Casas, Chiapas, México. By means of the remote webcast participation from Chiapas members of Friends of the Earth International Amigos de la Tierra México, and

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allied community organizations such as el Movimiento REDDeldía also participated in the Workshop.

The submission of this comment letter does not mark the first instance in which FoE-US has engaged with CARB and the State of California on Cap-and-Trade climate policy, and specifically on proposals to include International Sector-Based Offset Credits in the California Cap-and-Trade Program. We believe that previous FoE-US comments provided in regards to the REDD Offsets Working Group Recommendations (see Appendix materials) are still salient and merit further review by CARB. These comments go into great detail, and contain citations to many relevant studies, both academic and based on civil society and market reports, in order to convey an understanding of the shortcomings of the REDD proposal to meet its stated social and environmental objectives. In seeking to ensure that California residents are fully informed of the risks inherent in the proposed policy, we recommend a full review of these comments and the literature cited therein.

Therefore, to avoid needless repetition of points made in other comment letters and through submission of evidence on previous occasions, we have provided in accompaniment of this letter an Appendix List cover sheet referencing those materials. We are also resubmitting those materials listed in the Appendix in PDF format. This material is submitted through the web portal, to ensure that CARB will integrate and make reference to those materials in future public and transparent discussion of these issues.

One concern that Friends of the Earth has not raised in previous interventions toward CARB is the fact that no distinction has been made in the materials developed by the REDD Offsets Working Group and now the White Paper developed by CARB, between "donor-based REDD," in which jurisdictions and communities are provided with clearly accounted performance-based payments, and "offset-based REDD," in which payments are based on the fluctuations of the carbon market. CARB's proposal is clearly for offset-based REDD, and yet there is in the White Paper and was in the October 28th workshop a deliberate and systematic conflation of these two very distinct climate finance mechanisms.

This letter itself, accompanied by the Appendix, will pursue a different approach than previous communication. Frankly, our organization believes it is imperative that the policy makers at CARB, as well as residents of the State of California, be made sufficiently aware of the diverse and exceptional risks that are associated with the International Forest Sector-Based Offsets proposal, and specifically with *Sub-national Jurisdictional "Reducing Emissions From Deforestation and Forest Degradation" Programs* (hereafter REDD). After participation in the Workshop, and after review of the White Paper, it is clear that the concepts of **risk,** and the rapidly evolving and very real on-the-ground dynamics of **conflict and controversy**, especially and specifically as they are associated with REDD and the potential establishment of rules regarding International Forest Sector-Based Offsets,

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are not being accurately portrayed by CARB staff in the discussion of potential expansion of the Cap-and-Trade Program. It is in the best interest of serving the State of California that our organization takes these steps to insure that the Chair of the Air Resources Board, the members of the Board, and the residents of California are fully informed as to the profound ***risks*** that are associated with the potential expansion of the California Cap-and-Trade program with the establishment of Sector-Based International Forest Offsets. The seriousness of the ***risks*** that this proposal represents to the reputation of California, to the eventual success of California climate policy in responding to climate challenges, and to the affected communities on the ground both in California and around the world who would be the most impacted by this potential policy expansion merits full and complete disclosure. With this letter we are raising concerns regarding the failure to accurately represent these risks in the White Paper and the initial October 28 workshop, as well as presenting to CARB staff a viable structure for assessment of this policy proposal, and we wholeheartedly encourage CARB staff to engage in a robust ***risk assessment*** of the proposed policy that is transparent and openly developed with a high level of public participation.

To achieve that goal, the remainder of this letter is divided into sections of risk that will assist in accurately outlining the dangers and pitfalls that this policy proposal represents, and that will also highlight the inadequacies thus far of the CARB staff approach to this policy debate. We encourage future staff discussion of this policy proposal to take this structure of breaking down the types of risk as a contemporary means by which to explore in an objective manner the potential costs and benefits of International Forest Sector-Based Offsets. Following in the main body of this comment letter are brief discussions of several of the most important and relevant types of risk to be understood when assessing the predicted exposure of the State of California to the risks that are an intrinsic part of carbon credits markets, especially one that attempts to expand into International Forest Sector-Based Offset credits. These risks can be mutually exclusive, or they can be overlapping and interactive with distinct negative feedback loops, and they include, but are not limited to: ***invalidation risk, economic risk, environmental risk, political risk, social risk, reputational risk,*** and ***legal risk***.

Invalidation risk

Invalidation risk is that risk specific to offsets and carbon credits markets that arises from instances in which offset credits are found to be faulty and/or fraudulent, and which require regulated entities to surrender replacement offsets for compliance, or in some other manner assume financial and legal responsibility for the faulty credits.

This is in basic terms the risk associated with the reversal of credits, when credits are associated with projects which are found to not be achieving their legally mandated environmental and emissions reductions goals, or to have violated other laws in an effort to meet those stated goals. The CARB White Paper and Workshop

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participants fully failed to articulate that the California carbon market is currently under tremendous pressure due to exposure to *invalidation risk*. A news report from October 14, 2015, was explicit in containing a statement from a representative of a company that develops offsets that "(Y)ou can trace limited demand [for offsets] almost entirely to invalidation risk" (see http://www.eenews.net/climatewire/2015/10/14/stories/1060026292).

The issue of *invalidation risk* as an undeniable reality that permeates the California carbon credits market, and thus the entire California Cap-and-Trade Program, is a dynamic that was for the most part ignored in the Workshop. However, the issue of risk is mentioned briefly in the White Paper, in one instance on p.29, when reference is made to the "invalidation of credits that fail to meet program requirements" as being evidence of the need to "spread risk through an insurance or buffer mechanism." The White Paper fails, however, to recount the recent history of invalidated credits in the California offsets markets even though a historical recounting of this evidence would be fundamental to understanding what the financial and political impacts of invalidation could be for the meeting of environmental and emissions reductions goals, as well as the clearly negative impact of *invalidation risk* on the carbon credits markets in California, as well as on offset project developers and stakeholders in foreign jurisdictions whose livelihoods are directly impacted by REDD offset projects (cf. social risks, below).

From a perspective of equity and justice in California climate policy, and specifically in the expansion of the Cap-and-Trade Program into International Sector Based Offsets, it is quite worrisome that the White Paper is explicit in making the recommendation, upon analysis of the admitted difficulties in insuring that environmental management and social safeguard protection capacity is in place in partner jurisdictions, that "partner jurisdictions should clarify that liability of the REDD program remains with them and not California." This statement can be interpreted as an admittance of the expectation of credit invalidation arising from the REDD program, and at the same time it is a clear effort of California to ultimately pass that liability and associated *invalidation risk* on to the very communities and threatened forests that this policy is purported to be designed to support.

Economic risk

Economic risk is that risk which is financial in nature and which can be associated with the economic losses that may arise from events directly connected with other risks described here. REDD poses economic risks to many stakeholders, from the project developers, compliance entities and California government, to the forest-dependent and indigenous communities that become subject to the relevant policies and policy implementation.

The most basic of understandings of markets includes recognizing their inherent volatility, a volatility to which carbon markets, with all of their complexities, are especially vulnerable. This presents a constant and never-ending

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economic risk due to the potential for changing market values to incur loss on specific market stakeholders, or the market as a whole. This *economic risk* permeates all market based climate policy whose mandated end goal is to reduce emissions, resulting in a threat to the permanence that in theory should be underlying all policy intended to implement laws designed to protect California residents and businesses from the negative impacts of climate change. As such, the *economic risk* creates *environmental risk*, which creates an avalanche effect in other risk categories.

The White Paper recognizes and confirms that this risk exists, and suggests that buffering of the risk is possible through a credit buffer or the use of insurance policies. Given the socio-economic contexts in which REDD projects are developed, the use of political risk insurance may insulate California from economic risk, but it does nothing to mitigate the risks to project stakeholders in local jurisdictions – thus leading to potential exposure to additional social, environmental, legal and reputational risks. Indeed, a 2012 paper entitled "Precedent-Setting Insurance for REDD Project in Cambodia Raises Concerns" (see Appendix), examines the Oddar Meanchay REDD project in Cambodia, which is referred to in the White Paper, and finds that political risk insurance "protects foreign investors against the potential for Cambodia to rightfully fulfill international climate change commitments… this, when combined with inherent weaknesses in the REDD model, may lead to perverse results in which the project's stated beneficiaries may not benefit – and some may even become entities that trigger the political risk insurance."

The White Paper also neglects to address serious questions about the long-term effectiveness of these buffers—for instance, how long would insurance remain affordable for carbon markets once insurance claims start being made on invalidated credits? The White Paper also fails to address the *market signal* that is made by the admittance of this very real liability, and fails to address the impacts that this growing atmosphere of risk surrounding the carbon credits market will have both on the market and on the ability of the market to contribute in a meaningful long-term way to the reduction of emissions.

Lastly, in a series of instances where projects have been advanced, REDD has proven to be expensive to implement (see Appendix List item I.FoEInternational_The-great-REDD-gamble.pdf), and the *economic risk* that is inherent in these sorts of "aid" programs could also have a very negative economic impact on the market, as well as undermining the stated environmental goals of reducing tropical deforestation. Clearly the issues of *economic risk* merit far more discussion than was granted in the White Paper or the Workshop, and they most certainly are serious enough that policy makers may see the wisdom in abandoning the proposed International Forest Sector Based Offsets expansion based on an objective assessment of *economic risk* alone.

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Environmental risk

Environmental risk is in this instance that risk which is associated with the failure of policies or projects to meet their stated environmental protection and emissions reductions goals, due to failed program design or due to extenuating circumstances on both a local and global level, both in California and internationally.

The question of *permanence* is one that the White Paper and the Workshop both struggled immensely to address in an adequate manner. This conundrum of *permanence* is not due strictly to the nearly insurmountable challenge of establishing a factual and reliable baseline for the current status of forest conservation and the current rate of deforestation and forest degradation in the partner jurisdictions, an issue that was brought up during the workshop and that has been discussed in previous comments presented to the CARB on this issue. The complex interrelation between human economic activities combined with global and local climate change impacts presents a series of *environmental risks* to an International Forests Sector-Based Offsets program. Note that storms, fires, drought, and other amplified disturbance regimes associated with changing climatic patterns are the source, in and of themselves, of tremendous stress on communities and forest landscapes in the partner jurisdictions. As well, forest ecosystems are by their nature highly dynamic systems, and since time immemorial primary tropical forest ecosystems have been host to very complex carbon cycles that have never been and never will be static in the way that the quest for permanence in the offsets program seemingly desires. The analysis of *Environmental Risk* and the issues of *permanence* merit much closer scrutiny than the CARB staff have provided up to this moment in both the White Paper and the Workshop.

Questions regarding baselines and permanence are important, as they do raise important doubts as to the promised benefits of an offsets program of this nature. For instance, the perverse incentive of markets on REDD projects has been identified as an *environmental risk* factor in the manner in which the markets can encourage the maintenance of a certain rate of deforestation to increase the likely returns on the offsets, a complication that is exacerbated by the fluctuations in deforestation rates due to market and political factors entirely beyond the control of the program. The scientifically questionable strategy of using forest carbon sequestration as a means of compensating for the ongoing burning of fossil fuels, which results in a number of atmospheric contaminants that forests can do absolutely nothing to alleviate, is a very serious *environmental risk* that remains unaddressed by CARB and the California Cap-and-Trade Program in general.

Another issue of *environmental risk* is that of *additionality*, which is the difficulty in guaranteeing that new credits are based on forest protection efforts that would clearly not take place through conservation strategies already being implemented or forecast for implementation in partner jurisdictions. This concern is addressed in depth in various materials cited in the appendix; notably, *additionality*

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is also a serious legal concern, given the UNFCCC requirement that all offsets be real, verifiable, and additional.

After reviewing the White Paper and attending the Workshop presentations it is very clear that far more discussion needs to be given to the jurisdiction level carbon density mapping methodology as proposed in the White Paper and the Workshop. It seems highly improbable that carbon density monitoring at this scale can be accurate in measuring on the ground realities regarding forest protection and reduced emissions from deforestation. On repeated instances CARB has received information illuminating the dangers of exotic species plantations for palm oil or wood products to tropical forest conservation as the means by which such "green desert" plantations can be calculated to be serving as a carbon sink, even though they are a prime motor of tropical forest loss and also are not in any way a permanent, presenting a very high *environmental risk* to the stated goals of reducing emissions and protecting forests. Yet the issue of exotic species plantations and their threat to tropical forests in the potential partner jurisdictions was not substantially addressed in either the White Paper or the Workshop. It remains totally unclear exactly how the subnational jurisdictional scale carbon density based monitoring, review, and verification methodology will provide assurances that recently established exotic species plantations are not being included in carbon density measurements. Another example of *environmental risk* that was not addressed in the White Paper or the Workshop, and one that is specific to potential linkage with Central Kalimantan, Indonesia, is how much risk exists due to the increasing occurrence of unprecedented human disturbance of tropical forest ecosystems such as with the fires currently underway in Indonesia. These fires, and the associated deforestation, have largely been traced to failures in governance, which millions of dollars in REDD financing have thus far been unable to resolve. The absence of discussion of these contextual issues is evidence that *environmental risk* is not being addressed adequately by CARB in exploring this potential policy proposal.

Another question that begs transparent debate in the process evaluating whether or not California should move forward with rule making regarding International Sector-Based Offsets is predicting the repercussions if, and when, it is discovered, whether through negligence or the inexorable pressure of extenuating circumstance, that partner jurisdictions have actually failed in the goals of maintaining or expanding carbon density at the proposed scale, or at any relevant scale. In the White Paper CARB has essentially stressed the importance for California that the liability for such potential invalidation rest with the partner jurisdiction, <u>which is essentially admittance that such reversals are likely</u>, and that California needs somehow to be shielded from the liability of that likely invalidation when it does occur. This logic serves to confirm in no uncertain terms the high level of *environmental risk* inherent in the REDD proposal.

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Another inadequacy of the White Paper and the Workshop in terms of describing *environmental risk* is the absence of discussion of the larger policy context permeating those jurisdictions with which California is considering making offset linkages. Though some of these policy developments can be seen on the horizon, others happen rapidly and may precipitate landscape level change in partner jurisdictions that is occurring faster than the State of California is prepared to anticipate.

For instance, significant in the consideration of the future management of natural resources in México is the recent passage in 2013 of a package of reforms regarding the governance of the state controlled energy sector in México, preparing México for an unprecedented influx of foreign investment in the energy sector, including from corporations based in California. This increase in government facilitated foreign investment in the Mexican energy sector is not just to be limited to fossil fuels development, even though that does create *environmental risk* regarding the efficacy of California climate policy in and of itself. More pressing for tropical forest preservation are the prospects for sudden and massive investment in hydroelectric development in many regions of México, including in Chiapas, which was not addressed even in passing within the White Paper. Important to understanding the global and local threat that is present in large-scale hydroelectric development in Chiapas is the increasingly robust body of science demonstrating that reservoirs from mega-dams, especially in tropical areas, are a significant emitter of methane, a shorter-lived but more powerful greenhouse gas than carbon dioxide. These concerns lead to a question that ought to be addressed fully and transparently in future CARB workshops: while developing jurisdiction-wide reference levels that require "own-effort" reductions before any reductions are credited is a positive approach, it is unclear how "Business-as-Usual" projections take into account the expanding GHG emissions specific to large infrastructure projects that are planned for all of the partner jurisdictions – all of which also have associated social impacts.

Parallel to México, the Brazilian Amazon is slated to be host to the development of literally dozens of new mega-dams, facilitated by federal and state agencies with the involvement of the private sector, yet the White Paper and the Workshop in no substantial way discusses the larger context of threats such as hydroelectric development to tropical forests, much less the impacts such development would have on longer-term permanence of reduction of deforestation and emissions on a jurisdictional level. *Considering these rapidly evolving contextual dynamics we consider that it is an imperative that there be a full and transparent discussion regarding the economic and political contexts within which REDD based linkages for offsets are proposed.* We are confident that an open and transparent debate of these issues will illuminate what the larger context implies in terms of the *environmental risk* of the offsets proposal, especially in regard of any actual permanence, or not, of reduced deforestation. Open debate will inform the assessment of risk and the ensuing impact on the California carbon credits market

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regarding *environmental risk* as negative feedback loops will precipitate issues with *invalidation risk* that would certainly begin to contaminate the stability of any explicitly designed insurance or buffering strategies to reduce liability, with deeper repercussions resulting in a predictable and increasing instability of the California carbon market itself.

Political Risk

Political risk is that risk associated with political changes in other jurisdictions, or in jurisdictions superior or even inferior to the subnational jurisdiction, in which the regulatory frameworks for offset programs and offset dependent activities are subject to political changes that negatively affect the validity of the credit and/or negatively impact the ability to meet stated objectives.

Though the White Paper and the Workshop placed a tremendous amount of hope in the prospects of California carbon market linkage with the Brazilian state of Acre, news reports on Oct 28 as well as an email question from a webcast participant in South America exposed the extreme *political risk* that the International Sector-Based Offsets proposal faces. In this instance, though there are issues of *environmental risk* due to the potential "double counting" of credits if markets in both Brazil and California were to commercialize credits from Acre, the most important contemporary issue to recognize is that extenuating political circumstances, specifically regarding the development of the national climate change policy in Brazil, are placing serious political impediments to the conclusion of a California linkage through REDD with Acre (http://www.bloomberg.com/news/articles/2015-10-28/brazil-deals-blow-to-schwarzenegger-championed-carbon-trade). In this news report Carlos Klink, the Secretary of Climate Change in the Brazilian National Environment Ministry, was quoted as saying that ***"securities generated by protecting the Amazon rainforest will be needed by Brazil to meet it's own emissions-reduction targets, and won't be sold to another nation or state."*** The lack of an adequate answer by both CARB staff and Acre state officials to this question as it was raised during the Oct 28 Workshop calls into question the seriousness with which CARB is considering political dynamics in other jurisdictions and their corresponding national governments, and how those dynamics directly impact the viability of the proposed offsets program. It also seems completely incongruent that the Federative Republic of Brazil would officially submit their Intended Nationally Determined Contribution (see Appendix) more than a month before the Workshop, yet the CARB was either unwilling to discuss this development, or was willfully obfuscating the news by not making direct reference to this clearly relevant political situation in any substantial way at all.

All of the above is evidence that there is a desperate need for informed, open, and transparent debate regarding this specific topic of tension between Brazil and California and the growing demand for potential REDD based credits in the State of Acre, as well as in regards to the diverse and multiple *political risks* confronting

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linkage with other jurisdictions as conflictive as Kalimantan, Indonesia; Cross River State, Nigeria; and Chiapas and others states in México. Acre is also host to a diversity of stakeholder positions regarding REDD, and there are critical voices that have documented the social and environmental inadequacies of REDD implementation in Acre, and which CARB must include in a transparent debate regarding this policy proposal (see Appendix Item A.acre_preliminary_report_green_economy.pdf). Essentially, each of the potential partner jurisdictions are recognized to present their own very unique and serious political challenges, several of which will be discussed in more detail in the following sections on *social* and *reputational risk*. The varied and multiple jurisdictional complexities create a risk laden political landscape in which California would have to be forced to respond in real time in order to manage political, financial, and public relations issues arising from events in these partner jurisdictions that will have a direct impact on the permanence of any potential offsets credits. It is easy to conceive of situations in which California is ultimately scrambling to attempt to control and mitigate exceptional market volatility arising from any potential offsets program that may find itself in turmoil, putting the entire Cap-and-Trade Program in jeopardy due to poorly understood *political risk*.

Social risk

Social risk is that risk to the well-being of affected communities associated with social conflict, human rights violations, political upheaval, the repression of political organizations and rights of democratic participation, the perpetuation of economic scarcity and poverty, and/or by the negative impacts from human caused climate change itself, as well as the other social, economic, environmental, and political challenges faced by affected communities in the partner jurisdictions in consideration, and which may fail to be alleviated or may even be exacerbated by policies such as REDD.

As provided in previous comment to the CARB, the research of Friends of the Earth International and others (see Appendix) has shown that REDD program implementation exacerbates preexisting tensions in forest communities due to conflicts with law enforcement, ongoing corruption, and unresolved disputes regarding land tenure. It is imperative that CARB provide transparent and equal opportunities to hear from affected communities that are critical of REDD in order that California residents be informed about the *social risk* inherent in an expansion of California Cap-and-Trade into Sector-Based offsets. Experience on the ground shows that a majority of local forest-dependent communities in every potential partner jurisdiction are already unstable and traumatized due to the circumstances of poverty, a repression of democratic processes, and historic conflicts with the states. To insinuate that REDD does not run the risk of exacerbating pre-existing conditions of conflict is to ignore both history and reality.

Another topic for transparent discussion is that of how exposure of affected communities to programs that rely on volatile carbon markets can result in elusive

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benefits for those communities. It is clear that artificial dependence on unreliable offsets payments promises more harm than good, which can increase social tensions as opposed to alleviate them. (See Appendix for numerous academic and civil society studies demonstrating this concern.)

In the place of a robust discussion of the real *social risk* associated with REDD in many of the jurisdictions in question, the White Paper mentions in passing the need for "extreme care" for working with affected communities. The White Paper goes on to express explicit concern about the need for California to choose to link only with jurisdictions that have "strict social safeguards in place," while fully failing to describe any sort of proposal for the development of the necessary criteria by which an accurate assessment of the efficacy of the "safeguards" can be made, or what would be the consequences of future failure to abide by these "safeguards." The White Paper does make the oblique admittance to the existence of real *Social Risk*, by again insisting that "partner jurisdictions should clarify that liability of the REDD program remains with them and not California," <u>which amounts to a confession that the failure of the social safeguards is to be anticipated</u>, and that California wants to insulate itself as much as possible from this anticipated failure of social safeguards in partner jurisdictions.

If the Workshop were to be taken as an example of how processes regarding REDD will take place on the ground in affected communities, the exclusion of diverse voices and marginalization of those who are critical of REDD is cause for great concern. The explicit exclusion from the Workshop panel of voices from affected communities who are critical of REDD was an unfortunate error that puts into doubt the commitment of the CARB to an open and robust debate of these issues. CARB will need to take immediate steps to include more diverse voices on the REDD proposal in order that the CARB and the citizens of California are properly and objectively informed as to the conflict and controversy that surrounds REDD based offsets programs.

Historically REDD has been criticized and even outright rejected by many affected communities in potential partner jurisdictions, and this controversy and conflict merits discussion within those communities as Free, Prior, and Informed Consent (FPIC) is a critical component to human rights issues associated with REDD implementation, as recognized in all relevant international norms. Failure for programs to abide by basic concepts of human rights and democratic participation, including the opportunity to have an opposing opinion without risk of assassination or disappearance, is to expose the development of a potential offsets program to severe *social risk*. (We recognize that this claim may appear alarmist; for documentation, see Appendix for current and prior submissions and news sources from Acre, Brazil and Cross River State Nigeria, specifically the cases of Ninawa Huni Kwi in Acre and Odey Oyama in Cross River State, Nigeria.)

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It is clear that CARB staff must be more upfront with the CARB board, decision makers and the public about the realities of conflict and controversy that surround REDD in partner jurisdictions. This includes a robust discussion regarding the current state of human rights in potential partner jurisdictions and what that implies for equity and justice, as well as environmental outcomes.

This discussion should also include an explicit and ongoing recognition of the difference in the implementation and outcomes between donor-based REDD programs and carbon-offset based REDD. The danger of the ongoing conflation by CARB between "donor based REDD," in which jurisdictions and communities are provided with clearly accounted performance-based payments and "offset-based REDD," in which payments are based on the fluctuations of the carbon market, is that the State of California intends to make a major policy decision based on an incomplete understanding and inadequate analysis of the history and development of REDD, and what that history implies for potential policy establishment in California.

Failure by CARB to be transparent regarding social conflict and the controversial nature of REDD offsets schemes in affected communities will only exacerbate the *social risk* that this controversy engenders. An analysis that is one-sided and attempts to "sell" a particular policy proposal while excluding critical voices will be incomplete, and thus does decision makers and public a disservice, even more so when the proposed program is not mandated by law nor an obligation that the State must fulfill by mandate. An analysis that ignores *social risk* only exposes the market to greater *economic risk* when predictable complications arise, such as further violation of human rights or the repression of democratic processes in the affected communities. Such repercussions create market instability due to *invalidation risk* and outright cancelation of credits, further jeopardizing an already vulnerable and volatile market as a whole, as well as promising failure to achieve the necessary action regarding climate change itself.

Reputational risk

Reputational Risk is that risk associated with the damage done to the reputation and "brand" of government institutions or business entities, and the individuals representing those entities, due to their direct or indirect association with partners who are revealed to have been involved with failed environmental policies, human rights violations, corruption, the exacerbation of social risk, and other public relations liabilities.

Though it may seem grotesque to discuss human rights violations in terms of how such violations can present *reputational risk* and negatively impact the "brand" of an entity, such as a State government or a transnational corporation, it seems to be necessary to open the discussion of *reputational risk* in just these terms in hopes that the gravity of human rights violations is fully understood by CARB officials. In essence, and what the State of California seems to want to ignore, is that human

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rights violations that have historically and are currently occurring in potential partner jurisdictions in México, Nigeria, Indonesia, and Brazil are oftentimes directly associated with issues that are an integral aspect of any potential REDD project, such as land tenure disputes or access to public participation and democratic processes. It is evident that a California REDD based offsets program could very easily find itself trapped in a public relations quagmire of human rights atrocities and corrupted democratic processes. In essence, the value of the "California effect" as a "brand" representing innovation and global leadership on environmental and climate policy is at risk of suffering irreparable damage because of the manner in which ongoing and persistent human rights violations in potential partner jurisdictions could become, speaking frankly, a public relations nightmare for the Cap-and-Trade Program.

Central to this *reputational risk* is the absence of an analysis, much less any recognition, of the existence of concerns regarding the human rights situation on the ground in potential partner jurisdictions, even when efforts are made to explicitly caution the State of California about these risks, such as was done with the letter of January 6, 2015 from civil society organizations in México to the CARB regarding specifically the crisis with human rights in México (see Appendix Item D.carta-ayotzinapa-california.1.5.15.pdf). This letter not only received no response from the CARB or the governor's office—*this letter and the documentation of historic and recent human rights violations in potential partner jurisdictions were apparently insufficient to merit mention in the White Paper, and were only obliquely discussed in the Workshop due to the raising of the issues in email questions by Workshop observers.* It was notable in the October 28 workshop that Sr. Hernandez, the official from Chiapas state, had no response to this concern.

In real terms *reputational risk* is not a liability that can be passed off to partner jurisdictions, in the market place of public perception doing business with partners includes the assumption of responsibility for public relations liabilities of those very partners, including any direct or indirect implication in violations of human rights, in corruption, or in otherwise anti-democratic behaviors. Damage to the "brand" of REDD is already extensive, further damage due to *reputational risk* will lead ultimately to the unleashing of an avalanche of negative feedback loops of *social*, *reputational*, *legal*, and *economic risks*, all of which cumulatively could have severe impacts on the efficacy of the offsets program, as well as carry significant environmental and economic consequences both locally and internationally.

It is worth mentioning that the offsets concept in itself carries with it a certain amount of *reputational risk* due to the questions of equity that accompany a scheme that is designed to protect businesses in California more than respond to the existential threats of climate change. The White Paper and the Workshop both could have been strengthened by a robust debate around the question of whether offsets divert attention in an obvious manner from California industries own responsibilities for climate change pollution. The manner in which the White Paper

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and the Workshop attempted to link causality for current drought conditions in California to tropical deforestation (White Paper, pp. 9-11) while ignoring historical and current industrial forest management issues in California has already created public comment in response to news coverage of the Oct 28 Workshop, in the form of a Letter to the Editor that raised the very question of "why would California not do more to address forest degradation at home if it is that the State desires to take innovative action in response to climate change and drought?" More *reputational risk* based on negative public opinion of the offsets program is guaranteed if CARB continues forward on the trajectory sketched out by the White Paper and the Workshop without building mechanisms for more robust debate about salient environmental and social issues, including that of human rights, into any potential rule making process.

Legal risk

Legal Risk is that risk associated with the financial costs, public relations liabilities, and political exposure that comes with facing litigation, and especially if litigation were to be successful and expose illegal actions on the part of a responsible agency, whether it be for reasons attributed to inadequate environmental review of a policy proposal or violations of the rights of public participation and access to public governmental information.

The White Paper and the Workshop both made mention of the process under which any potential rule making would take place, including analysis of any proposed rule under the auspices of the California Environmental Quality Act (CEQA) and the Administrative Procedures Act (APA). Questions have already been raised in this paper regarding the equity of participation in CARB processes regarding any potential rule. Since CEQA and APA describe regulations regarding not only the compliance of state agency decisions with adequate environmental assessment but also in terms of proper notification of the public and equitable public participation, it would be prudent for CARB to be highly attentive to exposure to *legal risk* in the California judicial system as any potential rule making for an offsets program proceeds. It would also be prudent for CARB to evaluate exposure to *legal risk* in any international forum that may be involved with litigation responding to any human rights violations in potential partner jurisdictions, especially related to issues associated with the implementation of Convention 169 of the International Labor Organization regarding the right of indigenous communities to Free, Prior, and Informed Consent (FPIC). Failure to correctly assess and plan for these legal responsibilities will have repercussions that jeopardize not only a REDD based offsets scheme but will undermine the entire California Cap-and-Trade Program.

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Recommendations for next steps

We offer the following list of items as recommendations for next steps in the evaluation of the potential role of International Sector-Based Offsets in the California Cap-and-Trade Program.

- The establishment of a publicly available, transparent, and contemporary risk analysis methodology for evaluating in both qualitative and quantitative terms the issues of risk described in this letter, as well as other dynamics of risk that come into view as the public and CARB staff identify them.
- An exhaustive and detailed evaluation, by an independent third-party, of the actual and perceived economic and environmental effectiveness to date of the California Cap-and-Trade Program, including an objective analysis of the role of offsets in the program to this point, and a robust evaluation of ***invalidation risk*** and the impacts that these dynamics have on the realization of the economic and environmental goals of the program as a whole.
- A transparent accounting of how stakeholders are selected for participation in CARB sponsored processes and events related to potential integration of REDD based offsets into the California Cap-and-Trade Program, including the use of public funds and staff time to facilitate participation in the Oct 28 Workshop, and any future events ostensibly designed to serve the public interest.
- The explicit inclusion of voices from potential partner jurisdictions that are critical of REDD into any publicly funded events, such as Workshops, briefings or hearings, to insure that residents of California are presented with a fair and robust debate about the costs and benefits of these proposed program expansions.
- Considering the high level of risk and the rapidly evolving and highly complex contextual dynamics surrounding the policy proposal, FoE-US considers it an imperative that there be a full and transparent discussion regarding the economic, social, and political contexts within which REDD based subnational jurisdictional linkages for offsets are proposed.
- We recommend the development of human rights and public participation criteria by which the State of California can evaluate the status of human rights issues on the ground in potential partner jurisdictions. It is imperative that the State make an informed and educated decision about whether the conditions are present in partner jurisdictions to assure that domestic laws and international treaties concerning human rights are being respected in said jurisdictions. This includes a set of steps to be taken for the severance of linkage when violations of these criteria occur. Organizations such as Amnesty International or Transparency International, amongst others, have proven methodologies for evaluating human rights that CARB would be prudent to integrate into the process evaluating the viability of a potential Sector-Based offsets program.
- Accompanying the development of this set of criteria is the development of a publicly approved plan as to how the State of California is prepared to

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respond and sanction partner jurisdictions in regards to human rights violations that occur in the future, including severance of any linkage.

- Before moving forward with any offsets program planning *Friends of the Earth US and allies demand a transparent and public answer to the Jan 6, 2015 letter* addressed to the California Air Resources Board Chair and the Governor regarding the perpetuation of ongoing human rights atrocities in México by local, state, federal and paramilitary forces, such as the crimes known as the Ayotzinapa Case of Sept 26, 2014, in which 6 people died and 43 students were disappeared. The Mexican national government has received international condemnation for the incompetent and willful mismanagement of the investigation into these crimes. This letter of Jan 6, 2015 was explicit in describing the need for the State of California to consider the human rights situation in México before moving forward with any possible linkage between California and subnational jurisdictions in México on climate change and carbon markets issues. It is imperative that an informed answer be provided to this letter.
- We recommend a full debate and consideration of the development and pursuit of alternative policies for the State of California regarding the stated objective of protection of international forests in response to the challenges of climate change. These alternative policies include the consideration of potential divestment and procurement strategies within the institutions of the State of California, as well as an assessment of opportunities to address the main motors of tropical forest destruction, which is the production and consumption of commodity goods such as palm oil, wood products, and petroleum, to name a few.

<u>Conclusion</u>

The primary purpose of this letter has been to present a stronger model for the evaluation of the potential role of an International Forest Sector-Based Offsets Program for the California carbon credits market. This model is based upon a detailed and complete assessment of the multitude of risks that are both directly and indirectly associated with such an offsets program. The White Paper and the Workshop were woefully inadequate in the presentation of issues of risk, and also fully failed to incorporate an assessment of how major developments in current international climate change policy, such as the Intended National Determined Contribution from the Federative Republic of Brazil, will impact the potential role of a REDD based offsets program in California. Considering such severe inadequacies in the work of CARB staff on both the White Paper and the Workshop <u>there are many indications that the conditions are not appropriate for California to be moving forward with the international forests sector-based offsets program</u>. We contend that the resources for developing any future REDD based offsets rule be redirected to more tangible and effective applications for the addressing of climate change issues in the State of California. <u>There is no obligation under any law or statute for the CARB to be developing such high risk policy as is the proposed International Forests Sector-Based Offsets</u>, and as such when a full consideration of the risks

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intrinsic to this proposal are assessed it becomes increasingly clear that there is no compelling public interest reason for continuing forward with this proposed offsets program. Barring the State righting course and abandoning this high risk and exceptionally complex policy development proposal, we believe that a robust, transparent, and democratic debate regarding a California REDD based offsets program, including the broad diversity of issues related to this policy development, will be more than sufficient to illuminate the need for the State of California to dedicate time and resources to more environmentally effective and socially just opportunities for responding to the existential threat of climate change.

Thank you for having considered these comments.

Respectfully,

Gary Graham Hughes

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