



Forest Carbon Takes Root in Uncertain Regulatory Climate

The regulatory market for forest carbon in the United States is, simply put, a mess. Rather than join the \$140-billion worldwide carbon markets by creating a unified system, the U.S. trudges along towards regional, state, and voluntary markets. Fortunately for most landowners the lack of a unified system isn't a hindrance.

Today's Landscape

While the rest of the world is taking proactive steps in places such as Australia, Canada, China, Europe, Japan, and New Zealand, progress is stalled in the United States. After the House of Representatives passed a nationwide cap-and-trade bill, the Senate failed to reach agreement.

Despite almost two-thirds of Americans (63%) supporting regulation of carbon emissions (June 2010 Wall Street Journal-NBC poll), the failure of Congress to enact legislation released a cloud of uncertainty that led many leaders to declare that a federal carbon-compliance system is dead.

What is certain, however, is that the U.S. Supreme Court's ruling in *Massachusetts v. EPA* [April 2, 2007] that greenhouse gases could be regulated under the Clean Air Act has put pollution regulation in the hands of the Environmental Protection Agency (EPA).

Currently, working through Congress and the EPA is how the Obama administration wishes to approach climate-change issues, as opposed to fighting in the courts, although lawsuits already are in progress and are likely to keep coming.

Looking down a double-barreled shotgun of EPA regulations and lawsuits, mega-polluters could find that a federal system might just be the preferable option.

But assuming that nothing happens on the federal level, regional, state, and voluntary markets will continue to grow to fill the void in carbon regulation. According to a Bloomberg News report citing U.S. Commerce Department data on November 24, 2009, in the U. S. already more than half of the economy (53%) and almost half of the population (49%) are covered by current or proposed carbon regulations.

Among these regulations are those established by the Regional Greenhouse Gas Initiative (RGGI), the first mandatory carbon market in the U.S. that includes the power companies from 10 states in the Northeast and California, which regulate emissions on a statewide basis. Following the regulatory path blazed by RGGI and California are the Western Climate Initiative, the Midwestern Governor's Accord, and Oregon.

Multiple Standards

Most (if not all) regulatory frameworks consider offsets (also referred to as "tons") within their own systems to be the best. This is to be expected since offsets serve the single purpose of controlling compliance costs. Consider that while the current cost of a "quality" offset is around \$6 per ton, the U.S. Department of Energy estimates the cost of reducing carbon at power companies using carbon, capture, and storage at some \$150 per ton of carbon.



Even more modest estimates from a February 2010 Point Carbon Research report suggest a price of \$42 per ton under regional markets, demonstrating the need for cost containment via offsets.

But what qualifies as a “quality” offset? After considerable time, money, and research, Finite Carbon recommends one of three major standards in the United States:

- The American Carbon Registry, which is part of Winrock International
- The Climate Action Reserve – formerly, the California Climate Action Registry
- The Voluntary Carbon Standard, an international standard that only recently started looking at forest carbon in the United States

It seems reasonable to expect that all three standards would qualify as compliance grade, if a federal standard emerges.

An EPA analysis of the American Power Act estimates demand at 600 million offsets per year with utilities alone requiring 300 million offsets annually. Our own analysis estimates annual supply at well below 10 million offsets per year. With that type of supply-and-demand imbalance, regulators may be forced to grab for everything they can.

Short-term vs. Long-term Market View

When the regulatory market sorts itself out during the next few years, the price of carbon is headed higher; the American Carbon Act even included an implied price collar — a minimum price of \$12 a ton and a maximum price of \$26 a ton, increasing on the high end to \$46 a ton by 2020.

Enrolling in a carbon market before the dust settles allows a landowner to grandfather a forest carbon project under one of the three standards that maximizes carbon revenue. And since offsets can be banked or sold at any time, a landowner accumulates offsets each passing year and can sell at the most opportune — or necessary time. Remaining on the sidelines is always an option, but participating now eliminates the risk of losing the carbon annually created from growth. The opportunity is real and can either be captured or missed.

What the carbon markets will look like in 10 years is anyone’s guess. But I’m sure that forests will still be standing, regulations will be clearer and, with a bit of preparation, forest owners will have a decade of timber AND carbon to harvest.

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