Testimony of Stuart E. Eizenstat[*]
"International Deforestation and Climate Change"
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Good morning, Mr. Chairman and members of the Subcommittee. Thank you very much for holding this hearing and for the opportunity to testify on international deforestation and climate policy. This is one of the most important aspects of the climate change problem and I commend you for your attention to it. The Senate Foreign Relations Committee can help create the bridge between domestic U.S. climate change legislation and the international effort necessary to deal with one of the greatest challenges of the 21st century. During my tenure as Under Secretary of State in the Clinton Administration, I led the U.S. delegation in the negotiation of the Kyoto Protocol. Forests were a major source of contention in those negotiations, and although we were able to get credits for afforestation and reforestation projects in developing countries, emissions from tropical deforestation were ultimately excluded from the Kyoto regime. But much has changed since Kyoto was negotiated, and the recent meetings in Bali put the deforestation issue squarely on the agenda of international climate policy -- providing a critical boost to efforts to fill the gap left open by Kyoto by bringing deforestation into the international climate regime. I believe that the US has a significant opportunity to lead on this issue -- in the international process but also, importantly, in the way that we design our domestic cap-and-trade system.

I currently serve on the advisory board of Sustainable Forestry Management and we have been working with the Environmental Defense Fund, the Nature Conservancy, Conservation International, Defenders of Wildlife, and the Wildlife Conservation Society as well as a number of major companies, including Shell, AIG, PG&E, AEP, and Duke Energy, to develop a Forest Carbon Dialogue that seeks to include domestic and international forest carbon provisions in U.S. climate legislation.

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I. Deforestation and Climate Policy

There are two important observations that must be kept in mind as we explore options for including deforestation in international and domestic climate policy.

1. The forest sector is a key part of the climate change problem. As some of you may know, deforestation -- almost all of which occurs in the tropics -- accounts for about 20% of global greenhouse gas emissions. That is more than the entire global transportation sector. Deforestation is the largest source of emissions in many developing countries – accounting for over 90% of the emissions from some key developing countries. Some of the world's top emitters, such as Indonesia and Brazil, have achieved their rank largely because of emissions associated with deforestation.

2. We cannot solve the climate problem if we do not include forests. Despite its massive contribution to global climate change, deforestation in developing countries is currently excluded from the international climate regime by the rules governing the first commitment period (2008-2012) under the Kyoto Protocol. This makes no sense scientifically, and it makes no sense politically or economically.

The scientific case for including deforestation in the effort to address global climate change is very strong, as articulated by the recent reports by Sir Nicholas Stern of the U.K. Government and the Intergovernmental Panel on Climate Change, among others. We simply cannot stabilize the composition of the atmosphere at anything remotely close to what scientists consider a prudent level if we leave 20% of global emissions out of the effort. In addition to the obvious climate protection benefits that come from reducing emissions from deforestation, protection of tropical and sub-tropical forests also generates significant social and environmental co-benefits, including the conservation of biodiversity (tropical forests are home to half of the world's terrestrial species), the maintenance of critical ecosystem services, and the protection of livelihoods for many of the world's rural poor.

The political case is equally strong: finding a way to bring deforestation and forest restoration into the climate regime offers the only meaningful path for many developing countries to participate in international efforts to deal with climate change, since regrettably they are opposed to economy-wide targets, even growth reduction targets, as we learned at Kyoto. And without developing country participation, there will not be an effective post-2012 international climate regime. Put another way, the forests issue provides a possible way to break the logjam plaguing the Kyoto process by creating opportunities for certain developing countries to receive tradable credits for reducing their emissions from deforestation. This, in turn, could serve as a model for similar approaches in other sectors, such as electric power or transportation, allowing developing countries to take important steps without having to embrace Kyoto-like economy wide commitments from the start, which is highly unlikely in the short term.

Bringing deforestation into climate policy also provides a possible linkage between a U.S. cap-and-trade program and trading systems in nations that are part of the Kyoto and post-Kyoto process. I believe it is unlikely in the near term that the U.S. Senate will ratify a climate change treaty without specific commitments from China and India, which they are unlikely to provide. Recognizing credits for reduced emissions from deforestation in evolving compliance regimes can therefore help bridge the divide with our international partners.

And, of course, the economic case for including deforestation in the climate regime is compelling given that this is a low-cost mitigation option that is available now, as both the Stern Report and the IPCC have noted. Accordingly, we should be developing mechanisms to take advantage of these reductions as we work toward the fundamental transformation of our energy system. From the U.S. domestic perspective, recognizing credits for reduced emissions from deforestation in our own cap-and-trade system could therefore provide significant cost-control benefits and much needed flexibility to regulated entities in the U.S., as they move toward adoption of low- and no-carbon technologies. Allowing regulated entities in the U.S. to satisfy part of their compliance obligations with international forest credits is like allowing them to design their supply chains in a manner that takes advantage of cheaper inputs. A key beneficiary is the U.S. consumer, who pays lower prices for the goods and services produced by these U.S. companies. Forest carbon is a critical part of the effort to control compliance costs in a U.S. cap-and-trade system.

Finally, efforts to bring international deforestation into the climate regime also have important synergies with efforts to promote and enhance adaptation to climate change in developing countries. Given the vital role of forests in providing environmental goods and services, recognition of credits for international forest carbon activities would generate numerous environmental co-benefits, including restoration of degraded lands and watersheds, improved habitat, reduced erosion, clean water, and enhanced ecosystem services -- all of which enhance the adaptive capacity of rural communities. Efforts to protect forests and promote sustainable forestry are also critical components of an effective strategy to reduce migration and conflict among vulnerable rural populations, thereby promoting environmental security. By channeling much-needed capital to the rural poor and providing incentives for them to sustainably manage their landscape, forest carbon credits could reduce pressures that lead to migration and conflict. Indeed, forest carbon credits provide one of the only means by which many of the rural poor in the developing world can stabilize their local forested environments and themselves adapt to climate change.

Simply put, we believe that reduced emissions from deforestation, together with efforts to plant new trees and restore forests, must be part of the solution to global climate change. It is certainly not the solution by itself, but we cannot achieve real climate protection without including forests.

II. Policy Options at the International Level for Financing Efforts to Prevent Deforestation

The current international policy debate has identified two main options for financing efforts to reduce emissions from deforestation:

1. An international fund (or collection of funds) that channels money to developing countries in order to finance forest protection efforts. This money could come from a variety of sources, including Overseas Development Assistance (ODA), carbon taxes,

emissions allowance auction revenues, or debt-for-nature transactions. The important point is that this would depend on public sector, government-to-government financing.

2. Market-based mechanisms that channel private sector capital to developing countries in order to fund forest protection efforts. The basic idea here is that existing and emerging cap-and-trade systems could be designed to recognize credits for efforts to reduce emissions from deforestation and thereby leverage potentially significant flows of private sector capital for efforts to reduce emissions from deforestation.

In evaluating these two options, several key points should be kept in mind:

<u>First</u>, in order to have a meaningful impact on the problem, significant and sustainable flows of capital must be mobilized. The Stern Review, for example, estimates that it would take between $5 and $10 billion per year to significantly reduce deforestation in developing countries. It is highly unlikely that ODA or some other type of public financing could realistically provide this level of investment on a consistent and sustainable basis over time. My view is that it cannot. Although multilateral and bilateral funding sources have an important role to play in this effort, we must harness the carbon market -- which doubled in size in 2007 to $60 billion -- as a vehicle for delivering capital on the scale needed to have an impact on the problem. Having a fund is not inconsistent with using market-based mechanisms. Both can play a role, but market-based mechanisms are far more powerful in leveraging private sector investment.

<u>Second</u>, regardless of which policy instrument (or combination of instruments) is put in place to deal with the problem, careful attention must be given to monitoring and quantifying changes in forest cover and forest carbon and to the development of appropriate accounting frameworks for measuring progress and ensuring environmental integrity. Without environmental integrity, the whole effort will collapse. In contrast to the situation prevailing a decade ago at Kyoto, significant progress has been made, particularly in the development of remote sensing capabilities and accounting methodologies, and in our ability to quantify changes in land cover and forest carbon stocks with confidence.

<u>Third</u>, deforestation cannot be considered in a vacuum and there is no one-size-fits-all recipe for solving the problem. Regardless of how the financing for reduced emissions from deforestation is ultimately designed, careful attention must be given to the promotion of policies and projects that will address the fundamental drivers of deforestation -- drivers that vary within and among countries. Integrated approaches will be necessary to provide meaningful and economically rational alternatives to deforestation, which means that we must look at afforestation and reforestation projects in addition to and as complements of avoided deforestation efforts.

III. The Current State of International Negotiations to Create Mechanisms to Prevent Deforestation

The 13th Conference of the Parties to the United Nations Framework Convention on Climate Change, held last December in Bali, Indonesia (COP-13), produced three major outcomes:

<u>First</u>, COP-13 defined a path forward for the negotiation of a comprehensive agreement to take

effect when the Kyoto Protocol's first commitment period ends in 2012. This is the so-called "Bali Action Plan." Notably, the United States joined the global consensus to launch this negotiation process.

Second, the developing countries assumed at least some qualified responsibility for reducing their own greenhouse gas emissions, within the context of their own economic development and with the assistance of wealthier countries. This is a significant development. It opens the door to an eventual agreement that will in some manner address the critical role of China, India and certain other G-77 countries that already are – and will be with further economic growth -- major contributors to climate change in the decades to come.

Third, and most significant for our purposes here, was the recognition by all countries that whatever climate change regime emerges in the next round of negotiations, it should include provisions for Reduced Emissions from Deforestation and forest Degradation (known as "REDD"). To that effect, the Bali Action Plan specifically references the importance of addressing, in the context of the post-2012 agreement, "policy approaches and positive incentives on . . . reducing emissions from deforestation and forest degradation in developing countries." This represents an important step in the direction of filling the gap left open by Kyoto and including deforestation in international climate policy.

Concurrently with the Bali Action Plan, COP-13 adopted a decision specifically on REDD, focusing on "approaches to stimulate action." This additional decision, which I will refer to as the "REDD Decision," calls for countries to undertake immediate efforts, including demonstration projects and activities, to begin to address the drivers of deforestation and to determine the efficacy of various different approaches. Those early efforts are meant to be taken into consideration - and, presumably, credited in a post-2012 regime - when the eventual framework on "policy approaches and positive incentives" is ultimately agreed.

Attached to the REDD decision is a set of principles meant to provide "indicative guidance" with respect to the nature and goal of these demonstration activities. Of particular interest is the question of precisely how these demonstration activities, if conducted at a subnational level, will contribute ultimately to the development of "national approaches, reference levels and estimates [of deforestation]." This, like many other methodological issues, will be addressed over the course of the next two years.

What is critical here is that the international community, as represented by the Parties to the Framework Convention, now clearly recognizes that efforts to conserve the world's tropical and subtropical forests must be part of any long-term global framework for climate change mitigation. This is due in no small part to the remarkable efforts of the Coalition for Rainforest Nations and their allies in putting this issue on the agenda. It is now clear that the developing countries that are the stewards of these tropical and subtropical forests are offering to take real and measurable action to reduce deforestation, provided that the international regime is designed to offer the right incentives for action. It is essential, therefore, that we provide these incentives, including in the United States in forthcoming climate change legislation.

With regard to specific policy instruments, the REDD Decision does not expressly endorse any particular approach and certain countries have thus far insisted that this decision be pushed to future meetings. It is also important to recognize that different countries and blocks of countries have endorsed different instruments for dealing with REDD. In our view, market-based approaches offer the most realistic opportunity for generating the scale of capital flows needed to make a significant dent in the rate of deforestation -- let alone the amounts required to actually reverse the overall trends and eventually to halt deforestation altogether. And the Bali Action Plan expressly calls for considering "[v]arious approaches, including opportunities for using markets, to enhance the cost-effectiveness of, and to promote, mitigation actions." Many participants in the negotiations have noted that the term "positive incentives" is generally viewed as encompassing market mechanisms. My view is that markets must play a fundamental role in developing an effective policy for reducing emissions from deforestation.

For the reasons that I have outlined, the Parties to the Framework Convention will almost certainly include efforts to reduce emissions from deforestation in the global climate change strategy that emerges over the next couple of years. I submit to you that this will be a very good thing, for the following reasons:

First, the enormous environmental significance of preserving the world's forests, from the standpoint of the avoided carbon emissions and the protection of the Earth's climate system as well as the conservation of irreplaceable biological diversity and protection of vital ecosystem services;

Second, the importance of having – for the first time -- the active participation by developing countries, such as those of the Coalition for Rainforest Nations, in the global effort to mitigate climate change;

Third, the importance of an avoided deforestation regime as a model for other developing countries to take targets in other sectors, such as electric power or transportation, if they refuse to take Kyoto-like, economy-wide commitments, which many will refuse to do in the near term;

Fourth, the contribution that this will make to the willingness of the United States and other developed countries to take on ambitious targets or goals -- knowing that all cost-effective alternatives are being explored and will eventually be available so long as they have environmental integrity; and

Last, but decidedly not least, the opportunities created by such an effort, if properly designed and implemented, for developing countries to forge an economic development path that is sustainable and consistent with the preservation of these vital natural assets. Significant incentives must be put in place to counter the existing pressures to cut and burn forests for agricultural expansion and other economic development.

IV. Opportunities for U.S. Leadership

The U.S. has a real opportunity -- in our domestic climate legislation -- to lead on the deforestation issue by including provisions that recognize credits for reduced emissions from deforestation in developing countries. Such forest carbon credits would provide much-needed flexibility and cost reductions for regulated entities under a U.S. cap and trade system, while incentivizing developing countries to take action to reduce emissions from the forest sector.

And this does not have to wait -- indeed it should not wait -- until a post-2012 agreement is negotiated and in place. My view is that Congress can design legislation that allows credits for reduced emissions from deforestation and other international forest carbon activities to be traded in a U.S. cap-and-trade system in a manner that ensures environmental integrity without imposing massive transactions costs on the whole effort.

To that effect, we are encouraged by the provisions in the current version of the Lieberman-Warner bill which allocate 2.5% of total emissions allowances to international forest carbon activities. We would like to see that percentage increase. But we also believe that the current provision that allows regulated entities to satisfy 15% of their compliance obligations with allowances from foreign greenhouse gas emissions trading markets should be expanded and opened up to explicitly include credits for international forest carbon activities. And we believe that there should be provisions in the bill that incentivize developing countries to move toward national accounting frameworks for forest carbon, and that credits from countries that adopt national accounting frameworks should not be subject to quantitative limitation. These provisions would give a huge boost to the whole effort to protect and restore tropical forests in developing countries and encourage those countries to participate in a global climate protection effort. They would also allow regulated entities in the U.S. to tap into the cost-control benefits of these activities, thereby reducing the overall costs of a cap-and-trade program to the U.S. economy.

We hope, therefore, that the members of this important subcommittee will recognize the importance of incorporating reduced emissions from deforestation in U.S. cap-and-trade legislation in a manner that comports with the ongoing effort to bring deforestation into the international climate regime.