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U.S. Government Announces Principles for Voluntary Carbon Markets

Principles Intended to Build High-Integrity Voluntary Carbon Markets

SUMMARY

On May 28, 2024, the Biden-Harris administration (the "Administration") released its Voluntary Carbon Markets Joint Policy Statement and Principles (the "Statement") setting out the U.S. government's approach to advancing high-integrity voluntary carbon markets ("VCMs"). The Statement was co-signed by the U.S. Secretary of the Treasury, the U.S. Secretary of Agriculture and the U.S. Secretary of Energy, as well as several senior White House advisors. The Statement advances the notion that VCMs can support decarbonization efforts within the United States and globally by unlocking capital and demand for real, additional, lasting, and independently verified emissions reductions and removals.

The Statement encourages the U.S. private sector and other stakeholders in the carbon credit ("credit") value chain to follow seven principles (the "Principles") when participating in VCMs. The Principles are designed to promote (1) integrity of credits (*i.e.*, supply integrity), including protections regarding climate and environmental justice, (2) credible credit use (*i.e.*, demand integrity), and (3) market-level integrity, including facilitating efficient market participation and lowering transaction costs. Although the Principles are voluntary, companies that participate or are considering participating in VCMs should review the Principles to better understand how the Administration intends to approach VCMs and its expectations for market participants.

SUMMARY OF PRINCIPLES FOR RESPONSIBLE PARTICIPATION IN VOLUNTARY CARBON MARKETS

Supply Integrity

- ***Principle 1*:** Carbon credits and the activities that generate them should meet credible atmospheric integrity standards and represent real decarbonization.
  - The Statement specifies that activities generating credits, as well as the credits themselves, should be certified to a robust standard, applying procedures that deliver on core integrity principles, including:[1]
    - additionality (*i.e.*, the activity would not have occurred in the absence of the incentives of the crediting mechanism and is not required by law or regulation);
    - uniqueness (*i.e.*, no double-issuance);
    - real and quantifiable claimed emissions reductions and removals, with activities designed to prevent emissions leakage;
    - validation and verification by a qualified, accredited and independent third party;
    - permanence of greenhouse gas benefits; and
    - robust baselines for emissions reduction and removal activities.
  - With respect to credit certification standards bodies, which register activities and issue credits on the basis of verification against standards and approved methodologies, the Statement outlines a series of criteria for ensuring credit integrity, including operating or using registries to track credits, having procedures in place to effectively address double-counting risks, and requiring publicly available information on crediting activities, among others.
- ***Principle 2*:** Credit-generating activities should avoid environmental and social harm and should, where applicable, support co-benefits and transparent and inclusive benefits-sharing. Developers should:
  - implement safeguards to identify and avoid potential adverse impacts on people and the environment, including those relating to local communities, land use and tenure rights, food security, nature and biodiversity;
  - proactively monitor and mitigate any adverse impacts that remain and seek to enhance positive impacts where appropriate; and
  - design and implement projects and programs in consultation (and, where applicable, in partnership) with relevant stakeholders.

Demand Integrity

- ***Principle 3*:** Corporate buyers that use credits ("credit users") should prioritize measurable emissions reductions within their own value chains.
  - The Statement emphasizes that VCMs should be used to complement within-value-chain emissions reductions.
  - The Statement references the Treasury's Principles for Net-Zero Financing and Investment, released on September 19, 2023, for further guidance on credible approaches to climate strategies that reduce value chain emissions.
- ***Principle 4:*** Credit users should publicly disclose the nature of purchased and retired credits.
  - According to the Statement, credit users should disclose purchased, cancelled or retired credits on at least an annual basis and include details that enable outside observers and relevant

stakeholders to assess whether such credits are of high integrity and avoid negative environmental and social impacts.

- The Statement enumerates examples of information that should be disclosed, including the relevant certification standard name, project name, project ID, host country, credit vintage, methodology and project type, as well as whether the credits met relevant third-party principles for integrity.[2]
- The Statement further notes that, in some cases, adherence to this Principle may involve voluntary public disclosures exceeding those required by applicable law.

- ***Principle 5*****:** Public claims by credit users should accurately reflect the climate impact of retired credits and should only rely on credits that meet high integrity standards.
    - For stakeholders that are developing frameworks for defining appropriate emissions-related claims, the Statement suggests that such frameworks should increase incentives to purchase high-integrity credits on an ongoing, regular basis without reducing incentives for companies to expeditiously pursue within-value-chain emissions reductions (*e.g.*, by allowing a company to count credits toward a portion of its Scope 3 emissions associated with science-aligned emission pathways where it would be unreasonable to expect the company to fully abate those emissions within a given timeframe).
    - In addition, emissions-related claims of credit users should rely only on the impact of credits that meet current high integrity standards at the time the claim is made and that avoid adverse impacts. Credited emissions reductions or removals that have been reversed, revealed as inflated or exposed as failing environmental or social safeguards should not be used as the basis for any claims unless remediation has taken place.

Market-Level Integrity

- ***Principle 6*****:** Market participants should contribute to efforts that improve market integrity.
    - The Statement outlines the expectation that, through collaboration among the private sector, civil society and the public sector, participants in VCMs will actively contribute to improving the integrity of the overall VCM, including by:
        - creating incentives to develop and purchase high-integrity credits;
        - improving transparency and the publicly available data of credit-generating projects and programs;
        - promoting fair and equitable treatment of suppliers involved in credit generation;
        - controlling for potential conflicts of interest among VCM service providers;
        - preventing fraud and manipulation by bad-faith actors undermining credit integrity;
        - providing for the appropriate accounting and legal treatment of credits and resolving any related ambiguities;
        - enabling global interoperability of relevant standards, market infrastructure and reporting;
        - supporting robust and equitable participation in these markets; and
        - taking other measures separate from credit and demand integrity to improve the functioning and health of these markets.
- ***Principle 7*****:** Policymakers and market participants should facilitate efficient market participation and seek to lower transaction costs.
    - According to the Statement, "[e]xpanding market opportunities for credible credit providers is an important component of the United States' climate strategy."

- This Principle focuses on the importance of addressing barriers (*e.g.*, high transaction costs) facing credit-generating suppliers and calls on policymakers and buyers to consider ways to enhance market certainty for credit providers undertaking long-term and often significant investments in decarbonization that plan to rely on VCM revenues to finance their actions.

OBSERVATIONS

Although the Principles are voluntary and do not create any new legal or regulatory obligations, they offer insights into the Administration's views on VCMs, as well as carbon credit markets more broadly, and measures that should be adopted to enhance their integrity.

As noted in the Statement, the U.S. government, including U.S. regulatory agencies, is playing an increasingly important role in carbon credit markets. For example, the Securities and Exchange Commission ("SEC") incorporated carbon credit disclosure standards into its recently adopted climate-related disclosure rules (these rules have been stayed by the SEC pending litigation). The federal banking regulators have proposed amendments to the regulatory capital rules applicable to large banking organizations (often referred to as "Basel III Endgame") to include a prescribed risk weight for "carbon trading" for purposes of market risk capital requirements. In addition, the Commodity Futures Trading Commission's ("CFTC") proposed guidance regarding the listing for trading of voluntary carbon credit derivatives by regulated derivatives trading platforms (designated contract markets). The CFTC also recently launched two enforcement-related efforts regarding VCMs: (1) a whistleblower alert to help the public identify and report potential violations of the Commodity Exchange Act connected to fraud or manipulation in the carbon markets, including manipulative and wash trading, "ghost" credits, double counting, fraudulent statements relating to material terms of the carbon credits and potential manipulation of tokenized carbon markets; and (2) the Division of Enforcement's establishment of the Environmental Fraud Task Force to investigate potential fraud and material misrepresentations and misconduct regarding environmental products and strategies.

Overall, the Statement highlights the Administration's view that VCMs—if developed responsibly with clear incentives and guardrails—can meaningfully contribute to decarbonization, while at the same time supporting economic development, conserving resources and biodiversity, and facilitating innovation in climate technologies. In accompanying remarks, Treasury Secretary Janet Yellen highlighted both the key role VCMs could have in the United States' efforts to reduce emissions through the use of private markets, and the importance of creating high-quality market mechanisms. John Podesta, Senior Advisor for International Climate Policy and a signatory of the Statement, stated that mobilizing "enormous amounts of private capital" is necessary to reach the Administration's net-zero goals, and that VCMs that adhere to the principles of high-integrity are one way to get "private capital off the sidelines."

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ENDNOTES

1 Elements such as additionality, permanence and robust quantification also feature in the quality standards of CFTC's proposed guidance.

2 The disclosures contemplated by this Principle are similar to those required under California's Voluntary Carbon Market Disclosures Act (AB 1305).

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