Input to VERRA's Stakeholder Consultation Process Relative to Capitalizing VCUs under the Paris Accord

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FURTHER SUBMISSION TO GOLD STANDARD APRIL 15 2021

There are a series of nuanced questions revolving around whether Corresponding Adjustments (CA's) under Article 6 of the Paris Accord (PA) are needed for private entities (not governmental signatories under the Accord) to apply voluntary credits issued in Paris-signatory countries in order to be able to make carbon neutral or net zero claims without the confusions and cross purposes of double counting. If the premise that double counting arises for private Carbon Neutral (CN) claims/VCU purchases under Paris is not carefully scrutinized and up-coming decisions are poorly framed, the recent significant expansion of private investment into VCU carbon project development and into carbon neutral/net zero investments risks serious decimation. Specifically, there needs to be clarity about whether double counting **does or does not** have material import for private entities' Carbon Neutral (CN) claims/VCU purchases under Paris. At stake is the future of the carbon capital markets, the extent of private parties' commitment to apply their capital to help mitigate climate change, the clarity of property rights which are essential legal underpinnings required for the viability of any financial capital market – and thus the financial contributions made by all private parties (other than the Paris country signatories) to help address climate change. So unless Paris signatory governments wish to rely entirely on their own governmental investment proceeds to accelerate state-of-the-art technology deployment in order to meet their Accord commitments (sometimes complemented by solely domestic private party investments), the contribution that international carbon capital markets could make to expand global climate mitigation would risk a decline to de minimis levels unless a new framework for the role of VCU credits, CA's and CN commitments is successfully clarified. These questions therefore require very careful nuanced consideration.

1. THERE IS NO DOUBLE COUNTING UNDER COUNTRY PARIS ACCORD REPORTING WHEN PRIVATE PARTIES PURCHASE/RETIRE VCU's FOR CARBON NEUTRAL PURPOSES

Definition: a private entity is an organization that purchases VCU's which is not a Paris Accord government signatory. Although the term "private" is used for brevity's purpose, such entities can comprise private companies, campuses (whether private or public/state), NGO's, individual, cities/states – that is all VCU purchasing entities other than Paris signatory governments

i) If a private party purchases a domestic VCU in a Paris Accord country to make a carbon neutral claim for emissions arising in that same country, then there is no double counting under the country's Paris Accord reporting since all transactions take place within the country's own emission-reduction accounting umbrella.
   - No CAs come into play

ii) Furthermore, there is also no double counting under a governmental reporting for the Paris Accord when a VCU is purchased from a project located in a Paris Accord signatory (host) country by a private entity seeking to make a carbon neutral claim whose emissions arise in another country.

- This foundational insight is illustrated best by initially assuming that the project host country does issue a CA to the project for the VCU tons sold to an overseas CN buyer
- A project is located in country A (host Paris Accord signatory country) and it obtains CAs from its host government to issue CA-ADJUSTED-VCU's (CA-VCU's)
- The CA-VCU's are purchased by a private entity whose emissions arise in Country B, potentially transmitted via an intermediary broker
- The CA-VCUs enter the country B purchaser's VERRA registry account (the VCU's along with the CAs) where as a CN claim is made they are retired on behalf of the planet
- The country A government has zero visibility into the buyer's Registry account. It cannot see the private information regarding how many VCU's and CA's were purchased.
- The country A government therefore cannot know that country A CAs were purchased by a private entity and cannot therefore know to apply them to its own Paris Accord reporting
- It is therefore impossible in the context of the private entity CA-VCU purchase for CAs transferred as part of a country A-B international VCU purchase to be double counted by two governments against both their Paris Accord goals. Only country A (through its Paris According accounting roll up of domestic GHG's) will account for the project's reductions
- There is therefore no double counting under the Paris Accord where governments are the ultimate reporting entities if VCU's are purchased by private entities
- Thus no CA's need to be issued for internationally traded VCU's purchased by private entities making CN claims in order to avoid double counting by governments in their Paris Accord reporting

➔ The premise that VCU's must have CA's in order for a carbon neutral claim by a private entity to be valid is void

iii) However, CA's will continue to be needed for GOVERNMENT TO GOVERNMENT VCU purchases in order to avoid double counting under the Paris Accord

- CA-VCU designations will be important to sustain for government overseas VCU purchases under the Paris Accord.
- In this case, the reductions that the project VCUs contain must be adjusted in country A (by adding VCU's sold back into the PA net GHG result) in order for the government in country B to be able to count the VCU's as reductions in their own Paris Accord report.
- Countries could legitimately require projects to acquire CAs if credits were sold to overseas government purchasers

➔ there is still an important role for ART 6 compliance VCU's but such VCU's are not needed for private CN commitments to avoid double counting under the PA

2. **<u>IF CA's WERE DEEMED TO NONETHELESS BE NECESSARY</u>** FOR PRIVATE PARTY INTERNATIONAL VCU PURCHASES WHEN MAKING CN CLAIMS (1, ii)) THE IMPLICATIONS FOR THE CARBON CAPITAL MARKETS AND PRIVATE SECTOR INVESTMENT TO ADDRESS CLIMATE ARE SEVERE RETRENCHMENT
   - The foundation of any well-functioning private capital market rests in secure property rights for the assets capitalized, supported by clear legal frameworks.
     - Absent such pillars, private capital markets such as the voluntary carbon credit market do not function
   - The premise for the carbon credit capital market has always lain with the certification process which established that the entity making the investment in the assets (technology or activity) which result in the GHG reductions is the owner of the GHG reductions and carbon credit capital
     - This is the foundation that determines who owns the carbon capital in all the carbon credit certification systems
   - This result is congruent with a property rights framework: the entity which invests in the project asset owns the GHG reduction assets

➔ Requiring CA's for VCU sales to overseas private entities making CN claims removes secure property rights from both project developers' assets VCUs (and CN VCU purchasers claims)

Implication #1: Private Investment in Carbon Credit Projects Will Decline

- If under Paris Accord, a project developer like Ball State University would need to secure corresponding adjustments from the US government (considered here a Paris Accord signatory) in order to retain ownership of the carbon credits resulting from its investment in geothermal and other energy efficiency state of the art technologies, such progressive investors and the GHG their leadership delivers will wither on the vine when sales are contemplated for overseas buyers (see #3 below)
  - "If you were to say that the US government under Paris could simply take ownership of the BSU carbon credits -- if we proposed to sell them to overseas buyers, that would comprise a serious property-takings issue; a very questionable intrusion in the marketplace by eminent domain! Rather, a university such as BSU would need the assurance that its creation of carbon capital and decisions to invest those privately-created monies in clean energy and energy efficiency would remain a protected right." Prof Bob Koester Ball State University
- The integrity of property rights associated with such assets would be deeply undermined and the VCU capital market evaporate for progressive project development/investment
  - "The CA requirement would transform VCU's from unencumbered to encumbered assets, making them less valuable overnight and creating a severe chilling effect on the private carbon capital markets. All consequences flow from this foundation (per #2) and will severely undermine every private entities' willingness to contribute their capital resources to tackling climate change" Mark Moore, UK Associate Chartered Accountant (ACA)

- The Californian Low Carbon Fuel Standard (LCFS) market has already seen an outcry when the state awarded the LCFS credit ownership to utilities and EV charging networks rather than the EV charging asset owners themselves. The state has now been revising its rules in order to ensure that the exceptionally valuable credits (valued at $200/ton CO2) are now equitably restored to the parties whose investment in the charging infrastructure delivered the reductions in the first place
    - There thus are precedents for the *restoration* of carbon-based property rights to the investing parties should governments -- by fiat -- deem those rights to be awarded to other parties

Implication #2: precedents for countries releasing CA's under Kyoto is extremely slim: with trivial comparable CA volumes released going forward, the price of VCU's which include CA's will skyrocket

- There have been very few precedents under Kyoto in which governments have released the equivalent of CA's to avoid double counting for domestic VCU projects' credits to be sold. Most governments would assume that such CA issuance would not be in their best interest to secure targets
    - See innovation section #4 below for business cases that would suggest such governmental assumptions were premature; but the weight of historical precedent indicates governments are slow to recognize the wisdom of such precedents
- Absent CA issuance, the price of ART-6 COMPLIANT VCU's will rise dramatically given the very substantial volume of carbon neutral commitments in the global market currently which would be seeking to make such purchases
- With a de minimis volume of CA's issued, only the highest net worth private entities could continue to make carbon neutral commitments (and pay such high prices). Private entities' contributions to addressing climate change therefore would fall to de minimis levels as companies back away from their untenable high priced CN commitments since the cost of doing so would be prohibitive relative to the competitive advantage gains CN would secure
    - "When 3M's Display Materials & Systems Division wanted to buy carbon credits we wanted to purchase credits from worldwide sources since our division does business on a global scale. Had the VCU-CA requirements then been in place and the price of global credits increased substantially, it might have prevented us from supporting global efforts to reduce carbon." Brett Sitter, Product Development Engineer, 3M
- CAs could also be withheld from projects by governments to advance more political ambitions (e.g. relative to cross-border trade issues) which would intensify concerns regarding CA quantify and VCU pricing for reasons beyond the Paris Accord's objectives

Implication #3: If VCU's require CA's to be sold internationally, carbon markets will restructure to "domestic island markets" to the detriment of many countries which would most need access to the private investment VCU capital

- If VCU's are deemed to require CAs in order to avoid double counting, then buyers and sellers will seek to make transactions solely within the "domestic" sphere of a single country's Paris Accord accounting – because then the CA is not required in order to make a carbon neutral claim with the VCU purchase.

    - If the credit seller and the emissions profile of the credit buyer are both within the umbrella of one single country's PA accounting, then no double counting arises under the Paris Accord
- Carbon capital markets will thus restructure towards "domestic only transactions"
- For countries with a strong supply of both CN-committed buyers (those with significant domestic emissions) and ample domestic project developers it may be possible to sustain some carbon capital market amongst CN committed purchasers whose emissions profile would be significant in that same country
    - The US could fare reasonably well under such a scenario as might other countries with strong sources of both emissions from CN-committed entities and robust sources of domestic VCU credits
- However for countries (as might be the case in LDCs) with high potential for VCU issuance – but very few local emitter purchasers – such a "domestic only" carbon capital market would be very limited: a profound set back. The flows of private carbon capital investment into VCUs would fall significantly.
- Limiting "domestic only" VCU transactions would also end up disadvantaging all host governments: if private entities' investments cannot result in overseas VCU sales, revenues will be lost, alongside government tax revenues and job creation opportunities
    - "As 3M's carbon credit project moves forward, we may need to increase our staffing on our manufacturing lines to keep up with the higher volumes of our energy efficient display films. This increase in staffing has the potential to create more manufacturing jobs for the local community. If the carbon credit industry drops because of the CA, then these jobs may not be created." Brett Sitter, 3M Display Materials and Systems Division

Implication #4: if the price of CA-VCUs skyrockets and carbon capital markets restructure towards domestic only transactions, larger private entities' continued commitment to CN targets will be exceptionally difficult to sustain due to management complexity and VCU quality concerns if these entities attempt to use only less expensive non-CA VCU's

- CN commitments from private parties would increasingly get priced out of range using CA-VCU's forcing entities to consider achieving CN using non-CA VCU's
- CN product commitments could theoretically be achieved with non-CA-VCUs by matching geographically the emissions of a product along its supply chain to a set of local credit projects purchased in those same countries. However, given the complexity of such products' supply chains, the sheer number of countries involved and the lack of quality credits available in many of those locations, achieving carbon neutrality on such a "supply-chain-balanced" basis would be exceptionally hard to sustain.
    - For example: "Interface's flooring sources one of its principle materials from Slovenia. What quality would the VCU's be in that country? We've never been able to buy them there before. And the sheer complexity of a product's supply chain emissions profile would seriously diminish a company's ability to deliver upon such CN product commitments if we had to balance emissions with local VCU purchases along such complex supply chains". Buddy Hay, Interface Inc

- Similarly, CN corporate commitments for entities like multi-national corporations with significant emissions profiles (spanning scope 3) outside of a single country would face the same hurdles in meeting their carbon neutral commitments through a "domestic only, no CA" carbon market. In practice, smaller organizations with emission profiles limited to one country could still achieve carbon neutral claims in a domestic only market (including possibly university campuses, smaller companies). However, given the interdependencies for any larger corporation across their global supply chains, even a CN corporate commitment (which per Natural Capital Partners and SCS would need to include 40-100% of their scope 3 emissions) would face similar implementation challenges in a domestic-focused non-CA-VCU only carbon capital market since they would need to follow a similar product "supply-chain-balanced" strategy.
- The result would be a profound diminution in CN product and corporate commitments and the loss of private entities' funding to help address climate change at a time when we need every dime and molecule of CO_2 reduction that such entities can supply

Implication #5. As confusion arises regarding whether CN claims are credible (e.g. would claims need to be CA-ART 6 compliant or not and which claims are being made on what basis?), the competitive foundations upon which CN commitments are credibly and clearly founded will over the medium term erode – and thus the commitments will wane

- It's taken 20 years to reach the level of CN commitments in the market place with the depth and breadth currently achieved
    - 800+ campuses; coalition cities (Carbon Neutral Cities Alliance), multiple companies competing within the same industry etc
- Uncertainty regarding whether private parties' CN commitment double count with Paris Accord accounting by governments will undermine the integrity of the CN market even more
- Even new net zero protocols from the Science Based Targets Initiative do not appear to have begun thinking about how to integrate Article 6 CA's into its standard
    - Based upon questions posed during its recent webinar, SBTI has not it seems yet considered the Art 6 issues in its engagement with compensating and neutralizing reductions in its draft net zero protocol. Nor yet addressed this in its emerging offset discussions

Implication #6. Entities might consider making alternative claims but this would undermine the CN/net zero momentum and set back private investment commitments and funding

- Companies might consider making alternative claims other than carbon neutral or net zero if there is no clear or credible basis rapidly established for these claims under Paris.
- There are compelling business precedents for such alternative climate marketing claims where companies like Chevrolet (see business case below) have retired very significant VCU's (8m tons, twice the size of the voluntary market at the time) and secured major competitive gains (measurable reputational gains and market restructuring in support of e-transportation infrastructure) while not making any CN or net zero claim. Rather Chevy just indicated that it had retired 8m tons of VCUs on behalf of the planet.

- The compelling simplicity of CN/net zero claims, however, is that they carry a common yard stick against which such commitments can be compared across different companies, products, sectors and countries. The equivalence between the emissions profile of the entity/product and the countervailing reductions and credits provides a universal means of comparing the CN/net zero commitments that entities make. While avoiding making a CN claim, the significance of an entity's commitment to retire xm tons of CO2 on behalf of the planet, whilst flexible and not in conflict with any Paris Accord accounting, would be harder to evaluate: what is the yard stick to be used here? What is this retirement equivalent to and is this reasonable relative to impact this entity has upon the planet? Absent such clear comparable yard sticks the value of a climate commitment risks being undermined.
- Companies have used more "open ended" terminology during the early CN commitment period (2000+) to market their products: Interface's CN flooring which was originally branded "Cool Carpet" comes to mind. However, as CN product commitments from competitors rose due to Interface's marketing success for Cool Carpet, the company chose to re-brand their flooring as carbon neutral for the reasons outlined above.
- Companies also could consider pivoting away from investments in VCU's to make investments in their scope 3 supply chain reductions, following the Science Based Targets Initiative (SBTI). However, the same questions arise relative to how to account for such scope 3 reductions claimed outside of the company's host country when those reductions also would be reported by the overseas government against their Paris Accord targets. SBTI hasn't yet convened stakeholder discussions to address this topic explicitly (or answered questions re PA reporting on a recent webinar). Unfortunately, a pivot to SBTI style "GHG reduction" investments (rather than offset credit VCUs per se) would not therefore avoid a double reporting/claiming of the scope 3 GHG reductions between the private entity and the project host government.
    - And the goal of the SBTI is to achieve a net zero GHG position against an entity's residual GHG emissions which in so many respects is a claim so similar to carbon neutrality that both claims would likely be viewed in a similar light under Paris Accord reporting
- Changing to a different kind of claim thus carries many risks
    - It's taken 20 years to mainstream carbon neutrality as a metric; over the next 10-20 years needed to establish adoption for new alternative claims, the momentum and intensity of private commitments to tackle climate change will be defrayed
    - To undermine the credibility of CN claims now risks reputational damage for private entities that have established bona fides with their stakeholders based upon this commitment. Are they still keeping their promises?
    - Alternative claims may be harder to compare and, like SBTI net zero program, carry identical concerns to those raised for CN VCU accounting under Paris

Chevy Business Case for 8m ton VCU Investment/Retirement

- When Chevrolet decided to invest $40m of marketing funds to purchase and retire 8m tons of US VCU's, its strategy was informed by an extensive stakeholder dialogue process
- GM already had a track record of reducing its operation's GHGs by 60% since 1990 and was bringing pioneering lower carbon vehicles to market, namely the electric Volt
- However, rather than pursuing a carbon neutral or net zero strategy, Chevy upon the advice of its stakeholder advisory board decided to simply retire the 8m tons of VCU's on behalf of the planet
- Explaining their actions, Chevy compared the significance of the 8m tons to US household GHG emissions – not their own GHG footprints. Their investment was in fact so large that its 8m ton VCU purchase had to be deployed over a 5 year period because 8m tons was twice the size of the annual VCU market at the time
- Even though Chevy made no CN claim, its approach secured significant business returns. Its reputation as a "green" brand entered the top 100 list for the first time ever; stakeholder engagement with an Earth Day twitter dialogue (that Chevy campus students designed and lead) resulted in the second highest ranking twitter hashtag on Earth Day …
- Even more importantly, Chevy pioneered investment in campus based EE VCU's – and opened the door for other credit purchasers to emulate such investments. As a pioneering manufacturer of electric vehicles, Chevy realized that utility networks would need to accelerate their EE savings if they were going to be able to deliver the additional kWh needed to power the new EV's on the road. However, as an auto OEM, Chevy to that point had not been able to directly influence such accelerated EE savings.
- With the Campus Clean Energy Efficiency methodology, Chevy was able to not only direct some of its $40m funds to this more rapid EE deployment but open the door for other VCU investors to champion this same objective as they purchased the campus VCUs.
- This introduce a new source of private carbon capital to accelerate utility network EE savings and thus help prepare the electricity grid better to deliver e-transportation services.

➔ In such a light, the false premise that CN claims are double counted absent government issued CA's when internationally traded VCU's are purchased by private entities comes at a very high price to the climate, LDC's and future generations. Private investment – both in project development of VCU's and the purchasing of credits across international emission/VCU location borders to make CN claims – will wither. The future of the climate will rest upon investments made only by government entities or some degree of "domestic only" CN private investment.

Implication #7. Entities might consider reframing the foundations for their project funding as a contribution accelerating a country's attainment of its Paris Accord goals (rather than a VCU credit per se). However, absent a clear definition of the asset and property right arising, it may be harder to sustain a private capital market in such investments

- In such cases it would be preferable to frame such investments as VCU purchases made without CAs since at least then the investments would continue to rely upon the strong VCU certification systems. (See section 7, Climate Progressive Commitments)

3. THERE ARE PRECEDENTS IN OTHER ASSET ACCOUNTING SYSTEMS WHICH DEMONSTRATE THAT THE PREMISE THAT CAs ARE REQUIRED TO MAINTAIN CREDIBLE ACCOUNTING FOR VCU ISSUANCE IS NOT VALID

- As noted above (#1), the premise that CAs are required to be issued by projects' host governments in order for private entities' project VCUs to be sold overseas to non-governmental purchasers essentially transfers by fiat the ownership of such entities' carbon capital to the host government themselves.
- However, there are several highly credible paradigms in which all stakeholder recognize that accounting for asset generation/transactions do not require a premise upon which a governmental agency needs to own such assets in order to account for them in a credible, transparent fashion.
- In both these accounting paradigms, the double reporting (or accounting) of the assets across more than one entity's reporting is recognized as valid and the resulting claims still credible. Indeed, such double accounting is deemed inevitable and even desirable to maximize progress towards the objectives that the accounting systems track
- So even if one were to argue that a private entity's CN claim were to double claim relative to a country's Paris Accord reporting (which would not be the case given that double counting does not arise (ref #1)) such double claiming would be highly desirable since it would reflect significant private investment in addressing climate change (rather than the lack thereof).
- Similar recognitions need to be made to CN claims made using internationally purchased non-CA VCU's when these are made by private entities making CN claims

i) Scope 3 GHG reporting

- WRI's Scope 3 GHG reporting protocol recognizes that double counting with entities' scope 3 emission is "inevitable". For example, the product use emissions associated energy consuming products would arise in both the product manufacturers' scope 3 emissions (product use), the customer's GHG inventory (as scope 2 electricity or scope 1 energy-based GHGs) and even the customer's utility (for electricity generation GHGs)
- This does not mean however that targeting reductions in scope 3 emissions across all such entities' efforts is not either desirable or reportable in a credible fashion
- WRI's scope 3 protocol also recommends that project based accounting be used when capitalizing reductions on a discrete basis, as would be the case for VCU certification
- All such activities can be accommodated within an entity's scope 3 reporting without losing credibility or transparency
- In the same way, the parallel accounting between Paris Accord country reports and VCU domestic projects would be considered inevitable and indeed desirable. Otherwise the country would not be taking advantage of carbon capital markets to accelerate GHG reduction in leading edge technology sectors (see 4 ii business cases for WA State and Chevy campuses). The parallel reporting of such activities under both ledgers does not however mean that double counting has arisen under the Paris Accord reporting as demonstrated in #1.

ii) GDP

- Governments roll up accountings tracking economic activity based upon the cashflow, revenues and payments made by its private (and governmental) entities into a reporting of the country's gross domestic product.
- Within this system, the associated cashflows are expressly and chronically double counted not only between the private entities' profit/loss reports/tax returns and the government's GDP reports but also economy wide across and between all the entities' activities.
- This system of reporting GDP is nonetheless recognized to be a valuable tool to assess a country's progress towards its economic goals
- Further, a government doesn't need to own – or by fiat take ownership – of the private entities' assets in order to "avoid double counting" of these financial flows. Double accounting in this context is recognized as inevitable and indeed desirable. My income generation helps contribute to enhancing GDP – just like a VCU's project reductions when sold to overseas buyers will help accelerate a country's progress towards its low carbon future on a far more business savvy basis (see 4 ii WA State case business study). Such double accounting of activities does not make the transactions any less credible.

➔ There are credible accounting protocols and systems which have established precedents in which the parallel reporting of activities is not only deemed inevitable but desirable. Surely if governments seek to enhance private entities' commitments to invest in addressing climate change a similar frame of reference can be applied to the Paris Accord reporting and VCU issuance/purchase across international borders (particularly when there are mechanisms to ensure accurate Paris reporting, see sections 4 and 5). These parallel forms of accounting, with their mission and transparency, demonstrate that the two can co-exist without compromising the integrity of the market and/or the governmental commitment

➔ It is not necessary for countries to assume ownership of VCU carbon capital in order to account for it in a credible transparent fashion, when VCU international transactions arise with overseas private parties.

➔ Private entities can continue to make CN claims using internationally purchased non-CA VCU's without incurring a loss of credibility or double counting under the Paris Accord

➔ Even if such a CN commitment were considered double *claiming*, the GPD and WRI scope 3 GHG Protocol guidance recognize that there are conditions under which such double claiming is inevitable and indeed desirable. Such credible standing should be granted to these private entities' CN commitments.

4. IF COUNTRIES ARE NOT TO UNDERMINE UNECESSARILY the PROPERTY RIGHTS ASSOCIATED WITH PRIVATE INVESTMENT IN VCUs' LEADING EDGE GHG REDUCTION TECHNOLOGIES – and eviscerate private carbon capital markets' contribution to achieving their goals – A DIFFERENT PREMISE SHOULD HOLD: VCU's (potentially in government approved sectors) SHOULD AUTOMATICALLY BE DEEMED THE PROPERTY OF PROJECTS TO SUSTAIN PRIVATE INVESTMENT FOCUSED ON VCU TRANSFORMATIVE TECHNOLOGIES, ENABLE INTERNATIONAL SALES AND THUS ATTRACT OVERSEAS FUNDING TO ACCELERATE A COUNTRY's PROGRESS TOWARDS LOW CARBON GOALS ON A BUSINESS-SAVVY BASIS

i) RATIONALE

- Rather than governments assuming that CAs are required to be granted by them to project developers seeking to retain ownership of the carbon asset their investments have generated if VCUs are to be sold to private entities outside the project's host country …
    - That is asset stripping such investments of their carbon capital (per #2, Implication 1 above)…
- And assuming that governments wish to continue to secure private investment in leading edge VCU technologies in their country to accelerate their progress towards a low carbon future …
    - Specifically private investment that is domestic for project development and international for VCU purchases
    - Rather than making all low carbon investment out of their own treasury resources …(per 2 above)
- It would be in a country's best interest to automatically assume that GHG reductions arising in such VCU projects – those certified as contributing at the leading edge to beyond business as usual reductions – are retained by the project investors themselves, who have the right to sell the resulting credits to international purchasers without corresponding CA's
    - There are precedents demonstrating a compelling business case for this strategy as outlined in the cases below (see section WA state and Chevy campuses)
- The vast majority of GHG reductions arising in a Paris signatory government's accounting (that would not be beyond business as usual) would continue to contribute to a country's PA reduction targets. Only the most leading edge technologies – including those most likely to accelerate a country's progress towards an ultimate low carbon emissions goal – would be eligible to be considered as certified VCU's and thus eligible for international sale/investment.
    - So a country's Paris Accord GHG reduction goals would continue be achieved through these business as usual reductions (and over the long-term by the market restructuring achieved by the sold VCU low carbon technologies)
- However, and most importantly, the leading edge VCU technologies' deployment would be accelerated by the carbon credit capital funding they would receive *from external international sources* – and thus turbo-charge the country's progress towards a lower emissions profile

    - Strikingly, this enables countries to accelerate progress towards low carbon goals in mission critical sectors using VCU's sources investments funds that arise from OUTSIDE the country's own financial resources. Other investors would be paying for leading edge technologies in the short term to be deployed more aggressively in their country.
- At the end of the VCU crediting period – say 10 years – the country stands to benefit from the lower carbon footprint achieved by the accelerated GHG reductions delivered as the result of OVERSEAS INVESTORS' CAPITAL. The country's longer term emissions profile is thus far lower than it would otherwise have been without requiring domestic $ investment – and results in the far easier attainment of the country's 2030/2040/2050 Paris Accord goals
    - By that stage the country is no longer granting permission for projects to sell credits to overseas VCU purchasers
- VCU certification organizations – such as VERRA, Gold Standard – would also be able to report to a host country the volume of issued and purchased VCU's sold each year from such sectors to non-domestic private purchasers so that, since host governments would not be able to track the private information in VCU registries associated with such sales, **the government would then be able to make a note of this in their Paris Reporting the VCU's sold outside its country boundary.** However, as per #1 above, such sales would not have been double counted with other Paris Accord country reports and so such aggregated VERRA reports would be for informational purposes only.
    - VERRA is already anticipating being able to make such transparency reports public
    - NOTE: this is the inverse of the kind of transparency reporting that VERRA is currently considering because the premise of ownership by the project of internationally sold VCUs is to be considered granted upfront.
- If government purchases of other country's VCUs had been made, then VERRA would also be able to issue similar aggregated transparency reports for government to government purchases of VCUs since these would require adjustments under the project host country's Paris Accord reporting.

 Thus double counting for VCUs sold overseas to government purchases would be avoided

NOTE: if governments were to decide alternatively that CAs were to be needed for VCU issuance, it would still be particularly savvy of countries to make clear that certain leading edge technologies would automatically be awarded such CAs. This would be particularly business-savvy in sectors with very high emissions where countries are targeting mission critical investment in leading edge technologies to drive market restructuring – such as energy and transportation sectors – since they would then be leaving open the doors to the infusion of external (non-domestic) private investors to help accelerate their progress towards a low carbon future in these sectors. This was the approach that WA State pursued in its original Clean Air Rule design (see case study below).

    - Expanding beyond the own governmental and private domestic capital resources
    - Countries could indeed designate certain sectors as eligible for this new premise, where non-CA VCU's could automatically be owned and issued by project developers on an "approved list" of sectors/technologies
        - Such approved lists would of course have corresponding VCU methodologies under which certifiers would certify such credits

ii) THE BUSINESS CASE WISDOM OF PURSUING SUCH AN APPROACH HAS IMPORTANT PRECEDENTS in BOTH WA STATE AND US UNIVERSITY INNOVATIONS.

Business Case Study: WA STATE

- When Washington (WA) state introduced its Clean Air Rule it established a set aside reserve whose emission reductions could be awarded to energy and transportation in-state offset projects (which served as compliance VCUs) thus avoiding double counting with the emission reductions arising from utilities, industrial sources and fossil fuel importers that served as covered entities in these same sectors under the Rule
- This not only avoided double counting (see below). It attracted investment into the very state of the art "mission critical" VCU project technologies where WA wanted to accelerate investment in order to more rapidly reduce GHG's in these major emission sectors (e.g. EV charging, etc.)
- Such investment in these credits could arise from either the covered entities or investors from out of state – securing funding sources to "turbo charge" these technologies beyond those which would have otherwise been within their reach. (Notably the California set aside reserve only applies to domestic renewables investment and so the additional funding for energy/transport based VCU's is lost)

 WA Department of Ecology recognized that such new revenue streams would accelerate their progress towards a low carbon future using other parties' investment funds to drive the desired market restructuring.

- The Department of Ecology set up a list of approved methodologies under which such in-state credits could be capitalized
- Once the project crediting period ended and VCUs were no longer sold, WA would have a lower carbon emissions profile in the energy and transportation sector than would have otherwise been the case, securing their low carbon/CN goals sooner

Business Case Study: Chevy Campuses

- When Chevrolet approach university campuses to suggest they collaborate to develop a new VCS energy efficiency performance methodology so that it could purchase and retire campuses' EE carbon credits, the same business logic applied to the campuses' decision making
- Campuses realized that if they capitalized EE VCU's due to their superior EE GHG performance and sold the credits to Chevy, they could invest this "external" funding to accelerate even more investment in their EE activities. The Chevy funds would supplement their own internal capital investment sources and help accelerate their progress towards their low carbon/CN goals
- Over the period of the project crediting period, VCU's would be sold (and accounted for under their public GHG reporting to Second Nature) thus transparently avoiding double counting (see accounting case below)

- However, by year 11 after the project crediting period closed, the campuses would have secured a far lower carbon profile than would otherwise have been the case, using other entities' capital investment resources.
- The Chevy campus case study is particularly salient because some of the credits transacted (post Chevy) have crossed international boundaries.

iii) THESE CASE STUDIES ALSO DEMONSTRATE THAT THERE ARE OTHER ALTERNATIVE MECHANISMS THAT COUNTRIES CAN INCORPORATE TO CREDIBLE REPORT PROJECT VCUs and AVOID DOUBLE COUNTING

- WA State and Chevy campuses again provide case studies demonstrating mechanisms by which the accounting for such VCU GHG reductions (as credits sold) can be made transparently and without double counting.
    - WA State used a set aside mechanism to avoid double counting for the sale of domestic in-state credits in the transport and energy sectors also covered under its Clean Air Rule
    - Chevy campuses transparently added back in the volume of their energy efficiency based VCU credits sold when reporting publicly at Second Nature their emerging progress towards their longer term CN goals
- There are also other precedents for other "set aside" mechanisms that state governments have pioneered in the past that would similarly avoid such double counting of reductions while securing external parties' carbon capital investment funds to accelerate their progress towards their long-term low carbon and CN goals
    - Such set asides have been used by RGGI and CA for in-region private parties' renewables investment under their caps
    - The Transportation Climate Initiative in the North Eastern States is also considering a similar set aside reserve design as Washington State
- All these mechanisms have served comparable roles to those outlined above for CAs if required to be applied to the subset of domestic VCUs sold to international private purchasers under a host government's Paris Accounting reports. The business motivations have all been the same: to preserve and sustain private capital investment in the very leading edge technologies which the government itself wished to ensure would continue to restructure their most strategic markets towards a low carbon future.
   However absent assurance that the environmental attributes (whether renewable or in most cases carbon capital) would be retained by the private entities investing in these leading edge technologies and thus available (under PA) for sale to external international investors to purchase, such fundamental property rights assurance will be lacking and the very private capital that could otherwise be leveraged to a government's advantage as it pursued a low carbon future would be lost.

Accounting Case Study: WA STATE

- WA State's set aside reserves were designed to apply to the covered sectors under their Clean Air Rule – energy, industrial, transport – in order to facilitate VCU development and investment in these same sectors within state without double counting
- Drawn down as VCU's were capitalized/sold, the set aside reserve allowances functioned essentially as corresponding adjustments
- Double counting was avoided and a resulting savvy business case pursued that could accelerate WA's progress towards a low carbon/CN future leveraging entirely new sources of investment funds

Accounting Case Study: Chevy Campuses

- Chevy campuses publicly accounted for their EE VCU's sold (separately from their underlying profile of accelerated energy-based scope 1 and 2 GHG reductions) when reporting publicly their GHG profile to Second Nature, the non-profit entity that has secured CN commitments from over 800 US universities/colleges.
- Such transparent VCU sale accounting served a similar purpose as CAs when VCUs under Paris would be exchanged between two governmental Paris Accord signatories, avoiding any potential double counting

5. ABSENT SUCH ASSURANCES BY GOVERNMENTS THAT SUCH PRIVATE VCU ASSETS ARE OWNED BY THE PROJECT INVESTORS INDEPENDENT OF SECURING CAs, VERRA COULD STILL PROVIDE TRANSPARENCY SERVICES IN SUPPORT OF SHREWD VCU PURCHASERS INTERESTS

- VERRA and other registries could publish annual reports aggregating the purchasing volumes of VCU's to overseas private entity and governmental purchasers (separately) so that host governments could enter these GHG flows accurately in their Paris Accord reporting – whether the host government required projects to acquire CAs or not
- In each case the Paris accounting reporting would benefit. For example:
  - All overseas government purchases of domestic project VCU's would require integration into the host government's Paris Reporting – either by accounting adjustments (if projects did not require CAs to sell) or as a check/balance for the host country to ensure that project volumes sold to overseas governments did indeed match the volume of CA's they had granted domestic projects for such overseas government purchases
  - The private entities' aggregated VCU volumes would not require accounting adjustments under the host government's Paris Accord reporting (since there would be no double counting per #1). The value of this aggregated report would informational. However, if countries did require projects to acquire CAs to sell to international private purchasers, the aggregate report would enable governments to again verify that transaction volumes matches (as above)
- Such aggregated Registry reports would also benefit market participants. For example, VCU purchasers would know if a country's total volume of internationally sold CA-ADJ

VCU's was comparable to its claimed PA reductions. Under such terms, project purchasing might not be considered as desirable since the country would not be making its own domestically funded/delivered GHG reductions on their own behalf

- In this way, it would be possible to distinguish between domestic technology investments a country had made on its own behalf from "dispensations" in which a country had either a) purchased VCUs overseas for the purpose of meeting a Paris Accord goal; and/or b) sold VCUs to overseas purchasers
- Since culturally speaking there are differences in the ways in which countries typically address challenges and achieve their objectives (spanning top-down regulatory driven and bottom-up market approaches), it's possible that, absent clarity in the Paris Accord itself regarding the role CAs play for private carbon capital markets/commitments, some countries may require VCU's to acquire CAs, others not. It's notable that aggregated registry transparency reports could contribute a valuable role to help sustain market confidence and accurate Paris Accord reporting in both cases.
    - In all scenarios (with respect to how CAs are/aren't required), the value of such VERRA Registry aggregate transaction reports would hold all parties accountable through these transparency mechanisms

6. IN THIS LIGHT, A TRANSITION PERIOD IN WHICH IT IS CLEARLY ESTABLISHED THAT CN CLAIMS IN 2020+ CAN CONTINUE TO BE CREDIBLY MADE USING non-CA-VCUs is ESSENTIAL
    - 2020 is already upon us so the need for flexibility is already apparent
    - More importantly, it will be critical to take the time to very carefully assess how the private carbon capital markets and commitments can best be structured and integrated within the Paris Accord if their vital contributions are to be sustained
    - The challenge in front of us is to establish frameworks for the future carbon capital systems successfully not fast. There is too much at stake to make speed the criterion for success: sustaining private entities' contributions to addressing climate change is the metric by which we should be assessing our outcomes here

7. IN THE LONGER TERM, CERTIFICATION OF CREDITS WOULD BENEFIT FROM MORE DETAILED LEXICON to CLARIFY THEIR PURPOSE UNDER PARIS ACCORD AS COMPLIANT CN STRATEGIES (avoiding double counting)

Given the range of possible VCU purchasers (governmental vs private entities) and geographic boundaries (international vs domestic VCU purchases relative to the geography of the entity's GHG emissions location), VERRA should consider a broader set of VCU credit designations beyond just CA ADJ and non-CA ADJ VCUs.

The following VCU lexicon is based upon a set of CN commitments that entities would likely want to make going forward (even if VERRA is not going to certify these on the part of buyers):
A CN – Paris Compliant – DOMESTIC - COUNTRY X

- for private entities: CN companies/products whose emissions are entirely contained within country X and whose VCUs are similarly sourced from that same county X

B. CN – Paris Compliant – SUPPLY CHAIN BALANCED

- for private entities: CN companies/products whose emissions extend beyond one country and whose VCU purchases are geographically balanced to match emissions sources (ART 6 CA_VCUs are therefore not needed)

C-1. CN – Paris Compliant – INTERNATIONAL ARTICLE 6 TRADED

- for governments seeking to acquire VCU's overseas to apply their Paris targets

C-2. CN – Paris Compliant – INTERNATIONAL ARTICLE 6 TRADED

- for private entities seeking to go CN (for enterprises or products) whose emissions may span more than one country and whose projects would be sourced from countries beyond their emissions sources (including those quantities that are not geographically balanced per B)

D. Paris Compliant – CLIMATE PROGRESSIVE

- for private entities which wish to purchase VCUs (not CA VCUs) so that they can accelerate progress towards a low carbon future or simply retire credits on behalf of the planet – i.e. where no CN or net zero claim is to be made relative to their own emissions size or location

I: With the premise that private parties making a CN claim can credibly purchase internationally VCUs WITHOUT requiring CA-ADJ VCU credits to avoid double counting, the VCU certification lexicon would be:

1. VCUs (not CA Adjusted)
    a. Applicable to C-2, A and B and D
2. VCU CA ADJ
    a. Application to C-1

II: With the premise that international purchased VCU's by private parties making a CN claim covering emissions in a country outside the project location DOES require CA-ADJ credits, the lexicon would be:

1. VCU – DOM – COUNTRY X
    a. Applicable to A, B, D
2. VCU – ART 6 ADJ
    a. Applicable to C1 and C2

The difference under the second premise is that the country of origin of the VCU becomes more important for purchasers to see clearly.

Clearly C-2 is a category of CN commitments and VCU purchasers that should be studied further since under one premise these purchasers require CA ADJ VCU's and under the other they don't but can use regular VCU's. Further analysis would confirm that these C-2 private entities whose emissions span more than one country and/or whose VCU purchases arise in countries other than those where their emissions are located represent a very large portion of private sector investment to address climate change. Private entities in category A are likely to be much smaller; and category B commitments face significant complexity and quality sourcing challenges which would wane dramatically under premise II. So unless category C-2 investors can confidently continue to make CN claims without requiring CAs under premise I, the future of the climate system under premise II will rest upon government action (category C1) and a set of new "climate progressive claims (category D) which will likely take another 10-20 years to be defined and gain market momentum. The planet unfortunately cannot wait for such outcomes (D) or rely upon government only action (C-1). Further, since CN claims can be made by C-2 private parties without double counting under Paris Accord (see section 1) and this sector represents a significant private sector investment in keeping the climate system below a 1.5-2^0 C rise, we must ensure that our clarity of thinking does not tragically or inadvertently prevent such private sector investment from sustaining its commitments and investments – and with them, the security of our planet.

Submitted by Sue Hall, CEO, Climate Neutral Business Network (sue@climateneutral.com)
With thanks for the generous creative contributions in developing this input, including from:

Buddy Hay, Assistant Vice President, Sustainable Strategies, Interface Inc
"This paper lays out so clearly the potential implications that would arise from our decisions as to how CAs will or won't be applied. It's vital we understand these details in order to make well informed, final framing decisions carefully so that we can sustain the kind of private entities' carbon investments/commitments that Interface originally pioneered back in 2000. I commend this paper for serious consideration."

Matt Macunas, Connecticut Green Bank
"Connecticut Green Bank was an early innovator as a public organization in renewable energy credit (REC) markets; now, with $2 billion in economic activity catalyzed, we are turning attention to the role of private capital in carbon offset credit markets supporting faster deployment of electric vehicle charging. Private capital markets can bring momentum to tackle climate change. This paper asks vital questions – examining them now can curb unintended consequences later as VCS contemplates the accounting integrity procedures of the Paris Accord."

Brett Sitter, Product Development Engineer, 3M
"When 3M's Display Materials & Systems Division wanted to buy carbon credits we wanted to purchase credits from worldwide sources since our division does business on a global scale. Had the VCU-CA requirements then been in place and the price of global credits increased substantially, it might have prevented us from supporting global efforts to reduce carbon."

Mark Moores ACA, CEO Founder Carbon Reduction Initiative Ltd
"There is no reason why private entities' CN claims based upon international VCU purchases double count with governments' Paris Accord reporting. There are ample mechanisms as described in this paper demonstrating this to be the case. What's really at stake here is the future of the private carbon capital markets and private entities' CN commitment and investments. So the crux question is whether Paris signatories (governments) want to sustain private funding to help them attain their GHG goals. If this is the case, assuring property rights for VCUs without "asset stripping" their value by requiring Corresponding Adjustments for international sales is essential. Property rights are the fundamental requirements for any capital market: without them, as detailed in this paper, all other market implications flow – and represent a disaster for sustaining private investment to help secure our climate future."

Professor Robert J Koester, Ball State University
"We need to extend every effort to develop and secure carbon capital commitments from private entities without policy or accounting procedures that would unintentionally set back by decades the opportunities for achieving planetary health."

Angus Duncan,
Pacific Northwest Consultant, Natural Resources Defense Council

Sue,

I regret not having the band width to plunge into the deep end of this pool, so am happy you continue able to do so.

Of course I concur in the primary premise: that the party that causes the emissions reduction should own that reduction, to retire or resell it as she/he sees fit. Absent that, or in the presence of a state that (double) claims the same credit, the private incentive to reduce dries up.

The difficulty arises in the distinguishing between the state “claiming” the reduction and the state “reporting” the reduction. States that are party to the Paris Accord will report their emissions levels of their respective nations, which will by definition include total emissions reflecting regulatory and market reductions both(including reductions sold as offsets inside or outside the state.

Those reductions that result from the state either regulating emisssions (and so driving reductions) or incenting them with government purchases are reductions the state has an ownership claim to (although the state then selling these is a separate question).

Private sales, within or outside the state, fall into the difference between the reported emissions level and the emissions level (from a baseline) that the state can reasonably be seen to “own.” Other emissions reductions that may occur as a result of direct action but are retired (e.g., on behalf of the planet per GM) also reside in this delta slice.

If this distinction is respected, I see no need for a state-by-state CA adjustment that captures and tracks all such reductions, sales and reselling. But then I was always put off by the green eyeshade types who would rather be precisely right, the numbers all lining up in their columns and adding up, than accept a measurable margin of error in the interests of driving emissions reductions further and faster.

The qualifier to this conclusion is that if the Paris Accord nation is seeking to establish compliance with its voluntary obligations under the Accord, and private offsets result in either a significant reduction in its emissions (helping it to compliance) or a significant decrement from its reported emissions reductions (handicapping its compliance), a CA adjustment factor may be required to give credit where credit is due.

Not sure this is helpful to you, or even that it fairly reflects the issues you are addressing since it’s awhile since I attended to the intricacies of carbon markets. But your paper, and its logical train (if I followed it accurately) certainly seems to me to hold together.

Angus

Angus Duncan
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