EVOLUTION MARKETS

The Intersection of Environment, Energy and Finance.

April 15, 2021

Evolution Markets: Gold Standard Consultation Response

1. **Introduction**

Evolution Markets has been active in environmental markets brokerage since 2000. Our Environmental Markets Group has facilitated over $50 billion in transactions, including some of the carbon markets' landmark trades. As such, we seek to bring a market participant's perspective to this discussion based on our extensive experience transacting and structuring carbon financing. The focus of Evolution Markets' comments is on promoting environmental integrity, while ensuring the efficient functioning of the underlying markets that provide vital financing.

In this vein, we would like to highlight our two main inputs for the consultation:

First, we believe that a five-year crediting periods with mandatory on-going financial needs (OFN) assessments would introduce an undue additional level of risk for project developers or investors providing upfront project finance. In our view, the voluntary carbon market (VCM) will evolve in the future toward more projects with high capital expenditures and hence debt financing. For the amortization of such high CAPEX projects, the tenor of the crediting period makes a fundamental difference. For example, amortizing the same CAPEX over five instead of ten years would mean that carbon credits would need to be priced twice as high, making them much less competitive. Therefore, the more uncertainty there is with regard to the renewal of a crediting period, the higher the necessary cost per metric ton of CO_2 from a financial modeling perspective - thus making projects increasingly unattractive for buyers and investors. While we recognize that an OFN review is intended to enhance project integrity, we believe the policy could have the unintended consequence of preventing the implementation of many good high CAPEX projects.

Second, we believe that the main priority should be financing immediate large-scale carbon reduction to limit global warming to 1.5°C. Introducing premature corresponding adjustments (CAs) for developing and least-developed countries would deter much-needed voluntary carbon finance flows. Likewise, differentiating between adjusted and non-adjusted claims could deter corporate buyers seeking to make immediate investments.

2. **Transitioning from the CDM**

- Evolution Markets recognizes the need to preserve environmental integrity, but this must be balanced against preserving the market conditions necessary to efficiently finance emissions reductions.
- Evolution Markets agrees with the existing rule that transitioning CDM projects must demonstrate vulnerability to discontinuation.
- Evolution Markets believes LDCs/LLDCs/SIDS/conflict zones should be excluded and that any technology on the Gold Standard positive list should also be excluded. These projects are deemed additional based on non-financial factors so it wouldn't necessarily make sense to exclude them based on financial indicators that admittedly can be difficult to measure.
- Evolution Markets does not believe that carbon credit buyers will find it useful to have all programs adopt a five-year on-going financial needs assessment. To begin to have the crucial immediate impact

on lowering global emissions, the market must encourage long-term financing of carbon offset projects. An apt analogy can be found in the market for renewable energy power purchase agreements: project developers need the security of multi-year revenue streams to realize their projects. If buyers believe their stream could stop generating credits after five years, they will be less inclined to purchase long-term offtake, which is often essential to financing projects.

- Evolution Markets is concerned that project developers could find the OFN assessment unwieldy, costly, and at a level of analysis that is too difficult to complete every year. If, on the other hand, long-term debt service to a bank to finance a project's CAPEX would be considered OFN, then mandatory OFN could actually contribute to *lower* the perceived extension risk of a project and thus increase investor appeal.
- In our experience, many non-additional projects continue to be registered not because conditions have changed and they've become non-additional, but because they were not additional in the first place and there has been little scrutiny of their documents. (For example, How Additional is the CDM? Study). One approach that could alleviate this concern is improving data transparency. The first and most important requirement for any transitioning project or new project should be to have accurate and organized documents that can be analyzed by market participants – e.g. brokers – or carbon credit buyers. Public scrutiny will help improve environmental integrity.

3. Voluntary Markets Post-2020

- Evolution Markets recognizes the importance of ensuring there is no double counting of emission reductions and that the VCM contributes to overall mitigation. However, requiring a letter of assurance and authorization (LoAA) before the Paris Article 6.2 and 6.4 rules are agreed upon is premature.
- That said, requiring LoAAs for developed countries beginning this year is logical. These countries will likely have all-encompassing NDCs, and many already cover some industries through an emissions trading scheme.
- However, the 2023 and 2025 requirements for developing and least-developed countries could discourage early investment in projects. Project developers and funders would face significant risk if these countries are unwilling or unable to grant LoAAs.
- At the height of the Clean Development Mechanism credit market, Evolution Markets found that many LDCs did not have the capacity to provide letters of approval, despite capacity building efforts by the UN and climate-focused NGOs. Once obtained, the letters of approval were also in danger of not being respected by successive political regimes.
- It is incumbent upon the VCM to encourage as much investment into emissions reductions projects as possible before the Paris Agreement rules come into action in order to put us on a path to 1.5°C. Setting the timelines independently of the Article 6 rules would unnecessarily dampen investment from corporates who are looking to immediately begin investment in carbon reductions.
- For this reason, Evolution Markets supports the staggered approach proposed by Gold Standard but recommends allowing for more flexibility depending on the timelines that will be determined at the next Conference of Parties.
- With regards to the treatment of domestic versus international offsets, Evolution Markets agrees that there should be no differentiated treatment. Whether corresponding adjustment are required or not, the rules should be uniform for both domestic and international offsets.

- In relation to the statement above, Evolution Markets does not believe that requiring a corresponding adjustment should apply to projects outside the NDC. Many developing countries and LDCs have narrow NDCs and the majority of interventions in these countries will face financial and institutional barriers, making them additional. Requiring an uncertain corresponding adjustment would discourage reductions that would otherwise be additional.
- With regards to the differentiated claims – offsetting and financing – Evolution Markets believes this is a fundamental misunderstanding of how corporate actors are seeking to use the VCM and provide carbon finance. Based on our experience as brokers, corporate buyers, who are constituting a rapidly growing share of carbon offset end-users, are seeking a non-financial return on their investment in a climate project. Most corporates engaged in offsetting are setting net zero targets, and turning to the VCM after exhausting opportunities to reduce emissions and replace high-carbon sources. Removing the ability to claim the offsetting of one metric ton of carbon would disable this use of offsetting, deter corporate buyers, and punish environmental leaders. This is especially true if projects outside of NDCs in developing countries and LDCs would not count as "offsetting" projects.

4. Aligning with Paris: Other

a. Ensuring real emissions reductions
   - No comment here except that CA should not be required for these projects.

b. SDG Monitoring
   - Evolution Markets does not find additional rules to be necessary. Currently, Gold Standard's procedures for verification of SDGs seem sufficient to comply with the Paris Agreement's stipulation that any tradeable emissions reductions contribute to sustainable development. Although we do not think any changes are necessary, future changes will need to preserve the market flexibility to monetize SDGs separate of the underlying carbon reduction.

c. OMGE: 'Overall Mitigation in Global Emissions'
   - OMGE should be left to each individual state. States are likely to consider this on their own terms, and any GS OMGE would be an additional and likely unnecessary tax on offset development.