OUTLINING POTENTIAL SCENARIOS FOR THE VOLUNTARY CARBON MARKET POST- 2020

A follow-up statement for consultation on the future role and design of the Voluntary Carbon Market to support the goals of the Paris Agreement

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Introduction and background

The advent of the Paris Agreement in 2015 prompted many experts in the carbon market discourse to reflect on the role and design of the voluntary carbon market (VCM) under the new climate regime.

In 2017, an ICROA paper (here) posited three broad potential operating solutions for the VCM that could apply post-2020. Similar ideas were also reflected in publications and consultations by other carbon crediting organisations, including Verra and Gold Standard. The three solutions considered were:

1. **Non-NDC Crediting Model:** Credits are generated from sectors which are not currently part of a host country's NDC
2. **Financing Emission Reductions Model:** Emission reductions are financed by non-state actors and contribute to the host country's NDC
3. **NDC Crediting Model:** Emission mitigation units generated under the Paris Agreement's Article 6.4 mechanism are voluntarily purchased and retired by non-state actors

In this paper, the "NDC Crediting Model" option has been renamed the "Corresponding Adjustment Model," wherein the host country adjusts its NDC reporting to deduct for the impact of climate mitigation delivered by the VCM.

In addition to the above, the option of 'business-as-usual', i.e. continue to use VCM for the purposes of offsetting without requiring CA has also been put forward by some stakeholders within the working group for consideration.

In July 2019, Gold Standard, convened a civil society working group[1] comprised of WWF, The Nature Conservancy, World Resources Institute, CDP, Carbon Market Watch, ICROA, Gold Standard and Verra and observed by World Bank[2], produced a short paper exploring the future role for voluntary carbon markets (VCM) post-2020. An updated version of Envisioning the Voluntary Carbon Market Post-2020 was published in October 2019.

The key takeaways from this paper included:

- Achieving net zero by 2050 requires filling 1) the emissions gap (the estimated amount of emissions that the current NDCs are deviating from what climate science requires), 2) the finance gap (the amount of financial capital required to meet and exceed the current NDCs), and 3) the time gap that prioritises climate action taken sooner versus later.

[1] This convening was generously supported by the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety (BMU). The discussion and conclusions of this paper do not represent the views of BMU.
[2] Experts from Gold Standard, Verra, ICROA, WWF, CDP, WRI, The Nature Conservancy, Carbon Market Watch contributed, but we stress that this statement is for further consultation and does not represent the formal positions of the individual members of this group. The development of the statement was observed (which does not imply endorsement) by World Bank.

- To achieve this, the VCM can be deployed to (1) finance actions beyond organisational boundaries that lead to a reduction in the concentration of greenhouse gases in the atmosphere in a way that is real, additional, verifiable, and permanent and (2) target actions (such as emerging technologies) that raise ambition and accelerate the transition towards the goal of net zero emissions.
- Buyers of carbon credits can make “foundational claims”—i.e. a claim that the buyer has purchased YY carbon credits to reduce of YY tons of CO2e, which represents a tangible contribution to the climate mitigation goals of the host country and the Paris Agreement.
- Carbon credit projects may not need to obtain Letters of Approval or Corresponding Adjustments from host country governments if they are *only* making foundational claims.
- The paper did not analyze the legitimacy of purchasing carbon credits and claiming them towards carbon neutrality goals nor the impact on climate ambition of corresponding adjustments in the VCM.

The working group received and considered a large amount of feedback and has both convened and attended events at COP25 in Madrid. This paper reflects further on key issues raised during these consultative rounds and explores the potential solutions above. The paper does not make universal recommendations towards a final working model, nor does it reflect the final views of the individual organisations involved; instead, it is intended to provoke and promote further discussion and to allow carbon crediting organizations like Gold Standard and Verra to begin considering any updates to requirements or guidance.

This paper considers the three solutions in further detail, assessing the relative pros and cons of each, before recommending options to inform the viewpoints of various stakeholders including governments, carbon crediting organisations, project developers and brokers, corporate carbon credit buyers, and civil society organisations. To properly assess the solutions the core issue of double claiming is unpacked.

The feedback raised during consultation for the 2019 papers, plus discussions at COP25, has largely centered around the key question of whether CAs[3] should be required to issue and/or retire a voluntary carbon credit for the purpose of offsetting/carbon neutrality claims. If so, what role could the Financing Emissions Reductions Model discussed in 2018 play, if any?

Other feedback received focused on the following thematic questions (paraphrased for ease):

- Are the emission reductions from voluntary carbon credits ‘double claimed’ by the host-country and the carbon credit buyer if used in the context of offsetting? Would this double claiming negatively impact environmental integrity?
- Is this situation the same if the unit is not used against a target such as Carbon Neutrality?

[3][A **corresponding adjustment** is an accounting entry that countries make in the context of Article 6 of the Paris Agreement to avoid double counting of emission reductions. Corresponding adjustments are applied for the transfer of emission reductions between countries but might also be applied if the country hosting a project explicitly authorizes the use of the emission reductions for other purposes, such as for voluntary purposes.

- Is it essential for a voluntary carbon credit to represent a unique claim and/or unique ownership of the underlying attributes? Does this depend on the use of the credit?
- Is a unit backed by a corresponding adjustment more valuable to project proponents and buyers than a unit with no adjustment?
- Will it be practically feasible to obtain authorisation from host countries and the necessary paperwork to demonstrate CAs?
- Will there be any incentive, if not offsetting, for companies to purchase credits under the Financing emissions reductions model?
- How should we think about domestic voluntary offsetting schemes whose purpose is intended to support the host country NDC achievements?
- What will happen with regards to VCM rules and requirements concerning these topics? How will they impact on standards, projects, buyers and host countries on 1st January 2021, and will there be any transition periods to support market participants?

To recommend a way forward it is important to unpack the underlying challenges and assumptions. Hence this paper will review the issue of Double-Claiming before re-considering each of the three options, building on the work conducted over previous years towards a set of policy options for stakeholders to consider. This paper also briefly highlights the importance of additionality and explores the legitimacy of voluntary carbon neutrality claims.

Double claiming between a host-country NDC target and a company target

The primary focus of this paper is to assess the impact double claiming in the VCM could have on climate ambition (at the global and host-country level primarily) and propose policy pathways related to this assessment of impact.

Double claiming is a form of double counting and defined as: "A situation in which the same emission reduction or removal is claimed by two different entities towards achieving climate change mitigation: once by the country in which the emission reduction or removal occurs, and once by the country or entity using an emissions unit [i.e. carbon credit]". Double issuance or double use of a carbon credit are two other important forms of double counting but not re-considered here, as they are issues that are dealt with at the level of the carbon credit organization and are not impacted by the new context under the Paris Agreement. Carbon crediting organizations should prevent these issues irrespective of the form the VCM takes post-2020. (See Box 1 for double counting definitions.)

Box 1: Definitions for various types of double counting

The 'Avoiding Double Counting Working Group' Guidance was produced with input from some of the members of this Working Group (and others), in the context of the ICAO CORSIA. As part of this guidance the common definition of double counting were defined:

Double Counting: A situation in which a single greenhouse gas emission reduction or removal is counted more than once towards achieving climate change mitigation. Double counting can occur through double issuance, double use, and double claiming.

Double Issuance: A situation in which more than one emissions unit is issued for the same emissions or emission reductions. This leads to double counting if more than one of these emissions units is counted towards achieving climate change mitigation. Some programs and stakeholders also refer to double registration – the registration of the same project under two different programs or twice under the same program.

Double Use: A situation in which the same emissions reduction unit is counted twice (for example by the same or separate buyers) towards achieving climate change mitigation. This leads to an overestimate of the total mitigation achieved and is largely resolved through robust registry systems to track ownership and retirement of credits.

Double Claiming: A situation in which the same emission reduction or removal is claimed by two different entities towards achieving climate change mitigation: once by the country in which the emission reduction or removal occurs, and once by the country or entity using an emissions unit, such as an aeroplane operator under CORSIA.

The type of double claiming considered in this paper potentially occurs where a carbon credit is issued by a project and retired by a third-party claimant (typically a company or an individual) for use in offsetting towards a voluntary ‘carbon neutrality’ or other mitigation goal (represented as a claim made by voluntary buyers), while the mitigation benefit is also captured (intentionally or inadvertently) in host country reporting, towards an NDC or other domestic targets.

Any policy decisions concerning potential VCM solutions, particularly the role of CAs, should be determined by whether the double claim between credit buyer and host-country has a negative impact on countries’ or non-state actor’s climate ambition.

The core question to address is whether the emissions reductions or removals caused by the VCM would otherwise undercut the climate ambition of countries or other non-state actors to set or strengthen climate mitigation policies and measures that it should be endeavoring to set to meet its NDC. If so, then the impact of purchasing a carbon credit may be effectively null (or even an increase in overall emissions if the user decides, for example, to fly more because of the ability to offset travel emissions), because it would been delivered by the host country in its efforts to meet its NDC target.

Box 2: How do claims by voluntary carbon market buyers relate to avoiding double claiming under Article 6 or CORSIA?

Under Article 6 it is essential that no two Parties to the Paris Agreement count the effect of a single reduction or removal. The solution under Article 6, would be to require a corresponding adjustment to ensure that only one party counts the reduction or removal to achieve its NDC.

Although not a Party to the Paris Agreement, under the ICAO CORSIA emissions reductions or removals (“offset credits”) being used by airlines to meet their CORSIA offsetting obligations also cannot be claimed by the project’s host country.[4] If corresponding adjustments were not also applied for the context of CORSIA, this would skew the overall global picture of emissions and global efforts to address them, inaccurately showing better achievement than the reality. In turn, this could lead to lower national (emissions) inventories[5] which could undercut their ambition to set or strengthen climate mitigation policies and measures that it should be endeavoring to set to meet or exceed its NDC and ultimately lead to a failure to achieve the goals of the Paris Agreement. In the VCM, it is not possible for the voluntary claimant’s country of incorporation to claim the mitigation impact because emissions would not be transferred from the project host country to the voluntary claimant’s country of incorporation. Hence, this specific form of double counting, i.e. between two countries, does

[4] There is ambiguity and therefore a variety of views as to whether countries would need to make an adjustment to their NDC for pre-2020 offset credits.
[5] Countries report a national inventory to the UNFCCC.

not arise. This does not preclude double claiming between the host country and the voluntary claimant of the credit, however.

The reporting by two entities of the same climate mitigation, or any other benefit beyond climate is not inherently negative. There are many common examples of multiple entities reporting the same or related benefits, within and beyond climate mitigation:

- A company reports an increased employment count which is correspondingly captured in overall country employment figures. In this case both claims are true and there is no obvious negative to both levels of reporting being captured and claimed.
- A region reports increased economic productivity, a country reports overall economic success and a bloc of countries working together also captures the benefit in reporting.
- A company reduces its internal emissions (voluntarily) for reporting against a Science Based Target while the host country also reports this improvement in tracking progress towards its NDC.

In all of the above, it could be argued that there is no negative effect of these overlapping claims. By design or otherwise, responsibility for delivering these benefits is shared. However, there is a key difference between the above examples and the carbon market in that they do not represent double claiming at a ‘target’ level and do not make claims that the impact being driven by the action is ‘additional’ to the efforts at country level.

In the case of VCM it is typical for the buyer of the credit to use it for the purpose of offsetting towards a ‘Carbon Neutrality’ target while the host-country has a declared target via its NDC. Hence while there may not be an issue with double claiming at the level of the credit itself, dependent on claims the double claim at target level may be problematic. (See Financing emissions reductions model).

The main issue to consider therefore is whether there could be a situation where, in the absence of the VCM contribution, the host country would implement regulation and/or policy to reduce the same emissions, whereas with the contribution of the VCM the host country would not need to do so. In this case, the VCM would partially displace the implementation of further host country policies, with the result that the atmosphere does not see a reduction from the VCM as compared to the situation that the VCM would not exist.

Due to the nature of host-country reporting it is possible that, in some cases, a credit used for offsetting displaces an equivalent reduction by the host-country resulting in no-net impact beyond original NDC expectations. For example, if the host-country has a 20% reduction target for a given sector and the VCM contributes 1%, the total achievement should be 21% for the VCM to have had an impact. However, if the host country inadvertently considers the 1% as part of its achievement then ambition may be limited to 20% and thus the VCM could be argued to have had no net mitigation impact, despite the project itself being additional.

The question as to whether this occurs in all cases is dependent on a number of factors, including how the country reacts to the benefits driven by VCM (for example, if this is a catalyst to prompt higher ambition or over-achievement against targets). Hence it is noted that this 'displacement effect' is not certain to happen in all cases. It is also likely to be challenging to prove for a specific project, given the nature of NDC reporting at the national level vs the specificities of a given project/unit.

VCM policy must therefore determine whether the possible reporting of a reduction or removal by both the credit buyer and host country can lead to this displacement effect, resulting in the impact of offsetting causing no atmospheric difference compared to its absence. If so, then it would be essential to deal with the issue in order for credible offsetting claims (involving an 'additional' benefit) to be made.

This also depends on whether the credit is used in the context of offsetting (unacceptable double claiming at the level of use of the credit towards two targets, host-country and company) or under the Financing emissions reductions model (used only against one target, the host-country). This is further explored in the previous Working Group statement and later in this document.

Additionality of impact is essential for credits that are used as offsets/neutrality claims (i.e. nothing has been neutralised if the claimed impact would have happened anyway) – whereas additionality is not essential for other forms of voluntary action.

However, not all stakeholders agree that there could be an inherent negation of additionality caused by the double claiming, or that it does not always occur and hence should not be regulated. Conversely some stakeholders consider this effect to be universal, with others still considering it to be dependent on a number of other factors such as host-country response.

Aside from the additionality of the impact of VCM in the context of offsetting, it is also important to consider its impact on host country policy ambition more broadly.

Amongst the feedback at COP25, one of the key concerns raised in relation to the application of CAs to the VCM was whether the use of the VCM could displace or disrupt the creation of robust national policy and target setting within the host country.

This disruption or displacement could occur in two ways:

a) **Conscious free-riding:** The host country could 'free ride' on the emissions reductions and/or removals that the VCM is triggering and not set robust policy itself (which is a stated aim of the Paris Agreement) and/or
b) **Unconscious free-riding:** The host country is not sufficiently aware of the emissions reductions and/or removals that the VCM is triggering and perceives that its policies have been more successful than they are, due to 'propping up' by the VCM.

Conscious freeriding suggests a level of awareness and advertent capture by the host-country, while unconscious free-riding is more likely to be inadvertent. While the former suggests illintent, the impact of each (less ambitious national policies and measures) is effectively the same.

Conversely, it is noted that this scenario is not certain in all cases. For example, the above assumes that the underlying impact is definitely included (i.e. the impact is reported) in the inventory or other indicators used to track progress towards the host country NDC where, in some cases, the GHG inventories (or other indicators) do not have sufficient granularity to capture the VCM's emission reductions.

In fact, the opposite may also be true; for example, where countries intend to use VCM to supplement policy in their achievements. At the present time it is not possible to know the extent of either potential scenario due to the lack clarity concerning how countries will set policies to plan and implement their NDCs.

Some stakeholders have questioned whether, at its current scale, the VCM would realistically trigger the disruption or displacement of national policies and measures. Others have argued that the scale of VCM may become much larger in the future, so these risks must be considered and addressed.

Box 3: Targeting specific NDC elements is challenging

It has been proposed by some stakeholders that VCM could target either emissions reductions/removals that are outside the host-country NDC scope and/or target the portion of the NDC that is stated as ‘conditional’ upon receiving further finance. Some stakeholders noted that these options are incompatible with CAs as:

a) a host-country could find it difficult to make an adjustment for something that it is not reporting on (in the case of non-NDC units) and
b) a CA would mean that this would not contribute to the any portion of the NDC (as it would be removed from accounting).

Other stakeholders and discussions at COP25, however, also highlighted that issuing credits for non-NDC scope activities may contribute to disincentivising the country’s NDC to become economy-wide, and that corresponding adjustments should, therefore, be applied to carbon credits inside and outside the scope of a country’s NDC.

It has also been assessed that the proportion of current VCM activities that fall outside or beyond the scope of the NDC is likely to be low. Anecdotal estimates have ranged between 10-20% of current VCM activity.

There are also practicality issues with this approach. In 2017-18, for example, Gold Standard examined a sample of project/country combinations and found few that could be stated with certainty as being either outside the NDC scope or clearly in the conditional portion of an NDC. This was for two main reasons:

a) The wording of the NDC is not clear enough to determine. For example, a clean cooking project may not be explicitly stated as an activity reported under the NDC, but the NDC may address related elements such as deforestation, domestic services, and/or energy efficiency without sufficient detail on what is included. In such cases, the host country would have to be consulted to determine intentions and may or may not be able to clarify in a reasonable timescale.

b) It is unlikely to be possible, at the project level to determine whether its impact falls in the unconditional or conditional portion of an NDC. For example, if a host country has an unconditional 20% renewable target that would increase to 30% if a conditional amount of 10% was financed from outside sources, it cannot be easily determined whether a specific project falls within the 0-20% portion or the 20-30% portion.

In sum, targeting either emissions reductions/removals that are outside the host-country NDC scope and/or targeting the conditional portions of NDCs cannot be realistically implemented by carbon crediting organisations. This option may become feasible, however, as NDCs and reporting infrastructure improve and become more transparent.

Legitimacy and ambition of "carbon neutrality" claims

'Carbon neutrality' is a commonly applied term to describe a state where organisations balance or compensate their residual emissions with the purchase and retirement of carbon credits. While this is a common term used in the market, no definitive consensus exists on its precise definition, application, and legitimacy.

Partly for this reason, not all organisational carbon neutrality goals, or their implementation, are created equal.

The credibility of a given carbon neutrality claim depends on several key aspects which includes but may not limited to:

a) The scope and boundary of the carbon neutrality target that has been set,
b) The ambition of the organisation's emissions reduction targets and strategy for its own emissions,[6]
c) The type, quality and attributes of the emissions reductions or removals (which could be packaged as carbon credits) being used to balance out the organisation's residual emissions; and
d) The transparency of the reporting and accounting of achievement towards the carbon neutrality target.

The last Working Group Statement highlights the particular importance of the ambition of the organization's emission reduction targets and strategy for its own emission:

> *Organisations should reduce internal emissions in line with science (i.e. a Science Based Targets Initiative 1.5C degree*

[6] A company's "own emissions" can in and of itself have different interpretations. A company could have a strategy to address only its operational emissions (Scope 1 and 2) or value chain emissions (Scope 1, 2, and 3).

trajectory or in line with further guidance from the initiative) which is reflected in the net zero ambition of the Paris Agreement. Without this, the retiring/purchasing organisation could not credibly claim to be on a "net zero pathway". Financing beyond boundaries without reducing sufficiently within boundaries will not lead to a global balance of emissions and sinks, i.e., achieve the goals of the Paris Agreement. Rather, this requires all organisations to balance internal emissions and sinks in line with science within the required timeframe.

In sum, companies should ideally move to set goals to put their internal emissions on science-based pathways and be using voluntary carbon credits to 'go beyond' these targets. Whether they are <u>always</u> compatible with organisational carbon neutrality or net zero targets is a question for which there is no consensus.

Assessing options related to double claiming for the VCM

This section considers the potential solutions put forward at the beginning of this paper, in light of the considerations of double claiming and its effect on integrity, additionality, and ambition.

Solution 1 – Non-NDC Crediting Model

This model assumes that VCM can issue voluntary credits for use in offsetting, from activities and units that are outside the scope of the host-country NDC, without the need to make CAs. In 2017, Gold Standard developed a tool to assess the potential for identifying projects that would qualify for this model. Testing concluded that generally, based on the current status of NDCs, it would be impracticable for carbon crediting organisations to determine with certainty whether projects were in or outside the scope of the NDC unless clear authorisation and clarification from the host country was issued. This may, of course, improve as NDC clarity improves.

In addition, the Article 4.4 of the Paris Agreement indicates that countries should move towards 'economy-wide' NDCs,[7] in other words not leaving sectors or activities outside the scope. Limiting the VCM to credits issued outside the scope of an NDC could be perceived as disincentivising the move to economy-wide NDCs and would also unfairly discriminate against countries that have submitted economy-wide NDCs already.

[7] "Developed country Parties should continue taking the lead by undertaking economy-wide absolute emission reduction targets. Developing country Parties should continue enhancing their mitigation efforts and are encouraged to move over time towards economy-wide emission reduction or limitation targets in the light of different national circumstances." [(UNFCCC. 2015. "Paris Agreement.")]

Solution 2 – Financing Emission Reductions Model

This option was considered in the 2019 Working Group discussions.

It was recognised that, in the Financing emissions reductions model the mitigation impact is intentionally double claimed by the host-country towards its NDC and the buyer of the emissions reduction/removal. As previously noted, this may be acceptable if the target of the buyer is not to use them for voluntary offsetting or for meeting a carbon neutrality target. This may be useful, for example in the case of domestic voluntary schemes designed to contribute to NDC targets or where companies simply wish to support a given country without a need for offsetting. This implies a consideration by the host-country of the appropriateness and regulation of claims under the scheme to avoid confusion.

Solution 3 – Corresponding Adjustment Model

As previously noted, the text of the Paris Agreement does not enforce a policy or legal mandate upon voluntary markets to act in a particular way. Hence, discussion of whether and how CAs are required for VCM are limited to environmental integrity risk of the mechanism itself. The group acknowledges, however, that individual countries may set requirements for CAs within their jurisdiction, to which individual projects (and standards) would need to adhere.

Based on the above exploration of double claiming and other solutions, the working group concludes that the negative effects stated could potentially occur where the impact of offsetting is nullified by capture by host-country reporting (i.e. where achievements are limited to rather than enhanced by the contribution of the VCM). This could also lead to weak host country policy being ‘propped up’ by the VCM or where the country sets less robust or lower ambition policy to achieve climate mitigation and instead ‘free-rides’ on the VCM.

A CA would help to ensure that the carbon credit project provides emissions mitigation benefits that go beyond the level of ambition of the host country’s NDC that otherwise would not have been achieved. The key potential benefits of the application of a CA (or other equivalent mechanism that may be developed) are:

- Resolving the issue of the impact of VCM being nullified by displacement of host-country action;
- Removing the possibility of host-country free-loading and propping-up of poor policies;
- Transparency;
- Guaranteeing the unique ownership of claim/attribute by voluntary buyer; and
- Allowing flexibility to use the credit in regulated markets such as CORSIA (dependent on other criteria being met).

Alongside these benefits, a number of other issues should be considered:

- **Responsibility**: As has been demonstrated, a voluntary project will be assessed for additionality (i.e. project-level additionality) and could be assessed for ongoing financial need (i.e. unit-level additionality). In the “conscious free-riding” or “unconscious free-riding” scenarios described above, the risk of negative perception will be felt by the project and its beneficiaries as buyers become concerned about the validity of the credits. This results in a disincentive to voluntary, privately financed action which is contradictory to the stated aims of the Paris Agreement.
- **Practicality**: Based on current understanding, status of the Paris Rulebook negotiations and previous experience (for example under CDM) the obtaining of a Letter of Authorisation (LOA) from the host country and CA could be challenging and complex as they require NDC interpretation and detailed processes on the part of host country, carbon crediting organisations, and project developers. In the short- to medium-term this may be a risk to projects, particularly those with lower capacity to obtain.
- **Sovereignty**: This solution assumes that the host-country did not intend to use VCM financed activities and then takes advantage of the situation once it becomes aware. An alternative position may exist where a country was fully aware of the VCM and intended to use it to attract finance to certain sectors, for example through domestic voluntary schemes or a general assumption that part of its target would be achieved through voluntary contributions. This could be overcome by applying the Financing Emissions Reductions Model in such cases, however.
- **Safeguarding against exclusion, exploitation, or corruption**: Concerns were raised to Working Group members at COP25 that in some circumstances, the requirement for CAs could lead to:
    - Corruption, for example where a CA is obtained from host country through corrupt means, such as illicit payment
    - Exclusion, for example where a country cannot take advantage of voluntary market financed projects as it does not have capacity to assess whether authorizing CAs may conflicts with the country’s best interest such as meeting their NDC or even other development priorities; and
    - Exploitation, for example where a host country does not feel it can afford to refuse voluntary investment and hence gives up emission reductions that it otherwise did not intend to.
- **Broader voluntary climate action**: The above issues are framed in light of the VCM. This challenge however is not exclusive to the VCM and could be just as relevant for direct action by organisations, based on voluntary targets such as Science Based Targets, charitable giving, or other climate action. This primarily relates to the claims being made by the VCM buyer, specifically the interpretation of offsetting as an additional environmental impact.

Box 4: Additionality in VCM

Additionality will remain a critical component of carbon markets, regardless of the use and claim associated with the credit. It is likely that new or updated approaches to assessing additionality will be developed in the coming years, focusing on the two traditional levels:

1. Additionality and prior consideration at project inception – an assessment of whether the mitigation activity requires carbon market finance to be implemented at that time and that this source of finance was considered in decision making.
2. Additionality reviews (for example, when a project is seeking a renewal for another crediting period) – an assessment of whether the activity is now mandated or subsidised by regulation or policy and should no longer receive carbon market support.

While these two approaches already exist in carbon crediting programmes, it may be useful to review whether these are sufficient to ensure that the VCM is always complementary to government climate policies and an enabler of greater ambition.

Conclusions

This paper builds upon the Working Group's first statement and namely explores the risks of double claiming in the VCM.

The paper analyses other key issues including how additionality assessments could change to be more impactful and the legitimacy and ambition of "carbon neutrality" claims. The Working Group acknowledges the importance of these questions and encourages experts to continue exploring these.

With regard to the impact of double claiming emission reductions from voluntary carbon credits, the Working Group lays out two options. The policy position on potential options depends on whether it is considered that double claiming has the potential to nullify or even increase the intended impact of using VCM for offsetting purposes (as well as other potential concerns around host-country policy). Hence, the Working Group and different stakeholders fall into three groups: Those that support having CAs for carbon credits voluntarily purchased by companies outside the host project country, those that support a transition to CAs for these transactions, and those that do not consider there to be an issue (and therefore advocate the continuation of 'business as usual').

Pathway 1 – Maintain business as usual + transparency

This option would allow the VCM's registry and accounting systems to operate as they currently do and does not consider CAs necessary when buyers purchase carbon credits for voluntary purposes. A CA would likely only be required if legislated by the host-country or when the buyer would like to use it in the context of regulated programmes, such as CORSIA. Transparency of the transaction would be provided by carbon crediting organizations maintaining and sharing registry records with host-countries who can then decide how to act on that information. The Financing Emissions Reduction Model could still operate under this pathway

Pathway 2 – Corresponding Adjustment Model applied to units intended for offsetting and a Financing Emissions Reductions Model applied for all other units

This option resolves the potential that offsetting has no overall impact (or even an increase in emissions), as described earlier in this document, while maintaining the possibility of using the VCM for other purposes through the Financing emissions reductions model. It implies a differentiation between the two types of units in registries[8]: one type of carbon credit that can be used for offsetting where a CA has or will be made and another credit that cannot be.

A further decision for advocates of this model is then required for credits from activities that fall outside NDCs – i.e. can these be considered for offsetting or limited for use in the Financing Emissions Reductions Model.

Carbon crediting organizations, policymakers and other stakeholders to the VCM are invited to assess between these options, which should also be considered in light of market understanding and receptiveness to change. For example, the difference (or overlap) between CA and Financing Emissions Reductions Model may not be immediately obvious to all market participants and risks confusion and misuse by buyers. Likewise, individual actors may wish to purchase or recommend credits only if they have a CA, based on their view of the scenarios described, assuming they are available.

Box 5 - Are credits that are guaranteed not to be double claimed by the host country more valuable than those that are not?

It is clear from the previous sections that there may be valid reasons for and against the application of CAs, either to resolve negative integrity effects or potentially to optimise, increase or improve the value the units have. This box considers whether a carbon credit that has a CA or other equivalent alignment with the Paris Agreement is more beneficial or valuable than one that does not.

The value of carbon credits can be affected by several factors including project type, location, vintage (i.e. year in which the emissions reduction occurred), whether a CA was applied, and other attributes.

In the context of compliance schemes such as CORSIA (see Box 1), a CA is essential. This flexibility for a credit to be used in compliance schemes or VCM could also increase its value in the market. In addition, some companies may prefer carbon credits with CAs because they might be perceived as being of higher integrity, even if none actually exists.

Conversely, some companies may prefer to support the host country and not wish for a CA to be in place, for example if the company has extensive interest in and ties to a country or

[8] This differentiation of units is likely to be even more complex as individual compliance systems could have specific requirements. In other words, registries will have to tag carbon credits so buyers can know, for example, if it can be used under the ICAO CORSIA, the Columbian carbon tax, etc.

region. This would also be impacted by any perception of exclusion, exploitation or corruption potential caused by VCM in vulnerable places, particularly for development projects, war/disease zones, refugee camps, etc.

The supply and availability of different types of units will also be a factor. For example, if CAs prove difficult to obtain in the VCM then natural scarcity may drive up the cost. Conversely, if only a very limited pool of CA credits is available (for example, if airlines option the vast majority under CORSIA) then the price may increase as a result of scarcity.

It is, therefore, not possible to properly address whether or not a CA universally increases the market value of a voluntary carbon credit at this time, beyond acknowledging that it potentially could, alongside a wide range of other factors.

When and how could a transition to the CA Model happen?

This section considers the need for a robust transition to Pathway 2 specifically, as described above. This is not relevant to Pathway 1 as no transition is necessary in that case.

As highlighted earlier in the document, while a CA model can resolve a number of potentially negative effects on climate ambition, there are also concerns about its practicability and its impact on safeguarding and viability of projects (i.e. that projects may fail due to an inability to obtain necessary host country documentation). Conversely the Financing Emissions Reductions Model is currently not well understood in the market and its potential applications remain nascent. Hence an immediate roll-out of Pathway 2 would likely be unsuccessful on a number of levels.

Alongside this, it is clear that the Paris Rulebook negotiations, encompassing the issue of CAs, remains ongoing. It would not, therefore, be practicable to immediately require these as few, if any, host-countries would be able to provide them.

Hence, a transition period that should define the conditions under which it would be appropriate to require CAs for off-setting and differentiate these from carbon credits tagged for use under the Financing Emissions Reductions Model. This should be designed with the following, non-exhaustive conditions, and principles in mind:

- Agreement among countries within the UNFCCC on the role and implementation of CAs under Article 6 of the Paris Agreement
- The practicability, willingness, and readiness of host-countries to apply the mechanism, also considering the safeguarding issues for vulnerable countries
- Ensuring continuity of good mitigation projects while the application of the mechanism is realised, for example, recognising the willingness of countries to issue them
- Ability of carbon crediting organisations to implement robust policies and processes to assess CAs
- Ability of carbon crediting organisations and registries to differentiate between different types of carbon credits and their uses

- Further assessment of the role of VCM in domestic policies and how to define the claims associated

During any transition period, consideration may need to be given to whether credits issued are suitable for off-setting or fall into the Financing emissions reductions model. The transition period could be used to develop further market insight and understanding of the difference between these models and hence clear delineation in registries may be better held until the conditions for robust and fair transition are met. However, some Working Group members and other stakeholders consider this transition unnecessary.

Due to the uncertain nature of UNFCCC negotiations on Article 6 and lack of clear insight from host countries, it is not feasible to set a specific timeline for transition. Instead, a number of options could be applied, for example review during first reporting period of Paris Agreement or staggering the roll out of new requirements based on country capacity and the ongoing viability of projects. Proponents of this option are recommended to carefully consider the implications of this requirement and develop robust and fair transitionary requirements accordingly.