VCMI

05

Ensuring high-integrity carbon market activities

CLIMATE FOCUS

UNDP

KEY DECISION STEP 05

The host country ensures high-integrity carbon market activities

Considerations

5.1 Align VCM activities with host country policies
5.2 Put in place national carbon accounting rules
5.3 Ensure high-quality supply of carbon credits
5.4 Ensure high-integrity use of carbon credits

Ensuring integrity is critical to building trust in VCMs and enabling them to grow in size and value. Entities operating in VCMs who do not act with integrity undermine the reputation and ultimately the value of VCMs. Building the foundations for thriving VCMs requires integrity to be realized on both the supply-side and demand-side. This will underpin a pricing system that is fair, reflects true value, creates jobs, and protects nature.

5.1 Align VCM activities with host country policies

Carbon market investors often gravitate to projects with the lowest abatement costs and lowest risk. Carbon investment often flows to projects that generate the highest value from carbon credits with the lowest investment risk. To ensure that these carbon credits correspond to real and measurable greenhouse gas (GHG) emission reductions and removals, strong carbon crediting and certification standards are needed. VCM activities also must adhere to safeguards and comply with the legal frameworks of the host country.

Host countries can align VCM activities with national climate and development policies by proactively taking measures to regulate the market and direct investments. Governments can promote investments into voluntary and compliance carbon market activities with the goal of attracting national or international direct investment. Lack of alignment between government policies and VCM stakeholders can result in duplication of efforts, unnecessary costs, and inferior policy outcomes. Host countries can align VCM activities and promote overall policy coherence through, for example:

- Integrating safeguards for carbon investments into national environmental, social and governance (ESG) requirements

- Establishing a common reporting framework for carbon investments that ensures transparency and enhances investor accountability

- Actively promoting carbon investments in priority sectors and areas through data sharing and building an enabling environment for investments.

Host countries can consider permitting limited use of certain credits generated by VCM activities in national carbon pricing schemes. National carbon pricing schemes put a price on GHG emissions and seek to create national investment incentives into mitigation action. Governments can mandate the inclusion of only high-quality credits for high-integrity uses under these schemes. These measures can increase the cost-effectiveness and efficiency of climate measures. In designing such schemes, governments can ensure that mitigation obligations are fairly distributed, put in place relief measures for more vulnerable groups, and mandate benefit sharing by VCM activities.

5.2 Put in place national carbon accounting rules

Integration of carbon market activities – voluntary and regulated – into national climate strategies requires host countries to implement robust and transparent carbon accounting and tracking systems. For many countries, participation in Article 6 transactions and the ability to claim mitigation outcomes generated through carbon market activities towards their NDC will require updating national carbon accounting systems.

Robust systems are needed to ensure that GHG inventories, NDCs, and Article 6 accounting for internationally transferred mitigation outcomes (ITMOs) are aligned and interlinked, and measurement, reporting and verification (MRV) is harmonized. Where governments include VCM activities in their climate strategies and/or where they decide to make corresponding adjustments for carbon credits transacted in VCMs, MRV systems need to extend to VCM activities.

When planning carbon market engagement, governments need to assess MRV capacities, particularly in the context of Article 6.2 cooperative approaches under the Paris Agreement. Implementation of Article 6 of the Paris Agreement requires designation of institutional responsibilities for NDC accounting and environmental permitting. Governments must also consider how to align GHG reporting of corporates and the measurement of carbon market project GHG emission reductions and removals with the country's NDC accounting. In some cases, new public institutions may need to be built, for example, to establish and maintain carbon registries.

There are different initiatives that support countries in achieving Article 6 "readiness" (e.g., the West African Alliance for Carbon Markets and Climate Finance, Article 6 pilot transactions, or bilateral technical assistance programs).

Lack of consistency between national climate change reports and other national reports is a longstanding issue. GHG inventories included in developing countries' Biennial Update Reports and National Communications, forest reference levels submitted to the UNFCCC, and NDC targets often do not align, leading to challenges in measuring mitigation progress.

There are a variety of reasons for divergence in data sources and projections, for example:

– A lack of institutional coordination

– Uncoordinated support by different capacity building projects

– Different calculation assumptions and/or data compiling and reporting periods

– Specific sets of rules that have been applied – for example, the requirements to access carbon markets via Article 6 versus in the context of REDD+[1].

Improving consistency is important for clarifying how GHG emission reductions and removals generated through VCM activities can be counted towards NDC achievement. Aligned MRV systems are necessary for accounting under the Paris Agreement, particularly if a country intends to engage in Article 6 transactions or

[1] REDD+ stands for Reducing emissions from deforestation and forest degradation and the role of conservation, sustainable management of forests and enhancement of forest carbon stocks (see Glossary).

other finance opportunities that require integration with national accounting (e.g., CORSIA transactions).

Previous experience in aligning national and project-level carbon accounting can inform preparations to extend national MRV systems to VCM activities. The nesting of REDD+ projects in jurisdictional REDD+ programs provides an example of aligned national and VCM MRV systems.

Nested REDD+ refers to the integration of different accounting systems – at the levels of both private-sector-led projects and government-led jurisdictional programs – to create a common accounting and carbon crediting system. Nested REDD+ exemplifies how a host country can align systems to optimize the way in which projects, or subnational programs, contribute to the country's targets. This is particularly relevant where VCM projects request corresponding adjustments for carbon credits generated through approved activities, which would result in the deduction of GHG emission reductions or removals from national NDC accounting.

5.3 Ensure high-quality supply of carbon credits

Carbon credits are high-quality if they represent real, additional, and measured GHG emission reductions or removals generated by an activity that applies robust social and environmental safeguards. The credibility of project types and individual projects is based on the methodologies used, demonstration of additionality and permanence of mitigation outcomes, how leakage and GHG emission reductions or removals reversal risks are addressed, and on the political and social contexts in which a project is developed.

Credible standards apply methodologies that conservatively measure and assess baselines, additionality, leakage, and permanence to ensure carbon credit quality. However, standards are not without fail and there are various initiatives that seek to build greater transparency around the quality of carbon credits.

Independent international initiatives have defined, or are in the process of defining, criteria to distinguish the supply of high-quality carbon credits. The most prominent effort to define quality criteria for carbon credits are the Core Carbon Principles of the Integrity Council for Voluntary Carbon Markets (ICVCM)[2] (see Box 1). In parallel, the Environmental Defense Fund (EDF), the World Wide Fund (WWF) for Nature, and Oeko-Institut have founded the Carbon Credit Quality Initiative with the goal of formulating a methodology to assess the quality of carbon credits.[3]

Various private companies also offer also the rating of carbon credits (e.g., Sylvera, BeZero, or Calyx Global).

[2] ICVCM (2022). *Core Carbon Principles*. Available at: https://icvcm.org/wp-content/uploads/2022/07/ICVCM-Public-Consultation-FINAL-Part-2.pdf (Accessed 4th April 2023)

[3] CCQI (2023). *The Carbon Credit Quality Initiative website*. Available at: https://carboncreditquality.org (Accessed 4th April 2023)

Box 1: Core Carbon Principles

The ICVCM has developed Core Carbon Principles to assess the quality of carbon crediting standards and types of carbon credits. Under the ICVCM, high-quality credits and programs must go beyond demonstrating additionality, conservative baselines, and permanence, to include:

- Providing public, comprehensive, and transparent information about mitigation activities
- Ensuring there is no double counting
- Demonstrating that the crediting program has effective governance
- Maintaining a registry that tracks each mitigation activity and carbon credit
- Requiring validation and verification by independent third parties
- Following best practices for environmental and social safeguards
- Delivering positive sustainable development impacts
- Transitioning to net-zero emissions by avoiding practices that lock in emissions or are incompatible with net-zero pathways.

5.4 Ensure high-integrity use of carbon credits

High-quality carbon credits must be used as part of a science-aligned mitigation strategy, transparently reported, and credibly claimed to be high-integrity. Corporates are the main users of carbon credits transacted in VCMs and therefore are primarily responsible for ensuring high-integrity use. The Voluntary Carbon Markets Integrity Initiative (VCMI) provisional Claims Code of Practice[4] identifies the following steps that corporates should follow when using carbon credits and making climate claims:

- Corporates must set and make demonstrable progress toward science-aligned emission reduction targets across their value chains before making voluntary use of carbon credits

- Corporates must use high-quality credits that are associated with a credible carbon standard, from activities that promote environmental quality and positive socio-economic impacts, compatible with human rights, and from activities that apply social safeguards and equity

- Corporates must report transparently on their use of carbon credits. This includes reporting on the number of credits claimed and retired, whether or not carbon credits are associated with corresponding adjustments, the standard, and project names.

[4] VCMI (2022). *Provisional Claims Code of Practice*. Available at: https://vcmintegrity.org/wp-content/uploads/2022/06/VCMI-Provisional-Claims-Code-of-Practice.pdf (Accessed 4th April 2023)

The final VCMI Claims Code of Practice for corporate and non-state buyers of carbon credits will be released in 2023.

Host countries can facilitate high-integrity use by creating supportive legal and policy frameworks. For example, governments can:

- Clarify government expectations on buyers for the high-integrity use of carbon credits, including actions buyers should take and claims that can credibly be made
- Provide information on what buyers should seek in terms of high-quality carbon credits, including social and environmental safeguards and how benefit sharing agreements should be arranged
- Align regulation on corporate sustainability disclosures, consumer protection, advertising standards and financial regulation with guidance on high-integrity use of carbon credits
- Refuse advocacy proposals by corporates for regulation that would undermine climate action and call out corporates that are engaged in the use of carbon credits while advocating against climate action
- Co-sponsor or co-develop carbon market activities and ensure that credits are only sold to high-integrity buyers
- Clarify and enforce land tenure laws. Selectively provide concessions for VCM activity development only to projects that meet high-quality and high-integrity standards.
- Require that VCM activities report to domestic GHG inventories and GHG emission reductions and removals registries, and make those inventories and registries publicly available
- Clarify if and how approvals and authorizations for VCM activities will be provided, and under what conditions. If governments will authorize for corresponding adjustments, they can specify the conditions and requirements for VCM activities to be approved.

The Voluntary Carbon Markets Integrity Initiative is a multistakeholder platform to drive credible, net zero-aligned participation in voluntary carbon markets.

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