

# **VCM and Article 6 interaction**

## **Discussion paper on the use of Corresponding Adjustments for voluntary carbon credit transfers**

*6 January 2021*



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# 1. Problem statement

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The challenge of how the Voluntary Carbon Market works in the context of the Paris Agreement has been the subject of much debate and analysis. The purpose of this paper is to summarise the debate and provide a potential framework for resolution. The views in this paper have been developed based on interviews with a wide range of market participants and experts.

The scope of this paper is relatively narrow - how the voluntary carbon market can most effectively interact with the Paris Architecture. It does not consider processes for emission transfers between compliance entities under the Paris Agreement – including CORSIA - as well as governments. These transfers require the use of International Transferred Mitigation Outcomes (ITMOs) and whilst more work needs to be done to operationalise these systems, the accounting arguments are relatively settled. In this paper we also do not explore other potential issues associated with double-counting, such as credits potentially being registered in more than one place. These types of issues are readily solvable.

The problem statement in this paper centres around the issue of potential double-counting between the emission reductions from a voluntary project used to offset corporate emissions, and the host country that has made a commitment to reduce emissions through its Nationally Determined Contribution (NDC) under the Paris Agreement.

From the perspective of global accounting for emissions, there should be no double-counting, as voluntary buyers have no reporting requirements under the Paris Agreement. Only countries have obligations to set emissions targets and report on progress at the global level. Emission reductions from projects in a particular country – whether funded internally within the country or from corporates elsewhere – end up being included that country's national emissions inventory. The host country's national emissions inventory is then compared against that country's NDC. This position has been put forward by the likes of ICROA, IETA and Verra.

This argument, however, is over-simplified. The issue is less about double-counting and more about double-claiming. Even though companies have no reporting obligations under the Paris Agreement, the behaviour of customers and other stakeholders could be influenced by the claims companies make on their use of carbon credits – also referred to as offsets where the intention is to compensate for a company's own emissions. For example, an airline may use carbon offsets to offer "Carbon Neutral" flights, which may lead to an increase in flights by customers who are concerned about their personal carbon footprint. In this example it is important that the carbon credits genuinely reduce emissions beyond what would have otherwise occurred.

The argument for not allowing a voluntary buyer to claim they have offset their emissions by the use of a voluntary carbon credit is that a country's NDC acts like a target. Once a country has made such a declaration it will find a way to achieve those reductions with or without the presence of that project. The project creating the emission reduction, partially financed through the sale of carbon credits, displaces other activities that would achieve the same outcome. Therefore, the claim on the emission reduction is not additional to what would have otherwise occurred, and cannot be interpreted as offsetting emissions created elsewhere.

To ensure that an emission reduction is additional to what a country has committed to achieving in its NDCs, the national emissions in the country where the project takes place would need to be increased by an equivalent amount – known as a Corresponding Adjustment (CA). Without this adjustment there is a risk of a company claiming for a reduction in emissions that also shows up in the host country's national accounts.

The rest of this paper examines the issues around the claims on voluntary carbon credits and their relationship to NDCs, the effect on mitigation incentives and explores a potential solution space.

## 2. Offset Claims and NDCs

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Two issues are at the heart of the accounting issue for voluntary carbon credits or offsets: (i) the type of corporate claim on the carbon credit, and (ii) the nature of the NDC in the host country.

The simplification of whether CAs should be applied to projects is effectively an insurance policy against non-additionality of the project. In principle, if methodologies and standards are reliable measures of additionality, then Corresponding Adjustments should not be required. Tests of additionality should in theory, guard against projects that would have been undertaken in the absence of the finance from the sale of the carbon credits. All methodologies exclude projects that are required by regulation, but it is more difficult to determine additionality against policy aims and potential future legislation. The fact that there remains a debate over the use of Corresponding Adjustments indicates that these tests cannot be 100% accurate, which, in itself, suggests a need for CAs in some instances.

### 2.1. The Claim – “offsets” vs “contributions”

Whether Corresponding Adjustments should be applied to the export of carbon credits depends on the claim being made by the acquirer of the credit. We outline 3 main types of claims – the first one being the most widely used.

#### **Claim 1 : “Carbon offsetting” / “Carbon Neutral” / “Net Zero”**

Corporates acquire carbon credits in order to reduce their carbon footprint. Many firms want to communicate to their customers and stakeholders that their emissions have been “offset”, meaning that the firm’s emissions of CO<sub>2</sub> have been reduced by an equivalent amount, resulting in no net increase in emissions. This could occur through reductions in emissions or removals of CO<sub>2</sub> from the atmosphere. CO<sub>2</sub> is constantly being removed from the atmosphere (eg by plants), and many human activities both increase (eg fossil fuel combustion) and reduce emissions (eg renewable energy, energy efficiency). The challenge of defining the carbon credit, or offset, is determining whether the project would have happened in the absence of the sale of the carbon credits – whether the project is “additional”. If it is not additional, the term offset cannot be applied.

Customers’ and stakeholders’ interpretation of the term “offset” is relatively clear. However, if a project that generates a carbon credit falls under another entity’s emissions cap – for example a national NDC – then ambiguity is introduced. If the project does not go ahead there is the possibility that the country will undertake other measures to achieve its emission reduction target, suggesting that the project might not be additional.

Corporates often use the term “offset” as it is simple and intuitive. Alternative claims embody a similar understanding, such as “Carbon Neutral” and “Net Zero”. Although there can be subtle

differences in understanding of these terms amongst the expert community, corporates tend to use these terms interchangeably. The concept of additionality is central to these claims.

The other advantage of an offset (or Carbon Neutral) claim is that the firm's climate impact and the process of offsetting it, can be calculated precisely through the unit of tonnes of CO<sub>2</sub>. This adds clarity to the company's communications.

### **Claim 2 : Contributions to emission reductions**

A firm can avoid the claim of offsetting its carbon emissions, but achieve a similar effect, by claiming to have contributed to another entity's emission reduction target. This avoids the problem of determining whether a project is additional to what a country might achieve under its NDC. The efforts of the company making a voluntary action and that of the government of the country where the project takes place are aligned.

The disadvantage of this approach is that the company cannot claim categorically that its emissions have been "offset". It is possible to calculate the emissions benefit of contributing to a country's NDC target, but it is impossible to say whether the emission reductions associated with project would have been achieved by other means. The government may find other ways to achieve their targeted emission reductions.

We are not aware of many companies using this terminology to date. Most companies using carbon credits have wanted to convey the concept of offsetting or neutralising their emissions. However, it could become more popular if the associated carbon credit does not require host government approval for a Corresponding Adjustment, where the transaction would be simpler and easier.

### **Claim 3 : "Emission reductions"**

It is also possible to create a more nuanced claim that sits between the carbon offset claim and contributions claim. For example, some companies are using the general term "use of emission reductions" in association with their climate achievements, and are avoiding the use of the term "offsets". In this case it is not clear whether the company is claiming additionality, although if the intention is to sell a Carbon Neutral product or service then the implication would be closer to Claim 1.

## **2.2. Not all NDCs are equal**

As noted above, whether emission reductions from a project can be treated as an "offset" rely on whether the emission reductions associated with that project would have happened in its absence. If the emissions targets contained in the National Declared Contributions are considered legally binding emission caps, then there is a good case that governments will find other ways of achieving the required emission reductions. In such a situation the NDCs are assumed to act like a regulatory cap

with penalties for non-compliance, such as the EU ETS, California cap and trade scheme, and how the Kyoto Protocol was intended to work at a national level. However, the reality of NDCs under the Paris Agreement is different. This is for two main reasons:

### 1. NDCs are not legally binding targets

The Paris Agreement was designed to be a voluntary process, with an informal process of peer review and 5 yearly updates (the ratchet). Under the Kyoto Protocol there were penalties for countries that failed to meet their targets, but these only applied to developed countries.<sup>1</sup> Developing countries had no targets. Without an enforcement regime it is more difficult to make the argument that countries would find ways of achieving their targets if the voluntary emission reduction project had not gone ahead.

### 2. NDCs are produced by countries of widely varying wealth and institutional capacity

To set emission reduction targets in an NDC and put in place measures to achieve them, requires resources and expertise. Developed countries should have the capacity to understand their emission projections, the costs of emission reduction measures and to set targets that they believe are achievable. They should also have the legal systems to set and implement appropriate regulations and to enforce compliance.

This is typically not the case in developing countries and even less so in least developed countries. In these countries, the NDCs are more likely to be seen as aspirational, with higher levels of uncertainty over whether the targets will be achieved. In many countries, even if legislation is passed, enforcement is difficult to achieve on the ground. This is certainly the case in land-use activities, such as the protection of forests, where governments often lack the resources to adequately police and enforce national policies. In countries such as Brazil, forestry and deforestation laws are notoriously unenforceable.

In theory, because NDCs are created voluntarily, all countries should be able to set NDCs that are stretching but achievable. Many NDCs of developing reflect this uncertainty. They often allow for growth in energy use and emissions in line with economic growth, or are partial, setting targets for some sectors of the economy.

However, there is still a gap between what countries set themselves and their ability to achieve the targets. Even in the G20 by 2019 only 6 out of 20 countries were on track to meet their NDC targets

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<sup>1</sup> A party that failed to achieve its Kyoto emissions target would be required to make good its deficit in the following period, by buying the equivalent number of credits from other party plus an additional deduction of 30%.

by 2030. High additional effort was needed by 5 countries, including Canada, Australia, South Africa, South Korea and the US. Argentina and the EU28 were also not on track, needing low additional effort.<sup>(2)</sup>

In a country falling short of its NDC target, it is easier to argue that the emission reductions from a project funded voluntary would not have been achieved elsewhere. Such a project would therefore be more likely to be additional – and by implication – be achieved without the need of a Corresponding Adjustment.

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<sup>2</sup> *Elzen et al, 2019, Are the G20 countries making enough progress to meet their NDC targets?, Energy Policy*

### 3. The impact of Corresponding Adjustments on mitigation incentives

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Before assessing options for accounting for transfers between the voluntary market and the national NDCs we need to clarify what the system is actually trying to achieve. Too often in the debate on Corresponding Adjustments this step is overlooked. We propose that the overall purpose of using voluntary carbon credits should be the following:

***“to ensure the maximum benefit for the climate from corporate and government commitments to reduce emissions”.***

With this objective, it follows that emission reduction activities should be maximised, in aggregate, across all participants in the system. There are three main actors:

1. Countries as parties to the Paris Agreement – Governments are required to submit their NDCs containing self-determined levels of ambition in reducing greenhouse gases. These are revised and improved on a five yearly cycled (2020-21 being the first update from the signing of the Paris Agreement in 2015).
2. Corporates committing to voluntary action – Corporates have no reporting requirements under the Paris Agreement but can set themselves voluntary emission targets, potentially using carbon credits to achieve them.
3. Consumers and related stakeholders – Individuals may react to corporate statements on their emission response and change their behaviour, potentially consuming more or less of a firm’s products/services. It is a more theoretical link, but “related stakeholders” may also include governments who could be influenced by voluntary corporate climate commitments, and change their approach to climate policies and legislation. However, we are not aware of governments taking individual corporate climate commitments into account when setting national climate policies. Governments consider trends in sectoral emissions and their projections using various technical and economic forecasting techniques, but these tend not to use individual voluntary corporate climate commitments as inputs. It is possible that in the future, governments may look at Scope 1 corporate commitments to understand where corporate emissions may be heading, but they would not consider the use of carbon credits. Any transfers of carbon credits for national emissions accounting and contribution to NDCs would need to be accounted for as Internationally Transferred Mitigation Outcomes (ITMOs) under Article 6.2 of the Paris Agreement.

## The impact of Corresponding Adjustments on mitigation incentives

The extent to which each of these actors reduces emissions in the future is a function of two factors:

1. **Ambition** - Governments and corporates set targets for reducing emissions. Government targets are contained in their NDCs. Corporates can volunteer their own emissions targets although increasingly they are under pressure to be aligned with Net Zero pathways. Consumers and other stakeholders do not set targets but may change their behaviour.
2. **Effort** - Having set a target these actors need to invest resources in trying to achieve them. The voluntary market and government activities could interact here. If corporates invest to reduce emissions in a host country, it is possible that governments may then do less to achieve the same target in their NDCs. In this scenario, the corporate claim that emissions have been “offset” is ambiguous.

Figure 1 summarises the direction and approximate magnitude of these effects, resulting from the transfer of emission reductions for voluntary use under an NDC.

**Figure 1. Effects of applying Corresponding Adjustments for voluntary market transactions**  
 +++ / - - - sign indicates direction and strength of impact on emissions (+ indicates emissions reduced)

	Host Country NDC		Corporate Buyer		Consumer / other
	Ambition	Effort	Ambition	Effort	Effort
Without Corresponding Adjustment	+++ Governments incentivised to be more ambitious as they will use all means available to achieve their targets.	- Likely that emission reductions from voluntary project would be seen as contributing to emission targets in NDC, leaving less for government to do.	+ Likely that corporates will seek higher levels of ambition in knowledge that supply of credits is more accessible.	- With the supply of cheaper credits more available, corporates may be incentivised to undertake less abatement internally and rely more on offsets.	- If corporate claims for offsetting emissions are not genuinely additional, consumers risk being misled and potentially consuming more of a product/service.
With Corresponding Adjustment	- - - If governments are required to adjust up their emissions for exports of credits for voluntary purposes they would be incentivised to set more lenient targets in the first place. if they want to access to finance associated with carbon credits.	+ With CAs the effort required to achieve the host country's NDC remains the same, irrespective of emission reductions generated from a project supported voluntarily	- Corporates could seek lower levels of ambition in knowledge that supply of credits might be more restricted.	+ If credit supply is more restricted corporates may be incentivised to undertake more abatement internally than rely on offsets.	+ An offsetting claim backed up by a CA gives consumers reassurance that offsets are additional to what would otherwise occurred.

### 3.1. Impact on host country NDC ambition

The magnitude is a qualitative judgment at this stage of the study, but the direction of effect is arguably a more robust assumption. The point made here is that the total value of the voluntary carbon market is small relative to the efforts to reduce emissions applied at the national level <sup>(3)</sup>. NDCs are central to addressing the climate challenge.

If CAs are not applied to voluntary market transactions, governments are more likely to be incentivised to create stretching targets in their NDCs. They would set targets in the knowledge that voluntary market capital could be accessed, as well as all the public sector policy tools. Conversely, if CAs are applied to all VCM transactions, governments may be more reluctant to set ambitious targets. There is even a risk that governments may “low-ball” their NDC targets in order to ensure that if CAs were applied after any transactions they would still have head room to achieve the NDC. The incentive is set up because of the difficulty in ensuring additionality of project-based credits, as in the VCM. By introducing a CA, the government under-writes the additionality risk of the project.

#### ***Could Conditional NDCs be used to increase ambition incentives?***

Conditional NDCs could be used as an alternative to a Corresponding Adjustment in order to ensure emission reductions are not double-claimed through voluntary market transactions. Conditional NDCs were introduced to incentivise governments to set more ambitious NDCs if they had greater access to international finance. One of the sources of international finance could be the voluntary carbon market. However, Conditional NDCs are considerably less robust and well-developed than underlying NDCs, and even these need greater work to refine and update for many countries. For example, how international finance is defined is unclear and could include a wide range of instruments from carbon finance to multi-lateral loans and other forms of concessional finance. Tracking and monitoring this finance would add complexity. The general view from experts spoken to in this study was that until such time as a consistent framework for defining conditional NDCs is introduced, they would be a difficult benchmark against which to assess the achievements of a country. However, in theory Conditional NDCs provide an elegant mechanism to ensure VCM transactions are not double-claimed by voluntary buyers and host governments.

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<sup>3</sup> We calculate that under optimistic assumptions the voluntary market for carbon credits would be no more than 10% of world investment in clean energy by 2030. Put another way the combined emission reduction ambitions from the voluntary market in 2030 would represent between 1-2% of current global carbon emissions.

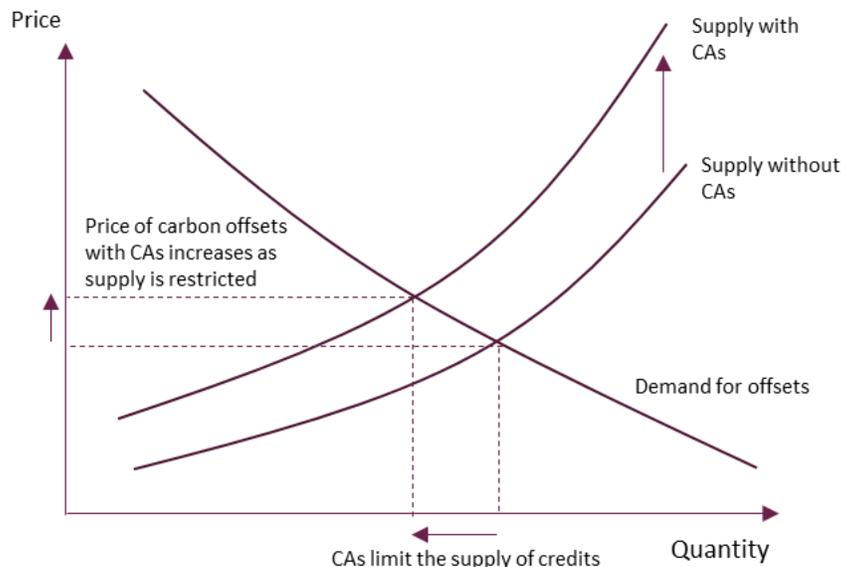
### Impact on host country NDC effort

If Corresponding Adjustments are applied to a VCM transaction the effort required by the host country to achieve its NDC is unchanged. Assuming that the project is truly additional, actual emissions are reduced in the host country, but accounting emissions are increased by an equivalent amount. If a CA is not applied to the transaction, then the emission reduction project supported by voluntary action helps the country achieve its target. Host governments would be unlikely to raise the level of ambition in such circumstances (unless the conditional NDC approach is used).

### 3.2. Impact on Corporate ambition

The question we explore here is; *“Is the willingness of corporates to set ambitious climate targets influenced by the availability and cost of carbon credits?”*. Logically, if the effect of CAs is to ensure high standards of environmental additionality, beyond the commitments of the host country, then there would be less supply available. The effect would be to increase the price of these CA adjusted credits. A simplified schematic is shown in Figure 2.

**Figure 2 Simplified impact on demand for carbon credits from Corresponding Adjustments**



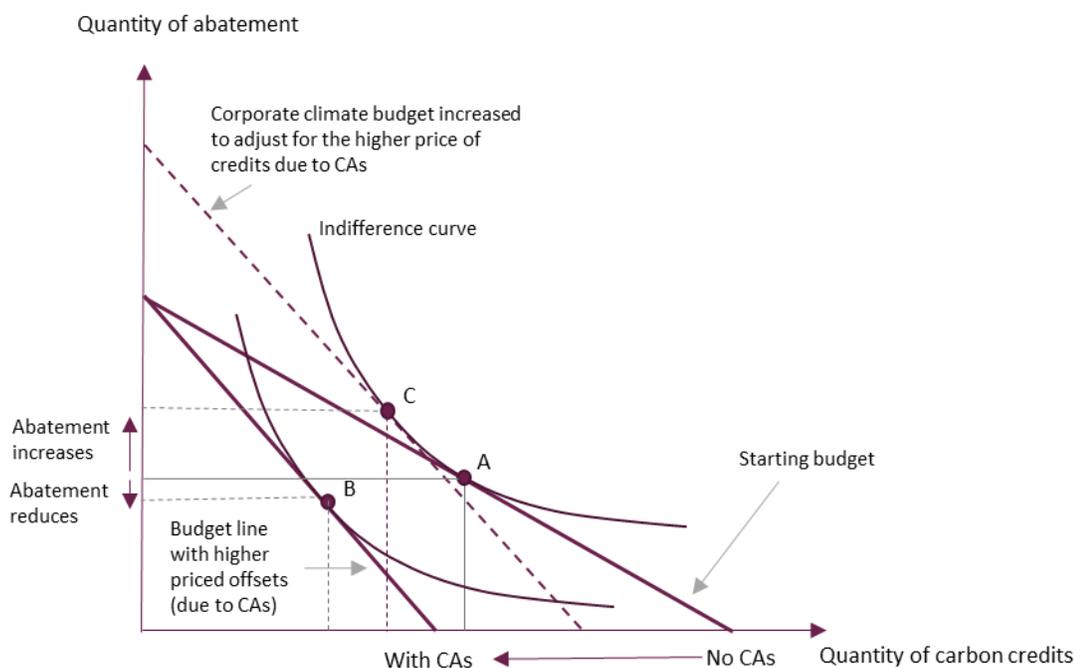
The question then is how this will affect abatement activities for firms interested in setting emission targets and using offsets. On the one hand, if corporate climate related activities are determined by budget constraints, and the cost of carbon credits increases, corporates will have fewer resources available for climate related activities. Under these conditions, corporate abatement will reduce.

## The impact of Corresponding Adjustments on mitigation incentives

This is illustrated below in Figure 3 which shows the trade-off between CAs and internal abatement. If CAs increase the price of carbon credits and the corporate budget remains the same, fewer credits can be afforded (the trade-off point moves from A to B). In this example, there is also a small reduction in internal abatement, although other curves can be drawn to show slight increases in abatement.

If, on the other hand, corporate climate targets are to be achieved come what may, and budgets are increased to accommodate the rise in the cost of carbon credits, there would likely be an *increase* the amount of internal abatement (A moves to C). This is the pure substitution effect of a change in the price of carbon credits, altering the balance of internal abatement and use of carbon credits.

**Figure 3 Impact on corporate abatement of higher priced carbon credits**



The net effect is difficult to predict, although corporate budgets for climate mitigation are unlikely to be infinitely flexible. However, concern about corporate demand for carbon credits being affected by the availability of supply should not be overplayed. The requirement for host countries to apply CAs would only be to increase the environmental integrity of the credits, allowing corporate buyers to claim their emissions had been offset with full confidence. In this sense a CA-adjusted credit is a different product to one without CAs.

*Overall, we believe that the effects of CA adjustments on corporate behaviour are likely to be small in relation to the effects on NDCs. If companies buy fewer carbon credits because of the extra costs of moving to a high integrity system (using CAs), the challenge is to raise ambition, not lower the cost of carbon credit supply.*

### **3.3. Impact on consumer / stakeholder behaviour**

The final consideration in terms of mitigation incentive, is the effect on consumers and other stakeholders, such as governments. The central issue is that if corporate claims for offsetting emissions are not genuinely additional, consumers risk being misled. Climate conscious consumers could potentially consume more of a product/service in the belief that their actions do not contribute to an increase in carbon emissions. If the “offset” claim is not genuine then emissions could increase as a result – clearly an undesirable outcome.

#### ***How material is this effect?***

The airline sector is one industry where the consumer’s carbon footprint is visible and high profile, and the likes of EasyJet have set out their intention to offset all the emissions from their flights. This is a material investment for EasyJet, and the decision was presumably made because the company believes that customers are sensitive to the carbon footprint of flying. The motivations for other firms to voluntary offset are very varied, but it is difficult to know how consumers react in each sector. There are however a few trends that shed light on the issue:

Awareness of climate change and climate conscious consumption is increasing – Today’s consumer market is changing with more companies making claims around being “Carbon Neutral” or selling “Climate Neutral” products. As awareness increases, corporate claims will come under greater scrutiny and consumer choices are likely to be more influenced by the integrity of such claims.

Credibility – As the voluntary market grows and more companies set climate commitments, it will be important for the legitimacy of the market to be maintained. The more stories that surface on non-additional projects that risk undermining the corporate claims, the more damage it will cause to growth of the voluntary market.

For these reasons, the issues of environmental integrity and the application of Corresponding Adjustments is broader than the immediate effect on patterns of consumption.

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## 4. Defining a solution space

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This paper has highlighted the main issues in the debate around whether Corresponding Adjustments should be applied to the export of carbon credits from countries where the activity takes place under an NDC. A number of trade-offs are required. We summarise the main considerations as follows:

1. The nature of corporate claims materially affects the accounting treatment in the host country. Claims over “offsets” should be treated differently to claims around contributing to achieving the host country NDCs. We have included a middle definition that is more nuanced - “emission reduction” - which some companies are using to describe their carbon position.
2. The voluntary carbon market can bring material benefits to countries that lack the capacity and finances to implement appropriate climate policies. In the least developed countries, there is a reasonable case that voluntary action undertaken within the rules of the voluntary market standards is additional to what the host country could achieve. Calculating carbon credits from these activities and using them to meet voluntary corporate climate targets, would therefore be unlikely to need a Corresponding Adjustment to provide an additional level of reassurance. More advanced countries, for example those in the G20, have a greater capacity and resources to achieve their original NDCs. For these countries, the additionality of any voluntary market activities is more difficult to justify and would require a CA if the credit is transferred out of the country.
3. Timing. 2021 and the few following years are critical for mobilising capital to invest in low carbon infrastructure. Corporate voluntary climate commitments, and the potential use of carbon credit transfers, provides a useful source of finance, above and beyond commitments required or supported by regulation. The longer that the accounting treatment of carbon credits is left unresolved, the more time is lost in deploying this corporate capital.

### 4.1. Potential solution framework

A potential solution space is highlighted below in Figure 4 below. This approach is high level, generalising whether CAs would be applied at the level of the country according to whether the country “developed”, “developing” or “least developed”. These are broad generalisations for a more specific issues on whether countries have in place the appropriate policies, financing & enforcement. In principle, countries with similar levels of income should have similar abilities to achieve climate targets, especially when these targets are set on a voluntary basis. Alternatively, rather than simple categorisations based on levels of national income, more specific assessments could be made on the preparedness of national NDC plans.

The buyers of carbon credits would also have the option of adjusting their claims according to the source of the offset. For example, if a buyer wants to claim the credits for “offsetting” their emissions, and they want to source them from a developed country (or one where policies, financing and enforcement processes are in place), then they would need to use credits with CAs. If the claim was not for offsetting, but worded in a way that suggested financing or assisting a country in achieving its NDC, then a CA adjustment would not be required. If, however, the buyer intends to use a credit from a least developed country where all financing is helpful to achieving reductions in emissions, a CA would not be required not matter what the claim.

**Figure 4 Simplified solution space for application of Corresponding Adjustments for voluntary transactions taking place in NDCs**

Country classification	Nature of corporate claims		
	“Offset”	“Emission reduction”	“Contribution”
<b>Developed country</b> – policies, financing & enforcement in place	CA required	CA required	No CA
<b>Developing country</b> – some policies, financing & enforcement in place	Sector specific assessment required	Sector specific assessment required	No CA
<b>Least developed country</b> – policies, financing & enforcement not in place	No CA	No CA	No CA

The main challenge lies in the large group of developing countries, which include many countries where carbon credits may be located, especially credits produced from Nature-Based Solutions. These countries have widely varying NDCs. Some may only cover parts of the economy (eg power or transport sectors) and others may be loosely defined with relative, rather than absolute targets. For these countries, an assessment on the preparedness of the NDC would still be undertaken but the level of the coverage of the NDC rather than at a national level.

In terms of the claims corporates may want to use, we have erred on the side of environmental caution, suggesting that even for more ambiguous claims such as the “use of an emission reduction” there should be a CA from the host country in line with the use as a complete “offset”.

## **4.2. A transition period**

Any implementation of a regime that requires CAs needs to acknowledge that today's voluntary carbon market requires no such adjustments. A period of transition will be needed if such rules are introduced.

We suggest that the transition period should be consistent with the process for revising national NDCs under the Paris Agreement. This starts in December 2021 and the assessment of NDCs is likely to run into 2022. A grace period could therefore be extended to the end of 2022 for the start date for new projects. After this date a new regime for applying CAs for claims of offsets could be introduced for specific countries, as identified in Figure 4.

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## 5. Challenges

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The proposed solution is not without challenges, three of which are discussed below:

### ***(i) Nature of corporate claims***

The nature of the claim is material, but in practice defining the claim is not straight-forward. The concept of “middle way” could lead to some confusion. “Offsetting” and “Carbon Neutral” are likely to be easier to define. In all cases guidance would be needed.

The nature of the claim would also need policing. If the claim is linked to the offset definition and accounting, then there will need to be an independent arbitrator on what is acceptable. There are several options, including Trading Standards, Financial Market Authorities or standard setting bodies.

### ***(ii) Sequencing***

The sequencing of developing the project, obtaining CA approval from the host government, and its final use by the buyer presents a potential challenge. Projects may need to be financed upfront without certainty on the claim of the final user. Ultimately the responsibility on use of the carbon credit falls on the corporate buyer and the claims the organisation makes. The project developer can also request to obtain a CA unilaterally. If a CA is needed for offsetting use, and permission is granted by the host government, then the credit can be used for this purpose. If permission is not granted, the developer may still be able to sell the credit for other uses, but its value would be lower.

The challenge for the developer is knowing the value the carbon credits will receive in the market, as this will determine the investment case for the project. A solution to this is securing long term offtake agreements before the investment decision is made.

### ***(iii) Assessing status of NDCs***

Our proposal is to link the requirement for a CA for the creation and export of a carbon credit to the achievability of the host country’s NDC. This will maximise the flow of capital to projects where it is most needed and reduce the undesirable effects of claims of offsetting where this is not justified.

Criteria will be needed that assesses the achievability of the NDC. As noted earlier in this paper, the simplest approach would be to use the level of income per head as a proxy for achievability.

However, more sophisticated approaches could be developed that take into issues such as:

- Policy preparedness
- Institutional capacity
- Legal underpinning
- Financial resources and agreed budgets

## 6. Consultation questions

This paper attempts to bring together diverging opinions on the issue of the use of Corresponding Adjustments for the use of voluntary carbon credits. We believe opposing views can be reconciled. Views are sought from market participants on a number of issues presented in this paper, specifically:

1. *If Corresponding Adjustments are NOT applied to exported carbon credits intended for offsetting, how significant would the risks be for mitigation action on:*
  - *Governments and their ambition for NDCs?*
  - *Corporates and their internal abatement targets?*
  - *Consumers and other stakeholders*
2. *Is it appropriate to use the type of claim for carbon credits as a basis to decide whether a Corresponding Adjustment needs to be applied to the credit transaction?*
3. *Is it appropriate to use the concept of achievability of a country's NDC as a basis to decide whether a Corresponding Adjustment needs to be applied to the credit transaction? If so, what is the most appropriate way of assessing this achievability?*
4. *What transition period would be most suitable in moving to a system of CAs for some project types and countries?*
5. *Other issues that would usefully help clarify the solution space*

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## Sources and acknowledgements

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This paper has benefitted from conversations with a number of experts and market participants with knowledge of the issue of the VCM and Article 6. These have included:

- Verra
- IETA
- Gold Standard
- Perspectives Climate Group GmbH
- Swedish government
- New Zealand government
- EBRD
- Macquarie Group
- EcoSecurities
- Baker McKenzie
- Althelia
- Reed Smith
- Standard Chartered Bank
- Carbon Market Watch
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