

IETA Response: IOSCO Voluntary Carbon Markets Consultation Report and 21 Good Practices

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ABOUT IETA

IETA welcomes the opportunity to provide feedback on IOSCO's Voluntary Carbon Markets Consultation Report that includes the proposed 21 Good Practices.

For over 20 years, IETA has been the leading global business voice on robust market solutions to tackle climate change while driving clean finance at scale. IETA represents a broad and diverse group of stakeholders (300+ members worldwide) that includes carbon offset project developers, insurance providers, standards, investors, banks and financial institutions, law firms, funds, and businesses who are at the forefront of climate action. IETA's expertise is regularly called upon to inform carbon market solutions that deliver measurable climate outcomes, address economic competitiveness and carbon leakage concerns, balance efficiencies with social equity, and support a just transition.

IETA is the pre-eminent global organization dedicated to the promotion and maintenance of robust and sustainable carbon markets. IETA was the first international, multi-sectoral, purely business group devoted to pricing and trading greenhouse gas reductions. From the start, IETA has had a strong focus on the Kyoto mechanisms and helped members using, hosting, and investing in Clean Development Mechanism (CDM) and Joint Implementation (JI) projects by disseminating policy and market information and promoting development and reform. In more recent years, IETA has also developed work streams on aviation, natural climate solutions, voluntary carbon markets, and carbon removals.

GENERAL COMMENTS

IETA appreciates the principles-based approach that IOSCO has taken in developing the 21 Good Practices. The proposed recommendations are a helpful and pragmatic way for regulators to engage with the market to address potential vulnerabilities, and we appreciate that IETA's comments on the previous consultation were considered and included in this latest iteration. In particular, IETA appreciates IOSCO's recognition of ongoing public and private sector initiatives whose objectives are to raise the environmental integrity of the VCM. IETA supports efforts by regulators to enforce rules and actions to reduce and eliminate market manipulation, fraud, or misconduct. Equally, we encourage IOSCO to be cognizant of not over-regulating the market to a detrimental degree. Regulation is welcome insofar as it does not inhibit the nimbleness of the market or stifle growth.

IETA recognizes that the guidance is framed as being directed at the "voluntary" carbon market, but we would like to highlight the increasing convergence between the voluntary and compliance carbon markets. Lines between voluntary carbon credits and compliance carbon credits are becoming less clear as credits issued by independent crediting programs may be authorized for use in national or international compliance regimes (i.e., CORSIA, California Air Resource Board). This means carbon credits may be used for either voluntary or compliance purposes and the exact usage would become known only at the end stage when the credit is retired or cancelled for a specific purpose.



COMMENTS ON THE 21 GOOD PRACTICES

Good Practice 1 – Regulatory approach and scope: Consistent with their respective mandates, relevant regulators and other authorities could consider ways to apply appropriate and effective regulation, supervision, and oversight to VCMs, covering, among other things, the issuance, trading, and retirement of carbon credits.

IETA supports well intentioned and well-designed policies to ensure the VCM is guided by high integrity. It is to be noted that, in general, most jurisdictions consider carbon credits as intangible property or commodities, and not securities. The existing regulatory framework for the issuance of securities is different from the current process for issuing carbon credits, which is overseen by carbon crediting programmes, without the involvement of financial intermediaries. Also, while securities are traded mostly for investment purposes, carbon credits can be traded for compliance and other utility purposes, which necessitate a different set of considerations for their issuance.

We reinforce our previous stance that securities regulators should be careful in treating and regulating carbon credits as securities, especially the issuance thereof. Instead, we think, as financial regulators, the focus should be on regulating the trading conduct of carbon credits (e.g. transaction monitoring and market surveillance requirements) and ensuring an adequate level of data transparency and **risk** disclosure for traders to buy or sell carbon credits should a securities regulator consider carbon credits to be an asset class that is under its purview.

In relation to the functions of issuance and retirement of carbon credits, these are currently performed by independent registries, some of which also perform the function as a carbon crediting standard. Should IOSCO consider carbon registries to be financial market infrastructures (e.g. akin to central securities depositories), we strongly suggest that any regulatory principles should be aligned with the current multi-lateral initiatives like ICVCM, which are focused on governance and ensuring no-double counting (e.g. proper accounting and record-keeping, and cyber resilience), without imposing undue burden on such registries. It is also to be noted that most countries will have to establish their own national registries to comply with the reporting requirements under the Paris Agreement and that securities regulators should consider the appropriateness of bringing carbon registries under a financial regulatory framework.

Good Practice 2 – Regulatory treatment: Where possible and consistent with their respective mandates, relevant regulators and other authorities could consider ways to provide clarity regarding the regulatory treatment of carbon credits.

IETA strongly supports the suggestion that regulators, where appropriate, provide clarity regarding the regulatory treatment of carbon credits clearly and transparently. We agree that clarity on the regulatory treatment of carbon credits (commodity instrument, financial instrument, etc.) would help create consistency and integrity in carbon markets, especially as the markets increasingly converge and operate internationally. For example, by treating carbon credits as financial instruments, any financial services provided thereto would be brought within a financial regulatory framework. This would provide investors with confidence to trade and hold carbon credits through financial intermediaries, and thus reducing the friction or operational burden to administer multiple registry accounts, which in turn increase depth and liquidity of the market.



However, we also note that not all current regulatory regimes provide opportunities for IOSCO and its members to weigh in on this process (e.g., in the U.S. carbon credits have long been treated as a commodity, not a security). In the near term, we encourage IOSCO and its members to embrace existing regulatory treatment, where possible, to avoid market disruptions. IOSCO should also, as noted in the Consultation Report, continue to track the work of other entities in this space, such as UNIDROIT and UNCITRAL.

Good Practice 3 – Domestic and international consistency and cooperation: To foster the global development of VCMs, where possible and if consistent with domestic processes and mandates, regulators and other relevant authorities could consider seeking both domestic (between various domestic authorities) and international consistency and alignment when developing their own regulatory approach to carbon credits, including with regards to cross-border cooperation for enforcement.

IETA strongly supports collaborative approaches to domestic and international consistency and the recommendation for cross-border cooperation between regulators. We believe that consistent practices will better aggregate liquidity to support the development of a deep and robust market and better price discovery, and subsequent positive environmental benefit. As carbon credits are developed all around the world, we would like to highlight that, while carbon credits can be “produced” globally, carbon financing is a way to channel financing to the Global South and to support a just transition. Cross-border cooperation and international regulatory harmonisation are necessary to support such a goal.

Good Practice 4 – Participants’ skill and competence: Consistent with their respective mandates, relevant regulators and other authorities could consider promoting the need for firms and senior management to have adequate skills and competence, including an understanding of the benefits and risks of trading in VCMs, and how existing regulatory frameworks may, or may not, apply. In addition, they could consider developing investor education programs to improve the public’s knowledge of carbon credits.

IETA supports the notion of promoting the need for firms and senior management to have adequate skills and competencies to understand the benefits and risks of trading in the VCM; however, it is unclear exactly how IOSCO defines ‘adequate skills and competencies.’ IETA supports the suggestion that regulators could develop investor education programs to improve the public’s knowledge of carbon credits as it is important that this recommendation does not have the unintended consequence of slowing down the market. IETA further notes that many market participants act in advisory roles and could support both companies and regulators in these endeavours.

Good Practice 5 – Standardization: Consistent with their respective mandates, relevant regulators and other authorities could consider engaging with carbon crediting programs, spot exchanges, derivatives exchanges, private sector initiatives, and other market participants to standardize a taxonomy of carbon credit attributes, strengthen verification methodologies, and streamline verification processes.

IETA recognises the need for standardization and its importance in ensuring the credibility, transparency, and comparability of emission reduction projects. However, IETA reiterates that market



participants and multi-lateral initiatives such as ICVCM, ICROA, and CORSIA are best suited to define and ensure the environmental integrity of carbon credits in the VCM.

We further note that, while some standardization (e.g., harmonized principles of integrity promulgated by ICVCM) are beneficial to carbon markets, too much standardization in the primary market could lead to a lack of recognition of the bespoke or unique value of particular carbon credits sourced from certain projects. Increasingly, there are a range of unique attributes in each carbon credit that purchasers value and sellers want to uniquely price (e.g., co-benefits, process considerations, methodology and project type, and community relations issues). Imposing too much primary market standardization risks obscuring such unique benefits of different projects and depressing prices for credits sourced from more complex projects with additional co-benefits.

Good Practice 6 – Transparency: Consistent with their respective mandates, relevant regulators and other authorities could consider appropriate ways to promote transparency around the creation of a carbon credit. This could include comprehensive disclosures on the project development process, verification and auditing methodologies, and the entities responsible for measurement, reporting, and verification. Transparency of contracts and pricing in the primary market could also be encouraged.

IETA recognizes the importance of transparency and consistency in the VCM. However, it should be noted that the current issuance process is overseen by carbon crediting programmes and is not within the control of financial intermediaries. Imposing prescriptive transparency requirements on financial intermediaries may place an undue burden on them and causing them to stay away from facilitating the trading of carbon credits. Also, we strongly recommend IOSCO to review the information requirements of the independent registries, which are presently available to the public via project documentation on registries (i.e., in monitoring or verification reports). IETA further encourages IOSCO to review the work of ICVCM, CORSIA and ICROA who have been working with crediting programmes and other market participants to enhance and promote transparency around the creation of a carbon credit.

Market participants are already starting to disclose more information related to the credits that they are buying and selling. Some IETA members are in favour of increasing transparency around contracts and pricing as this is important for liquidity and price discovery, while others note that certain contractual terms, in particular with over-the-counter transactions (including pricing, contract length, etc.) should remain proprietary. Transparency creates a fairer process for project participants, such as landowners joining a nature-based solutions project.

Good Practice 7 – Disclosure: Consistent with their respective mandates, relevant regulators and other authorities could consider appropriate requirements to promote complete, accurate, and understandable disclosure of information related to the primary issuance of carbon credits as well as transparent disclosure of any associated risks.

IETA recognizes the importance of complete, accurate, and understandable disclosure of information related to the primary issuance of carbon credits, but it is unclear what additional information IOSCO is proposing to be disclosed in this recommendation. We again recommend the currently available information is evaluated so that a more specific recommendation can be made. IETA believes that carbon crediting programs are well positioned to ensure the quality of credits on their registries while



striking a balance between transparency of information necessary to ensure integrity, and the proprietary information of project developers. IETA further encourages IOSCO to review the work of ICVCM, CORSIA and ICROA who have been working with crediting programmes and other market participants to enhance and promote transparency of information related to carbon credit projects. As mentioned, financial intermediaries are currently not involved in the issuance process and thus it would be very challenging for compliance purposes if disclosure requirements that are higher than those provided by the carbon crediting programmes are imposed on such financial intermediaries. We support that financial intermediaries should ensure there is transparent disclosure of any associated risks.

Good Practice 8 – Soundness and accuracy of registries: Consistent with their respective mandates, relevant regulators and other authorities could consider appropriate requirements, that registries, as custodians of carbon credits, are accurate, complete and current in order to serve as reliable sources of information regarding the price at issuance, tracking and/or retirement of carbon credits.

IETA encourages caution with this Good Practice. Registries are a tool of carbon crediting programmes that traditionally have not published information regarding the price at issuance but already provide tracking and retirement information. IETA sees several potential challenges with registries being asked to provide information regarding price at issuance, such as:

- a perceived COI if they were to know and publish price information,
- discrepancies and/or market confusion in the event different approaches are adopted by various jurisdictions or standards bodies
- logistical challenges with collecting and verifying this information, and
- the consideration that many credits do not have a price at issuance as the credits may not have an immediate buyer.

Registries already provide public information that allows for tracking of information related to issuances and retirements but are not involved in pricing or execution of transactions.

IETA notes that registries, as custodians of carbon credits, are a critical part of the VCM's infrastructure, but are not currently subject to oversight or standard operating procedures. IOSCO may be well-positioned to develop such principles in line with its existing guidance in this area, including operational, privacy, and cyber security protections. An internationally coherent oversight framework for registries may be useful for scaling well-functioning carbon credit markets, and by developing principles for registries, IOSCO can further strengthen and accelerate initiatives on transparency, integrity and scalability.

Good Practice 9 – Due diligence: Consistent with their respective mandates, relevant regulators and other authorities could consider appropriate requirements to ensure that carbon crediting programs perform adequate levels of know-your-customer (KYC) and due diligence procedures to prevent the use of carbon credits for money laundering.

IETA understands the importance of preventing money laundering and notes that many crediting programmes already have very robust procedures in place. It is unclear to IETA how exactly this Good Practice could be operationalised, though we note that guidance or a framework on this topic may be helpful for carbon crediting programmes.



Good Practice 10 – Access to VCMs: Consistent with their respective mandates, regulators and other relevant authorities could consider requirements or policies to ensure open and fair access to secondary market trading on VCMs for interested market participants.

IETA supports open and fair access to secondary market trading for interested market participants recognizing a robust secondary market aids in transparent price discovery. We note that access to secondary trading on exchange platforms is already common practice. However, we do not support access to OTC transactions which are confidential between parties. We think requirements or policies that ensure investor protection, e.g. KYC requirements, client asset segregation, conflicts of interest management, proper record-keeping, frequent reconciliation or audit, would help to scale the market by removing friction when trading and providing confidence to end users to transact through financial intermediaries, (e.g. end users do not have to open accounts with different registries but can use financial intermediaries to access carbon credits issued by different registries).

Good Practice 11 – Integrity of trading: Consistent with their respective mandates, relevant regulators and other authorities could consider requirements to ensure that VCM participants observe high standards of integrity and fair dealing with respect to business activities relating to carbon credits.

IETA fully supports the need to observe high standards of integrity in voluntary markets and encourages IOSCO to review the work of ICVCM, CORSIA and ICROA who have established definitions for high integrity. IETA would like further clarity on IOSCO's comment that 'only carbon credits satisfying established and recognised standards for quality and integrity are eligible for trading on regulated trading venues.' While IETA supports the ICVCM and anticipates that the Core Carbon Principle (CCP) labels will play an important role in identifying high quality credits, there may be functional delays in evaluating certain categories of carbon credits that could arbitrarily limit credit trading if this recommendation were to be implemented. We anticipate this space will continue to evolve rapidly.

Good Practice 12 – Public reports: Consistent with their respective mandates, relevant regulators and other authorities could consider requiring that trading venues and registries, including for OTC trading, make public reports which disclose, on an equal basis to all market participants, relevant data regarding trading, including, but not limited to, pre- and post-trade price transparency, trading volume, bid-ask spreads, and deliveries of carbon credits.

IETA supports efforts to promote disclosures in the VCM if done thoughtfully and effectively, and where they build on the work of existing data agencies that provide this information to the market. Proper disclosures, up to a point, should be able to prevent 'bad actors' from trying to manipulate the market for their own benefit. However, we are concerned about the lack of information on who would be responsible for these disclosures and how this recommendation may be implemented. Frequency of disclosures is also an important consideration because daily or even weekly formats could hinder market participants' ability to operate and execute trades effectively. IOSCO may consider recommending a model similar to other physical energy commodities where separate data/price aggregators report on behalf of the market and these entities could be, in turn, regulated.

In addition, with respect to OTC transactions, this Good Practice appears to assume that all traded carbon units have similar characteristics such that price discovery would be universally



applicable/helpful to all transactions. That is not the current reality, so effective price discovery for primary market transactions would need to be tied to specific types of credits with common attributes.

Good Practice 13 – Pre-and post-trade disclosure: Consistent with their respective mandates, relevant regulators and other authorities could consider encouraging an entity operating a VCM, which lists carbon credits that are the underlying for regulated derivatives, derivatives exchanges, or an intermediary to provide pre- and post-trade disclosures in a form and manner that are the same as, or that achieve similar regulatory outcomes consistent with, those that are required in traditional, regulated financial markets.

In respect of Good Practices 12 and 13, IETA encourages IOSCO to (1) consider removing the suggestion that registries should be involved in disclosing trading data/information, as registries are explicitly not a part of trading in terms of pricing, and therefore would likely have no access to the type of trading data described; and (2) more explicitly specify that any OTC trading disclosure requirements follow what is required in other products/markets to avoid mandatory disclosures of bid/asks or OTC trade prices beyond what is required in other markets.

Good Practice 15 – Governance framework: Consistent with their respective mandates, relevant regulators and other authorities could consider requiring that VCM participants, including carbon credit project developers, registries, validation and verification bodies, brokers, traders, marketplaces and exchanges, rating agencies, third-party entities, and private sector supply and demand side standardization initiatives, have in place a comprehensive governance framework with clear lines of responsibility and accountability for the functions and activities they are conducting.

It is unclear to IETA what this recommendation would entail, and what is not already covered when counterparties conduct KYC / AML due diligence. Governance framework requirements tend to be generalized as a highly specific framework is difficult to implement across the wide range of entities involved in the VCM. IETA would appreciate more clarity on this recommendation.

Good Practice 16 – Risk management: Consistent with their respective mandates, relevant regulators and other authorities could consider requiring that carbon credit intermediaries, marketplaces, and exchanges have effective enterprise risk management frameworks in place to address any potential operational or technological risks associated with the trading of or provision of services relating to carbon credits. Appropriate enterprise management, information technology, and security protocols could be deployed by each of the key market participants, including the registries where carbon credits are transferred, to effectively guard against fraud, hacking, and other, criminal activities related to carbon credits. Regulators could consider requiring the employment of an enterprise risk officer with sufficient staffing and support resources. Regulators could also consider requiring the implementation of a business continuity disaster recovery plan and operational resilience programs with system safeguards that are developed and routinely reviewed for consistency with industry best practices.

In respect of Good Practices 16 and 17, IETA fully supports the need for adequate enterprise risk management frameworks and mechanisms to address and mitigate conflicts of interest. IOSCO and its members are well-suited to encourage trading venues to establish clear processes to identify and monitor conflicts of interest in respect of secondary market issues and to take appropriate actions if there are risks to orderly trading or market integrity. However, we would encourage regulators to



exhibit caution so as to avoid exceeding their mandates or reinventing the wheel in the context of establishing new policies and procedures to address primary market issues.

Good Practice 18 – Enforcement actions: Consistent with their respective mandates, relevant regulators and other authorities could consider bringing enforcement actions if there are fraudulent or abusive practices in VCMs, such as false and misleading statements regarding the attributes of carbon credits. In anticipation, consistent with their respective mandates, relevant regulators and other authorities as well as trading venues could consider implementing rule enforcement programs with disciplinary mechanisms to discourage trade practice violations, including monetary sanctions to deter recidivism. This would include putting in place measures to ensure the avoidance of fraud with respect to any systems used to issue, track, record, and/or register ownership of a carbon credit.

IETA supports efforts by regulators to enforce rules and actions to reduce and eliminate market manipulation, fraud, or misconduct. However, we are very concerned that given the nuances related to the attributes of carbon credits, “false and misleading statements” is too broad a term to be left open to interpretation, and we do not want to see market participants prosecuted for mistakes rather than blatant fraud. If this term is not defined further, enforcement actions around this could lead to the unintended consequence of dampening market activity due to lack of clarity.

Good Practice 19 – Market surveillance and monitoring of trading: Consistent with their respective mandates, relevant regulators and other authorities and trading venues could consider appropriate ways to conduct market surveillance and trade monitoring to identify fraud, manipulation, price distortion, and/or other market disruptions.

IETA supports efforts by regulators to enforce rules and actions to reduce and eliminate market manipulation, fraud, or misconduct.

Good Practice 20 – Trading venue resources: Consistent with their respective mandates, relevant regulators and other authorities could consider ensuring that trading venues maintain adequate resources to detect and investigate fraudulent or manipulative practices, including a Chief Compliance Officer and Chief Regulatory Officer.

IETA believes the intent behind this recommendation is good, and we note this is common practice in other commodity markets, however, some members note concern with how this may be implemented in practice. For example, for small firms with limited resources, this seems unnecessary and potentially cumbersome and/or redundant.

Good Practice 21 – Disclosure of carbon credits use: Consistent with their respective mandates, relevant regulators and other authorities could consider, consistent with their jurisdiction’s laws and domestic legal requirements, encouraging or requiring disclosures regarding an entity’s use of carbon credits to achieve any net GHG emission targets.

Improved transparency and disclosures can help make companies more resilient against greenwashing claims and help enhance trust in the market. We strongly encourage that regulators conduct extensive engagement with market participants before implementing requirements related to disclosures as a large body of work is underway on this topic led by market participants.

