International Carbon Reduction & Offset Alliance

Innovate4Climate
Frankfurt
23rd May 2018

3rd ICROA Forum on Increased Voluntary Action under the Paris Agreement

REPORT

IETA CLIMATE CHALLENGES MARKET SOLUTIONS

Introduction

The Paris Agreement presents an opportunity for the private sector to step up and take a leadership role by helping to bridge the existing ambition gap. We have already witnessed an increasing number of private-sector focused initiatives to acknowledge the risks of climate change and take action.

The voluntary carbon market provides the tools to enable such climate leadership. However, sufficient progress on Article 6 of the Paris Agreement will be needed to ensure the future Paris rulebook enables voluntary action by the private sector in ways which respect environmental integrity.

In this context, ICROA has undertaken a programme of work to develop collaborative solutions with voluntary market stakeholders. In May 2017, we organized our first workshop with a broad range of participants to gather opinions on key questions regarding the future of voluntary action. Since then, we have built on this workshop and developed guidance on pathways to increased voluntary action by non-state actors. Released in October 2017, this sets out ICROA's views on how the market can grow after 2020, and how voluntary action can contribute to delivering the objectives of the Paris Agreement.

In November 2017, we held our second workshop at COP23 to discuss key issues on future supply and demand for voluntary offsetting, based on the guidance's three potential models for the future framework of the voluntary carbon market.

On Wednesday 23rd May 2018, ICROA held its third event during Innovate4Climate in Frankfurt. Representatives from governments, development banks, the UNFCCC, NGOs, academia, consultancies and market participants gathered at this Forum to discuss options to increase voluntary action under the Paris Agreement. A list of registered participants can be found in appendix A.

The purpose and objective of this Forum was threefold:

- Provide an update on initiatives enabling voluntary action under the Paris Agreement,
- Identify requirements for resilient growth and impact, and
- Establish a platform for information sharing and collaboration.

The event - moderated by Jonathan Shopley (Natural Capital Partners) and Ana Aires Carpinteiro (Nexus for Development) - started with a short presentation of the key elements developed in ICROA's guidance report. This introduction was followed by three scene-setting interventions, before moving into a roundtable discussion with all participants.

The Forum concluded with the launch of a voluntary market portal on the ICROA website, where participants were invited to put forward their views on ways to scale voluntary action post-2020. This space intends to be a neutral repository for ongoing research conducted by leading organisations.

ICROA would like to thank all stakeholders who participated in this Forum for their invaluable contributions to move forward the discussion on the future of voluntary action under the Paris Agreement.

Summary of the interventions

As a way to set out some of the key challenges and opportunities lying ahead, the event started with interventions from speakers and representatives from the ICROA membership, before moving into a general discussion with all participants.

These interventions aimed at highlighting (i) the key technicalities implied by the transition from a Kyoto world to the global architecture of the Paris Agreement, (ii) the consequences in terms of future supply in the voluntary market, and (iii) the ways that demand can be sustained in the future landscape. Through these conversations, the objective was to identify key areas for the voluntary market community to focus on ahead of the publication of the Paris rulebook in 2018 or 2019.

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1. Enabling architecture: What are the most important requirements of Article 6 and NDC development required to enable voluntary action to flourish?

Interventions:

- Frank Wolke: Head, Emissions Reduction Projects section, German Environment Agency
- Jeff Swartz: Director Climate Policy & Carbon Markets, South Pole Group

FW: Voluntary action will have an important role to play in meeting the Paris Agreement's long term targets. Germany is conducting some research on the voluntary market and we are about to release guidelines on the inclusion of voluntary action. We will need robust accounting in place to track what will count towards the Parties' climate targets set out in the NDCs, and what can count towards voluntary action. Compared to the Kyoto world, I see the accounting issue as the main issue. Under the Kyoto Protocol, the financing of projects that delivered emission reductions was not a concern. It helped develop many valuable projects in developing countries. These projects were additional because they did not overlap with climate policies in these countries and it was easy to avoid double counting risks. Under the Paris Agreement, all Parties have targets and everything is different. If voluntary action contributes to meeting a country's target, the projects will be reflected in the inventory and there is a double counting risk. I see ways to address it:

- Include the voluntary standards into the negotiating text. Just like what CORSIA is trying to do at the moment, where voluntary standards will likely be eligible under ICAO's scheme. But then we would no longer see voluntary action per se, as it would become part of a compliance commitment. It would generate demand for the voluntary standards but the emission reductions could no longer be used by corporates for offsetting purposes.

- Another way would be to differentiate activities under the Paris Agreement, from inside NDCs and outside NDCs. We could then say in theory that when outside NDCs, emission reductions achieved can be eligible for voluntary use. But this creates no incentive to transition to an economy-wide target. What is necessary is a system that allows for a separate accounting of mitigation activities for different purposes. We need to be able to say some emission reductions are for the Parties' own use, and others can be used in the voluntary market. How can we come to this differentiation in the accounting arrangements? What we could do is add the projects' emission reductions to the country's inventory, issue the corresponding certificates which the host Party decides how to use: for their own effort, for a transfer to another Party, or made available to non-state actors for voluntary use.

Everything is still possible as nothing has been decided. There is still enough room for manoeuvre in Article 6 to find some hooks for voluntary action.

JS: There is no mention of voluntary action in the Paris Agreement or in the subsequent Article 6 text that is being negotiated by the Parties. The focus among Parties is now on the Paris rulebook. As the negotiator for Germany, is there any Party that mentioned that voluntary action should be included?

FW: We only have headings at this stage; we are still far away from a decisive text and we did not get to that level of detail. However the procedures will not be that different from those that will apply to Party-to-Party transfers.

JS: A concept that has come out is that of inside and outside NDCs. How might that formulate itself in the rulebook, ultimately? In the negotiations, is the voluntary market defined by what's outside the NDCs?

FW: Some Parties are in favour of having activities outside their NDC, which obviously facilitates the accounting. Action outside the NDC could be like a buffer for the lack of alignment with the country's target but in the longer term, everything needs to be inside the NDC, in my view.

JS: The idea of a transition period is sometimes hard to grapple with. We have credits used for compliance – such as Kyoto and other compliance systems around the world - and some used for voluntary purposes. How long will that world continue to exist? Does it suddenly stop on Dec 31st 2020? What happens on Jan 1st 2021? It is hard to understand this transition period and its implications, is this also being discussed in the negotiations?

FW: The conditions under which projects can be converted from the old mechanism (CDM) to the new (6.4) need to be discussed. This transition period is one the most difficult things to discuss. We do not want to repeat mistakes made in the past and it will be important not to transfer former problems into the new system. We need to have an active role of Parties that designed and benefited from the Kyoto mechanisms.

2. Delivering emission reductions: What are the most important requirements to enable supply?

Interventions:

- Philipp Hauser: Board Member, Project Developer Forum
- Jochen Gassner: CEO, First Climate

PH: We will need a functioning global carbon market to answer the supply question. In my view, there are four important pillars to get there:

- **Demand will drive supply**
  Corporates will need a vital access to flexible mechanisms to facilitate the design, management and execution of their Science Based Targets. Non-state actors should adopt long term strategies, not opportunistic approaches. How can we position voluntary action as a driver towards such a global carbon market which is being built? If long term/strategic demand is there, supply will follow.

- **Domestic Action (NDCs)**
  We live in a world of domestic policies. Projects will co-exist with other regulations after 2020, in every jurisdiction. How will countries create incentives for more voluntary action? We do not have such oversupply currently, because in many cases the issuance fees are simply not paid, mostly in the CDM. For investors, there is an opportunity cost: do I want to sell my credits for a few cents today or wait until future demand-creating regulations are in place? If we want cost-effective climate mitigation, there are plenty of opportunities out there and a need for investments. But we need to understand that there are opportunity costs.

- **The accounting issue**
  It is difficult to know how the accounting will work between compliance action and voluntary action. There is a difference between domestic voluntary use vs. international use. In my view there is no accounting issue if a unit is generated in a country and used by that same country, this can be reflected in the national inventory. In the presence of an international transaction, voluntary action will not be reported in the NDCs. In the case of regulated targets (like CORSIA), emission reductions will be reflected in the host country's inventory. There is a need for double entry book keeping to differentiate between voluntary action and action in the context of a regulated target. What is voluntary action today could be regulated action tomorrow.

- **A new narrative to explain what an emission reduction is**
  Projects should help deliver on the SDGs. If we want to continue mitigating actions in developing countries, the narrative on avoided emissions and contribution to the SDGs will be critical.

Corporates need to embrace flexible mechanisms, which are needed to meet ambitious Science Based Targets. They are the link in a fragmented market where we need to see more convergence. NDCs will be a big driver of emission reductions, but voluntary action and CORSIA can be the link between isolated markets and help achieve a convergence of pricing, rules and procedures. The world of cheap carbon credits is over as host countries will keep the low hanging fruits for themselves. The market needs to promote and focus on large scale, transformational projects.

JG: In the context of the CDM, investments by the private sector were promoted with the expectation that there would be a long term market. Under the Paris Agreement, we do not know to what extent private sector activities will be facilitated or needed. As a project developer, how do you see the business of developing supply change from a CDM world to a Paris Agreement world?

PH: A first lesson from the CDM is that it has been a very powerful tool to engage the private sector and create substantial investments. We started to promote investments in developing countries, often financed by domestic capital, in the expectation that there would be a long term market. Transformational projects – such as wind - take time to implement. It's not fair to say that actors were aware of the regulatory risk, because the market expected a long term mechanism. We now hear that we could be letting go of the CDM in order to move on to a new sustainable development mechanism. We need a bridge. Some form of transfer and recognition of existing projects under NDCs is essential. The new regulatory complexity is starting to concern many stakeholders. We need to have more certainty on what contributes to NDCs domestically, and what can be exported to non-state actors - thereby attracting investments and technology transfers.

JG: How do we make sure that developers get some kind of certainty in this transitory period, to get projects off the ground? REDD projects have 30/40-year crediting periods, for instance.

PH: That is a big question mark. Under the CDM, the demand side was very short-sighted. Long-term signals are needed. With CORSIA, that is the case, and the financial sector could manage that risk for the market, signing long term agreements and market them to more short-sighted actors in the market.

JG: There is a perception of oversupply and low prices in the voluntary market. But there will soon be competition for that supply. Where do you see pricing for project-based emission reductions in a few years, and what is a reasonable price we need to convince governments to make these emission reductions available for export to non-state actors?

PH: After 2020, prices will vary among countries. Some will restrict the issuance of LOAs and there will be uncertainty around future investments. Some countries will figure it out, keep the cheap emission reductions and the more expensive ones will go to the voluntary market. Under $5, one is taking advantage of the current market situation but it is not sustainable. $5 to $10 seems to be the way forward. We need to mobilize more capital for transformational projects - such as in transport infrastructure and renewable energy - which transform a country in the long term.

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3. Scaling voluntary action: What are the most important requirements to scale demand?

Interventions:

- David Antonioli: CEO, Verra
- Edward Hanrahan: CEO, ClimateCare

DA: Reflecting on the conversations so far in this Forum, I think there are two critical points that we need to address:

- The first one is the risk of generating emission reductions outside NDCs, which creates a perverse incentive. In the long run, regulated targets are needed across all sectors of all economies, as required by the Paris Agreement. We need to think about what the incentives are.

- The second one is related to the financing emission reductions model in ICROA's guidance report, which is an important pathway to consider. What is the claim associated with crediting in the future? We certainly need to avoid double counting. The "apples and oranges" argument leading to emission reductions being counted towards a national target and used by a non-state actor based somewhere else will not wash, that is clear double counting.

- Hence the idea of a new unit, which Verra has put forward and calls the Domestic Climate Contribution (DCC). By creating an alternative unit that meets all best practice requirements, that would be listed on a registry and could be retired like any other verified emission reduction, the market could transition to a model that would raise ambition while dealing with double claiming concerns. The DCC leads to a contribution claim, related to the financing of a mitigation activity by the non-state actor who retires that unit. Ultimately, the reduction contributes to the host country's NDC. This has numerous consequences for the voluntary market, which was built on the concept of carbon neutrality, through the ownership of carbon credits.

- Market stakeholders have the opportunity provide comments on this new DCC concept through a public consultation that Verra recently launched on the next version of its Verified Carbon Standard Program. We believe this pathway would provide a lot of flexibility to the market. But market participants need to make sure that corporates understand it and find value in it. We are in a transition period and we need to put forward some solutions that work.

EH: How do we catalyze and increase demand? How do we create an environment in which corporates increase their ambition and responsibility? How can governments change the environment and drive demand, is it a carrot or a stick?

DA: Ultimately your clients probably do not only look at you as providers of carbon credits but also as risk managers. You are providing options to corporates. It's risky because some of them have made long term commitments of carbon neutrality. Therefore we as market stakeholders have a responsibility to put solutions forward today. We have a hard time figuring out what's inside and what's outside NDCs, because NDCs are not clear enough. Corresponding adjustments seem to be complicated too as cancelling allowances has already proven difficult under the Kyoto Protocol. There is a real risk we could end up with very low volumes post 2020.

EH: Given that most voluntary buyers are in Europe and in the US, where do we leave the poorest countries that have been getting finance to date, and that might not get it in the future if this market no longer works?

DA: Colombia's hybrid carbon tax and offset system provides an element of response. It is driving a lot of action domestically and provides flexibility. REDD projects are operating on 30-year + timeframes. The DCC is one way to address the changes to come. We need to turn this theoretical concept into an actual system. Is the voluntary carbon market as we know it bound to disappear if it does not change? We probably need different instruments. Carbon credits may not be the response.

Summary of the roundtable discussion

There are many uncertainties ahead: which issues should we concentrate our efforts on for this transition period? This is a summary of the main points raised and initiatives mentioned.

- Ministries and market stakeholders in developing countries are not clear on what we are discussing today in this Forum. Issues such as double counting are not on their radar. We need to engage with them and bring them up to speed on these questions.

- The World Bank's Partnership for Market Readiness is working with many developing countries and organizes workshops on capacity building. An important topic in these workshops relates to how Article 6 could impact them in the future.

- NDCs are a simple communication from a Party. Saying that sectors outside the NDC represent the voluntary market is not accurate. We are in this transition period already and there won't be a big bang in 2021 only regulatory uncertainties that Parties need to resolve. Capital intensive infrastructure and transformational projects are necessary. In many instances, the lifetime of these projects goes far beyond the NDC's time horizon. How does the private sector manage that risk? Right now, there is no recognition of early action and no recognition of internal carbon prices that can influence a corporate's capital expenditures for the coming 15 or 20 years. Some basis of recognition for such action going beyond what NDCs require is needed.

- The idea of a voluntary cancellation account proposed in ICROA's guidance report is one to look into. The focus should be on getting the corresponding adjustments right. A series of meetings are currently taking place under the aegis of the ClimateWorks Foundation and convened by the Meridian Institute to discuss how to avoid double counting under CORSIA. Guidelines will be made publicly accessible later this year in autumn. These could certainly inform this conversation.

- WBCSD is also discussing the design of an initiative to scale up investments in Natural Climate Solutions. The objective is to speak about it with an engaged group of stakeholders. The critical mass of companies in WBCSD is there. Now we need to better understand the barriers and develop the solutions.

- We won't get all the answers from the UNFCCC process. We need to launch initiatives and not wait for the Paris rulebook, which we might only get in 2019 in its final version. We can't sit here and wait around. There is no clarity over what will count for domestic use, ITMO use or voluntary use. Should we set out principles, like ICROA did it when it was formed?

- We could focus on ambitious NDCs and/or position the voluntary market as a tool for the least developed countries to learn on. The Colombian example of a combined carbon tax and offset system has lead to a lot of action, and sends the right price signals. We could also focus our action on the conditional part of NDCs.

Voluntary Market Portal: a platform for information sharing and collaboration

Many initiatives are looking into ways to scale voluntary action post-2020. ICROA decided to create a publicly accessible portal where a broad range of actors can put forward their views on this topic and related key questions.

This space intends to be a neutral repository for ongoing research conducted by leading organisations, including academia, governments, NGOs, voluntary market participants and more. The views and opinions expressed in the publications are those of the authors.

This portal can be accessed here: https://www.icroa.org/Voluntary-Market-Portal.

ICROA welcomes additional contributions. If you would like to be part of this initiative and submit your publications, please contact Antoine Diemert on diemert@ieta.org.

Next steps

This workshop was the third of a bi-annual series of workshops designed to build a broad coalition of stakeholders to address forthcoming market challenges and help secure a role for voluntary action in a post-Paris world.

Building on Ana Aires Carpinteiro's and Jonathan Shopley's summary of the discussions, we identified several areas that ICROA intends to work on going forward, in the lead-up to COP24:

- Getting a better understanding of the NDCs and identify which ones are a welcoming home for private sector investment.
- ICROA should be socializing the idea that we need a transition period for voluntary action to find its place in the Paris Agreement infrastructure, to avoid market confusion. The work conducted by the main voluntary market standards on the NDCs and on future claims should be embraced and encouraged by the industry.
- The three models identified in ICROA's guidance report should all be allowed to operate in parallel. We will conduct further analysis on their implications, e.g. encouraging non-NDC projects in LDCs that have a crucial need for finance, testing out the relevance of a different claim for the private sector, assessing the feasibility of corresponding adjustments within NDCs.
- We will look do more work on the concept of a voluntary market account and see what it might look like in the light of recent progress made on CORSIA.

ICROA International Carbon Reduction & Offset Alliance

Appendix A: Forum Participants

Wednesday 23rd May 2018, Frankfurt

Name	Organisation	Title
Andrea Abrahams	BP Target Neutral	Global Director
Malin Ahlberg	BMU	Policy Advisor
Ana Aires Carpinteiro	Nexus for Development	Director Business Development
David Antonioli	Verra	CEO
Conor Barry	UNFCCC	Strategy Lead
Tom Baumann	ClimateCHECK	Co-Founder
Kathy Benini	IHS Markit	Managing Director
Martin Berg	EIB	Senior Investment Officer
Daniel Besley	World Bank	Senior Climate Change Specialist
Rodrigo Bezerrra	BP Target Neutral	Marketing Supply Manager
Harry Clemens	Hivos	Program Officer Carbon Finance and Green Society
Nick D'Alleva	APX Inc	Manager of APX VCS Registry
Antoine Diemert	ICROA	Programme Director
Thomas Forth	BMU	Senior Expert
Hilda Galt	Climate Focus	Senior Consultant
Ben Garside	Carbon Pulse	Correspondent
Jochen Gassner	First Climate	CEO
Billy Hamshaw	Numerco	Energy Trader
Edward Hanrahan	ClimateCare	CEO
Philipp Hauser	Engie	VP Energy Transition
Tatsushi Hemmi	Mitsubishi UFJ Research and Consulting Co., Ltd.	Chief Analyst
Simon Henry	IETA	EU Policy Director
Owen Hewlett	The Gold Standard Foundation	Chief Technical Officer
Joanne Hochheiser	IHS Markit	Director
Sam Hoffer	Verra	Manager, VCS & CCB Programs
Patricia Kastner	ClimatePartner GmbH	Carbon Offset Projects
Lene Keerberg	Climate Neutral Group	Carbon Portfolio Manager
Junaed Khan	UK Department of Business, Energy and Industrial Strategy	Policy Officer
Matthias Krey	Perspectives	Senior Advisor
Gerald Maradan	EcoAct	CEO
Wolfgang Obergassel	Wuppertal Institute for Climate, Environment, Energy	Project Co-ordinator, Energy, Transport and Climate Policy
Janet Peace	C2ES	Senior VP Policy and Business Strategy
Louis Redshaw	Redshaw Advisors Ltd	CEO
Lucile Rogissart	I4CE	Project Officer
Sandeep Roy Choudhury	VNV Advisory Services LLP	Head, Originations
Lambert Schneider	Stockholm Environment Institute	Associate
Chris Shipley	UK Department of Business, Energy and Industrial Strategy	Programmer Manager, Global Carbon Markets
Jonathan Shopley	Natural Capital Partners	Managing Director
Christopher Stephenson	Plan Vivo Foundation	Head of Operations
Jeff Swartz	Director Climate Policy & Carbon Markets	South Pole Group
Naomi Swickard	Verra	Director, Land-based Frameworks
Gareth Turner	Numerco	Director, Environmental Markets
Johan Ununger	ZeroMission AB	Chairman of the Board
Karl Vella	World Business Council for Sustainable Development	Climate Policy Manager
Marion Verles	The Gold Standard Foundation	CEO
Lisa Walker	Ecosphere+	CEO
Carsten Warnecke	NewClimate Institute	Partner
Vicky West	UK Forestry Commission	Woodland Carbon Code Programme Manager
Nicolás Westenenk	Ministry of Energy, Chile	Adviser
Claire Wigg	ZeroMission AB	CEO
Frank Wolke	German Environment Agency	Head of Section, Emissions Reduction Projects

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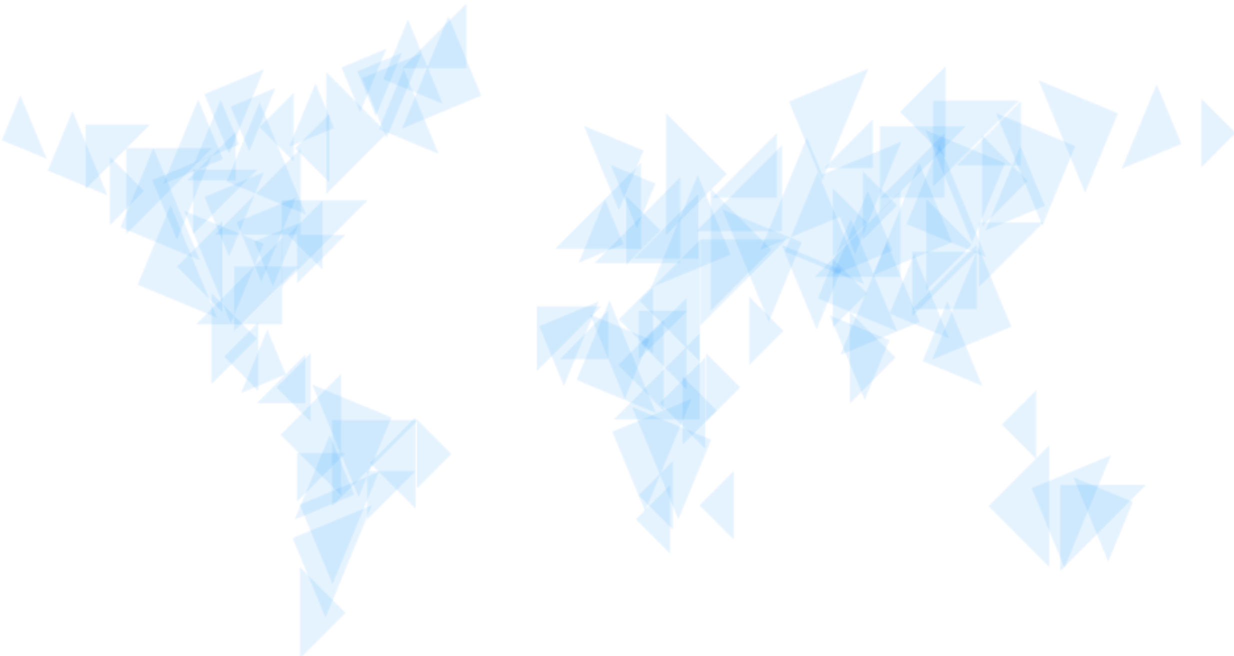

About ICROA and our purpose

ICROA is a non-profit organization made up of the leading carbon reduction and offset providers in the voluntary carbon market. It is housed within the International Emissions Trading Association (IETA). ICROA's primary aim is to deliver quality assurance in carbon management and offsetting through our member's adherence to the ICROA Code of Best Practice. This ensures credibility and quality for corporates using voluntary carbon offsets to reduce their greenhouse gas emissions and meet their carbon targets.

At a time when governments, businesses and organizations all over the world are looking for immediate and actionable solutions to keep the global temperature rise to below 2°C, ICROA plays a vital role in advocating for the use of offsetting and carbon finance to mitigate climate change. Being comprised of the leading companies in the voluntary carbon market, we provide a unified voice in these critical policy and market discussions.

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