10 February 2023

International Organization of Securities Commissions
Calle Oquendo 12
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Spain

Attention: Kris Nathanail
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By email, facsimile and post

Dear Sirs

Re: GFMA response to Voluntary Carbon Markets – Discussion Report

The Global Financial Markets Association (**GFMA**)[1] welcomes the opportunity to comment on the International Organization of Securities Commissions (**IOSCO**) "Voluntary Carbon Markets – Discussion Report" (**Report**).

Voluntary carbon[2] markets (**Voluntary Markets**) have an important role to play in supporting the transition to a low-carbon economy by facilitating the trading of carbon credits[3] which are capable of being surrendered to offset a corresponding volume of carbon emissions.

Voluntary markets have not yet scaled to their full potential. They are highly fragmented and derive from a range of standards which make them vulnerable to criticism for lacking integrity and transparency.

Voluntary Markets must be underpinned by the same core principles that underpin any sound and robust financial market: (i) transparency; (ii) integrity; (iii) stability; and (iv) accountability. Private initiatives such as the Integrity Council for Voluntary Carbon Markets[4] (**Integrity Council**) and the Voluntary Carbon Markets Integrity Initiative (**VCMi**)[5] are important because they seek to strengthen the robustness and integrity of Voluntary Markets.[6]

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[1] GFMA represents the common interests of the world's leading financial and capital market participants to provide a collective voice on matters that support global capital markets. It also advocates on policies to address risks that have no borders, regional market developments that impact global capital markets, and policies that promote efficient cross-border capital flows to end users. GFMA efficiently connects savers and borrowers, thereby benefiting broader global economic growth. The Association for Financial Markets in Europe (**AFME**) located in London, Brussels, and Frankfurt; the Asia Securities Industry & Financial Markets Association (**ASIFMA**) in Hong Kong; and the Securities Industry and Financial Markets Association (**SIFMA**) in New York and Washington are, respectively, the European, Asian, and North American members of GFMA. This submission reflects the views of a majority of the GFMA board members rather than those of any one member. Individual GFMA members may have views that differ from those expressed in this document.

[2] In this letter, references to 'carbon', 'emissions' and 'greenhouse gases' are references to those gases that become trapped in the Earth's atmosphere and contribute to the increase of surface temperatures, including: carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, chlorofluorocarbons, sulphur hexafluoride and nitrogen trifluoride.

[3] Carbon credits (each representing one metric ton of carbon dioxide equivalent) are issued in relation to climate change mitigation projects that prevent, mitigate, remove, sequester, or reduce emissions. Under the 2022 Verified Carbon Credit Transaction Definitions published by the International Swaps and Derivatives Association, Inc. a "Verified Carbon Credit" or "VCC" means "a unit with a unique serial number, measured in tCO2e, representing an Emission Reduction and quantified, verified and Issued into a Registry Account". An "Emission Reduction" is defined as "the removal, reduction, avoidance, sequestration or mitigation of emissions of greenhouse gases measured in tCO2e from the atmosphere which are capable of being represented in a form of unit of measurement pursuant to the relevant Carbon Standard Rules".

[4] In September 2021, the Taskforce for Scaling Voluntary Carbon Markets announced the formation of the Integrity Council as a new, independent governance body for Voluntary Markets. The Integrity Council is currently consulting on the 'Core Carbon Principles' and associated Assessment Framework and Assessment Procedure which aims to drive alignment of the standards applied to identify high-integrity carbon credits. The Integrity Council is concerned with the integrity and development of Voluntary Markets from the supply side.

[5] The VCMi, an independent, non-profit organisation, was launched in June 2021 and is concerned with the integrity and development of Voluntary Markets from the buy-side.

[6] For example by establishing principles for benchmarking the integrity of carbon credits and providing guidelines relating to transparency and climate related reporting.

Effective carbon markets, whether regulated or voluntary, should adhere to science-based decarbonisation principles. Their successful expansion, in line with global emissions reduction targets, is reliant upon collaboration between policymakers, regulators, market participants and other stakeholders across all jurisdictions to promote best practice and neutralise the risk of greenwashing,[7] carbon leakage,[8] double counting[9] and double claiming[10]. Globally consistent approaches are key to avoiding fragmentation, reducing costs and complexity, increasing usability and bolstering stability.

Divergent jurisdictional opinion as to the legal nature and regulatory treatment of carbon credits, means that there is currently no consensus as to which entity has, or should have, jurisdiction (at domestic or international level) to oversee and regulate Voluntary Markets. Nevertheless, we suggest that IOSCO's deep understanding of financial markets means IOSCO is best placed to:

- drive the dialogue relating to the development of Voluntary Markets forward; and
- mobilise the support of market participants and public bodies necessary to realise the potential of Voluntary Markets as a tool to help achieve global net-zero.[11]

We support IOSCO's efforts to:

(a) generate an open and meaningful, cross-industry dialogue with a view to maximising the potential of Voluntary Markets;

(b) identify the vulnerabilities relating to Voluntary Markets and collaborate with the private initiatives that seek to address them;

(c) identify the key regulatory considerations relating to Voluntary Markets to guard against market abuse;

(d) promote sound and well-functioning Voluntary Markets that adhere to best practice;

(e) identify and make recommendations to resolve uncertainties relating to the rules and procedures for: (i) trading 'mitigation outcomes' (under Article 6.2 of the Paris Agreement); (ii) trading carbon credits (under Article 6.4 of the Paris Agreement); and (iii) developing frameworks for co-operation between countries to reduce emissions through non-market based mechanisms (under Article 6.8 of the Paris Agreement), taking into account 'corresponding adjustments'[12] to avoid double counting and double claiming;

(f) strive for certainty as to the legal classification and treatment of carbon credits; and

(g) propose recommendations to relevant authorities (e.g. securities and commodities market regulators as well as public policy governmental institutions) to support the integrity and development of primary and secondary Voluntary Markets as a means to upscale and accelerate global decarbonisation efforts.

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7 Greenwashing refers to the act of providing misleading or false information about the environmental impact of an entity's products and operations.

8 Carbon leakage occurs when carbon generating activities are relocated to a jurisdiction which has a more lenient regime in respect of carbon emissions.

9 In this letter 'double counting' refers to where the benefit of a particular carbon allowance is claimed by more than one country as part of their respective emissions reduction commitments under the Paris Agreement.

10 In this letter 'double claiming' refers to where the benefit of a particular carbon allowance is claimed by: (i) a country; and (ii) a natural or a legal person, as part of their respective emissions reduction commitments under the Paris Agreement.

11 For example, by: (i) supporting the alignment of the language and integrity-benchmarking principles used in Voluntary Markets and the development of robust and liquid primary and secondary Voluntary Markets; and (ii) working with global regulatory bodies to determine the regulatory treatment of carbon credits and Voluntary Markets.

12 Corresponding adjustments are a type of accounting tool used by parties to the Paris Agreement to avoid the double counting of emissions reductions. Corresponding adjustments are effected by the host party adding the transferred emissions back into its national account whilst the receiving party subtracts the transferred emissions from its own account. This ensures that the host Party no longer counts the emissions reduction or removal as its own.

Our responses to the questions raised in the Report are set out in the schedule to this letter. We very much appreciate the opportunity to comment on the Report and we look forward to engaging with IOSCO further as may be helpful.

If you have any questions, or you would like to discuss the points raised in this letter, please feel free to contact us or our counsel, Richard Mazzochi (richard.mazzochi@hk.kwm.com; +852 3443 1046) and Claire Potter (claire.potter@hk.kwm.com; +852 3443 1093) at King & Wood Mallesons.

Yours faithfully

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Schedule – Responses to Questions

Question 1: Is our description of the issuance of carbon credits accurate? Have we properly reflected all key market participants?

We generally agree that the description of the issuance process for carbon credits set out in the Report is accurate. Our supplementary comments are set out below.

- Voluntary Markets support global decarbonisation efforts by:
  - allowing entities to support projects that avoid, mitigate, remove, reduce or sequester emissions through the sale, purchase and retirement of carbon credits over and above mandated emissions targets;
  - allowing entities to realise their individual climate change mitigation objectives by purchasing carbon credits derived from climate change mitigation projects that most resonate with them;
  - recognising the value of climate change mitigation projects by monetising their benefits;
  - directing capital flows in support of climate change mitigation projects and a 'fair transition' to net zero;
  - helping countries to realise their decarbonisation goals and commitments; and
  - promoting and preserving natural resources as a valuable commodity and supporting biodiversity.
- Carbon credits may be traded within Voluntary Markets irrespective of the location of the corresponding climate change mitigate project.
- In relation to the 'Carbon Credits Ecosystem' diagram on page 9 of the Report, we note that:
  - in cases where the project developer is not the same person as the owner (**Owner**) of the land or assets forming part of the applicable climate change mitigation project, the project developer must first engage with the Owner in order to fully develop the project and then present the same to a third party auditor for verification;
  - global initiatives (such as the Integrity Council and VCMi) work with individual certification bodies (such as Verra, The Gold Standard or Climate Action Reserve) that certify carbon credits; and
  - there is a growing number of ESG[13] rating agencies[14] that issue ratings in respect of carbon credits according to their own baseline and 'additionality'[15] models.
- Although the terms 'verification' and 'certification' may be used interchangeably by some, we consider that:
  - the terms 'verification' and 'verifier' relate to the auditors (or validation and verification bodes) that independently vet emissions reduction or removal before a project is certified (see below) as a project that generates carbon credits; and
  - the terms 'certification' and 'certifier' relate to the standard setting bodies (such as Verra, The Gold Standard or Climate Action Reserve) that certify, issue and register the carbon credits relating to a project.
- Voluntary Markets are highly fragmented due to the volume of different standards against which the existence and integrity of carbon credits are assessed. This variety of standards makes Voluntary Markets vulnerable to criticism for lacking integrity and transparency.
- The fact that Voluntary Markets are largely unregulated helps to promote innovation within Voluntary Markets and allows Voluntary Markets to be flexible and agile in their response to

[13] The acronym 'ESG' refers to environmental, social and governance.
[14] The Report identifies companies such as Sylvera or Calyx Global.
[15] The term 'additionality' refers to the 'value' that a climate mitigation project is assessed to have in terms of the volume of carbon reduced or removed from the atmosphere and correlates with the volume of carbon credits issued in respect of that project.

change. That is not to say that some form of regulation cannot benefit Voluntary Markets, provided that it is not at the expense of their innovation, flexibility and agility.

- The bodies that verify (i.e. auditors) and certify (i.e. standard setters) carbon credits are currently unregulated. We suggest that it may be beneficial for such bodies should be subject to formal regulation in order to help address concerns relating to integrity and transparency within Voluntary Markets.
- Within prescribed limits, it is possible for covered entities[16] to use carbon credits generated within a Voluntary Market in order to help them satisfy their compliance obligations within a compliance carbon market.[17] We consider that the use of carbon credits within compliance carbon markets is acceptable in principle provided that:
  - such use is closely monitored; and
  - the applicable carbon credits satisfy robust eligibility criteria;[18].
- Article 6 of the Paris Agreement has not automatically created "significant links" between Voluntary Markets and compliance carbon markets and is not expected to do so in the near future. Whilst there are connections between the Voluntary Markets and compliance carbon markets, they are not so similar or so interlinked that they should be automatically regulated in the same way.
- As regards the legal nature of carbon credits, please refer to our response to Question 6.

Question 2: Has the consultation identified the relevant vulnerabilities? Are there any others that should be considered? Please explain.

During IOSCO´s roundtables, key stakeholders and industry participants, expressed some concerns with respect to the lack of coordination between environmental regulators and securities markets regulators, highlighting the need for better coordination of industry-specific organizations and global standards.

We agree with the vulnerabilities relating to Voluntary Markets described in the Report, namely:

- the lack of standardisation within Voluntary Markets;
- assessing the integrity of carbon credits (including: (i) the 'value' and permanency of the benefits that they generate versus a 'business as usual' base-case; and (ii) their alignment with science-based decarbonisation pathways) in the absence of robust and consistent integrity benchmarks;
- the risks of carbon leakage, double counting and double claiming;
- the lack of transparency as regards the application and enforcement of climate change mitigation 'standards';
- the lack of transparency as regards the methods used to calculate the volume of carbon credits generated;
- the fact that Voluntary Markets (including verifiers and certification standard bodies) are unregulated;
- potential conflicts of interest arising between project developers, verifiers, certification standard bodies, traders and investors; and
- Voluntary Markets are decentralised. There is no single organisation that oversees (or takes responsibility for) the development or operation of Voluntary Markets.

[16] A "covered entity" is an entity that is mandated to participate in a compliance carbon market.
[17] For example, eligible credits may be converted into compliance instruments for use by covered entities within the Compliance Market in California.
[18] Such eligibility criteria may include: (i) only the highest-integrity carbon credits may be used; (ii) the project generating the carbon credit has the capacity to permanently remove or reduce carbon from the atmosphere; (iii) the project is assessed as satisfying the requirement for 'value' (or 'additionality') over and above a business-as-usual base-case; and (iv) the offset mechanic attaches only to 'unavoidable' or 'hard to abate' emissions.

We also wish to highlight the following as additional vulnerabilities relating to Voluntary Markets:

- the lack of certainty as to the legal nature and treatment of carbon credits. The legal classification of a carbon credit is crucial in determining, for example:
  - how title (or ownership) to it is evidenced, transferred and extinguished (upon retirement);
  - (subject to applicable law) whether a carbon credit (or an interest in it) can be held on trust;
  - (subject to applicable law) how security can be taken over a carbon credit and how that security may be enforced;
  - how a carbon credit is treated in the event of the insolvency of a transferor or transferee (including with regard to close-out netting); and
  - what rights of redress are available in the event of a dispute;
- the lack of certainty as to the accounting treatment of carbon credits;
- the lack of certainty as to the capital (risk-weighting) treatment of carbon credits (which may limit the extent to which financial institutions are willing to participate in Voluntary Markets, hold positions in carbon credits or manage portfolios that include carbon credits);
- inconsistent taxonomy and nomenclature creates confusion and results in market fragmentation;
- the potential reputational risk for financial institutions and other regulated entities being associated with 'low integrity' carbon credits or greenwashing (e.g. market manipulation through 'wash' trades, or where the underlying climate change mitigation project does not in fact exist);
- the potential reputational risk for financial institutions and other regulated entities being associated with the parties that verify or certify 'low integrity' carbon credits or that may otherwise be involved in greenwashing;
- the growing litigation risk associated with, for example, greenwashing and the legality of emissions reduction requirements in the context of a 'fair transition' to net zero emissions;
- with the potential for oversupply of carbon credits to lead to market saturation and low pricing. We suggest that market stability mechanisms[19] will be important to the overall development of the Voluntary Markets and mitigating pricing volatility;
- the lack of liquidity and price discovery;[20]
- clarification as to whether (and, if so, to what extent) carbon credits may be used to offset scope 1 emissions (to the extent that scope 1 emissions are not covered by a compliance carbon market);
- the absence of a clear and streamlined disclosure framework relating to the credentials of climate change mitigation projects and the carbon credits that they generate;
- the integrity (and therefore the 'value') of data 'output' relating to trading carbon credits relies on the integrity of data 'input'. We suggest IOSCO works with standard-setters to support the development of robust reporting frameworks and disclosure standards;
- the absence of standardised documents and procedures for trading and settlement within Voluntary Markets; and
- the existence of and access to 'low integrity' (and lower cost) carbon credits within Voluntary Markets is contrary to the spirit and purpose of Voluntary Markets.

[19] Examples include staged auctions and carbon credit volume thresholds.
[20] There is a lack of publicly available information available in relation to trading carbon credits, particularly over-the-counter trades (due to the bilateral and bespoke nature of over-the-counter transactions).

Question 3: **What kind of role could IOSCO play in coordinating the actions of industry-specific organisations and public authorities?**

As a well-established, international and highly respected organisation, we consider that IOSCO can (and should) support the development of Voluntary Markets by:

- actively participating in cross-industry dialogue and engaging with market participants (as it is already doing by issuing the Report) relating to the role and development of Voluntary Markets;
- actively participating in dialogue with industry bodies and relevant authorities as to the practical implementation of Article 6 of the Paris Agreement, and the role and use of 'mitigation outcomes' and non-market based approaches;
- (on the basis that scope 1 emissions are generally covered by compliance carbon markets) socialising the use of Voluntary Markets to address scope 2 and scope 3 emissions and inviting relevant authorities to define scope 3 emissions;[21]
- advocating a collaborative approach to the development of Voluntary Markets;
- making recommendations and issuing guidance as to 'best practice' based on IOSCO's financial market experience, in particular with respect to derivatives;
- publicly offering support to bodies such as the Integrity Council and the VCMi and inviting comments as to how IOSCO can best support them;
- publicly supporting overarching principles published by global governing bodies[22] as a means of setting an umbrella standard for best practice and encouraging alignment within Voluntary Markets;
- encouraging relevant bodies to provide certainty as to the legal classification and the regulatory, fiscal and accounting treatment, of carbon credits;
- encouraging regulators to closely monitor the use of carbon credits by covered entities;
- supporting the use of an umbrella standard proposed by the global governing body (such as the Core Carbon Principles proposed by the Integrity Council) as a means to assess the integrity of carbon credits and drive up competition for, and the pricing of, high integrity carbon credits even where the volume of available carbon credits outstrips demand; and
- canvassing analysis of, and better understanding as to the similarities and differences between, Voluntary Markets in key jurisdictions.

Question 4: **How do you think IOSCO should achieve these objectives?**

We consider that IOSCO is well placed to support (and should support) the development of Voluntary Markets by:

- identifying those standards and principles that reflect best practice and (where standards and principles differ) opportunities for achieving harmonisation through collaboration between the applicable standard setting bodies;
- supporting the development of the ICVCM 'Core Carbon Principles' and associated Assessment Framework and Assessment Procedure which aim to drive alignment of the standards applied to identify high-integrity carbon credits;
- supporting the standardization of the creation process for carbon credits;

[21] Scope 1, scope 2 and scope 3 refer to the classification of emissions pursuant to the Greenhouse Gas Protocol Corporate Standard published (as a joint initiative) by the World Resources Institute and the World Business Council for Sustainable Development to promote best practice for accounting and reporting emissions. Scope 1 emissions are direct emissions from owned or controlled sources. We expect that all Scope 1 emissions will eventually be covered by compliance carbon markets. Scope 2 emissions are indirect emissions from the generation of purchased energy. Scope 3 emissions are all indirect emissions (not included in scope 2) that occur in the value chain of the reporting company, including both upstream and downstream emissions.

[22] For example, the Core Carbon Principles proposed by the Integrity Council (when they are settled), in particular as regards the eligibility criteria for a 'high integrity' carbon credit.

- supporting the development of integrity-benchmark frameworks and disclosure standards; and
- leveraging their international reach and expertise to support (and engage the support of market participants in connection with) dialogue and coordination between governments, regulators and market intermediaries as regards the development of Voluntary Markets.[23]

IOSCO can consider the following suggestions as a means to achieve the objectives described above and in our response to Question 3:

- using the feedback received in response to the Report to identify commonalities and material differences between respondents as regards the role and development of Voluntary Markets;
- publishing the feedback received in response to the Report and canvasing views as to the priority of issues for further discussion;
- inviting comments on the published feedback from bodies such as the Integrity Council and the VCMi; and
- inviting collaboration between IOSCO and bodies such as the Integrity Council and the VCMi as regards the role and development of Voluntary Markets.

We note the challenge for IOSCO (as a securities regulator) that carbon credits are not classified as 'securities' in many jurisdictions. Relevant authorities therefore need to agree how, and the extent to which, IOSCO is able to best leverage their international reach and expertise in the context of Voluntary Markets.

Question 5: Should IOSCO seek to collaborate more closely with these private initiatives? How might such a collaboration function?

We think that it would be helpful for IOSCO to offer to collaborate more closely with bodies such as the Integrity Council and the VCMi as regards the development of Voluntary Markets. These bodies are important because they are driving alignment of climate-related taxonomies[24] with a view to supporting decarbonisation at the scale and speed necessary for countries to meet their emissions reduction objectives under the Paris Agreement. The advent and development of umbrella standards that are championed by bodies such as the Integrity Council and the VCMi are key to standardise the baseline for qualification as a 'high-integrity' carbon credit, which in turn underpins the integrity of, and public confidence in, Voluntary Markets.

We suggest that IOSCO could consider:

- establishing a working group (and potentially, sub-groups thereunder) to liaise with identified organisations, report developments and canvass opinion for action points and next steps; or
- endorsing (either independently or by joining with other interested parties) preferred frameworks, standards, approaches, processes or outcomes in relation to Voluntary Markets.

Where possible, we suggest that IOSCO should aim to leverage and endorse existing research and standards that are fit for purpose (or would be fit for purpose with some amendment). Again, where work has already been carried out to harmonise existing standards (as for example in the case of the ICVCM), we suggest that IOSCO should aim to leverage and endorse that work if appropriate.

[23] We note IOSCO's role in supporting the establishment of the International Sustainability Standards Board under the umbrella of the International Financial Reporting Standards Foundation, and we support IOSCO taking a similar approach as regards supporting the development of Voluntary Markets.
[24] For example, with through the development of the Core Carbon Principles and guidance relating to the use of carbon credits as part of credible net-zero pathways.

Question 6: What, in your view, is the legal nature of an offset credit? Should IOSCO recommend a specific approach to relevant authorities?

What, in your view, is the legal nature of an offset credit?

It is important to distinguish: (i) the legal classification and treatment of carbon credits; from (ii) the regulatory classification and treatment of carbon credits.

Whilst the legal classification of carbon credits determines, for example: (i) how title to carbon credits is evidenced and transferred; and (ii) how security over carbon credits can be taken and enforced, the regulatory classification of carbon credits determines which regulatory regime (and therefore which regulatory requirements and restrictions) applies to them. The analysis that follows focuses on the legal nature of carbon credits as a matter of common law.

There is currently no single global legal position as to the legal classification of voluntary carbon credits as an asset class. Without an authoritative statement in each applicable jurisdiction, market participants must look to the courts in common law[25] jurisdictions for guidance (albeit that the courts in such jurisdictions may be unwilling to make statements of general application in the absence of supporting legislation and also noting that the underlying facts of a particular case mean that distinctions can be drawn from other cases). Outside the courts, market participants must rely on general legal principles to determine the legal nature of carbon credits.

In determining the legal classification of a voluntary carbon credit, it is helpful to step back and consider what a carbon credit is, and most importantly, what benefits are conferred on the holder of a carbon credit.

The lifecycle of a carbon credit can generally be described as follows:

- an emissions reduction or carbon removal project is developed (a **Project**);
- the Project is certified by a recognised third party standard body (such as Verra, The Gold Standard or Climate Action Reserve) (a **Certification Standard Body**);
- the Certification Standard Body issues[26] carbon credits referable to the Project and adds them to a registry that constitutes the carbon credits. Each carbon credit represents one metric ton of CO_2e (being carbon dioxide or an equivalent greenhouse gas) that has been avoided or removed from the atmosphere;
- carbon credits may be purchased, traded, and sold to purchasers, either over the counter or (subject to suitability) through exchanges[27], in primary or secondary Voluntary Markets; and
- once a carbon credit is surrendered to reduce the volume of emissions attributable to a purchaser's operations, it is permanently retired so that no one else can claim the same reduction.

Based on the above attributes, carbon credits can be seen to represent exclusive access to a finite resource; that is, certification that the holder of the voluntary carbon credit (being the person in whose account it is credited from time to time in the register) has the right to claim a reduction or removal of the volume of greenhouse gas specified by the carbon credit, with such right being exercisable upon the retirement of the carbon credit.

It is possible for more than one legal classification to apply to a carbon credit, taking into account:

- its particular attributes: each carbon credit carries the attributes associated with the particular Project that it relates to (e.g. the nature or location of the Project); and
- how an interest in it is evidenced: for example, a bundle of contractual rights or title by registration.

[25] Common law jurisdictions are jurisdictions in which the decisions made by judges carry equal weight to statute.
[26] Carbon credits may either be issued according to: (i) verified emissions reduction or removal; or (ii) future expected emissions reduction or removal.
[27] For example, the Singapore-based global carbon exchange and marketplace, "Climate Impact X" facilitates the sale of large-scale, high-integrity carbon credits through standardised contracts that cater primarily to multinational corporations and institutional investors.

Whilst the rationale will vary between jurisdictions, from a common law perspective, a carbon credit is most likely classified as:

- a type of 'intangible property'; or
- a 'chose (or thing) in action'.

Voluntary carbon credits as a type of intangible property

In order for something to be classified as a type of property under English law:

> "…*it must be definable, identifiable by third parties, capable in its nature of assumption by third parties, and have some degree of permanence or stability*".[28]

Carbon credits can be said to satisfy these criteria on the basis that:

- (***definable***) they can be defined as a collection of rights conferred on the holder pursuant to the applicable CO2e emissions trading scheme;
- (***identifiable***) they can be identified by third parties by a unique reference number;
- (***assumption by third parties***) they are capable of assumption by third parties because they can be transferred under an CO2e emissions trading scheme; and
- (***permanence and stability***) they have permanence and stability because they are held in a registry account until transferred or retired and they can exist for a term of years.

Intangible property is an asset that has no physical form but that can nonetheless be owned and possessed. Some intangible property might have a paper embodiment (such as stocks, bonds, or certificates) but other intangible property does not (such as intellectual property and goodwill). Other examples of intangible property that have been recognised by the English courts include cryptocurrency assets such as Bitcoin[29] and carbon allowances traded on the European Union Emissions Trading Scheme (a compliance carbon market).[30]

In recognising EU allowances as intangible property, the court in question focused on the existence of a statutory regime to draw parallels with other types of intangible property such as export quotas[31], milk quotas[32] and waste management licences.[33] Whilst carbon credits may be distinguished from carbon allowances traded on the European Union Emissions Trading Scheme on the basis that: (i) they do not exist under a statutory regime; and (ii) have no special role in facilitating compliance with regulated emissions reduction obligations, such distinction does not, of itself, mean that carbon credits cannot be classified as a type of intangible property under English law.

It is therefore possible to view voluntary carbon credits as intangible assets, that are established in accordance with the relevant carbon standard and registry rules, title to which is evidenced by the register entries with the registry that constitutes the carbon credits. The courts have however stopped short of making any determination as to what type of intangible property they may be and have not ruled out classification of carbon credits as *choses in action*.[34]

Voluntary carbon credits as *choses in action*

A chose in action is a right that is claimed or enforced by action rather than by taking physical possession. Recognised examples of choses in action include:

- a right to receive a service under a contract; and

[28] National Provincial Bank v Ainsworth [1965] AC 1175.
[29] AA v Persons Unknown [2019] EWHC 2556 (Comm) (17 January 2020); Vorotyntseva v Money-4 Ltd (T/A Nebus.com) and others [2018] EWHC 2596 (Ch).
[30] Armstrong v Winnington [2012] EWHC 10, [2013] Ch 156
[31] Attorney General of Hong Kong v Nai-Keung [1987] 1 WLR 1339; Commonwealth of Australia v WMC Resources Ltd [1998] 194 CLR 1
[32] Swift v Dairywise Farms Ltd [2000] 1 WLR 1177
[33] Re Celtic Extraction [1999] EWCA Crim J0714-2
[34] Armstrong v Winnington [2012] EWHC 10, [2013] Ch 156

- a right to access cash in a bank account.

The ability of a Project to generate carbon credits (and the volume of carbon credits that such Project is capable of generating) must be certified by a recognised third party standard body (such as Verra, The Gold Standard or Climate Action Reserve). That verification process could be viewed as a contractual right to benefit from the entitlements of the verification process.

If a Project is later found not to comply with the prescribed verification requirements or the rules of the registry with which it is registered, then the carbon credits associated with that Project (and the corresponding rights to, and interests in, those carbon credits) may be cancelled. A claim may then arise against (by way of example) the Project owner or developer, the third party verifier, the applicable registry or any intermediary through whom a right or interest in the cancelled carbon credits is acquired or facilitated.

Practical consequences of different legal classifications

A carbon credit's legal classification is crucial in determining:

- how title (or ownership) to it is evidenced, transferred and extinguished (upon retirement);
- whether a carbon credit (or an interest in it) can be held on trust;
- how security can be taken over a carbon credit and how that security may be enforced;
- how a carbon credit is treated in the event of the insolvency of a transferor or transferee (including with regard to close-out netting); and
- what rights of redress are available in the event of a dispute.

The practical consequences of legal classification of carbon credits as *intangible property* or *choses in action* include those specified in the table below.

Carbon credits as intangible property	**Carbon credits as *choses in action***
The legal nature and treatment of carbon credits (in terms of the benefits they confer on the holder) would be consistent for all carbon credits.	The legal nature and treatment of carbon credits (in terms of the benefits they confer on the holder) may be affected by differences in drafting or contractual restrictions.
An asset, title to which passes upon transfer and registration.	A bundle of contractual rights, with transfer being effected by way of assignment (provided there is no contractual restriction against assignment) or novation (all parties' consent must be obtained).
Property without a physical existence (as opposed to tangible property).	Personal property right which can only be claimed or enforced by action at law or equity, and not by taking physical possession of the asset (as opposed to a *chose in possession*).
An equitable interest may be held in it which is capable of being the subject matter of a trust.	An equitable interest may be held in it which is capable of being the subject matter of a trust.
Legal and beneficial ownership of intangible property can be split, allowing different interests to exist at the same time.	Legal and beneficial ownership of a *chose in action* cannot be split.
A security interest over it may be created by way of charge or pledge and perfected by way of registration or as otherwise specified by applicable local law.	A security interest over it may be created by way of assignment (provided there is no contractual restriction against assignment) and perfected by way of notice or as otherwise specified by applicable local law.

Carbon credits as intangible property	Carbon credits as *choses in action*
Remedies available to a successful claimant in the event of a dispute may include a claim for proprietary restitution, conversion or unconscionable receipt of trust property. The defences available to a defendant may include that of a '*bona fide* purchaser for value without notice'.	Remedies available to a successful claimant in the event of a dispute may include a claim for equitable tracing, specific performance, damages or injunction.

Should IOSCO recommend a specific approach to relevant authorities?

As a matter of common law, the legal classification of carbon credits as a type of intangible property can be preferred from a financing perspective because, by way of example:

- the legal nature and treatment of carbon credits (in terms of the benefits they confer on the holder) would be consistent for all carbon credits (and would not be affected by differences in drafting or contractual restrictions);
- security can be taken over intangible property by way of a mortgage or a charge and perfected by way of registration;
- registration of a mortgage or a charge on a public registry promotes transparency;
- there is no need to separately serve notice of the creation of a mortgage or charge on applicable counterparties to preserve priority; and
- legal and beneficial ownership of intangible property can be split, allowing different interests to exist at the same time.

As noted above, the legal classification of carbon credits has wide-ranging implications. The possible legal nature of carbon credits currently differs across jurisdictions. In the absence of domestic legislation or an authoritative legal statement (supported by policies that set out the precise regulatory, fiscal and accounting treatment of carbon credits), the residual uncertainty as to the legal classification of carbon credits will undoubtedly impede the development of Voluntary Markets.

Given the difficulties in trying to reach an international consensus as to the legal or regulatory treatment of carbon credits, it may be more helpful for IOSCO to emphasise the need for legal and regulatory clarity as regards carbon credits within each jurisdiction that operates Voluntary Markets and to promote the need for open discussion and engagement on these issues.

Ultimately, the question as to what legal and regulatory classification is appropriate for carbon credits within a particular jurisdiction must be determined having regard to the underlying legal and regulatory framework that exists within that jurisdiction.

Question 7: **What is the role of blockchain and distributed ledger technology in voluntary carbon markets?**

In the context of Voluntary Markets, blockchain and other distributed ledger technologies (collectively, **DLT**) may be used in multiple ways, including:

- to evidence the control (and potentially ownership) of certain rights, or other interests, such as those inherent in a carbon credit, a green bond or a governance token;
- to evidence transactions (and facilitate tracing of transactions), such as the transfer of carbon credits from one person to another to enable the latter to meet their carbon offset requirements. The ability to trace transactions has the potential to help mitigate the risk of double counting or double claiming carbon credits (e.g. by being able to identify the underlying assets that are 'attached' to a particular carbon credit) as well as transactional counterparty risk;

- to facilitate the storage of immutable data about emissions reductions and emissions removals achieved – for example, as part of the smart metering of water, gas and electricity, or satellite-based forest measurements; and
- to standardize trading procedures and protocols.

For the reasons summarised above, we consider that DLT is capable of giving comfort to participants in Voluntary Markets as regards the ownership, security of transfer of, and data-capture in relation to carbon credits and related transactions. Consideration should however be given as to how DLT interfaces with carbon registries.

Question 8: **What are the benefits and vulnerabilities of using tokenisation over relying on more traditional market infrastructure? Do these benefits outweigh how energy-intensive the use of blockchain is?**

Some of the key benefits of tokenisation are:

- at the token level, enabling an agreed definitive record of property. This can avoid double counting, double claiming and disputes;
- programmability. This includes the ability to control who may participate in a DLT platform and hold tokens, as well as to pre-define multiple other rules to achieve commercial and compliance objectives;
- accessibility, by enabling the fractionalisation of interests in property to enable a greater level of access to that property in a direct manner;
- at a transactional level, enabling the efficient and auditable flow of value recorded on DLT. Efficiency can be particularly enhanced when transactions are deployed with the aid of smart contracts to permit, by way of example, the pre-programmed (or 'atomic') trade of a digital carbon credit against a stablecoin or the automated trigger of a payment under a digital green bond; and
- liquidity, although this is highly dependent on the availability of relevant markets.

The key vulnerabilities of DLT relate to its application, design and execution. DLT is not 'trustless' even though it can enable transactions and other interactions between parties that do not know one another. Typically, the following factors must be addressed:

- pertinence. DLT is not always the most appropriate solution. Certain systems are appropriately centralised because of their nature and related governance framework. Or they may be decentralised among only a small number of participants;
- suitability. Any DLT solution must be designed and executed to ensure it offers the functionalities required and meets fundamental performance, scalability, security, resilience, settlement finality and compliance objectives;
- compliance, including to meet data protection, taxation, financial crime, ESG and reporting obligations. Wherever possible, this should be by design;
- interoperability, particularly where transactions are envisaged;
- legal framework. Beyond the code itself, the natural language contracts and arrangements between participants are essential for legal certainty; and
- "black swan" readiness, including with a carefully considered intervention and liability model. This should address smart contract exploits, malfeasance and technology breakdown.

DLT need not be energy intensive. While a 'proof-of-work' public blockchain such as Bitcoin requires a significant amount of energy, this is not true of all other protocols. The source of energy used by different protocol participants can also vastly differ. As such, the 'greenness' of a DLT solution should be examined on a case-by-case basis, including on a comparative basis with its traditional alternatives. Other environmental, social and governance factors should also be taken into account when undertaking that review.

Question 9: **Should IOSCO recommend good practices regarding transparency on the use and impact of carbon credits by market players?**

"*We recommend that standard-setting bodies, in coordination with the broader ecosystem, facilitate the transformation and scaling of the [Voluntary Market] to ensure its integrity, role, and additionality*."[35]

IOSCO has a strong track record in developing high-integrity, international standards and we would welcome IOSCO's recommendations for good practices as regards transparency on the use and impact of carbon credits, and defining what 'transparency' means within Voluntary Markets. We suggest that this is best achieved in consultation with other industry bodies such as the Integrity Council so as to ensure consistency, command attention and be persuasive (and avoid creating barriers that could restrict the growth of Voluntary Markets).

In particular, we suggest that it would be helpful for IOSCO to support:

- initiatives to align climate-related taxonomy and disclosure;[36]
- initiatives to align the attributes of a high-integrity carbon credit;[37]
- the development of robust pathways for the implementation of Article 6 of the Paris Agreement; and
- the development of 'best practice' guidance as to the use carbon credits to offset unavoidable or 'hard to abate' emissions (with the key message being that carbon credits should not be used to 'dilute' compliance obligations or otherwise as a substitute for emissions reduction).

As set out in our response to Question 4, the challenge for IOSCO is that carbon credits are not classified as 'securities' for regulatory purposes in many jurisdictions. Relevant authorities therefore need to agree how, and the extent to which, IOSCO (as a securities regulator) is able to best leverage its international reach and expertise in the context of Voluntary Markets.

Question 10: **Are these the key considerations appropriate for the sound functioning of voluntary carbon markets?**

IOSCO has identified fourteen key considerations which could be relevant for regulators contemplating frameworks to promote market integrity in Voluntary Markets and help overcome some of the present limitations of these markets. Those key considerations, and our comments in relation to the same, are set out below.

1. The degree to which, and how, to allow for open, broad market participation in Voluntary Markets.

   To ensure that:

   - the obligations of covered entities within compliance carbon markets are enhanced;
   - compliance carbon markets can effectively expand their coverage; and
   - participation in Voluntary Markets is as open as possible,

   we suggest that Voluntary Markets are best suited to offset emissions that are not covered by a compliance carbon market i.e. Voluntary Markets should complement emissions reductions within compliance carbon markets.

   Effective management of the use of carbon credits as described above will require guidance from relevant authorities as to the measurement, reporting and verification of emissions (in particular scope 3 emissions).

[35] "*Unlocking the Potential of Carbon Markets to Achieve Global Net Zero*", October 2021 – GFMA and Boston Consulting Group; section 4.2; "*Drive standardization and maturity*".
[36] Such as (when finalised) the ICVCM 'Core Carbon Principles' and associated Assessment Framework and Assessment Procedure.
[37] Ibid.

2. How to ensure that Voluntary Markets have sufficient integrity to operate without fraud, manipulation, or disruption.

The orderly functioning of Voluntary Markets, as with any financial market, relies on robust trading and settlement infrastructure. Such infrastructure cannot remove the risk of market abuse entirely but can mitigate the scale of that risk. Exchanges, brokers and other market intermediaries, as well as carbon registries are all essential to the smooth operation of Voluntary Markets and, at all levels (from project development, to certification, to registration, to transfer, to retirement), transparency is key. At the same time, standardisation of documents, consistency of definitions, alignment of taxonomy, and clarity as to the legal and accounting treatment of carbon credits (among other things) are all important to the integrity, efficiency and scalability of Voluntary Markets.

Global bodies such as the Integrity Council will be pivotal to:

- creating meaningful and positive dialogue (and knowledge sharing) about the role and development of Voluntary Markets;
- establishing frameworks for cross-border and cross-market trading in Voluntary Markets;
- publishing guidance as to the implementation of Article 6 of the Paris Agreement;
- avoiding further fragmentation within Voluntary Markets;
- establishing market protective measures within Voluntary Markets;
- coordinating enforcement of applicable rules and standards across Voluntary Markets;
- liaising with governments and regulators;
- incentivising alignment with 'best-practice'; and
- procuring sufficient certainty as to the operation of Voluntary Markets and the legal treatment of carbon credits to attract large-scale investment in net-zero transition.

3. How to provide market participants in Voluntary Markets with sufficient liquidity and price discovery to execute trades on a timely basis with minimal price dislocation.

Liquidity is a function of the size of the underlying market. For so long as, and to the extent that, participation in Voluntary Markets is voluntary, the liquidity of primary and secondary Voluntary Markets depends (at high level) on:

- the volume of carbon credits available for purchase; and
- the demand[38] for carbon credits.

The liquidity of Voluntary Markets can be improved through carbon based derivatives. However, this must not be at the expense of global decarbonisation targets.

Potential market protective measures to help ensure that trades are executed in a timely manner with minimal price dislocation include: (i) reserve pricing or pricing adjustments; (ii) volume thresholds for carbon credits; (iii) assessing the integrity of carbon credits by reference to an umbrella standard such as the Core Carbon Principles (when finalised); (iv) greater centralisation of trading activities and data collation; (v) minimum disclosure standards; and (vi) 'delivery versus payment' settlement.

[38] Demand for carbon credits may be driven, for example, by the desire for competitive advantage or to achieve philanthropic objectives.

4. How to promote transparency by ensuring that market participants in Voluntary Markets have sufficient data publicly available.

In the absence of mandatory disclosure requirements[39], the volume and scope of available data will be driven by investor demand, the requirements of Voluntary Market exchanges and the requirements of Voluntary Market intermediaries.

We suggest that data relating to trading carbon credits is made publicly available[40] on the websites of carbon exchanges and carbon registries. Ideally, over time, data collection will become centralised so as to effectively manage the risk of double counting, double claiming and carbon leakage.

We support initiatives such as the Climate Action Data Trust[41] and encourage IOSCO to consider the opportunities that meta-registries offer (whilst recognising the importance of robust cybersecurity and effective disaster recovery planning).

5. How participants in Voluntary Markets may disclose their use of carbon credits in their financial reporting.

We note that bodies such as the International Sustainability Standards Board (**ISSB**) and the International Accounting Standards Board (the standard setting bodies for the IFRS Foundation) have published proposals regarding the disclosure of material information about a company's significant sustainability-related risks and opportunities, and that such proposals have been developed in response to requests from (among others) G20 leaders and IOSCO. We support the development of such proposals and welcome the finalisation of ISSB's Climate-related Disclosures Standard (IFRS S2).

6. How to facilitate price discovery for carbon credits in Voluntary Markets.

See our response at paragraph 3.

7. How to accord with global, high-integrity standards against which the environmental integrity of carbon credits and their underlying methodology can be assessed.

It is critical to the integrity of Voluntary Markets that climate-mitigation projects demonstrate: (i) clear 'additionality' over and above a business-as-usual base-case; and (ii) permanence of emissions removal or reduction, in each case firmly based in science.

We encourage internationally respected bodies such as IOSCO to publicly support:

- those certification standard bodies that adhere to the most robust, comprehensive and project-focused standards for the certification of carbon credits; and
- best-in-class, umbrella standards (such as those being developed by the Integrity Council).

Given the critical role that certification standard bodies have to play in Voluntary Markets, we would ideally like all certification standard bodies to be independently regulated and audited, and we would welcome an open dialogue with key market participants as to the perceived costs and benefits of implementing such an approach. We would also welcome a discussion

[39] To the extent that disclosure is voluntary, the content and volume of available data may be more limited and the presentation of available data may have greater inconsistency, all of which potentially impacts the transparency and integrity of Voluntary Markets.

[40] We note that publicly available data is limited for over-the-counter transactions given the bilateral and bespoke nature of such transactions. However, given the potential scale for over-the-counter trades in (or referencing) carbon credits, we suggest that the scope of data-capture in respect of (and public availability of data relating to) over-the-counter transactions relating to carbon credits is a topic that merits open discussion.

[41] The Climate Action Data Trust is a joint initiative of The International Emissions Trading Association, the World Bank and the Government of Singapore which is intended to act as "a global platform that links, aggregates and harmonises all carbon credit data from project registries to facilitate transparent accounting", through the use of distributed ledger technology.

as to whether there could be merit in the implementation of a resolution mechanism for cases where the integrity of a carbon credit is questioned.

8. How, and to what extent is it possible to standardise carbon credits in order to promote greater liquidity.

Whilst we agree that standardisation of trading documents promotes efficiency and liquidity and also reduces operating costs, this should not detract from the individual attributes of the underlying projects generating carbon credits. The variety of projects that generate carbon credits means that a single, standardised approach to the classification and regulation of carbon credits is not necessarily appropriate or helpful.

In order to promote competition for high-integrity carbon credits (and increase the price of carbon), we would welcome clarification (from a body such as the Integrity Council) as regards the criteria for classification of carbon credits as 'high-integrity'. Integrity benchmarking (by reference to an umbrella standard) is a common feature within commodities markets (e.g. metals, green coffee, white sugar and cocoa[42]) which promotes fungibility and helps to mitigate market fragmentation risk.

9. How to take steps to improve the interoperability of offset registries in Voluntary Markets.

Interoperability between Voluntary Markets is currently limited. Greater interoperability between Voluntary Markets with similar decarbonisation ambitions will help to scale up trading and market liquidity (provided that increased interoperability does not dilute emissions reduction targets within individual Voluntary Markets) and help to mitigate the risk of double counting and double claiming.

Alignment of standards and procedures within Voluntary Markets requires effective 'measurement, reporting and (independent) verification', including as regards the integrity of carbon credits traded and the ambition of decarbonisation targets. Again, we suggest that benchmarking the integrity of carbon credits against an internationally recognised, umbrella standard such as the Core Carbon Principles (when finalised)) is an important part of the toolkit for mitigating fragmentation risk in Voluntary Markets.

10. How to ensure that market participants engaging in Voluntary Markets have sufficient financial integrity to ensure the cash settlement or physical delivery of a carbon credit transaction.

We agree with the approach set out the Report. Whilst the innovation, flexibility and agility of Voluntary Markets should be preserved, we consider that market intermediaries should be regulated entities that are required to comply with minimum standards as to (by way of example) their financial standing; data collection, transfer and storage; fit and proper personnel; internal governance; compliance monitoring and operational infrastructure.

We suggest that certain principles and objectives applicable to securities or commodities derivatives markets may (by extension) have application within Voluntary Markets. For example:

- protecting integrity through fair and equitable rules;
- transparency of transactions;
- the ability to detect and deter market manipulation and other unfair practices; and
- policies and procedures relating to data handling, market disruption, risk management and internal audit.

[42] Grading applies to metals traded on the London Metal Exchange and to commodities such as green coffee traded on the Intercontinental Exchange.

11. What are the legal challenges that stakeholders in Voluntary Markets may encounter during the lifecycle of an offset.

Please see our response to Question 6. The legal nature and treatment of carbon credits has yet to be clarified by an authoritative legal statement at jurisdictional level.

A carbon credit's legal classification is crucial in determining key issues such as:

- how title (or ownership) to it is evidenced, transferred and extinguished (upon retirement);
- whether a carbon credit (or an interest in it) can be held on trust;
- how security can be taken over a carbon credit and how that security may be enforced;
- how a carbon credit is treated in the event of the insolvency of a transferor or transferee (including with regard to close-out netting); and
- what rights of redress are available in the event of a dispute.

12. How to ensure that key participants and infrastructures in Voluntary Markets have appropriately robust governance frameworks.

We agree with the approach set out in the Report.

13. How to identify, manage, and resolve conflicts of interest in Voluntary Markets.

Conflicts of interest in Voluntary Markets can arise in circumstances such as:

- where the purchaser of carbon credits deriving from a particular industry is also the regulator of that industry;
- where the purchaser of carbon credits deriving from a particular project is also the project developer;
- where the purchaser of carbon credits is a connected party to the project developer (or otherwise has an interest in the proceeds from the sale of carbon credits);
- where the project developer or a purchaser of carbon credits deriving from a particular project have connection with the organisation that certifies the environmental credential of that project; and
- where the verifier of the project is appointed (and paid for) by the project developer.

Effective management of conflicts of interest in Voluntary Markets requires:

- disclosure and transparency about all of the parties (directly or indirectly) connected with a carbon credit generating project;
- tracking details about the holders of carbon credits; and
- tracing the use of funds deriving from the sale of carbon credits.

We note however that overly prescriptive requirements may impede the development, and impose unnecessary expense during the development phase, of Voluntary Markets . An acceptable compromise may be for spot checks and self-audit.

14. How to ensure that key participants and infrastructures in Voluntary Markets have effective systems of risk management and internal controls.

We agree with the approach set out in the Report. Risk management (including the ability to identify and effectively manage operational risk) is central to robust internal governance, as part of which risk management policies (and details as to who has primary responsibility for such matters) should be regularly updated.

Question 11: What other key considerations may be necessary in order to scale up carbon markets?

We list some additional considerations relating to upscaling of Voluntary Markets below. As regards compliance carbon markets, please refer to our separate response to IOSCO's "Compliance Carbon Markets – Consultation Paper".

Additional considerations:

- We suggest that the long-term role of Voluntary Markets needs to be clarified. Voluntary Markets may be viewed as:
  - a transitionary coverage mechanism for sectors or regions that are not covered by compliance carbon markets, carbon taxes, or other control-based mechanisms, until regulated mechanisms take over;
  - a long-term marketplace for carbon removals and carbon reductions to support the growth and funding of new technologies and the neutralisation of residual emissions; or
  - a complementary mechanism for entities to compensate for value-chain decarbonisation, helping to channel capital where it is needed most.
- We consider that an authoritative legal statement is required from each jurisdiction that participates in Voluntary Markets to remove residual uncertainty as to the nature and treatment of carbon credits.[43]
- We consider that financial intermediaries have an important role to play in Voluntary Markets, not least by:
  - facilitating trades and creating liquidity in primary and secondary Voluntary Markets;
  - driving standardisation of documentation and trading systems;
  - disseminating market information that is not readily available; and
  - identifying potentially harmful trading activity and taking steps to counter such activity.
- We consider that guidance is required:
  - in order for market participants to effectively measure, report and verify scope 2 and scope 3 emissions;
  - as to the fiscal and risk-weighting treatment of carbon credits;
  - as to how participants in Voluntary Markets should disclose their origination (if applicable) and use of carbon credits in their corporate filings and any marketing or disclosure materials; and
  - about to the extent to which carbon credits may be used to satisfy the obligations of covered entities in compliance carbon markets. It is important that the focus of all market participants remains firmly on emissions reduction (with the use of carbon credits being limited to offset unavoidable or 'hard to abate' emissions).
- We suggest that there is a balance to be struck within Voluntary Markets between: (i) regulation/supervision; and (ii) organic market development. Too much regulation, too early, risks to stifle growth and be 'out of sync' with how Voluntary Markets operate in practice. In addition, until Voluntary Markets reach a certain size and scale, the cost of regulation/supervision (and the resources required to implement the same) may outweigh the benefits.

[43] We agree with the analysis published in December 2021 by the International Swaps and Derivatives Association in its paper titled Legal Implications of Voluntary Carbon Credits, that the "*characterization of a [carbon credit] itself will be distinct from the characterization of a transaction in [carbon credits] (including from a regulatory perspective)*".

- We suggest that governments:
  - take active steps to support, formalise operational policies relating to, and issue clear guidance on the use and implementation of, Article 6 of the Paris Agreement; and
  - enter into or memoranda of understanding with other governments to promote interoperability within Voluntary Markets prior to the completion of 'official' steps to implement Article 6 of the Paris Agreement.