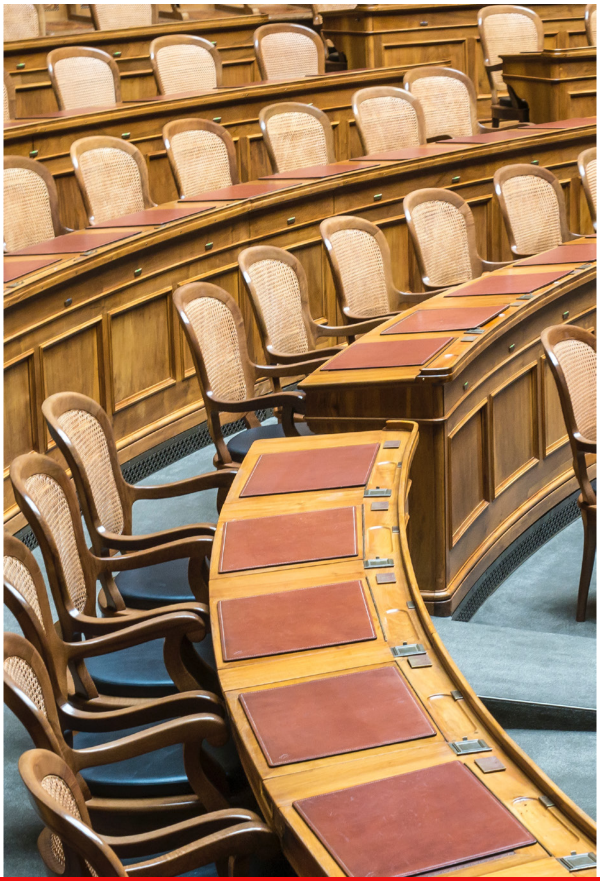
The Voluntary Carbon Market **Explained**

Chapter 2



Chapter 2: What is the role of governments in the VCM?

Governments engage with the voluntary carbon market (VCM) by instituting policies, regulations, and safeguards that influence VCM activities, create enabling environments that facilitate VCM projects or programs, and sponsor VCM projects or programs within their territories.

Who regulates the VCM?

The VCM is governed by private carbon standards that define the rules for the generation, monitoring, and certification of greenhouse gas (GHG) reductions and removals. The private and voluntary characteristics of the VCM distinguish it from regulated carbon crediting programs like the Clean Development Mechanism (CDM), which requires project developers to obtain a letter of approval from a country's Designated National Authority to register a CDM project.

The private character of the VCM makes it nimble and flexible. It allows the VCM to support climate mitigation, biodiversity protection, or sustainable development goals by providing finance for new technologies, nature-based solutions (NbS), and other important climate change mitigation activities that are not or not fully covered by public policy. However, like any other investment, VCM projects can also violate public policies, particularly where activities disregard the rights of local communities, ignore principles of good governance, or fail to align with and complement public sector goals and regulations.

Companies engage in the VCM to reduce and remove GHG emissions beyond public requirements. However, that does not mean that governments do not have a role to play in accelerating, channeling, or regulating VCM investments. Governments can institute policies, regulations, and safeguards to guide the development of VCM projects in their territories and attract beneficial VCM finance. They can create an enabling environment for VCM investments and actively encourage investments in projects or programs that generate carbon credits. They can also directly engage in the development of projects and programs.

Although the VCM is governed by private standards, governments can engage with and benefit from the VCM. Governments engage with the VCM in two main ways: as regulatory authorities in "host countries" where VCM activities take place and as investors in VCM activities. In all cases, governments can provide regulatory and political certainty to VCM transactions by clarifying the rules of engagement for the VCM.

How can governments proactively and strategically engage with the VCM?

Host countries can develop strategies to proactively engage with the VCM. Strategic engagement can attract carbon finance to support national policy priorities and minimize risks from poorly-designed VCM activities. When developing strategies for VCM engagement, host countries should consider their specific finance needs for implementing Nationally Determined Contributions (NDCs) and other national priorities. Once host country governments have clarified their NDC financing needs, they can determine the role for the VCM in delivering this finance. Deciding on the role the VCM can play in financing NDC goals involves identifying climate change mitigation areas that are not or insufficiently covered by public policy and making decisions about offering corresponding adjustments under Article 6.

Governments can provide regulatory and political certainty to VCM transactions by specifying the rules of engagement for the VCM in their countries, explicitly stating that they are ready to attract and support project developers and investors, and clarifying relevant rules, regulations, and safeguards. Host country governments can establish legal and regulatory frameworks to ensure that the VCM is operating in legal certainty and is aligned with public policies.

The VCM also influences public policy and compliance markets, and in some cases, voluntary carbon crediting programs directly interact with government carbon pricing schemes. The carbon pricing policies of California, Colombia, Germany, South Africa, Thailand, or the United Kingdom are examples of governments harnessing VCM activities to achieve climate goals. In Colombia and South Africa, for example, companies can meet some obligations under national carbon taxes by acquiring carbon credits from domestic VCM projects.

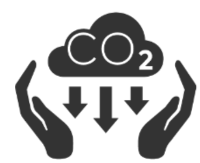
What are the roles for governments in the VCM?

Governments can leverage VCM finance by engaging in the VCM as program regulators, program proponents or facilitators:

As regulators, governments can define environmental and social performance standards or safeguards that bind project developers. Stable and predictable policy environments reduce investment risks and help private investors align their plans with public policies. Efforts to combat corruption, promote the rule of law, recognize the rights of Indigenous Peoples and Local Communities (IPs&LCs), and clarify land rights and titles facilitate private investment into VCM projects. When governments assign and enforce land and resource rights, they help to clarify carbon rights—defined as who holds the right to benefit from GHG emissions reductions and removals—and facilitate benefit sharing arrangements.

Government regulation can influence corporate claims with respect to the use of carbon credits. Governments encourage the high-integrity use of carbon credits by developing policies such as mandatory sustainability disclosures, refusing advocacy proposals from or concessions to corporates that seek to undermine climate action, and clarifying and enforcing land tenure laws.

Finally, governments can provide clarity on how VCM activities will be considered under country laws and regulations, including for corresponding adjustments under Article 6 of the Paris Agreement. While some buyers are expecting corresponding adjustments on VCM credits, the availability of corresponding adjustments depends on VCM host countries' political will and technical abilities. Governments can reduce uncertainty by making public statements about whether, and under which circumstances, they are likely to provide corresponding adjustments for VCM transactions. These statements can be conditional upon the government's technical ability to make corresponding adjustments. Governments may also limit corresponding adjustments to the parts of the NDCs that are conditional on climate finance, more expensive mitigation options or offer corresponding adjustments on the condition that they will receive financial benefits from the sale of carbon credits in return.



As program proponents, governments can sponsor VCM projects and programs. In some countries, public agencies—such as national park authorities (e.g., in the case of forestry projects) or municipalities (e.g., in the case of waste management projects) — act as project proponents and use carbon finance to support public investments. For example, in Guatemala, the national park authority acts as a proponent in the **GuateCarbon project** by granting land-use rights to communities and private organizations who carry out sustainable forest harvesting and help to monitor the reserve.

The **Daegu City Municipal Waste Project** in the Republic of South Korea is an example of a municipality acting as a project proponent and the **Weatherization for Low-Income Dwellings** project in the U.S. State of Maine is an example of subnational government acting as a project proponent. Governments can also support large-scale territorial programs in the form of jurisdictional Reducing Emissions from Deforestation and Degradation Plus (REDD+) programs that generate GHG emission reductions or removals across landscapes. If such programs are accredited under a VCM carbon standard, then governments can generate and sell program-level credits in the VCM. Jurisdictional programs allow governments to align public policies with REDD+ goals and access carbon finance directly. REDD+ also offers jurisdictional crediting options that require governments to be the proponents of such programs. Governments can adopt nesting rules that allow the integration of projects and subnational programs into national REDD+ programs.

As facilitators, governments can attract and direct VCM finance. The way that governments communicate about the VCM and engage with VCM actors influences overall confidence in the VCM, and encourages or discourages the development of VCM projects. By encouraging the development of domestic VCM projects, governments can use the VCM to drive investment in climate change mitigation activities that are underfinanced, such as clean cooking, developing decentralized energy supplies, or agroforestry and other NbS.

Governments can direct financial flows from the VCM to the sectors or policy priorities where finance is needed most by defining criteria for engagement and by recognizing VCM standards, methodologies, or protocols for particular sectors. This, together with publication of information and data, enhances the transparency and efficiency of the market. In addition, governments can maintain registries to track and monitor carbon credits and projects, simultaneously demonstrating their support for the VCM and increasing transparency of VCM-related activities in their countries.

Further reading

Climate Focus & UNDP. (2023). VCM Access Strategy Toolkit. Retrieved from https://vcmintegrity.org/wp-content/uploads/2023/05/VCMI-VCM-Access-Strategy-Toolkit-1.pdf

Streck, C., Dyck, M., Mithra Manirajah, S., & Fernandez Armenteros, M. (2022). Voluntary Carbon Market: Considerations for host countries. Retrieved September 28, 2023, from https://climatefocus.com/publications/voluntary-carbon-market-considerations-for-host-countries/

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