ENERGY CLUB
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THE CARBON CODE: TRADING, TRACKING AND TRANSFORMING EMISSIONS

DAY 2

CARBON CREDITS IN A NUTSHELL

click here

WHAT ARE CARBON CREDITS?

Carbon credits are generated by projects that have avoided or removed greenhouse gas emissions. Each credit represents one fewer tonne of carbon dioxide, or another greenhouse gas equivalent, (CO_2e) in the atmosphere. The projects rely on the sale of carbon credits in order to operate, and are independently audited to verify the tonnes of carbon emissions avoided or reduced.

HOW DO CARBON CREDITS WORK?

Many organizations have ambitious climate targets. Meeting these often involves reducing the emissions associated with their own activities, while funding external decarbonization projects to offset the emissions that cannot yet be reduced.

This is where carbon credits come in. Because they are issued, monitored, and verified according to stringent, internationally recognized standards, they allow businesses to compensate for their unavoided emissions reliably and transparently.
Through their use of carbon credits, companies can provide stakeholders with proof that when they say they have offset carbon emissions they have done so.

Carbon credits enable critical finance to flow to decarbonization projects around the world, which is necessary to ensure that we meet our global climate goals, and support communities most impacted by climate change, yet least responsible.

WHAT IS THE DIFFERENCE BETWEEN CARBON CREDITS AND CARBON OFFSETS?

The terminology is not consistent, which can be confusing. Offsetting is when a company funds external carbon projects that remove, reduce, or avoid greenhouse gas emissions to compensate for their own.

Carbon credits are what the company purchases in order to offset its unavoided emissions. Each credit proves that one tonne of CO_2e has been avoided or sequestered out of the atmosphere.

Importantly, we are referring exclusively to carbon credits in the voluntary carbon market, where businesses choose to invest in external carbon reduction projects.

There are also compliance markets, where government programs cap emissions, often aimed at high emitting sectors, and businesses therefore must take action. Compliance schemes work differently around the world, but in some a certain percentage of a company’s emissions can be covered through the purchase of carbon credits.

WHO SELLS CARBON CREDITS?

Carbon projects need to be registered to an internationally recognized standard, which issues carbon credits once there has been independent verification that the project has generated the required emissions reductions or removals.

The credits are issued into a registry, which is a giant database holding all the details of each credit (i.e. standard, methodology, geography, vintage, date of issuance etc.). The credits are issued into the registry account of the project owner who is responsible for the Carbon Asset Development, i.e. all the processes that go into designing a project to issue carbon credits and then making sure they are audited and delivered. There may be more than one organization involved in setting up and running projects and it may include local community partners or corporate investors.

Following issuance, credits are then available to be bought and sold. Often credits are sold to a specialist carbon market 'retailer' - a company that has set up the systems and processes to assess carbon project quality, source the best projects, and create and manage portfolios of carbon credits for end buyers who want to meet more ambitious climate targets than they can deliver through internal reductions alone. The carbon credits enable them to compensate for their unavoidable emissions and contribute to the low carbon transformation in another country.

For a company to compensate for its unavoidable emissions, the carbon credit must be 'retired'. This is done on a publicly available registry and means the standard counts the carbon credit as spent - it cannot be sold or used by anyone else - allowing the end buyer to officially offset one tonne of CO_2e against its carbon footprint.

WHAT DETERMINES THE QUALITY OF A CARBON CREDIT?

To qualify as a carbon finance project it must meet some fundamental criteria. Specifically, high-quality projects must meet the following criteria to establish the quality of the carbon credit. These are designed to ensure quality in carbon market approaches to meet global climate goals:

- Real. The avoidance or removal of CO_2e must actually occur.
- Measurable. It must be possible to reliably quantify an emission reduction.
- Additional. This means that there is a net emission reduction that would not have happened were it not for the sale of carbon credits. For example, if a project were already legally required to do what it is doing it would not count as additional, nor would it be additional if it can achieve all its funding through other mechanisms. The sale of carbon credits is required to enable the project to take place.
- Unique. Each tonne of CO_2e avoided or removed must count towards only one carbon credit. Companies cannot double count the same carbon credit towards separate emission reductions targets.

WHAT DETERMINES THE QUALITY OF A CARBON CREDIT? (CONTINUED..)

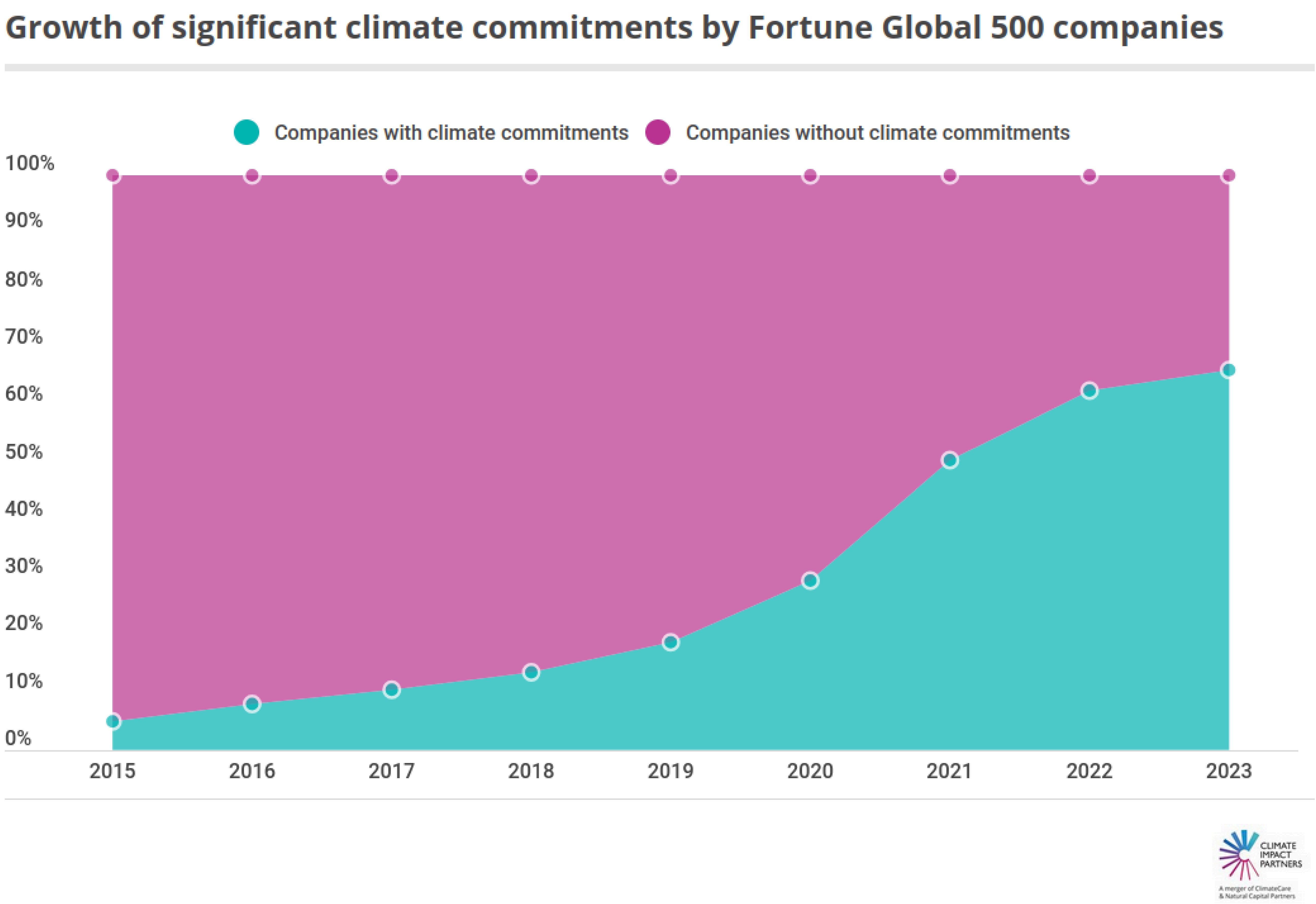
- Permanent. This focuses on how long the carbon dioxide removed or avoided will be kept out of the atmosphere. To count as permanent, the reduction must be designed to last for at least 100 years, with robust measures to prevent and compensate for future events that might reverse the reduction. Projects that are at risk of reversal, such as forestry projects that may be damaged by wildfire, must allocate a portion of carbon credits - determined by risk factors - to a central buffer pool, which cannot be traded on the voluntary carbon market. The buffer pool acts as an insurance pot, ensuring there are spare carbon credits, in the event of future worst-case scenarios.
- Risk managed. This involves taking steps to ensure that the project is developed as envisaged, continues to follow evolving scientific evidence and meets the relevant standard's rules, and doesn't fall foul of changing legislation and regulations. Climate Impact Partners has considerable expertise here, with more than 25 years taking projects through the full cycle, from idea through to carbon credit retirement (see below).
- Independently verified. An independent auditor must review each project to validate that it follows the appropriate methodology that has been set by a standard, and to verify that the monitoring and measurement of emission reductions are accurate before carbon credits are issued.

WHO BUYS CARBON CREDITS?

Recognizing the increasing risks of climate change on communities throughout the world, the sustainability of businesses, and a thriving planet for future generations, organizations of all sizes are setting public targets to reduce emissions and offset what they cannot avoid in order to meet ambitious climate targets. By 2023, 66% of the Fortune Global 500 had made a significant climate commitment.Many of these (35%) are Science-Based Targets that focus on internal reductions in line with the Paris Agreement's goal of limiting global heating to 1.5C above pre-industrial levels. Others commit to further action now to compensate for unavoidable emissions through carbon credits which avoid emissions, such as avoided deforestation and clean cooking. And increasingly there are commitments (39%) to go further and aim to reach net zero in the future, where any remaining annual emissions generated by the business will be entirely cancelled out using removal only carbon credits.

These businesses want to demonstrate to their stakeholders that they have a committed and ambitious plan, and carbon credits are critical to meeting targets along the way. Investing in them provides a way to take immediate action towards long-term sustainability goals in a way that delivers carbon emissions reductions and supports the communities most impacted yet least responsible for climate change.

WHO BUYS CARBON CREDITS?



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