Reclaim Finance and Amazon Watch's response to the TSVCM consultation

June 19th 2021

Dear TSVCM

For years, **carbon offset markets failed to provide real climate or environmental benefits**. They have been riddled with fraud and human rights abuses, rely on debunked assumptions, suffer from intractable conceptual issues and at scale create serious risks of food prices skyrocketing. In recent years, offsets have also transferred the responsibility of climate action to poorer – and often less regulated – areas, with major companies from rich countries purchasing offsets that require action in so-called developing countries. By itself, this should be enough to question the idea of creating new offset markets to supposedly mitigate climate change.

Of course, the TSVCM might argue that one of its stated goals is also to provide a harmonized and strengthened framework for carbon offsets that would potentially increase their quality and reduce the risks of them being ineffective or dishonest. However, this would require a major increase in the strength of the norms set and effective verification process – though achieving this would be extremely difficult. While carbon offsets may look serious "on paper," they have delivering little to no environmental benefits. Even if the many fraud, additionality, human rights, and other problems inherent in offsets were resolved, it is highly doubtful that enough carbon offset projects would be available to feed demand for this pay-to-keep-emitting model.

The TSVCM ignores the fact that **carbon offsetting does not accelerate, but on the contrary delays, climate action**. By condensing alleged climate action in a small, easy-to-buy product, the model creates distance between the cause of the climate crisis – the buyer – and the solution to the problem.

More importantly, **offsetting is not about trapping past emissions but about enabling current and future emissions, at best it simply displaces – and not reduced – emissions**. The whole point of an offset is that one entity gets to keep emitting. For this reason, offsetting is not about mitigating climate change, but about providing the social license for high emitting activities to continue and about minimizing the cost of compliance to new climate regulation and voluntary pledges.

Furthermore, **failed or non-permanent "offsetting" – for example, in the event of forest offsetting that burns or leaks CO2 storage – could unexpectedly add up large quantitates of GHG to the atmosphere**. These risks can never be eliminated, as offsets rely on "nature-based solutions" that are exposed to major external events or on unproven technologies like carbon capture and storage (CCS).

These dangerous effects would be greatly increased by a highly efficient and liquid carbon offset market that TSVCM wants to create, by allowing companies to easily purchase offsets to artificially fulfill their climate pledges. For carbon intensive sectors, where reducing GHG emissions often requires important investments, the purchases of carbon offsets is an easy way to escape responsibility and might provide a "cost-efficient" replacement for real GHG reduction. It is worth noting that several companies – notably airlines – already started billing their customers for "carbon compensation". Such practices could allow them to make profits while misleadingly claiming environmental progress.

In a word, **carbon offsets should not be considered a climate solution**. While in some cases offsets could deliver environmental benefits, they never compensate for the non-reduction of GHG emissions and using them as such creates major problems that could severely derail the transition to a carbon-free economy. So-called "**Carbon offsets" should only be used as additional voluntary environmental contribution, that do not replace GHG reduction and cannot be used to claim compliance with any regulation nor pledge**. The wording "carbon offsets" itself is misleading and dangerous and another wording – like "environmental contribution" or "ecosystem protection" - should be used.

While the TSVCM fail to acknowledge the risks tied to carbon offsets, it already recognizes that "companies' internal decarbonization and emissions reporting remain the priority with offsetting playing an important but complementary role". However, this statement is **not followed by binding measures and mechanisms that would ensure that offsets are used only when all decarbonization measures have been taken**. The justification for offset purchases will always ultimately be made by the buyers, and thus rely solely on their good faith.

While we strongly disagree with the general approach of the TSCVM and its goal to set up a carbon offset market that could be used by companies to purport to meet their climate pledges and obligations, we also want to stress several specific weaknesses in the framework designed by the TSCVM:

1. **Forestry offsets dangerously included:**
   Despite the problems with forestry offsets, including much harder to calculate additionality, documented cases of human rights abuses, conflicts over land-use and risks of "green" land grabbing, forestry offsets are not excluded from the proposed market. The recent study documenting how the Amazon rainforest now appears to release more CO2 than it is storing as a result of widespread deforestation is a case in point in the inherently temporary and uncertain nature of CO2 storage in trees – and the related risks for investors of including forestry offsets.
2. **The risk of linking carbon offsets with Emission Trading Schemes:**
   The Taskforce report foresees links to and convergence with compliance markets, including the forthcoming Sustainable Development Mechanism that is expected to be finalized at the COP26. We strongly hope that this voluntary market will not be linked directly or indirectly to any Emission Trading Scheme (ETS), as allowing the use of offset credits in cap-and-trade markets would once again remove the cap, thereby significantly weakening climate change mitigation.
3. **Design features favor gambling over climate action:**
   - **Futures and options contracts**: While spot contracts (contracts to buy and sell credits now) are necessary for offsetting purposes, futures and options contracts are not. They enable betting on the future prices of credits, either for speculative purposes or for hedging purposes. About the first purpose, financial speculation on the future price of carbon is not necessary from an environmental perspective. Furthermore, speculation leads to increased price volatility that makes any price signal unobservable. Yet if there is no price signal, markets do not provide any incentives, and are therefore useless. As for hedging, it would allow insuring against a future rise in the price of carbon, through

either purchasing credits to be delivered at a future date but at a price agreed today (futures contract) or buying tailor-made insurance contracts against a future rise in the price of carbon (option contract). Hedging removes the incentive that support curbing emissions, and as such it is bad for the climate. Since both potential uses and purposes of options and futures contracts are detrimental from a climate perspective, we believe that such contracts should be not allowed in the market, and only spot contracts should be.

- **Carbon index fund**: the report also foresees investments in "carbon index funds" as a way for private corporations to fulfil their carbon neutral pledges. The way it is supposed to work according to the report is that corporations purchase a stake in the index fund, then at the time of their choosing sell the stakes and use the cash to purchase credits with physical delivery. Such a fund would seem to only play a role for hedging, which would is problematic for the reasons described above.
- **Securitization of offsets**: The technical appendix describes the possibility of having pooled portfolios of offset projects, whose tranches could be traded OTC or through exchanges. This seems to suggest the securitization of carbon offset projects, the technique that was at the heart of the 2008 financial crisis and led to the originate-to-distribute model of subprime mortgages. The potential issues associated with carbon securitizations have been amply documented.

4. **Potential conflicts of interests in the governance:**
The report foresees a new umbrella governance body that "is an independent, voluntary, stakeholder-led and self-regulating body." This would mean that those who benefit directly from the new carbon market would oversee its governance and therefore set the standards for themselves and their clients. The mandate of the governance body itself is problematic as it requires providing oversight and fostering the growth of the market, two objectives that may be contradictory if oversight imply high-level standards.

We hope the TSVCM will globally reframe its project to account for the dangers highlighted above and prohibit the use of offsets to fulfill any type of carbon reduction or climate action claims.

Yours sincerely,

Reclaim Finance

Amazon Watch