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January 5, 2023

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Re: Reply to Comments Submitted in Response to Request for Information on Climate-Related Financial Risk, 87 Fed. Reg. 34856

This comment letter responds to the Commodity Futures Trading Commission's (the "CFTC's" or the "Agency's") Request for Information on Climate-Related Financial Risk (the "RFI") and, in particular, certain comments submitted by other stakeholders regarding that RFI. Verra appreciates the opportunity to comment on the above referenced request and to inform the Agency's understanding of the voluntary carbon markets ("VCMs").

This comment letter focuses, in particular, on responses that were submitted regarding RFI questions 22, 23, and 24, which ask questions regarding the VCMs. Verra believes it is well-positioned to provide responses to these questions given we operate the Verified Carbon Standard ("VCS") Program, the world's largest greenhouse gas (GHG) crediting program in the VCMs and which includes related protocols to certify reductions and removals of carbon emissions.[1]

This comment letter is organized as follows: Part I outlines the benefits of VCMs to project developers, consumers and the environment; Part II sets forth the process by which VCMs continue to evolve; and Part III discusses the legal status of VCMs and VCMs' participants under the Commodities Exchange Act ("CEA") and the CFTC's corresponding regulations.

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[1] While often referred to as "registries," "GHG crediting programs" include a series of requirements (e.g., for demonstrating project integrity, to ensure proper auditing), as well as a registry which serves to ensure transparency and avoid double counting, among other benefits. In short, a registry is part of a GHG crediting program and should not be referred to in isolation.

In summary, VCMs have delivered and are poised to continue to deliver substantial carbon emission reductions and climate financing. Verra has played a leading role in the development of the VCMs and its success in doing so is rooted in its commitment to ensuring the integrity of VCMs through development of a comprehensive set of program-level requirements as well as project-specific protocols for carbon reductions and removals, and through participation in collaborative initiatives like the Integrity Council for the Voluntary Carbon Market ("ICVCM").

Carbon instruments meet the definition of commodities under the CEA and, accordingly, the CFTC can bring enforcement actions against fraud or manipulation in VCMs, as it does in other commodity spot markets. However, contrary to the positions of some other commenters which responded to the RFI, in Verra's view, VCMs are spot markets for carbon credits, and thus are not derivatives markets implicating broader CFTC authority under the CEA. Rather, the CFTC's regulatory authority over VCMs is limited to its general anti-fraud/anti-manipulation statutory authority described above. Of course, the CFTC has broad authority over futures, options, and swaps that are based on carbon credits, including any such derivative instruments issued by market participants based upon credits issued by Verra or other GHG crediting programs. But Verra's carbon credits themselves are not such derivative instruments, and we thus are of the view that the CFTC's authority to police fraud and manipulation in VCMs does not extend to deciding whether a particular carbon reduction or removal project meets criteria warranting the issuance of a credit.

I. VCMs Play a Significant Role in the Fight Against Climate Change

VCMs are an important tool in efforts to combat climate change and are well-positioned to support corporate net-zero targets, including among companies that have adopted science-based targets. Companies and other entities that purchase carbon credits in VCMs do so voluntarily, driven by a desire to reduce their net emissions and to contribute to the climate transition. GHG crediting programs such as Verra's VCS Program have facilitated the rapid growth of VCMs by creating an ecosystem with the trust and fungibility necessary for buyers to confidently purchase carbon credits, which, in turn, has created a robust and growing source of climate financing for carbon removal and emissions reduction projects worldwide.

Ecosystem Marketplace estimates that, through December 2021, VCMs have traded $8 billion of carbon credits—representing $8 billion of financing for carbon removal and emissions reduction projects that would not exist absent VCMs.[2] Of that $8 billion, almost a quarter came just in 2021.[3] VCMs continue to grow as corporate and other buyers recognize the benefits of leveraging carbon credits to make progress toward emission reduction goals, in support of their science-based targets and in pursuit of the goal of a net-zero future.

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[2] *The Art of Integrity: State of the Voluntary Carbon Markets 2022 Q3*, Ecosystem Marketplace (Aug 2022), available at https://registry.verra.org/app/projectDetail/VCS/1408.

[3] *Id.*

Verra is a nonprofit corporation organized under the laws of the District of Columbia and a tax-exempt organization under Section 501(c)(3) of the U.S. Internal Revenue Code. Its mission is to develop and manage standards that help countries, the private sector, and civil society achieve their sustainable development and climate action goals. To those ends, Verra oversees and implements the VCS Program, which is the world's leading voluntary GHG crediting program. Developers of projects that will reduce carbon emissions can seek VCS certification, and if successful, they are issued Verified Carbon Units ("VCUs"), tradeable carbon credits that each represent a reduction of carbon emissions or removal from the atmosphere of one ton of carbon dioxide equivalent.

The VCS Program, through the projects for which it unlocks climate financing, supports climate resilience and sustainable development for the communities that need it most, including projects that provide demonstrable benefits to local communities and enhance biodiversity and other environmental objectives. For example, the one billionth VCS Program carbon credit was issued from the Chyulu Hills REDD+ project in Kenya, which is run by a conservation trust that uses carbon credit revenue from deforestation prevention and degraded forest restoration activities to help the Chyulu Hills region community rehabilitate their local environment and improve living conditions through work, education, water access, and health initiatives, amongst others.[4]

Chyulu Hills REDD+ is not an exception; many of the projects on the Verra Registry, beyond reducing global carbon emissions and issuing VCUs, support holistic climate adaption and sustainable development. The most recent round of projects open for public comment offer a number of additional examples.[5] One proposes to distribute high-efficiency cook-stoves to remote and low-income households in Uttar Pradesh and Madhya Pradesh, India, which will reduce the time needed to collect firewood, as well as the prevalence of illnesses attributable to inefficient indoor cooking with solid fuels and kerosene.[6]

Another proposes to construct solar-powered water filtration systems in rural communities in southern Madagascar, ensuring access in those communities to safe water, and removing the need to collect and burn wood and other biomass in order to boil untreated water.[7] In short, through the leadership of nonprofit organizations like Verra, VCMs continue to benefit the places and communities most at-risk on our warming planet, in addition to mitigating the threat posed by a warming plant through

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[4] *See id.*; *Chyulu Hills Redd+ Project*, Verra Registry, https://registry.verra.org/app/projectDetail/VCS/1408.

[5] *See Projects Open for Public Comment: 12 December, 2022*, Verra (Dec. 12, 2022), available at https://verra.org/projects-open-for-public-comment-12-december-2022/.

[6] *See Installation of High Efficiency Cookstoves in Uttar Pradesh and Madhya Pradesh (India)*, Verra Registry, https://registry.verra.org/app/projectDetail/VCS/3942.

[7] *See Mila Rano – Safe Water Access for Madagascar*, Verra Registry, https://registry.verra.org/app/projectDetail/VCS/3936.

carbon reduction and removal projects, amounting to over 1,900 projects around the world delivering over one billion carbon reductions or removals to-date.

II. The VCMs Continue to Evolve and that Evolution Enhances their Integrity and Transparency

VCMs are constantly evolving. Verra, in particular, is continually refining its standards and processes for carbon credits, and engaging with the public, in order to ensure its programs are reliable and trusted. For example, Verra recently announced the development of a long-term monitoring system ("LTMS") to track the agriculture, forestry, and land use projects after they issue carbon credits, in order to ensure that issued credits reflect permanent reductions in carbon removals.[8] As with many of Verra's ongoing initiatives to build on the solid foundations of the VCS Program, the LTMS is being developed through a public consultation process. New projects similarly undergo a public consultation process before their registration with the VCS Program is finalized.[9] Verra has also recently established a dedicated Auditing and Accreditation team to oversee the performance of validation and verification bodies that certify projects, one of a number of steps taken to increase the capacity of the VCS Program to issue rigorously-certified carbon credits as VCMs continue to grow.[10]

A key element of the VCS Program is the Verra Registry, which, in addition to containing information on certified projects, tracks the issuance of VCUs and their retirement (when buyers decide to claim the associated emissions reduction). All information on projects is available for public access and inspection: their registration and certification documents, their record of VCU-issuance and associated verifications, and whether their issued VCUs have been retired, and by whom.[11]

Verra believes that it is imperative to the healthy functioning of the VCU-market, and its contributions to the climate transition, that the Verra Registry only list projects that meet the high standards of the VCS Program, that it accurately track the ownership of VCUs and their retirement status, and that it facilitates a market that serves the cause of global emissions reduction. In service of those ends, Verra has implemented strict controls over the Verra Registry. For example, Verra conducts "Know-Your-Customer" background checks on all new Verra Registry account applicants; requires accountholders to seek Verra's written permission if they are transacting in "related instruments" such as carbon credit derivatives; prohibits accountholders from acting as

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[8] *Development Of Long-Term Monitoring System (LTMS) Begins*, Verra (Dec. 1, 2022), available at https://verra.org/development-of-long-term-monitoring-system-ltms-begins/.

[9] *See, e.g., Projects Open For Public Comment: 5 December, 2022*, Verra (Dec. 5, 2022), available at https://verra.org/projects-open-for-public-comment-5-december-2022/.

[10] *New Auditing And Accreditation Team*, Verra (Nov. 3, 2022), available at https://verra.org/new-auditing-and-accreditation-team/.

[11] For example, see the project page for the Chyulu Hills Redd+ Project, referenced in note 4 above.

brokers for natural persons for investment purposes; and formally commits Verra to acting as a "reasonable and prudent operator" of the Verra Registry.[12]

Verra also participates in collaborative initiatives, such as the ICVCM. The goal of the ICVCM and its participants, including Verra, is to set a global threshold for carbon credits that will ensure their high quality and underpin VCMs' growing importance in contributing to the climate transition. Verra supports the work of the ICVCM, and is an active participant in the ongoing effort to draft and adopt effective principles for carbon credit standards and project assessments. To these ends, Verra submitted detailed responses and comments this September on the ICVCM's proposed Core Carbon Principles and Assessment Framework.[13]

III. Legal Landscape of VCMs

A. The legal status of carbon credits

VCMs implicate the CFTC because carbon credits are commodities under the CEA. The CEA's definition of commodity includes a long list of specific enumerated commodities such as cotton or soybeans, along with the catch-all language "and all services, rights, and interests . . . . . in which contracts for future delivery are presently or in the future dealt in."[14] Verra understands that the CFTC has therefore taken the view that the definition of a "commodity" effectively means any service, right, or interest for which a futures contract exists, or could exist in the future.

As carbon credits are a right to claim the associated emissions reduction generated by a certified project, and may be the subject of a futures contract, they qualify as commodities under this definition. Indeed, over the past decade, the CFTC has taken the position that carbon credits are commodities, including by identifying an "environmental, commodity, such as an emission allowance" as an example of a deliverable intangible commodity in a 2012 rulemaking.[15]

B. The CFTC's authority over spot commodity markets, including VCMs

The CFTC has the authority to police fraud and market manipulation in spot commodity markets. The CEA and CFTC regulations make it illegal, in connection with any commodity transaction in interstate commerce, to employ fraudulent schemes, to make any untrue or misleading statement of material fact or omit a material fact

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[12] *See Verra Registry Overview*, Verra, https://verra.org/registry/overview/; *Verra Registry – Terms of Use*, Verra, https://verra.org/registry/terms-of-use/.

[13] *Verra's Comments On The ICVCM Consultation*, Verra (Sept. 28, 2022), available at https://verra.org/icvcm-consultation-verra-comments/#.

[14] CEA Section § 1a(9).

[15] Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48208, 48233 (Aug. 13, 2012).

necessary in order to make a statement not misleading, or to engage in any other form of deceit.[16] Verra understands that the CFTC regularly brings enforcement actions against individuals and entities who engage in price manipulation, misappropriation of material, confidential, non-public information, and other forms of fraud and deceit that disrupt the orderly operation of commodity markets.[17]

Verra supports the CFTC's exercise of its enforcement authority in VCMs to protect investors and the integrity of the market. The CFTC is well-positioned, within the bounds of its existing enforcement program, to pursue instances of fraud or market manipulation in the VCMs. Verra, as described above, is committed to the continued development and enhancement of VCMs, in order to continue to unlock climate financing and deliver meaningful reductions in global carbon emissions.

C. The CFTC's regulatory authority over commodity futures

Under the CEA, the CFTC has broad regulatory authority—beyond its enforcement authority—over derivatives as well as commodity futures contracts, that is, "transactions involving . . . contracts of sale of a commodity for future delivery."[18] The CEA, however, "does not provide the Commission with [regulatory] jurisdiction over true 'spot' transactions. In a spot transaction, immediate delivery of the product and immediate payment for the products are expected on or within a few days of the trade date."[19] Carbon credit transactions in VCMs, including those recorded by counterparties on Verra's Registry, are spot transactions; the sale of a carbon credit results in the delivery of the credit in exchange for payment.

Because the purchases and sales of carbon credits within VCMs are spot transactions, the CFTC does not have broad regulatory authority to regulate carbon credits or offsets bought and sold in VCMs, although it has clear authority to police fraud and market manipulation in VCMs. By contrast, the CFTC has clear authority to regulate the markets for futures based on carbon credits and, indeed, carbon credit futures and derivatives that are created by market participants other than Verra trade on CFTC-registered exchanges and are certified by those exchanges to the CFTC.[20]

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[16] 17 C.F.R. § 180.1. *See also* CEA Sections 4c, 6(c), 8(a)(5).

[17] *See generally* Commodity Futures Trading Commission, Division of Enforcement, *Enforcement Manual* (May 2020).

[18] CEA Section 2(a)(1)(A).

[19] Commodity Futures Trading Comm'n, Div. of Trading & Markets, CFTC Letter No. 98-73 (Oct. 8, 1998).

[20] *See, e.g.*, CME Group, *Notification Regarding the Initial Listing of the Physically-Delivered CBL Global Emissions Offset Futures Contract* (Feb. 11, 2021), available at www.cftc.gov/sites/default/files/filings/ptc/21/02/ptc021621nymexdcm001.pdf.

D. Issues raised by other commenters

Some commenters suggested that the CFTC should undertake significant regulation of VCMs. Verra would like to take this opportunity to respond to two such arguments, in particular.

First, some commenters, such as CarbonPlan, argue that the CFTC should create standards for carbon credits, despite the establishment of such standards by Verra and similar organizations. Those standards reflect the consummation of scientific and technical research and stakeholder collaboration to establish the value of a particular carbon reduction or removal project in reducing the concentration of CO_2 in the atmosphere and thereby mitigating climate change. That value is denominated in metric tons of CO_2-equivalent (CO_2e) and incorporates conservative factors and buffer pools to ensure the integrity of the denominated reduction or removal. Despite these standards, CarbonPlan suggests that the CFTC should impose its own definitions of carbon removal and carbon credit durability, as well as creating a registration framework for carbon registries that would allow the CFTC to investigate and review registries' carbon credit methodologies.[21]

These proposed approaches are beyond the CFTC's authority over VCMs. As described above, VCMs are spot commodity markets, and as such the CFTC's authority is intended to prevent fraud and market manipulation. The type of regulation CarbonPlan is suggesting—entity-registration and oversight of product standards—is characteristic of the CFTC's activities in the futures and derivatives markets, *not* spot commodity markets. Moreover, CarbonPlan does not explain why a financial markets regulator, such as the CFTC, is better placed to regulate carbon offsets and the spot market for the same, than, for example, a federal agency focused on environmental or consumer protection or a nonprofit organization such as Verra, whose mission is the development and maintenance of the highest standards of integrity and transparency in the VCMs.[22] In the view of Verra, the CFTC's authority over fraud and market manipulation does not extend to determining the criteria for whether products purchased in the VCMs are worthy of consideration as an offset that produces demonstrable climate benefits.

Second, a few commenters suggest that carbon registries should be regulated as "delivery points" for carbon credit-based futures and derivatives products. The Center for American Progress, for example, suggests that the CFTC could directly regulate

[21] CarbonPlan Comment on CFTC Request for Information on Climate-Related Financial Risk, Oct. 7, 2022, Comment #70871.

[22] Indeed, the EPA ended its voluntary Climate Leaders Program in 2010 for precisely the reason that it "determined that climate programs operated by the states and NGOs are now robust enough to service our Partners and other entities that wish to continue to advance their climate leadership..." *See* Gina McCarthy, Assistant Administrator, Office of Air and Radiation, U.S. EPA, "Climate Leaders" Letter (Sep. 15, 2010), *available at*: https://19january2021snapshot.epa.gov/climateleadership/climate-leaders-partners-letter-15-september-2010_.html.

registries as delivery points and require them to engage in "market surveillance, compliance, and enforcement practices and procedures."[23] This, however, reflects a misunderstanding of the delivery points-authority. In fact, the authority cited by the Center for American Progress requiring "market surveillance, compliance, and enforcement practices and procedures" applies to regulated boards of trade, not delivery points.[24] While futures exchanges (which are ultimately regulated by the CFTC) may, through their rulebooks and certification processes, set quality thresholds for commodities that underlie listed futures and derivatives products,[25] there is no separate CFTC authority to impose a regulatory regime on delivery points.

Moreover, it is unclear whether a registry within a GHG crediting program, such as Verra's Registry, is a "delivery point," because the legal transfer of ownership of carbon credits occurs bilaterally through agreements executed between the transacting parties; those transactions are then recorded by Verra in its Registry. The Verra Registry tracks the issuance of VCUs and their retirement by an entity claiming ownership of a carbon credit and the resulting emissions reduction or removal, but in no instance does Verra ever take custody of VCUs or financial assets.

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In sum, the standards for determining whether a carbon reduction or removal project warrants issuance of a credit are dynamic and constantly evolving, as new scientific information is produced and the VCMs continue to evolve. Verra would submit that, despite the CFTC's authority both to police fraud and market manipulation in commodity markets and to regulate futures and derivatives markets, the scientific and technical questions that some commenters suggest the CFTC should answer concerning the additionality and validity of carbon credits may be better addressed through stakeholder processes convened by nonprofit organizations or by other federal agencies. For instance, the Federal Trade Commission ("FTC") recently sought input on its existing Green Guides' treatment of carbon offsets to consider, among other things, any evidence of deception in the VCMs, how the FTC could provide guidance to help VCM-participants avoid such deception, and research concerning how the use of carbon credits supports corporate "climate change-related claims such as 'net zero,' 'carbon neutral,' 'low carbon,' or 'carbon negative.'"[26]

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[23] Center for American Progress Comment on CFTC Request for Information on Climate-Related Financial Risk, Oct. 7, 2022, Comment #70821.

[24] *Id.*; 17 C.F.R. § 38.250.

[25] *See, e.g.,* NYMEX Rulebook, Chapter 200: Light Sweet Crude Oil Futures, available at https://www.cmegroup.com/content/dam/cmegroup/rulebook/NYMEX/2/200.pdf (setting quality thresholds for light sweet crude oil that is deliverable for NYMEX light sweet crude oil futures, including, for example, the oil having 0.42% or less sulfur content).

[26] *See* Guides for the Use of Environmental Marketing Claims, FTC, 87 Fed. Reg. 77766, 77768 (Dec. 20, 2022), https://www.federalregister.gov/documents/2022/12/20/2022-27558/guides-for-the-use-of-environmental-marketing-claims.

Verra looks forward to working with the CFTC to ensure that the VCMs operate with transparency and integrity and thereby fulfill Verra's charitable mission of helping countries, the private sector, and civil society achieve their sustainable development and climate action goals.

Best Regards,

/s/ *David Antonioli*

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