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Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st St NW
Washington, DC 20581

Re: RIN 3038-AF40, Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts; Request for Comment

We are filing this comment on behalf of James Copland, Senior Fellow and Director of Legal Policy at the Manhattan Institute.

Thank you for the opportunity to comment on the Commodity Futures Trading Commission ("CFTC")'s proposed guidance, "Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts," 88 Fed. Reg. 89410 (Dec. 27, 2023). We share the Biden Administration's worry that voluntary carbon credits are rife with fraud. But we write to express our concern that the CFTC is overstepping its statutory authority to confront a problem that simply isn't the CFTC's to address. While the proposal is couched in the very limited language of "guidance" to prevent "market manipulation," *id.* at 89410–11, its actual effects will be much broader. Indeed, the real goal appears to be setting politically expedient "quality" standards for voluntary carbon credits by applying pressure to derivative markets and disfavoring (or eliminating) "practices that are incompatible with the objective of achieving net zero GHG emissions by 2050." *Id.* at 89421. The CFTC lacks authority to do so, and its proposal should be withdrawn.

I. The Proposed Guidance Is Directed at Policing Carbon Credit "Quality," Not the Integrity of the Derivatives Markets.

The proposed guidance suggests it is only intended to "promote[] transparency and liquidity" in designated contract markets ("DCMs") for voluntary carbon credits, *id.* at 89410, but its true purpose seems to be an attempt to regulate the characteristics of the underlying credits themselves.

Under the Commodity Exchange Act ("CEA"), DCMs trading in "commodities" must comply with various "Core Principles" that set general requirements and standards for how they conduct business. 7 U.S.C. § 7(d). As relevant here, the proposed guidance explains that Core Principle 3 requires DCMs to "only list for trading derivative contracts that are not readily susceptible to manipulation." 88 Fed. Reg. at 89416. While the CEA does not define "manipulation," federal courts have explained that manipulation occurs when a party (1) "possessed an ability to influence market prices;" (2) "an artificial price existed;" (3) the party "caused the artificial prices;" and (4) the party "specifically intended to cause the artificial price." *In re Amaranth Nat. Gas Commodities Litig*., 730 F.3d 170, 173 (2d Cir. 2013) (quoting *Hershey v. Energy Transfer Partners*, *L.P.*, 610 F.3d 239, 247 (5th Cir. 2010)).

Notably, the proposed guidance suggests that, to ensure "transparency" and prevent "manipulation" involving voluntary carbon credits, DCMs must pay special attention to the "quality" of those credits. 88 Fed. Reg. at 89412–13. The point appears ultimately to be one of effectuating climate policy: "Liquid and transparent markets in high-integrity [voluntary carbon credits] may serve as a tool to facilitate emissions reduction efforts." *Id.* at 89412. The CFTC notes concern that "businesses or individuals may be utilizing low integrity [voluntary carbon credits] which do not accurately reflect the nature or level of [greenhouse gas ("GHG")] emission reductions or removals that are associated with the mitigation projects or activities for which the [voluntary carbon credits] have been issued." *Id.* at 89413.

To remedy this perceived problem, the proposed guidance suggests a grab bag of signs of a "high quality" voluntary carbon credit, including:

- "Additionality—The Underlying [Voluntary Carbon Credit] Represents GHG Emission Reductions or Removals That Would Not Have Been Developed and Implemented in the Absence of the Added Monetary Incentive Created by the Revenue from the Sale of Carbon Credits," *id.* at 89417;

- "Permanence and Accounting for the Risk of Reversal," *id.*; and

- "Robust Quantification—GHG Emission Reductions or Removals Should be Conservatively Quantified," *id.* at 89418.

The CFTC's attempt to define "high quality" voluntary carbon credits jumps the line between authority over DCMs and attempting to regulate the underlying credits. The proposed guidance justifies this decision because a characteristic like "[a]dditionality is viewed by many as a necessary element of a high quality [voluntary carbon credit]." *Id.* at 89417. As a result, the proposal reasons that "a crediting program's procedures for assessing or testing for additionality may constitute an economically significant attribute of the underlying [voluntary carbon credits], which should be described or defined in the terms and conditions of a [voluntary carbon credit] derivative contract." *Id.*

But the phrase "high quality" reflects a normative judgment about the credits that appeal to certain market participants, particularly those who complained that prices weren't high enough, and to the Biden Administration's climate policy preferences. It is not about "quality" to resist manipulation, but about whether it does the kinds of things the CFTC thinks should be done. Even if "[a]dditionality"—or any of the CFTC's other characteristic—is "a necessary element of a high quality [voluntary carbon credit]," "high quality" voluntary carbon credits aren't necessarily what companies are trying to buy or sell. The CFTC concedes this point, reasoning only that some undefined "many" companies value these characteristics and does not dispute that nonconforming credits are nonetheless voluntary carbon credits to which market participants prescribe value.

It is also unclear whether the guidance means that DCMs should "consider" whether to require the disclosure of these properties in a relevant contract's terms and conditions or "consider" whether to exclude altogether the voluntary carbon credits that lack these properties. If it is the latter, and that seems to be the intent, *see also* Part III, *infra*, then the proposed guidance stretches far beyond preventing the manipulation of market prices and straight into determining what goods will be available, or providing cover for DCMs to exclude futures contracts for disfavored voluntary carbon credits, in the name of conforming to the CFTC's preferred ideal and "[p]romot[ing] . . . [s]tandardization." 88 Fed. Reg. at 89413. It also runs headlong into the antitrust considerations in Core Principle 19, 17 C.F.R. § 38.1000.

An analogy here is helpful. While the CFTC could certainly regulate futures contracts for apples, it cannot say that the only apples for which there can be futures

contracts are Honeycrisps, or even that only Honeycrisps are "high quality" apples. So, too, with carbon credits.

The very nature of carbon credits makes the problem here more pernicious than the CFTC picking its favorite apple. Carbon credits are by their nature intangible and abstract. They represent a lack of something (GHGs) and are justified by an entity taking a course of action that theoretically results in less GHGs than the counterfactual. As one commentor at the CFTC's Second Voluntary Carbon Markets Convening noted, the CFTC is trying to liquidate "an abstract representation of achievements against a hypothetical counterfactual. That's hard." Transcript, CFTC, *Second Voluntary Carbon Markets Convening* 134–35 (July 19, 2023) (statement of Robin Rix, Chief Legal, Pol'y, & Mkt. Officer, Verra), https://perma.cc/YT2T-3WNM. This is a far cry from the "wheat, cotton, [and] rice" that are the core "commodities" the CFTC was created to supervise, 7 U.S.C. § 1a(9), which strongly indicates these waters aren't where the CFTC should wade. *See Biden v. Nebraska*, 143 S. Ct. 2355, 2382 (2023) (Barrett, J., concurring) ("Another telltale sign that an agency may have transgressed its statutory authority is when it regulates outside its wheelhouse."); *cf., e.g.*, *West Virginia v. EPA*, 597 U.S. 697, 729–30 (2022).

Such abstract commodities would have at least some real-world parameters and value if they were certified credits, created to comply with a government program like the SO_2 or NO_x allowances associated with the Acid Rain Program. But here the agency is dealing with futures contracts for *voluntary* carbon credits. In other words, the agency is setting standards for the future delivery of an abstract concept that is not a fungible commodity or required by any government program. As the CFTC is well aware, the class includes a wide variety of completely disparate types of voluntary carbon credits with different protocols and potential verification schemes that in no way resemble a uniform class of commodities.[1] Regulating as a body such

[1] The proposal does include related guidance for "third-party validation and verification" of voluntary carbon credits. 89 Fed. Reg. at 89419. Of course, DCMs are responsible for—and therefore must be able to justify—whatever standards or requirements those third parties impose. DCMs cannot use third parties to circumvent any laws, regulations, or obligations that would otherwise apply. *Cf. Students for Fair Admissions, Inc. v. President & Fellows of Harvard Coll.*, 600 U.S. 181, 230 (2023) (quoting *Cummings v. Missouri*, 71 U.S. (4 Wall.) 277, 325 (1867)); *Cal. Rest. Ass'n v. City of Berkeley*, 89 F.4th 1094, 1107 (9th Cir. 2024).

a broad and ill-defined class is unreasonable and heightens the appearance that the CFTC is doing this not to prevent "market manipulation," but because it wants to regulate the quality of the underlying credits themselves to achieve the Biden Administration's well-publicized climate goals.

And this is just the first step. Standardization is what centralized governmental authorities *always* want: to clean up the variegated and disparate forms of emergent order into something "legible" to the state, since only what can be measured and understood can be taxed and controlled. *See generally* James C. Scott, *Seeing Like a State* (1998).

II. Labeling the Proposal as Guidance Is Misleading.

Labeling the proposal as "guidance" is a misnomer that falls far short of capturing its real effect. CFTC regulations *require* DCMs to "[i]nclude, if requested by Commission staff, additional evidence, information or data demonstrating that the contract meets, initially or on a continuing basis, the requirements of the [CEA], or other requirement for designation or registration under the [CEA], or the Commission's regulations *or policies* thereunder." 17 C.F.R. § 40.3(a)(10) (emphasis added); *see also id.* § 40.2(b). Requiring entities to show how they conform to CFTC policy creates binding rules, not guidance. The message of the proposed guidance seems to be quite clear: trade only in voluntary carbon credits the agency deems acceptable or suffer the pains of CFTC inquiries and possible enforcement actions.

If the CFTC proceeds, it must clarify the effect of this proposed guidance, that it *at most* recommends transparency about certain voluntary carbon credit characteristics, but in no way imposes a standard or otherwise excludes non-conforming voluntary carbon credits, and that it cannot form the basis for further CFTC inquiries and action.

III. The Proposal Appears to Be Just Another Piece in the Biden Administration's Whole-Of-Government Approach to Net Zero.

The net-effect of the considerations discussed above indicates that the CFTC isn't trying to provide DCMs with helpful guidance to avoid market manipulation, but instead to create a new quasi-mandatory carbon market that every company with a net-zero pledge can be forced to participate in. Of course, many of these net-zero

pledges weren't really voluntary to begin with. Climate activists, blue states, and various arms of the Biden Administration have repeatedly pressured companies into adopting these pledges through pursuing, implementing, or otherwise enabling activist shareholder proposals,[2] contract requirements,[3] and so-called "climate-risk" disclosures.[4] And now with the pledges in place, the terms of compliance will change.

This has been the plan all along. Neither voters nor Congress has ever authorized an economy-wide carbon tax. So instead, for years, the ESG-industrial complex has labored to implement a *de facto* carbon tax entirely through the back door. Because the government will not require it, these groups have conspired to get big banks, hedge funds, and large international corporations to commit to reducing greenhouse gas emissions in exchange for the availability of funds or the ability to even engage in commerce with other parties. And now they want the government to bless and help regulate it.

This is precisely what participants advocated for at the Second Voluntary Carbon Markets Convening. It's no secret—and the CFTC acknowledges—that "supplies of [voluntary carbon credits] are generally considered to be high relative to demand." 88 Fed. Reg. at 89413. Several speakers thus complained that the price of voluntary carbon credits is too low and advocated for regulation in this space to (artificially) raise prices to provide financial support to their companies and to their preferred environmental projects. *See, e.g.,* Transcript, *Second Voluntary Carbon Markets Convening*, *supra*, at 47 (Statement of Kyle Harrison, Head of Sustainability Rsch., BloombergNEF) ("Because you have an oversupply, you have a surplus of cheaper credits and companies can go ahead and use those in many cases as a band-aid solution, as opposed to de-carbonizing and reducing their gross emissions."); *id.* at 49–50 ("[B]ecause of this huge range in the terms of sectors that are creating carbon credits, and because of the overall general oversupply that I mentioned before,

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[2] Division of Corporation Finance, SEC, Staff Legal Bull. No. 14L (Nov. 3, 2021), https://perma.cc/FUN8-2QTB; Consumers' Rsch., *Consumers' Research SEC No-Action Audit 2018–2022* (May 4, 2023), https://perma.cc/8CY6-BGK5.

[3] *See, e.g.*, *Federal Acquisition Regulation: Sustainable Procurement,* 88 Fed. Reg. 51,672 (Aug. 3, 2023).

[4] *See, e.g.*, *The Enhancement and Standardization of Climate-Related Disclosures for Investors*, 87 Fed. Reg. 21334 (Apr. 11, 2022).

there's a huge range in prices for carbon offsets and how they're exchanged. . . . But in general, they're all still far too cheap. . . . So there's a huge way to go in terms of price discovery, increasing prices in this market."). Others explained that companies shouldn't have access to carbon markets at all without surety that it is "really reducing emissions in a real way." *Id.* at 105 (statement of Dr. Nat Keohane, President, Ctr. for Climate & Energy Solutions). One speaker repeatedly explained that the goal of CFTC regulation should be to mimic or emulate a compliance market, which he, his organization, and the rest of the ESG-industrial complex would prefer (and profit from). *See id.* at 90, 263 (statements of Dirk Forrister, President & CEO, Int'l Emissions Trading Ass'n).

Buried at the end of the proposed guidance, the CFTC asks the quiet part out loud: When designing contract requirements, should DCMs consider whether voluntary carbon credits involve "practices that are incompatible with the objective of achieving net zero GHG emissions by 2050"? 88 Fed. Reg. at 89421. The answer is *no*. The CFTC has no authority to impose standards for voluntary carbon credits in pursuit of political goals, no matter how it frames the matter. Nor does the Biden Administration have the authority to try and implement what would effectively be an economy-wide carbon tax without authorization from Congress.

Repeated comments from CFTC Chairman Rostin Benham underscore the inappropriate objectives of the proposed guidance. He has been clear that the proposal "represents a whole-of-government approach in coordination with our partners across the federal complex" to pursue political ends regarding climate change. *Statement of Chairman Rostin Behnam on the Proposed Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts*, CFTC (Dec. 4, 2023), https://perma.cc/5U22-32LA. He also trumpeted the proposal at COP28 as "one of the most important developments for the carbon industry," providing guidance to "help channel capital in support of decarbonization efforts." *Keynote of Chairman Rostin Behnam at the ABA Business Law Section Derivatives & Futures Law Committee Winter Meeting*, CFTC (Jan. 26, 2024), https://perma.cc/PFD2-QQX7.

The proposed guidance is thus not about ensuring transparency for DCMs, but about achieving political goals the CFTC has no authority to regulate. The Chairman's claim that the proposal is "not intended to signal that [the CFTC] ha[s]

a role in creating or mandating compliance with any kind of climate policy" rings hollow considering these repeated assertions to the contrary. *Id.* If the CFTC has no role, it has no role.

As the federal courts have explained, "agencies, as mere creatures of statute, must point to explicit Congressional authority justifying their decisions." *Clean Water Action v. EPA*, 936 F.3d 308, 313 n.10 (5th Cir. 2019). "[A]n agency literally has no power to act . . . unless and until Congress confers power upon it." *La. Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374 (1986). And if an agency has no power to do something directly, it "cannot be done indirectly," either. *Students for Fair Admissions, Inc. v. President & Fellows of Harvard Coll.*, 600 U.S. 181, 230 (2023) (quoting *Cummings v. Missouri*, 71 U.S. (4 Wall.) 277, 325 (1867)); *see Cal. Rest. Ass'n v. City of Berkeley*, 89 F.4th 1094, 1107 (9th Cir. 2024) (similar). Congress conferred no power upon the CFTC to create or regulate voluntary carbon credits.

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For the reasons stated above, the CFTC should withdraw its proposed guidance.