New standards to ensure voluntary carbon credits' integrity and transparency

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10 January 2025

lakyara vol.393

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Executive Summary

Concerns about the integrity of voluntary carbon credits have led many companies to hesitate in their use, driven by fears of reputational risks. To address these challenges and restore confidence, new standards are being developed to ensure transparency and credibility in the market. As adherence to these improved standards gains traction among both suppliers and users, the adoption of voluntary carbon credits is expected to increase, fostering greater trust and supporting broader sustainability goals.

Doubts about voluntary carbon credits' integrity

Issuance and use of voluntary carbon credits[1] (VCCs) have slowed in recent years, with issuance trending downward since 2022 and retirement volume, a proxy for usage, flat-lining since 2020. VCC issuance previously had been growing robustly, driven largely by VCCs' flexibility advantage over mandatory credits. These shifts in VCC market trends likely reflect emergent doubts about whether VCCs are legitimately backed by commensurate reductions in atmospheric CO2[2], as illustrated by a class-action lawsuit filed against Delta Airlines in May 2023.

The lawsuit's plaintiffs are Delta customers who allege they were misled into patronizing Delta by its claim of being the world's first carbon-neutral airline. They disputed this claim on two grounds. The first is that Delta's purported carbon-neutrality relied mostly on carbon offsets instead of reductions in Delta's own emissions. The second is that VCCs purchased to offset CO2 emissions have been found to often overstate the actual decarbonization impact of the projects from which they originated.

In the wake of the lawsuit, Delta has faced criticism for being too dependent on carbon offsets to achieve its decarbonization goals. Use of VCCs has consequently come to be associated with lack of effort to reduce one's own emissions. Meanwhile, the emergence of questions about VCCs' integrity has caused a growing number of companies to shy away from using them, lest they incur negative publicity. One such company is Nestle, which has announced it will no longer use VCCs to achieve carbon neutrality. It plans to instead place priority on reducing emissions within its own value chain. Such avoidance of VCCs due to reputational concerns has become a headwind for the VCC market.

NOTE

1) There are two types of carbon credit markets: mandatory (a.k.a. compliance) and voluntary. The discussion herein is limited to the latter.

2) Projects that raise capital through VCCs are required to ensure their VCCs' integrity by accurately quantifying emissions reductions and meeting other requirements such as not releasing sequestered emissions back into the atmosphere.

The prevalence of low-integrity VCCs in circulation is unknown, but a paper published in the journal Science in 2023 estimated that a mere 6% of the VCCs expected to be generated by 26 forest conservation projects in Columbia, Peru, Tanzania, Democratic Republic of Congo, Zambia and Cambodia are likely to be backed by actual reductions in atmospheric CO2. This study is just one example. Distrust of VCCs has yet to be dispelled.

Survey of Japanese companies' VCC usage intentions

Against such a backdrop, we surveyed people in sustainability-related roles at Japanese companies to take the pulse of the Japanese VCC market. We found that many companies are placing priority on reducing greenhouse gas emissions within their respective value chains through their own efforts in pursuit of near-term targets but are open to using VCCs to achieve longer-term targets. Such companies apparently recognize they cannot attain carbon neutrality through their own efforts alone and will eventually need to utilize VCCs to neutralize their remaining emissions[3] after exhausting other means. Despite recognizing that VCCs will play an essential role in achieving carbon neutrality, many Japanese companies seem to be putting off using them out of reputational-risk concerns.

3) They would do so by purchasing and retiring VCCs in a quantity equivalent to their remaining emissions (i.e., emissions not practically reducible through their own efforts).

Standards rapidly emerging in VCC market

Given such widespread concerns about using VCCs both in Japan and overseas, it bears asking whether VCCs might become obsolete at some point in the future. The answer hinges on VCCs' role.

To efficiently accelerate reductions in greenhouse gas emissions globally, lots of capital must be raised through decarbonization activities in highly cost-efficient countries/regions[4]. In many cases, decarbonization activities yield ancillary benefits beyond decarbonization itself. For example, forestation of flood-prone areas may not only reduce atmospheric greenhouse-gas concentrations but also mitigate the risk of urban flooding and improve local residents' health. The VCC market has an important role to play in financing such co-benefits of decarbonization.

4) The per-ton cost of removing greenhouse gas from the atmosphere varies substantially among regions of the world.

To dispel concerns about using VCCs, concerned parties have been working on establishing international standards to ensure VCC transparency. On the supply side of the market, the Integrity Council for the Voluntary Carbon Market[5] (ICVCM) published Core Carbon Principles (CCPs) in March 2023. The ICVCM allows VCCs

5) The ICVCM was established as a standard-setting governance body in response to the final recommendations of the Taskforce on Scaling the Voluntary Carbon Markets, an initiative launched by former Bank of England Governor Mark Carney et al.

generated by decarbonization projects that comply with the CCPs to be labeled as “CCP-approved.” The CCP label attests that the VCC represents real and verifiable decarbonization impacts.

On the demand side, the international Voluntary Carbon Markets Integrity Initiative (VCMI) published a Claims Code of Practice in November 2023. The Code calls for companies to set a science-based emissions reduction target, demonstrate progress toward attainment of the target through their own efforts and, after having done so, use VCCs to neutralize remaining emissions (or emissions external to their own value chain). Users of high-quality VCCs in compliance with the Code are permitted to make VCMI Carbon Integrity Claims.

Promotion of VCC use

Bain & Company, a global management consultancy, made the inaugural VCMI Carbon Integrity Claim in February 2024. Bain has long provided sustainability-related consulting services. In the first six weeks after it made its VCMI Claim, its orders for such services doubled relative to the year-earlier period[6]. Bain seems to have benefited reputationally from its status as the first VCMI claimant.

6) Source: https://trellis.net/article/why-bain-going-beyond-net-zero/

In June 2024, Brazil’s Natura Cosmetics, which had participated in the VCMI Early Adopters Program together with Bain, made the second VCMI Carbon Integrity Claim. Several other companies also participated in the program, some if not all of which may make their own claims.

Use of VCCs to contribute to emissions reductions beyond the VCC user’s own value chain will hopefully become more common as more companies comply with international VCC standards.

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