was accompanied by a Presidential Memorandum titled “Modernizing United States Spectrum Policy and Establishing a National Spectrum Strategy,” which calls for the Secretary of Commerce, acting through NTIA, to publish an Implementation Plan for the Strategy. This will chart the course for federal agency actions, pursuant to the Presidential Memorandum, to further the policy objectives stated in the Strategy.

The strategic objectives in the Strategy are grouped under four “pillars” for further action:

- **Pillar One:** A spectrum pipeline to ensure U.S. leadership in advanced and emerging technologies;
- **Pillar Two:** Collaborative long-term planning to support the nation’s evolving spectrum needs;
- **Pillar Three:** Unprecedented spectrum innovation, access, and management through technology development; and
- **Pillar Four:** Expanded spectrum expertise and elevated national awareness.

Speakers from the Department of Commerce, the Executive Office of the President, the Federal Communications Commission and Congress have been invited to provide keynote remarks. Panelists are expected to include participants from the FCC, Executive Branch agencies, and the private sector. Prior to the symposium event, NTIA will post detailed program information on its website: www.ntia.gov.

The symposium is open to the public and members of the press to attend or to view through a webcast available on the NTIA website. While it is not required, NTIA asks that online attendee provide registration information prior to the event. This information will include names, email addresses, and organizations (optional). Registration information, the agenda, meeting updates, if any, and other relevant documents will be available on NTIA’s website.

The event webcast will be closed-captioned. Individuals requiring special accommodations, such as sign language interpretation or other ancillary aids, should notify Mr. Alden at the contact information listed above at least ten (10) business days before the event.

**Stephanie Weiner,**

Chief Counsel, National Telecommunications and Information Administration.

[FR Doc: 2023–28564 Filed 12–26–23; 8:45 am]

**BILLING CODE 3510–60–P**

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**COMMODITY FUTURES TRADING COMMISSION**

**RIN 3038–AF40**

**Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts; Request for Comment**

**AGENCY:** Commodity Futures Trading Commission

**ACTION:** Proposed guidance; request for comment.

**SUMMARY:** The Commodity Futures Trading Commission (the “Commission” or “CFTC”) is issuing for public comment this proposed guidance regarding the listing for trading of voluntary carbon credit (“VCC”) derivative contracts. Specifically, the Commission is proposing to issue guidance to outline factors that designated contract markets (“DCMs”) should consider when addressing certain provisions of the Commodity Exchange Act (“CEA”), and CFTC regulations thereunder, that are relevant to the listing for trading of VCC derivative contracts. The Commission recognizes that VCC derivatives are a comparatively new and evolving class of products, and believes that guidance that outlines factors for a DCM to consider in connection with product design and listing may help to advance the standardization of such products in a manner that promotes transparency and liquidity. The Commission requests comment on this proposed guidance and further invites comment on specific questions related to the listing for trading of VCC derivative contracts.

**DATES:** Comments must be received on or before February 16, 2024.

**ADDRESSES:** You may submit comments, identified by “Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts” and RIN 3038–AF40, by any of the following methods:

- **CFTC Comments Portal:** https://comments.cftc.gov. Select the “Submit Comments” link for this release and follow the instructions on the Public Comment Form.
- **Mail:** Send to Christopher Kirkpatrick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581.
- **Hand Delivery/Courier:** Follow the same instructions as for Mail, above.

Please submit your comments using only one of these methods. Submissions through the CFTC Comments Portal are encouraged.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to https://comments.cftc.gov. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that you believe is exempt from disclosure under the Freedom of Information Act (“FOIA”), a petition for confidential treatment of the exempt information may be submitted according to the procedures established in § 145.9 of the Commission’s regulations.1

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse, or remove any or all of your submission from https://www.comments.cftc.gov that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the guidance will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under FOIA.

**FOR FURTHER INFORMATION CONTACT:** Lillian A. Cardona, Assistant Chief Counsel, (202) 418–5012, lcardona@cftc.gov; Steven Benton, Industry Economist, (202) 418–5617, sbenton@cftc.gov; Nora Flood, Chief Counsel, (202) 418–6059, nflood@cftc.gov; Division of Market Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581.

**SUPPLEMENTARY INFORMATION:**

**I. Background**

**A. The Regulatory Framework for DCMs**

The CFTC’s mission is to promote the integrity, resilience, and vibrancy of the U.S. derivatives markets through sound regulation.2 An independent agency of the U.S. federal government, the CFTC exercises the authorities granted to it under the CEA to promote market integrity, prevent price manipulation and other market disruptions, protect customer funds, and avoid systemic risk, while fostering responsible innovation and fair competition in the derivatives markets.3

DCMs are CFTC-regulated exchanges that provide participants in the derivatives markets with the ability to execute or trade derivative contracts

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1 17 CFR 145.9.
3 See CEA section 3(b), 7 U.S.C. 5(b).
with one another. In order to obtain and maintain designation with the CFTC, DCMs must comply with statutory “Core Principles” that are set forth in the CEA, as well as applicable CFTC rules and regulations. The statutory Core Principles for DCMs reflect the important role that these exchanges play in promoting the integrity of derivatives markets. DCMs are self-regulatory organizations, and each DCM has Core Principle obligations to, among other things, establish and enforce rules for trading on the DCM to provide a competitive, open and efficient market for trading, and monitor trading activity. For example, DCM Core Principle 4 requires a DCM to have the capacity and responsibility to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement process, through market surveillance, compliance, and enforcement practices and procedures. DCM Core Principle 5 requires a DCM to adopt for each contract that it lists for trading, as is necessary and appropriate, position limitations or position accountability for speculators, in order to reduce the potential threat of market manipulation or congestion, especially during trading in the delivery month. DCM Core Principle 12 requires a DCM to establish and enforce rules to protect markets and market participants from abusive practices, and to promote fair and equitable trading on the DCM. Additionally, each DCM has a statutory obligation, under DCM Core Principle 3, to only list for trading contracts that are not readily susceptible to manipulation. As discussed in greater detail below, a DCM may generally elect to list a new derivative contract for trading either by certifying to the Commission that the contract complies with the CEA and CFTC regulations, or by seeking Commission approval of the contract. In either case, the DCM must submit the contract’s terms and conditions, and other prescribed information relating to the contract, to the Commission prior to listing. For a number of the statutory Core Principles for DCMs, the Commission has adopted rules that establish the manner in which a DCM must comply with the Core Principle. These implementing rules are set forth in Part 36 of the Commission’s regulations. The Commission has also adopted, in Appendix B to Part 38, guidance and acceptable practices for DCMs to take into consideration with respect to certain of the Core Principles.

With respect to the DCM Core Principle 3 requirement that a DCM only list for trading contracts that are not readily susceptible to manipulation, the Commission has adopted guidance that is set forth in Appendix C to Part 38 of the Commission’s regulations (the “Appendix C Guidance”). The Appendix C Guidance outlines certain relevant considerations for a DCM when developing derivative contract terms and conditions, and providing supporting documentation and data in connection with the submission of the derivative contract to the Commission. The Commission takes these considerations into account when determining whether, with respect to the contract, the DCM is satisfying its Core Principle obligation only to list contracts that are not readily susceptible to manipulation.

Among other things, the Appendix C Guidance outlines, for both physically-settled and cash-settled derivative contracts, certain considerations in connection with the design of the contract’s rules and terms and conditions. With respect to physically-settled derivative contracts, the Appendix C Guidance states, among other things, that the contract’s terms and conditions should conform to the reasonable common standards of market practice and conditions in the cash market for the underlying commodity. The Appendix detailed examples of how a DCM may satisfy particular requirements of a DCM Core Principle. Similar to guidance, acceptable practices are for illustrative purposes only, and do not establish a mandatory means of Core Principle compliance. 17 CFR part 38, Appendix B.

21 17 CFR part 38, Appendix C. Guidance set forth in Appendix B to Part 38 states that a DCM may use the Appendix C Guidance as guidance when meeting DCM Core Principle 3 for both new product listings and existing listed contracts. 17 CFR part 38, Appendix B, Core Principle 3 Guidance.

22 See Core Principles and Other Requirements for Designated Contract Markets, 77 FR 36612 at 36642 (June 19, 2012), The Appendix C Guidance is also relevant to swap execution facilities (“SEFs”), another category of CFTC-regulated exchange that provides eligible contract participants with the ability to execute or trade, with one another, derivative contracts that are swaps. Like DCMs, SEFs are obligated by statute only to permit trading in contracts that are not readily susceptible to manipulation. 17 CFR part 38, Appendix B.

23 Physically-settled derivative contracts are contracts that may settle directly into the commodity underlying the contract. If the holder of a position in a physically-settled derivative contract still has an open position at the expiration of trading in the contract, then the position holder must, in accordance with the rules for delivery set forth in the contract, make or take delivery (as applicable) of the underlying commodity. By contrast, cash-settled derivative contracts are, at the expiration of trading in the contract, settled by way of a cash payment instead of physical delivery of the underlying commodity.

24 Appendix C Guidance, paragraph (b)(1).
The Appendix C Guidance also states that the contract’s terms and conditions should be designed to avoid impediments to the delivery of the underlying commodity, so as to promote convergence between the price of the contract and the cash market value of the underlying commodity at the expiration of trading in the contract.25 The Appendix C Guidance outlines certain criteria that should be addressed in the contract’s terms and conditions, including contract size, the period for making and taking delivery under the contract, delivery points, quality standards for the underlying commodity, and inspection/certification procedures for verifying compliance with those quality standards or any other related delivery requirements under the contract.26

The criteria outlined in the Appendix C Guidance that relate to the quality and other attributes of the underlying commodity that would be delivered under a physically-settled contract upon the expiration of trading, inform the pricing of the contract. Addressing these criteria clearly in the contract’s terms and conditions, in a manner that reflects the individual characteristics of the underlying commodity, helps to ensure that trading in the contract is based on accurate information about the underlying commodity. This, in turn, helps to promote accurate pricing and helps to reduce the susceptibility of the contract to manipulation. Further, when a contract’s terms and conditions help to ensure that, upon delivery, the quality and other attributes of the underlying commodity will be as expected by position holders, this helps to prevent price distortions and fosters confidence in the contract that can incentivize trading and enhance liquidity.

With respect to cash-settled derivative contracts, the Appendix C Guidance states that an acceptable specification of the cash settlement price would, among other things, include rules that fully describe the essential economic characteristics of the underlying commodity, as well as how the final settlement price is calculated.27 The Appendix C Guidance states that the utility of a cash-settled contract for risk management and price discovery purposes would be significantly impaired if the cash settlement price is not a reliable or robust indicator of the value of the underlying commodity.28

The Appendix C Guidance states that, accordingly, careful consideration should be given to the potential for manipulation or distortion of the cash settlement price, as well as the reliability of that price as an indicator of cash market values.29 Appropriate consideration also should be given to the commercial acceptability, public availability, and timeliness of the price series that is used to calculate the cash settlement price.30

B. Voluntary Carbon Markets

1. Overview of Voluntary Carbon Markets

As discussed further below, this proposed guidance addresses an emerging class of climate-related derivative contracts listed for trading by DCMs, where the underlying commodity is a VCC.31 In addition to direct greenhouse gas (“GHG”) emissions reduction initiatives, market-based mechanisms, such as carbon markets,32 have developed to support emissions reduction efforts. A carbon market generally refers to an economic mechanism to support the buying and selling of environmental commodities that represent GHG emission reductions or removals from the atmosphere. Carbon markets are intended to incentivize carbon mitigation activities. Carbon markets generally fall into two categories: (i) mandatory (or compliance) markets, and (ii) voluntary carbon markets.

Mandatory markets, such as cap-and-trade programs, emissions trading systems and allowance trading systems, are established and regulated by national, regional, or international governmental bodies.34 Entities subject to the requirements of a mandatory market generally must demonstrate compliance by directly reducing their emissions from their own operations or activities, or by purchasing eligible compliance credits representing emission reductions or removals achieved by others. Voluntary carbon markets are not established by any government body. They enable market participants to purchase, on a voluntary basis, carbon credits that upon retirement represent reductions or removals of GHG emissions. A voluntary carbon credit, or “VCC,” is a tradable intangible instrument that is issued by a carbon crediting program (“crediting program”).35 The general industry standard is for a VCC to represent a GHG emissions reduction to, or removal from, the atmosphere equivalent to one metric ton of carbon dioxide.36

A participant in the voluntary carbon markets may purchase a VCC, representing an emissions reduction or removal by another party, to supplement emissions reductions or removals achieved from the participant’s own operations or activities. Liquid and transparent markets in high-integrity VCCs may serve as a tool to facilitate emissions reduction efforts.37

25 Id.
26 Id.
27 This proposed guidance uses the term “voluntary carbon credits,” as proposed by the International Swaps and Derivatives Association ("ISDA"), in the market participants’ physically-settled spot, forward or option transactions. See 2022 ISDA Verified Carbon Credit Transactions Definitions (“VCC Definitions”) Frequently Asked Questions, available at: https://www.isda.org/a/jbXgE/2022-IXDA-Verified-Carbon-Credit-Transactions-Definitions-FAQs-061323.pdf.
28 While the term “carbon” is generally intended to include other greenhouse gases, such as methane, nitrous oxide, sulfur hexafluoride, hydrofluorocarbons and perfluorocarbons, most emissions trading involves emissions trading of carbon dioxide.
29 An agreement, contract or transaction in an environmental commodity may qualify for the forward exclusion from the “swap” definition set forth in section 1a(47) of the CEA, 7 U.S.C. 1a(47), if the agreement, contract or transaction is intended to be physically settled. For further discussion of the Commission’s interpretation of whether agreements, contracts, or transactions in environmental commodities fall within the forward exclusion from the definition, see Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule, 77 FR 48208 (August 13, 2012).
30 Id.
34 This is calculated as the difference in GHG emission reductions or removals from a baseline scenario, to the emission reductions or removals occurring under the carbon mitigation project or activity, with any adjustments for leakage. See The Integrity Council for the Voluntary Carbon Market Core Principles, Section 5 Definitions, available at: https://icvcm.org/wp-content/uploads/2023/07/CPP-Section-5-R2-FINAL-26Jul23.pdf.
35 The Board of the International Organization of Securities Commissions (“IOSCO”) published a Voluntary Carbon Markets consultation for public comment. The IOSCO consultation paper sought feedback on a potential approach that regulatory authorities and market participants could take to foster sound and well-functioning voluntary carbon market structure and, as a consequence, scale up these markets to allow them to achieve their environmental objectives. Voluntary Carbon Markets, Discussion Paper, CR/06/22, November.
The process by which VCCs are issued deserves careful consideration, as that process informs VCC quality and, by extension, the overall integrity and effective functioning of voluntary carbon markets. Generally, parties that play a role in the issuance of a VCC include: (1) the developer of a mitigation project or activity that is intended to reduce or remove GHG emissions from the atmosphere (“project developer”); (2) a crediting program that, among other things, issues VCCs for mitigation projects or activities that satisfy the crediting program’s standards; and (3) an independent third party that verifies and validates the mitigation project or activity.

A project developer must first select the crediting program with which it seeks to certify its mitigation project or activity. The crediting program will certify the project or activity if it satisfies the crediting program’s standards for issuing VCCs. A crediting program generally engages an independent third party to review project or activity documentation, including, among other things, to verify the accuracy of the estimated amount of emission reductions or removals that are expected to be associated with the project or activity, based on the project’s or activity’s baseline scenario and the crediting program’s methodology or protocol for quantifying reduction or removal levels. The estimated emission reductions or removals serve as the basis for the determination of the number of VCCs to be issued for the project or activity.

Once the crediting program determines that the mitigation project or activity satisfies the crediting program’s standards for issuing VCCs, the project or activity will be certified. The crediting program typically operates or makes use of a registry, which serves as a central repository for tracking certified emission reductions or removals. Some registries are purpose-built for the crediting program, while others are general purpose (e.g., the Gold Standard, the Verified Carbon Standard). A central repository for tracking certified emission reductions or removals that are associated with the mitigation projects or activities for which the VCCs have been issued can erode confidence in voluntary carbon markets. Furthermore, opaque or inadequate calculation methodologies or protocols, which can obscure or mischaracterize the carbon impact of a mitigation project or activity, can undermine both the integrity and purpose of those markets.

On the demand side, concerns have been raised that, in connection with meeting their carbon mitigation goals, businesses or individuals may be utilizing low integrity VCCs which do not accurately reflect the nature or level of GHG emission reductions or removals that are associated with the mitigation projects or activities for which the VCCs have been issued. This can raise questions not only about the business’s or individual’s progress towards their goals, but also about whether any claims related to those goals are misleading.

Market participants that are purchasing VCCs to help meet their mitigation goals may be focused largely or primarily on price, and also may not have ready access to all of the information that they need to make informed evaluations, and comparisons, of VCC quality. All of this may incentivize, intentionally or not, the purchase of lower quality VCCs. This may be facilitated by the opaque pricing of VCCs, as described above—and by the fact that, recently, supplies of VCCs are generally considered to be high relative to demand.

The voluntary carbon markets have continued to develop and mature, private sector and multilateral initiatives have sought to address certain issues—relevant to both the supply side (generation of VCCs from carbon mitigation projects or activities), and the demand side (businesses or individuals purchasing VCCs)—impacting the speed at which transparent, robustly traded markets for high-integrity VCCs are scaled.

2. Initiatives To Promote Transparency, Integrity and Standardization in the Voluntary Carbon Markets

As the voluntary carbon markets have continued to develop and mature, private sector and multilateral initiatives have sought to address certain issues—relevant to both the supply side (generation of VCCs from carbon mitigation projects or activities), and the demand side (businesses or individuals purchasing VCCs)—impacting the speed at which transparent, robustly traded markets for high-integrity VCCs are scaled. On the supply side, a key focus has been on the quality of VCCs, particularly, whether they accurately reflect the nature and level of GHG emission reductions or removals that they are intended to represent. Given the current absence of a standardized methodology or protocol to quantify emissions reductions or removal levels, there is a possibility that methodologies or protocols of differing degrees of robustness may calculate different reduction or removal impacts for two projects that are identical in type and size (or even for the same project). This could result in different amounts of carbon credits being issued for each project, despite their actual reduction or removal impact being the same. It may also create incentives for project developers to seek to apply the quantification protocol or methodology, or to seek to certify with the crediting program, that would result in the issuance of the most credits. Among other things, these possibilities create challenges for accurately pricing VCCs. Further, it can be difficult to discern the extent to which the price of any particular VCC reflects the price of one metric ton of carbon dioxide equivalent reduced or removed from the atmosphere, and the extent to which the price reflects understandings or concerns relating to the mitigation project or activity for which the VCC was issued, or other aspects of the process for issuing the VCC.

Early investors may enter into agreements with a project developer for funding in exchange for discounted VCCs, once issued. Factors that may affect the price of VCCs issued for any particular mitigation project or activity may include the type of the project or activity, the geographic location of the project or activity, and the methodology or protocol used to measure the levels of emissions reductions or removals associated with the project or activity. Types of carbon mitigation projects or activities for which VCCs are issued include renewable energy, industrial gas capture, forestry initiatives (avoiding deforestation), regenerative agriculture, wind power, and biogas. The location of a mitigation project or activity may, for example, impact the cost of implementing and/or operating the project or activity. Mitigation projects and activities for which VCCs are issued are located in countries worldwide. Some exchanges for trading VCCs have been established and are evolving. For example, the AirCarbon Exchange (https://acx.com/), located in Singapore; Carbon Trade Exchange (https://ctxglobal.com/), located in the United Kingdom; and Xpansiv CBL (https://xpansiv.com/cbl/), located in the United States. For example, see, e.g., Forbes, Carbon Neutral Claims under Investigation In Greenwashing Probe (June 16, 2023), available at: https://www.forbes.com/sites/amynnguyen/2023/06/16/carbon-neutral-claims-under-investigation-in-greenwashing-probe/?sh=2a6170466431.

33 Currently, the four largest crediting programs in the voluntary carbon markets are the American Carbon Registry, the Climate Action Reserve, the Gold Standard and the Verified Carbon Standard.
34 A baseline scenario is the predicted or assumed outcome in the absence of the incentives created by carbon markets. Generally, a high baseline scenario serves as a benchmark against which to compare the outcomes of a mitigation project or activity could begin as early as the planning stage.
40 Funding by investors for a mitigation project or activity could begin as early as the planning stage.
Private sector and multilateral efforts have spearheaded the development of various initiatives to address the above challenges, and to promote transparency, integrity and standardization in the voluntary carbon markets. To support and promote VCC quality, these private sector and multilateral initiatives have focused on developing standards for high-integrity VCCs. Among other things, these standards are intended to help provide assurance that the VCCs that have been issued for a carbon mitigation project or activity accurately reflect the actual GHG emissions reduction or removal levels associated with that project or activity. These standards also generally highlight the importance of effective crediting program processes, procedures, and governance arrangements, in ensuring that a crediting program is issuing high integrity VCCs.

Standards that assist market participants in making informed evaluations, and comparisons, of VCC quality may promote accurate pricing and encourage confidence that the voluntary carbon markets can serve as a tool to assist in emissions reduction efforts. Such standards can thereby play a valuable role in supporting market transparency and liquidity, and the scaling of high-integrity voluntary carbon markets.

Such standards may also support initiatives being developed to address concerns about the accuracy of claims made by purchasers of VCCs regarding the role that VCCs play in the purchasers’ progress toward carbon mitigation goals. Such standards could serve as a foundation or reference for criteria that purchasers of VCCs could voluntarily adhere to, in order to demonstrate their commitment to using high integrity VCCs to support their mitigation goals, and to being transparent in their progress towards those goals.

C. The Commission and Voluntary Carbon Markets

1. Derivative Contracts on Environmental Commodities, Including VCCs

Derivative contracts on environmental commodities have been trading on CFTC-regulated exchanges for decades. Derivative contracts on mandatory emissions program instruments have been trading since 2005, with GHG emissions-related instruments first listed in 2007. There are currently over 150 derivative contracts on mandatory emissions program instruments listed on DCMs. As of November 2023, eighteen future contracts on voluntary carbon market products have been submitted by DCMs to the Commission for listing. Three of those contracts currently have open interest.

Derivative contracts on VCCs base their prices on the spot price of VCCs. For example, NYMEX’s CBL Global Environmental Offset futures contracts, and Nodal Exchange’s Verified Emission Reduction futures and options contracts, are physically-settled contracts. If the holder of a position in the contract still has an open position at the expiration of trading in the contract, then the position holder must, in accordance with the rules for delivery set forth in the contract, make or take delivery (as applicable) of 1,000 VCCs that meet the contract’s rules for delivery eligibility.

2. Initiatives Relating to Voluntary Carbon Markets

First Voluntary Carbon Markets Convening

In June 2022, Chairman Behnam held the first-ever Voluntary Carbon Markets Convening to discuss issues related to the supply of and demand for high quality carbon credits, including product standardization and the data necessary to support the integrity of carbon credits’ GHG emissions removal and reduction claims. A further goal of this convening was to gather information from a wide variety of 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.”

46 The Chicago Climate Futures Exchange ("CCFE") listed its Vintage Financial Instruments Current Vintage Delivery futures contract in 2005. In 2006, the New York Mercantile Exchange ("NYMEX") listed a nitrogen oxide ("NOx") Emissions Allowance futures contract. In 2007, CCFE listed the first Carbon Financial Instrument futures contract and other emission contracts. In 2008, NYMEX listed the first RGGI futures contract. In 2011, Green Exchange listed its European Union Allowance futures contract. In 2012, NYMEX listed its California Carbon Allowance futures contract. To date, there have been over 1,500 mandatory emissions-relationship futures contracts listed for trading on various DCMs. The vast majority of those contracts are no longer listed for trading.


48 For example, NYMEX lists the following physically-settled futures contracts based on voluntary carbon market products: (1) CBL Global Emissions Offset (GEO) futures contract; (2) CBL Nature-Based Global Emissions Offset (N-GEO) futures contract; (3) CBL Core Global Emissions Offset (C-GEO) futures contract; (4) CBL Nature-Based Global Emissions Offset Trailing futures contract; (5) CBL Core Global Emissions Offset Trailing futures contract; (6) NYMEX’s CBL Nature-Based Global Emissions Offset (N-GEO) futures contract; (7) NYMEX’s CBL Core Global Emissions Offset (C-GEO) futures contract; and (8) NYMEX’s CBL Core Global Emissions Offset (N-GEO) futures contract. These contracts are currently the only listed futures contracts with open interest and trading volume. Information is available at: https://www.cmegroup.com/markets/energy/emissions/cbl-global-emissions-offset.volume.html.

49 The CME Group CBL contracts permit VCCs to be delivered from the Verified Carbon Standard (“VCS”) Verra Registry, the American Carbon Registry (“ACR”), and the Climate Action Reserve (“CAR”). The Nodal contracts permit VCCs to be delivered from VCS’s Verra Registry and from the Gold Standard Impact Registry, as well as from the American Carbon Registry for certain contracts.

50 For the official announcement of the convening and related materials, see https://www.cftc.gov/PressRoom/Events/opaevent/cccarbonmarketconvene06222.
market participants in the voluntary carbon markets to better understand the potential role of the official sector in these markets, particularly in connection with the emergence of CFTC-regulated derivatives referencing VCCs.55 The convening included participants from carbon credit standard setting bodies, a credit rating program, private sector integrity initiatives, spot platforms, DCMs, intermediaries, end-users, public interest groups, and others.

Commission Request for Information

In June 2022, the Commission issued for public comment a Request for Information ("RFI")44 in order to better inform the Commission on how, consistent with its statutory authority, to address climate-related financial risk as pertinent to the derivatives markets and underlying commodities markets.55 The responsive comments that the Commission received included feedback on specific questions relating to product innovation and voluntary carbon markets.56 Several commenters expressed support for the Commission to take steps that could support transparency and confidence in the voluntary carbon markets, particularly through recognition or support of private sector and multilateral initiatives to promote standardization and integrity.57 In connection with product innovation, certain commenters expressed the view that the Commission’s current statutory framework and regulations are sufficient to regulate voluntary carbon market derivatives products.58 While there were comments expressing different views on the reach of the Commissions’ jurisdiction to regulate voluntary carbon markets,59 many commenters supported the Commission utilizing its spot market anti-fraud and anti-manipulation authority in the voluntary carbon market space.60

Second Voluntary Carbon Markets Convening

In July 2023, Chairman Behnam held the Second Voluntary Carbon Markets Convening. The purpose of this convening was to discuss recent private sector initiatives for high quality carbon credits; current trends and developments in the cash and derivatives markets for carbon credits; public sector initiatives related to carbon markets; and market participants’ perspectives on how the CFTC can promote integrity for high quality carbon credit derivatives.61

II. Guidance Regarding the Listing of VCC Derivative Contracts

The Commission is proposing guidance that outlines factors that DCMs should consider when addressing certain requirements under the CEA and CFTC regulations that are relevant to the listing of trading of VCC derivative contracts. The Commission recognizes that VCC derivatives are a comparatively new and evolving class of products,62 and believes that guidance that outlines factors for a DCM to consider in connection with product design and listing may help to advance the standardization of such products in a manner that promotes transparency and liquidity.

This proposed guidance addresses certain Core Principle compliance considerations, as well as certain requirements relating to the submission of new contracts, and contract amendments, to the Commission. This proposed guidance is not intended to modify or supersede existing statutory or regulatory requirements, or existing Commission guidance that addresses the listing of derivative products by CFTC-regulated exchanges, including the Appendix C Guidance. Rather, taking into account certain unique attributes of VCC derivatives and voluntary carbon markets, this proposed guidance outlines particular matters that a DCM should consider, to help ensure compliance with existing requirements when listing a VCC derivative contract. Among other things, this proposed guidance addresses how certain aspects of the Appendix C Guidance should be understood to apply in the specific context of VCC derivative contracts.

This proposed guidance focuses primarily on the listing by DCMs of physically-settled VCC derivative contracts. In part, this focus reflects the fact that all VCC derivative contracts that are currently listed for trading on DCMs are physically-settled contracts. To date, no DCM has listed for trading a cash-settled VCC derivative contract. In addition, the Commission believes that at this juncture in the evolution of VCC derivatives as a product class, it may be of particular benefit to outline considerations for a DCM, when developing contract terms and conditions, that can help to ensure that, upon delivery, the quality and other attributes of the underlying VCC will be as expected by position holders. This will support accurate pricing, help reduce the susceptibility of the contract to manipulation, and foster confidence in the contract that can enhance liquidity.

While this proposed guidance focuses primarily on physically-settled VCC derivative contracts, the Commission continues to believe that, with respect to cash-settled derivative contracts, an acceptable specification of the cash...
settlement price would include rules that fully describe the essential economic characteristics of the underlying commodity. Accordingly, the Commission preliminarily believes that discussions in this proposed guidance of VCC commodity characteristics that a DCM should consider when developing the terms and conditions of a physically-settled VCC derivative contract, should also be considered for cash-settled derivative contracts that settle to the price of a VCC, unless otherwise noted.

Further, while this proposed guidance focuses on the listing of VCC derivative contracts by DCMs, the Commission preliminarily believes that the proposed guidance also should be considered by any SEF that may seek to permit trading in swap contracts that settle to the price of a VCC, or in physically-settled VCC swap contracts.

In developing this proposed guidance, the Commission has considered those public comments on the RFI that addressed product innovation and voluntary carbon markets. Taking into account those public comments, the Commission believes that this proposed guidance furthers the agency’s mission and may help to advance the standardization of VCC derivative contracts in a manner that fosters transparency and liquidity, accurate pricing, and market integrity.

The Commission recognizes that VCCs and voluntary carbon markets are evolving and that it may therefore be appropriate for the Commission to revisit this guidance or to issue additional guidance in the future, as VCCs and voluntary carbon markets continue to develop and mature.

A. A DCM Shall Only List Derivative Contracts That Are Not Readily Susceptible to Manipulation

As discussed above, DCM Core Principle 3 provides that a DCM shall only list for trading derivative contracts that are not readily susceptible to manipulation. With respect to DCM Core Principle 3, the Appendix C Guidance outlines certain relevant considerations for a DCM when developing contract terms and conditions and providing supporting documentation and data in connection with the submission of a contract to the Commission.

With respect to a physically-settled derivative contract, the Appendix C Guidance states that the terms and conditions of the contract “should describe or define all of the economically significant characteristics or attributes of the commodity underlying the contract.” Among other things, failure to specify the economically significant attributes of the underlying commodity may cause confusion among market participants, who may expect a commodity of different quality, or with other features, to underlie the contract. This may render the precise nature of the commodity that the contract is pricing ambiguous, and make the contract susceptible to manipulation or price distortion.

The Appendix C Guidance states that, for any particular contract, the specific attributes of the underlying commodity that should be described or defined in the contract’s terms and conditions “depend upon the individual characteristics of the commodity.” Where the underlying commodity is a VCC, the Commission recognizes that standardization and accountability mechanisms for VCCs are currently still developing. The Commission believes that the fact that standardization and accountability mechanisms for VCCs are currently still developing is, itself, an “individual characteristic of the commodity” that should be taken into account by a DCM when designing a VCC derivative contract and addressing the underlying commodity in the contract’s terms and conditions.

To that end, the Commission recognizes that, while standardization and accountability mechanisms for VCCs are currently still being developed, there are certain characteristics that have been identified broadly—across both mandatory and voluntary carbon markets—as helping to inform the integrity of carbon credits. The Commission preliminarily believes that a DCM should take these characteristics—referred to in this proposed guidance as “VCC commodity characteristics,” and discussed more fully below—into consideration when designing a VCC derivative contract, and addressing in the contract’s terms and conditions the underlying VCC. The Commission believes that consideration of these VCC commodity characteristics will help the DCM to ensure that it understands, and is clearly specifying in the contract’s terms and conditions, the economically significant attributes of the underlying VCC.

As a general matter, the Commission believes that a DCM should consider the VCC commodity characteristics when selecting one or more credit programs from which eligible VCCs, meeting the derivative contract’s specifications, may be delivered at the contract’s expiration. The Commission believes that this will help the DCM evaluate whether the crediting program is a reliable source of high integrity VCCs.

Specifically, the Commission preliminarily believes that, at a minimum, a DCM should consider the VCC commodity characteristics when addressing the following criteria in the design of a VCC derivative contract:

- Quality standards,
- Delivery points and facilities, and
- Inspection provisions.

These are among the criteria identified in the Appendix C Guidance as criteria that should be addressed in the terms and conditions of a physically-delivered derivative contract.

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63 Appendix C Guidance, paragraph (c)(1). 64 As noted herein, and for the avoidance of doubt, product innovation guidance is not intended to modify or supersede the Appendix C Guidance, which outlines considerations for both cash-settled and physically-settled derivative contracts—including contracts that are not touched on in this proposed guidance. DCMs are reminded to consult and consider the Appendix C Guidance when developing terms and conditions, and contract submissions to the Commission, for all derivative product types—including VCC derivative products.

65 As noted above, the Appendix C Guidance is also relevant to SEFs, which, like DCMs, are obligated by statute only to permit trading in contracts that are not readily susceptible to manipulation, CEA section 5h(f)(4), 7 U.S.C.7b–3(f)(4). Like DCMs, SEFs also are subject to a statutory obligation to monitor trading in swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement process through surveillance, compliance, and disciplinary practices and procedures. CEA section 5h(f)(4) 7 U.S.C.7b–3(f)(4). See also 17 CFR 37.400–408.

66 See also, e.g., International Emissions Trading Association (supporting comments in response to the Second Voluntary Carbon Markets Convening at 5–6 (stating that the CFTC is in a fortunate position to leverage the evolving work of existing initiatives to support the drive for quality and integrity in the voluntary carbon markets), and BP America, Inc. (supporting guidance for CFTC regulated exchanges.)

67 As noted above, the Appendix C Guidance is also relevant to SEFs, which are similarly obligated by statute only to permit trading in contracts that are not readily susceptible to manipulation. CEA section 5h(f)(4); 7 U.S.C.7b–3(f)(4).

68 Appendix C Guidance, paragraph (b)(2)(i)(A).

69 Appendix C Guidance, paragraph (b)(2)(i)(A).

70 Appendix C Guidance, paragraph (b)(2)(i)(A).

71 Appendix C Guidance, paragraph (b)(2)(i)(A).

72 Id.
As discussed above, addressing these criteria clearly in the contract’s terms and conditions helps to ensure that trading in the contract is based on accurate information about the quality of the VCC underlying the contract. This, in turn, helps to promote accurate pricing and helps to reduce the susceptibility of the contract to manipulation.

1. Quality Standards

The Commission preliminarily believes that a DCM should consider the following VCC commodity characteristics when addressing quality standards in the development of the terms and conditions of a VCC derivative contract: (i) transparency, (ii) additionality, (iii) permanence and risk of reversal, and (iv) robust quantification.73

a. Transparency—Publicly Available Data to Promote Transparency

As a threshold matter, the Commission believes that a DCM should provide, in the terms and conditions of a VCC derivative contract, information about the VCCs that are eligible for delivery under the contract. The contract terms and conditions should include information that readily specifies the crediting program or program—and, as applicable, the specific types of projects or activities—from which VCCs that are eligible for delivery under the contract may be issued. Specifying which crediting programs, and as applicable, which types of projects or activities, are eligible for purposes of delivery will help to provide clarity to market participants regarding the VCCs that can be expected to deliver under the contract, and will thereby help to ensure that the pricing of the contract accurately reflects the intended quality of the underlying VCCs. Where there is ambiguity or confusion about the quality of the VCCs that may be delivered under the contract, this may render the contract susceptible to manipulation or price distortion. The Commission preliminarily believes that developing the terms and conditions of a VCC derivative contract, DCMs should also consider whether the crediting program for the underlying VCCs is making detailed information about the crediting program’s policies and procedures and the projects or activities that it credits, such as relevant project documentation, publicly available in a searchable and comparable manner. Making such information publicly available would assist market participants in understanding how GHG emission reductions or removals are calculated by the crediting program—including how additionality, which is discussed further below, is assessed—and how GHG emission reductions or removals are quantified. This would assist market participants in making informed evaluations, and comparisons, of the quality of the VCCs that underlie derivative contracts, which would help to support accurate pricing.

Accordingly, information regarding the crediting program’s policies and procedures for making program information publicly available may constitute an economically significant attribute of the underlying VCC that should be described or defined in the terms and conditions of the VCC derivative contract.

b. Additionality—The Underlying VCC 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

The Commission preliminarily believes that, in developing the terms and conditions of a VCC derivative contract, a DCM should consider whether the underlying VCCs represent GHG emission reductions or removals that are “additional”—in other words, whether the VCCs are credited only for projects or activities that result in 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.74 Additionality is viewed by many as a necessary element of a high quality VCC; if a VCC does not represent emission reductions or removals that would not have occurred in the absence of the added monetary incentive created by the revenue from the sale of carbon credits, then the VCC will not serve a market participant’s goals of contributing to emissions mitigation.

Accordingly, as part of its contract design market research, a DCM should consider whether a crediting program can demonstrate that it has procedures in place to assess or test for additionality. A DCM should consider whether those procedures are sufficiently rigorous and reliable to provide a reasonable assurance that GHG emission reductions or removals are credited only if they are additional. If holders of positions in a VCC derivative contract understand and intend for VCCs that are eligible for delivery under the contract to be additional, but in fact they may not be, then the pricing of the contract may not accurately reflect the quality of the VCCs that may be delivered under the contract: the cheapest-to-deliver VCC,75 that otherwise meets the contract’s specifications, may not have additionality.

Given that additionality is viewed by many as a necessary element of a high quality VCC, information regarding a crediting program’s procedures for assessing or testing for additionality may constitute an economically significant attribute of the underlying VCCs, which should be described or defined in the terms and conditions of a VCC derivative contract.

c. Permanence and Accounting for the Risk of Reversal

The Commission preliminarily believes that, in developing the terms and conditions of a VCC derivative contract, a DCM should consider whether the crediting program for the underlying VCCs can demonstrate that it has measures in place to address and account for the risk of reversal (i.e., the risk that VCCs issued for a project or activity may have to be recalled or cancelled due to carbon removed by the project or activity being released back into the atmosphere, or due to a revaluation of the amount of carbon reduced or removed from the atmosphere by the project or activity). Understanding and evaluating the measures that a crediting program has in place to address and account for the risk of reversal may be particularly important where the underlying VCCs are issued for project or activity types with a higher reversal risk.

The risk of reversal may impact the risk management needs of VCC derivative market participants. Market participants that are utilizing physically-settled VCC derivative contracts to help meet their carbon mitigation goals have an interest in ensuring that, upon physical settlement, the underlying VCCs will actually reduce or remove the amount of emissions that they were intended to reduce.

73 As is the case for physically-settled VCC derivative contracts, for cash-settled derivative contracts that settle to the price of a VCC, it is important to clearly specify the VCC quality standards in the contract’s terms and conditions to help ensure that the pricing of the contract reflects the quality of the VCC underlying the contract.
74 For example, a project or activity may not be considered to be “additional” if the project or activity is already required by law, regulation, or any other legally binding mandate applicable in the project’s or activity’s jurisdiction.
75 The term “cheapest-to-deliver” refers to the least expensive commodity that can be delivered under the derivative contract that otherwise meets the contract’s specifications.
reduce or remove. Accordingly, the risk of reversal—and the manner in which it is accounted for by a crediting program—is tied to the quality of the underlying VCCs and, by extension, to the pricing of the derivative contract. As a result, information regarding a crediting program’s measures for estimating, monitoring, and addressing the risk of reversal may constitute an economically significant attribute of the underlying VCCs that should be described or defined in the terms and conditions of a VCC derivative contract.

As part of its contract design market research, the Commission preliminarily believes that a DCM should consider whether the crediting program for a VCC has measures in place that provide reasonable assurance that, in the event of a reversal, the VCC will be replaced by a VCC of comparably high quality that meets the contemplated specifications of the contract. Most crediting programs have established VCC “buffer reserves” to address the risk of credited GHG emission reductions or removals being reversed. Under this approach, VCCs are set aside into a common buffer reserve (or “pool”). Reserved VCCs can be drawn upon to compensate for reversals associated with a project or activity. If a reversal occurs, VCCs are drawn upon from the buffer reserve to replace VCCs that are canceled, proportional to the size of the reversal.

A DCM should consider whether a crediting program has a buffer reserve or other measures in place that provide reasonable assurance that, in the event of a reversal, the VCCs intended to underlie the derivative contract would be replaced by VCCs of comparable high quality that meets the contemplated specifications of the contract. The DCM could also consider whether the crediting program regularly reviews the methodology by which the size of its buffer pool is calculated in order to address evolving climate risks that may heighten the risk of reversal, and whether there is a mechanism in place to audit the continuing sufficiency of the buffer pool.

d. Robust Quantification—GHG Emission Reductions or Removals Should be Conservatively Quantified

The Commission preliminarily believes that, as part of its contract design market research, a DCM should consider the methodology or protocol used by a crediting program to calculate the level of GHG emission reductions or removals associated with credited projects or activities. Given the current absence of a standardized methodology or protocol to quantify GHG emission reductions or removal levels—only not across crediting programs, but even by a particular crediting program, with respect to different types of projects or activities—the Commission believes that a DCM that lists a VCC derivative contract should consider whether the crediting program for the underlying VCCs can demonstrate that the quantification methodology or protocol that it uses to calculate emission reductions or removals for the underlying VCCs is robust, conservative, and transparent. A robust, conservative, and transparent quantification methodology or protocol helps to ensure that the number of VCCs that are issued for a project or activity accurately reflects the level of GHG emission reductions or removals associated with the underlying VCCs. For the derivative contracts that they list, DCMs are required to adopt, as necessary and appropriate, exchange-set position limits for speculators. To establish exchange-set position limits, a DCM should derive a quantitative estimate of the deliverable supplies of the underlying commodity for the delivery period specified in the contract. A DCM’s estimate of a VCC’s deliverable supplies is likely to be informed by understanding how the relevant crediting program determines the amount of VCCs that are issued for credited projects or activities. Where the quantification methodology or protocol used to calculate the amount of VCCs is robust, conservative, and transparent, the DCM should have a more reliable basis from which to form its deliverable supply estimate. That deliverable supply estimate, in turn, can be used as the basis for effectively setting the DCM’s exchange-set speculative position limits to help reduce the possibility of corners or squeezes that may distort or manipulate the price of the derivative contract.

2. Delivery Points and Facilities

The Appendix C Guidance states that the delivery procedures for a physically-settled derivative contract should, among other things, seek to minimize or eliminate any impediments to making or taking delivery by both deliverers and takers of delivery, to help ensure convergence of cash and derivative contract prices at the expiration of the derivative contract. When addressing delivery procedures for a physically-settled VCC derivative contract, the Commission preliminarily believes that a DCM should consider the governance framework and tracking methodologies of the crediting program for the underlying VCCs, as well as the crediting program’s measures to prevent double-counting.

a. Governance

The Commission preliminarily believes that a DCM should consider whether a crediting program for the underlying VCCs can demonstrate that it has a governance framework that effectively supports the crediting program’s independence, transparency, and accountability. As a threshold matter, a governance framework that effectively supports transparency and accountability helps to ensure the overall quality of the VCCs issued by a crediting program. Furthermore, it is the Commission’s understanding that a governance framework that effectively supports transparency and accountability helps to ensure that the crediting program operates or makes use of a registry that has appropriate measures in place to...
facilitate the physical settlement of a VCC derivative contract.

In reviewing a crediting program’s governance framework, the Commission preliminarily believes that a DCM should consider, among other things, the program’s decision-making procedures, including who is responsible for administration of the program and how the independence of key functions is ensured; reporting and disclosure procedures; public and stakeholder engagement processes; and risk management policies, such as financial resources/reserves, cybersecurity, and anti-money laundering policies. The DCM also should consider whether information regarding these procedures and policies is made publicly available.

Given the importance of a crediting program’s governance framework in ensuring the overall quality of the VCCs issued by the program, as well as the potential importance of a crediting program’s registry in facilitating delivery, it may be appropriate for the DCM to include information about the crediting program’s governance framework in the terms and conditions of a physically-settled VCC derivative contract.

b. Tracking

The Commission preliminarily believes that a DCM should consider whether the crediting program for the underlying VCCs can demonstrate that it has processes and procedures in place to help ensure clarity and certainty with respect to the issuance, transfer, and retirement of VCCs. The DCM should consider whether the crediting program operates or makes use of a registry that has measures in place to effectively track the issuance, transfer, and retirement of VCCs; to identify who owns or retires a VCC; and to make sure that each VCC is uniquely and securely identified and associated with a single emission reduction or removal of one metric ton of carbon dioxide equivalent. In circumstances where the registry will serve as the delivery point for a physically-settled VCC derivative contract, it may be appropriate for the DCM to include as a condition of the contract that the registry have such measures to address tracking in place, as well as effective measures to address double-counting, as discussed below.

c. No Double Counting

The Commission preliminarily believes that a DCM should consider whether the crediting program for the underlying VCCs can demonstrate that it has effective measures in place that provide reasonable assurance that credited emission reductions or removals are not double counted. That is, that the VCCs representing the credited emission reductions or removals are issued to only one registry and cannot be used after retirement or cancelation. As discussed above in connection with the VCC commodity characteristics of additionality and permanence, market participants that are utilizing physically-settled VCC derivative contracts to help meet carbon mitigation goals have an interest in ensuring that, upon physical settlement, the underlying VCCs will actually reduce or remove the emissions that they were intended to reduce or remove. In order for VCCs to effectively further carbon mitigation goals, it is important for each credited VCC to be uniquely associated with a single emission reduction or removal of one metric ton of carbon dioxide equivalent—and a crediting program should have effective measures in place that provide reasonable assurance of this. If there is not a reasonable assurance that the VCCs underlying a derivative contract are each unique, then, among other things, this could distort or obscure the accuracy of the derivative contract’s pricing.

In the context of evolving national and international carbon markets and emissions trading frameworks, effective measures to ensure that emission reductions or removals are not double counted may include, among other things, procedures for conducting cross-checks across multiple carbon credit registries.

3. Inspection Provisions—Third-Party Validation and Verification

Consistent with the Appendix C Guidance, the Commission believes that any inspection or certification procedures for verifying compliance with quality requirements or any other related delivery requirements for physically-settled VCC derivative contracts should be specified in the contract’s terms and conditions. The Commission believes that these inspection or certification procedures should be consistent with the latest procedures in the voluntary carbon markets. To that end, the Commission preliminarily believes that the DCM should consider, among other things, how the crediting program for the underlying VCCs requires validation and verification that credited mitigation projects or activities meet the crediting program’s rules and standards.

The Commission preliminarily believes that, when designing a VCC derivative contract, a DCM should consider whether the crediting program has up-to-date, robust and transparent validation and verification procedures, including whether those procedures contemplate validation and verification by a reputable, disinterested party or body. By providing independent confirmation that mitigation projects or activities are achieving the claimed GHG emission reductions or removals, third-party validation and verification can help to ensure that the underlying VCC accurately reflects the quality intended by the DCM and supports voluntary carbon market integrity. A DCM should consider whether the crediting program is employing best practices with respect to third-party validation and verification, which may include conducting reviews of the performance of validators, procedures for remediating performance issues, not using the same third party validator to verify every project type or project category, and using a separate third party to conduct ongoing validation and verification from the third party that completed the initial validation and verification process.

B. A DCM Shall Monitor a Derivative Contract’s Terms and Conditions as They Relate to the Underlying Commodity Market

DCM Core Principle 4 requires a DCM to prevent manipulation, price distortion, and disruptions of the physical delivery or cash-settlement process through market surveillance, compliance, and enforcement practices and procedures. For physically-settled derivative contracts, the Commission has recognized DCM Core Principle 4 to include, among other things, an obligation to monitor the contract’s terms and conditions as they relate to the underlying commodity market, and to the convergence between the contract price and the price of the underlying commodity, and to monitor the supply of the underlying commodity in light of the contract’s delivery requirements. Such monitoring will help a DCM identify circumstances that may cause the contract to become susceptible to price manipulation or distortions, and
to assess whether the terms and conditions of the contract continue to be appropriate—or whether a change in circumstances should be addressed, for example, through changes to the contract’s terms and conditions.86

Given that VCC derivatives are a comparatively new and evolving class of products, and given that standardization and accountability mechanisms for VCCs are still being developed, the Commission preliminarily believes that the monitoring by a DCM of the terms and conditions of a physically-settled VCC derivative contract should include continual monitoring of the appropriateness of the contract’s terms and conditions that includes, among other things, monitoring to ensure that the delivery instrument—that is, the underlying VCC—conforms or, where appropriate, updates to reflect the latest certification standard(s) applicable for that VCC. For example, where there are changes to either the crediting program or the types of projects or activities associated with the underlying VCC, due for example to new standards or certifications, then the DCM should amend the contract’s terms and conditions to reflect this update. In such circumstances, the DCM should also ensure that it is monitoring the adequacy of the estimated deliverable supply of the underlying VCC to satisfy the contract’s delivery requirements.

Finally, the Commission reminds market participants that Commission regulations implementing DCM Core Principle 4 require DCMS to have rules requiring their market participants to keep records of their trading that include records of their activity in the underlying commodity and related derivatives markets.87 A DCM’s rules also must require market participants to make such records available upon request to the DCM.88 As such, DCM market participants are required, upon request, to make records of their trading in underlying VCC cash markets available to the DCM, in order to assist the DCM in fulfilling its market monitoring obligations. These records also are subject to Commission inspection under applicable Commission recordkeeping rules.

86 The Commission has, similarly, recognized that a DCM has a responsibility to monitor the continued appropriateness of the terms and conditions of a cash-settled derivative contract. See, e.g., 17 CFR 38.253(a)(2).
87 17 CFR 38.254(a).
88 Id.

G. A DCM Must Satisfy the Product Submission Requirements Under Part 40 of the CFTC’s Regulations and CEA Section 5c(c)

There are generally two processes by which a DCM may list a new derivative contract for trading.89 The DCM may elect to list the contract for trading by providing the Commission with a written certification—a “self-certification”—that the contract complies with the CEA, including the CFTC’s regulations thereunder.90 Alternatively, the DCM may elect voluntarily to seek prior Commission approval of the contract.91 In each case, the DCM must submit prescribed information to the Commission, including but not limited to the contract’s terms and conditions.92 Amendments to an existing derivative contract also must be submitted to the Commission, along with prescribed information, either by way of self-certification or for prior Commission approval.93

This proposed guidance highlights three submission requirements in connection with the listing of VCC derivative contracts. These requirements apply regardless of whether a DCM elects to list the contract by way of self-certification, or with prior Commission approval. These requirements generally apply with respect to the listing by a DCM of a derivative contract, regardless of the underlying asset class. However, the Commission wishes to remind DCMS of the importance of fully complying with these requirements in a submission for a VCC derivative contract. The relevant requirements provide, first, that a contract submission to the Commission must include an explanation and analysis of the contract and its completeness with applicable provisions of the CEA, including core principles and the Commission’s regulations thereunder.94 Second, the relevant requirements provide that the explanation and analysis of the contract either be accompanied by the documentation relied upon to establish the basis for compliance with applicable law, or incorporate information contained in such documentation, with appropriate citations to data sources.95 Third, the relevant requirements provide that, if requested by Commission staff, a DCM must provide any additional evidence, information or data that demonstrates that the contract meets, initially or on a continuing basis, the requirements of the CEA or the Commission’s regulations or policies thereunder.96

Since VCC derivatives are a comparatively new and evolving class of products, and since standardization and accountability mechanisms for VCCs are still being developed, the Commission anticipates that in connection with the submission for a VCC derivative contract, a DCM may provide qualitative explanations and analysis to assist in addressing the three above-described requirements. The Commission expects that the information—including supporting documentation, evidence and data—provided by the DCM to describe how the contract mcomplies with the CEA and applicable Commission regulations, will be complete and thorough. Given unique and developing aspects of VCCs and VCC derivative markets, including complete and thorough information in a submission for a VCC derivative contract will assist the Commission and its staff in their understanding of the contract and their analysis of the contact’s compliance with applicable statutory and regulatory requirements, including whether or not the contract is readily susceptible to manipulation.

III. Request for Comment

The Commission requests comment from the public on all aspects of the Commission’s proposed guidance regarding the listing of VCC derivative contracts, and further invites comments on specific questions related to the listing of such contracts. The Commission encourages all comments, including whether or not the contract is readily susceptible to manipulation. The Commission requests comment on the following questions:

analysis of contracts that are submitted for affirmative Commission approval.

89 17 CFR 40.2(a)(3)(i)(v) (for self-certification) and 40.3(a)(4) (for Commission approval).
90 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
91 17 CFR 40.2(a)(3)(i)(v) (for self-certification) and 40.3(a)(4) (for Commission approval).
92 17 CFR 40.2(a)(3)(i)(v) (for self-certification) and 40.3(a)(4) (for Commission approval).
93 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
94 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
95 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
96 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
97 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
98 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
99 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).
100 17 CFR 40.2(b)(1) (for self-certification) and 40.3(a)(10) (for Commission approval).

General

1. In addition to the VCC commodity characteristics identified in this proposed guidance, are there other characteristics informing the integrity of carbon credits that are relevant to the listing of VCC derivative contracts? Are there VCC commodity characteristics identified in this proposed guidance that are not relevant to the listing of VCC derivative contracts, and if so, why not?

2. Are there standards for VCCs recognized by private sector or multilateral initiatives that a DCM should incorporate into the terms and conditions of a VCC derivative contract, to ensure the underlying VCCs meet or exceed certain attributes expected for a high-integrity carbon credit?

3. In addition to the criteria and factors discussed in this proposed guidance, are there particular criteria or factors that a DCM should consider in connection with monitoring the continual appropriateness of the terms and conditions of a VCC derivative contract?

4. In addition to the criteria and factors discussed in this proposed guidance, are there particular criteria or factors that a DCM should consider, which may inform its analysis of whether or not a VCC derivative contract would be readily susceptible to manipulation?

5. Should the VCC commodity characteristics that are identified in this proposed guidance as being relevant to the listing of a VCC derivative contract, also be recognized as being relevant to submissions with respect to VCC derivative contracts made by a registered foreign board of trade under CFTC regulation 48.10?

Transparency

6. Is there particular information that DCMs should take into account when considering, and/or addressing in a VCC derivative contract’s terms and conditions, whether a crediting program is providing sufficient access to information about the projects or activities that it credits? Are there particular criteria or factors that a DCM should take into account when considering, and/or addressing in a contract’s terms and conditions, whether there is sufficient transparency about credited projects or activities?

Additionality

7. Are there particular criteria or factors that DCMs should take into account when considering, and/or addressing in a VCC derivative contract’s terms and conditions, whether the procedures that a crediting program has in place to assess or test for additionality provide a reasonable assurance that GHG emission reductions or removals will be credited only if they are additional?

8. In this proposed guidance, the Commission recognizes VCCs as additional where they are credited for projects or activities that would not have been developed and implemented in the absence of the added monetary incentive created by the revenue from carbon credits. Is this the appropriate way to characterize additionality for purposes of this guidance, or would another characterization be more appropriate? For example, should additionality be recognized as the reduction or removal of GHG emissions resulting from projects or activities that are not already required by law, regulation, or any other legally binding mandate applicable in the project’s or activity’s jurisdiction?

Risk of Reversal

9. Are there particular criteria or factors that DCMs should take into account when considering, and/or addressing in a VCC derivative contract’s terms and conditions, a crediting program’s measures to avoid or mitigate the risk of reversal, particularly where the underlying VCC is sourced from nature-based projects or activities such as agriculture, forestry or other land use initiatives?

10. How should DCMs treat contracts where the underlying VCC relates to a project or activity whose underlying GHG emission reductions or removals are subject to reversal? Are there terms, conditions or other rules that a DCM should consider including in a VCC derivative contract in order to account for the risk of reversal?

Robust Quantification

11. Are there particular criteria or factors that a DCM should take into account when considering, and/or addressing in a contract’s terms and conditions, whether a crediting program applies a quantification methodology or protocol for calculating the level of GHG reductions or removals associated with credited projects or activities that is robust, conservative and transparent?

Governance

12. In addition to a crediting program’s decision-making, reporting, disclosure, public and stakeholder engagement, and risk management policies, are there other criteria or factors that a DCM should take into account when considering, and/or addressing in a VCC derivative contract’s terms and conditions, whether the crediting program can demonstrate that it has a governance framework that effectively supports the program’s transparency and accountability?

Tracking and No Double Counting

13. In addition to the factors identified in this proposed guidance, are there other factors that should be taken into account by a DCM when considering, and/or addressing in a VCC derivative contract’s terms and conditions, whether the registry operated or utilized by a crediting program has processes and procedures in place to help ensure clarity and certainty with respect to the issuance, transfer, and retirement of VCCs?

14. Are there particular criteria or factors that a DCM should take into account when considering, and/or addressing in a VCC derivative contract’s terms and conditions, whether it can be demonstrated that the registry operated or utilized by a crediting program has in place measures that provide reasonable assurance that credited emission reductions or removals are not double-counted?

Inspection Provisions

15. Should the delivery procedures for a physically-settled VCC derivative contract describe the responsibilities of registries, crediting programs, or any other third-parties required to carry out the delivery process?

Sustainable Development Benefits and Safeguards

16. Certain private sector and multilateral initiatives recognize the implementation by a crediting program of measures to help ensure that credited mitigation projects or activities meet or exceed best practices on social and environmental safeguards, as a characteristic that helps to inform the integrity of VCCs issued by the crediting program. When designing a VCC derivative contract, should a DCM consider whether a crediting program has implemented such measures?

17. Certain private sector and multilateral initiatives recognize the implementation by a crediting program of measures to help ensure that credited mitigation projects or activities avoid locking in levels of GHG emissions, technologies or carbon intensive practices that are incompatible with the objective of achieving net zero GHG emissions by 2050, as a characteristic that helps to inform the integrity of VCCs issued by the crediting program. When designing a VCC derivative contract, should a DCM
consider whether a crediting program has implemented such measures?

Issued in Washington, DC, on December 21, 2023, by the Commission.

Christopher Kirkpatrick,
Secretary of the Commission.

NOTE: The following appendices will not appear in the Code of Federal Regulations.

Appendices to Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts; Request for Comment—Voting Summary and Chairman’s and Commissioners’ Statements

Appendix 1—Voting Summary

On this matter, Chairman Behnam and Commissioners Johnson, Goldsmith Romero, and Pham voted in the affirmative. Commissioner Mersinger voted to concur. No Commissioner voted in the negative.

Appendix 2—Statement of Support of Chairman Rostin Behnam

The CFTC as a market regulator has a significant role to play in the voluntary carbon markets (VCMs). As we have seen the listing of listed futures on voluntary carbon credits (VCCs), the Agency’s relationship and responsibility is real. These markets present an opportunity for the agricultural economy that historically underpins the need for derivatives markets for risk management and price discovery, but they also provide a useful tool throughout the financial markets and the real economy. And today, the Agency takes the most significant step of a financial regulator to promote fundamental standards for high integrity VCCs.

Market participants from across all asset classes will increasingly turn to the derivatives markets as they manage the impact of physical and transition risks related to extreme weather events and climate-related financial risk. The CFTC’s role is to ensure that these developing derivatives markets including those for VCCs, have integrity, adhere to basic market regulatory requirements, and remain resilient as we most certainly will continue to experience extreme and dramatic weather events that will impact pricing and volatility.

The Commission’s proposed guidance for designated contract markets (DCMs) that list derivatives contracts with voluntary carbon credits (VCC) as the underlying commodity is an important step in shaping the development of high-integrity voluntary carbon markets. For the first time ever, the CFTC is proposing regulatory guidance for exchanges listing products aimed at providing tools to manage risk, promote price discovery, and help channel capital to support decarbonization. The publication of this proposed guidance and request for public comment marks the culmination of years of work with stakeholders such as farmers, foresters, end users, energy traders and associations, emission-trading focused entities, carbon-credit rating agencies, credit programs, CFTC-registered exchanges and clearinghouses, and derivatives trade associations. This proposal also presents a whole-of-government approach in coordination with our partners across the federal complex.

Each step has been intentional. My sponsorship of the Market Risk Advisory Committee’s Climate-Related Market Risk Subcommittee, which issued a report on Managing Climate Risk in the U.S. Financial System Report in 2020 identified putting a price on carbon as a fundamental element for financial markets to efficiently channel capital to reduce greenhouse gas emissions (GHGs). My establishment of the CFTC’s Climate Risk Unit in March 2021 allowed the Commission to build its subject matter expertise regarding the role that climate-related derivatives will have in pricing and managing climate-related financial risk. I hosted two VCM Convenings to gather information from a wide variety of market participants to better understand the potential role of the official sector in these markets, particularly as we began to see the emergence of listed futures products that reference VCC cash markets. The CFTC, with the support of my fellow commissioners, issued a Request for Information on Climate-Related Financial Risk that received more than 100 comments on ten priority areas of interest including VCMs and product innovation. I have also testified before Congress on several occasions specifically on the role of financial markets in addressing the climate crisis and my views on the CFTC’s role in supporting solutions.

The primary takeaway from this research and public engagement is clear; the Commission should act, consistent with its statutory authority under the Commodity Exchange Act (CEA), to strengthen market integrity, transparency, and liquidity for derivatives with an underlying VCC that are real, additional, permanent, verifiable, and represent unique metrics of GHG emissions reduced or removed from the atmosphere.

While VCC derivatives are a comparatively new and evolving class of products, DCMs must ensure that any listed derivatives comply with the CEA and Commission regulations. The proposed guidance outlines factors that DCMs should consider when listing products including: DCM Core Principle 3, which requires DCMs to list only contracts that are not readily susceptible to manipulation; DCM Core Principle 4, which requires DCMs to have the capacity and responsibility to prevent manipulation, price distortion, and other market disruptions through market surveillance, compliance, and enforcement practices and procedures; the Commission’s regulations promulgated for these DCM Core Principles; and the product submission provisions set forth in CEA section 5c(c) and Part 40 of the Commission regulations.

The proposed guidance is not intended to modify or supersede existing statutory or regulatory requirements, or existing Commission guidance that addresses the DCMs’ listing of derivative contracts, such as Appendix C to Part 38 of the Commission’s regulations. Instead, the proposed guidance outlines particular VCC commodity characteristics that a DCM should consider in the design of a VCC futures contract’s terms and conditions such as (i) quality standards, which include transparency, additivity, permanence and accounting for the risk of reversal, and

robust quantification of emissions reductions or removals; (ii) delivery points and facilities which include effective governance at the carbon crediting program, tracking the issuance, transfer, and retirement of VCCs, and no double counting; and (iii) inspection provisions which includes independent third-party validation and verification. A DCM’s consideration of these factors during the design of a derivative product’s terms and conditions should promote accurate pricing, reduce susceptibility of the contract to manipulation, help prevent price distortions, and foster confidence in the VCC contracts. Consistent with the current statutory and regulatory requirements, DCMs would retain reasonable discretion in establishing the manner in which it complies with a DCM Core Principles and the Commission’s regulations.

I believe the proposed guidance outlines well-researched VCC commodity characteristics that build on several private sector and multilateral initiatives that have made great strides to strengthen VCC credit integrity standards. I also believe the proposed guidance supports transparency, liquidity, and market integrity. This effort is the product of a strong public-private partnership that I have strived to achieve with the CFTC’s traditional stakeholders as well as those VCM stakeholders that may be newer to the derivatives markets.

The Commission is cognizant that the derivatives markets are global markets and has crafted this proposed guidance to be complementary to the important work underway by the International Organization of Securities Commissions (IOSCO) through its Sustainable Finance Task Force’s Carbon Market Workstream, which I co-chair with Verena Ross, the Chair of ESMA. While this proposed Commission guidance focuses on the due diligence that DCMs should undertake when designing and monitoring their proprietary listed VCC derivative contracts, IOSCO’s work over nearly two years is focused on how regulators can promote sound market structure and enhance financial integrity in the VCMs so that high-quality carbon credits can be traded in an orderly and transparent way. I invite our stakeholders to also provide comment on IOSCO’s December 2023 publication of its VCM Consultation Report.6

The proposed guidance is not intended to suggest that the Commission has a role in creating or mandating compliance with any kind of climate policy. The CFTC’s unique mission focused on risk mitigation and price discovery, however, puts us on the front lines of the now global nexus between financial markets and decarbonization efforts. Leveraging the CFTC’s personnel and expertise demonstrates our commitment to taking thoughtful and deliberate next steps toward building a financial system that provides effective tools in achieving emission reductions.

I thank my fellow commissioners for enabling the Commission to publish this proposed guidance for public comment. I greatly appreciate the expertise and all of the hard work done by the staff in my office, the Division of Market Oversight, and the Office of the General Counsel on this proposed guidance. I look forward to reviewing the public comments on all aspects of the guidance as well as on the seventeen specific questions relating to the listing for trading of VCC derivative contracts.

Appendix 3—Statement of Commissioner Kristin Johnson

Today, the Commodity Futures Trading Commission (Commission or CFTC) adopts proposed Guidance and a Request for Comments regarding the listing of voluntary carbon credit (VCC) derivative contracts on designated contract markets (DCMs)—boards of trade that operate under the regulatory oversight of the CFTC (Proposed Guidance). I support the Proposed Guidance as it advances important transparency and market integrity efforts.

However, evidence suggests that environmental commodity markets, specifically the underlying spot markets for carbon credits, are rife with fraud. Consequently, I find the Proposed Guidance to be necessary, but insufficient. I am hopeful that the Proposed Guidance ushers in discussion and the development of a comprehensive regulatory initiative to address the deeply concerning, and nearly indisputable, proliferation of fraud in the carbon credit markets. As I noted, in a recent speech at a joint convening of the Environmental Advisory Council and the Financial Sector Advisory Council of the Dallas Federal Reserve Bank:

While the issues and concerns regarding climate risks are endemic, complex, and inherently require multi-lateral solutions effectuated by an international coalition of stakeholders—let’s call it: a coalition of the willing—I strongly believe that financial market regulators and committed market participants may play a pivotal role in developing and implementing some basic, foundational market reforms.1

tools, designed to address mounting evidence of climate change and the attendant, significant effects on the global economy. Under Chair Behnam’s leadership, in 2020, the Climate-Related Market Risk Subcommittee of the Commission’s Market Risk Advisory Committee (an Advisory Committee that I currently sponsor), released a report identifying actions the Commission could take to address climate change and finding that climate-related financial risks pose a major risk to the stability of the U.S. financial system.2

A report by the U.S. Department of the Treasury released in September explains that “[t]he impacts of climate change are significant and escalating, including through more frequent and severe weather events, rising sea levels, and higher temperatures.” 3 The report details how climate risks are impacting individual household finances, U.S. financial markets, and supply chains. “In 2022 alone, the cost of climate and weather disasters in the United States totaled more than $176 billion—the third most costly year on record.”4

There are deep and persistent concerns regarding the integrity, credibility, and lack of visibility in the market for carbon credits. Indisputably, challenged efforts to establish universally-adopted and enforceable integrity standards has further stymied attempts to scale carbon credit markets.

Just last fall, U.S. Senators Elizabeth Warren, Cory Booker, and Kirsten Gillibrand alongside several other Senators, encouraged the CFTC to use its enforcement jurisdiction aggressively to investigate and prosecute fraud and manipulation in spot and forward environmental commodity markets.5

On June 29, 2023, the Commission announced the Environmental Fraud Task Force, which was created to address misconduct in the regulated derivatives markets and to investigate fraud in the spot market for VCCs, in particular with respect to the purported environmental benefits of purchased carbon credits, and registrants’ misrepresentations regarding purported environmental benefits and environmental, social, and governance (ESG) products or strategies.6

These issues have become so much a part of the cultural dialogue that The New Yorker featured an article titled “The Great Cash-For-Carbon Hustle,” which detailed the rise and fall of South Pole, led by its forty-four-year-old CEO Rant Heuberger, and the revelation that it sold carbon credits that were not real. In recent speeches at the Federal Reserve Banks in Atlanta and Dallas and Rice University’s Baker Institute for Public Policy Annual Energy Summit, I outlined the necessity for market structure reforms in the VCC markets as well as derivatives on VCCs.7 As I have previously stated:

in order for the carbon offset markets to have any significance (and, arguably, for such markets to avoid extinction), we must ensure the integrity of the market.8 Financial market regulators and committed market participants play a pivotal role in developing and implementing some basic, foundational market reforms.9

Today’s Proposed Guidance marks a step in the right direction.

Commission Regulatory Authority

The Proposed Guidance applies to the listing of futures with VCCs as the underlying assets. DCMs that list and offer derivatives on VCCs, which are commodities, must be registered with the Commission prior to offering such contracts. Pursuant to the Commodity Exchange Act (CEA), to be designated, and maintain a designation, as a contract market, a board of trade must comply with all core principles and any requirement that the Commission may impose by rule or regulation.

Core principle 3 requires a DCM to demonstrate that listed contracts are not readily subject to manipulation. Core principle 4 requires a DCM to prevent manipulation, price distortion, and disruptions of the physical delivery or cash-settlement process through market surveillance, compliance, and enforcement practices and procedures.10 Guidance and acceptable practices provide contextual information regarding the core principles and detailed examples of how a DCM must satisfy a core principle. Additionally, DCMs must comply with “submission requirements ... prior to listing a product for trading,” including by way of self-certification or Commission approval of such products.

The Commission reviews the product specifications, including information about the underlying asset, as part of this review process.

Futures on VCCs: Great Interest, Limited Volume

Over the last several years, the Commission authorized the listing of futures contracts on certain environmental instruments, including mandatory emissions and voluntary carbon program instruments. There are almost two hundred derivative contracts on environmental commodities although at this time only three contracts have open interest. As of November 2023, DCMs submitted eighteen futures contracts on voluntary carbon market products the Commission for listing. Derivative contracts on VCCs base their prices on the spot price of VCCs,11 and therefore the integrity of the underlying spot market is critical to the stability of the derivatives market for those underlying VCC commodities.

General Summary of the Proposed Guidance

Endemic fraud in the VCC spot market impacts the integrity of environmental derivative contracts that reference spot market projects. While the Commission’s authority to introduce regulation is limited to commodity

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4 Id.
5 Id.
6 For example, NYMEX’s CBL Global Environmental Offset futures contracts, and Nodal Exchange’s Verified Emission Reduction futures and options contracts, are physically-settled contracts. If the holder of a position in the contract still has an open position at the expiration of trading in the contract, then the position holder must, in accordance with the rules for delivery set forth in the contract, make or take delivery (as applicable) of 1,000 VCCs that meet the contract’s rules for delivery eligibility.
derivatives, the Commission has broad authority to address fraud and market manipulation in the spot market.

The Proposed Guidance outlines factors that DCMs should consider when addressing certain requirements under the CEA and CFTC regulations that are relevant to the listing for trading of VCC derivative contracts, as previously mentioned, without providing a qualitative element in terms of identifying how the Commission expects the DCM to weigh those factors to create a certain aspirational goal.

Specifically:

• When addressing quality standards in the development of the terms and conditions of a VCC derivative contract, the Proposed Guidance states that a DCM should consider transparency, additivity, permanency and risk of reversal, and robust quantification in connection with the underlying VCC.

• The Proposed Guidance provides much-needed direction to DCMs (and SEFs) to facilitate their compliance with core principles when they list futures contracts (and swaps contracts) on VCCs. However, the Commission is only addressing one small aspect of the market for derivatives on these underlying assets. There is also a segment of the swaps market that is not traded on a SEF for which VCCs are underliers and an even more significant volume of environmental commodities that are not currently traded on a SEF.

• The Commission has broad authority to address fraud and market manipulation in the spot market.

• As part of the product review process, a DCM is required to submit the contract’s terms and conditions and any contract amendments and must also include an explanation and analysis of the contract and its compliance with applicable CEA provisions. The submitted information—including supporting documentation, evidence and data—provided by the DCM should describe how the contract complies with the CEA and applicable Commission regulations and should be complete and thorough.

DMO suggests that the Proposed Guidance should be considered by aswap execution facility (SEF) that proposes to trade swaps with VCCs as underlying commodities. Similar to DCMs, SEFs are directly subject to core principles, guidance, acceptable practices, and product listing requirements. 12

The Proposed Guidance may help to improve the integrity of the VCC markets. Yet, there are additional and significant issues that the Proposed Guidance does not address.

On November 13, 2023, I delivered a keynote speech at the Federal Reserve Bank of Atlanta. During that discussion, I noted:

There are certain principles that must guide the development of market structure for VCC markets: including the introduction of transaction reporting; secondary market regulation including, where relevant, clearing and settlement guidance; accountability standards for intermediaries to ensure integrity and reliability (and in the context of environmental commodities additivity); business conduct standards, including standardized documentation (and requirements for certification of environmental commodities); and appropriate guardrails for any retail market participation. 13

On November 29, 2023, I delivered keynote remarks at a joint convening of the Energy Advisory Council and Financial Sector Advisory Council of the Dallas Federal Reserve Bank. There, I outlined additional interventions that may mitigate the proliferation of fraud in VCC markets and foster innovation and competition, while ensuring the integrity of our commodities.

The Proposed Guidance provides a comprehensive approach to regulating VCC markets: 14

A Comprehensive Approach To Regulating VCC Markets

A comprehensive framework enhances the integrity of futures and OTC markets enabling risk transfer, investment, hedging, and price discovery.

12 17 CFR part 37 and Appendix B to Part 37 (Guidance on, and Acceptable Practices in, Compliance with Core Principles).


14 For reference, in futures markets, futures commission merchants are required to provide comprehensive disclosures under CFTC Regulation 1.55 where all materials risks are specifically addressed. Registered commodity pool operators and commodity trading advisors are also required to provide disclosures on risks of trading futures and swaps.

15 7 CFR 23.431. This provision requires the disclosure of market, credit, liquidity, foreign currency, legal, operational, any other applicable risks; the financial economic terms of the swap, the terms relating to the operation of the swap, and the rights and obligations of the parties during the term of the swap; and the price of the swap, the midmarket mark of the swap, and any compensation or other incentive from any source other than the counterpart that the swap dealer may receive in connection with the swap.

Continued
In my view, the concepts of material information, material risks, material characteristics, material incentives and conflicts of interest of a derivative must necessarily include the underlying commodity on which a derivative is priced. In light of the lack of visibility into pricing in the VCC markets and the dearth of publicly available information regarding pricing methodologies, such disclosures are particularly important.

Using the risk disclosure requirement as a framework, the Commission should provide guidance that applies to all environmental derivative products. In the context of derivatives on VCCs or other environmental products, where the risk of loss may be magnified because of leverage, the sellers must ensure their counterparty has adequate information to understand how observed volatility and inherent risk in the nascent and evolving VCC market could impact the price of the derivative.

For certain forward contracts on VCCs, it is possible that no material risk disclosure requirement applies; however, the CFTC does have enforcement jurisdiction if there is fraud, including where incorrect or misleading information is provided. CFTC regulations do not require parties to make affirmative statements about nonpublic information—but if a party does speak, CFTC Regulation 180.1(b) specifically requires that a materially misleading statement be corrected, including nonpublic information that may be material to the market price, rate, or level of the commodity transaction.17

The Commission may not need to prescribe the precise language of the disclosures. The material risk disclosure rule is principles-based. Instead, the Commission may identify factors that a market participant must consider in a risk disclosure, including all the factors that could lead to significant losses. Information about a carbon credit, including information about the environmental project and market structure, is material because there is a substantial likelihood that a reasonable counterparty would consider it important in making a trading decision.

**Guidance on Good Faith and Fair Dealing**

The principles of good faith and fair dealing are well-established in the futures, swaps and securities industries. The National Futures Association’s customer communication rule also imposes a duty to communicate in a fair and balanced manner.

In the swaps market, the risk disclosure requirement is closely linked to the swap dealer’s obligation to communicate in a fair and balanced manner. Swap dealers have a duty to communicate with all of their counterparties in a fair and balanced manner based on principles of fair dealing and good faith.18 This duty, the Commission notes, “is designed to ensure a balanced treatment of potential benefits and risks.”19

In the adopting release for the fair dealing requirement, the Commission noted:

In a complex swap, where the risks and characteristics associated with an underlying asset are not readily discoverable by the counterparty upon the exercise of reasonable diligence, the swap dealer or major swap participant is expected, under both the disclosure rule and fair dealing rule, to provide a sound basis for the counterparty to assess the swap by providing information about the risks and characteristics of the underlying asset.20

The Commission should offer guidance as to its expectations of how the fair dealing requirement should be considered in the context of an underlying asset that is a VCC. The fair dealing rule provides an independent basis for enforcement proceedings—for example where the swap dealer makes exaggerated or un warranted claims, opinions, or forecasts in violation of the fair dealing requirement.21

Such a requirement may not apply to certain forward contracts on VCCs. Yet, the Commission maintains broad enforcement jurisdiction in the event that there is an allegation of fraud, including where incorrect or misleading information is provided. CFTC Regulation 180.1(a)(2) makes unlawful the making of an untrue or misleading statement of a material fact or omitting a material fact necessary to make a statement made not untrue or misleading.22

17 CFR 39.12(b).

18 7 CFR 23.433.


20 Id. at 9760.

21 Id. at 9769.

22 17 CFR 180.1(a)(2) (providing that it is unlawful for any person in connection with any contract of sale of any commodity in interstate commerce to intentionally or recklessly make, or attempt to make, any untrue or misleading statement of a material fact or to omit to state a material fact necessary in order to make the statements made not untrue or misleading).

In the future, should the market evolve and become more standardized, the clearing framework may also provide valuable risk reduction benefits for derivatives on environmental commodities. Clearing, by way of novation, reduces counterparty credit risk because a DCO serves as a seller to every buyer and a buyer to every seller, remaining neutral. DCOs are highly regulated by the Commission, are subject to core principles, and have significant, articulated financial resources. At settlement, DCOs may facilitate the physical delivery of the actual underlying commodity or cash payments based on the final price of the underlying commodity in connection with the derivatives contract.

In the context of environmental derivatives, DCOs would facilitate delivery of the VCC or determine the cash amount based on the price of the VCC in the cash market. For purposes of physical settlement, a well-functioning carbon credit cash market is essential. Core principle C sets out product eligibility requirements. A DCO must have appropriate requirements for determining the eligibility of contracts submitted to the DCO for clearing, taking into account the DCO’s ability to manage the risks associated with such contracts.

Some factors the DCO must consider include the availability of reliable prices, the ability of the DCO and clearing members to gain access to the relevant market for purposes of creating, liquidating, transferring, auctioning, and/or allocating positions, and the operational capacity of the DCO and clearing members to address any unique risk characteristics of a product clearing member.23 A DCO should take care not to clear transactions that present an unacceptable level of risk.

In the context of the current VCC market, significant questions arise as to whether certain elements of the DCO core principles would be easily established, including whether there are reliable prices for these carbon credits, the access to carbon credit markets, and whether there is material information about the carbon credit. Additional Commission guidance perhaps could facilitate the market, increase volumes and promote sound risk management, reasonably-designed policies and procedures, and robust rules.

The development of rules that facilitate the clearing of derivatives

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17 CFR 180.1(b) (stating that nothing in that section shall be construed to require any person to disclose to another person nonpublic information that may be material to the market price, rate, or level of the commodity transaction, except as necessary to make any statement made to the other person in or in connection with the transaction not misleading in any material respect).
based on environmental commodities would be greatly advanced by Commission guidance on the application of those principles to the clearing of such products. Forwards on carbon credits are not required to be cleared at a DCO; but clearing and settlement provide critical counterparty credit risk management.

**Conclusion**

It is difficult to overstate the significance of today’s announced Proposed Guidance. Once again, the CFTC is demonstrating leadership in the novel carbon credit markets and contemporaneously enhancing the integrity of carbon-credit markets.

I believe the Commission has taken an important step forward by announcing the Proposed Guidance advanced today. However, I am hopeful that this step is the first on a long journey to introduce effective market structure reforms in VCC markets.

**Appendix 4—Statement of Commissioner Christy Goldsmith Romero**

I am pleased to support today’s proposed guidance regarding the listing of voluntary carbon credit derivatives. I want to recognize Chairman Behnam’s leadership in the voluntary carbon credit space. The proposed guidance follows efforts by the Commission to develop capacity in understanding and regulating voluntary carbon credits.

The physical effects of climate change are amplifying. 2023 is likely to go down as the warmest year on record. The intensifying physical impacts of climate change pose serious risks to commodities derivatives markets and potentially systemic risk to the financial system if not effectively managed. Our mission includes promoting resilience in derivatives markets that can play a critical role in managing climate risk.

Many market participants are seeking opportunities in derivatives markets to promote resilience to climate risk, including through voluntary carbon credits. The CFTC oversees voluntary carbon credit derivatives listed and trading on CFTC-registered exchanges. In addition to regulatory authority over derivatives, the CFTC also has antifraud authority in the spot voluntary carbon credit markets given the potential for impact to the derivatives markets.

In response to our public consultation, various market participants, public interest groups, and U.S. Senators have asked the CFTC to take a leading role in promoting the integrity of voluntary carbon markets. I was pleased to help launch the CFTC’s Environmental Fraud Task Force that will pursue individual cases of fraud related to carbon credits, weeding out bad actors, and promoting market integrity. Today’s proposed guidance is the next step in promoting market integrity.

I have met with exchanges to discuss their process for listing these emerging products, and found differing approaches to these products and due diligence in the underlying credit. CFTC-registered exchanges have certain requirements under the Commodity Exchange Act including to list only contracts that are not readily susceptible to manipulation, to have the capacity and responsibility to prevent manipulation, price distortion and other market disruptions, and other requirements aimed at market integrity.

**Conclusion**

Commission guidance, like what is proposed today, can help exchanges understand what compliance means in a still rapidly evolving market for voluntary carbon credits, one where there can be concerns about integrity, including for carbon credits listed on some of the largest registries, a lack of transparency, and uncertainty related to pricing. These concerns in the spot market could affect the regulated derivatives market. For a market to work well, market participants need to be confident they have credible information about the product, that there are appropriate levels of pricing, and that the market has integrity, so that they do not face legal, reputational and regulatory risks.

I continue to believe that bringing more of this market onto regulated exchanges could increase integrity, transparency, and bring greater confidence to the market. I agree with a response to our consultation which said that “the expansion of exchanges offering products . . . would help grow liquidity and therefore the value of the market for price discovery and risk shifting.” CFTC-regulated exchanges have important responsibilities under the Commodity Exchange Act and stand as the first line of defense to ensure market integrity. The market should signal through pricing which carbon credits are high quality compared to credits reflecting projects that do not achieve the requisite level of one ton of greenhouse gases removed or reduced.

However, one of the biggest challenges in voluntary carbon markets is fragmentation which different projects, registries, and standards, that can impact derivatives markets and harm market confidence. A lack of transparency through consistent, comparable data can present challenges to proper functioning of markets, including price discovery. There are important and welcome efforts by voluntary bodies like the Integrity Council on Voluntary Carbon Markets (“ICVM”) to create voluntary .

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24In June 2022, the Commission held the first-ever Voluntary Carbon Markets Convening to discuss issues related to the supply and demand for high quality carbon offsets. Then in July 2023, the Commission held the second Voluntary Carbon Markets Convening to discuss recent private sector initiatives for high quality carbon credits, among other topics.

2The Commission has held two convenings to gather information from a range of carbon market stakeholders and last year conducted a request for information on climate-related risks, which asked several questions about carbon markets. The Commission received significant comments on voluntary carbon credit products and markets.


4In one relevant example, several press sources reported serious allegations about a project developed by the market’s largest firm, a project that has been among the leading sources of carbon credits globally. Blake, Heidi, *The Great Cash for Carbon Hustle*, The New Yorker (Oct. 16, 2023); Ben Elgin, Alastair Marsh, and Max de Haldevang, *Free Credit Tarnish Billion-Dollar Carbon Offset Seller*, Bloomberg (Mar. 24, 2023). The allegations were sufficiently credible that the project’s registry put on hold issuance of credits from the project, pending an investigation. Verra Statement on the New Yorker Article of October 16, 2023, Verra (Oct. 17, 2023).

standards to address concerns about credibility and to develop a common understanding of a high-quality credit, efforts that are ongoing.

In March, I proposed that the Commission work with regulated exchanges to develop common baseline standards for listing voluntary carbon credit derivatives. At a conference held by ISDA, I proposed that the Commission consider requiring exchanges to take certain actions to increase confidence that underlying voluntary carbon credits reliably remove or avoid the amount of carbon claimed of one ton of greenhouse gases per credit. I proposed that such actions could include information sharing agreements with carbon registries and baseline standards for carbon credits that could reference either the ICVCM carbon principles once they became final or the basic principles on which they are based. I thank the Chairman for working with me on these efforts.

Today’s guidance adapts terminology, concepts and standards from the ICVCM’s Core Carbon Principles and its recently issued Assessment Framework. I support the Commission’s recognition of the efforts made by this body that could improve integrity, transparency, and price discovery, and thereby improve confidence in these markets.

The Commission’s guidance adapts ICVCM concepts and standards that commenters told us were needed for integrity in voluntary carbon markets. The guidance sets an expectation for exchanges to ensure that underlying VCC’s represent an actual ton of carbon dioxide removed or reduced and that there is no double counting of those reductions or removals. It also sets an expectation that underlying VCC’s are subject to a meaningful independent evaluation and verification before issuance. Aligning the CFTC’s expectations with the ICVCM’s work also recognizes the global nature of this market and of the challenges posed by climate-related financial risk.

I am interested in hearing from commenters if the guidance adapts the right parts of the ICVCM standards to encourage integrity and transparency in these markets and if the Commission’s adaptation provides clear, workable expectations. As the ICVCM standards have only been recently released, it will be important to monitor the adoption of these standards.

I am also interested in hearing more from commenters about whether market integrity can be improved by exchanges relying on a crediting program’s processes and diligence, as assumed in the proposed guidance, or if there is a benefit to exchanges conducting additional due diligence into specific categories, protocols, or projects.

I am interested to hear from commenters, including participants in our previous public consultation if this guidance meets their needs and helps address concerns they have raised. I especially hope to hear from farmers and others in the agricultural community, several of whom encouraged the CFTC to play a role in ensuring integrity in carbon markets in response to last year’s public consultation.

As derivatives markets evolve, it is important that the Commission remain nimble and aware of changes, and continue to work with exchanges in listing products. I applaud the staff for their hard work on this guidance and I thank them for working with me to incorporate feedback I have heard in meetings with exchanges, market participants and public interest groups over the past 18 months.

FOR FURTHER INFORMATION CONTACT: Christina Gomer, (240) 474–2403, Electricity Exports@hq.doe.gov.

SUPPLEMENTARY INFORMATION: The United States Department of Energy (DOE) regulates electricity exports from the United States to foreign countries in accordance with section 202(e) of the Federal Power Act (FPA) (16 U.S.C. 824a(e)) and regulations thereunder (10 CFR 205.300 et seq.), Sections 301(b) and 402(f) of the DOE Organization Act (42 U.S.C. 7151(b) and 7172(f)) transferred this regulatory authority, previously exercised by the now-defunct Federal Power Commission, to DOE.

Section 202(e) of the FPA provides that an entity which seeks to export electricity must obtain an order from DOE authorizing that export. (16 U.S.C. 824a(e)). On April 10, 2023, the authority to issue such orders was delegated to the DOE’s Grid Deployment Office (GDO) by Delegation Order No. S1–DEL–S3–2023 and Redelegation Order No. S3–DEL–CD1–2023.

On December 19, 2018, DOE issued Order No. EA–463 to BETM to transmit electric energy from the United States to Canada as a power marketer for a period of five years. On November 14, 2023, BETM filed an application with DOE (Application or App.) for renewal of their export authority for a five-year term. App. at 8.

The Application for Renewal of Authorization To Export Electric Energy; Boston Energy Trading and Marketing LLC

AGENCY: Grid Deployment Office, Department of Energy.

ACTION: Notice of application.

SUMMARY: Boston Energy Trading and Marketing LLC (the Applicant or BETM) has applied for renewed authorization to transmit electric energy from the United States to Canada pursuant to the Federal Power Act.

DATES: Comments, protests, or motions to intervene must be submitted on or before January 26, 2024.

ADDRESSES: Comments, protests, motions to intervene, or requests for more information should be addressed by electronic mail to Electricity.Exports@hq.doe.gov.