PROPOSAL TO CREATE EARLY FINANCE CARBON UNITS

1   BACKGROUND

Verra is considering creating a new unit to be offered under the VCS Program to support the development of GHG emission reduction and removal projects. The proposed unit, the Early Finance Carbon Unit (EFCU), could be assigned at project registration, thereby enabling projects to transact units prior to verification and the issuance of Verified Carbon Units (VCUs). The potential to assign EFCUs could help projects attract early investment and be useful for prospective VCU buyers. EFCUs would sit on the Verra registry and would be converted into VCUs after verification. We would like to note that EFCUs are not ex-ante credits, but rather reflect the emission reductions or removals that a given project is expected to generate in the future.

Verra is seeking stakeholder input on the design of EFCUs. This public consultation provides details about the proposed units and includes key questions Verra is seeking to answer in order to finalize and operationalize the concept.

This public consultation will be open for 60 days until 30 January 2021.

2   PROPOSED DESIGN

Verra would assign EFCUs to projects prior to the generation of VCUs and allow purchasers of the EFCUs to automatically receive the associated VCUs if and when they are generated. Specifically, EFCUs would allow project proponents to sell a serialized unit to a buyer prior to completing a given verification and issuance of VCUs. By "assignment of an EFCU" we refer to the administrative action taken by Verra to create and deposit an EFCU into a project proponent's registry account. The purchase of one EFCU would entitle the purchaser to receive one VCU upon generation and issuance of a verified emission reduction or removal.

EFCUs would not represent an ex-ante carbon credit; a holder of an EFCU could not make an offsetting claim by buying or retiring an EFCU. Indeed, EFCUs cannot be retired; rather, holders of EFCUs will only be able to cancel EFCUs, whether they are converted into VCUs or canceled because the emission reductions and/or removals never materialized. In other words, once a project verifies emission reductions and/or removals and decides to issue VCUs that were preceded by EFCUs, the EFCUs are canceled and automatically become a corresponding VCU, which could then be used to offset carbon emissions. However, if no VCU is generated with respect to a particular EFCU, then the EFCU is simply canceled. In addition, the assignment of EFCUs would be optional, at the discretion of the project

proponent, and could be requested at any time after validation of a project and prior to the issuance of the VCUs.

From a project developer's perspective, EFCUs could be useful because they would provide an externally (Verra-) approved and registered unit that can be used to track and link to future deliveries of VCUs, including selling these to an end-buyer or other entity early in a project's life cycle. This is especially valuable for nature-based carbon removal (e.g., Afforestation, Reforestation and Revegetation (ARR), wetlands restoration) projects, which typically require significant upfront investment to undertake initial activities (e.g., tree planting) but take a long time to generate verifiable removals. EFCUs could also play a critical role bringing new players into the climate arena by reducing contracting and delivery risks, building market liquidity, and facilitating transactions, thereby unlocking significant new capital for climate action.

From a buyer's perspective, EFCUs could be useful because they would enhance the transparency of the carbon market by providing a unit of measure held in an independent registry. Specifically, this would enable buyers of credits to lock in a project developer's commitment to deliver a specified number of VCUs. Once EFCUs have been sold to a particular buyer, project developers would be unable to deliver VCUs to a different buyer until the original EFCU delivery obligations are satisfied.

Further details describing how the EFCU might work are set out in Section 3 below.[1]

3   CREATION OF EFCUS

The diagram below sets out the key procedural steps for generating and using EFCUs; the following, notes provide additional details.

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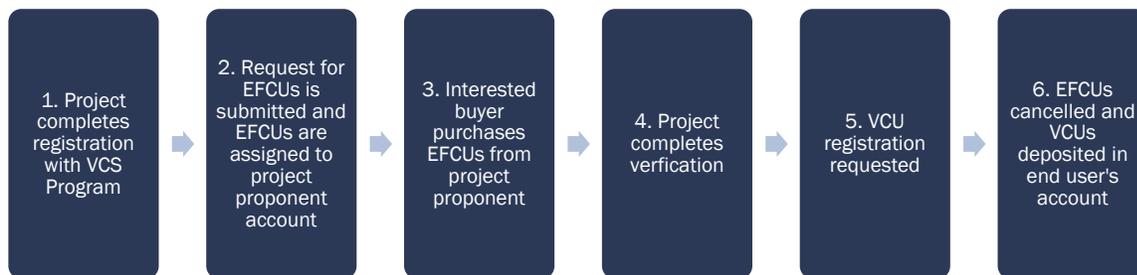
[1] EFCUs would be similar in purpose to Pending Issuance Units (PIUs), which have historically been offered and successfully transacted through the IHS Markit registry in the context of the VCS Program and the Woodland Carbon Code. Verra appreciates that the PIU construct was useful for many buyers and sellers, and sees the value in offering a similar product on the Verra Registry.

1) The project is registered with the VCS Program, following validation by an independent Validation/Verification Body (VVB). As part of that validation process, the VVB assesses and validates the estimated annual emission reductions/removals to be generated by the project, and these are stated in the project description, the validation report, and on the Verra registry.

2) The project proponent may request the assignment of EFCUs after project validation and registration. The amount of EFCUs to be assigned would be limited to the project's estimated annual emission reductions/removals as confirmed at validation.[2] Verra would charge a fee of USD0.04 for each EFCU assigned. Further details on this step in the process are set out in Annex 1 at the end of this document.

3) A contract for the sale/purchase of EFCUs sets out the legal and financial terms of a sale of EFCUs. In other words, the purchase of EFCUs would equate to the purchase of a corresponding amount of VCUs. In purchasing EFCUs, the purchaser would commit to take ownership and delivery of the VCUs upon issuance. Once this contract is signed, EFCUs would be transferred from the project proponent's account to the buyer's account.

4) The project conducts its verification. As part of that verification process, the actual volume of emission reductions/removals generated is assessed and confirmed by the VVB and stated in the monitoring report and the verification report.

5) The project proponent (and potentially the EFCU holder -- see consultation questions below) may request issuance of VCUs after verification, noting that these would be capped by the actual volume of emission reductions/removals verified and thus may represent fewer emission reductions/removals than EFCUs assigned.

6) Once the request for VCU issuance is received, the corresponding EFCUs are automatically cancelled and the issued VCUs are automatically transferred to the EFCU holder's account on the Verra Registry. In other words, the project proponent has no control over the destination of issued VCUs that are associated with EFCUs, with such VCUs being automatically transferred to the buyer's account.

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[2] For example, if a project's estimated annual emission reductions were 100 tCO$_2$e / year and the project proponent requested EFCU assignment for their first vintage year, then only 100 EFCUs could be assigned. If the project proponent requested EFCUs for its first five vintage years, then only 500 EFCUs could be assigned.

4   SUMMARY COMPARISON BETWEEN EFCUS AND VCUS

The table below provides a summary of the main characteristics of EFCUs as compared to VCUs.

	VCU	EFCU
Definition	A unit created and recorded in the Verra registry representing the right of an account holder in whose account the unit is recorded to claim the achievement of a GHG emission reduction or removal in an amount of one (1) metric tonne of CO_2 equivalent that has been verified by a Validation/Verification Body in accordance with the VCS Program rules. Recordation of a VCU in the account of the holder on the Verra registry is prima facie evidence of that holder's entitlement to that VCU.	A unit assigned by and held in the Verra registry representing the right of an account holder in whose account the unit is recorded to claim a VCU if and when it is issued in the future, the basis for which is the expected achievement of a GHG emission reduction or removal in an amount of one (1) metric tonne of CO_2 equivalent that has been validated verified by a Validation/Verification body in accordance with the VCS Program rules. Recordation of an EFCU in the account of the holder on the Verra registry is prima facie evidence of that holder's entitlement to that VCU if and when it is issued.
What underlies the unit?	A GHG emission reduction or removal in an amount of one (1) metric tonne of CO_2 equivalent	An expected (future) GHG emission reduction or removal in an amount of one (1) metric tonne of CO_2 equivalent
Does a VVB assess the basis upon which the unit is issued/assigned?	Yes. A VCU may be recorded only after the actual GHG emission reduction or removal has been verified, and an EFCU may be recorded only after the estimated GHG emission reductions or removals have been validated.	
Does Verra engage in the contracting process for buying/selling the unit?	No. If the seller or buyer renege on any terms in bilateral contracts related to the asset (VCU or EFCU), it is up to the counterparties to resolve potential disputes on their own.	
Is the unit crafted in a bespoke manner to fit any contractual specifics between buyer and seller?	No. The definition of the unit and what it represents is standardized, and the registry functionality that sits behind a VCU and EFCU is fundamentally the same for all units issued/assigned.	

5   REGULATORY CONSIDERATIONS

Verra has engaged legal counsel to assist in determining whether EFCUs may be subject to regulation by either the U.S. Securities and Exchange Commission (SEC) or the Commodity Futures Trading

Commission (CFTC). In particular, Verra is examining whether EFCUs might be exempted from regulation as forward contracts or whether they might be subject to regulation as securities or swaps.

Verra will address the regulatory status of the EFCUs in our eventual rules.

6   REQUEST FOR INPUT

Verra requests input on the following EFCU design considerations:

1) Do you think the EFCU is a helpful concept and for what situations or use cases do you think such a unit might be most useful?

2) Is the name, Early Finance Carbon Unit (EFCU), fit for purpose? Other options considered included "Projected Carbon Unit", "Prospective Carbon Unit", and "Early Finance Unit".

3) Should Verra restrict EFCU volumes to a percentage of a project's estimated annual emission reductions/removals to mitigate underperformance risks of projects? If so, should such conservative estimates of EFCUs be related to specific project risks (e.g., based on type of project, location, reversal risk rating, time to VCU issuance [vintage])?

4) Should Verra require that EFCUs be linked to specific vintages or should these be aggregated over the corresponding time/crediting period? For example, should an ARR project that was projected to generate verified emission removals according to the schedule below be required to link EFCUs (and eventual VCUs) to each of the vintages, or should it be allowed to transact 1,000 EFCUs without vintage indications/constraints?

Years	Projected Emission Reductions /Removals
1-5	0
6	100
7	150
8	200
9	250
10	300
Total	1,000

5) In the case of project underperformance, should VCU delivery be on a first-come, first-served basis (i.e., EFCU holders would be first in line for any issued VCUs regardless of the associated vintages), or should VCU delivery be proportional to the EFCUs assigned for a given vintage, or entire monitoring, period (so all buyers share risks and potential underperformance losses equally)?[3]

6) For how many years into the future should Verra permit projects to issue EFCUs? Full project crediting period? 5 years? 10 years? 30 years? Should different project types have different restrictions? For example, should biosequestration projects, for which it may take decades to generate substantial verifiable removals, be allowed to create EFCUs for periods further into the future than other project types?

7) Should EFCUs expire after a certain date (e.g., associated with their expected vintage or monitoring period) if they have not been converted into VCUs by then? For example, if a project consistently underperforms over several years and issues a lot fewer VCUs than EFCUs, should the "over-assigned" EFCUs expire after a certain date? If so, what might that date be (e.g., five years after first verification)?

8) Should Verra incorporate new functionality into the registry that would enable a project proponent to enter the Verra Registry account ID of a buyer of EFCUs so that when VCUs are issued they are automatically transferred to the buyer's account?

9) How important is it that the EFCU could be traded (e.g., in secondary markets) beyond the original asset holder and would the legal characterization of an EFCU (e.g., as a security, swap or forward contract) materially impact the decision to purchase an EFCU?

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[3] For example, imagine a project proponent has transferred 100 EFCUs to Buyer A and subsequently 100 EFCUs to Buyer B for a specific vintage period. The project conducts verification and the VVB verifies that only 150 emission reductions were generated during that vintage period. One option would be that Buyer A receives 100 VCUs and Buyer B receives the remaining 50. Alternatively, both Buyer A and Buyer B could receive 75 VCUs. In any case, note that Verra would take no responsibility for resolving any contractual consequences of project underperformance.

ANNEX 1: VERRA REGISTRY FUNCTIONALITY

Updates to Verra Registry functionality would include (a) adding the option to create EFCU registry records, (b) establishing new functionality to facilitate EFCU holdings, and (c) creating public reports that would provide details on volumes of EFCUs assigned and cancelled, dates of registry and cancellation, beneficiary information, etc.

With respect to EFCU assignment functionality, it is envisioned that this would be very similar to the current VCU issuance functionality,[4] with a few changes as described below:

1) For a given VCS project record, it will be necessary for a project to have the option to request EFCU assignment in addition to current functionalities (e.g., requesting registration and VCU issuance).

2) When creating a new EFCU assignment request, new fields may need to be created, such as enabling the project proponent to enter the buyer's Verra Registry account ID as a means to facilitate the automatic transfer of EFCUs to the buyer's account. Additionally, new automated checks will need to be created such that the validated estimated annual emission reductions/removals for the project act as a limit on the volume of EFCUs that can be requested. A new serial number format will also need to be designed to facilitate the serialization of EFCUs. Most other fields will be the same as the VCU issuance request screens (i.e., verification period, vintage period, etc.).

3) New functionality will need to be created in order to facilitate EFCU cancellation and automatic VCU transfers where a VCU issuance request is made for a batch of VCUs tied to an EFCU record.

With respect to new functionality to facilitate EFCU holdings, it is also envisioned that this would be very similar to current VCU holdings functionality, with a few changes as described below:

1) New reporting screens would need to be designed such that Verra Registry account holders could clearly see the volumes of EFCUs held and with which projects they are associated. Likewise, project proponents will need to clearly see the volumes of EFCUs already transferred to buyers.

2) New reports will also need to be created such that the history of EFCU transfers and cancellations can easily be viewed and downloaded by account holders.

With respect to creating public reports, it is envisioned that these will be similar to the existing public reports for VCU issuance records. However, it is likely that some account holders may wish to keep their EFCU assignments and holdings records private.

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[4] See the Verra Registry User Guide for further information on current VCU issuance functionality.