

# ERCST DISCUSSION PAPER

## *Introduction of International Credits in the EU Climate Change Framework*

### Authors

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# **Introduction of International Credits in the EU Climate Change Framework**

## **1. Objective of the Paper**

The objective of this new initiative is to explore the technical criteria, barriers and potential solutions for the establishment of a regulatory framework that permits the use of high-quality international carbon credits within the EU climate change policy toolbox. This paper, which will be developed through an iterative process with a limited number of stakeholders, is intended to serve as an intellectual backstop for a discussion that will continue past its May 12 launch.

Specifically, it examines the technical criteria that could be used to permit the use of high-quality international carbon credits within the EU climate policy framework. To this end, it develops a strict set of criteria to ensure that only credits from projects with robust climate, social, and environmental benefits are included. The initiative also especially seeks to ensure that the integration of international credits does not undermine the stability or environmental integrity of the ETS.

This paper is not intended as an in-depth study of the Why, Where or How international credits can play a role in the EU climate change policy framework, but rather as an attempt to capture the headlines and options that would underpin the logic and the arguments, and provide an initial idea on how such an approach could be tested.

## **2. Background**

### **2.1 Broader Context**

The EU has a long-standing history of integrating international credits into its climate change policy framework. During its first and second trading phases, for instance, the EU ETS allowed the use of Clean Development Mechanism (CDM) and Joint Implementation (JI) credits. However, a number of factors, including the lack of stringent criteria, both quantitative as well as qualitative, impacted the carbon price in the EU ETS in a manner that undermined its ability to achieve its objectives. Consequently, the EU largely discontinued the eligibility of credits issued under the Kyoto Protocol starting in 2012 for CDM second commitment period credits and selected methodologies.

Any discussion about opening up the EU climate framework to international credits will take place against the backdrop of contextual realities and evolving developments, which will influence both the substance and tone of the debates.

The European Climate Law Regulation explicitly emphasizes domestic mitigation only, a limitation strongly supported by significant stakeholders, including civil society. However, unlike previous debates about integrating international credits, the upcoming discussions will benefit from a richer repository of past experiences, lessons learned, and best practices within the EU and other jurisdictions, as detailed further in Section 2.2. For instance, California's cap-and-trade system incorporates offsets subject to strict criteria, thus maintaining environmental integrity. Similarly, Norway, Switzerland, and Singapore have successfully integrated high-quality international credits into their national targets, providing useful models for the EU. Japan, South Korea, and Türkiye are currently considering the inclusion of international credits under Article 6 of the Paris Agreement, while other jurisdictions, such as Colombia, Mexico, and South Africa, already permit offsets within their national carbon tax systems.

In the context of the UNFCCC negotiations, the Rulebook of Article 6 became operational at the recent international climate summit in Baku, Azerbaijan. Here, the EU successfully secured most of its demands regarding environmental integrity assurances and procedural clarity under Articles 6.2 and 6.4 of the Paris Agreement.

Competitiveness and affordability have become increasingly significant – and potentially critical – issues under the new European Commission. The impact of the ETS 2 on consumers has emerged as an especially prominent concern, alongside the ongoing implications of the ETS 1 on EU industrial competitiveness, particularly as decarbonization pressures increase and traditional leakage safeguards are phased out in favor of novel, yet untested, approaches.

The acceptance or use of credits is also being discussed in relation to various obligations under different EU legislative frameworks, such as the Corporate Sustainability Reporting Directive (CSRD), the Green Claims Directive, and the Carbon Border Adjustment Mechanism (CBAM).

Furthermore, liquidity in the EU ETS is becoming problematic, with expectations that liquidity will reach zero by 2039 – or potentially by 2045, contingent upon aviation inclusion. Credits, more broadly, are thus being considered to help address this issue. Additionally, the EU aims for net-zero emissions in the broader economy by 2050 and within the EU ETS by 2039 or 2045. However, at that point, process emissions are anticipated to remain around 400 million tonnes. Therefore, removal credits, whether domestic or international, will be indispensable in the ongoing discussions.

These considerations have fostered active debate on international credits within European institutions, individual Member States, and among various stakeholder groups. Notably, during African Climate Week in September 2023, European Commission President Ursula von der Leyen endorsed using "true carbon credits" to unlock significant resources for climate action in Africa.<sup>1</sup>

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<sup>1</sup> [https://ec.europa.eu/commission/presscorner/detail/en/speech\\_23\\_4344](https://ec.europa.eu/commission/presscorner/detail/en/speech_23_4344).

Similarly, Peter Liese, a Member of the European Parliament and one of the European People's Party's senior climate policy experts, has called "major flexibilities" essential to achieve the ambitious EU emissions target for 2040, including "[l]imited inclusion of high quality third country certificates."<sup>2</sup>

At the Member State level, the draft Coalition Agreement presented by the German Christian Democratic and Social Democratic Parties in April 2025 supports meeting European and German climate targets through "limited use of ... highly qualified and credible emission reductions in non-European partner countries."<sup>3</sup> At a high-level conference in Paris in February 2025, French government officials advocated utilizing Article 6 of the Paris Agreement to bolster European climate ambitions.<sup>4</sup>

Lastly, the New Collective Quantified Goal (NCQG) on climate finance, agreed in Baku last year, calls for substantial international climate finance transfers from public and private sources—at least USD 300 billion annually by 2035, potentially mobilizing up to USD 1.3 trillion per year. Carbon finance through international mitigation project credits is viewed as a vital mechanism to fulfill these commitments, especially amid constrained public budgets and limited fiscal capacity.

## 2.2 Use of International Credits in other Jurisdictions

A survey of carbon pricing systems around the world shows that international credits are already accepted in a growing number of jurisdictions. This use of international credits is driven by national carbon pricing regimes that recognize offsets towards compliance, as well as corporate net-zero and voluntary strategies that have been supplied by voluntary and CDM credits. More recently, Article 6 pilot activities have begun establishing a broader framework for international credits for NDC compliance and voluntary offsetting.

These expanding practices further support consideration of international credits under the EU ETS to avoid competitive asymmetries and an imbalance in the treatment of European emitters vis-à-vis their international counterparts. What is more, these other jurisdictions are building experience, defining best practices and setting regulatory frameworks, giving them a lead that will only expand as Europe rejects crediting under the EU ETS. Specifically, the following jurisdictions already allow, or are actively considering, use of international credits subject to varying conditions.

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<sup>2</sup> <https://peter-liese.de/en/32-english/press-releases-en/4322-90-target-for-2040-extremely-ambitious-and-not-possible-without-flexibilities>.

<sup>3</sup> "in begrenztem Umfang ... hochqualifizierte und glaubwürdige CO<sub>2</sub>-Minderungen in außereuropäischen Partnerländern", see paras. 905-906 in <https://www.koalitionsvertrag2025.de/sites/www.koalitionsvertrag2025.de/files/koalitionsvertrag.pdf>.

<sup>4</sup> <https://www.tresor.economie.gouv.fr/Articles/2025/02/20/high-level-conference-on-carbon-border-adjustment-mechanism-cbam>.

### **2.2.1 Australia**

Australia's reformed Safeguard Mechanism (2023) allows liable facilities to surrender domestic Australian Carbon Credit Units (ACCUs) or internally generated Safeguard Mechanism Credits. While the rules currently state that "the Safeguard Mechanism does not allow the use of international offsets", a statutory review in 2026-2027 will reconsider that position; until then, compliance is met entirely with domestic units (7.1 million ACCUs were surrendered in 2023-24).

### **2.2.2 New Zealand**

A paragraph on "use of market mechanisms and cooperative approaches" in New Zealand's NDC states that it "intends to use international carbon markets with environmental integrity" to supplement domestic action. The country's carbon budget for 2021-2030 implies a 149 Mt CO<sub>2</sub>-eq gap that could partly be closed with ITMOs if domestic options prove insufficient.

### **2.2.3 Japan**

The forthcoming national GX-ETS carbon pricing system will accept credits from the bilateral Joint Crediting Mechanism (JCM); detailed rules on volume limits are still being finalized, but the Basic Plan states that JCM units will count toward compliance once the scheme becomes mandatory in Fiscal Year 2026. Uptake is expected to be modest at first because JCM supply is limited and the ETS begins with a voluntary, learning phase. At the national level, Japan's updated NDC explicitly says the government will "establish and implement the Joint Crediting Mechanism (JCM) ... and use such contributions to achieve Japan's NDC," thereby drawing on ITMOs transferred under Article 6.2. Cabinet plans aim for about 100 million t-CO<sub>2</sub> of cumulative reductions by 2030 through JCM projects in 29 partner countries, with all tons subject to corresponding adjustments recorded in Japan's initial Article 6 report to the UNFCCC in 2024.

### **2.2.4 Türkiye**

Türkiye's planned pilot ETS (TR-ETS) is still at the design stage; authorities are exploring a domestic crediting system and potential links to Article 6 of the Paris Agreement, but no decision has yet been taken on whether international units will be eligible. Consequently no credits have been used to date.

### **2.2.5 Republic of Korea**

The Korean ETS (K-ETS) allows covered entities to meet up to 10% of their compliance obligation with offset credits, of which a maximum of 5% may be international and only

from projects in least-developed countries or Korean-led CDM activities; this limit falls to 5% total in Phase III (2026-30). Firms routinely exhaust the quota, making Korea a major system with steady international-credit demand.

Korea's updated 2021 NDC also notes that Korea "will utilize ITMOs under Article 6 as a complementary measure to its domestic mitigation efforts" to reach a 40%-below-2018 target. It has earmarked up to 89 Mt CO<sub>2</sub>-eq of overseas reductions by 2030, reflecting its longstanding policy of buying offsets from Least Developed Country (LDC) partners.

### **2.2.6 California**

Covered entities may use compliance offsets for 4% of 2021-2025 emissions and 6% from 2026-30; at least half must provide "direct environmental benefits" to California, effectively restricting many overseas projects. Offset use has dropped sharply – from 13% of retirements in 2017 to about 5% in the 2022 surrender cycle – as limits tightened and prices converged with allowances.

### **2.2.7 Sweden**

While Sweden is bound by the EU ETS rules (under which offsets are no longer eligible), it pursues supplementary mitigation for its national climate goals through a government-backed Article 6 program run by the Swedish Energy Agency. In July 2023 the Government triples the program's budget to SEK 1.5 billion through 2032, aiming to acquire high-integrity ITMOs from developing-country projects; purchases are still in the piloting phase, so no credits have yet been counted toward Swedish targets.

### **2.2.8 Norway**

As a full participant in the EU ETS, Norway follows the Phase IV rule that prohibits any international (or domestic) offset use after 2020; earlier, operators had exhausted the 11% CER/ERU quota available through 2020. Offset use has by now ceased.

At the national – rather than installation – level, Norway launched the Norwegian Global Emission Reduction (NOGER) Initiative in November 2024, authorizing up to USD 740 million to purchase emission reductions in developing countries and to mobilize private co-investment. ITMOs will be used to cover any gap in delivering Norway's 2030 NDC – currently aligned with the EU-wide-55% goal – and to help achieve the separate national pledge of climate-neutrality from 2030.

### **2.2.9 Singapore**

From 1 January 2024, carbon-taxed facilities may cancel high-integrity International Carbon Credits for up to 5% of taxable emissions. Credits must satisfy Singapore's

Article 6-aligned ICC Framework; demand is only just emerging as the tax rises from SGD 5 to 25 t-CO<sub>2</sub>e.

### **2.2.10 Switzerland**

Since linking with the EU ETS in 2020 the Swiss ETS mirrors EU rules: no offsets of any kind are now accepted. Companies relied heavily on CERs before 2021, but the market has since closed.

Switzerland has embedded Article 6 cooperation at the heart of its 2030 NDC, which aims to cut emissions by 50% below 1990 levels, “primarily at home but supplemented by mitigation abroad.” The Federal Office for the Environment has already ratified bilateral Article 6.2 agreements with more than a dozen partner countries (Peru, Ghana, Senegal, Thailand, Chile, etc.) to secure ITMOs, and publishes authorized project lists online. The government intends to reduce – though not eliminate – reliance on ITMOs after 2030 as domestic decarbonization accelerates.

### **2.2.11 Colombia**

Fuel suppliers can reduce their carbon-tax liability through the “non-causation” mechanism by cancelling eligible domestic or international credits, but a 2022 tax reform capped this avenue at 50% of the tax due. Offsetting remains popular: in most years more than two-thirds of liabilities have been met with credits, channeling finance into forestry and REDD+ projects.

### **2.2.12 Mexico**

The forthcoming operational phase of Mexico’s national ETS will allow covered installations to meet up to 10% of their surrender obligation with offset or “early-action” credits generated by projects inside Mexico. Credits must be validated under recognized international or domestic protocols and cancelled in their original registry before SEMARNAT issues fungible units; international units generated outside Mexico will not be eligible. Because the system has been running only in pilot mode, no offsets have yet been surrendered and the detailed rules are still being finalized.

### **2.2.13 South Africa**

Phase I of the Carbon Tax (2019-2025) allows firms to use offsets for 5% (process and fugitive emissions) or 10% (combustion) of taxable emissions; only projects located inside South Africa qualify, though they may be certified under CDM, VCS or the Gold Standard. Up to 90% of large emitters are expected to claim the allowance, making domestic offset supply a policy priority.

#### **2.2.14 United Arab Emirates (UAE)**

The UAE has no domestic carbon price yet, but its third NDC (2024) sets up a national registry and accounting framework to trade ITMOs under Article 6, pledging robust double-counting safeguards. The NDC states that the UAE “may consider” using such cooperation to meet part of its target, signaling future demand, yet commits primarily to domestic reductions; implementation is still in the design phase and no credits have been applied so far.

#### **2.2.15 Kuwait**

Kuwait’s updated first NDC (2023) aims to avoid 7.4% of BAU emissions by 2035 and explicitly “hopes that... market, non-market mechanisms, and cooperative approach under Article 6” will supply finance and technology. With no national carbon pricing instrument, participation in international crediting remains prospective and has not yet generated usable units for compliance.

#### **2.2.16 Monaco**

Monaco has neither its own ETS nor access to the EU ETS, but bilateral discussions in 2024 with Tunisia and Morocco were held “within the framework of Article 6 ... which allows States to enter into voluntary cooperation to achieve their national climate objectives.” The principality therefore intends to meet part of its 55%-by-2030 mitigation pledge through ITMOs from partner countries; operational modalities and volumes are still under negotiation.

### **3. Why Should International Credits Be Included in the European Climate Change Policy Framework?**

More broadly, there are other important reasons, with implications beyond the EU current legislation, that would militate for the consideration of international credits under the EU climate change framework:

#### **3.1 Enhanced Level of Ambition in the EU NDC**

The EU NDC has 3 elements: ETS, ESR and LULUCF. Meeting targets in all these segments can be achieved also though including international credits as compliance mechanisms. The method of integration will differ between the three areas.

Currently the EU must, according to the Climate Law, reach climate neutrality by 2050 and have to come with a new NDC (for 2035 and voluntary for 2040) that should be informed by first GST and submitted six months after the GST). The EU was planning to

issue this new NDC in Q1 2025, that would include a new 2040 target for the Belem COP but was postponed, without a specific date being mentioned, which also takes into consideration political events in the EU.

In February 2024, the European Commission presented its assessment for a 2040 climate target for the EU. The Commission recommended reducing the EU's net greenhouse gas emissions by 90% by 2040 relative to 1990. However, there has been vocal opposition from a variety of stakeholders to a flat 90% target. Some stakeholders have argued that part of the 90% should be done through international credits. This was also mentioned in the new political agreement that led to the formulation of the new German government. The integration of international credits can be seen as a way to allow for an increased level of ambition without hurting competitiveness further.

### **3.2 Enhancing Competitiveness and Flexibility**

While the passing of the EU Green Deal has dominated the previous Commission, competitiveness has become a central plank of the new EC, as seen through the measures in the Clean Industrial Deal and the Antwerp Declaration.

It is also becoming quite clear that many jurisdictions are allowing or planning to allow international credits in the existing or nascent carbon markets which will impact the competitiveness of its industry covered by these carbon markets.

This will lead to a situation where the EU may be one of the few jurisdictions not to be involved in the international credit market in achieving at least part of its NDC, which may be put its industry, currently already under tremendous competitive pressure, at a further disadvantage. The introduction of international credits, depending on how its done, can contribute to the competitiveness of EU industry and provide flexibility to meet compliance obligations with commitments at EU level.

### **3.3 EU ETS Liquidity Concerns**

Liquidity in the EU ETS is not an immediate concern, but at the same time one that has been widely acknowledged in the policy debate in the EU. It is anticipated that by 2039, in its current form, the EU ETS will reach zero allowances. With the inclusion of aviation that date is extended to 2040s. This being an objective mathematical situation, the market will anticipate the situation and there will be a liquidity problem, with consequences for good market functioning before that.

The introduction of credits, domestic and/or international, is seen as a potential way to address a very real and important problem, even if they are restricted to certain categories, such as CDRs.

### **3.4 Mobilizing Private Finance for Decarbonization**

By creating a demand for high-quality carbon credits, the EU could catalyze investments in climate mitigation projects globally, particularly in developing countries.

The initiative could help direct private capital into projects that are not typically supported by mainstream finance, which remains slow outside of the energy, buildings, and transport sectors. AFOLU, including soil restoration, industry, and water and wastewater sectors have a large mitigation potential; however, their climate investment levels have remained low from 2018 to 2022.

Further, the initiative could help direct private capital into projects such as nature-based solutions and community-led initiatives, which would have a transformative impact particularly in Least Developed Countries (LDCs).

Nature-based solution projects represent 52% of LDC-sourced carbon credits, and LDCs have significant land-based mitigation potential, equal to 70% of global aviation's 2019 CO<sub>2</sub> emissions. Cambodia, Democratic Republic of Congo, Bangladesh, Uganda, Malawi, Zambia, Nepal, and Myanmar are amongst the more active players.

Further, LDCs are among the early movers under Article 6.2 of the Paris Agreement:

| LDC host                         | Buyer(s)                              |
|----------------------------------|---------------------------------------|
| Bangladesh                       | Japan                                 |
| Cambodia                         | Japan, Singapore                      |
| Ethiopia                         | Japan                                 |
| Lao People's Democratic Republic | Japan, Republic of Korea              |
| Malawi                           | Switzerland                           |
| Myanmar                          | Japan                                 |
| Nepal                            | Sweden                                |
| Rwanda                           | Kuwait, Singapore                     |
| Senegal                          | Japan, Norway, Singapore, Switzerland |

Source: UNCTAD, based on information in the Article 6 pipeline database of the UNEP Copenhagen Climate Centre, available at <https://unepccc.org/article-6-pipeline> (accessed 3 July 2024).

Development finance and climate finance delivered through bilateral and multilateral channels have proved insufficient to fund the investment needs of least developed countries (LDCs) for meeting their goals in key areas of sustainable development. Consequently, it is believed that carbon markets, and the mobilization of private finance, could be a possible source of additional finance for this purpose.

Accelerating clean energy transitions around the globe is essential to avoid catastrophic global warming and to achieve universal access to clean and affordable energy. Decarbonization hinges on the rapid transformation to zero-carbon electricity, mainly through the deployment of wind, solar, hydroelectric, geothermal, and other non-carbon primary energy sources. This transformation depends substantially on the terms of finance for zero-carbon energy. If finance for decarbonization is ample and at low cost, decarbonization will proceed rapidly – not only because it is desirable for climate change, but also because it is a low-cost, and often the lowest-cost, source of electricity.

If finance for decarbonization is at high cost, the burden of decarbonization is much higher – because fossil-fuel-based power is then typically cheaper and easier to finance. The public sector will have to leverage several hundreds of USD billions of private investments per year to enable low-carbon development limiting global warming to 2 degrees Celsius.

This is very much in line with Art 2.1c of the Paris Agreement which stipulates that the Paris Agreement, in enhancing the implementation of the Convention, including its objective, aims to strengthen the global response to the threat of climate change, in the context of sustainable development and efforts to eradicate poverty, including by making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

It must be emphasized that it is becoming clear, especially with the withdrawal of the US from the Paris Agreement, that the availability of public finance has been reduced and needs to leverage private sector finance. In 2022, US contributions accounted for 12% of developed countries' climate finance through bilateral channels and multilateral climate funds. On the other hand, the private sector needs to see an incentive to provide this finance and carbon markets and international credits could be that instrument. Some estimates suggest that carbon markets under the Paris agreement could grow to \$300bn per year by 2030 and up to \$1tn per year by 2050.

### **3.5 Contributing to International Climate Finance Obligations**

Finance through international carbon markets could contribute to the 300 billion NCQG, which can be provided from a wide variety of sources, public and private, bilateral and multilateral, including alternative sources. Carbon markets can serve as an alternative source of funding for climate-related projects, offering additional financial resources beyond traditional development aid or foreign direct investment.

Carbon Markets can provide funding through:

- **Revenue Generation:** Carbon credit sales generate revenue that can be used to finance new climate or biodiversity projects.
- **Incentive for Mitigation:** The price of carbon credits can incentivize companies and organizations to reduce their emissions, leading to further emission reductions.
- **Additional Finance:** Funds raised from carbon credit sales can be used to develop new climate or biodiversity projects that would not have been possible otherwise.

The CDM experienced showed that the CDM leveraged private investment 10 times the public funds allocated.

International cooperation through carbon markets could significantly reduce NDC compliance costs, i.e. \$250 billion annually by 2030, and could exceed USD 1 trillion by 2050.<sup>5</sup>

Article 6 of the Paris Agreement, specifically sections 6.2 and particularly 6.4, can also unlock financial support for adaptation. This is achieved through mechanisms like cooperative approaches and the Paris Agreement Crediting Mechanism (PACM), which can generate resources that can be directed towards adaptation efforts, including contributions to the Adaptation Fund.

CMA 6 provided for the possibility of raising alternative funds for the Adaptation Fund (AF) by advancing the operationalization of Article 6.4 of the Paris Agreement and establishing a 5% share of proceeds to the AF from the sales of carbon emission reduction project credits. In the long term, it can also be considered on a voluntary basis under Article 6.2.

### **3.6 Strengthening EU Leadership in International Carbon Market Development**

The EU has been a leader in carbon markets as the introduction of the EU ETS in 2005. It then allowed international credits in the EU ETS through the so-called Linking Directive (Directive 2004/101/EC). The total number of international credits exchanged since between March 2014 and April 2021 amounts to 506.3 million. The termination of the Linking Directive in 2021 was primarily due to what was perceived as the influence of international credits on EUA prices, which lead to price increase from a low of EUR 9 in January 2019 to EUR 89 in January 2022. Another serious concern was the fact that many of the credits that entered the EU originated from technologies and regions that the EU did not find appropriate.

The EU has continued to make carbon markets an Important element of Its climate change policy and climate diplomacy through the establishment of the new Unit – Clima Task Force International Carbon Pricing and Markets Diplomacy and the introduction of CBAM, which the EU credits with the upcoming ETS in places such as Brazil and Türkiye. Allowing international credits in the EU climate framework, which may or may not include the EU ETS, will provide a significant boost to the Art 6 mechanism which is currently suffering from a lack of demand. The EU ETS, an established and credible mechanism would certainly provide a big boost to the use and credibility of Art 6.

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<sup>5</sup> See, e.g., the range of estimates in James E. Edmonds, Sha Yu, Haewon McJeon, Dirk Forrister, Joseph E. Aldy, Nathan Hultman, Ryna Cui, et al. 'How Much Could Article 6 Enhance Nationally Determined Contribution Ambition toward Paris Agreement Goals through Economic Efficiency?' *Climate Change Economics* Vol. 12, No. 2 (2021): 2150007. <https://doi.org/10.1142/S201000782150007X>; Pedro Piris-Cabezas, Ruben N. Lubowski, and Gabriela Leslie. 'Estimating the Potential of International Carbon Markets to Increase Global Climate Ambition'. *World Development* Vol. 167 (2023): 106257. <https://doi.org/10.1016/j.worlddev.2023.106257>.

### **3.7 Shaping the Framework for International Removal Credits**

Establishing a framework for utilizing international CDR credits within the EU's climate policy necessitates significant cooperation and the harmonization of robust technical standards beyond European borders. Central to this is the development and mutual recognition of stringent criteria for MRV systems applicable in diverse global contexts. Crucially, mechanisms must be instituted to prevent double counting of removals – ensuring they are not claimed by both the host nation under its climate commitments and by an entity purchasing the credit for use within the EU.

Beyond the technical specifications, a functional international framework requires effective governance structures and clear integration pathways. This includes establishing or accrediting independent bodies responsible for validating projects and verifying removals according to the agreed standards, alongside a reliable, interoperable registry system to track the issuance, transfer, and retirement of CDR credits globally. Furthermore, integrating these international credits into the EU's climate architecture demands clear rules on their eligibility, potential quantitative or qualitative limitations on their use within specific EU policies (like the EU ETS) and how they interact with EU and member state climate targets.

### **3.8 Contributing to International Climate Diplomacy**

The EU has also been a key player in the negotiations on Article 6 of the Paris Agreement and one could argue that it has obtained all the guarantees it wanted to ensure environmental integrity from both Art 6.2 and Art 6.4. As a strong supporter of the UNFCCC multilateral process, and multilateralism in general, the EU should have a vested interest that Art 6 takes is a success as an instrument for international cooperation in reaching NDCs. The success of Art 6 is linked with the points above on climate finance and EU ambition.

In addition, it is well documented the impact that Japan, through its JCM, has on climate diplomacy – this is an important element for the EU.

## **4. Where Should International Credits Be Included in the European Climate Change Policy Framework?**

The use of credits in general (implicitly domestic credits as spelled out in the EU Climate law), and by extension, also international credits, could be considered in the context of a number of policies and obligations that are currently in force in the EU, or will make the object of an examination in the process of EU policy formation, which are listed below:

### **4.1 Inclusion of International Credits at the EU Level**

#### 4.1.1 EU ETS Compliance

The EU ETS, a cornerstone of EU climate policy, drives cost-effective emissions reductions across industry and, with ETS2's 2027 launch, buildings, road transport, and additional sectors. Historically, from 2004 until 2020, international credits were permitted in the EU ETS, under the Kyoto Protocol (KP) (Article 25) mechanisms: CDM (Clean Development Mechanism) and JI (Joint Implementation)<sup>6</sup>. The Linking Directive (Directive 2004/101/EC) enabled compliance, with 1.6 billion credits used by 2020, the vast majority of which originated from China (422 million), Ukraine (212 million), Russia (130 million), and India (108 million)<sup>7</sup>. At the start of Phase 3 (2013-2020), the EU ETS was revised, with quantitative and qualitative limits were put in place on the credits that could be used<sup>8</sup>. This led to the halving of the use of international credits, dropping to 500 million in Phase 3, compared with over 1 billion in Phase 2 (2008 to 2012). The KP mechanisms have, undeservedly, a negative name in the EU and in the ETS1, being accused of being too cheap, not providing the environmental integrity the EU expected and partly being one of the causes of the price crash. These criticisms are, in our view, unfair and unwarranted and reflect overwhelmingly views that come from that section of stakeholders which are ideologically not favourable to markets in general, and international carbon markets. The true problem was identified as a design flaw, the lack of supply flexibility provisions in the ETS1 design, which was later addressed through the MSR.

Today, as the EU targets 90% emissions reduction by 2040<sup>9</sup>, facing liquidity shortfalls by 2039, ensure ETS2 affordability, and maintain competitiveness, international credits are reconsidered, with the ETS market being significantly larger and more mature. The European Commission's mandated reviews— Review of the EU ETS Directive (2026)<sup>10</sup>, ETS2 Implementation Review (2026), and CBAM and Leakage Review (2028)<sup>11</sup>—provide a legislative opportunity to bring about a concrete discussion to reintroduce high-integrity credits. Driven also, by a shift in their political feasibility, international credits were strongly endorsed in Germany's CDU-SPD coalition agreement (April 2025)<sup>12</sup>, which called supports the limited, credible non-EU credits to balance ambition with industrial viability, echoing similar calls for flexibility from MEP Peter Liese. ETS2's introduction of carbon prices to households raises concerns about affordability, particularly for low-income groups. This necessitates the need for mechanisms to mitigate price spikes, such as allowing use of international credits.

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<sup>6</sup> From [ERCST \(2024\)](#), Future of emissions trading in the EU: Coverage Analysis.

<sup>7</sup> From [European Commission \(2021\)](#), Report from the Commission to the European Parliament and the Council on the Functioning of the European Carbon Market in 2020 COM(2021) 962 final.

<sup>8</sup> For example, nuclear energy projects and forestry projects were not allowed. Only credits from eligible projects created after 2012 were allowed, except for projects in least-developed countries.

<sup>9</sup> From [European Commission \(2024\)](#), Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Securing our future – Europe's 2040 climate target and path to climate neutrality by 2050 COM(2024) 63 final.

<sup>10</sup> Art. 30 of [European Commission \(2003\)](#), Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community.

<sup>11</sup> [Regulation \(EU\) 2023/956](#) of the European Parliament and of the Council of 10 May 2023 establishing a carbon border adjustment mechanism.

<sup>12</sup> [Politico \(2025\)](#), German coalition deal backs EU's 90 percent climate target — with caveats.

#### **4.1.2 Green Claims Directive (GCD)**

The proposed Green Claims Directive (GCD) – on the substantiation and communication of voluntary environmental claims in business-to-consumer practices – explicitly includes climate-related claims in its scope. The GCD is still undergoing trilogue negotiations, being the third trilogue schedule for 10 June 2025. Climate claims are expected to be discussed in this.

The proposal – specifically in the positions of the European Parliament and the Council – foresees the possibility of two types of climate-related claims: (i) contribution claims; (ii) compensation/ off-set claims. For each, the proposal establishes minimum requirements for the substantiation and communication of these claims. A ‘contribution claim’ is a claim where the company claims to have contributed to climate action by purchasing carbon credits, but without using those carbon credits for balancing out a share of its emissions. An ‘offset claim’ is a claim where the company claims to have balanced out a share of its emissions by purchasing carbon credits.

While a final agreement is not adopted yet, the previous positions of the proposed GCD, specifically the Commission and the Council, were essentially silent – apart from a vague mention in recital (21b) – about the use of international carbon credits. Thus, potentially allowing climate-claims based on all type of high-quality carbon credits. On the other hand, the EP position introduced a restriction stating that the carbon credits used must be certified units issued in accordance with the EU Carbon Removals and Carbon Farming (CRCF) or other units in duly justified cases – i.e., schemes recognized by the Commission as part of the list of compliant schemes corresponding to at least equivalent requirements to those provided by CRCF.

As a consumer protection and marketing legislation, the GDC has the potential, if well designed, to create a framework of transparency, bringing confidence to the players, and to incentivize corporate climate action. The use of high-quality international credits could play a significant role meeting the voluntary corporate climate targets. Therefore, the GCD should explicitly allow claims based on all credible credit types.

#### **4.1.3 Corporate Sustainability Reporting and Due Diligence (CSRD/CS3D)**

The Corporate Sustainability Reporting Directive (CSRD), and its delegated regulation – i.e., the European Sustainability Reporting Standards (ESRS) – requires companies to disclose their ‘transition plan for climate change mitigation’, if they have one, explaining how the companies’ strategy and business model are compatible with the 1.5°C goal of the Paris Agreement and the objective of achieving climate neutrality by 2050 as established in the EU Climate Law (cf. Article 19a (1) and (2)(a)(iii) of CSRD and Disclosure Requirement E1-1 of ESRS). Furthermore, the Corporate Sustainability Due Diligence Directive (CS3D) also mandates companies “*to adopt*” and “*put into effect*” –

this last obligation is expected to be eliminated in the context of the Omnibus legislation – a transition plan for climate change mitigation, aiming to ensure, through best efforts, that the company's business model and strategy are compatible with the transition to a sustainable economy and the goal of limiting global warming to 1.5°C in line with the Paris Agreement ... (cf. Article 22 of CS3D).

To comply with this obligation, international carbon credits may play an instrumental role for companies aiming to mitigate their GHG emissions on the way to net zero, address residual emissions, or make positive climate contributions.

The CSRD mandates detailed disclosures of companies' environmental efforts, including the use of carbon credits. The directive requires that the use of carbon credits be reported separately to ensure transparency and prevent the misrepresentation of actual emission levels and reduction progress. Companies must disclose their use of carbon credits for GHG removals and mitigation projects under ESRS Disclosure Requirement (DR) E1-7. This includes disclosures for both GHG removals from projects a company develops or contributes to within its own value chain (i.e., insetting) and carbon credits purchased for offsetting. Regarding the latter, detailed disclosures on the quantity, type, location, and quality standards of carbon credits are required. This includes: (i) the total amount of carbon credits purchased (in metric tons of CO<sub>2</sub>e) that are verified against recognized standards and cancelled during the reporting period. Planned (future) cancellations and their contractual basis must also be disclosed; and (ii) the percentage breakdown (as a % of the total carbon credits reported) – i.e., share of carbon credits from reduction versus removal projects, types of carbon sinks (biogenic/nature-based or tech-based), share of carbon credits adhering to each recognized quality standard, share of carbon credits issued from projects in the EU, share of carbon credits qualifying as a corresponding adjustment under Article 6 of the Paris Agreement.

GHG emissions (E1-6) and GHG emission reduction targets (E1-4) must be reported separately from carbon credit disclosures (E1-7). This separation ensures that the use of carbon credits does not obscure actual emission levels or progress toward reduction targets. Additionally, carbon credits from insetting should be distinctly reported from those purchased for offsetting to avoid double counting.

#### **4.1.4 Storage Target under the NZIA**

The European Union's Net-Zero Industry Act (NZIA), which entered into force in June 2024, establishes the objective to bolster carbon capture and storage capabilities across the bloc. A key provision is the legally binding target to achieve at least 50 Mt of annual CO<sub>2</sub> injection capacity in geological storage sites within the EU by 2030. This target aims to create an EU-wide market for CO<sub>2</sub> storage services, address the current scarcity of available storage sites, and accelerate the deployment of carbon management

technologies. Notably, the regulation places a specific obligation on oil and gas producers operating within the EU. Companies holding production licenses under the Hydrocarbon Directive must contribute proportionally to achieving this 50 Mt storage capacity target, based on their share of EU oil and natural gas production.

High-quality international credits could potentially interact with NZIA in a meaningful way. Leveraging international credits might offer additional pathways to finance essential CO<sub>2</sub> storage infrastructure, enhance the cost-effectiveness of meeting long-term decarbonization goals, or provide flexibility for industries utilizing the infrastructure developed under the Act.

#### **4.1.5 Carbon Border Adjustment Mechanism (CBAM)**

Currently, CBAM allows for deductions of carbon prices already paid in the country of origin, provided these are in the form of direct carbon pricing mechanisms like taxes or ETS. The potential recognition of international carbon credits, such as those under Article 6 of the Paris Agreement, to offset CBAM obligations is under consideration. These credits, often generated through emission reduction projects in developing countries, could offer a flexible compliance option for importers. Proponents contend that with stringent standards and oversight, international credits could enhance global climate finance and support decarbonization efforts in developing countries.

However, allowing international carbon credits could weaken the incentive for exporting countries to establish their own domestic carbon pricing schemes. If importers can rely on credits from unrelated or loosely verified emission reduction projects, there may be less pressure on trading partners to adopt robust carbon pricing or emissions trading systems. This could undermine one of CBAM's broader strategic goals: to encourage global convergence around strong climate policies. Additionally, there are ongoing concerns about the environmental integrity of many international credits, particularly in ensuring they represent real, additional, and verifiable emission reductions.

As the EU continues to refine CBAM's implementation, it faces a delicate balancing: enabling fair global trade and climate finance while safeguarding the momentum of climate action worldwide. The CBAM review by the European Commission expected in July 2025 may address credit eligibility and their broader implications.

## **4.2 Inclusion of International Credits at the Member State Level**

Article 4 paragraphs 16 to 18 allow Parties to the Paris Agreement to submit a joint nationally determined contribution (NDC). To date, the European Union and its member states are the only parties to the Paris Agreement that have a joint NDC. [...] As a result, the EU member states do not have individual NDCs under the Paris Agreement. They, however, remain responsible for the emission levels allocated to each member state as part of an agreement whose terms have to be notified to the UNFCCC secretariat.

In the case Sweden will use supplementary measures such as Art 6 credits, to go beyond Sweden's share of the EU NDC, as outline above.

Another example is the French initiative “**Coalition for Paris-aligned and high integrity use of carbon credits**” which asks companies as potential buyers of Art 6.4 credits to commit to Net Zero target consistent with the Paris Agreement. It also asks these companies to choose high-integrity carbon credits, aligned with the Article 6.4 ambition. It is important to the French Govt to ensure that any carbon credits used fulfils the high environmental integrity principles laid out in the *G7 High Integrity Carbon Market Principles* and the *Call for Action on Paris Aligned Carbon Markets*, including in particular: alignment of crediting levels with the Paris Agreement temperature goal; additionality; permanence; prevention of leakage; robust and conservative monitoring and quantification methods; social, environmental and human rights safeguards; no double-counting of credits, among others.

Finally, a "German Upstream Certificate," officially referred to as a UER certificate, is a compliance option for German fuel suppliers to meet their greenhouse gas reduction targets. These certificates represent certified emission reductions achieved in climate protection projects within the upstream oil and gas production sector. Specifically, they allow companies to meet their greenhouse gas quota by up to 1.2% through these projects

## **5. Challenges in Including International Credits in the European Climate Change Policy Framework**

### **5.1 EU ETS Market Stability**

Everyone understands that the main concern with respect to the introduction of international credits in the EU climate change framework will focus on their impact on the EU ETS, as that instrument will naturally be considered a first target for examination. The concern will be about the impact on EUA prices, with stakeholders pointing out to the Linking Directive and the impact that CDM and JI credits had on EUA prices. A large inflow of relatively cheap credits could potentially depress allowance prices, weakening the incentive for domestic decarbonization and investment in low-carbon innovation within the EU. While the veracity of such claims is an issue for another debate, the

articulation of such concerns is an inevitable reality, and will need to be addressed in any proposal to allow international credits into the EU ETS.

## **5.2 Political Feasibility**

Under the current European Climate Law, meeting EU targets and its NDC is meant to be done through domestic migration efforts. There has been, and will continue to be, strong opposition within the EU institutions as well as from civil society, with respect to using international credits. The precedent of using CDM and JI and the outcomes will be brought in, and it is unlikely that any conditions/filters that will be put in place will satisfy those that are ideologically opposed to markets – and to whom international carbon markets are another step away from good and safe EU mitigation measures. What is essentially being questioned is Article 2 of the UNFCCC, which focuses on “stabilization of atmospheric GHG concentrations at levels and within a time frame that would achieve this objective” – therefore making this a global concern of emissions, rather than a local concern of reductions.

## **5.3 Impact on EU Climate Targets**

Without robust accounting and corresponding adjustments, both currently mandated in Article 6 of the Paris Agreement and its rule book, both the host country and EU actors might claim the same emission reductions, potentially undermining the environmental credibility of the EU ETS cap. Integrating international credits would also necessitate amendments to EU legislation such as the EU ETS Directive, Effort-Sharing Regulation, and the Climate Law, a legislative process prone to political deadlock and potential legal challenges at the European Court of Justice.

## **5.4 Supply/Demand Issues**

In the Kyoto Protocol market, the supply-demand balance was never an issue, with supply overwhelming demand which came from a limited number of places, primarily EU and Japan.

In the Paris Agreement, all Parties have NDCs, and it is unclear to many as to who will be buyers, and who will be sellers, and at what point in time. In addition, while Article 6 was largely made operational in Baku at COP 30, it has yet to start delivering supply in significant quantities, and still needs some time to take off, as well as a significant, solid and credible source of demand.

On the demand side, Japan, Korea and some other jurisdictions will provide demand. Other demand will come from ICAO as well as from voluntary commitments – but there is little literature to provide a global view on the likely scale of demand. Some of it is

proving controversial, such as the position of SBTi with respect to offsets, and does not provide stability.

On the supply side, significant efforts have been made by multilateral institutions and through other channels to help countries identify sectors of the economy that could benefit from carbon finance and participation in carbon markets. However, a global view on the potential supply that could emerge is still lacking, with emerging indicators largely fragmented and unclear.

While it is clear that including international credits into the EU climate change policy framework will add to global demand, qualitative and quantitative filters will be important, so speculating on the demand impact would again be misleading.

However, what is clear, is that before considering the inclusion of international credits in the EU climate change framework, a full assessment on the implications on the global demand/supply balance needs to be undertaken to understand its impact, including price impacts in the market.

## **5.5 Reputational Damage**

Ensuring that external credits represent real, additional and permanent emission reductions is difficult, and experience with CERs under the CDM has raised questions about additionality and over-crediting that could dilute EU-wide climate ambition. This makes, from a reputational point of view, the use of credits, and especially international credits, vulnerable to the weakest link in the carbon credit market – a problem in one project can get magnified by those that do not like carbon markets to a generalized credibility crisis.

Any high-profile event, such as the case in the CDM with human rights violations at a project in Central America, will cast a shadow on the whole carbon credit market. By association, this may translate into a reputational risk for those that use international credits as a compliance instrument, in this case in the EU ETS or any of the other uses that may be envisaged in the EU climate change policy framework discussed above in Section 4.

While many safeguards have been introduced in Article 6.2 and 6.4 to ensure that such incidents do not recur, nothing is fool-proof. A reputational attack on international credits can come as a result of an individual project failure or the failure of a standard or methodology, as was seen recently in the press, whether that was a fair and accurate statement of fact or not.

The international market, in terms of supply, through initiatives such as the ICVCM, has made significant efforts to ensure a reputational clean sheet. There will also continue to be risks associated with voluntary standards that will never be able to be completely mitigated.

Finally, the rent extracted from the production and use of international credits has been and will continue to be a reputational issue to which many will be sensitive to. The example that is cited are HFC credits under the CDM, which were produced at a very low cost and sold in the EU ETS market at EUA prices with a huge rent being extracted (\$.5 US vs 17 Euros). While such rent may be acceptable in the luxury goods market, this is not something that society is willing to tolerate when it comes to environmental compliance, no matter how much lip service is being paid to the efficiency of markets in a market economy.

## **5.6 Impact on other EU policies**

Once international credits are allowed to be used in certain EU instruments for decarbonization, there will be – not illegitimate – demands that such an approach be mirrored. The classic example would be how the use of international credits in the EU ETS will result in calls for allowing the same to meet CBAM obligations of exporters to the EU. Depending on how it is done, it will impact the incentive to introduce carbon pricing in the form of an ETS or carbon taxes in jurisdictions that export to the EU.

# **6. How to Include International Credits in the European Climate Change Policy Framework**

## **6.1 Mitigating Challenges to the Inclusion of International Credits**

Integrating international project-based credits into the European climate change policy framework presents a range of challenges, as outlined in Section 5. To address these concerns, a suite of policy options can be employed to ensure that any use of external credits upholds the environmental integrity and political credibility of affected European climate policies. The following subsections elaborate on each mitigation strategy, building on past lessons and existing policy frameworks to facilitate the inclusion of high-quality international credits without undermining EU climate policy ambitions.

### **6.1.1 High-Integrity Standards**

One critical option to address the challenges identified in the previous section is to impose high-integrity standards on all international credits admitted into the European climate change policy framework. This means only allowing credits that meet stringent criteria for additionality, accurate measurement, verification, and permanence. Past experiences underscore why rigorous standards are needed: for example, a significant share of credits issued under the Kyoto Protocol through Joint Implementation project activities and used for compliance within the EU ETS was later found to lack

environmental integrity, potentially undermining EU ETS emissions targets by roughly 400 million tonnes.<sup>13</sup> Likewise, certain CDM projects (such as HFC-23 industrial gas destruction) generated spurious credits – project operators earned windfall profits for destroying gases that would not have been emitted if not for the incentive of credits.<sup>14</sup> These cases illustrate the risks inherent to low-quality credits and justify applying a strict screening process for eligible credits. In particular, a focus should be placed on ensuring that credits come from projects which do not result in negative social or environmental outcomes, such as displacement of local communities or biodiversity loss. Implementing high-integrity standards could involve establishing an EU-administered framework of quality control, or leveraging existing mechanisms with robust oversight. For instance, credits issued under Article 6.4 of the Paris Agreement will be subject to internationally agreed rules on baselines and additionality, which are being designed to reflect best-practice principles. To this end, the EU could require that any international credits used for compliance be verified under such approved mechanisms or under an EU-sanctioned certification scheme. This may include only accepting credits that adhere to independent principles such as the “core carbon principles” developed by the Integrity Council on the Voluntary Carbon Market, or have been validated by reputable standards such as the Gold Standard and are aligned with Paris Agreement criteria. An independent regulatory body or expert panel could vet projects for additionality, monitor reporting methodologies, and reject credits from project types with high risks of non-permanence or leakage.

### 6.1.2 High-Impact Criteria

In tandem with the foregoing integrity requirements, the EU could adopt high-impact criteria to filter international credits, prioritizing those that maximize genuine environmental and social benefits. Not all carbon credits are equal in their impact on global emission reductions. To avoid credits that merely shift emissions or deliver minimal benefits, regulators can set criteria that favor projects with clear, substantial contributions to mitigation and sustainable development. For example, crediting could be restricted to project types that support long-term transformational change (such as breakthrough clean technologies, critical infrastructure in developing countries, or carbon removal through afforestation, ecosystem restoration, and regenerative agriculture) rather than one-off incremental improvements. Emphasis might be placed

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<sup>13</sup> Anja Kollmuss, Lambert Schneider, and Vladyslav Zhezherin, *Has Joint Implementation reduced GHG emissions? Lessons learned for the design of carbon market mechanisms*. Stockholm: Stockholm Environment Institute, 2015. <https://www.sei.org/publications/has-joint-implementation-reduced-ghg-emissions-lessons-learned-for-the-design-of-carbon-market-mechanisms>.

<sup>14</sup> Stephanie La Hoz Theuer, Maia Hall, Alexander Eden, Emma Krause, Constanze Haug, and Stefano De Clara, *Offset Use Across Emissions Trading Systems*. Berlin: ICAP, 2023. <https://icapcarbonaction.com/en/publications/offset-use-across-emissions-trading-systems>.

on credits from carbon removal projects or those that achieve permanent sequestration of CO<sub>2</sub>, given their importance for reaching net-zero targets. This would address the challenge that some offsets may only delay emissions (or risk reversals), by steering usage toward projects with durable climate impacts.

Another high-impact measure would be to ensure that credit use leads to an overall mitigation in global emissions (OMGE) beyond simple offsetting. Under Article 6.4 of the Paris Agreement, a portion of credits will be mandatorily cancelled (at least 2%) to guarantee a net atmospheric benefit. The EU could mirror or exceed this practice by, for instance, applying a discount factor to all international credits used towards compliance with European climate change policies (e.g. requiring surrender of 1.1 credits for each tonne of emissions covered by the EU ETS) or by voluntarily cancelling a share of purchased credits. Such an approach ensures that international trading contributes to a net decrease in global emissions, addressing the concern identified in Section 5 that offsets might otherwise represent a zero-sum calculation. High-impact criteria might also incorporate co-benefits: encouraging projects with significant sustainable development gains (e.g. community-based renewable energy or ecosystem restoration) can build broader support and ensure the credits deliver social value in addition to carbon reductions, for instance by creating jobs for the rural poor, improving food security, and enhancing climate resilience for vulnerable communities.

### **6.1.3 Paris Agreement Alignment**

Given the EU's commitment to the principles and objectives of the Paris Agreement, ensuring alignment with the international obligations therein will be a further important condition for inclusion of international credits. All credits used in Europe should be generated and transferred in a manner that avoids double counting and preserves the integrity of both the EU's and host countries' climate commitments. Depending on the context and specific circumstances of the underlying project activities and the nature of the international credits, this may require that credits applied towards compliance with European climate change policies must carry a Corresponding Adjustment (CA) by the host country. During COP26 in Glasgow, for instance, Parties agreed that host countries would have to apply a CA for all ITMOs authorized under Article 6. In practice, this would require the host country's government to formally authorize the credit and subtract the emission reduction from its own Nationally Determined Contribution (NDC) accounting. By adhering to this principle, the EU would prevent the same reduction from being counted twice (once in the host NDC and once under the relevant EU climate change policy). Alignment with the Paris Agreement also implies selecting credits from countries that are committed to the international climate regime and ideally have economy-wide emissions targets. The EU could limit credit imports to those originating from Parties that have robust emissions monitoring and transparent reporting under the Paris Agreement.

Furthermore, to support global ambition, the EU might only accept credits from countries that over-achieve their NDC targets or have raised their ambition, thereby ensuring that the sale of credits does not undermine the host country's own climate policy ambition. This could be operationalized by requiring host countries to demonstrate that credited reductions are “beyond NDC” – for instance, through bilateral agreements verifying that the transfers are part of cooperative efforts to increase overall ambition. Any credits issued under Article 6.4 of the Paris Agreement would also need to comply with the Supervisory Body's rules on baselines, avoidance of environmental and social harm, and the payment of the stipulated share of proceeds to support adaptation. By aligning use of international credits with Paris Agreement mechanisms and safeguards, the system can support international cooperation without compromising global climate goals or the equity considerations underpinning NDCs.

#### **6.1.4 Limited Use for Compliance**

A further mitigation strategy can be to place quantitative limits on the use of international credits for EU ETS compliance. Capping the volume or share of international credits that companies can surrender addresses the risk that low-cost credits would displace domestic emissions reductions and flood the market. Indeed, experience has shown that unrestricted offset use can gravely destabilize carbon markets. In the New Zealand ETS, for example, allowing unlimited imports of credits from the Kyoto Protocol project mechanisms led to a surge of inexpensive units that caused the domestic carbon price to collapse and effectively halted local abatement efforts.<sup>15</sup> To prevent such outcomes, the EU could impose a strict limit on how many international credits each regulated entity (or the system as a whole) may use during a compliance period. Historically, the EU itself set strong precedents for limiting offset usage. During Phase 2 and 3 of the EU ETS, for instance, companies were only allowed to cover a portion of their emissions with credits from the Kyoto Protocol project mechanisms, subject to country-specific limits and an overarching cap of about 1.6 billion tonnes over the two phases (approximately 50% of the total emissions reduction effort).

Other ETS have taken even stricter approaches: California, for instance, initially allowed offsets for up to 8% of a firm's compliance obligation, tightening this to 4% in the 2021–2025 period. Drawing on these models, the EU could reintroduce international credits with a low usage threshold – for example, capping their use at a single-digit percentage of each installation's verified emissions. This limit could be gradually adjusted over time, either starting conservatively at first and expanding if the credits are proven to be high-quality and if EU climate targets are being met, or conversely starting with a generous limit that is tightened over time as decarbonization technologies mature and decline in

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<sup>15</sup> La Hoz Theuer et al., n. 14 above.

cost. Banking rules might also be adapted: regulators could restrict banking of imported credits across phases to avoid accumulation of a surplus. By quantitatively constraining credit use, EU climate change policies would maintain pressure on domestic decarbonization while still reaping most of the cost-efficiencies and cooperation benefits from international trading.<sup>16</sup>

### 6.1.5 Price Measures

In addition to quantity limits, price-based measures can help manage the impact of international credits on European climate change policy frameworks. One concern identified in Section 5.1 was that a flood of low-cost credits could depress the EU allowance price, undermining investment signals for clean technology. To mitigate this, the EU could implement mechanisms to preserve a robust carbon price even when credits are introduced. For instance, a minimum price or exchange rate for credits might be imposed – whereby international credits cannot be acquired below a set minimum price. Alternatively, international credits used towards compliance could be counted at a fraction of a tonne, requiring emitters to surrender more than one credit for each tonne of emissions, effectively raising the price of using credits and narrowing the cost difference with EU allowances. Such credit discounting would incentivize emitters to prefer on-site reductions when possible, and also creates a buffer against a price collapse by reducing the economic advantage of low-cost credits.

Another price measure is to integrate the use of international credits with the existing Market Stability Reserve (MSR) or a similar supply management system, such as a Carbon Central Bank. If international credits start to accumulate in the system and drive the total supply of compliance units above its surplus thresholds, the MSR could automatically absorb a corresponding number of EU allowances from future auctions. In effect, the MSR would counteract excess supply introduced by credits, helping to stabilize prices. Additionally, the EU might consider an offset usage levy – a small monetary charge on each credit used, with proceeds possibly going into a designated climate fund. This would resemble the adaptation levy applied to CDM Certified Emission Reductions (CERs), or the share of proceeds under Article 6 of the Paris Agreement. It, too, would make using credits slightly more costly, dampening excessive use. The levy's proceeds could then support adaptation or innovation, thus recycling any cost savings from offsets into further climate action. By employing such price measures, emitters gain flexibility from credits without undermining the integrity of the carbon price signal that drives low-carbon investment in the EU.

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<sup>16</sup> Lambert Schneider, Michael Lazarus, Carrie Lee, and Harro van Asselt. "Restricted Linking of Emissions Trading Systems: Options, Benefits, and Challenges." *International Environmental Agreements: Politics, Law and Economics* Vol. 17, No. 6 (2017): 883–98. <https://doi.org/10.1007/s10784-017-9370-0>.

### **6.1.6 Reputational Measures**

Even with robust rules in place, the reputational aspect of using international credits can influence their role in the European climate change policy framework. Emitters and policy makers alike face scrutiny from environmental groups, investors, and the public regarding the use of credits, often viewed skeptically as a form of outsourcing emissions reductions. To mitigate reputational risks and encourage responsible use of credits, the EU could institute transparency and disclosure requirements. For example, emitters might be required to disclose in their annual emissions reports how many international credits they used and from which projects or countries these credits originated. Such transparency would enable external stakeholders to evaluate whether firms are relying heavily on offsets instead of reducing their own emissions. Enhanced disclosure aligns with emerging trends in climate governance: financial regulators in a number of jurisdictions are moving toward requiring companies to report offset usage, recognizing that heavy reliance on carbon credits introduces material reputational and regulatory risks. By making offset use public, the EU would harness scrutiny as a tool – firms will be aware that poor-quality credits or excessive offsetting could tarnish their climate credentials.

In addition to disclosure, the EU could support rating or labeling systems for credits used in compliance. Credits could be tagged with quality labels (for instance, indicating if a credit meets a “high-integrity” designation) so that both regulators and observers can distinguish between standard and premium credits. Companies that voluntarily go beyond compliance – such as using only high-grade credits or limiting their offset share well below the allowed maximum – might be recognized through sustainability indices or industry benchmarks, creating a positive reputational incentive. Conversely, the EU could issue public guidance on best practices, warning that over-reliance on offsets is discouraged and will be monitored. Reputational measures also tie into consumer and investor expectations: as corporate climate strategies face greater scrutiny, emitters in the EU have strong incentives to avoid the perception of greenwashing (see also Section 4.1.2 above). By institutionalizing transparency and normative guidelines, the EU can leverage market reputation dynamics to ensure international credits are used as a supplement to, not a substitute for, ambitious internal abatement.

### **6.1.7 Geographical Considerations**

Finally, the EU can mitigate certain challenges by being strategic about the geographical sources of international credits. Not all host countries have the same need for external carbon finance or the same track record of credit quality, and political considerations may favor directing support to particular regions. One option is to restrict eligible credits to least developed countries (LDCs) or vulnerable nations, as a way to channel investment to where it is most needed and most likely to be truly additional. The EU

employed this approach in the later years of its acceptance of credits from the Kyoto Protocol project mechanisms: starting in 2013, new credits were only accepted from LDCs, while credits from major emerging economies were largely phased out. This policy was partly introduced to ensure additionality – many projects in advanced developing countries had become business-as-usual – and partly to distribute climate finance more equitably. Focusing on economically disadvantaged countries with lower capacity to fund emissions reductions can also help reputationally, signaling that the use of international credits serves to support international equity and not just cost reductions in wealthier nations.

Geographical criteria could also be designed to ensure diversification and political alignment. The EU might prioritize credits from countries with which it has established bilateral climate partnerships or cooperative agreements, for instance under Article 6 of the Paris Agreement or the new EU Clean Trade and Investment Partnerships (CTIP). Such agreements can set additional safeguards and mutually agreed standards, giving the EU more confidence in the integrity of acquired credits. Conversely, the EU may choose to exclude credits from countries where governance is weak or where concerns about human rights and local impacts of projects have emerged, thus preemptively addressing ethical criticisms. Limiting geography can reduce the risk of over-concentration of credit supply from a single country (which could create dependency or market manipulation issues) and can encourage broader participation in carbon markets. Another geographical mitigation strategy is to pilot credit imports on a regional basis – for instance, initially accepting credits only from neighboring regions or specific least-developed regions to manage oversight more closely. Over time, if those credits prove effective and controversies are avoided, the EU could expand the geographic scope.

## **6.2 Options for Implementation**

Based on the challenges and mitigation strategies discussed above, this section will explore several options for implementation. A fully developed logical tree will provide a very large set of options and, in order to avoid this, we have amalgamated options to the degree possible.

Below, relevant options for the potential inclusion of international credits into the EU climate change framework has been disaggregated into four categories.

### **6.2.1 Sources of Credits: Where Do Credits Originate?**

The source of credits has been identified as a challenge, with some sources seen more credible than others based on the standards and processes used to certify them. In

terms of sources, another segmentation is based on geographical origin, as well as on the type of credit: mitigation or removal.

Geographically, LDCs and SIDS would represent an acceptable source of credits, both from a development and sustainability point of view, given their higher SDG attributes. Sourcing credits from countries that are more advanced as recognized under UN criteria might be prone to more questioning.

In terms of protocols used to originate credits, further segmentation could include:

- **Article 6.2:** ITMOs that go through the regulatory process under Article 6.2 and observe all rules, including contribution to the Paris Agreement goals and the avoidance of double counting, are one possibility. The concern may arise around the quality of such credits. While there are transparency safeguards that have been put in place, the governance, methodologies employed, etc. are still under bilateral governance, and this may not provide enough reassurance to mitigate the quality concerns that many will have.
  - **Creation of a EUCM:** A newly created EU mechanism, like the Joint Crediting Mechanism (JCM) which Japan has developed over the last decade, and which could be labelled a EUCM. This would produce a subset of Art 6.2 ITMOs, and would have the advantage that it will encourage the export of EU clean technologies and have protocols for issuing ITMOs largely under EU control. It is however a laborious undertaking, and the efficiency of creating totally new mechanisms may come into question.
  - **Non regulatory/voluntary standards.** A number of voluntary standards are currently in operation and have achieved some international recognition and acceptance. ITMOs issued under Article 6.2 but originating from these voluntary standards can also provide a supply of international credits to the EU, should it decide to recognize them under a EU certification process. As an example, ICAO has recognized for CORSIA use credits issued by the Gold Standard, Verra, Climate Action Reserve, and Global Carbon Council. The Integrity Council for the Voluntary Carbon Market (ICVCM) has issued the Core Carbon Principles (CCPs), which are a set of ten fundamental principles that define high-quality carbon credits in the voluntary carbon market. These principles focus on governance, emissions impact, and sustainable development, aiming to create a more transparent and reliable market for carbon credits. The EU could adopt these or similar principles.
- **Article 6.4.** Article 6.4 can be another option as a source of international credits. These credits are issued by the Supervisory Board subject to

multilaterally agreed rules, which may provide more reassurance regarding quality. There is however the precedent of the CDM, where CERs were issued by the CDM Executive Board, but some were later found to be entirely unacceptable to the regulator of the EU ETS.

One issue that also needs to be considered is the fact that in some cases the EU has put a significant level of effort and invested its credibility in developing approaches for crediting, such as the Carbon Removal and Carbon Farming Regulation (CRCF). However, this standard deviates significantly from what the Supervisory Board of Article 6.4 has agreed to in Baku. Such situations will represent an important challenge and will need to be recognized and addressed.

### 6.2.2 Credit Acquisition: How and by Whom are they Acquired?

Two steps can be envisaged in this discussion:

- How are international credits acquired from credit suppliers?
- How do final users acquire international credits?

Both steps are examined in greater detail below.

#### 6.2.2.1 Acquisition of International Credits from Suppliers

Once generated, credits would need to be acquired from the project developers and credit suppliers. There are several options that could be envisaged:

- **A Decentralized Process:** In this case, entities that would want to own credits would have to enter into direct transactions with those that implement activities that generate credits. For illustration purposes, should the EU ETS accept international credits, covered entities would have to acquire them from project developers, which would make public intervention and mitigation strategies towards prices more difficult to implement.
- **A Centralized Process:** This option would see a centralized purchasing agent, allowing much more public interest control on prices paid and types of credits purchased. Several sub-options could be envisaged under such a scenario:

*Multilateral acquisition (MDB).* Under this option, multilateral development banks, potentially coming together as a group, could serve as the intermediary buyer and hold the credits to make them available to final users.

*EU ETS Market Stability Reserve (MSR).* In this option, the MSR would acquire and hold credits sourced from the international market. The MSR is an existing and well understood EU ETS mechanism that plays a role in stabilizing the EU ETS market through quantitative interventions and by ensuring liquidity in the market.

*Carbon Central Bank (CCB).* Conceptually, a carbon central bank has been put forward as an option to address several issues, including managing the

introduction of CDRs in the EU ETS. Its functions could include managing liquidity and the acquisition and management of international credits in the EU ETS. At a functional level, one could argue that a CCB and the MSR are not fundamentally different concepts, with the exception of the functions that each is assigned (a CCB would have a broader mandate). Differences would however apply to the governance modalities, with a CCB being less mathematically driven and afforded more discretionary powers.

In addition to the mechanism or procedure used to acquire international credits, another set of options emerges from the procedure used to acquire them. Direct acquisition implies direct negotiations between seller and buyer. Other options that could be explored include:

- *Price floor.* In this case a price floor would be set for both decentralized or centralized purchasing. Clearly, such a price floor would be more difficult to monitor in a decentralized approach. It could be calculated on the basis of what is seen as an equitable price for credit producers, as well as having some correlation with the market price (e.g. a percentage of the prevailing EUA price).
- *Auctioning.* In this case a reverse auction could be envisaged. This could also be combined with a price floor.

Another set of options can emerge as to where physically the auction or the purchase takes place, and in this case an exchange can be used for that purpose.

#### 6.2.2.2 Acquisition of International Credits by Final Users

Another layer of options is provided when deciding how the end users of these credits access them (e.g. EU ETS covered entities):

- *Direct access by EU entities in the market (private or public).* This has been discussed, and, in this case, users interact with credit producers, with or without any public supervision.
- *Centralized platform:* If entities are not allowed direct access to the international market, then a centralized access approach could be introduced through which credits can be procured from an MDB consortium, CCB or MSR. They could be acquired in several ways, but with strong public supervision through, for instance, an auction with a price floor. For illustration purposes, EU ETS covered entities could participate in an auction run by the CCB with a price floor that is set a percentage above the acquisition price from the producers, or a percentage below the average EUA price.

### 6.2.3 Credit Use: Where Can Entities Apply Them?

International credits can be used in several areas, depending on decisions by the EU, Member States, and affected private sector stakeholders. Some of these were already discussed above (see e.g. Section 4).

- *EU Member State commitments.* International credits could be used by EU MS to go beyond their NDC, as Sweden is doing.
- *Use towards a percentage of the EU NDC, as outlined in the German Coalition Agreement.* This may allow of a more ambitious NDC, while providing flexibility and addressing competitiveness concerns.
- *Insertion in the EU ETS.* This can be undertaken in several ways:

Option 1: The gross cap can be increased by the introduction of international credits, be they reductions or removals.

Option 2: A different option would be to swap an EUA for an international credit. In the case of the international credit being a CDR, this would result in the gross cap being unchanged, but will lead to reduction in net emissions.

- *Use in CBAM.* There has been discussion with respect to the use of international credits to meet importer CBAM obligations. This option has been pushed by both EU importers as well as developed country entities, but has so far been rejected by the EU. Some of the objections include disincentives to develop domestic carbon pricing systems as well as lack of symmetry, since EU ETS covered entities cannot use international credits. These discussions keep resurfacing, with additional and innovative approaches.<sup>17</sup> One potential approach is to aim not for equivalence in terms of tonnes of CO<sub>2</sub>, but for monetary value equivalence in the use of international credits under the CBAM.
- *Compliance with other regulations.* Other regulation – such as transition plans under the CS3D, or use related to the Green Claims Directive – could also serve as an application for international credits. Both these regulations were discussed in Section 4.

### 6.2.4 Revenue Management: Who Captures the Rent?

One of the challenges that were already identified earlier, and which played a significant role in the poor image that some stakeholders had of carbon markets during the Kyoto Protocol period, relates to the rent obtained from transactions, and who retains that rent.

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<sup>17</sup> See, e.g., Ely Sandler, and Daniel P. Schrag. 'Leveraging Border Carbon Adjustments for Climate Finance: Matching Carbon Tax Assets with Carbon Tax Liabilities'. White Paper. Science, Technology, and Public Policy Program. Cambridge, MA: Belfer Center for Science and International Affairs, 2 December 2024.  
<https://www.belfercenter.org/research-analysis/cbam-climate-finance>.

Some CDM projects produced emission reductions for as little as 50 cents and were sold in the EU ETS at prices of 15-20 Euros.

To avoid a recurrence, public participation is critical if international credits are to be contemplated for inclusion in the EU climate change policy framework. This can be addressed as part of the two steps referred to above, that is, when credits are acquired and when they are made available to the final users.

It is essential that a “fair” price be offered to producers, and that users also have a price floor when they buy these credits. In the middle of the value chain, there will be a rent that is extracted, a rent that needs to be used for the public benefit, given the nature of carbon markets as regulated environmental markets. This rent can be reinvested by the CCB or the MDBs as part of development and/or climate mitigation programs, potentially with a focus on the geographies from where the international credits originated.

## **7. Next Steps and Consultation Plan**

A next step would be to work towards operationalizing a concrete Pilot, using the Annex as a starting point.

This will involve the development of a White Paper to frame the Pilot below (see Annex) in greater detail. This document will outline design options, identify key risks, and present mitigation strategies. It will serve as the basis for stakeholder engagement. The parallel, technical design of the pilot will include defining credit sourcing methodologies, prequalifying eligible projects, building IT registry systems, and conducting legal assessments for the needed policy and regulatory frameworks.

Consultations will follow, involving EU Member States, Brussels-based policy think tanks, private sector participants in the ETS, and major development finance institutions such as EBRD, KfW, and EIB.

## **Annex**

### **Pilot Program Proposal: Integrating High-Integrity International Carbon Credits into the EU Emissions Trading System (EU ETS)**

## **1. Core Design Features**

### **1.1 Eligibility Criteria**

Only nature-based removal credits will be eligible under this pilot. This includes projects such as afforestation and reforestation, blue carbon restoration, soil carbon enhancement through regenerative agriculture, and agroforestry.

These types of projects have the potential to remove atmospheric CO<sub>2</sub> at scale and offer co-benefits in terms of adaptation and resilience to climate shocks and slow onset climate events, biodiversity conservation and ecosystem services. Each mitigation activity must demonstrate permanence, additionality, and measurable removal of CO<sub>2</sub> from the atmosphere, validated through robust monitoring, reporting, and third party verification procedures through agreed standards.

The pilot will prioritize carbon removal activities located in Least Developed Countries (LDCs) and Small Island Developing States (SIDS), where climate finance has the highest development leverage. Many of these regions have contributed the least to global emissions but are the most vulnerable to climate change impacts. Supporting mitigation in these areas also advances broader EU development cooperation goals

All credits used in the pilot must comply with internationally recognized carbon standard. They must be authorized under Article 6.2 or 6.4 of the Paris Agreement and must include full Corresponding Adjustments (CAs) to ensure that the same emission reductions are not claimed by both the host country and, potentially, the EU.

Furthermore, mitigation activity credits must align with the Core Carbon Principles of the Integrity Council for the Voluntary Carbon Market (ICVCM) or the Paris Agreement Crediting Mechanism (PACM) ensuring environmental and procedural integrity.

The mitigation removal activities must also demonstrate social integrity. They should deliver co-benefits that contribute to the Sustainable Development Goals (SDGs), including gender equality, indigenous peoples' rights, biodiversity protection, and climate adaptation. Each project will be required to submit a monitorable benefit-sharing plan, indicating how local communities will be consulted, involved, and compensated. Independent audits and stakeholder feedback mechanisms will ensure these commitments are fulfilled.

## 1.2 Quantitative Limits and Phased Implementation

To safeguard the environmental integrity of the EU ETS and avoid undermining domestic decarbonization efforts, the Pilot will introduce strict quantitative limits. In Phase 1 (2026–2030), EU ETS-covered entities will be permitted to meet up to [7%] of their annual compliance obligations through the use of eligible international carbon credits. This threshold will ensure that the core of decarbonization still occurs domestically through corporate action, while allowing a modest and controlled level of flexibility.

In Phase 2 (2031–2040), the compliance cap for international credits will be reduced to [5%]. This reduction will reflect the increasing decarbonization of the EU economy over time and ensure that international credits remain supplemental to, and not a substitute for, local climate ambition. These limits will be subject to review and adjustment based on market performance, environmental impact, and stakeholder feedback.

Additionally, a system-wide cap will be imposed to ensure aggregate control: the total volume of international credits used under the EU ETS must not exceed 1% of the EU's 1990 baseline emissions across any compliance period. This aggregate limit serves as an important backstop, preventing the program from unintentionally diluting the stringency of the EU's emissions cap.

## 1.3 Market Stability Provisions

To prevent disruption of EUA prices and to manage market expectations, international credits will be introduced via a controlled auction-based mechanism. These auctions will be organized periodically by the EU or its implementing agency and will include a reserve price pegged at [70%] of the prevailing EUA price. This price parity ensures that international credits do not undermine EUA prices or reduce incentives for domestic mitigation.

Moreover, international credits may be held in a dedicated registry, separate from the EUA market. This administrative separation may help ensure that international credits do not enter the open market, thereby minimizing opportunities for speculative trading or blending with EUA instruments. By maintaining distinct registries, the EU may also achieve more precise monitoring and control over the use and flow of international credits. The pilot also includes regular monitoring of price impacts and includes a contingency mechanism for suspending auctions if volatility exceeds defined thresholds.

Furthermore, each international credit used triggers an equivalent adjustment in the Market Stability Reserve (MSR), either through the cancellation or withholding of an EUA.

The MSR functions as a key tool in the EU ETS to manage the supply of allowances and stabilize prices by absorbing surplus EUAs from the market. By leveraging the MSR, the pilot ensures that introducing international credits does not inadvertently increase the total emissions allowed under the EU ETS. This adjustment mechanism addresses several critical concerns.

First, it preserves the environmental integrity of the cap-and-trade system by maintaining the scarcity of EUAs, which is central to driving decarbonization investments. Second, it

reassures stakeholders that international credits will not dilute climate ambition or undermine the emissions reduction trajectory established under the EU's Climate Law.

Finally, it provides a transparent and enforceable means to balance flexibility with environmental rigor, which is vital to maintaining market confidence and political support for the ETS framework. This approach ensures that total emissions allowed under the system do not increase because of credit use, while enabling strategic climate finance flows to vulnerable countries.

## **1.4 Use of revenues**

Proceeds from auctions (to EU ETS covered entities) will be reinvested into climate finance initiatives. A portion of the revenue will support new mitigation and adaptation programs in host countries, particularly those with limited access to traditional financing. Another share will fund improvements to MRV systems, registry infrastructure, and institutional capacity, ensuring that developing countries are equipped to participate meaningfully in global carbon markets.

A portion of the revenues raised through auctions will be allocated toward purchasing additional international credits that exceed the compliance obligations of participating entities. These surplus credits will be retired rather than used for compliance, thereby creating an "Over-Mitigation Buffer".

This mechanism serves as a contribution to Overall Mitigation in Global Emissions. By voluntarily exceeding minimum compliance requirements, the EU reinforces its leadership role in promoting net global emissions reductions, rather than simply shifting emissions geographically. The over-mitigation buffer not only boosts climate ambition but also sends a powerful market signal that encourages high-integrity project development in Least Developed Countries.

These additional purchases can stimulate greater private sector investment and innovation, strengthen host country institutions, and support the emergence of robust carbon market infrastructure in regions that have historically lacked access.

## **1.5 Governance and Oversight**

A central institutional body/unit will be established [within DG CLIMA] to oversee the governance and implementation of the pilot. This unit will be responsible for managing the registry of the international credits acquired for the use in the EU ETS, coordinating the annual credit auction process, ensuring the application of eligibility and quality standards, and liaising with host country authorities and authorized third-party verifiers.

Following the MSR model, credit adjustments and EUA withdrawals or cancellations will be governed by a transparent rulebook. This rulebook will define the credit-to-EUA adjustment mechanism, including the use of TNAC-style metrics to calibrate volume, if relevant. The Commission will publish annual "International Credit Market Reports," akin to the Carbon Market Reports prepared under the MSR, to detail credit flows, environmental performance, and financial distribution.

Oversight will be conducted through:

- **Independent Annual Reviews:** Conducted by a technical advisory group comprised of experts in carbon markets, development finance, MRV, and climate science.
- **European Commission Reporting:** The Commission will calculate and disclose total international credits used, EUA adjustments, and OMGE contributions each year by May 15, following the MSR's TNAC reporting precedent.
- **Public Consultations:** The Commission will solicit stakeholder input every three years, timed with broader EU ETS review cycles. These consultations will inform any revisions to eligibility criteria, credit limits, or financial reinvestment mechanisms.

The introduction of international credits will be done through an amendment to the EU ETS legislation which requires co-decision, to ensure high institutional

A consultation on this issue open to all stakeholders will provide additional transparency and buy-in.

This governance structure ensures that the inclusion of international credits is managed with the same rigor and transparency that underpin the EU ETS. It protects market integrity, minimizes regulatory uncertainty, and allows for consistent, performance-driven evolution of the pilot over time.

## **1.6 Procurement Modality and Financial Structure**

Procurement will be composed of two steps: i) procurement from the international market and ii) procurement by end users in the EU ETS.

### **1.6.1 Procurement From the International Market**

International credits will be sourced through a global tender process, administered in partnership with [the World Bank, EIB, EBRD, etc.] or a similar multilateral development institution. This process will identify, prequalify, and contract with projects that meet the pilot's high integrity standards. The use of criteria or a mechanism, such as a price floor, is necessary to ensure that projects receive a fair price signal that has some relationship with the market price for the end users.

A sufficient price signal is important to finance robust and transparent Monitoring, Reporting, and Verification (MRV) systems, which underpin the credibility and traceability of these credits. Furthermore, it enables fair and sustained benefit-sharing with local communities and Indigenous Peoples, whose long-term engagement is vital to the success and permanence of nature-based removals.

Importantly, such a price signal also helps compensate host countries for the opportunity cost of applying Corresponding Adjustments (CAs), ensuring that their own climate ambitions are not compromised by transferring mitigation outcomes abroad leaving a public liability for achieving the additional reductions at a higher (marginal) cost for their NDCs. Using this approach, the EU can catalyze durable mitigation while setting a global standard for integrity, equity, and ambition in international carbon markets.

### **1.6.2 Procurement by EU ETS Covered Entities**

EU ETS entities will acquire credits through a centralized auction platform. Access will be limited to compliance entities within the ETS.

Legal protocols and IT infrastructure will be developed to integrate this pilot with the EU ETS. This includes secure APIs for registry data transfer, legal frameworks for recognizing international credits under EU law, and contractual mechanisms to guarantee non-duplication and enforce Corresponding Adjustments.

## **1.7 Expected Outcomes**

The pilot will target up to [25] million tonnes of verified carbon removals from LDCs between 2026 and 2030. This mitigation will not only support EU climate targets but also provide vital climate finance to countries most in need.

It is estimated that the pilot could mobilize EUR [1] billion in private capital, supporting mitigation and resilience programs in areas that typically lack access to such resources. These funds will strengthen climate adaptation, biodiversity conservation, and sustainable development.

Development co-benefits will include improved livelihoods for rural populations, enhanced food and water security, empowerment of indigenous and local communities, and strengthened institutional capacity in LDCs.

Finally, the initiative will reinforce the EU's position as a global leader in credible and equitable carbon markets, setting a precedent for other regions to follow.