

MARKET NOTICE

10 October 2022

N19/22 – Feedback on N12/22 and publication of the Admission and Disclosure Standards



Introduction

1. On 11 May 2022, the **Exchange** published Stock Exchange Notice N12/22 (and further updated by Stock Exchange Notice N14/22), which set out proposed amendments to the **Standards**¹.
2. This Notice provides feedback on N12/22 (as updated) and confirms the resulting rule changes.
3. The attachments to this Notice contain the clean (Attachment 1) and marked up versions² (Attachment 2) of the amended **Standards**, which will take immediate effect other than in respect of changes to the early notification period³, which will take effect 30 days from the date of this Notice.

Feedback and adoption of the Standards

4. 19 responses were received, all of which were focused on the proposed changes to Schedule 8 (London Stock Exchange's Voluntary Carbon Market **designation**). The responses were from a range of stakeholders with interests and/or expertise in the sustainability sector. The **Exchange** would like to thank all respondents for taking the time to respond.
5. There was universal support for the objectives of the **Exchange** in establishing the Voluntary Carbon Market **designation**, which seeks to identify **Funds** and **Operating Companies** that are investing in climate change mitigation projects.
6. We have addressed repeated themes arising in the responses in greater detail below and, where appropriate, made amendments to the **Standards**.

¹ Any words in bold are defined in the **Standards**, which is appended to this Notice.

² Minor administrative changes will not be shown.

³ As set out in Rule 2.16 of Section 2 of the **Standards**.



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7. No responses were received in relation to any of the other proposed changes set out in N12/22 or to the Stock Connect changes set out in N14/22 and these changes, together with immaterial, clarification or administrative changes, have been incorporated in the **Standards**.

Themes relating to the creation of the Exchange's Voluntary Carbon Market designation

8. There was support for the **Exchange's** proposal to extend the Voluntary Carbon Market **designation** to **Operating Companies**, alongside **Funds**, although one respondent suggested that the **Funds** route be established first before expanding it to **Operating Companies**.

The **Exchange** considers that the choice of corporate structure should be left to the **Eligible Issuer** and its advisers, provided that the **Eligible Issuer** meets the relevant eligibility criteria and is suitable, having regard to the following:

- a) that both **Funds** and **Operating Companies** are afforded the protections provided by existing laws, market rules and regulatory framework; and
- b) one of the underlying principles for the **designation** is to identify those **Eligible Issuers** that are directing capital into climate change mitigation projects, as set out within Schedule 8 of the **Standards**, either through investments or direct/indirect funding.

Accordingly, Schedule 8 has now been amended to extend the Voluntary Carbon Market **designation** to **Operating Companies**, with appropriate adjustments to the **Standards**. The changes recognise the different corporate structure of an **Operating Company**, which may indirectly fund projects generating **Carbon Credits**. An **Operating Company** whose business is focused primarily on trading **Carbon Credits** and does not provide funding to **Proposed Projects** or **Qualifying Projects**, will not be deemed eligible for the Voluntary Carbon Market **designation**.

The **Exchange** welcomes early engagement in respect of prospective issuers seeking the Voluntary Carbon Market **designation**.

While the other themes below are set out in the context of a **Fund**, where applicable the same principles are applied to **Operating Companies** and are explained further, where appropriate.



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9. There were differing views on whether the **Standards** should require a minimum percentage of funds to be invested in projects seeking to generate **Carbon Credits**. Amongst those who advocated a minimum percentage, there was no consensus in relation to the percentage level itself.

Respondents who supported the approach of not including a minimum percentage suggested that the **Fund** be able to make its own decision on investment strategy and considered that it should be left to demand from investors to determine the expected level of investment.

Given the wide range of views submitted by respondents and noting that the purpose of the Voluntary Carbon Market **designation** is not to prescribe a structure or policy for an **Eligible Issuer**, the **Exchange** considers that it is for the **Eligible Issuer** to determine its own strategy and for investors to determine their required level of investment. To support transparency, the **Standards** have been amended so that **Eligible Issuers** must disclose the minimum percentage of their gross assets to be invested in **Proposed Projects** and **Qualifying Projects**, at admission and update the market if this changes on at least an annual basis.

Further, where a **Fund** is not investing fully in **Proposed Projects** or **Qualifying Projects**, the remainder of its investments must be compatible with climate change mitigation *i.e.* avoiding or reducing emissions of heat-trapping greenhouse gases into the atmosphere or provides other defined environmental solutions. As such, Schedule 8 of the Standards requires that where a **Fund** is not investing fully in **Proposed Projects** or **Qualifying Projects**, the remainder of the investments must be mapped to the Tier 1 or Tier 2 micro sectors within FTSE Russell's Green Revenues Classification System. This identifies sectors that are deriving green revenues from products and services that have a positive environmental utility. Comparable changes have also been introduced for **Operating Companies**.

10. Schedule 8 refers to an **Eligible Issuer** determining how it will distribute the **Carbon Credits**. Noting certain responses, the **Exchange** confirms that it is open to the **Eligible Issuer** to determine whether to sell those **Carbon Credits** rather than to distribute them through a dividend *in specie* or retire them on behalf of shareholders. This has now been clarified. This is consistent with the approach of the **designation**, which is not intended to restrict the normal strategy choices available to an **Eligible Issuer**. It is for investors to take responsibility for considering the disclosures made and to be satisfied with the **Eligible Issuer's** chosen strategy to deal with the **Carbon Credits**.



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11. Many respondents highlighted risks such as lack of additionality and/or permanence and leakage in the **Qualifying Projects** themselves. This issue is addressed by the **Exchange's** rationale behind selecting independent and expert third-party industry bodies that endorse suitable **Qualifying Bodies**:
- i. the International Carbon Reduction & Offset Alliance ("**ICROA**"), which includes the following **Qualifying Bodies**: the UK Woodland Carbon Code, Gold Standard and Verra's Verified Carbon Standard, among others; and
 - ii. the Integrity Council for the Voluntary Carbon Market ("**ICVCM**") (once its Core Carbon Principles are issued as final).
- The **Qualifying Bodies** have approved methodologies in place for carbon project design, implementation and carbon accounting requirements, which may lead to the issuance of **Carbon Credits**, and are established organisations with recognition of this being supported by the responses to the consultation. Specifically, it is noted that as part of the methodology development, approval and grievance process undertaken by the **Qualifying Bodies**, additionality, permanence and leakage are reviewed periodically. Accordingly, it is open for investors to consider and be satisfied with the various requirements of these **Qualifying Bodies**. In addition, a risk factor requirement in respect of these risks has now been included.
12. A few respondents highlighted that there are differences between how the **Qualifying Bodies** endorsed by ICROA operate. It is noted that the **Qualifying Bodies** are endorsed by ICROA, as the collective view of market experts, and as such are recognised by respondents as being appropriate voluntary carbon standards. This is a rapidly evolving and innovative sector and, in this regard, it is noted that ICVCM is seeking to establish a new global threshold for high-quality carbon offset projects. As industry bodies and associations evolve, the **Exchange** will be able to review and amend the list through a Stock Exchange Notice.
13. One of the **Exchange's** objectives for the **designation** is to facilitate the financing of projects which are helping with climate change mitigation. Accordingly, the **Exchange** proposed at the outset that a **Fund** would need to invest in at least one **Proposed Project** or **Qualifying Project** within three years of receipt of the Voluntary Carbon Market **designation**. This time frame was questioned by some of the respondents. Due to the infancy of the market, which is recognised by many respondents and noting that timeframes will differ significantly depending on the type of project, the **Exchange** considers it is important to have a period which can be applied to various projects. However, noting that the underlying principle is to ensure that an **Eligible Issuer** is progressing its **Carbon Credit** strategy, the **Standards** have been amended so that the **Eligible Issuer** must commence investment in at least one **Proposed Project** or **Qualifying Project** within two years and must maintain at least one investment thereafter. The **Fund** will also be required to provide updates in its annual accounts on the estimated targets and timeframes.



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14. A few respondents were keen to understand whether **Funds** would be taking into account specific environmental and social benefits in respect of the **Qualifying Projects** they invest in (particularly, how the local communities, where the projects are situated, may be affected) and, whether the **Exchange** would be monitoring this. One of the **Exchange's** aims for the Voluntary Carbon Market **designation**, is to contribute to scaling the supply of **Carbon Credits** from projects which should by their nature also provide social benefits such as public health improvements and community job creation. However, the **Exchange's** role is not to opine on or monitor the appropriateness of an **Eligible Issuer's** strategy. Further, it is noted that Schedule 8 of the **Standards** requires specific disclosure against the United Nations Sustainable Development Goals; which recognise that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth, at the same time as tackling climate change. An **Eligible Issuer** also has the ability to provide additional disclosure over and above the minimum requirements as set out in Schedule 8 of the **Standards**. Investors can actively make choices based on an **Eligible Issuer's** strategy of environmental and social benefits.
15. For clarification purposes, there was a query as to whether or not an investment in a project developer would be suitable or whether the **Fund** can only invest in specific projects, which will produce **Carbon Credits** directly. The **Exchange** confirms that it would consider such a structure provided it met the principles of the Voluntary Carbon Market **designation**. The **Exchange** will consider the structure on a case-by-case basis and any issues should be raised with the **Exchange** at the earliest possible opportunity.
16. A number of respondents have suggested that additional information in relation to **Carbon Credits** would be helpful for investor consideration. Accordingly, further requirements have been included at paragraph 9 of Schedule 8.
17. Some respondents have highlighted the risk of non-delivery in respect of **Carbon Credits**. This is an inherent risk in investing in a **Fund** or an **Operating Company** as there cannot be any guarantee of delivery of **Carbon Credits** and/or even where they are delivered, the timetable in achieving them may be long term. As noted above, the **Exchange** is not responsible for, nor does it monitor or opine on the **Eligible Issuer's** strategy, operations or delivery. The **designation** utilises the existing protections afforded by the regulation and rules of public markets to support transparency for **Carbon Credit** projects and the **designation** disclosure requirements are not the **Eligible Issuer's** primary market obligations. As such, the additional disclosure requirements of the **designation** are not intended to be comprehensive nor a substitute for the **Eligible Issuer's** existing disclosure and legal obligations (including **UK MAR**) and other legal and regulatory requirements. Investors must make their own judgments on investment risk based on all the information available to them and, to emphasise this, we have further expanded the risk warning.



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18. The initial consultation stipulated that a **Fund** with the Voluntary Carbon Market **designation** be managed by a person authorised by the **FCA** or the Jersey, Guernsey or Isle of Man regulatory bodies to manage an unauthorised **Alternative Investment Fund**. This has now been extended to **Funds** managed by a person registered with these named regulatory bodies so as to capture **Funds** with assets under management of less than €500 million, which do not use leverage. The **Standards** also clarify that a **Fund** may be managed by a person registered with the **FCA** to market an unauthorised **Alternative Investment Fund**, where that person is regulated in a jurisdiction which is deemed suitable by the Exchange from time to time.
19. Further clarification in respect of certain queries raised by respondents is set out below:
- a) the **Exchange** is not responsible for, nor will it review, the **Eligible Issuer's** investment strategy or funding policy, nor determine whether the strategy is expected to result in the creation of **Carbon Credits**;
 - b) at the point of seeking the Voluntary Carbon Market **designation**, only the **Qualifying Projects** need to be **Independently Certified** and appear on the register of the relevant **Qualifying Body**. However, if the **Eligible Issuer** is investing in any **Proposed Projects** there must be a reasonable expectation that the project will be a **Qualifying Project**, but it would not need to be on the register of the relevant **Qualifying Body**; and
 - c) **Eligible Issuers** with the Voluntary Carbon Market **designation** may issue **Carbon Credits** and determine to distribute them *in specie*, but this will not necessarily lead to their retirement. Further, as noted above, it is open for the **Eligible Issuer** to sell the **Carbon Credits**.

Documents published today

20. Today, the **Exchange** publishes the revised **Standards**, as per paragraph 2.
21. The **Standards** will also be available on the **Exchange's** website.



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Queries

22. Queries on the further consultation in respect of the rule changes should be addressed to primarymarketregulation@lseg.com.

Nilam Statham

Co-Head of Market Regulation

This Stock Exchange Notice will be available on the website at: <https://www.londonstockexchange.com/resources/london-stock-exchange-notices>

Calls to the London Stock Exchange plc may be recorded to enable London Stock Exchange to carry out its regulatory responsibilities.



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