3 February 2025

To: Article 6.4 Supervisory Body, A6.4mechanism-info@unfccc.int

From: CarbonPool Holding AG

Subject: **CarbonPool comment on SBM015 annotated agenda and related annexes**

Dear Sir or Madam,

With reference to the call for input on the issues included in the annotated agenda and related annexes of the fifteenth meeting of the Article 6.4 Supervisory Body ("SBM") from 10-14 February 2025 in Thimphu, Bhutan, we are pleased to provide our input on agenda items 3.4 and 3.5.

CarbonPool Holding AG ("CarbonPool") is a Swiss carbon insurance company[1] that has been working with stakeholders across the voluntary and compliance carbon markets to offer our reversal insurance as a supplement to existing or planned-for buffer pools. As the SBM is aware, there are limitations to buffer pools as a mechanism to secure carbon credit permanence. CarbonPool believes that some of the limitations posed by buffer pools could be efficiently remediated by the use of insurance.

This submission will focus on two issues: (i) an overview of the main issues that the Reversal Risk Buffer Pool raises, and which the SBM itself has signalled as a concern in its annotated agenda, and (ii) the potential for insurance to secure carbon credit permanence, and our suggestion for how the SBM may evaluate and approve the use of reversal insurance policies per its mandate granted by the COP29.[2]

I. Agenda Item 3.4: "Methodologies"

Agenda Item 3.4 states that the SBM may wish to consider the information note, "Further work on the methodological products for the Article 6.4 mechanism."[3] This section will focus on the issues raised in Table 2 of that document, which sets out further mandate/guidance to the Methodological Expert Panel ("MEP").

In particular, it will touch on the process for approving the "the basis and procedures for the SBM's initial and periodic review and approval of the sufficient coverage of insurance policies." The COP29 in 2024 gave the SBM the mandate to "consider and implement" the following, each of which will be addressed in turn:

(i) "any potential remedial actions necessary to manage risks to the robustness of the Reversal Risk Buffer Pool Account;" and

(ii) "other appropriate measures . . . that may provide suitable alternative means to remediate reversals, including . . . [r]equirements and approval procedures for the use of insurance policies".[4]

[1] Full insurance and reinsurance license expected from Swiss regulator FINMA.
[2] *See* A6.4-SBM014-A06.
[3] *See* A6.4-SB015-AA-A08.
[4] Para. 62(a), A6.4-SBM014-A06.

CarbonPool urges the SBM to consider not only the potential for insurance to serve as a backstop to the Reversal Risk Buffer Pool Account itself, but also for insurance to remediate reversal risks as a standalone mechanism.

It has become clear in recent studies and reporting[5] and by the SBM's own acknowledgement that there exist "risks to the robustness of the Reversal Risk Buffer Pool Account."[6] Firstly, buffer pools by their nature are insufficient to cover the most significant reversal events. Secondly, contributions are assessed upfront and are meant to secure the permanence of credits for the long term, even though it is exceedingly difficult to predict with meaningful accuracy how climate risk to a project is likely to evolve beyond even a few years. Thirdly, even if contributions are re-assessed periodically, the Reversal Risk Buffer Pool Account does not have any additional risk capital to backstop unexpected and catastrophic losses.

Insurance, by contrast, is a regulated, mature, and competitive sector, which has developed a deep understanding of which risks can be mutualized and covered by insurance policies. In the carbon context, the main risks posed especially to nature-based projects are already well understood by insurers, who have developed sophisticated agricultural and liability insurance products. Moreover, insurance remediates many of the limitations of buffer pools that the SBM has expressed concern about. Insurance companies hold risk capital that enables them to remain solvent even after a catastrophic loss; risk assessments are science-based and backed by actuarial models; and the short-to-medium-term duration of policies means that project risk is regularly reassessed and addressed in changing premium prices.

In the SBM's mandate to both remediate risks to the Reversal Risk Buffer Pool Account and to explore "suitable alternative means" to mitigating reversal risk, insurance can and should play a key role.

First, insurance can be used as a backstop to the Reversal Risk Buffer Pool Account. In other sectors, the risk of damage or destruction of assets has traditionally been managed through a combination of additional reserves to cover small losses (akin to the buffer pool), and supplementary insurance to cover large losses. The carbon sector is no different, and we believe that the Reversal Risk Buffer Pool Account could also be backstopped by insurance in case of large or catastrophic losses that exceed the buffer pool contribution.

To fully compensate for a reversal, the insurer's compensation should be in kind, i.e., the insurer must deliver A6.4ERs to replace reversed A6.4ERs one-for-one. Should in-kind insurance not be available, a fall-back solution would be to allow compensation in cash, so long as it is sufficient to purchase, or otherwise procure, the replacement A6.4ERs. This is in line with other emerging international compliance schemes, such as the CORSIA airline offsetting scheme, in which insurance is being used to compensate for Letter of Authorization revocation.

Additionally, by collaborating with insurers and tapping their actuarial expertise, the registry can optimize the size of the contributions and the management of the Reversal Risk Buffer

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[5] *See, e.g.*, Grayson Badgley et al., *California's forest carbon offsets buffer pool is severely undercapitalized*, FRONT. FOR. GLOB. CHANGE (Aug 5, 2022); Ben Elgin, *How Vintage Nike Airs Exposed a Flaw in a $700 million Carbon Market,* BLOOMBERG (Oct 29, 2024).
[6] Para. 60, A6.4-SBM014-A06.

Pool Account itself. This incentivizes the best practices in project development and ensures the maximum and most durable climate impact of the projects generating the A6.4ERs.

Second, insurance could be used in lieu of a buffer pool cancellation following a reversal, and CarbonPool encourages the SBM to create a process to allow a Party to avail itself of that option. In-kind insurance is particularly suited here, as an insured party could avail itself of an in-kind insurance payout and use these credits to compensate for a reversal in lieu of a buffer pool cancellation. In doing so, requiring in-kind reversal insurance can guarantee credits' permanence.

In addition, we believe that insurance could replace the buffer pool entirely in the future if clear guidance defining the characteristics that insurance products must meet is articulated in collaboration with the insurance industry. As a first step, CarbonPool urges the SBM and MEP to engage with insurers experienced in the carbon market to articulate a clear set of criteria for a satisfactory reversal insurance policy, as well as a process for evaluating whether policies are acceptable. This engagement should ensure that the criteria are robust enough to ensure sufficient coverage and are simultaneously achievable for insurers.

CarbonPool is willing and committed to engage on these points, and we are confident in the market's ability to meet this need. The global insurance industry has more than sufficient capacity to cover the risks present in the carbon market, and will step up to respond to the demand once the SBM creates the standards for approving insurance products to backstop or substitute the Reversal Risk Buffer Pool Account. This has proven to be the case in the CORSIA context, in which all of the major carbon insurers (including CarbonPool) have been working to develop CORSIA insurance products in the wake of registries' decisions to rely on insurance as the primary risk mitigation mechanism.

As a separate matter, also on Agenda Item 3.4, we wish to provide a second input concerning the reversal risk assessment tool (referenced in the same table 2). Consideration is given on whether to include upper limits in respect of the risk rating or specific risk factors; we recommend strongly that no upper limits be set. Indeed, any such limit will create arbitrage opportunities and distort incentives during project development, as high risk-taking will not be fully penalized compared to lower-risk alternatives.

I. Agenda Item 3.5: "Registry"

This agenda item puts forward the discussion of the draft procedure for the Article 6.4 mechanism registry, including the transaction procedure. The procedure does not appear to take account of cancellation of units due to non-permanence / reversal of the underlying physical assets. We urge the SBM to request that this possibility be included, as it is essential to enable the full accounting of reversal events and of the remaining sufficiency of the buffer pool.

We trust that this input will be deemed relevant and taken into consideration by the SBM.

Yours sincerely,

CarbonPool Holding AG

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