Carbon Credit

[UPSC Notes]

What is Carbon Credit?

A Carbon Credit is a tradeable certificate or permit that gives the holder power to emit carbon dioxide or other greenhouse gases over a certain period.

- These Carbon Credits are generated from projects around the world that keep the Greenhouse Gases (GHGs) altogether.
- Carbone credits are basically market mechanisms for the reduction of greenhouse gas emissions.
- Regulatory bodies or governments set the caps on the emission of greenhouse gasses. But for some companies, a sudden reduction in the emission is not viable financially. therefore they can purchase the carbon.
- Companies that are able to reduce the emission of greenhouse gases are usually credited with Carbon Credits.
- The sale of credits surpluses may be used for subsidizing the projects that would helo the in reduction of greenhouse gas emissions.

Types of Carbon Credits
There are two types of Carbon Credits

- Voluntary emissions reduction (VER): A carbon offset that is exchanged involuntary market for credits.
- Certified emissions reduction (CER): credits created through a regulatory framework with an aim of offsetting emissions from a project.

Carbon Trading (Carbon Credit Trading)
Carbon Credits can also be traded on both public and private markets. The current rules of traning allow the international transfer of credits as well.

- The prices of Carbon Credits depend on the levels of demand of supply in the markets. So the price fluctuates on the supply and demand in different countries.
- Carbon Credits have proven beneficial to society. However, it is not easy for the average investor to start using credits as investment vehicles.
- Certified Emissions Reductions are the only product that can be used as investments in credits. However, the CERs(Certified Emissions Reductions) are sold by special carbon funds which have been established by the big financial institutions.
- The carbon funds give an opportunity for small investors to enter the market.

Carbon Markets

Carbon markets allow for the selling and buying of carbon emissions with the objective of reduction of global emissions of greenhouse gases.

- Carbon markets can the emissions reduction over and above what the countries are doing on their own. It can be explained with an example. The emission of greenhouse gases in a factory in India can be achieved in two ways

1> A country that hasn't been able to reduce the emission can provide technology or financial support to that factory in India to claim the reduction of emissions as its own.

2> on the other way, that factory in India can make investments and offer sales of emission reduction which is called Carbon Credits. So other parties that are struggling to meet their target can purchase these Carbon Credits and show these as their own.

Carbon Market under the Paris Agreement

At first, the carbon markets existed under the Kyoto Protocol, but it has been replaced by the Paris Agreement in 2020.

- Article 6 of the Paris Agreement describes the provision related to setting up a new carbon market.
- Article 6.2 allows bilateral arrangements for the transfer of emissions reductions.
- Article 6.4 of the Paris Agreement, is about a wider carbon market in which reductions can be bought and sold by anyone.
- Article 6.8 talks about the non-market approaches available to countries to achieve targets.