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CFTC Enforcement Encourages Carbon Markets Whistleblowers

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On June 20, following a number of consultative papers, reports, committee hearings and public speeches by representatives of the Commodity Futures Trading Commission ("CFTC"), the staff of CFTC's Division of Enforcement ("DOE") has published its first alert on voluntary carbon markets ("VCMs"). The alert: (i) describes the CFTC's jurisdiction over VCMs; (ii) lists typical offenses involving VCMs; (iii) explains how to identify fraud and manipulation in VCMs; and (iv) lays out how to report alleged violations to the DOE.

Carbon credits (also known as offsets) and allowances, as well as many other environmental products, are generally recognized as "commodities." As a result, the CFTC has enforcement authority to pursue fraud and manipulation claims relating to interstate transactions in these commodities. Many of these contracts trade bilaterally over the counter or on spot exchanges. Further, carbon credits and other environmental commodities trade as futures contracts on CFTC-regulated exchanges (designated contract markets – "DCMs"), where the CFTC can exercise its full regulatory jurisdiction.

The CFTC provided a list of examples of misconduct involving VCMs for potential whistleblowers to "be on the lookout for," including manipulative and wash trades in futures carbon contracts; manipulation of tokenized carbon markets; and fraud in underlying spot carbon markets, such as listing of ghost (or illusory) credits on carbon market registries, double counting, and "fraudulent statements relating to material terms of the carbon credit, including, but not limited to: quality, quantity, additionally, project type, methodology substantiating emissions claim, environmental benefits, the performance or duration, or the buffer pool."

It is clear that the CFTC has the view that all VCM products underlying listed futures contracts are within the CFTC's jurisdiction. Given that there are approximately 200 such VCM-based listed futures contracts in the U.S., the CFTC has jurisdiction over a vast majority of VCM products. For example, if a carbon credit product underlies a DCM-traded futures contract and purports but falls materially short of achieving actual carbon reduction, the CFTC would have the authority to pursue based on alleged fraud and manipulation all those who had listed that carbon credit on a registry. However, it is not clear whether an unrelated entity will be subject to the CFTC's enforcement authority if such entity based corporate disclosures on these carbon credits and therefore arguably engaged in greenwashing. It appears, however, that at a minimum, the CFTC would nevertheless like to hear from whistleblowers about this conduct.

The alert notes that currently the VCM is estimated at $2 billion and is expected to grow to $250 billion by 2050 as more market-based initiatives are implemented to mitigate climate change and transition to a low-carbon economy. As a commodity market regulator, the CFTC would play a critical role in policing VCMs and environmental commodity markets for potential fraud and manipulation. To further study these markets the CFTC had established in 2021 a new Climate Risk Unit within the CFTC.
