

**WCI-GHG  
Cap & Trade****Program  
Proposal****Subcommittees****Threshold Levels****State Allowances  
&  
Early Actions****GREENHOUSE GAS CAP & TRADE UPDATE**

WESTERN CLIMATE INITIATIVE RELEASES NEW DETAILS

by Tom Wood, Steel Rives LLP (Portland)

On July 23, 2008, the Western Climate Initiative (WCI) released the latest draft of its proposed program design for the looming greenhouse gas (GHG) cap and trade program. Over the course of the past seven months WCI member states/provinces have been deliberating about details of the planned GHG cap and trade program. On July 23rd, WCI released the greatest level of detail seen to date and then followed this release with a meeting in San Diego on July 29<sup>th</sup> where the organization made brief presentations and took comments from the public. This article discusses ideas raised in the latest proposal and how the proposals may affect Oregon sources.

**Western Climate Initiative**

The WCI is a regional organization formed in February of 2007 and currently consisting of seven western states (Oregon, Washington, California, Montana, Utah, New Mexico & Arizona) and four Canadian provinces (British Columbia, Quebec, Ontario and Manitoba); a number of other US and Mexican states, as well as Canadian provinces, participate in WCI as observers. As discussed in previous *Insiders*, the purpose of WCI is to fill the void left by the lack of federal greenhouse gas regulation and to create a regional greenhouse gas strategy. Currently, WCI's primary focus is on the development of a GHG cap & trade program. [See Futornick *Insiders* #422/423, #424/425 & #431; Article, *Insider* #426/427; Duncan, *Insider* #430; and Wood, *Insiders* #433 & 434]

In order to grapple with the array of issues inherent in establishing a cap and trade program, the WCI established subcommittees. Five areas (reporting, allowances, offsets, electricity and scope) were carved out for specific subcommittee consideration. Member state non-elected representatives participated in these committees, drawing up a set of design options for each subcommittee that were first shared with the public in January 2008. Since that time the subcommittees and the full WCI committee have been meeting behind closed doors (the public is not allowed to attend or directly participate) with the goal of generating a cap and trade program to be adopted by the member states/provinces. The Scope Subcommittee and the Electricity Subcommittee initial proposals were released in March 2008. (See, Wood, *Insider* #433). The Reporting, Allowances and Offsets subcommittees released initial draft design recommendations in April. The July draft design recommendations sought to fill in key details not identified in prior drafts.

**Key New Design Features**

The July proposal both reiterates key themes previously identified as well as identifies threshold levels not previously noted. The July proposal reiterates WCI's intent to regulate industrial process and combustion emissions. However, a critical new element is that WCI has proposed that sources with less than 25,000 metric tons (MT) carbon dioxide equivalent (CO<sub>2</sub>e) are not subject to the cap and trade program. Commenters had previously argued for thresholds ranging from 10,000 MT to 100,000 MT. The proposal also clarifies that biofuel and biomass emissions are not considered under the cap and trade program (although might still be subject to reporting) given that they are carbon neutral. Electricity imported into the WCI region is still proposed to be addressed under the cap by the first jurisdictional deliverer, i.e., the first entity that handles the electricity as it enters the WCI region. Transportation, residential, commercial and industrial fuels used at sub-jurisdictional facilities are proposed to be similarly regulated at the level of the entity that first handles the fuel as it enters the WCI region.

One of the most concerning areas for Oregon sources that is discussed in the July document relates to how the total state allowances are decided and how early actors are addressed. A key concept of WCI since the outset has been to ensure that early actors are rewarded, rather than penalized, for having decreased GHG emissions prior to WCI implementing its cap and trade program. Oregon has been a case study for early action, having invested more than \$1 billion dollars in energy efficiency improvements through the state's Business Energy Tax Credit (BETC) program. However, in the July proposal WCI suggested that the amount of allowances that a state is entitled to would be based on the projected actual emissions in 2012. States are then supposed to reward early actors out of this allowance budget intended to reflect 2012 actual emissions. WCI did not propose to make any additional allowances available to states (such as Oregon) that have a documented history of early action and that have already achieved dramatic improvements. The proposed approach will put Oregon at a distinct disadvantage compared to states that have not made such dramatic investments in energy efficiency. If this approach is ultimately adopted, it will serve to penalize Oregon for having invested so much money in energy efficiency upgrades.

***WCI-GHG  
Cap & Trade******Possible Costs***

One area that the July document did not address is how allowances would be allocated by the states to the sources under the cap. Much of the debate to date has centered on whether WCI would require that some or all allowances be sold through an auction as opposed to given away for free to sources under the cap. Industrial advocates have argued that selling the allowances will have the effect of taxing industry and will result in many of the emitting industries moving out of the WCI region and shipping goods into WCI states. WCI member states lack the authority to impose a GHG tariff on goods entering WCI from other states or countries. Therefore, if industry in member states must face the cost of *both* paying for offsets at auction *and* paying for the additional energy efficiency projects needed to reduce below current emissions, the incentive will be to close shop and move elsewhere. The debate on this point has been quite heated and so WCI chose not to address it in this draft, instead focusing on reaching resolution on this hot issue in its late August deliberations.

***Offsets***

Another area that has sparked much debate is offsets. Offsets are essentially allowances that are generated by reducing GHG emissions at sources not subject to the cap. WCI has embraced the idea of offsets, but has been caught up in tremendous debate as to what constitutes a valid offset and how much of a facility's compliance obligation can be met through the use of offsets. In the July proposal WCI proposed for the first time limiting a source to meeting only up to 10 percent of its total allowance obligations through the use of offsets. No mechanism was proposed for increasing this percentage if the cost of obtaining allowances on the open market gets too extreme—an oversight that hopefully WCI will correct. WCI for the first time openly endorsed the idea of agricultural, forestry (including reforestation) and waste management projects as being capable of generating offsets.

***Mandatory  
Reporting***

A few key concepts were reported in relation to the WCI GHG reporting program. Mandatory reporting is proposed to commence for all six GHGs (carbon dioxide, nitrous oxide, methane, sulfur hexafluoride, CFCs and HCFCs) in 2011 for 2010 emissions. Sources with emissions of 10,000 MT CO<sub>2</sub>e or more will have to be subject to reporting, although states can push the threshold lower. Third party verification of emissions would not be mandatory. Oregon has already proposed rules that would equal or exceed the requirements proposed by WCI.

The cap and trade program is proposed to commence on January 1, 2012.

**Conclusions**

The proposals released in July provide the most tangible insight into the program that will soon be taken to the WCI state legislatures and cause fundamental impacts to our economy. Clearly, there will be winners and losers in any program. The proposals offer insight into who those may be, but are far from clear.

***Uncertainties***

There is no certainty that the member states will ultimately adopt requirements that are consistent with what the WCI representatives propose. WCI has no statutory or regulatory authority. Whatever WCI's representatives come up with will ultimately be reviewed by the Oregon legislature and have to be enacted into law. It is unclear whether the Oregon legislature has the appetite to impose dramatic costs on its industries at a time when many are struggling to survive and when the program is likely to be unable to protect Oregon voters from seeing its industries shut down and move outside WCI. As one environmental group representative commented at the July 29 meeting, a large number of employees are just going to have to move to new jobs if the WCI cap and trade program goes into effect. Many of those employees may prefer a state energy efficiency incentive program to a regional cap and trade program that prices their employer out of the market. Waiting for a federal cap and trade program means that they can have greater assurance that their job will not move to a less regulated state/country.

The WCI Subcommittee proposals are available at [www.westernclimateinitiative.org](http://www.westernclimateinitiative.org).

**FOR ADDITIONAL INFORMATION, CONTACT:**

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