

# Resolution of the Oregon Global Warming Commission

Resolution Number: 2009-1-009

Origin: Energy, Utilities, and Stationary Sources Committee

Resolved, that the Oregon Global Warming Commission recommends that Oregon continue to move forward with development of the Western Climate Initiative (WCI) proposed framework for establishing a western States and Canadian Provinces ("States") regional greenhouse gas ("GHG") cap and trade mechanism<sup>1</sup>, and complementary programmatic and regulatory measures, with additional work in 2009 to include further definition of market design and WCI-member-specific decisions on critical framework details including the qualifications noted below.

In making this recommendation the Commission reaffirms its support for a fair and effective national solution to achieving greenhouse gas reduction goals comparable to Oregon's, one that employs marketplace tools such as a cap and trade mechanism, as ultimately preferable to regional or state-based initiatives; and the Commission's intent, by offering this Resolution, to participate in shaping that solution.

## Qualifications

1. *Allocation of Allowances Among States*: The Commission recommends that Oregon receive GHG emissions allowances in amounts consistent with an Oregon obligation to meet the WCI *regional emissions goal*, while seeking to strengthen that regional goal to the levels adopted by the Oregon legislature in 2007.
2. *Allocation of Allowances – Transition Issues*: The Commission recommends that Oregon temporarily reserve some part of allowances from initial allocations, and make these available to regulated entities that meet pre-established economic hardship criteria.
3. *Use of Auction Proceeds*: The Commission recommends that auction or other program revenues should be used for actions (including related research) that will avoid GHG emissions in Oregon in the capped sectors and assist regulated entities to meet their compliance obligations while preserving jobs in those sectors; to assist workers and low-income energy consumers adversely affected by higher energy prices or job losses attributable to emissions regulation; and to support adaptation activities in Oregon's communities and its natural environment.
4. *Point of Regulation*: The Commission concurs with the WCI that the point of regulation of GHG emissions for all sources, whether emitted within the WCI or associated with energy imports, must be within the WCI's borders, and within the State's regulatory jurisdiction. In establishing a point of regulation, it is important that electric system reliability not be impaired.
5. *Transition to Federal Carbon Emissions Reduction System*: The Commission concurs with the WCI in recognizing the importance of anticipating national GHG regulation, and

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<sup>1</sup> As generally laid out in the WCI Design Recommendations dated September 23, 2008.

adopting a WCI design that can both influence national regulation, and be adapted readily into that regulation so it is not duplicative of Federal requirements.

6. Complementary Public and Private Sector Actions: The Commission has already acted to recommend to the Legislature and Governor new initiatives in energy efficiency, renewable energy, transportation efficiency and land use that also rely on individual and private sector participation. The Commission recommends the Oregon Public Utility Commission, the Oregon Department of Energy and Consumer-Owned Utility governing boards undertake processes to identify the technical potential, anticipated GHG avoided emissions benefits and associated costs, and new programmatic and regulatory measures at a minimum in the following key strategic areas:

- a. Electricity and gas energy efficiency;
- b. Smart Grid designs, costs and benefits;
- c. Combined heat and power facilities;
- d. Small- and medium-scale renewable energy facilities (e.g. solar photovoltaic, micro hydro, biomass, solar hot water)
- e. Automobile and light duty truck electrification and other low-carbon transportation strategies.

The primary goal of adopting new strategic programmatic and regulatory measures is to achieve avoided emissions prior to and during implementation of a cap-and-trade program.

## **Outstanding Questions**

[NOTE: The following is not an exhaustive list of outstanding questions, but represent issues the Commission particularly wishes to bring to the attention of the Governor and Legislature. The Commission emphasizes that these are issues to be addressed constructively and satisfactorily resolved as we move forward with the development of proposals for carbon cap and trade.]

1. **Economic Effects of a WCI Carbon Cap & Trade:** The Commission recognizes the potential for both economic opportunity and economic dislocation from implementing a regional carbon cap and trade mechanism. The Commission, in partnership first with the Oregon Business Association, initiated an Oregon-specific economic impact analysis that now includes co-sponsorship from the State and other business and environmental interests. That analysis will look at both opportunities and risks of Oregon's participation in the WCI framework, building on a larger regional WCI analysis. There are other analyses underway as well that are seeking to identify economic outcomes as well as effects on individual Oregon companies subject compliance requirements, the findings of which will be increasingly useful as greater clarity is achieved on the questions we identify below. The Commission will review these as well, and provide its evaluations to the Legislature as they become available. The Commission may empanel an Economists Advisory Board to peer-review selected studies and make its findings available to the Commission, the Governor and the Legislature. The Commission may also examine whether there could be electric system reliability consequences of programmatic and regulatory proposals, either favorable or adverse.
2. **Allocation of Allowances within Oregon:** How should carbon emissions allowances be allocated within the State of Oregon? What part of the allowances should be free, and what part subject to auction? If regulated and consumer-owned utilities receive most or all allowances free, should other companies subject to the cap be treated the same or differently? If some allowances are to be auctioned (WCI stipulates at least 10% of allowances are to be auctioned), should these come "off the top" before allocation of allowances to all other parties subject to the cap?
3. **Allocation of Allowances Among States:** Should allowance allocation methods be parallel among the WCI States to avoid creating competitive imbalances that could be expected to occur if like companies subject to emissions regulation have unequal access to allowances?
4. **Greater Clarity on Reduction Expectations for Potential Regulated Entities:** The WCI does not represent the proposed regional cap and trade framework as complete. Acknowledging this, the Commission particularly encourages greater clarity on how reductions requirements will apply to individual regulated entities. Some of the outstanding questions include:
  - How soon will the promised estimate of 2012 base period emissions be provided so entities can plan from that base emissions level?

- How will reduction obligations be allocated to regulated entities from that base level; and if reductions among regulated entities are not simply proportional to Oregon or regional WCI goals, what adjustments will be made, and for whom?
  - How will other adjustments to overall and individual allowance allocations be made – for example, treatment of emerging and of departing emitters within a State or within WCI, or allocating the effects of Early Reduction Allowances?
  - How will Combined Heat/Power (CHP) facilities be treated?
  - Should Oregon deem its in-state biomass combustion as carbon neutral?
  - Should companies subject to the cap be treated differently if there are no immediately available substitutable processes for the industrial processes that result in the regulated emissions? If so, how (e.g., recognition in distribution of allowances)? If the company has made investments in its processes within the last (10 years?), and those processes place it in the top quartile for GHG efficiency per unit of output, should it merit different treatment under the cap? If so, how?
5. **Distribution of Compliance Costs**: Since carbon emissions are a product of most of our business and personal activities, an equitable distribution of costs is critical to the success of and public support for any strategy. Our ability to accomplish this may depend on the following:
- Can we assure that all significant producers of carbon emissions subject to the WCI cap & trade framework must participate in reductions, not just the easiest to regulate. Thus while electric utilities may be most accessible to new regulation, the Commission concurs with WCI that other sources – most particularly industrial emitters and transportation – must be included as well.
  - Can design of WCI carbon markets assure that participants are neither unduly benefited nor penalized? Thus, equitable access to allowances may need to be ensured for regulated emitters with relatively less market power, such as smaller consumer-owned utilities (but that still exceed the 25,000 tonne threshold subject to the WCI cap and trade). If free allowances are issued to any participant, can this be done under rules that prevent windfall profits from accruing as a consequence of carbon allowance trading? If unregulated third parties are permitted to participate in auctions or market transactions to increase market liquidity, can this be done under rules that prevent market manipulation or limit access to allowances by participants with less market power?
  - Under a cap and trade, higher energy costs may disproportionately affect low-income consumers. How will provision be made for targeted assistance to these parties, particularly through energy efficiency investments that reduce consumer energy *costs* even as *prices* may be rising?
  - Under a cap and trade, workers may be displaced as a result of employer responses to carbon regulation. How will provision be made for targeted public assistance such as retraining, extended unemployment benefits, and, other forms of financial transition support?

6. **Competitiveness and Leakage Issues:** There is legitimate concern over the ability of a regional cap and trade to prevent leakage (e.g., emissions and production of goods relocating from inside the capped WCI region to outside, thwarting real overall emissions reductions). Many of Oregon's primary manufacturing employers produce global commodities (e.g., steel, cement, pulp and paper). These companies are price takers in global markets, not price setters, and may be disadvantaged competitively by such leakage effects. How can Oregon and other WCI participants anticipate and address economic hardship to these companies that may be materially and adversely affected by competition from areas not subject to WCI cap and trade regulation? How can Oregon and other WCI participants deal with carbon content from goods imported from areas not subject to WCI cap and trade regulation?
7. **Compliance Flexibility Tools; Consideration of a "Circuit Breaker":** The Commission appreciates that WCI Design Recommendations includes significant market flexibility tools to manage economic impacts on regulated entities, including banking of allowances and use of offsets. WCI and the State may wish to consider as well a limited "circuit breaker" mechanism that could temporarily cap the compliance costs a regulated company would see in extraordinary circumstances such as a breakdown in allowance market functioning. Such a mechanism should be designed to trip only rarely in order to preserve market predictability, and designed to resume normal market function – and progress toward meeting Oregon's GHG reduction goals – when costs fall back below the established threshold. Oregon would need to negotiate any such instrument with its WCI partners.
8. **Availability and Use of Offsets :** It is generally recognized that offsets may present low cost greenhouse gas reduction opportunities and that the wider the market from which offsets may be acquired, the lower average prices should be. How extensively should emitters subject to the cap be able to use offsets to meet compliance obligations in lieu of direct reduction of GHG emissions Should there be geographic as well as quantitative limitations on accessing offsets, in addition to the requirement for rigorous tracking and verification? There is also concern that the rigor of tracking and verification of offsets may suffer as offsets are increasingly relied upon for compliance purposes, and as their sourcing becomes increasingly global (e.g., third world "Clean Development Mechanism/CDM" offsets).
9. **Legal Review:** Can we assure stakeholders that all significant legal issues have been addressed within the final GHG cap-and-trade design? The ultimate purpose of a cap-and-trade mechanism -- to reduce emissions -- would be frustrated if it were delayed or ultimately overturned by a Federal lawsuit. Legal risk is one of the most significant initial objectives to consider when finalizing the details of a proposed WCI framework. It behooves Oregon to subject any WCI or Oregon cap-and-trade design or rule to careful legal review for consistency with Federal and State Constitutional and statutory obligations, and to invite stakeholder comment on that analysis.
10. **Carbon Content of Imported Products:** Should Oregon address the very substantial emissions associated with products (beyond energy) imported from non-WCI jurisdictions for use by Oregonians? What additional analytic or regulatory tools might be required to accomplish this?