Oregon Clean Fuels Program

Item A: Cost Containment

December 16th, 2016
Portland, Oregon

Agenda

- Discuss general themes in the comments from the first meeting
- Walk through two straw proposals for Credit Price containment mechanisms
- Discuss pros and cons

What we heard in the comments

Some clear disagreement about the need for a new mechanism, and if a cap on credit prices is necessary:

- “RPMG believes that allowing for innovation and technology to lead the way in achieving additional GHG reductions in the transportation fuel sector is far preferable to deferrals and/or artificial price manipulations.”
- WSPA: “There should be a true relief valve from credit price spikes”
- UCS: “[A] narrow constraint on metrics like the credit price may not be the best way to protect Oregon citizens from any costs or price instability from fuel costs, to say nothing of the harms of climate change.”

State of Oregon Department of Environmental Quality

What we heard in the comments

- Program's goal is not to generate revenue or punish entities that cannot comply despite good faith efforts
- Avoid creating opportunities for hoarding or gaming
- Fuel prices are complex and time-consuming to analyze, price containment should be based on the program's internal credit market
- Any new mechanisms should not disadvantage Oregon relative to other low-carbon fuel markets
- A price cap mechanism should not displace the fuel supply deferral or program reviews
- Any new mechanism should be reviewed after the credit market has been in operation for some time

What we heard in the comments

Objectives for a new cost containment mechanism should include:

- Promote market and regulatory stability
- Accommodate the natural dynamics of the credit and fuel markets
- Prevent disruptions in the price or supply of transportation fuel at retail
- Maintain the economic incentive to attract low-carbon fuels to Oregon
- Maintain the environmental benefit of the program
- Provide a level playing field for all parties based on free market principles
- Provide a clear path to compliance
- Function predictably and transparently for regulated parties and credit generators

Basics for the Straw Proposals

- DEQ believes that setting the price in terms of the credit price per ton is the most workable option
  - The maximum price for the Credit Clearance Market
  - The price for buying credits from the Credit Window
- The price should be set well above the expected range of trading for CFP credits
- DEQ will seek comments on what the set price should be
- There have been no discussions with the Oregon Dept of Justice on any of these proposals
- The potential cost per gallon impact varies depending on both the credit price and the annual target

DEQ State of Oregon Department of Environmental Quality

Straw Proposal for Oregon CCM

- Oregon DEQ would issue a call to pledge credits roughly a month prior to the submission of annual reports (March)
- In order to pledge credits, the prospective seller would agree to sell the credits at the maximum credit price if a buyer is willing to pay that value
- When annual reports are due (April), DEQ would determine if any regulated parties have shortages of credits
- Those regulated parties would be required to go into the CCM to make up their shortage

Straw Proposal for Oregon CCM

If **more** credits are pledged by sellers than are needed by the regulated parties that need credits, then:

- DEQ posts a list of the pledged sellers and the regulated parties which need to buy credits, along with designated contacts for the entities on both sides.
- The counterparties would be responsible for finding each other and negotiating a deal for the credits.
- Those deals would need to be done and credits transferred within the CFP Online System within a 30-day period.
- Once the credits are retired, the regulated parties would be in compliance.

Straw Proposal for Oregon CCM

If **fewer** credits are pledged into the CCM than are needed by the regulated parties to achieved full compliance, then:

- DEQ posts a list of sellers and buyers,
- DEQ calculates the pro-rata share for each buyer that they are required to buy
- Deals are completed within the CCM 30-day window for trading
- The remaining unfilled deficits are charged a 5% interest rate and rolled forward to next year’s compliance obligation
- Those rolled-over deficits must be filled within five years, and are charged an annual interest rate of 5% each year they are unfilled

DEQ State of Oregon Department of Environmental Quality

Straw Proposal for Oregon CCM

Any clarifying questions?

State of Oregon Department of Environmental Quality

Straw Proposal for Oregon CW

- Credit windows and alternative compliance payments (ACPs) are functionally similar.
- Comments received were generally opposed to ACPs so this discussion is focused on just the credit window option.
- Any usage of the funds may be constrained by existing law.
- If not, DEQ would seek comment on what to use these funds for.

Straw Proposal for Oregon CW

- DEQ would make ‘paper’ credits available at a set price for a period of time following the submission of annual reports.
- The credits would be:
  - available only to regulated parties with unfilled deficits at the time of the annual report
  - used in order to fill deficits associated with that annual report; they cannot be banked or traded
  - available only if the regulated party had no other credits in their account and had attempted to purchase real credits in the market

Straw Proposal for Oregon CW

Any clarifying questions?

State of Oregon Department of Environmental Quality

Other Considerations

Importers of finished fuel

- Have fewer options for compliance
- Is there a way to design a cost containment mechanism to give them priority status?
  - Allow importers of finished fuel to buy credits before importers of blendstocks
  - If the CCM can't supply all of the credits needed, then allow importers of finished fuel to enter the CCM first and then calculate the pro-rate share of the remaining credits for importers of blendstocks who have a greater ability to come into compliance through biofuel purchases, blending, or other means

Other Considerations

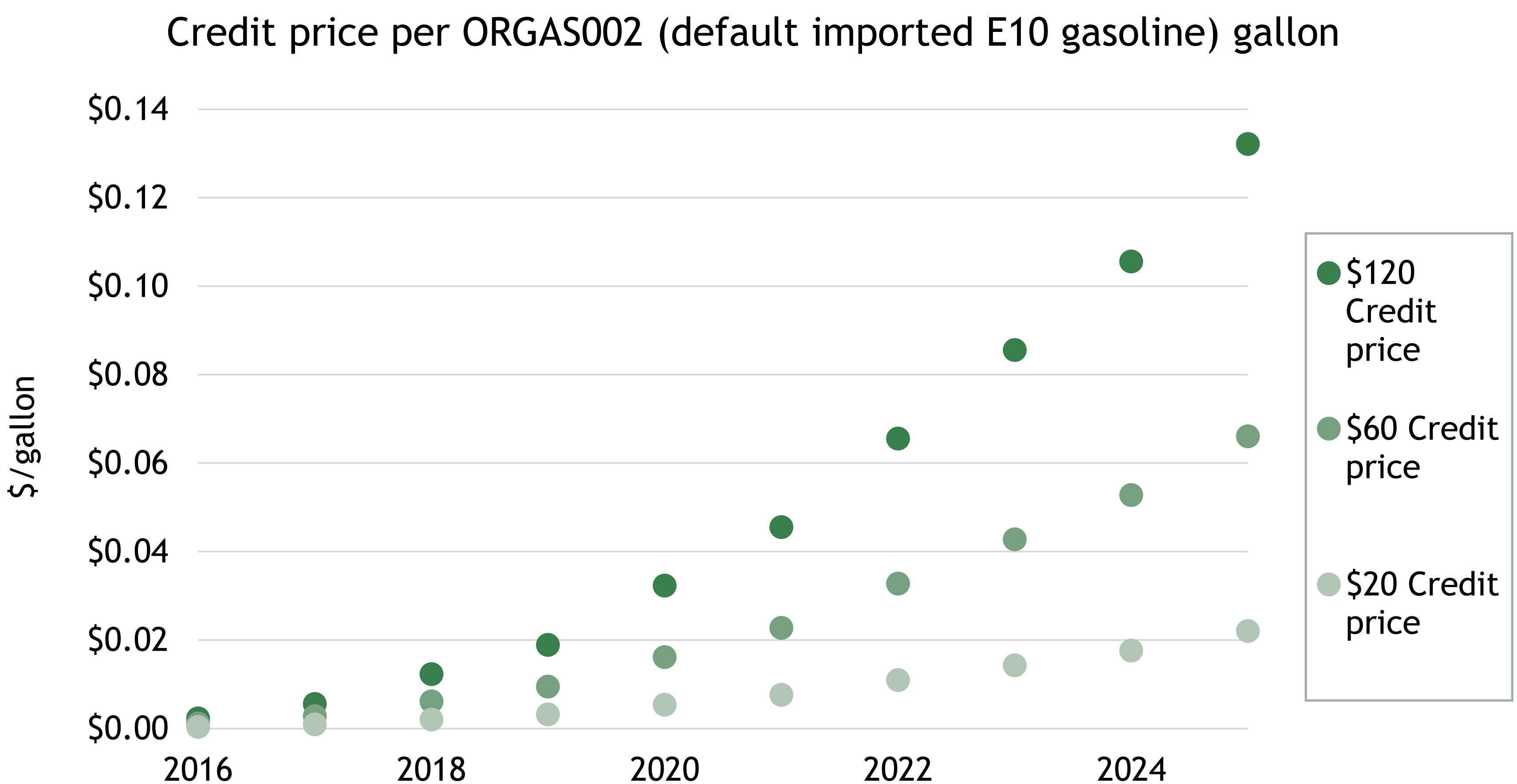
- The mechanism could prioritize exhaustion of market supplies of real credits prior to allowing paper credits, or alternative compliance payments

- One option for that prioritization could be through nesting one mechanism inside of the other
  - For example, a credit clearance market at $X, and second phase credit window at $(X+50)

- Second phase would create a harder cap, but be set at a high enough level that the economic logic is to exhaust any real supplies in the first step

DEQ
State of Oregon Department of Environmental Quality

Retail Impact



State of Oregon Department of Environmental Quality

Next Steps

- Written comments are due by COB Tuesday, January 3, 2017 to: OregonCleanFuels@deq.state.or.us

- DEQ will review oral and written public comments and use those to inform the next step in its discussions