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On September 23, 2008, the Western Climate Initiative (WCI) issued its "Design Recommendations for the WCI Regional Cap-and-Trade Program" (available at [www.westernclimateinitiative.org](http://www.westernclimateinitiative.org)). WCI's Design Recommendations are intended to effect its stated goal of reducing WCI partner states' greenhouse gas (GHG) emissions levels to 15% below 2005 levels by the year 2020.

With the defeat in the Senate of the Boxer-Lieberman-Warner Climate Security Act bill earlier this year and with the absence of any federal legislation governing the reduction of GHG emissions nearing passage, state governments have stepped in to fill the void. On September 25, 2008, the Regional Greenhouse Gas Initiative (RGGI) (comprising Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island and Vermont) will auction its first tradable allowances under its cap-and-trade system. RGGI caps the GHG emissions of electricity power generators, requiring a 10% reduction in these GHG emissions by 2018.

WCI's Design Recommendations are intended to exceed the scope of RGGI's sole focus on electric power generators. WCI describes its Design Recommendations as the "most comprehensive cap-and-trade program designed to date." The Design Recommendations purport to cover nearly 90% of GHG emissions in WCI partner states, and would cover more emissions sources than either RGGI or the European Union's Emissions Trading Scheme (EU-ETS)—the oldest of the GHG emissions cap-and-trade systems.

Currently, Arizona, California, Montana, New Mexico, Oregon and Utah and the Canadian provinces of British Columbia, Manitoba, Ontario and Quebec are WCI committed "partner" states. For now, Alaska, Colorado, Idaho, Kansas, Nevada and Wyoming, the Canadian province of Saskatchewan and the Mexican states of Baja California, Chihuahua, Coahuila, Nuevo Leon, Sonora and Tamaulipas are WCI non-committed "observer" states. Notably, of the ten member states in RGGI, three of

those states committed after first being observers.

While the specific protocols have yet to be designed, the Design Recommendations do make clear the following:

GHGs Covered: All six of the GHGs currently recognized by the United Nations Framework Convention on Climate Change are covered—carbon dioxide (CO<sub>2</sub>), methane (CH<sub>4</sub>), nitrous oxide (NO<sub>x</sub>), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs) and sulfur hexafluoride (SF<sub>6</sub>).

Compliance Periods: Mandatory compliance with GHG emissions caps will begin on January 1, 2012. The First Compliance Period will begin on January 1, 2012 and end on December 31, 2014. The Second Compliance Period will begin on January 1, 2015 and end on December 31, 2017. The Third Compliance Period will begin on January 1, 2018 and end on December 31, 2020. Future compliance periods and obligations will be determined at a later time.

Sectors Covered:

- All "facilities" (direct emitting sources) and "entities" (sources upstream of direct emitting sources) emitting more than 25,000 metric tons of carbon dioxide equivalent (CO<sub>2e</sub>) annually will have their emissions capped.
- The following sectors will be capped beginning in the First Compliance Period: electricity generation (including imported electricity), combustion at industrial and commercial facilities, industrial process emission (emissions from chemical, biological and other non-combustion process) sources, including oil and gas process emissions.
- Beginning in the Second Compliance Period, residential, commercial and industrial fuel combustion, transportation fuel combustion from gasoline and diesel GHG emissions will be subject to upstream caps.
- Carbon-neutral biomass and the CO<sub>2e</sub> emissions from the combustion of pure biofuels (or the related portion of such biofuels in a mixture) will not be regulated and capped, but must be reported.

Emissions Cap; Allowances; Penalties:

Allowances (each allowance represents the permission to emit 1 metric ton of CO<sub>2e</sub>) will be budgeted to each WCI partner state, based upon a "best estimate of expected annual emissions for those sources covered in the initial year of the program." The aggregate budgeted allowances will equal the regional emissions cap. While the budgeted allowances may be used and allocated by WCI partner states as they see fit, the Design Recommendations provide that (1) a minimum of 10% of those allowances must be auctioned, with that minimum to be increased to 25% in 2025, and (2) a minimum of 5% of those allowances must have a minimum or reserve price. By the end of 2009, WCI partner states will coordinate on a procedure to auction allowances on a regional basis.

All WCI allowances will be fungible and tradable. While banking of allowances is permitted, borrowing of allowances from future Compliance Periods is not. In the event that a facility or entity is not able to demonstrate compliance by surrendering sufficient allowances to cover each metric ton of CO<sub>2e</sub> it emits, it will suffer a penalty of three allowances for every shortfall allowance.

Offsets: Emissions credits from GHG emissions offset projects will be allowed, but will be limited to 49% of the total emissions reductions from 2012 through 2020. Projects must be real, surplus/additional, verifiable and permanent—standards that are consistent with those in international and U.S. voluntary markets. WCI has identified three project types for offset projects: (1) agriculture (soil sequestration and manure management); (2) forestry activities (afforestation/reforestation, forest management, forest preservation/conservation, forest products); and (3) waste management (landfill gas and wastewater management).

Early Action: The Design Recommendations recognize early action to reduce GHG emissions. The Design Recommendations provide for both "Early Reduction Allowances" that are achieved between January 1, 2008 and January 1, 2012, as well as early action or set-asides allowances. The former will be standardized between the WCI partner states, and awarded to each WCI partner state as supplemental budgeted allowances; the latter may be awarded as any individual WCI partner state sees fit, but will not be in addition to its budgeted allowance.

Measurement and Reporting: All entities and facilities emitting at least 10,000 metric tons of CO<sub>2e</sub> must begin reporting on January 2010. Measurement and reporting must be verified by a third party.

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