SENATE BILL REPORT
SB 5735

As of February 11, 2009

Title: An act relating to reducing greenhouse gas emissions.

Brief Description: Reducing greenhouse gas emissions.

Sponsors: Senators Rockefeller, Hargrove, Jacobsen, Ranker, Fraser, Keiser, Jarrett, Franklin, Shin, Kohl-Welles, Regala, McAuliffe and Kline; by request of Governor Gregoire.

Brief History:
Committee Activity: Environment, Water & Energy: 2/03/09, 2/10/09.

SENATE COMMITTEE ON ENVIRONMENT, WATER & ENERGY

Staff: William Bridges (786-7416)

Background: Cap and Trade. In general terms, a cap-and-trade program is a market-based mechanism to reduce air pollution. First, a cap is set on an air pollutant. Entities are then given or sold "allowances" to emit the pollutant. Entities with unused allowances are allowed to sell their surpluses to entities that have overspent their allowances. Sometimes, a cap-and-trade program allows the use of "offsets," which are emission cuts outside the cap but are nonetheless treated like an allowance.

A U.S. cap-and-trade program was established for sulfur dioxide in 1990. In 2005, the European Union enacted a cap-and-trade program for CO2 emissions called the European Union Emission Trading System. In the U.S., the first mandatory cap-and-trade program for CO2 emissions is the Regional Greenhouse Gas Initiative (RGGI), an effort of ten northeastern states that auctioned its first allowances last fall.

Western Climate Initiative (WCI). In 2007 the governors of Arizona, California, New Mexico, Oregon, and Washington formed the WCI. They were later joined by Montana and Utah, and the Canadian provinces of British Columbia, Manitoba, Ontario, and Quebec. Other U.S. and Mexican states have joined as observers.

The WCI has recommended the implementation of a cap-and-trade program as part of a comprehensive regional effort to reduce greenhouse gas (GHG) emissions by 15 percent below 2005 levels by 2020.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Washington's GHG Emission Reduction Targets. In 2008 the Legislature set the following GHG reduction targets for the state:

- by 2020 reduce overall GHG emissions in the state to 1990 levels;
- by 2035 reduce overall GHG emissions in the state to 25 percent below 1990 levels; and
- by 2050 reduce overall GHG emissions in the state to 50 percent below 1990 levels, or 70 percent below the state's expected GHG emissions that year.

The Legislature also required the Department of Ecology (DOE), in coordination with the WCI, to develop a design for a regional multisector market-based system to limit and reduce GHG emissions. The design was presented to the Legislature in December 2008, and its concepts are addressed in this bill.

Summary of Bill: Authorizing the Creation of a Regional Cap-and-Trade Program. DOE is authorized to create an allowance trading program for GHG emissions. DOE may not implement a cap-and-trade program that covers only the state, nor may it implement a cap-and-trade program until it covers the majority of the WCI's emissions or it is linked to other regional or national programs covering the equivalent amount of emissions.

Setting the Cap. By rule, DOE must set declining annual allowance caps from 2012 to 2020, and the caps must continue to decline until the state's GHG emission targets are met. The allowance caps for 2012 to 2020 must be set in advance of the program start in 2012. Allowance caps for each year after 2020 must be set at least three years in advance of the start of the next compliance period. One percent of the state's 2012 allowances must be pooled with allowances from the other WCI partners and reallocated using a formula that considers such factors as a partner's population growth and energy production and consumption.

Issuing and Retiring Allowances. DOE is authorized to issue and retire allowances. By rule, DOE must develop the following: (1) determinations on how to distribute the allowances, including the use of auctions consistent with the WCI; (2) a process for identifying and tracking allowances; (3) a schedule for distributing the state's allowances; (4) criteria for early reduction allowances; (5) a process for banking allowances; (6) prohibitions on borrowing allowances; and (7) criteria limiting allowances from other jurisdictions. DOE must convene a stakeholder group with equal representation from business and public interests to develop recommendations on how to distribute the state's allowances.

Specifying Covered Emissions. Starting in 2012, the cap-and-trade program must cover emissions that meet or exceed 25,000 metric tons of CO_2 equivalents annually from the following: (1) electricity that is generated or consumed within the state; (2) combustion at industrial and commercial facilities; and (3) industrial processes.

Starting in 2015 the program must cover emissions that meet or exceed 25,000 metric tons of carbon dioxide equivalents annually from the following: (1) transportation fuel combustion within the state; (2) residential fuel combustion within the state; and (3) fuel delivered or sold for industrial and commercial combustion within the state.

Certain emissions from woody biomass and biofuels are not covered by the cap-and-trade program

By rule, DOE must determine who has the compliance obligation for covered emissions. It may also expand the program below 25,000 metric tons to ensure consistency with the WCI.

Preventing Market Manipulation. When designing the cap-and-trade program, DOE must consult with other WCI partners and other state and federal agencies in developing provisions to prevent market manipulation. The cap-and-trade design must include auditing measures, penalties, and other provisions necessary to prevent market manipulation. DOE must provide a report to the Legislature by December 31, 2010, on the design of the market and explanations on how manipulation and speculation will be avoided.

Allowing Offsets. By rule, DOE must set criteria for issuing and accepting offset credits for meeting the emission caps. Offsets must be consistent with limitations established by the WCI, and they may include offsets recognized by other specified international programs. Priority must be given to investigating and developing criteria for offset projects within the forestry, agriculture, and waste management sectors.

When developing the criteria for forestry offsets within the WCI, DOE must advance the policies developed from consultations with the Forest Practices Board, the Department of Natural Resources (DNR), and the Forest Carbon Working Group.

Recommending Financial Incentives for Forestry. DOE must consult with the Forest Practices Board, DNR, and the Forest Carbon Working Group to develop and deliver to the Legislature by December 31, 2010, legislation to implement a financial incentives program for forestry and forest products.

Specifying Compliance and Enforcement Provisions. By Rule, DOE must specify the date when allowances and offsets must be submitted to the department. Penalties for noncompliance are three allowances for every one that was due. Appeals may be made to the Pollution Control Hearings Board. DOE may exercise its discretion to waive or reduce penalties for inadvertent violations. A failure to submit penalty allowances may result in a fine up to $5,000 for each penalty allowance not submitted.

Creating the Climate Protection Account. An account is created for any auction revenues and penalties received. The account may only be used for specified purposes listed in descending priority, with the first being the reduction of price impacts for low-income consumers.

Authorizing Agreements to Form a Regional Administrative Organization. The director of DOE is authorized to enter into an agreement with representatives of other WCI jurisdictions to form an organization that may carry out regional administrative functions, such as the coordination of regional auctions of allowances and the tracking of emissions. The bill states that Washington is not waiving its sovereign immunity by entering into such an agreement.

Posting GHG Emission Summaries. DOE must compile and post annual summaries of GHG emissions covered by the cap-and-trade program. The posting of the summaries and underlying data may be delayed to allow coordination with the WCI schedule. Prior to the WCI common posting date, the summaries and underlying data are exempt from public disclosure.

Specifying the Rulemaking Schedule. DOE's rules relating to the cap-and-trade program must be adopted December 31, 2010. An 11-member work group, including two Senators and two Representatives, must review DOE's rules and make recommendations to the Governor by May 1, 2011. The rules may not go into effect until June 1, 2011, and after approval of the Governor.

Accommodating a Federal Cap-and-Trade Program. DOE may modify or repeal its cap-and-trade program rules in order to participate in a federal cap-and-trade program.

Providing for Economic Emergencies. The Governor is authorized delay or suspend the cap-and-trade program for up to a year in the event of an economic emergency.

Maintaining Tribal Sovereignty. DOE must consult with tribal governments upon request on any elements of the cap-and-trade program that may affect tribal governments. Nothing in this bill is intended to expand state authority over Indian country.

Specifying GHG Emission Reporting Requirements. By rule, DOE must develop reporting requirements for the following: (1) imported fuels that will be combusted in the state with annual emissions of at least 10,000 metric tons of GHG; and (2) imported electricity for consumption in the state with associated emissions of at least 10,000 metric tons of GHG. Reporting must begin in 2011 for emissions in 2010. Failure to report emissions may result in a penalty of up to $10,000 per day that emissions are not reported after a deadline.

Defining Terms. Various terms are defined, including "allowances," which means a limited authorization, which is not a property right, to emit up to one metric ton of a GHG greenhouse gas as measured in CO2 equivalents.

Findings. Numerous findings are made, including that a well-functioning market is the least-costly path to achieving the state's statutory GHG reductions and that the market must be designed to prevent manipulation and avoid excessive speculation.

Other Changes. An expiration date of May 1, 2012, is set for the provisions in E2SHB 2815 (2008) that required DOE to submit a GHG reduction plan for review and approval to the Legislature by December 1, 2008.

Appropriation: None.

Fiscal Note: Requested on January 29, 2009.
[OFM requested ten-year cost projection pursuant to I-960.]

Committee/Commission/Task Force Created: Yes.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: The Legislature established the GHG targets last session and the challenge now is to decide how to effectively and efficiently meet those targets. The state exported $16 billion for fossil fuels; that money could have stayed in the state for the development of renewable energy. Washington's involvement with the WCI is important to influence the Congressional debate on a national cap-and-trade program. The business-as-usual reliance on voluntary action is not good enough – emitters need to be held accountable for any claimed reductions. With green building legislation, clean car legislation, and a GHG emissions performance law, the Washington Legislature has been an environmental leader the last several years. This bill needs to continue that legacy and to meet the mandated reduction targets. Cap-and-trade is not new; it has worked for SO_2 and it is being applied to CO_2 in Europe and in the Northeastern U.S. Cap-and-trade is the only program that can assure Washington will meet the mandated targets. The costs of not acting on cap-and-trade are high: rising firefighting costs, reduced stream flows, rising health-care costs, and agricultural loses. The current economic recession will end and something must be in place in 2012 if the state is to reach its reduction targets. The Governor may delay the program for up to one year if the recession continues past 2012. King County is already participating in the Chicago Climate Exchange. The country needs a structural change; we can no longer rely on cheap oil. The old economy is not hiring and the new economy is. The bill recognizes hydro by reallocating allowances out of a 1 percent common pool. Allowances should be auctioned and not distributed according to historic emissions.

CON: Businesses are struggling in the current economic recession and a cap-and-trade program would be very expensive, costing billions and jeopardizing thousands of jobs. A single national program is best. Many of the Washington companies operate in a world economy, and these companies would be at a competitive disadvantage if they had to incorporate allowance costs into their products. Many of these companies would either move to a nonWCI state or go out of business. A regional cap-and-trade would discourage investments in Washington. The effects of a regional cap-and-trade program are hard to model, so companies will have a difficult time making investment decisions. The bill delegates too much authority to DOE, and it does not protect Washington's unique hydro system. Market oversight provisions need to be determined before launching into a cap-and-trade program. The bill does not address the effect of low-water years on the hydro system, which could require utilities to rely on coal power and expensive allowances. When it comes to protecting Washington's hydro system, it is time that Washington dictate to the WCI and not the other way around. Why would the Legislature consider destroying Washington's economy in an attempt to impress the federal government? When mills close, the state's carbon footprint rises because the foreign products that are imported are produced with dirtier power. New Zealand has been unsuccessful in setting up a cap-and-trade program and that uncertainty has led to deforestation. The bill does not recognize previous efficiency efforts by companies. The bill is a blank canvas for DOE, and DOE has no duty to follow the recommendations of any of the work groups. The California experience with climate change efforts shows they underestimated the costs to their economy.

Persons Testifying: PRO: Senator Rockefeller, prime sponsor; Genesee Adkins, City of Seattle; Paul Birkeland, William Brent, Randi Gladwell, citizens from Seattle; Jessica Finn Coven, Climate Solutions; Bob Doppett, Climate Leadership Institute; Matt Kuharic, King County; Jay Manning, DOE; Ethan Schaffer, Bainbridge Graduate Institute; Clifford Traisman, Washington Conservation Voters and Washington Environmental Council.

CON: Cali Daly, NW Food Processors Association; Kyle Davis, PacifiCorp; Mark Doumit, WFPA; Nancy Hiteshue, Washington Roundtable; Bart Kale, Nucor Steel; Kent Lopez, Washington Rural Electric Cooperatives; Llewelln Mathews, NWPPA; Dave McEntee, Simpson Investments; Mike Mosman, Port Blakely Tree Farms; Grant Nelson, AWB; Steve Smith, Cardinal Glass; Tamara Smilanich, citizen from Seattle; Collins Sprague, Avista; Bill Turlay, citizen from Vancouver; Dave Warren, Washington PUD Association.

Signed in, Unable to Testify & Submitted Written Testimony: PRO: William Brent, Webber Shandwick, citizens; Dick Ewing, Farm Bureau, Winthrop.

CON: Wes McCart, Stevens County Farm Bureau.

OTHER: Amber Gunn, Evergreen Freedom Foundation.