
Environment & Energy Committee

E2SSB 5126

Brief Description: Concerning the Washington climate commitment act.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Carlyle, Saldaña, Conway, Das, Frockt, Hunt, Lias, Nguyen, Pedersen, Salomon, Stanford and Wilson, C.; by request of Office of the Governor).

Brief Summary of Engrossed Second Substitute Bill

- Establishes a program for capping emissions from certain covered entities and investing emission allowance auction proceeds in certain programs, projects, and activities, beginning January 1, 2023.

Hearing Date: 4/14/21

Staff: Nikkole Hughes (786-7156).

Background:

Greenhouse Gas Emissions Reporting.

The United States Environmental Protection Agency (EPA) and the Department of Ecology (Ecology) identify carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride as greenhouse gases (GHGs) because of their capacity to trap heat in the Earth's atmosphere. According to the EPA, the global warming potential (GWP) of each GHG is a function of how much of the gas is concentrated in the atmosphere, how long the gas stays in the atmosphere, and how strongly the particular gas affects global atmospheric temperatures. Under state law, the GWP of a gas is measured in terms of the equivalence to the emission of an identical volume of carbon dioxide over a 100-year timeframe (carbon dioxide equivalent or CO₂e).

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

Under the federal Clean Air Act, GHGs are regulated as an air pollutant and are subject to several air regulations administered by the EPA. These federal Clean Air Act regulations include a requirement that facilities and fuel suppliers whose associated annual emissions exceed 25,000 metric tons of CO₂e report their emissions to the EPA. At the state level, GHG reporting is regulated by Ecology under the state Clean Air Act. This state law requires facilities, sources, and sites whose emissions exceed 10,000 metric tons of CO₂e each year to report their annual emissions to Ecology. Distributors of gasoline, diesel, and aircraft fuel whose GHG emissions exceed 10,000 metric tons and who pay fuel taxes to the Department of Licensing (DOL) must use the fuel sale information submitted for the DOL fuel tax purposes to report to the state the GHG emissions associated with the fuel.

Ecology and the Department of Commerce must report to the Governor and Legislature by December 31 of even-numbered years regarding total GHG emissions and GHG emissions by source sector in Washington. According to the most recent Ecology data, as of 2017 the total annual GHG emissions in Washington were estimated at 97.5 million metric tons (MMT) of CO₂e. Of these emissions, a total of 43.26 MMT CO₂e were attributable to transportation sources, of which on-road gasoline accounted for 21.53 MMT CO₂e and on-road diesel accounted for 8.36 MMT CO₂e.

Statewide Emissions Limits.

In 2008 Washington enacted legislation that sets a series of limits on the emission of GHGs within the state. Ecology is responsible for monitoring and tracking the state's progress toward the emission limits. In 2020 additional legislation was enacted to update the state limits to the following:

- By 2020, reduce overall emissions of GHGs in the state to 1990 levels, or 90.5 MMT.
- By 2030, reduce overall emissions of GHGs in the state to 45 percent below 1990 levels, or 50 MMT.
- By 2040, reduce overall emissions of GHGs in the state to 70 percent below 1990 levels, or 27 MMT.
- By 2050, reduce overall emissions of GHGs in the state to 95 percent below 1990 levels, or 5 MMT, and achieve net-zero GHG emissions.

Clean Energy Transformation Act.

Under the Clean Energy Transformation Act, electric utilities in Washington must:

- eliminate coal-fired resources from their allocation of electricity by December 31, 2025;
- ensure that all retail sales of electricity to Washington customers are GHG neutral by January 1, 2030; and
- supply 100 percent of all retail sales to Washington customers with nonemitting and renewable resources by January 1, 2045.

Environmental Justice.

A proviso in the 2019-2021 Biennial Operating Budget directed the Governor's Interagency Council on Health Disparities to convene and staff an Environmental Justice Task Force (Task Force). The Task Force was directed to recommend strategies for incorporating environmental justice principles into future state agency actions across Washington. The Task Force published a report with its recommendations in the fall of 2020.

In 2018 a collaborative group began making available to the public an interactive mapping tool that compares communities across Washington for environmental health disparities, known as the Washington Environmental Health Disparities Map (Map). The Map was developed by the University of Washington's Department of Environmental and Occupation Health Sciences, Front and Centered, the departments of Health and Ecology, and the Puget Sound Clean Air Agency. The Map includes 19 specific indicators of health disparities, which are divided into four themes: environmental exposures, environmental effects, sensitive populations, and socioeconomic factors.

Summary of Engrossed Second Substitute Bill:

Cap and Invest Program.

In order to ensure that greenhouse gas (GHG) emissions are reduced consistent with the state's 2030, 2040, and 2050 emissions limits, the Department of Ecology (Ecology) must implement a cap on GHG emissions from covered entities and a program to track, verify, and enforce compliance through the use of compliance instruments (Cap and Invest Program, or Program).

The Program must consist of:

- annual allowance budgets that limit emissions from covered entities;
- defining those entities covered by the Cap and Invest Program, and those entities that may voluntarily opt into coverage under the Program;
- distribution of emission allowances;
- providing for offset credits as a method for meeting a compliance obligation;
- defining the compliance obligation for covered entities;
- establishing the authority of Ecology to enforce the program requirements;
- creating a Climate Investment Account for the deposit of receipts from the distribution of emission allowances;
- providing for the transfer of allowances and recognition of compliance instruments, including those issued by jurisdictions that may be linked with the state;
- providing monitoring and oversight of the sale and transfer of allowances;
- creating an Environmental Justice and Equity Advisory Panel to monitor impacts of the Cap and Invest Program on overburdened communities, advise on achieving positive workforce and job outcomes, and the equitable distribution of benefits to overburdened communities; and
- creating a price ceiling and associated mechanisms.

Ecology must consider opportunities to implement the Cap and Invest Program in a manner that allows linking the Program with those of other jurisdictions.

Environmental Justice.

Cap and Invest Program Review.

To ensure that the Cap and Invest Program achieves reductions in criteria pollutants as well as GHG emissions in overburdened communities highly impacted by air pollution, Ecology must:

- utilize the Department of Health's Environmental Health Disparities Map and complementary data to identify a high-priority list of overburdened communities where the highest emissions or concentrations of criteria pollutants are occurring;
- deploy an air monitoring network in high-priority overburdened communities to collect sufficient air quality data for the 2025 review and subsequent reviews of criteria pollutant reductions; and
- within the identified communities, analyze and determine which sources are the greatest contributors of criteria pollutants and develop a high-priority list of significant emitters.

Prior to listing any entity as a high-priority emitter, Ecology must notify that entity and share the data used to rank that entity as a high-priority emitter, and provide a period of not less than 60 days for the covered entity to submit more recent data or other information relevant to the designation of that entity as a high-priority emitter.

Beginning in 2025, and every two years thereafter, Ecology must conduct a review to determine if criteria pollutants are being reduced in identified overburdened communities. If this review finds that criteria pollutants are not being reduced in an identified overburdened community, then Ecology, in consultation with local air pollution control authorities, must establish air quality targets to achieve air quality consistent with neighboring communities that are not identified as overburdened. Ecology must also identify the sources that are the contributors of those emissions that are either increasing or not decreasing, and achieve the reduction targets through adoption of emissions control strategies or other methods.

In developing a high-priority list of overburdened communities and an air monitoring network, Ecology must create and adopt a community engagement plan to describe how it will engage with overburdened communities and vulnerable populations.

Environmental Justice Assessment.

When allocating funds from the Climate Investment Account or administering grants or programs funded by the account, state agencies must conduct an environmental justice assessment and establish a minimum of not less than 35 percent and a goal of 40 percent of total investments that provide direct and meaningful benefits to vulnerable populations within the boundaries of overburdened communities.

Agencies allocating funds or administering grants or programs from the Climate Investment Account must:

- report annually to the Environmental Justice and Equity Advisory Panel and the Office of Equity regarding progress toward meeting environmental justice and environmental health goals;
- consider recommendations by the Environmental Justice and Equity Advisory Panel; and
- create and adopt a community engagement plan.

Environmental Justice and Equity Advisory.

The Office of Equity must establish an Environmental Justice and Equity Advisory Panel (Advisory Panel) to provide recommendations to the Legislature, state agencies, and the Governor in the development and implementation of the Cap and Invest Program and the programs funded from the Climate Investment Account.

The Office of Equity must convene the Advisory Panel by January 1, 2023. The Office of Equity may seek nominations or recommendations from organizations across the state. Members of the Advisory Panel must be selected for geographic and organizational diversity and must include the following:

- individuals representing the interests of vulnerable populations residing in overburdened communities in different geographic areas of the state with expertise in environmental justice and equity issues;
- individuals representing union labor with expertise in economic dislocation, clean energy economy, or emissions-intensive, trade-exposed facilities;
- at least two members representing federally recognized tribes, with at least one from eastern Washington and one from western Washington; and
- a chair appointed by the Governor.

Tribal Consultation.

Before allocating funding or administering grant programs appropriated from the Climate Investment Account, agencies must engage in consultation with federally recognized tribes on all funding decisions and programs that may impact, infringe upon, or impair the governmental efforts of federally recognized tribes to adopt or enforce their own standards governing or protecting the tribe's resources or other rights and interests in their tribal lands and lands within which a tribe or tribes possess rights reserved by treaty. Agencies must develop a consultation framework in coordination with tribal governments that includes best practices, protocols for communication, and collaboration with federally recognized tribes.

If any funding decision or program that impacts land within which a tribe or tribes possess rights reserved by federal treaty, statute, or executive order is undertaken or funded under the Cap and Invest Program without consultation with a federally recognized tribe, an affected tribe may request that all further action on the decision or program cease until meaningful consultation with any directly impacted federally recognized tribe is completed.

Cap and Invest Program Budget and Timelines.

The program budget of allowances established under the Cap and Invest Program must be set to achieve the share of reductions by covered entities necessary to achieve the state's 2030, 2040, and 2050 emissions limits. Ecology must adopt annual allowance budgets for the Program on a calendar year basis that provide for substantially equivalent reductions on an absolute basis for each year.

An allowance distributed under the Program, either directly by Ecology or through auctions, does not expire and may be held or banked.

Ecology must complete an evaluation by December 31, 2027, and by December 31, 2035, of the performance of the Program, including its performance in reducing GHG emissions. If the evaluation shows that adjustments to the annual budgets are necessary to ensure achievement of the 2030 and 2040 emission reduction limits, Ecology must adjust the annual budgets accordingly. Ecology must complete additional evaluations by December 31, 2040, and by December 31, 2045, and make adjustments in the annual budgets to ensure achievement of the 2050 emission reduction limit. Ecology must determine and make public the circumstances, metrics, and processes that would initiate the public consideration of additional program adjustments to ensure successful achievement of the emission reduction limits.

First Compliance Period, 2023-2026.

By October 1, 2022, Ecology must adopt a budget of allowances for the first compliance period of the Cap and Invest Program to be distributed from January 1, 2023, through December 31, 2026. The program budget of allowances for the first compliance period must be based on an emissions baseline establishing the proportionate share that the total GHG emissions of covered entities for the first compliance period bears to the total anthropogenic GHG emissions in the state during 2015 through 2019, based on data reported to Ecology under the state's GHG Emissions Reporting Program.

Second Compliance Period, 2027-2030.

By October 1, 2026, Ecology must add to its emissions baseline by incorporating the proportionate share that the total GHG emissions of new covered entities in the second compliance period bear to the total anthropogenic GHG emissions in the state during 2023 through 2025. Ecology must adopt a program budget of allowances for the second compliance period to be distributed from January 1, 2027, through December 31, 2030.

Compliance Periods Beginning in 2031.

By October 1, 2028, Ecology must adopt by rule the annual program budgets of allowances for the calendar years 2031 through 2040.

Entities Covered Under the Cap and Invest Program.

First Compliance Period, 2023-2026.

A person is a covered entity as of the beginning of the first compliance period and all subsequent compliance periods if the person reported emissions for any calendar year from 2015 through 2019 under the GHG Emissions Reporting Program, or if additional data reported to Ecology indicates that emissions for any calendar year from 2015 through 2019 equaled or exceeded any of the following thresholds:

- where the person operates a facility and the facility's emissions equal or exceed 25,000 metric tons of carbon dioxide equivalent (MTCO_{2e});
- where the person is a first jurisdictional deliverer of electricity and generates electricity in the state and emissions associated with this generation equals or exceeds 25,000 MTCO_{2e};
- where the person is a supplier of fossil fuel other than natural gas, and from that fuel 25,000 MTCO_{2e} or more would result from the full combustion or oxidation;
- where the person supplies natural gas in amounts that would result in exceeding 25,000 MTCO_{2e} if fully combusted or oxidized, excluding amounts supplied to other covered entities and amounts delivered to opt-in entities;
- where the person who is not a natural gas company and has a tariff with a natural gas company to deliver to an end-use customer in the state in amounts that would result in exceeding 25,000 MTCO_{2e} if fully combusted or oxidized, excluding amounts supplied to other covered entities and amounts delivered to opt-in entities; and
- where the person is an end-use customer in the state who directly purchases natural gas from a person that is not a natural gas company and has the natural gas delivered through an interstate pipeline to a distribution system owned by the purchaser in amounts that would result in exceeding 25,000 MTCO_{2e} if fully combusted or oxidized, excluding amounts supplied to other covered entities and amounts delivered to opt-in entities.

Second Compliance Period, 2027-2030.

A person is a covered entity as of the beginning of the second compliance period and all subsequent compliance periods if the person reported emissions for any calendar year from 2023 through 2025 that equals or exceeds any of the following thresholds:

- where the person is a first jurisdictional deliverer importing electricity into the state and the cumulative annual total of emissions associated with the imported electricity from specified or unspecified sources equals or exceeds 25,000 MTCO_{2e}; and
- where the person operates a waste-to-energy facility utilized by a county and city solid waste management program and the facility's emissions equal or exceed 25,000 MTCO_{2e}.

Compliance Periods Beginning in 2031.

A person is a covered entity beginning January 1, 2031, and all subsequent compliance periods if the person reported emissions for any calendar year from 2027 through 2029, where the person

operates a landfill utilized by a county and city solid waste management program and the facility's emissions equal or exceed 25,000 MTCO_{2e}.

Exempt Emissions.

The following emissions are exempt from coverage under the Cap and Invest Program, regardless of emissions levels:

- emissions from the combustion of aviation fuels;
- emissions from watercraft fuels supplied in Washington that are combusted outside of Washington;
- emissions from the TransAlta coal-fired electric generation facility;
- carbon dioxide emissions from the combustion of biomass or biofuels; and
- emissions from national security facilities.

Addressing Leakage.

The Legislature intends to promote a growing and sustainable economy and to avoid leakage of emissions from manufacturing to other locations. The state must pursue the state's GHG emissions limits in a manner that recognizes that the siting and placement of new best-in-class facilities that provide for the displacement of more carbon intensive processes is in the economic and environmental interests in the state.

For new or expanded facilities that require review under the State Environmental Policy Act (SEPA) and which would result in annual GHG emissions in excess of 25,000 MTCO_{2e}, Ecology must evaluate the net cumulative GHG emissions of the facility, attributing any net displacement of global emissions resulting from the project in Ecology's decision making.

The state's emission reduction limits or GHG emissions that are addressed under the Cap and Invest Program may not be the basis for denial of a permit application or for judicial review of the grant of a permit for a new or expanded emissions-intensive and trade-exposed facility under the SEPA.

Compliance with the requirements of the Cap and Invest Program is the only mitigation for GHG emissions that can be required by any state agency, city, town, county, township, other subdivision, or municipal corporation of the state from these facilities.

Inclusion as a covered or opt-in entity under the Cap and Invest Program constitutes adequate mitigation of any significant adverse impacts with respect to GHG emissions for a facility subject to the requirements of the SEPA.

Registration Requirements.

All covered entities must register to participate in the Cap and Invest Program, following procedures adopted by Ecology by rule. Entities registering to participate in the Program must

describe any direct or indirect affiliation with other registered entities.

A person responsible for GHG emissions that is not a covered entity may voluntarily participate in the Program by registering as an opt-in entity. An opt-in entity must satisfy the same registration requirements as covered entities. Once registered, an opt-in entity is allowed to participate as a covered entity in auctions and must assume the same compliance obligation to transfer compliance instruments equal to their emissions at the appointed transfer dates. An opt-in entity may opt out of the Program at the end of any compliance period by providing written notice to Ecology at least six months prior to the end of the compliance period. The opt-in entity continues to have a compliance obligation through the current compliance period. An opt-in entity is not eligible to receive directly distributed, no cost allowances.

A person that is not covered by the Program and is neither a covered entity nor an opt-in entity may voluntarily participate in the Program as a general market participant. General market participants must meet all applicable registration requirements specified by rule. Federally recognized tribes and federal agencies may elect to participate in the Program as opt-in entities or general market participants.

Ecology must maintain a public roster of all covered entities, opt-in entities, and general market participants on its public website.

Auctions of Allowances.

Except for directly distributed, no cost allowances allocated to certain entities, allowances under the Cap and Invest Program must be distributed through auctions. Ecology must hold a maximum of four auctions each year, plus any necessary reserve auctions. An auction may include allowances from the annual allowance budget of the current year and allowances from the annual allowances budgets of prior years that remain to be distributed. Ecology must make future vintage allowances available through parallel auctions at least twice annually in addition to the auctions through which current vintage allowances are exclusively offered.

Ecology must engage a qualified, independent contractor to run the auctions. Ecology must also engage a qualified financial services administrator to hold the bid guarantees, evaluate bid guarantees, and inform Ecology of the value of bid guarantees once the bids are accepted.

Auctions are open to covered entities, opt-in entities, and general market participants that are registered entities in good standing. Ecology must adopt by rule the requirements for a registered entity to register and participate in a given auction.

To protect the integrity of the auctions, a registered entity or group of registered entities with a direct corporate association are subject to auction purchase and holding limits. Ecology may limit these if the agency deems it necessary to protect the integrity and functioning of the auctions. A covered entity or an opt-in entity may not buy more than 10 percent of the allowances offered during a single auction. A general market participant may not buy more than

4 percent of the allowances offered during a single auction and may not in aggregate own more than 10 percent of total allowances to be issued in a calendar year. No registered entity may buy more than the entity's bid guarantee. No registered entity may buy allowances that would exceed the entity's holding limit at the time of the auction.

Ecology must adopt by rule provisions to guard against bidder collusion and minimize the potential for market manipulation. A registered entity may not release or disclose any bidding information. Ecology may cancel or restrict a previously approved auction participation application or reject a new application if the agency determines that a registered entity has:

- provided false or misleading facts;
- withheld material information that could influence a decision by Ecology;
- violated any part of the auction rules;
- violated registration requirements; or
- violated any of the rules regarding the conduct of the auction.

Ecology must design allowance auctions so as to allow, to the maximum extent practicable, linking with external GHG emissions trading programs in other jurisdictions and to facilitate the transfer of allowances when the state's program is linked with other external GHG emissions trading programs. Ecology may conduct auctions jointly with other linked jurisdictions.

Auction Proceeds.

Upon completion and verification of auction results, the financial services administrator must notify winning bidders and transfer the auction proceeds to the State Treasurer for deposit each fiscal year, as follows:

- For fiscal year 2023, \$127,341,000 must be deposited into the Forward Flexible Account, and the remaining proceeds into the Climate Investment Account.
- For fiscal year 2024, \$356,697,000 must be deposited into the Forward Flexible Account, and the remaining proceeds into the Climate Investment Account.
- For fiscal year 2025, \$366,558,000 must be deposited into the Forward Flexible Account, and the remaining proceeds into the Climate Investment Account.
- For fiscal years 2026 through 2037, \$359,117,000 per year must be deposited into the Forward Flexible Account, and the remaining proceeds into the Climate Investment Account.

The deposits into the Forward Flexible Account made in fiscal years 2023 through 2037 must not exceed \$5.2 billion over the first 16 years of the Cap and Invest Program, and any remaining auction proceeds must be deposited into the Climate Investment Account. The deposits into the Forward Flexible Account must be prorated equally from the proceeds of each of the auctions occurring during each fiscal year.

For fiscal year 2038 and each year thereafter, upon completion and verification of the auction results, the financial services administrator must notify the winning bidders and transfer the auction proceeds to the State Treasurer for deposit, such that 50 percent of the auction proceeds

are deposited into the Forward Flexible Account and the remaining auction proceeds are deposited into the Climate Investment Account.

Forward Flexible Account.

The Forward Flexible Account is created in the State Treasury. All receipts from proceeds directed to the account must be deposited into the account. Moneys in the account may be spent only after appropriation. Expenditures from the account may be used only for transportation projects, programs, or activities identified as forward flexible projects, programs, or activities in an omnibus transportation appropriations act.

Allocations of Allowances to Emissions-Intensive, Trade-Exposed Industries.

First Compliance Period, 2023-2026.

Facilities owned or operated by a covered entity must receive an allocation of allowances for the covered emissions at those facilities at no cost if the operations of the facility are classified as emissions-intensive and trade-exposed (EITE), as determined by being engaged in one or more of the following industry processes:

- metals manufacturing;
- paper manufacturing;
- aerospace product and parts manufacturing;
- wood products manufacturing;
- nonmetallic mineral manufacturing, including glass container manufacturing;
- chemical manufacturing;
- computer and electronic product manufacturing, including semiconductor and related device manufacturing;
- food manufacturing;
- cement manufacturing;
- petroleum refining;
- asphalt refining;
- asphalt paving mixtures and block manufacturing from refined petroleum;
- asphalt shingle and coating manufacturing from refined petroleum; and
- all other petroleum and coal products manufacturing from refined petroleum.

Second Compliance Period, 2027-2030.

By July 1, 2022, Ecology must adopt by rule objective criteria for both emissions intensity and trade exposure for the purpose of identifying EITE manufacturing businesses during the second compliance period of the Cap and Invest Program and subsequent compliance periods. A facility covered for the first compliance period is considered an EITE facility and is eligible for allocation of no cost allowances for the second compliance period. In addition, any covered entity that is a manufacturing business that can demonstrate to Ecology that it meets this criteria is also eligible for treatment as an EITE business and is eligible for allocation of no cost

allowances.

For all compliance periods prior to December 31, 2034, the annual allocation of allowances for direct distribution to a facility identified as EITE must be equal to the facility's proportional obligation of the program budget, multiplied by 100 percent.

Facility-Specific Carbon Intensity Benchmarks.

Ecology must by rule provide for EITE facilities to apply for and receive from the agency an adjustment to the allocation for direct distribution of allowances based on a facility-specific carbon intensity benchmark. If Ecology determines that the net quantity of no cost allowances awarded according to the facility's proportional obligation of the program budget, multiplied by 100 percent, is lower than when using the facility-specific carbon intensity benchmark, Ecology must award additional no cost allowances up to the quantity of allowances resulting from using the facility-specific carbon intensity benchmark. Ecology must adjust the no cost allocation of allowances and credits to an EITE facility to avoid duplication with any other no cost allowances transferred under the Cap and Invest Program.

"Carbon intensity" means the amount of carbon dioxide equivalent emissions from a facility in metric tons divided by the facility-specific measure of production including, but not limited to, units of product manufactured or sold over the same time interval.

Mass-Based Baseline.

If an EITE facility is not able to feasibly determine a carbon intensity benchmark based on its unique circumstances, the entity may elect to use a mass-based baseline that does not vary based on changes in production volumes.

For each year during the first compliance period, these facilities must be awarded no cost allowances equal to 100 percent of the facility's mass-based baseline. For each year during the second compliance period, these facilities must be awarded no cost allowances equal to 97 percent of the facility's mass-based baseline. For each year during the compliance period beginning January 1, 2031, these facilities must be awarded no cost allowances equal to 94 percent of the facility's mass-based baseline.

Except for aerospace product and parts manufacturing EITE facilities, if a facility elects to use a mass-based baseline, it may not later convert to a carbon intensity benchmark during the first three compliance periods of the Cap and Invest Program.

An aerospace product and parts manufacturing EITE facility that is utilizing a mass-based baseline must receive an additional no cost allowance allocation in order to accommodate an increase in production that increases its emissions above the baseline on a basis equivalent, in principle, to those awarded to entities utilizing a carbon intensity benchmark. Ecology must establish methods to award, for any annual period, additional no cost allowance allocations to

such an aerospace product and parts manufacturing EITE facility and, if appropriate based on projected production, to achieve a similar ongoing result through the adjustment of the facility's mass-based baseline. An eligible facility that has elected to use a mass-based baseline may not convert to a carbon intensity benchmark until the next compliance period.

Emissions-Intensive, Trade-Exposed Facility Work Group.

By April 1, 2022, Ecology must convene a work group of EITE facilities and their affiliated trade associations, and independent experts in emissions regulation, industrial practices, or other related fields (Work Group).

By July 31, 2022, the Work Group must establish procedures for calculating carbon intensity benchmarks. The carbon intensity benchmark must be based on data from 2015 through 2019, unless the EITE facility can demonstrate that there have been abnormal periods of operation that materially impacted the facility and the baseline period should be expanded to include years prior to 2015.

By September 15, 2022, each EITE facility must submit its carbon intensity benchmark for the first compliance period to Ecology. The calculation must be consistent with the procedures established by the Work Group.

By November 15, 2022, Ecology must review and approve each EITE facility baseline carbon intensity benchmark.

Report to the Legislature.

By December 1, 2030, Ecology must provide a report to the appropriate committees of the Legislature that describes alternative methods for determining the amount and a schedule of allowances to be provided to facilities owned or operated by each covered entity designated as an EITE manufacturing business. The report must include a review of global best practices in ensuring against emissions leakage and economic harm to businesses in carbon pricing programs and describe alternative methods of emissions performance benchmarking and mass-based allocation of no cost allowances. In developing the report, Ecology must form an advisory group that includes representatives of the manufacturers designated as EITE manufacturing businesses for the first compliance period.

Allocation of Allowances to Electric Utilities.

Ecology must adopt an allocation schedule by rule, in consultation with the Department of Commerce and the Utilities and Transportation Commission, for the provision of allowances at no cost to electric utilities, consistent with a forecast of each utility's supply and demand and the cost burden resulting from the inclusion of the covered entities in each sequential compliance period, as follows:

- by October 1, 2022, for the first compliance period;

- by October 1, 2026, for the second compliance period; and
- by October 1, 2028, for the compliance periods between 2031 and 2045.

Under no circumstances may utilities receive any free allowances after 2045.

Allocation of Allowances to Natural Gas Utilities.

By October 1, 2022, Ecology must adopt rules, in consultation with the Utilities and Transportation Commission, establishing the methods and procedures for allocating allowances to natural gas utilities at no cost during the first two compliance periods. The rules must allow for a natural gas utility to be provided allowances to cover their emissions and decline proportionally with the cap. Allowances allocated at no cost to natural gas utilities must be consigned to auction for the benefit of ratepayers, deposited for compliance, or a combination of both.

By October 1, 2028, Ecology must adopt an allocation schedule for the provision of allowances for the benefit of ratepayers at no cost to natural gas utilities for the compliance periods between 2031 and 2040.

Beginning in 2023, 65 percent of the no cost allowances allocated to natural gas utilities must be consigned to auction for the benefit of customers, including at a minimum eliminating any additional cost burden to low-income customers from the implementation of the Cap and Invest Program. Rules adopted must increase the percentage of allowances consigned to auction by 5 percent each year until a total of 100 percent is reached.

In order to qualify for no cost allowances, covered entities that are natural gas utilities must provide copies of their GHG emissions reports filed with the United States Environmental Protection Agency under 40 C.F.R. Part 98 subpart NN - Supplier of Natural Gas and Natural Gas Liquids for calendar years 2015 through 2021 to Ecology on or before March 31, 2022. To continue receiving no cost allowances, these reports must be provided to Ecology for each reporting year in the manner and by the dates provided under the state GHG Emissions Reporting Program as part of the GHG reporting requirements of the Cap and Invest Program.

Emissions Containment Reserve Withholding.

To help ensure that the price of allowances remains sufficient to incentivize reductions in GHG emissions, Ecology must establish an emissions containment reserve and set an emissions containment reserve trigger price by rule. The trigger price must be set at a reasonable amount above the auction floor price and equal to the level established in jurisdictions with which Ecology has entered into a linkage agreement. In the event that the trigger price is met during an auction, Ecology must automatically withhold allowances as needed. Ecology must convert and transfer any allowances that have been withheld from auction into the emissions containment reserve account.

Allowance Price Containment.

To help minimize allowance price volatility in the auction, Ecology must adopt by rule an auction floor price and a schedule for the floor price to increase by a predetermined amount every year. Ecology may not sell allowances at bids lower than the auction floor price. Ecology's rules must specify holding limits that determine the maximum number of allowances that may be held for use or traded by a registered entity at any one time. Ecology must also establish an auction ceiling price to limit extraordinary prices and to determine when to offer allowances through the allowance price containment reserve.

Offsets.

Ecology must adopt by rule the protocols for establishing offset projects and securing offset credits that may be used to meet a portion of a covered or opt-in entity's compliance obligation under the Cap and Invest Program.

A total of no more than 5 percent of a covered or opt-in entity's compliance obligation during the first compliance period may be met by transferring offset credits. During these years, at least 50 percent of a covered or opt-in entity's compliance obligation satisfied by offset credits must be sourced from offset projects that provide direct environmental benefits in the state.

No more than 4 percent of a covered or opt-in entity's compliance obligation during the second compliance period may be met by transferring offset credits. During these years, at least 75 percent of a covered or opt-in entity's compliance obligation satisfied by offset credits must be sourced from offset projects that provide direct environmental benefits in the state. Ecology may reduce the 75 percent requirement if it determines there is not sufficient offset supply in the state to meet offset demand during the second compliance period.

The offset limits for the first and second compliance periods may be modified by rule when appropriate to ensure the achievement of the statewide emissions limits and to provide for alignment with other jurisdictions to which the state has linked. The limits may also be reduced for a specific covered or opt-in entity if Ecology determines that the entity has or is likely to:

- contribute substantively to cumulative air pollution burden in an overburdened community as determined by criteria established by Ecology; or
- violate any permits required by any federal, state, or local air pollution control agency where the violation may result in an increase in emissions.

An offset project on federally recognized tribal land does not count against the offset credit limits established for the first and second compliance periods. No more than 3 percent of a covered or opt-in entity's compliance obligation may be met by transferring offset credits from projects on federally recognized tribal land during the first compliance period. No more than 2 percent of a covered or opt-in entity's compliance obligation may be met by transferring offset credits from projects on federally recognized tribal land during the second compliance period.

Any offset credits used may not be additional to or allow for an increase in the program allowance budgets. The offset credit must be registered and tracked as a compliance instrument.

Beginning in 2031, the limits on offset credits established for the second compliance period apply unless modified by rule as adopted by Ecology after a public consultation process.

Assistance Program for Offsets on Tribal Lands.

In order to ensure that a sufficient number of high-quality offset projects are available, Ecology must establish an assistance program for offset projects on federally recognized tribal lands in the state. The assistance may include, but is not limited to, funding or consultation for federally recognized tribal governments to assess a project's technical feasibility, investment requirements, development and operational costs, expected returns, administrative and legal hurdles, and project risks and pitfalls. Funding or assistance may be provided upon request by a federally recognized tribe.

It is the intent of the Legislature that not less than \$5 million be provided in the biennial omnibus operating appropriations act for the purposes of an assistance program for offsets on tribal lands.

Compliance Obligations.

A covered or opt-in entity has a compliance obligation for its emissions during each four-year compliance period beginning January 1, 2023. A covered or opt-in entity must transfer a number of compliance instruments, including eligible offset credits, equal to their covered emissions by November 1 of each calendar year in which the entity has a compliance obligation. Ecology must set by rule a percentage of compliance instruments that must be transferred in each year of the compliance period such that covered and opt-in entities are allowed to smooth their compliance obligation within the compliance period, but must fully satisfy their compliance obligation over the course of the compliance period, in a manner similar to external GHG emissions trading programs in other jurisdictions.

A covered or opt-in entity submitting insufficient compliance instruments to meet its compliance obligation is subject to a penalty.

Allowances must be transferred in the order in which they were purchased. A covered or opt-in entity may not borrow an allowance from a future allowance year to meet a current or part compliance obligation. Upon receipt by Ecology of all compliance instruments transferred by a covered entity or opt-in entity to meet its compliance obligation, Ecology shall retire the allowances or offset credits.

Contingent Effective Date for Compliance Obligations.

Compliance obligations for covered entities and opt-in entities do not take effect until a separate, additive transportation funding act becomes law, at which time the Department of Licensing

must provide written notice to the Chief Clerk of the House of Representatives, the Secretary of the Senate, and the Office of the Code Reviser.

"Additive transportation funding act" means an act in which the combined total of new state revenues deposited into the Motor Vehicle Fund and Multimodal Transportation Account exceed \$500 million per biennium attributable solely to an increase in revenue from the enactment of the act.

Enforcement.

All covered and opt-in entities are required to submit compliance instruments in a timely manner to meet their compliance obligations and must comply with all requirements for monitoring, reporting, holding, and transferring emission allowances and other provisions of the Cap and Invest Program.

If a covered or opt-in entity does not submit sufficient allowances to meet its compliance obligation by the specified transfer dates, a penalty of four allowances for every one allowance that is missing must be submitted to Ecology within six months. When a covered entity or opt-in entity reasonably believes that it will be unable to meet a compliance obligation, the entity must immediately notify Ecology. Upon receiving notification, Ecology shall issue an order requiring the entity to submit the penalty allowances.

If a covered or opt-in entity fails to submit penalty allowances as required, Ecology must issue an order or issue a new penalty of up to \$10,000 per day per violation, or both, for failure to submit penalty allowances. The order may include a plan and schedule for coming into compliance.

Ecology may issue a penalty up to \$50,000 per day per violation for violations of the provisions protecting against bidder collusion and market manipulation. For the first compliance period, Ecology may reduce the amount of the penalty by adjusting the monetary amount or the number of penalty allowances.

All penalties must be deposited into the Climate Investment Account.

Appeals of order and penalties must be made to the Pollution Control Hearings Board.

Preemption Provisions.

No city, town, county, township, or other subdivision or municipal corporation of the state may implement a charge or tax based exclusively upon the quantity of GHG emissions.

No state agency may adopt or enforce a program that regulates GHG emissions from a stationary source except as provided under the Cap and Invest Program.

Linkage with Other Jurisdictions.

Ecology must seek to link the Cap and Invest Program with those of other jurisdictions in order to:

- allow for the mutual use and recognition of compliance instruments issued by Washington and other linked jurisdictions;
- broaden the GHG emission reduction opportunities to reduce the costs of compliance on covered entities and consumers;
- enable allowance auctions to be held jointly and provide for the use of a unified tracking system for compliance instruments;
- enhance market security;
- reduce program administration costs; and
- provide consistent requirements for covered entities whose operations span jurisdictional boundaries.

The director of Ecology is authorized to execute linkage agreements with other jurisdictions with established external GHG emissions trading programs. A linkage agreement must cover the following:

- provisions relating to quarterly auctions;
- provisions related to holding limits to ensure no entities in any of the linked programs are disadvantaged relative to their counterparts in the participating jurisdictions;
- other requirements, such as GHG reporting and verification, offset protocols, criteria, and process, and supervision and enforcement to prevent fraud, abuse, and market manipulation;
- common program registry, electronic auction platform, tracking systems for compliance instruments, and monitoring of compliance instruments;
- provisions to ensure coordinated administrative and technical support;
- provisions for public notice and participation; and
- provisions to collectively resolve differences, amend the agreements, and delink or otherwise withdraw from the agreements.

Before entering into a linkage agreement, Ecology must establish a finding that the linking jurisdiction and the linkage agreement meets certain criteria and conduct a public comment process to obtain input and a review of the linkage agreement by relevant stakeholders and other interested parties. The input received from the public comment process must be considered before finalizing a linkage agreement.

In the event that Ecology determines that a full linkage agreement is unlikely to meet the required criteria, it may enter into a linkage agreement with limitations, including limits on the share of compliance that may be met with allowances originating from linked jurisdictions.

A linkage agreement approved by Ecology must:

- ensure that the linking jurisdiction has provisions to ensure the distribution of benefits from the linked program to vulnerable populations and overburdened communities;

- be determined by Ecology to not yield net adverse impacts to either jurisdictions' highly impacted communities or analogous communities in the aggregate, relative to the baseline level of emissions; and
- not adversely impact Washington's ability to achieve its statewide emission reduction limits.

The state must retain legal and policymaking authority over the design and enforcement of its Cap and Invest Program.

Rulemaking.

Ecology must adopt rules to implement the provisions of the Cap and Invest Program. Ecology may adopt emergency rules for initial implementation of the program, to implement the state omnibus appropriations act for the 2021-2023 fiscal biennium, and to ensure that reporting and other program requirements are determined early for the purpose of program design and early notice to covered entities.

Climate Investment Account.

The Climate Investment Account is created in the State Treasury. Except as otherwise noted, all receipts from the auction of allowances under the Cap and Invest Program must be deposited into the account.

Projects or activities funded from the account must:

- meet high labor standards, including family sustaining wages, providing benefits including health care and pensions, career development opportunities; and
- maximize access to economic benefits from such projects for local workers and diverse businesses.

Each contracting entity's proposal for projects and activities funded from the account must be reviewed for equity and opportunity improvements efforts.

Moneys in the account may only be spent after appropriation and must be used for certain specified purposes, such as:

- to cover Ecology's and other agencies' costs to support and administer the Cap and Invest Program, including coordination of allowance auctions, tracking of emissions and allowances, rulemaking, evaluation, monitoring, and verification, and stakeholder communication and outreach;
- deposited into the State General Fund to implement the Working Families Tax Rebate;
- programs, activities, or projects that reduce and mitigate impacts from GHGs and copollutants in overburdened communities;
- clean transportation programs, activities, or projects that reduce transportation-related GHG emissions;
- natural climate resilience solutions;

- clean energy transition and assistance programs, activities, or projects that assist affected workers or people with lower incomes during the transition to a clean energy economy, or grow and expand clean manufacturing capacity in communities across Washington; and
- emissions reduction projects and programs.

Moneys in the account may not be used for projects that would violate tribal treaty rights or result in significant long-term damage to critical habitat or ecological functions. Investments from the account must result in long-term environmental benefits and increased resilience to the impacts of climate change.

Greenhouse Gas Reporting and Verification.

Ecology must adopt rules requiring persons to report emissions of GHGs where those emissions from a single facility, or from electricity or fossil fuels sold in Washington by a single supplier or local distribution company, meet or exceed 10,000 MTCO₂e annually. Annual reports must include emissions data for the preceding calendar year and be submitted to Ecology by March 31 of the year in which the report is due. The reporting rules must support implementation of the Cap and Invest Program.

Ecology must establish by rule the methods of verifying the accuracy of emissions reports. Verification requirements apply at a minimum to:

- persons that are required to report GHGs, if those emissions equal or exceed 25,000 MTCO₂e emissions, including carbon dioxide from biomass-derived fuels; or
- persons who have a compliance obligation under the Cap and Invest Program in any year of the current compliance period.

Ecology may adopt rules to accept verification reports from a linked jurisdiction where Ecology deems the methods or procedures are substantively similar.

When a person that holds a compliance obligation under the Cap and Invest Program fails to submit an emissions data report, or fails to obtain a positive emissions data verification statement, Ecology may assign an emissions level for that person.

Ecology may by rule include additional gases to the definition of GHG if that gas has been included in external GHG emission trading programs where Washington has a linkage agreement in effect. Ecology must update its rules whenever needed to ensure consistency with emissions reporting requirements for linked jurisdictions.

Contingent Expiration Date.

The Cap and Invest Program, and any rules adopted by Ecology to implement the Program, are suspended on December 31, 2055, in the event that the statewide 2050 emission limits have been met for two or more consecutive years.

Appropriation: None.

Fiscal Note: Available. New fiscal note requested on April 10, 2021.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.