

SENATE BILL REPORT

SB 5373

As of March 4, 2021

Title: An act relating to carbon pollution.

Brief Description: Concerning carbon pollution.

Sponsors: Senators Lovelett, Saldaña, Das, Dhingra, Frockt, Hunt, Kuderer, Nguyen, Pedersen, Salomon, Stanford, Wellman and Wilson, C..

Brief History:

Committee Activity: Environment, Energy & Technology: 3/04/21.

Brief Summary of Bill

- Imposes a carbon pollution tax beginning January 1, 2022, equal to \$25 per metric ton of greenhouse gas (GHG) emissions on the sale or use of all fossil fuel within the state of Washington, except for the sale or use of electricity in Washington generated using fossil fuels.
- Increases the tax rate annually by inflation, as measured by the consumer price index, plus 5 percent beginning July 1, 2023.
- Establishes a ten year climate finance program using carbon tax revenue and a bond program to reduce GHG emissions and increase the resilience of Washington's natural resources to the impacts of climate change.

SENATE COMMITTEE ON ENVIRONMENT, ENERGY & TECHNOLOGY

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Background: Greenhouse Gases. The United States Environmental Protection Agency (EPA) and Washington State 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.

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.

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, over a 100-year timeframe, to the emission of an identical volume of carbon dioxide (carbon dioxide equivalent).

Washington Greenhouse Gas Limits. Washington enacted legislation in 2008 setting a series of limits on GHG emissions within the state. Ecology is responsible for monitoring and tracking the state's progress toward the emission limits. Additional legislation in 2020 updated the state limits to the following:

- by 2020, reduce overall emissions of GHGs to 1990 levels, or 90.5 million metric tons;
- by 2030, reduce overall emissions of GHGs to 45 percent below 1990 levels, or 50 million metric tons;
- by 2040, reduce overall emissions of GHGs to 70 percent below 1990 levels, or 27 million metric tons; and
- by 2050, reduce overall emissions of GHGs to 95 percent below 1990 levels, or 5 million metric tons, and achieve net-zero GHG emissions.

Current Federal and State Greenhouse Gas Regulations. Under the federal Clean Air Act, GHGs are regulated as an air pollutant and are subject to several 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 carbon dioxide equivalent report their emissions to the EPA.

At the state level, GHGs are regulated by Ecology under the state Clean Air Act (CAA). The Clean Air Rule (CAR), adopted in September 2016, required entities emitting more than 100,000 metric tons a year to reduce their GHG emissions. In January 2020, the Washington State Supreme Court issued a 5-4 opinion partially invalidating CAR. The court held that the part of the rule which applies emission standards to actual emitters or direct sources of GHGs is valid because Ecology has this authority under the CAA. The court ruled Ecology does not have the authority to apply emissions standards to entities that do not directly emit, or indirect sources, such as natural gas distributors and petroleum product producers and importers.

Facilities, sources, and sites whose emissions exceed 10,000 metric tons of carbon dioxide equivalent each year are required to report their annual emissions to Ecology or to local air authorities that implement the state CAA. Liquid motor vehicle and aircraft fuel suppliers that supply fuel whose combustion would exceed that same 10,000-ton volumetric threshold must also report their annual emissions.

Apart from reporting and other regulations under the state and federal clean air acts, several other state laws and programs explicitly address GHG emissions.

Clean Energy Transformation Act. In 2019, the Legislature passed the Clean Energy Transformation Act, which requires all Washington electric utilities to transition to carbon-neutral electricity by 2030 and 100 percent carbon-free electricity by 2045.

Summary of Bill: The bill as referred to committee not considered.

Summary of Bill (Proposed Substitute): Carbon Pollution Tax. Beginning January 1, 2022, a carbon pollution tax (carbon tax) applies to the sale or use of all fossil fuels within the state of Washington, except for fossil fuels used to generate electricity. The tax rate is \$25 per metric ton of GHG emissions. The tax rate increases annually by 5 percent and adjusts for inflation as measured by the consumer price index starting on July 1, 2023.

Department of Revenue (DOR) must administer the tax. The carbon tax receipts must be deposited as follows:

- 85 percent into the Climate Finance Account; and
- 15 percent into Just Transition Assistance Account.

The carbon tax is imposed on the first sale or use of the fossil fuel within the state of Washington. A sale of fossil fuel takes place when the fossil fuel is delivered in this state to the purchaser or a person designated by the purchaser. A use of fossil fuel occurs when the fuel is consumed by the taxpayer in the state or the taxpayer possesses or stores the fossil fuel in the state in preparation for actual consumption by the taxpayer.

Natural gas possessed and stored within the state and natural gas transported through the state that is not produced or delivered in the state are exempt from the carbon tax. For natural gas, the carbon tax is imposed on:

- the gas distribution business upon the sale of natural gas to the retail customer; and
- the direct access gas customer upon the consumption of the natural gas by the customer.

Ecology, in consultation with the Department of Commerce (Commerce), will determine the carbon dioxide equivalent emissions and the measure of the carbon tax from the combustion or oxidation of various fossil fuels as a part of the carbon calculation.

Exemptions. The carbon tax does not apply to:

- fossil fuels brought into the state by means of the primary fuel supply tank of a motor vehicle, vessel, locomotive, or aircraft;
- fossil fuels exported from Washington State—export to Indian country is not considered export outside this state;
- the sale or use of coal transition power;
- diesel fuel, biodiesel fuel, and aircraft fuel used solely for agricultural purposes;
- biogas, biodiesel, cellulosic ethanol, landfill gas, and renewable diesel;
- aircraft fuel;

- the portion of fossil fuels purchased in Washington State and combusted outside the state by interstate motor carriers and vessels;
- activities or property of Indian tribes and individual Indians;
- motor vehicle fuel or special fuel used exclusively for agricultural purposes or those used by either log transportation businesses or any persons in the timber-extracting business; and
- fossil fuels consumed by an energy-intensive, trade-exposed (EITE) business in a sector designated by Commerce and Ecology.

Commerce and Ecology must adopt rules to designate EITE sectors by June 30, 2022. Ecology must provide a report regarding whether to restrict or eliminate the EITE exemption to the Legislature by July 30, 2026.

Reporting. Commerce must submit a report by December 31, 2024 and biennially thereafter. The initial report must establish a process to audit the uses of the GHG emissions reduction account and the natural climate solutions account. The report must contain:

- the total carbon pollution taxes collected during the reporting period and a list of taxpayers with the amount of carbon tax paid;
- estimated costs incurred by DOR, Commerce, and Ecology associated with the administration of the carbon tax, shown as a dollar amount and percentage of the collected revenues;
- the economic health impact of Washington State with verifiable data on emissions leakage and any job losses since the carbon tax implementation; and
- a summary of the investments made through Commerce's administration of the GHG Emissions Reduction Account, Natural Climate Solutions Account, and Climate Bond Proceeds Account.

Commerce must provide an environmental justice analysis reporting on the environmental, health, and economic impacts on highly impacted communities and vulnerable populations from the climate impacts and state measures taken to meet the state's GHG emission limits.

Ecology must submit reports by July 30, 2026, with recommendations on imposing requirements on emissions in both the agricultural and transportation sectors.

Rules and Technical Assistance. DOR, Ecology, the Department of Licensing, the Washington State Department of Transportation, the Employment Security Department (ESD) and Commerce may adopt rules to administer the tax. Commerce, Ecology, and Washington State University's Energy Program must provide technical assistance to DOR necessary to effectively implement the carbon tax.

Climate Finance Account. A Climate Finance Account (CFA) is created and 85 percent of revenues generated from the carbon tax are deposited into the CFA. The funds are used first and foremost for the payment of principal and interest on bonds. The remaining funds

are first appropriated for the administration of the carbon tax and cannot exceed 5 percent of the total carbon tax receipt.

Beginning July 1, 2023, the remainder of the funds are distributed as follows:

- 75 percent to the Greenhouse Gas Emissions Reduction Account; and
- 25 percent to the Natural Climate Solutions Account.

Just Transition Assistance Account. A Just Transition Assistance Account (JTAA) is created and 15 percent of carbon tax receipts must be deposited into it. Commerce must administer the JTAA in consultation with ESD. Account funds may be spent after appropriations and must be used for the following purposes:

- reducing the energy burden for lower-income Washington residents;
- supporting dislocated fossil fuel workers and other workers who loses their employment due to the transition from fossil fuel;
- economic support for communities with eligible workers;
- supporting vulnerable populations and highly impacted communities in facilitating public participation and developing eligible projects; and
- covering the costs to support and administer the work of the environmental justice and economic equity panel.

Climate Bond Financing. The state finance committee is authorized to issue special tax obligation bonds for a period not to exceed ten years, and for up to \$4,943,000,000. The bond authorization expires when the full authorization has been issued and dispersed, or until the end of the ten-year period, whichever comes first. The bonds issued:

- are not a general obligation of the state and the full faith, credit, and taxing powers of the state are not pledged for their payment;
- are payable solely from and secured by the carbon tax revenues received in the CFA;
- include the Legislature's pledge to appropriate the carbon tax revenues pledged to the payment of the bonds issued; and
- must be structured for the debt service obligations to be completed by December 31, 2050.

The total investments made through the climate bond proceeds account, GHG emissions reduction account, and natural climate solutions account, measured on a biennial basis, must at least meet:

- 35 percent of total investments providing direct and meaningful benefits to vulnerable populations within the boundaries of overburdened communities;
- 25 percent of total investments must benefit projects located in rural areas of the state; and
- 10 percent of total investments used for programs, activities, or projects formally supported by a resolution of an Indian tribe.

Climate Bond Accounts. The Climate Bond Retirement Account is created and used only for the payment of principal and interest on authorized bonds. The Climate Bond Proceeds

Account is created to receive funds from the sale of bond's proceeds. Account funds may be appropriated only for:

- projects categorized in the GHG emissions reduction account and the natural climate solutions account; or
- payment of expenses incurred in the issuance and sale of the bonds.

Greenhouse Gas Emissions Reduction Account. The Greenhouse Gas Emissions Reduction Account is created and funds are deposited from CFA. Account funds may be spent only after appropriation and be used by Commerce for projects and incentive programs physically located in Washington State, which yield verifiable reductions in GHG emissions in excess of baseline practices.

Twenty-five percent of account funds may be invested in projects and programs including, but not limited to:

- supplementing the growth management planning and environmental review fund and cover costs associated with adopting optional elements of the comprehensive plan and transportation improvement plans;
- deploying renewable energy resources, distributed generation, energy storage, demand side technologies and strategies, or other grid modernization projects;
- increasing industrial energy efficiency or reducing GHG emissions at manufacturing facilities with proposals to implement combined heat and power, district energy, or on-site renewables to upgrade existing equipment, reduce process emissions, and switch to less emissions intensive fuel sources;
- achieving energy efficiency and emissions reduction in the agricultural sector with fertilizer management, soil management, bioenergy, and biofuels;
- increasing energy efficiency in new and existing buildings or promoting low-carbon architecture using newly emerging alternative building materials that result in a lower carbon footprint in the built environment over the life cycle of the building and component building materials; or
- other technologies such as proposals promoting the electrification and decarbonization of new and existing buildings or improving energy efficiency and investments in market transformation of energy efficiency products.

Seventy-five percent of account funds must be invested in programs, activities, or projects located in the state and reduce GHG emissions, or mitigate the impact of GHG emissions from the transportation sector. The categories of eligible projects include, but are not limited to:

- increasing public transportation services and reducing vehicle miles traveled including nonmotorized transportation, transit-oriented housing, and high-speed rural broadband;
- deployment of clean alternative fuel vehicle charging and refueling infrastructure and support of clean alternative fuel car sharing programs to provide use opportunities to underserved communities and low to moderate income members of the workforce;
- electrification and decarbonization of the state's passenger ferry fleet; or

- conversion to battery or fuel cell electric fleets for the state, counties, cities, and public transit agencies.

Public and private entities are eligible for funding. Projects or activities funded must reduce GHG emissions, meet high labor standards, and maximize access to economic benefits from such projects for local workers and diverse businesses. Funding recipients must meet Commerce's criteria and submit a progress report providing information required by Commerce.

Commerce must:

- design project funding contracts, monitor project implementation, and track contract performance—Commerce may also suspend or terminate funding when projects do not achieve projected reductions as provided in the funding agreement, or require a return of grant funding in cases of gross misuse of funds;
- establish a public electronic database for tracking projects and incentive programs that received funding—projects must be ranked and sortable based on quantitative performance metrics such as the avoided cost of a ton of carbon dioxide equivalents; and
- develop an implementation plan for providing funding and submit it to the Governor and Legislature by December 31, 2022—Commerce must seek recommendations from the environmental justice and economic equity panel in the development of the implementation plan and the allocation funding's policies and procedures.

Natural Climate Solutions Account. The Natural Climate Solutions Account is created and all funds in the account are intended to increase the resilience of the state's waters, forests, and other vital ecosystems to climate change impacts, and increase their carbon pollution reduction capacity through sequestration, storage, and overall ecosystem integrity. Account funds may be allocated for the following purposes, but are not limited to investments in:

- wildfire response, forest restoration, and community preparedness; and
- clean water to improve resiliency from climate impacts.

The account funds must be spent in a manner consistent with existing and future assessments of climate risks and resilience from the scientific community and expressed concerns of and impacts to highly impacted communities. Investments must result in long-term environmental benefit and increased resilience to climate change impacts. Funds 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.

Environmental Justice and Economic Equity Panel. An environmental justice and economic equity panel is established to provide recommendations in the development of investment plans and funding proposals for GHG emissions reduction and natural climate solutions accounts. Co-chaired by one tribal leader and one person representing the interests of overburdened communities, the panel consists of ten members, appointed by the Governor, including:

- five members, including at least one tribal leader, representing the interests of vulnerable populations residing in overburdened communities in different geographic areas of the state and from rural and urban areas;
- two members representing union labor with expertise in economic dislocation, clean energy economy, or EITE facilities;
- a member in addition to at least one tribal leader to represent tribal governments; and
- two members representing low-income and community advocacy organizations.

Tribal Consultation. State agencies receiving any funds from the accounts created in this bill must consult with Indian tribes on all decisions that may affect Indian tribes' rights and interests in their tribal lands. Projects impacting tribal lands are prohibited from being funded prior to meaningful consultation with affected Indian tribes resulting in the state agency first receiving a written resolution providing consent or withholding consent.

Ecology's Authority. Ecology has the authority to impose air quality standards, emission standards, or emission limitations on entities producing or distributing fossil fuels or other products emitting GHG emissions.

By October 30, 2025, Ecology must determine whether the sources of emissions covered by the carbon tax is likely to achieve the proportionate share of the emissions reductions necessary for the state to achieve the established emission limits, and submit a report to the Legislature by January 1, 2026. If Ecology determines the reductions are not likely to meet the limits, it has the authority to adopt emission limitations upon entities sufficient to meet the state's established emission limits.

Severability Clause. If any provision of this act is held invalid, the remainder of the act is not affected.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: The bill contains an emergency clause and takes effect immediately.