Washington State Comments
Discussion Draft of the
American Clean Energy and Security Act of 2009

April 17, 2009

Washington offers the following recommendations for modifying, maintaining or strengthening these key provisions of the discussion draft: (1) regional cap-and-trade programs; (2) offsets; (3) definition of "renewable biomass"; (4) recognition for early action; (5) use of auction revenues; (6) low carbon fuel standard; (7) emission standards for mobile sources; (8) greenhouse gas reporting; (9) ensuring domestic competitiveness; (10) transportation; (11) transmission planning; (12) state authority; (13) coal fired power plants; (14) utility energy efficiency standards; (15) adaptation; and (16) Miscellaneous. We would welcome the opportunity to supplement these comments as we continue to analyze the discussion draft.

(1) Regional Cap-and-Trade Programs. Section 790 of the bill allows for the transition of allowances issued by Regional Greenhouse Gas Initiative (RGGI) and the State of California into the federal program. Section 335 of the bill adds a new section to the Clean Air Act that precludes states from implementing cap-and-trade programs from 2012-2017. We understand that this six year moratorium is intended to prevent states from implementing their current or planned regional cap-and-trade programs when a federal cap-and-trade is enacted. We have three comments on these provisions:

- ***We recommend that Section 790 be modified to allow any allowances issued under any state or regional programs prior to 2012 to be exchanged for federal allowances, including the programs being developed by the Western Climate Initiative, in which California participates. WCI member states other than California may issue allowances prior to 2012 that should be treated similarly to those that may be issued by California.***
- ***We recommend that the language in Section 861 be made clear that the moratorium is only for cap-and-trade programs and not a moratorium on any program that may "cap" emissions. As written, the moratorium could include a state's emission performance standard and other state programs that regulate the same sources as may be under the federal cap-and-trade program.***
- ***We recommend that the moratorium be limited to three years and start only after rules have been formally proposed for a national program. It will likely take EPA two to four years to develop rules to implement the cap-and-trade provisions of the ACESA. If the regional programs are allowed to continue, they will help achieve greater greenhouse gas reductions while the federal cap-and-trade program is being developed. In addition, the states will be able to continue to refine the collective thinking around cap-and-trade, providing EPA with the benefit of those experiences.***

(2) Offsets. We have several concerns on this program element. As we understand Section 734 of the discussion draft, offset projects may not be considered "additional" if they were commenced prior to January 1, 2009. The regional cap-and-trade programs that are either in

place or under development have an offset component. Recognition should be allowed in the federal system for otherwise qualifying offset projects that were developed as part of those regional programs.

- ***We recommend that offset projects that are approved or developed for use in any regional cap-and-trade program be eligible for recognition in the federal program even if commenced prior to January 1, 2009.***

We also read Section 734 as disallowing offset projects as being "additional" if the actions are required by any law or regulation. Forest practices regulations vary widely across the states. In an evaluation we commissioned in 2008, we found that Washington has very stringent regulations as compared to many other states and some Canadian provinces. Excluding practices required by regulation from the definition of additionality will result in inequities between states. A forest practice that will qualify as an offset in one state with less stringent forest practices regulations will not qualify as an offset in a state with stricter standards. This will serve to penalize those states who have taken steps to improve forest practices as compared to those states that have not done so. Offsets should not be used as a method to improve forest practices in states that are doing less than others.

- ***We recommend attention be given to how to mitigate the unintended inequities between states as a result of varying forest practices regulations. Section 741 could be expanded to include consideration of a state's forest practices requirements as one of the Environmental Considerations for forestry offset projects. A conforming amendment would be required to Section 734(a)(1)(A)(i).***

We read Section 741(2) to require that forestry offset projects must **enhance** biological diversity in order to qualify as an offset. In Washington State, most forest management is of largely natural forests with native species, and Washington's strict forest practices act serves to provide significant protection to native biodiversity as part of baseline conditions.

- ***We recommend the requirement in Section 741(2) be changed to read "enhance <u>or maintain</u> biodiversity."***

Section 722(c)(1)(B) seems to allow a significant number of offset credits into the system with half being international offsets. We recognize the important role that offsets play in keeping compliance costs low. We also understand that unlike other air pollutants, a reduction in greenhouse gases in any location is important to address global climate change. However, long term investments in emission sources that will permanently reduce emissions are critical to transforming our economy to one that does not overly rely on fossil fuels.

- ***Care must be taken to find the balance between allowing a sufficient number of credible offsets to be used while still ensuring investments are being made in this country to support the permanent shift to a clean energy economy.***

(3) <u>Renewable Biomass</u>. In 2005, the Washington Department of Ecology completed a biomass inventory and bioenergy assessment for the state. (http://www.ecy.wa.gov/pubs/0507047.pdf)

The goal of the study was to inventory Washington's *underutilized* bioresources as a first essential step to reduce the amount of organic residuals in solid waste. This inventory also represented a critical first step toward a sustainable energy policy and vision within the state to obtain information on the type and geographic distribution of biomass.

The result of this study showed that Washington State has an annual production of over 16.9 million tons of underutilized dry equivalent biomass, which is capable of producing over 15.5 billion kWh of electrical energy or 1,769 MW of electrical power. This amount of power total, which assumed complete utilization of the inventoried biomass, is equivalent to just about 50% of Washington State's annual residential electrical consumption.

Much of this biomass comes from forested lands in our state. Washington State contains approximately 42,612,480 acres of land. Of that, approximately 51% is classified as forest land. The largest owners are the federal government, which owns just over 30%; the forest industry, which owns 29%; and non-industrial private owners – also referred to as small forest land owners and small tree farmers – who collectively own 19% of the forested land in our state. We have one of the most comprehensive and protective forest practices acts in the United States, which includes a requirement that any commercially harvested trees be replanted. Our Department of Natural Resources is actively engaged in activities to improve forest health, which will become even more critical as we see more warming in the Pacific Northwest.

We are concerned that the definition of "renewable biomass" does not include brush, slash and other residue from actively managed forested lands that are not tree plantations. Industrial combustion of these materials is currently used to create electricity and because of our sustainable forest practices, they are considered carbon neutral. State law allows these sources be considered carbon neutral *only* if our silvicultural sequestration capacity is maintained or increased. These materials may also hold the key to successful development of cellulosic ethanol. Yet it is likely little if any of the lands in Washington State would be considered tree plantations as we understand the term. At a minimum

- ***We recommend that brush, slash and all residues from sustainably managed forests be considered renewable biomass.***

Utilization of this type of biomass also has great potential to contribute to closely related policy goals including improving the health of our nation's forest lands and reducing their susceptibility to catastrophic wildfires, made more likely by climate change itself. Washington State contains millions of acres of forest land at elevated risk of insect and disease related mortality (1.4 million acres experiencing such mortality in 2008), making them susceptible to catastrophic wildfires that release large volumes of greenhouse gasses. A significant proportion of these acres are on federal lands. Utilization of not otherwise merchantable forest materials as part of forest health or fire fuel reduction treatments is widely recognized as a beneficial measure to provide a sustainable source of woody biomass, improve forest health and reduce catastrophic fire risk. This is true for all categories of forest land, including federal land. By categorically excluding federal land from the definition of renewable biomass, the current discussion draft eliminates the opportunity to achieve forest health and catastrophic fire

abatement objectives that are critical to addressing climate change. Also, this categorical exemption fails to recognize that hazardous fuel or insect infestation conditions on federal lands can cause the spread of insects and fire onto neighboring non-federal lands.

- ***We recommend that attention be given to finding acceptable means of including sustainable and effective forest health and fuel abatement treatments on federal lands within the definition of renewable biomass.***

(4) Recognition for Early Action. To get a head start on meeting our emission reduction goals, it is important to encourage companies to make reductions now, and not wait until 2012. In the WCI design, facilities subject to the cap that make reductions after January 1, 2008 but before the program's start in 2012 will be issued Early Reduction Allowances provided the reductions are voluntary, additional, real, verifiable and enforceable. We reasoned that these emissions would have been part of our 2012 starting point had the reductions had not occurred. Therefore, issuing allowances directly to those companies in addition to the allowance cap would not result in an over-allocation of allowances. In addition, a failure to recognize qualifying early actions will almost certainly result in fewer emission reductions before the program rules are in place as emitters delay investment that would otherwise result in important efficiencies and reductions. This design element has received broad support from both our industry and environmental stakeholders.

- ***We support including in the bill a provision that will directly reward companies for qualifying greenhouse gas reductions that occur at facilities covered by the cap-and-trade program after a date certain but prior to the start of the program.***

(5) Allowances and Use of Auction Revenues. We appreciate the fact that the sponsors have left the disbursement of allowances and proceeds from any auctions for discussion before the full committee. As we in Washington have worked on cap-and-trade program development with our stakeholders and legislature, these two issues were the most contentious. Our experience suggests a transition period toward the low-carbon economy requires an allowances distribution methodology that drives resources to protect consumers from price impacts. It should also recognize those emitters who are already operating at their industry's best practice level. We also found for electricity consumers of utilities that remain vertically integrated, distributing allowances to the load-serving entity and requiring those entities to use the allowances to comply or to protect vulnerable ratepayers represents the most acceptable path. Some reasonable time for the transition to full auctioning of allowances is important. As you consider how to use the value of the allowances, we would recommend that consideration be given to

- ***Investing some portion in research and development to advance alternative energy sources and energy independence, and other measures that will reduce greenhouse gas emissions.***
- ***Protecting families and small businesses from undue financial impacts arising from the transition to a clean energy future***.

(6) Low Carbon Fuel Standard. We believe a federal low carbon fuel standard is appropriate and are pleased to see one included in the bill. We have two specifics concerns with this

provision in the discussion draft. As we understand, the renewable fuel standard is the low carbon fuel standard until 2023, so there are no added greenhouse gas reduction benefits (effectively no LCFS) until 2023. Also, under the current Section 211(c) of the Clean Air Act, once a federal fuel standard has been established under section 211 (c)(1), the states may not establish a motor vehicle fuel standard except in limited circumstances that do not appear to apply to Washington. We understand the concerns expressed by industry about "patchwork" requirements and are certainly willing to discuss creation of regional standards or a minimum market size to reduce the concerns of those who might be faced with complying with multiple LCFS programs.   To remedy our two specific concerns:

- ***We urge earlier and greater reductions than currently specified in the draft.***
- ***We recommend specific language that will preserve the states' ability to adopt a more stringent low carbon fuel standard than that established at the federal level. Preferably this would be accomplished by placing the national LCFS requirement in a new subsection under Section 211 of the Clean Air Act in addition to clear state authority to be more stringent. In addition, we should not be required to opt in to a California LCFS.***

(7) Emission Standards for Mobile Sources. We support inclusion of the requirement for EPA to enact nationwide automobile greenhouse gas emission standards that are at least as stringent as the California's.   Section 221(a)(4) provides that EPA's adoption of nationwide standards shall not preempt California from adopting and enforcing its own standards. It is unclear whether this language is intended to limit the authority of other states under CAA section 177, to adopt the California standards. In addition, the Energy Policy and Conservation Act addresses fuel efficiency standards for motor vehicles while at the same time the CAA allows EPA to adopt emissions standards for motor vehicles.

- ***We recommend that Section 221(a)(4) be clarified to ensure that other states may continue to exercise their authority under Section 177 to adopt and enforce the California standards***.
- ***We recommend that a provision be added to declare that California's GHG emission standards for motor vehicles are not preempted or otherwise invalidated under the Energy Policy and Conservation Act***.

(8) Greenhouse Gas Reporting. We have several specific recommendations for amendments to this section. We believe the reporting threshold needs to be clarified. We have consulted a number of other states and organizations involved in this issue. By and large, we have not found that any two who agree on the reading of Section 713(a)(2). Our reading of this section suggests that all covered entities as that term is defined are required to report, and those covered entities that are included in the definition because their emissions exceed 25,000 tons annually are required to report if they have emissions that exceed 10,000 tons annually.   Those entities would be those described in Section 700(12)(B), (C), (F), (G) and (H). If this is a correct reading of the reporting requirement, we support this reporting threshold. We believe, at a minimum, that those entities covered by a cap-and-trade program should have a lower reporting threshold than the threshold for regulatory coverage in the cap-and-trade program. Washington State's mandatory reporting statute requires reporting of emissions at or above

10,000 metric tons annually with fleets that emit 2,500 metric tons annually also required to report. A lower reporting threshold is vital to informing future policy decisions.

- ***The reporting threshold in Section 713(a)(2) needs to be clarified so that those required to report understand their obligation with a plain reading of the statutory language.***
- ***We recommend a reporting threshold of 10,000 metric tons for all reporting entities, including electricity generation.***

According to North American Electric Reliability Corporation, three of the electricity power grids that serve regions in the United States are interconnected with Canada: the Western Electric Coordinating Council, Midwest Reliability Organization and the Northeast Power Coordinating Council. This means that power generated in Canada will be part of the electricity that serves the U.S. in those power grids. We believe that the emissions associated with this imported power should be reported. While much of the power that comes out of Quebec, Ontario and British Columbia is likely clean hydropower, that is not the case throughout the provinces.

- ***We recommend requiring U.S. entities to report emissions associated with power generated outside of the United States that is imported for consumption in the states.***

As drafted, all the reporting data goes directly to EPA, which may then share it with the states. The states are closer to the reporters and can more easily and more quickly work with them to identify problems and correct any errors. Also, as the totality of the discussion draft shows, a host of efforts will be needed to reduce emissions, most of which are within the purview of state and local governments. The reported data will be needed by the states to determine if the collective actions are having the desired effect. Many states already have mandatory reporting. While the bill does not specifically preempt state-based reporting, it will be nearly impossible to retain two reporting schemes for the same pollutant, one done under a federal regime with its own timeline and requirements, and another done by the states. Because state legislatures only have authority over state agencies, the pressure from business will be put there to eliminate state reporting.

- ***We strongly urge that EPA be required to delegate reporting to the states that request such delegation and can demonstrate the ability to implement the requirements.***
- ***As an alternative, EPA should be required to work with states so that data that is not part of the cap-and-trade program may be reported to the states and to ensure that the data reported to EPA is easily and quickly accessible to the states in a manner that will be immediately useful to them.***
- ***States should be specifically authorized to require reporting above the federal minimum threshold and beyond the federally required sectors.***

Finally, to the extent the reported data is being used in a cap-and-trade program, it must be subject to third-party verification. This type of rigor is necessary to build and retain market confidence and its development should be part of the initial development of the program.

- ***The legislation should require third party verification of reported data that will be used to support the federal cap-and-trade program.***

(9) Ensuring Domestic Competitiveness. We appreciate inclusion of Subtitle A in Title IV from Congressman Inslee. Our experience suggests a transition period toward the low-carbon economy requires special consideration for internationally competitive industries that are energy-intensive. Washington has a significant manufacturing base. We believe that retaining these jobs and helping these companies transition to a clean energy platform is important for the overall economic health of our state and our country. We look forward to working with Congressman Inslee as he works with industries and EPA to ensure the provision provides the certainty to the industries it is intended to assist.

- ***The provision to compensate certain industrial sectors to prevent carbon leakage while rewarding innovation and energy efficiency investments in their facilities must be retained in the legislation***.

(10) Transportation. Section 841 of the discussion draft requires that each state develop goals to reduce greenhouse gas emissions from mobile sources in *concurrence* with air quality and transportation agencies and in *consultation* with Metropolitan Planning Organizations (MPOs) over a given size and the public. The states must also have as part of their transportation plan a plan to achieve those goals, which may include transportation and land use planning strategies. Transportation emissions are the largest sector in Washington's greenhouse gas emissions inventory. We appreciate how the discussion draft attempts to bring together all aspects of transportation emission reductions from planning to low carbon fuels to vehicle technology such as electrification in Sections 122 -124 and the previously mentioned vehicle emissions standards.

- ***We urge Congress to consider making similar connections when reauthorizing the*** **Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users** ***(SAFETEA-LU) surface transportation act. SAFETEA-LU reauthorization should consider a much stronger role for state environmental agencies in the transportation planning and project selection processes for federally funded and regionally significant projects and programs to ensure transportation plans, programs, and projects are consistent with the transportation greenhouse gas reduction goals.***

(11) Transmission Planning. We fully understand and support the concept of regional and national planning for the electrical grid. The challenge of course is that this is also very much a land use issue at the local level and care must be taken to not have the Federal Energy Regulatory Commission (FERC) making local land use decisions. Section 151 of the discussion draft is vague as to FERC's authority to resolve disputes, how and what kind of support it will provide, the extent of its participation and the nature of that participation in regional planning processes, and the ultimate fate of a regional electric grid plan that FERC returns to a planning entity for further consideration if the planning entity chooses to not make any changes based on the Commission's recommendations.

- ***We recommend Section 151 be clarified as to the extent and nature of FERC's role and authority relative to transmission planning***.

(12) State Authority. Several provisions in the discussion draft cause us some concern as they relate to authorities the state current enjoys. In addition to those previously mentioned we note the following sections:

- Page 359 section 721, addresses emission allowances and contains a generalized statement that nothing in the Act relating to allowances affects application of any other provisions of law to covered entities***. We recommend this language be clarified to explain or give examples of the types of laws this is intended to cover.***
- Page 449, section 761, addresses oversight of the carbon market. ***We recommend that there be an explicit savings clause to allow states dual authority to enforce for violations of state antitrust and consumer protection laws.***
- Page 457, section 761, creates a working group to propose regulations for regulated allowance derivatives. The language references agencies that would be involved in the group. ***We recommend that the language be clarified so that "agencies" expressly includes state agencies***.
- Page 485, Section 811, addresses stationary source standards. It prohibits adoption of new source performance standards established under section 111 for capped sources. ***We recommend an express savings clause to clarify that these provisions do not affect the authority of states to adopt such standards under state authority***.
- Page 490, Sections 831-834, addresses exemptions from other programs. It prohibits regulation of GHGs under other parts of the CAA. ***We recommend an express savings clause to clarify that these provisions do not affect the authority of states to adopt standards under state authority.***
- Page 526, Section 334, expands the savings clause in Section 116 of CAA to include any provision to cap GHGs or require the surrender of emission allowances or offsets issued under the Act. ***We recommend this language be made clear so that "cap" does not include state programs such as an emission performance standard or other types of state programs that regulate the same sources that may be under the federal cap-and-trade program.***

(13) Coal fired power plants. We support the inclusion of an emissions performance standard (EPS) for new coal fired power plants permitted after 2015 and its gradual improvement by 2020. As we read the discussion draft, any new pulverized coal plant permitted between 2009 and 2015 would have to use carbon capture and storage (CCS) within four years after EPA determines it is available and viable. If CCS is not available, there is no requirement for these coal plants to improve their emissions other than whatever will be required of them under the cap-and-trade program. Also, if CCS provides better emission reductions than the EPS, we read the discussion draft as only requiring the EPS.

- ***We recommend that if CCS becomes viable, the performance standard should be the best in emission reductions that CCS can deliver rather than the EPS.***
- ***We also recommend that if CCS is not available and viable by 2015, those coal plants permitted between 2009 and 2015 should be subject to more rigorous reductions than what would be expected under the cap-and-trade program given the somewhat generous use of offsets allowed in the draft.***

(14) Utility Energy Efficiency Standard. Section 231 establishes a new, mandatory federal energy efficiency standard. We read the discussion draft to set the standard as a target percentage of utility load that is not sensitive to utility integrated resource planning, utility circumstances, or cost-effectiveness. The U.S. Department of Energy is empowered to enforce the standard and assess penalties if the load-based efficiency targets are not met. The Department may delegate administration of the standard to states, but only if state programs meet or exceed the target levels set in the federal standard. Washington is a strong advocate of energy efficiency and requires its electric and gas utilities to include end-use efficiency as a resource in integrated resource plans. Electric utilities are required to develop all cost-effective energy efficiency resources under Washington's renewable portfolio standard (RCW 19.285.040). These policies promote development of energy efficiency as a resource while protecting ratepayers by ensuring that their rates are used cost-effectively. We read Section 231 to preempt these state policies with a mandatory federal target.

- ***We recommend that Section 231 be modified to exempt states that enforce policies requiring utilities to include efficiency in resource planning and that require utilities to develop all cost-effective energy efficiency.***

(15) Adaptation. We support the inclusion of the broad scale adaptation program contained in Subtitle E of Title IV of the discussion draft. Our state depends on hydroelectric power for the majority of its electricity. This is the resource most directly vulnerable to climate impacts. It also provides a legacy of emissions-free generation. We appreciate the recognition of Puget Sound as a large-scale estuarine ecosystem that may be eligible for funding of adaptation activities to restore and protect this critically important water body. Critical to our state's planning for adaptation is our work with British Columbia. Washington and British Columbia share coastal and ocean resources, forestry ecosystems, air sheds, and transportation systems. We believe this type of international cooperation at the local level should be encouraged and supported.

- ***We recommend a small amount of funding be provided specifically to Border States for work on shared cross-border adaptation strategies.***

(16) Miscellaneous. All tons should be measured in metric tons to assure compatibility with regional and international trading programs.

It is our belief that vigilant market oversight is critically important to the overall success of a cap-and-trade program. We urge you to give sufficiently broad authority to the Federal Energy Regulatory Commission to oversee this newly created market and then back that authority with the resources required to do the job well. We have had direct and unhappy experiences with markets– Enron and the west coast electricity market failure of 2000-2001 and the most recent subprime lending markets in 2008-2009 – where a lack of clear and complete regulatory authority, coupled with insufficient resources, have had devastating and widespread consequences. This should not be allowed to happen again or with this market.