

Blakes Bulletin

Environmental Law/CleanTech

Towards an Emissions Trading System: B.C. Releases Consultation Papers for Cap and Trade Regulations

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The B.C. Ministry of Environment (MOE) has released consultation papers for two proposed regulations under the *Greenhouse Gas Reduction (Cap and Trade) Act* (the Cap and Trade Act): (i) *Emissions Trading Regulation*; and (ii) *Cap and Trade Offsets Regulation*.

The Cap and Trade Act, which received Royal Assent on May 29, 2008, provides the regulatory framework for the province's participation in the Western Climate Initiative's (WCI) proposed cap-and-trade system. The WCI's cap-and-trade program has a planned start date of January 1, 2012. The purpose of the consultation papers is to seek comments from stakeholders, First Nations and the general public on the two proposed regulations. The deadline for comments is December 6, 2010 and the proposed regulations are expected to be finalized in early 2011.

EMISSIONS TRADING REGULATION

The proposed *Emissions Trading Regulation* is designed to establish an efficient, fair market for trading cap-and-trade compliance units. In particular, the proposed regulation will include clear rules on how allowances are created, distributed, traded, tracked and retired for compliance. Under the proposed *Emissions Trading Regulation*, operations that meet certain criteria will be considered a "Regulated Operation", i.e., those emitting more than 25,000 tonnes or more of carbon dioxide equivalent (CO₂e) from a listed source type in a calendar year of a compliance period. The following key provisions are under consideration:

- starting January 1, 2012 (or any subsequent year in which an operation emits 25,000 tonnes or more of CO₂e), the regulation will apply to the operator of an operation that emits 25,000 tonnes or more of CO₂e;
- source types listed in Schedule A of the current *Reporting Regulation* (including activities such as general stationary combustion, aluminum production,

cement production, coal mining, industrial wastewater processing, lime manufacturing, petroleum refining, and pulp and paper production) are under evaluation to be "covered sources" in the first compliance period;

- additional source types under consideration as "covered sources" include emissions from anaerobic or aerobic digestion of wastewater, emissions from surface coal mines and stored coal piles, specific oil and gas and petroleum refinery emissions, and fugitive hydrofluorocarbon emissions from cooling units at electricity generators;
- a registry will be established to ensure the accurate accounting of the issue, holding, transfer, retirement and cancellation of compliance units, as well as the compliance obligations and status of Regulated Operations;
- in addition to Regulated Operations, any other person or organization will be able to hold compliance units;
- verified emission reports and compliance unit liability may be linked in the registry, meaning that an amount equal to a Regulated Operation's annual greenhouse gas (GHG) emissions will become its corresponding compliance obligation;
- facilities below the 25,000 tonne threshold may be able to opt in to the emissions trading system;
- each compliance period will be three years in length;
- compliance will be assessed every three years on July 1 of the year following the last year of the compliance period and, at the end of each compliance period, one compliance unit will be retired for each tonne of GHG emissions;
- every three years, B.C. will prepare a nine-year "Allowance Budget Forecast", with the first forecast for the period from 2012 to 2020 being published in the first quarter of 2011 (in 2014, B.C. would release a forecast for the period from 2015 to 2023);
- every three years, B.C. would establish a cap on allowances issued for the following three-year compliance period, known as an "Allowance Budget";

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- in the third quarter of 2011, and every year thereafter, B.C. would publish an annual "Allowance Distribution Plan" that will describe how allowances will be allocated for the following year (including number of allowances to be auctioned, number of allowances to be distributed for free, number of allowances to be held in reserve or contingency accounts, and number of allowances to be sold directly in the market);
- there will be two main allowance distribution mechanisms for distributing allowances to a Regulated Operation: by auction and by distribution for free;
- auctions of allowances will be held quarterly in coordination with other WCI members on a single round, sealed-bid, uniform price basis;
- B.C. will have the ability to set a minimum price for allowances sold at auction;
- primary distribution of allowances and cash markets will be overseen by the Ministry of Finance and Climate Action Secretariat, while the BC Securities Commission will oversee the derivatives market (futures contracts, options and swaps for delivery of compliance units);
- Regulated Operations will transfer compliance units equal to their compliance obligations into their compliance account;
- allowances will be retired, meaning that Regulated Operations will not be able to take allowances out of their compliance accounts;
- a number of compliance mechanisms will be available to Regulated Operations including limited use of offsets and approved compliance units from other systems, unlimited banking, multi-year compliance period, linking with partner jurisdictions, and government support for low-carbon policies and programs;
- B.C. will set limits on the use of offsets as a percentage of an operator's compliance obligation and is still seeking input about the percentage to be adopted in B.C.; and
- penalty for non-compliance will be assessed at three additional allowances for every allowance that the regulated operation is short.

CAP AND TRADE OFFSETS REGULATION

Offsets will be a key component of the cap-and-trade program and help to reduce the compliance costs for Regulated Operations. The proposed *Offsets Regulation*

will govern the development and recognition of emissions offsets, consistent with the offset design recommendations of the WCI. In particular, the proposed regulation will set out steps for offset registration, validation, monitoring, quantification, reporting, verification, certification and issuance of offsets. The expectation is that certificates will be able to be traded and used for compliance across the WCI. The following key provisions are under consideration:

- offset project eligibility will be evaluated on the basis of the following criteria: definition of an offset, real, additional, permanent and verifiable;
- a B.C. offset of "emission reduction unit" (ERU), will be issued based on certification of verified emission reductions from a registered offset project (one ERU will represent a reduction or removal of one tonne of CO₂e);
- the proposed offset process will consist of the following steps: (i) submission of a proposed offset project plan; (ii) validation of the proposed offset project plan; (iii) registration of the project, which represents formal acceptance of the project plan; (iv) project monitoring, measurement, quantification and reporting; (v) verification of offset project reports and information; and (vi) certification and issuance of ERUs (issued offsets would be assigned a unique serial number and placed in an account in the registry);
- no project types would be excluded from consideration as protocols, and if there is no approved protocol that is applicable to a project type, a new one may be proposed;
- ERUs will be issued for projects located within B.C. and may also be issued for projects located outside of B.C. in a partner jurisdiction (Recognized Compliance Units, or RCUs, are compliance units that will be recognized by B.C. under the Cap and Trade Act, but not issued in B.C.);
- ERUs will only be issued for projects that have a start date of January 1, 2007 or later (the WCI Memorandum of Understanding was signed in 2007);
- annual reports will document project operation, application of project plan and project success;
- verification reports will ensure the environmental integrity of each tonne;
- third-party assurance providers will be accredited to ensure consistent, high-quality application of regulatory requirements;

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- to receive recognition, the assurance body should, at a minimum, be accredited or in the process of obtaining accreditation by a member of the International Accreditation Forum in accordance with ISO 14065 through a program developed under ISO 17011;
- assurance bodies will be recognized as: (i) accredited validation bodies in one or more sectors; and/or (ii) accredited verification bodies in one or more sectors; and
- the B.C. government will carry out periodic risk-based auditing.

UPDATES TO GHG REPORTING REGULATION

B.C.'s *Reporting Regulation* sets out requirements for the reporting of GHG emissions from B.C. facilities emitting 10,000 tonnes or more of CO₂e per year beginning on January 1, 2010. Those facilities with emissions of 25,000 tonnes or more are required to have emissions reports verified by a third party. MOE has indicated that the *Reporting Regulation* will be updated in fall 2010 to complete coverage of imported electricity and to reflect refinements to upstream oil and gas emissions quantification.

In addition, it is worth noting that B.C. and the Canadian federal government signed an Agreement in Principle (AIP) on April 6, 2010, to facilitate a co-ordinated approach to climate change. The AIP is the first step towards a formal equivalency agreement under the *Canadian Environmental Protection Act*. Through this co-ordinated effort, the B.C. and federal governments are seeking to avoid duplicating the regulatory burden on industry. The first deliverable under the AIP is a one-window reporting system through which B.C. emitters will be able to satisfy provincial and federal GHG reporting requirements in a single report. The one-window reporting system is anticipated to be launched online in December 2010.

EMISSIONS TRADING AND B.C.'S CARBON TAX

In B.C., a carbon tax, which has been in place since July 1, 2008, establishes a direct carbon price on the combustion and use of fossil fuels in the province. There have been industry concerns that the implementation of

an emissions trading system will have an adverse effect on the competitiveness of B.C.'s industries. In response to such concerns, the B.C. government has indicated that measures will be implemented to avoid the potential "double taxation" of B.C. companies as a result of the carbon tax and a cap-and-trade system. However, it is unclear which mechanisms will be implemented to ensure that the carbon tax and the emissions trading system will be integrated in a complementary manner.

LOOKING AHEAD

By releasing the consultation papers for its cap-and-trade regulations, B.C. has placed itself ahead of the WCI pack with respect to implementation of an emissions trading system. While both Ontario and Quebec continue to develop their cap-and-trade systems, regulations are not expected until later in 2011. However, with climate legislation stalled in the U.S. Senate, all eyes are on California which will hold its gubernatorial election on November 2, 2010. Also on the California ballot is Proposition 23. If passed by voters, Proposition 23 would suspend AB 32, the *Global Warming Solutions Act of 2006* (GWSA). The GWSA, passed by the California State Legislature in 2006, is California's landmark clean air legislation. Proposition 23 proposes to freeze the provisions of AB 32 until California's unemployment rate drops to 5.5% or below for four consecutive quarters (California's unemployment rate, which currently stands at approximately 12%, has been at 5.5% or below for four consecutive quarters just three times since 1980).

At this stage, it is uncertain whether B.C., Ontario and Quebec would proceed with emissions trading on their own if California decides to suspend or even withdraw its participation from the WCI's cap-and-trade system. WCI members continue to work towards the implementation of the region's cap-and-trade system. However, it would seem to be prudent strategy for all parties to keep their options open.

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