Sustainability & Climate Change Reporter

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October 25, 2011 by Mike Nesteroff

California Passes Cap and Trade. Now What?

When the eighth largest economy in the world, and one that happens to occupy a large portion of the western U.S. coastline, adopts a groundbreaking set of rules, you would think that would get a lot of attention. Yet, after the California Air Resources Board's landmark decision on October 20 to adopt the first of its kind in the U.S. economy-wide cap and trade rules for the state, the occasion seemed to prompt little notice.

It wasn't until nearly five days after CARB's action that a *San Francisco Chronicle* editorial cautiously praised the move: "There is nothing simple about the cap-and-trade approach. There will be a need to tinker and adjust a complex answer to the world's worst environmental problem. But at a time when other governments are hiding from reality, California has shown a willingness to lead." Anne Carlson in the Legal Planet: Environmental Law and Policy blog was more effusive, calling CARB's leadership on the issue "extraordinary," and concluding: "It's common place to attack government as inefficient, bloated and even corrupt and California itself has borne more than its share of attacks as a place where government has gone awry. CARB defies those characterizations. Corny as it sounds, I'm proud today to be a Californian." But the Climate Progress blog only included the adoption in its daily news summary, while devoting a lengthy column to an analysis of media coverage about Solyndra and several posts about the Keystone XL tar sands pipeline.

To be sure CARB's action is not a surprise; it has been in the works ever since California passed AB 32 in 2006, which mandates a reduction in greenhouse gas emissions to 1990 levels by 2020. Even though cap and trade is only one piece of the AB 32 puzzle, it has been the most controversial. The relative quiet in the wake of cap and trade's final adoption perhaps is the understandable result of exhaustion after years of arguments (including an expensive initiative campaign last year and a last-minute legal challenge this year) and the sheer complexity of the program. But now that California has adopted cap and trade, what happens next?

Cap & Trade Outline

Beginning January 1, 2012, 350 California businesses representing approximately 600 facilities, will be covered by the program. Electric utilities and large industrial facilities will come into the program the following year and distributors of transportation, natural gas and other fuels will start in 2015. The cap for 2013 is set at two percent below the forecast for 2012 emissions and will decline two percent in 2014 and three percent each year after until 2020.

Allowances, representing about 90 percent of average emissions, will be allocated free to large industrial facilities initially, but later they will have to buy those allowances at auction. The first auctions will occur in August and November 2012, with the first compliance obligation beginning January 1, 2013.

The trade part of the program will involve banking of allowances to guard against shortages and price swings, with a four percent reserve to contain costs and three-year compliance periods to minimize annual swings in production outputs.

Facilities will be allowed to offset up to eight percent of their compliance obligation, but can only buy offsets for emission-reductions projects in the U.S. The offsets initially will be limited to projects in forestry, urban forestry, dairy digesters and destruction of ozone-depleting substances. There must be independent verification of offsets.

Beyond California

Frequently as goes California, so goes (eventually) the rest of the U.S. Whether or not that is true for cap and trade remains to be seen. Efforts to adopt a national cap and trade program failed in Congress and the debate there has shifted to whether climate change is even an issue of concern.

The most likely venue for expansion of cap and trade is in the Western Climate Initiative (WCI). So far, however, none of the other U.S. members, including Washington and Oregon, have signed on yet and some have expressed serious reservations about ever participating.

Other WCI members, such as the Canadian provinces of British Columbia, Ontario and Quebec, appear to be moving forward with adopting cap and trade. In Ontario's recent election, the Liberal party retained its control over the provincial government, although one vote short of a majority in the legislature. While it's likely the province will continue towards a January 2013 adoption of cap and trade, that will be a year later than California and, in the meantime, the precarious nature of the minority government could change those plans.

Quebec, meanwhile, is about to launch cap and trade, first with a one year pilot program in 2012, that will not set caps but will include allowance auctions, followed by a three-year full cap and trade compliance program. British Columbia went through an election last spring and, after some initial uncertainty, appears to be continuing its efforts to start a cap and trade program although no regulations have been issued yet.

For now, it looks like California will be the laboratory for cap and trade. The path forward is bound to be bumpy as the state once again breaks new ground.

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