# The Future of Offsets in the United States

Alexander Ochs, Director of International Policy
Center for Clean Air Policy

*******

Carbon Market Insights Conference
Copenhagen, Denmark
March 18, 2009

# Center for Clean Air Policy (CCAP)

- Washington, CA, NY, Beijing and Brussels-based environmental think tank
- Committed to advancing pragmatic and cost-effective climate and air quality policy through analysis, dialogue, and education
- CCAP helped draft US CAA, EU ETS and reach agreements on emissions trading, the design of Clean Development Mechanism
- now focused on US domestic legislation and international post-2012 agreement

Center for Clean Air Policy

# Outline

- The change of climate in the US
- US offsets positions and proposals
- Possible solutions
- Transatlantic cooperation

Center for Clean Air Policy

# U.S. Leadership Matters

- Compare recent U.S. decision to support a global accord to reduce mercury emissions
- At the end of February, the Obama Administration reversed 7 years of US opposition to a global agreement on mercury and within days all major nations, including China and India signed onto the agreement

Center for Clean Air Policy

# Change in the U.S.

"I ask this Congress to send me legislation that places a market-based cap on carbon pollution and drives the production of more renewable energy in America."

President Obama, Address to Joint Session of Congress, 24 Feb 2009

Center for Clean Air Policy

# Progress in the House

- Chairman Waxman promises to pass a climate bill from Energy and Commerce Committee by the end of May
  - » Staff are feverishly drafting
    - – Two policy hearings a week
    - – Will change to legislative hearings
  - » Discussion Draft end of March
  - » Plans to combine Climate and Energy Bill
- Ways and Means Committee, which has jurisdiction over a carbon tax and the Treasury Department, is flexing its muscle

Center for Clean Air Policy

# Cost Containment Measures in Climate Legislation: 110th Congress

| | Markey H.R. 6186 | Doggett H.R. 6316 | Lieberman / McCain S.280 | Sanders / Boxer S.309 | Feinstein S.317 | Kerry/Snowe S.485 | Lieberman / Warner S.3036 |
|---|---|---|---|---|---|---|---|
| **Banking** | Allowed, no specified limits | Unspecified | Allowed, no specified limits | Unspecified | Allowed, no specified limits | Allowed, no specified limits | Allowed, no specified limits |
| **Borrowing** | Allowed for up to 15% of obligation. Max borrowing period of 5 years with 10% annual interest. | Unspecified | Allowed for up to 25% of obligation. Max borrowing period of 5 years with 10% annual interest | Unspecified | Allowed for up to 10% of obligation only when prices reach levels that threaten economic harm . Max borrowing period of 5 years plus interest | Unspecified | Allowed for up to 15% of obligation. Max borrowing period of 5 years with 10% annual interest |
| **Offsets** | Domestic and International offsets allowed | Allowed for up to 25% of obligation | Allowed for up to 30% of obligation | Allowed from biological sequestration | Allowed from biological sequestration. 5% limit on offsets from forest management and 25% limit on international offsets | Allowed from biological sequestration | Domestic and International offsets allowed |
| **Transition Assistance** | 6% of allowances allocated to eligible manufacturing facilities that produce "trade-exposed primary goods" | 10% of allowances allocated to affected entities, gradually decreasing to 2% by 2019 | Unspecified | Unspecified | Unspecified | Unspecified | Allocates a portion of allowances to power-generating facilities, rural cooperative owners and intensive manufacturing facilities |
| **International Credits** | Credits will be accepted from foreign cap and trade programs | Accepts credits from foreign cap & trade programs, up to 15% of obligation | Accepts credits from foreign cap and trade programs under "offsets" | Unspecified | Accepts credits from foreign cap & trade programs for up to 25% of obligation, 50% for new affected units | Unspecified | Accepts credits from foreign cap & trade programs up to 15% of obligation |
| **Other** | 1.) Bidding limits: No person can buy more than 33% of allowances for sale.<br>2.) Office of Carbon Market Oversight within FERC would guard against market manipulation | Cost relief measures in case of economic trouble: increasing offsets %, increasing foreign credits %, increasing quantity of allowances | Unspecified | Freezes cap if prices reach the Technology-Indexed Price Stop, a safety valve based on the avg price of reducting emissions given available technology options | Unspecified | Unspecified | Unspecified |

# Offsets in RGGI

- Allows offsets for projects outside the electric power generation sector
- Currently can only offset allowances constrained to 3.3% of installation's total compliance obligation (could grow to 5% or 10% if allowance price thresholds are reached)
- Allowances generated in U.S. may not be the result of projects resulting from any law, regulation, or order
- International offsets (such as CDM) allowed under limited circumstances

Center for Clean Air Policy

# California Offsets

- AB32 scoping plan limits use of offsets to 49% of allowances
- Intention to consider international offsets outside of Western Climate Initiative jurisdictions (incl. CDM)
- CARB has adopted California Climate Action Registry protocols for forestry, local government operations, urban forestry, and manure digestures (possible precursor to use for offsets)

Center for Clean Air Policy

# Government, NGOs, and Industry views on offsets – testimonies to Energy & Commerce Committee

- Most agree that offsets do have a role to play in a future U.S. cap and trade program ut also emphaisize the risks in current approaches including the CDM
- “these markets hold limited promise, both as a cost control mechanism and as a method of engaging developing countries on the problem of climate change while also presenting substantial risks” (Michael Wara, Stanford Law School)
- Must deal with problem of “inherent uncertainty” of offsets to ensure credibility – offsets should be measurable, verifiable, permanent, enforceable, and additional
- Environment America only NGO testifying vigorously against offsets as risk to “real and sustainable cuts”
- Developing country action should be required before offsets from that country will be credited

Center for Clean Air Policy

# Government, NGOs, and Industry views on offsets – GAO 2008 reports

- "While carbon offsets have the potential to lower compliance costs for entities that could be affected by regulatory limits on emissions, their use for compliance in a mandatory emissions reduction scheme could undermine the program's integrity if the offsets lack credibility."

Center for Clean Air Policy

# Government, NGOs, and Industry views on offsets – GAO 2008 reports

- "Our work on CDM identifies challenges with using carbon offsets in a mandatory emissions reduction program despite the use of rigorous quality assurance procedures."
- "Using offsets in a mandatory emissions reduction program would involve fundamental trade-offs between offset credibility and compliance costs."

Center for Clean Air Policy

# Government, NGOs, and Industry views on offsets – GAO 2008 reports

- Pros
  - » Cost containment
  - » Raises interest and engagement, DCs
- Cons
  - » Credibility, additionality
  - » Limitations to domestic changes

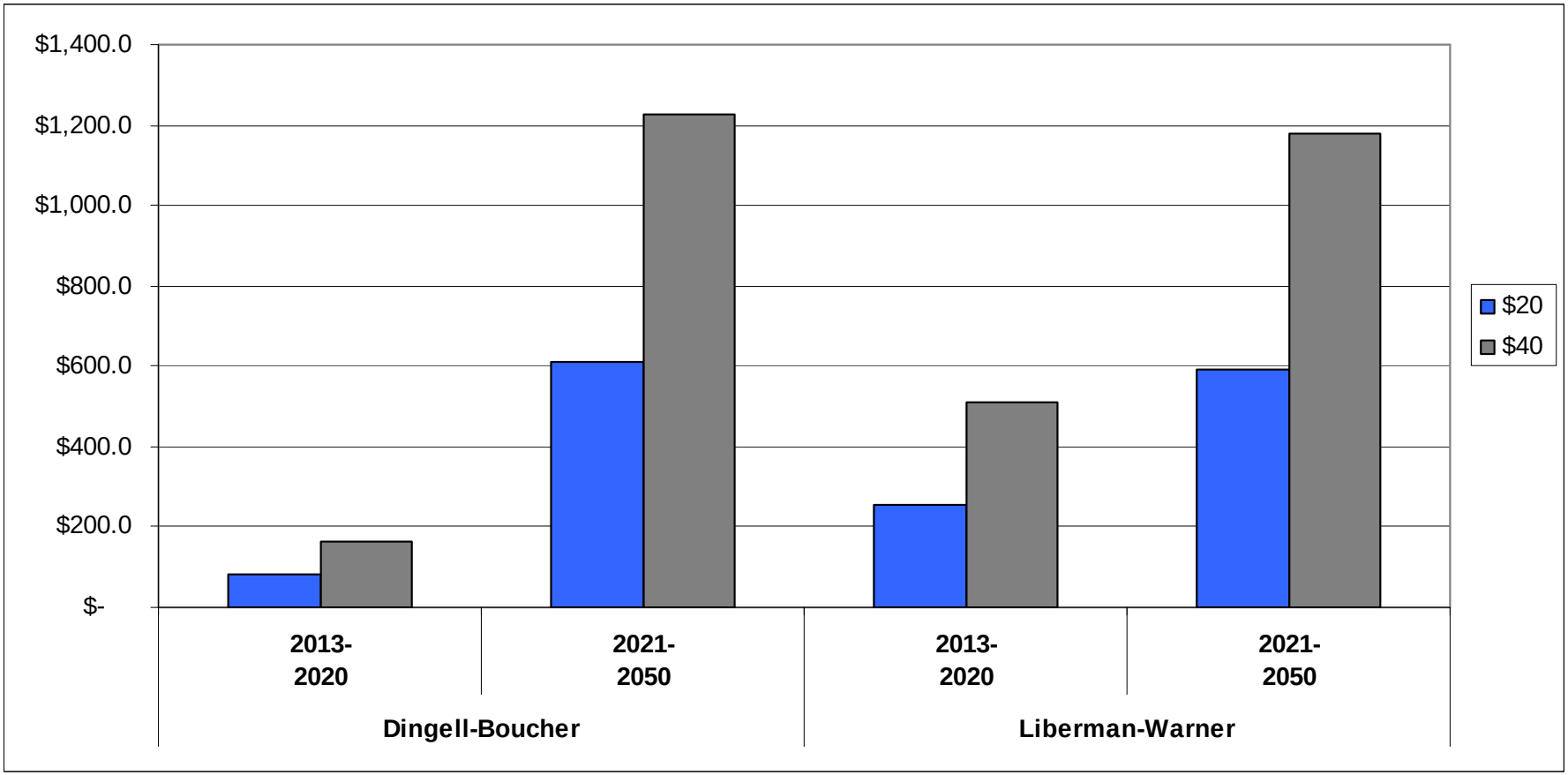
Center for Clean Air Policy

# Government, NGOs, and Industry views on offsets – GAO 2008 reports

- Procedural solutions
  - » Clear rules about the types that can be used
  - » Procedures to compensate for inherent uncertainty
  - » Standardized registry
  - » Procedures for amending offset rules based on experience

Center for Clean Air Policy

# U.S. estimated offset market size




(Billions USD)

Center for Clean Air Policy

# Lieberman-Warner offsets

| k-tones | *2013-2020* | *2021-2050* |
|---|---|---|
| Offsets | 42,370 | 98,249 |
| - International Offsets | 6,356 | 14,737 |
| a) Forestry (10%) | 4,237 | 9,825 |
| b) Other Projects (5%) | 2,119 | 4,912 |

Center for Clean Air Policy

# Sectoral Approach

- Sectoral approaches as reformed CDM present the following advantages:
  - Quantitative and qualitative criteria
  - Ease of administration
  - Data availability
  - Greater equity
  - Increased technology transfer
  - Targeted emission reductions

Center for Clean Air Policy

# Elements for a Sectoral Program

- Builds on developing country unilateral actions
- Places importance on both encouraging sustainable development and on achieving GHG reductions
- Builds goals from the bottom-up and provide incentives for going further
  - » Encourages developing countries to take actions without penalties
  - » Maintains “common but differentiated responsibilities and respective capabilities”

Center for Clean Air Policy

# Conclusions

- Time of change has arrived
- Role of offsets controversial
  - » Environmental vs. economic tradeoffs
  - » Cost advantages vs. competitiveness issues
- Overall negative take of current CDM
- Alternatives currently under consideration
  - » Performance-based/sectoral system
  - » Stringent limits

Center for Clean Air Policy

# Thank You!

Alexander Ochs
Director of International Policy
Center for Clean Air Policy
+1 202 408-9260
aochs@ccap.org

Center for Clean Air Policy