



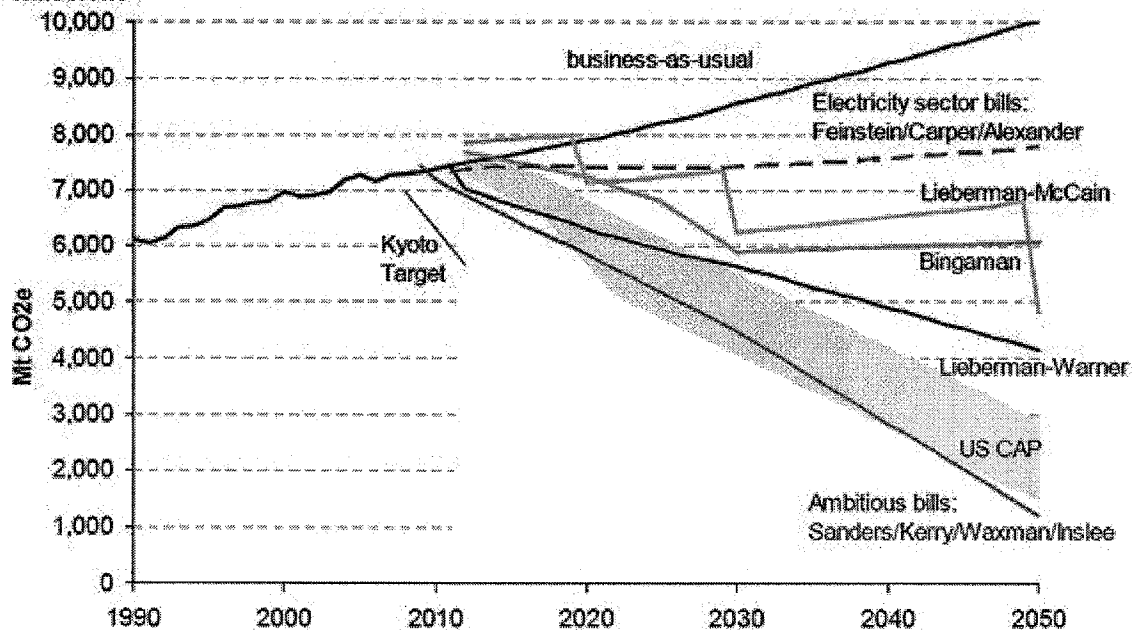
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## CLIMATE CHANGE POLICY AND CARBON MARKETS

- **U.S. Carbon Market Forecasted to Exceed \$1 Trillion by 2020.**

Economists from New Energy Finance (“NEF”) have examined the climate change bills pending before Congress. They conclude that an economy-wide greenhouse gas (“GHG”) cap-and-trade system will likely become operational within five (5) years. The U.S. GHG system will likely be accompanied by an as yet undefined “carbon credit” emissions trading market that NEF’s economists project will top \$1.0 Trillion (US) by 2020, if policymakers continue on their current path. The U.S. carbon market will be more than twice the size of the European Union’s Emissions Trading Scheme (“EU-ETS”), presently the world’s largest operating carbon credit marketplace. Based on its evaluation of the pending bills, NEF predicts that the federal government would ration the amount of GHGs that businesses could emit by issuing (at least at first) them permits. Thereafter, a business seeking to emit more than its permitted “entitlement” will have to buy carbon credits (*i.e.*, similar to SO<sub>x</sub> and NO<sub>x</sub> system). NEF projected each federal bill’s targeted GHG reductions, measured as million of tons of carbon dioxide equivalent (“CO<sub>2</sub>e”) in the following graph:

**Comparison of federal climate-change bills: Business as usual and targeted economy-wide emissions**



Source: New Carbon Finance



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NEF observed that “bills before Congress either prohibit or severely restrict the transfer of allowances from trading systems in other parts of the world, including the [EU-ETS], and the Kyoto Protocol’s Clean Development Mechanism (CDM) and Joint Implementation (JI) schemes.”<sup>1</sup> It concluded that such a U.S. policy that bans international project credits would likely drive up domestic carbon prices to \$35-\$40/ ton of CO<sub>2</sub>e by 2015. NEF further concludes that “any bill passed by the Congress is likely to include [some form of] trade sanctions on imports from countries unwilling to participate in mandatory carbon emission caps.”<sup>2</sup>

In addition to NEF, two other entities project significant growth for mandatory and voluntary carbon credit markets, respectively, in 2008 and beyond. Point Carbon’s report “Outlook for 2008” projects a 56% increase in global emissions trading volume to approximately \$92 billion in 2008, with about 4.2 billion tons of CO<sub>2</sub>e traded.<sup>3</sup> ICF International released its own “2008 Voluntary Carbon Offsets Market Outlook,” which projects growth in the global voluntary carbon market from 20 million tons of CO<sub>2</sub>e in 2006 to roughly 220 million tons in 2012.<sup>4</sup>

- **The Senate’s Lieberman-Warner Bill**

Widely known as the “Lieberman-Warner” bill (S.2191), the Climate Security Act of 2007 passed the Senate Environment & Public Works Committee on December 5, 2007. Among the dozen or so proposals in Congress, The Lieberman-Warner bill is now in the best position to become law. If the bill is enacted, companies will have to quickly begin monitoring and reporting GHG footprints. NACWA and WEF are both continuing to advocate the inclusion of water and wastewater agencies as regulated under the Bill while concurrently entitled to participate in any resulting domestic carbon market.

This bill would require a 70 percent reduction in GHG emissions from covered facilities between 2012 and 2050. It would put EPA in charge of handing out a descending number of allowances each year and require covered industries to surrender enough allowances at year-end to cover all their annual GHG emissions. The bill would establish a Climate Change Credit Corporation, and EPA would allocate an increasing share of the allowances — from 22.5 percent in 2012 to 70.5 percent in 2031 and beyond — to be auctioned. In this way, the program shifts over time from almost 80 percent allowances based on baseline emissions needs to 70 percent of allowances auctioned.

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<sup>1</sup> NEF Report, found at <http://www.newenergyfinance.com>, last visited March 7, 2008.

<sup>2</sup> *Id.*

<sup>3</sup> Point Carbon’s “Outlook for 2008” can be found at <http://www.pointcarbon.com>, last visited March 7, 2008

<sup>4</sup> See, e.g., <http://www.icfi.com/Markets/Climate-Change/>, last visited March 7, 2008



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In the early years particularly, there are special allocations of allowances reserved to encourage or compensate early action, energy savings, state programs, mass transit, electricity consumers, natural gas consumers, carbon capture and sequestration, agriculture and forestry, and even overseas reforestation projects. This bill does not cover mobile sources, or wastewater treatment, but it recognizes allowances from verified offset projects. Verified credits available through emissions reduction capital projects (*e.g.*, methane capture, microsludge waste-to-energy, wetlands redevelopment, carbon capture and storage, and CO<sub>2</sub> sequestration), could generate tradable “offsets” allowances to be transferred to other entities or sold into the future carbon trading exchange. The bill also permits covered sources to use up to 15 percent foreign GHG credits from EPA-certified markets.

The Bill also contains a controversial “safety valve” to be administered by a new Carbon Markets Efficiency Board. This Board would be empowered to gather information, to publish reports on the economic effects, and to adopt and implement “cost relief measures” spelled out in the bill.

- **House Cap-and-Trade Efforts**

Chairman Dingell (D-Mich) of the House Energy and Commerce Committee plans to have all House-developed cap-and-trade bills ready for comment by April 2008. On February 28, 2008, he and Rep. Boucher (D-VA) released their third White Paper on climate change regulation. It addresses “what roles are best played by each level of government as we marshal our country’s resources to address climate change and how should these roles be reflected in Federal legislation.”<sup>5</sup> The ultimate goal of the legislation is to reduce U.S. GHG emissions by 60 to 80 percent by 2050. The White Paper evaluated the following factors:

- (i) the global effects of GHG;
- (ii) the effect on the level and cost of national GHG reductions;
- (iii) the efficient use of government and societal resources
- (iv) the benefit of States, Tribes, and localities as demonstration laboratories;
- (v) local circumstances;
- (vi) interstate commerce issues; and
- (vii) costs to other States.

The White Paper concludes that each level of government needs to play certain pre-determined roles in the development of the ultimate federal climate change legislation.

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<sup>5</sup> The White Paper can be found at [http://energycommerce.house.gov/Climate\\_Change/white%20paper%20st-1cl%20roles%20final%202-22.pdf](http://energycommerce.house.gov/Climate_Change/white%20paper%20st-1cl%20roles%20final%202-22.pdf), last visited March 7, 2008.



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- **Proposed Changes to EU Emissions Trading Scheme**

On 23 January 2008, the European Commission presented the “European Union Climate Action” package, which included a new proposal to meet the EU’s GHG reduction commitments. The proposal was split into two scenarios, the first assumes a continued EU-only carbon market; the second, a global carbon market after the Kyoto Protocol lapses in 2012. The Commission’s proposal for a post-2012 market is to publish an absolute quantity of allowances by 2010, accompanied by a descending annual schedule to arrive at an EU-wide 21percent reduction below 2005 GHG levels by 2020. The allowances, or carbon credits, will be auctioned, rather than issued. If no global carbon treaty is secured post-2012, the Commission intends to avoid the “relocation” of GHG emitting activities outside of the EU by regulated, energy-intensive industrial sectors. The Commission also intends, among other innovations, to provide additional incentives for carbon capture and storage and EU-based offset projects to generate carbon credits.

- **Preparation for Climate Change Regulation**

Regardless of what the substance and infrastructure of any future federal climate change regulation actually turns out to be, there are steps that NACWA members can take and evaluate now to prepare for a carbon-constrained economy. The following is a short list of actions NACWA members might wish to consider:

- (i) depending on the jurisdiction of the agency, evaluate and understand the agency’s position and participatory role in all applicable carbon markets as established by the patchwork of state, regional and possibly international (*e.g.*, Western Climate Initiative) laws, regulations and policies that may affect not only the agency, but the local economy, such as carbon taxes and financial incentives;
- (ii) continue to inventory and track CO<sub>2</sub>e emissions levels and centralize any reporting activities;
- (iii) through NACWA, continue to monitor the debate on GHG legislation (and potential regulations) and be sure your emissions are fairly and accurately represented;
- (iv) evaluate your GHG offset project eligibility for verification, even in voluntary carbon markets;
- (v) evaluate your wastewater system for potential sustainable energy and water efficiency improvements or upgrades and identify specific GHG reduction project opportunities; and



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(vi) continue advocacy efforts both nationally through NACWA and at the state level to ensure legislators link climate change regulation with national water management efforts and objectives.

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If you would like additional information regarding any of the items discussed above, or if you would like to discuss these issues further, feel free to contact us anytime.

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