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Ms. Nicole Singh
Regional Greenhouse Gas Initiative Inc.
90 Church St. 4th Floor
New York, NY 10007

## IETA STAKEHOLDER COMMENTS ON RGGI STAKEHOLDER WEBINAR OCTOBER 18, 2012

On behalf of the International Emissions Trading Association (IETA), I am grateful for this opportunity to provide comments in response to the Regional Greenhouse Gas Initiative's (RGGI's) Request for Stakeholder Comments relating to the webinar hosted by RGGI Inc. on October 18. IETA welcomes this opportunity to provide our insight into how to best improve the program during this period.

IETA is dedicated to the establishment of market-based trading systems for greenhouse gas emissions that are demonstrably fair, open, efficient, accountable, and consistent across national boundaries. IETA has been the leading voice of the business community on the subject of emissions trading since 2000. Our member companies include some of North America's, and the world's, largest energy and industrial corporations—including global leaders in oil, electricity, cement, aluminum, chemicals, paper, and banking; as well as leading firms in the data verification and certification, brokering and trading, offset project development, legal, and consulting industries.

RGGI has put forward a number of proposed changes to the program during the stakeholder webinar:

- Introducing a cost containment reserve (CCR) that adds additional allowances into the market at price triggers that rise periodically
- Removing the offsets price trigger, whereby international units can be used for compliance at a certain price trigger, and replacing it with the CCR *or* a domestic offset expansion at a price higher than the CCR trigger
- Removing the potential to extend the control period at a certain price trigger
- Adjusting the reserve price inflation rate to a fixed 2.5% and removing provisions on "current market reserve price"
- The introduction of an interim true-up period, where 75-80% of annual emissions must be surrendered for the first two years, and then a final true-up in year 3 of the control period
- Potential adjustment of future caps to take into account first and second control period banked allowances
- Alterations to the timing of decisions for unsold allowances; either before implementation, or at a specified interval.

In addition, RGGI *will* be developing its own U.S Forests Offsets Protocol to replace the current Afforestation project category to include: Forest Management, Avoided Conversion, and Reforestation.

IETA believes that these potential changes need to be carefully considered. The development of a Cost Containment Reserve (CCR) must be used in clearly-defined circumstances and not become a source of confusion in the marketplace. Quantitative limits on offsets have the potential to cause liquidity problems in the RGGI marketplace for covered entities, and should be relaxed or eliminated. IETA also believes that the focus should be on broadening the types of offsets available, including simplifying access to international units, to broaden choice and draw upon the expertise and liquidity available from other programs and standards. A first step in this direction would be to harmonize the protocol for U.S Forestry with existing methodologies available and in use, helping project developers to invest resources in these projects.

Control periods should be clearly defined and predictable, and not subject to changes dependent upon exogenous factors such as market prices. The current market reserve price can be removed to simplify the minimum price at RGGI auctions. There are considerations that need to be taken into account for the interim true-up period. Banked allowances must be taken into account but must also maintain their value as a compliance instrument as the program continues. Finally, the impacts of various decisions taken on unsold RGGI allowances should be considered before decisions are taken.

IETA, therefore, presents the following insights and recommendations for consideration by RGGI Inc.

## COST CONTAINMENT RESERVE (CCR)

**Consider potential market distortions associated with a CCR**

RGGI has put forward a proposal to hold an additional number of permits *above the cap* in reserve, to be made available when allowance prices hit a defined trigger point. Based on the previous modeling that has been undertaken, the prospective quantity of allowances in the CCR would be 10 million and the trigger prices would be $5 in 2014, $7 between 2015 and 2017, and $10 in 2018.

IETA generally cautions against the use of an allowance reserve in program design. The CCR, as currently proposed, does set specific parameters for the sale of additional allowances at auctions in cases where there is an exhaustion of supply at prices above the CCR trigger. However, it does also introduce a “soft cap” on emissions under the program, because the reserve creates additional allowances over and above the defined cap.

An allowance reserve, at best, can perform a price smoothing function and reduce market risk, provided the mechanism’s parameters, size, and conditions under which reserves will be released into the market are defined and certain. Under this best-case scenario, the market will effectively factor reserve dynamics and impacts into pricing. While short term price smoothing can provide a consistency signal to project developers, a CCR does not provide any assurance of real long-term cost containment.

In contrast, if reserve parameters and conditions are not clear to market participants, the existence and impact of the allowance reserve essentially becomes a “wild card”, whereby unnecessary risk is injected into the market, debilitating the emergence of a fully functional market and impeding policy objectives.

## OFFSETS

**Caution against the use of Offset Price Triggers**

IETA has stated in its previous submissions to RGGI the need to draw from a broad range of potential offset credits to increase liquidity and options available to covered entities in the market. [1] This should be achieved by accepting protocols developed under respected external registries such as the Verified Carbon Standard (VCS), the American Carbon Registry (ACR), and the Climate Action Reserve (CAR). Additionally, the availability of international offsets should not be overlooked, such as Certified Emissions Reductions (CERs) developed under the robust framework of the UNFCCC Clean Development Mechanism (CDM). IETA believes drawing on the experience developed by the expertise in these areas will reduce transaction costs associated with implementing projects and issuing credits, and draw in greater levels of investment than relying upon protocols developed and maintained by RGGI.

IETA believes quantitative limits on offsets unnecessarily restrict the options available for compliance and raises program costs. Program and entity-usage limits would create uncertainty for offset project developers and investors with long-term planning horizons. Ideally, the total supply for offsets should be decided by market participants through price signals, rather than pre-determined in the program rules. This would create a situation in which private actors are given the greatest amount of flexibility to achieve real emissions reductions at the lowest economic cost.

However, IETA believes that if a quantitative limit is in place then it needs to be defined and not subject to exogenous price triggers to increase the permitted supply. Project developers will make investments based on projections of market conditions many years in the future, and regulations such as price triggers introduce unnecessary uncertainty into such planning.

Therefore, IETA would recommend removing the quantitative limit on offsets, alongside positive steps to broaden and simplify the availability of offsets in the RGGI program. If a quantitative limit must remain in place, it should be set at the highest percentage possible, and, to simplify the process, remove offset expansion price triggers. International offsets should be permitted for compliance without the need for a price trigger that adds complexity and uncertainty to the market.

## RGGI US FOREST OFFSETS PROTOCOL

Harmonization and standardization of offset protocols is an important incentive to drive capital investment in projects, by allowing projects to be potentially eligible to market credits in multiple systems. As mentioned previously, IETA believes that enabling protocols developed by the VCS, ACR, and CAR, as well as international offsets, will make significant strides in incentivizing such investments.

RGGI is moving forward to develop a U.S Forests protocol, which is similar to the protocol developed by the California Air Resources Board (ARB) for use in the California cap-and-trade program. To be clear, IETA would prefer to have RGGI allow offsets developed in other standards to be used for compliance, rather than adding complexity by building their own protocols. However, if RGGI continues to develop such a protocol, IETA believe that the U.S Forestry protocol should be

[1] See, for example: IETA Submission to RGGI June 11 2012. Download available here

developed to be as harmonized as possible with high-quality offset standards such as those developed by ACR, VCS, and CAR that are already produced.

## CONTROL PERIOD

Currently RGGI utilizes a period for compliance of three years, with the potential to increase to four years in the event of a stage two-price trigger event. IETA believes that multi-year compliance periods provide flexibility for companies in how they choose to comply with the regulations. However, changing compliance rules based on an exogenous factor, such as allowance prices, has the potential to undermine such predictability, and RGGI should take this into consideration when making potential changes to the RGGI program. Therefore, IETA recommends that the control period should be not be adjusted based on a price trigger.

## THE CURRENT MARKET RESERVE PRICE

IETA welcomes the proposal put forward by RGGI Inc. to remove the reference to the use of a current market reserve price when determining the auction floor price. IETA believes that this provision brings unnecessary complexity into the auction process and is please to see a more simplified auction floor price arrangement put in place.

## INTERIM TRUE-UP PERIOD

RGGI is suggesting that the rules on compliance will be modified to introduce an interim true-up annually of 75-85% of an entity's compliance obligation. Consideration should be given to the potential benefits of greater pricing transparency from mandating levels of surrender annually. However, there is also the potential to reduce flexibility and add administrative costs for covered entities. RGGI should take these issues into consideration when making a decision, and IETA would welcome a continued dialogue on this point.

## ADJUSTMENT OF FUTURE CAPS TAKING INTO ACCOUNT BANKED ALLOWANCES FROM FIRST AND SECOND CONTROL PERIOD

IETA believes that banked allowances should be treated as an equal, tradable instrument as current and future vintage allowances. It is important to maintain fungibility in the RGGI market, and any form of discounting to banked allowances would be detrimental to this fungibility. Entities who have acquired and banked allowances under good faith and under previous rules must realize the full benefits of this transaction. This is an essential point to ensure there is continued faith and confidence in transacting in the RGGI market. At the same time, the level of banked allowances between control periods can be taken into consideration in the determination of future emissions caps, though not imply any specific decision regarding the cap level.

## TREATMENT OF UNSOLD ALLOWANCES

IETA expresses concern that decisions taken to retire unsold allowances in the RGGI program may lead to greater compliance costs for covered entities. This should be taken into consideration before any decision is taken on the treatment of unsold allowances. Sufficient notice needs to be given in order to provide the market an adequate amount of time to respond without causing unnecessary volatility.

## CONCLUDING REMARKS

In summary, IETA believes that there are effective policy changes made possible under the 2012 Program Review that would improve the efficacy of the RGGI carbon market to drive cost effective emissions reductions. IETA is encouraged that RGGI is looking at potential amendments and the recommendations outlined in these comments would build upon the foundations of the current program, progressing RGGI further towards cost effective emissions reductions.

Once again, on behalf of IETA and our member companies, I would like to thank you for your attention to these comments. Please do not hesitate to contact either myself, or Anthony Mansell (Mansell@ieta.org) with questions.

Sincerely,

Dirk Forrister
President and CEO