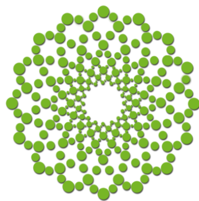
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Colin McConnaha
Manager, Office of Greenhouse Gas Programs
Oregon Department of Environmental Quality
Via email to CapandReduce@deq.state.or.us

Re: Comments on Climate Protection Program Rulemaking Advisory Committee Meeting No. 5

Dear Mr. McConnaha:

The Green Energy Institute at Lewis & Clark Law School is a nonprofit energy and climate law and policy institute within Lewis & Clark's top-ranked environmental, natural resources, and energy law program. We greatly appreciate the opportunity to participate in the Rulemaking Advisory Committee (RAC) for the Department of Environmental Quality's (DEQ) Climate Protection Program, and respectfully submit these comments on issues raised in the fifth RAC meeting and the initial draft rules.

1. Equity

DEQ has identified promoting equity as a key priority for the Climate Protection Program (CPP), and we urge the agency to clarify and emphasize the program's equity objectives in the draft rules. Specifically, the purpose and scope section should clearly state that the program aims to benefit rather than burden environmental justice and impacted communities. We urge DEQ to revise the draft rules to emphasize the program's equity goals.

Equity Recommendations:

- Revise § 340-271-0010(3) to clarify that the program aims to "*equitably protect and* enhance public welfare."
- Revise § 340-271-0010(3)(d)(C) to clarify that the program aims to "Support investments to reduce emissions in communities disproportionately impacted by air contamination and climate change *and promote benefits and alleviate burdens for environmental justice and impacted communities*."
- Add a definition for "impacted communities" in § 340-271-0020 to clarify that impacted communities include environmental justice, Black/indigenous/people of color, low-income, rural, coastal, and other communities that are impacted by or disproportionately vulnerable to the impacts of climate change and risk being left behind by the transition to a deeply decarbonized economy.

2. Applicability

A. Applicability Thresholds

DEQ's leanings on the applicability thresholds for natural gas suppliers and stationary source process-based emissions are reasonable. However, DEQ's proposed applicability threshold of 200,000 metric tons CO_2e ($MTCO_2$e) for non-natural gas fuel suppliers is inconsistent with the state's greenhouse gas (GHG) reduction goals and the directives established through Executive Order 20-04. Based on 2019 reported emissions data, a 200,000 $MTCO_2$e threshold would only cover 88% of the emissions from this sector. If applicability is determined by emissions averaged over a three year period (2017–2019), DEQ's proposed threshold would only cover 85% of non-natural gas fuel supplier emissions. This approach would leave millions of tons of GHG emissions unregulated under the CPP. In 2019, for example, a 200,000 $MTCO_2$e threshold would have exempted 2,708,328 to 3,440,855 $MTCO_2$e from regulation under the program. A regulatory gap of that magnitude would undermine the effectiveness of the program and jeopardize Oregon's ability to meet its GHG reduction goals.

We strongly urge DEQ to reduce the applicability threshold for non-natural gas fuel suppliers to 25,000 $MTCO_2$e. This threshold would cover approximately 99% of emissions from this sector, which reflects the level of regulation necessary for Oregon to achieve its climate targets.

B. Determining Applicability

We strongly agree with DEQ's leaning that non-natural gas fuel suppliers should be subject to regulation under the program the first year that they hit the program's emissions threshold. We also agree with DEQ's proposed approach to make initial applicability determinations based on historical emissions data. Due to the substantial annual variation in reported emissions from sources in this sector, we encourage DEQ to apply three metrics when determining applicability: 1) average emissions from the previous three years, 2) average emissions from the previous five years, and 3) the highest single-year emissions in the previous three years. If a source's emissions exceed the threshold under any of these metrics, the source should be subject to regulation under the program. We encourage DEQ to use these metrics to determine applicability for the initial compliance period and continue to follow this approach over the course of the program. For initial compliance period applicability determinations, DEQ should exclude 2020 emissions from review.

Applicability Recommendations:

- Revise §§ 340-271-0110(4) and 340-271-0130(1)(b) to reduce the applicability threshold for non-natural gas fuel suppliers from 200,000 $MTCO_2$e to 25,000 $MTCO_2$e.
- Revise § 340-271-0110 to clarify that for the purposes of determining applicability, "covered emissions" may include any single-year emissions reported over the previous three years, an average of reported annual emissions from the previous three years, or an average of reported annual emissions from the previous five years (excluding 2020 emissions).

3. Covered Emissions

We strongly urge DEQ to revise section 340-271-0110(6)(b)(B)(ix) to specify that the draft rules only exempt emissions from fossil fuel-fired power plants (*i.e.*, electric generating units) owned by electric utilities with service territories in Oregon. As proposed, the draft rules would create a significant regulatory gap for emissions from natural gas-fired power plants owned by merchant power producers. Proposed legislation currently under consideration by the Oregon legislature would direct the Public Utility Commission (PUC) to oversee the decarbonization of electricity sold by Oregon's investor-owned utilities, and would prohibit the Energy Facility Siting Council from issuing site certificates for new gas-fired power plants in Oregon. However, this bill, HB 2021, would not extend the PUC's regulatory authority to merchant gas plants, nor would it expressly prohibit investor-owned utilities from selling their existing in-state gas plants to merchant power producers. We share the concerns raised by Columbia Riverkeeper that this regulatory loophole could encourage unregulated companies to purchase Oregon's existing gas plants and lock in the emissions from these plants for decades to come. It is therefore imperative that DEQ revise the draft rules to remove any exemptions for emissions from merchant-owned gas plants in Oregon.

Covered Emissions Recommendation:

- Revise § 340-271-0110(6)(b)(B)(ix) to add the following italicized language: "Emissions from an air contamination source that has an applicable code of 221112 in the 2017 North American Industry Classification System *and that is owned by an electric utility as defined in ORS 757.600*."

4. Setting the Cap and Generating Compliance Instruments

The CPP's declining emissions cap will ultimately have the greatest influence over the program's integrity and impacts, and it is imperative that this cap remain as ambitious as possible for the entirety of the program. While we agree with DEQ's proposed strategy to determine a program-wide emissions cap and distribute compliance instruments (CIs) to sources from within that cap, we urge DEQ to revise section 340-271-0410(1) of the draft rules to enable the program to adapt and maintain ambition as needed if real-world conditions shift in unexpected ways.

In the current iteration of the draft rules, DEQ is proposing to create a table that specifies the program-wide cap and associated CIs for each compliance period. This approach will prevent DEQ from maintaining or increasing the program's ambition if real-world emissions drop more quickly than the cap declines. For example, if other regulatory programs or market dynamics unrelated to the CPP cause demand for transportation fuels or natural gas to drop more quickly than projected, the draft rules would force DEQ to generate more CIs than necessary. If these excess CIs are then distributed to fuel suppliers, the suppliers would have no need or incentive to make further emissions reductions, and could either bank the excess credits (preventing additional emissions reductions in the future) or sell them to other regulated entities and prevent emissions reductions in other sectors. If DEQ instead withholds the excess CIs in a reserve account, it could create opportunities for new market entrants to come online that lock in new emissions moving forward.

Given the urgency and severity of the climate crisis, the CPP must be able to respond and adapt to changing circumstances and shifting consumer behaviors. Rather than lock in a rate of emissions reductions that may seem achievable under existing conditions, the CPP should aim to maximize emissions reductions as quickly as possible.

Cap and Compliance Instrument Recommendations:

- Revise § 340-271-0410 to authorize the agency to review the cap at the close of every compliance period and revise the cap if necessary to reflect actual reported emissions during the compliance period *or* to respond to the best available science regarding necessary emissions reductions.
- Specify in § 340-271-0410 that the agency has discretion to withhold CIs from distribution to regulated entities.
- Clarify that the agency has discretionary authority to update the table in OAR 340-271-1300 to reduce the cap and/or the cap's rate of decline to maintain program ambition and integrity.

5. Compliance Instrument Distribution

With the exception of the program-wide cap and emissions reduction targets, CI distribution will arguably have the greatest impact on the program's integrity, particularly if the program allows for unrestricted banking and trading of CIs. If DEQ over-allocates CIs to any regulated entities in any compliance periods, it could deter or prevent necessary emissions reductions in the affected and future compliance periods. It is therefore imperative that DEQ establish clear criteria and processes for distributing CIs among sources and sectors. These criteria and processes must ensure that sources' baseline emissions are accurately calculated for each compliance period, and that CI distributions will result in meaningful emissions reductions relative to these baselines. At a minimum, CI distributions must always require meaningful reductions over baseline emissions reported in the preceding compliance period.

Given the risk that over-allocation of CIs presents for the integrity of the program, we urge DEQ to craft CI distribution rules that account for potential contingencies. For instance, under most circumstances, it will make sense to determine an entity's CI distribution by averaging the entity's emissions from the previous three years. This approach will help even out annual variability in emissions and deter entities from inflating their emissions in the last year of a compliance period to increase their CI distribution in the following period. However, a three-year average approach could also lead to over-allocations of CIs if a source's emissions are abnormally high in any single year. The CPP's CI distribution rules should allow DEQ to omit any abnormally high or unrepresentative emissions data from a source's baseline calculations in any compliance period. Another option is to distribute CIs based on a source's average annual emissions over any two years (out of the previous three years) that had the lowest reported GHG emissions during the compliance period.

CI distribution should also reflect any emissions reductions attributable to any CCIs purchased in previous compliance periods. For example, if an entity purchases five CCIs and applies them toward their compliance obligations in compliance period 1, the entity's CI distribution in compliance period 2 should be reduced by five to account for the emissions reductions associated

with the CCI credits. Under this approach, CCIs would effectively enable entities to borrow emissions from later compliance periods.

6. Compliance Instrument Reserves and Retirements

DEQ should establish a CI reserve to account for any emitting entities (primarily non-natural gas fuel suppliers) that do not currently exceed the proposed emissions thresholds but may hit the applicability thresholds at some point in the future. To create this reserve, DEQ should withhold a certain number or percentage of CIs from distribution during each compliance period. The appropriate number of CIs withheld will depend on the applicability thresholds in the final rule. For example, if DEQ retains the 200,000 $MTCO_2e$ threshold for non-natural gas fuel suppliers, DEQ must reserve a substantial number of CIs to account for the high level of emissions from any fuel suppliers that exceed the treshold. If, however, DEQ lowers this threshold to 25,000 $MTCO_2e$ (which we strongly urge the agency to do), DEQ would need to withold fewer CIs for the reserve. If there are insufficient CI reserves to cover the emissions from any new fuel supplier program entrants, total emissions regulated under the CPP will exceed the cap and the program's integrity will be compromised.

DEQ should establish limits on CI distribution for new entrants, but these limits should differ depending on the classification of the new entrants. For example, because new natural gas fuel suppliers would likely produce high quantities of emissions, yet are unlikely to enter the Oregon market, DEQ should establish stringent limits on CI distributions for this class of emitters to deter new natural gas suppliers from entering the Oregon market. However, because there are already a large number of non-natural gas fuel suppliers operating in Oregon with emissions below the proposed applicability threshold, DEQ must be prepared to distribute reserved CIs to any non-natural gas fuel suppliers that trigger the thresholds because those emissions will have already occurred—and will presumably continue to occur—in the state. DEQ should impose some limits on reserve CI availability to incentivize unregulated fuel suppliers to keep their emissions below the thresholds, but these limits should not be so low that they risk compromising program integrity by allowing regulated emissions to exceed the cap.

CIs held in the reserve should expire after a set period of time to increase program ambition. DEQ will likely face significant pressure to distribute CIs from the reserve as the cap declines and compliance obligations become increasingly stringent. If reserved CIs have indefinite lifespans and the reserve account continues to grow over time, the reserve would be vulnerable to industry and political pressure that could lead to a surge in emissions in later compliance periods. We encourage DEQ to allow reserved CIs to expire after one or two compliance periods to preserve the CPP's ambition and integrity.

While CIs from the reserve should be available for distribution to new program entrants, the reverse should not occur for any regulated entities that exit the program. If a regulated entity exits the program for any reason, section 340-271-0440 should require the exiting entity to surrender any unused CIs to DEQ, and DEQ should retire these CIs immediately. This requirement will become increasingly necessary as the economy decarbonizes and demand for fossil fuel decreases. If remaining entities are permitted to buy or otherwise absorb unused CIs from entities exiting the program, it could create a perverse "last entity standing" dynamic where

the remaining entities acquire enough CIs to delay additional emissions reductions for years or even decades. To prevent this outcome, CIs should expire when their holders exit the program. This expiration provision should also have a look-back period that extends to the close of the previous compliance period. Any CIs sold by an exiting entity during that look-back period should expire at the close of the current compliance period.

Compliance Instrument Reserve and Retirement Recommendations:

- Establish a CI reserve for non-natural gas fuel suppliers that exceed the program's applicability thresholds. Specify that CIs deposited into the reserve account must be withheld from CIs generated under the cap that would otherwise be distributed to regulated entities.
- Impose three or six-year expiration dates on CIs held in the reserve account.
- In the draft rules under development for reserved § 340-271-0440, mandate that any unused CIs by an exiting entity are ineligible for sale or trade and must revert back to DEQ.

We are happy to clarify or elaborate on any of the considerations or recommendations we have raised in these comments; please let us know if you have any questions. We greatly appreciate your consideration of our input on the draft rules and other program design elements still under development.

Sincerely,

Amelia Schlusser
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The Green Energy Institute at Lewis & Clark Law School