

EMISSIONS TRADING AND CLIMATE CHANGE BULLETIN

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CALIFORNIA ADOPTS TOUGH NEW RULES TO COMBAT CLIMATE CHANGE

While several states have adopted emissions trading programs to meet smog reduction requirements under the U.S. Environmental Protection Agency's *Clean Air Interstate Rule*, California's new *Global Warming Solutions Act of 2006* ("Bill 32") deserves special attention as it focuses exclusively on climate changing greenhouse gases ("GHGs")¹ and establishes a framework for some of the most significant controls on GHG emitters in North America.

Bill 32 requires the State Air Resources Board (the "State Board") to adopt statewide GHG emission limits equal to 1990 levels by the year 2020, achieving an estimated 25% reduction in GHG emissions. All entities (the "GHG Sources") whose emissions "are at a level of significance" will be required to reduce, limit and/or report their GHG emissions. A GHG Source's emissions will be deemed to be at "a level of significance" if that entity's participation in the mandated emission reduction program would enable the State Board to effectively reduce GHGs. These would certainly include the State's largest industrial participants such as cement plants, oil refineries and utilities, and may extend to any number of other sectors.

GHG Sources will be required to report their GHG emissions and have them verified. Emissions will be measured using carbon dioxide equivalents² as established by the United Nations Intergovernmental Panel on Climate Change. Once the reporting and verification procedures are in place, the State Board is authorized to enforce compliance measures imposed by the State. Of significance, however, is that market-based mechanisms, such as emissions trading, may be permitted.

Bill 32 establishes the following timeline:

- By June 30, 2007 the State Board will make available early action reduction measures. GHG Sources can adopt early action reduction measures beginning January 1, 2010 and receive credit for them when GHG emission limits are implemented in 2012.
- By January 1, 2008 regulations requiring the mandatory reporting and verification of GHGs will be adopted. These reporting requirements aim to account for GHGs from all electricity consumed in the State of California, including transmission and distribution line losses from local and imported generation. The State Board will use the reported numbers to monitor and enforce GHG emission reduction measures.
- By January 1, 2008 the State will also determine what statewide levels of GHG emissions were in 1990 and set the 2020 target at a similar level. This determination will only be made following public consultations, which are necessary since there was little, if any, reporting of GHG emissions in 1990.

¹ GHGs are defined for the purposes of Bill 32 as including carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons and sulphur hexafluoride.

² The carbon dioxide equivalent for a gas is derived by multiplying the tonnes of the gas by the associated Global Warming Potential (GWP). The GWP for the GHGs targeted by Bill 32 over a 100 yr time period are as follows: carbon dioxide (1), methane (23), nitrous oxide (296), hydrofluorocarbons (12,000), perfluorocarbons (various) and sulphur hexafluoride (22,000). For example, 1 million metric tonnes of methane emissions is equivalent to 23 million metric tonnes of carbon dioxide emissions in terms of the methane's effect on causing the greenhouse effect over a 100 yr period.

- By January 1, 2009 the State Board will prepare and approve a formal scoping plan (the “Plan”) pursuant to which the new targets can be met. The Plan will contain recommendations on direct emission reduction measures, alternative compliance mechanisms, market-based compliance mechanisms, and monetary and non-monetary incentives. The Plan also includes a *de minimis* threshold of GHG emissions below which emission reduction requirements would not apply, to protect small businesses who might not possess the economic means to comply.
- January 1, 2012 is the date on which GHG Sources must begin to comply with the GHG emissions limits. Any approved market-based mechanisms, including a possible climate exchange, will also become operative on this date.

The GHG emission limits set out by the State of California are indeed aggressive. As such, Bill 32 was met with widespread opposition by the Republicans in the Legislature and many industry representatives. However, the Chairman of Pacific Gas and Electric, supported the bill.

California frequently acts as a bellwether for the rest of the United States on environmental issues. It remains to be seen whether California’s implementation of tough new limits on GHG emissions will influence environmental policy in other states and policy at the federal levels.

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The foregoing provides only an overview. Readers are cautioned against making any decisions based on this material alone. Rather, a qualified lawyer should be consulted.

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