OFFSETS SYSTEM POLICY DEVELOPMENT CURRENT STATUS

Federal / Provincial / Territorial

National Forest Sinks Committee

May 28, 2004

PRESENTATION OUTLINE

- **Status of Policy Development**
- **Key Design Issues**
- **Next steps**

CONTEXT

- Presentation provides an overview of the current stage of thinking
- No decisions have been taken yet

POLICY DEVELOPMENT

Working Group on Offsets - federal government team

- EC (EC legal services), NRCan, AAFC, DFAIT, PCO

Offset System Discussion Paper (June 2003)

- options for addressing key design elements

National Consultations (June 2003) - based on Discussion Paper

- over 85 substantive written submissions
- informal contacts continue with individual jurisdictions and stakeholders

WGO workshops

- half day/week since January 2004 to work through key design issues

Treatment of Clean Energy Paper (February 2004)

Transaction and Administration Cost Report (April 2004)

Treasury Board approval of funding for offsets policy development (March 2004)

SCOPE

- **No final decision on the inclusion of any sectors beyond agriculture and forests, as established in the Plan**
- Signals have been sent to LFEs
  - Former PM's letter to CAPP (July 5, 2003)
  - MOU between the federal government and FPAC (November 6, 2003)
- Working assumption LFG in
- Treatment of Clean Energy paper suggests approach to renewable electricity generators
- Demand Side Management - same treatment as renewables?
- Energy efficiency/other sectors?

OFFSET SYSTEM POTENTIAL

Working estimates for 2010

- renewables: 0.5 - 3 Mt/year or 500 -3000 MW (assumes displacement at CCGT)
- forests: > 4 Mt/year
- agriculture: 10 Mt/year
- landfills: 8 -10 Mt/year
- energy efficiency: 0.5 - 2 Mt/year
- other: 1 - 3 Mt/year

Economics – example for wind power

- WPPI: 1.0 cents/KWh for 2004-2006, 0.8 cents/KWh for 2007
- offset value: 0.54 cents/kWh
  (using CCGT emissions intensity standard and carbon price of $15/tonne: 0.00036 t/kWh X $15/tonne = 0.54 cents/kWh)

EVOLUTION IN THINKING ON RENEWABLES

Discussion Paper

- Proposed to exclude generation of renewable electricity from the scope of the offset system
- Position reflected status of climate change policy development

Consultations

- Strong stakeholder objection
- General discontent with treatment of renewables thus far in climate change policy development

Clean Energy Paper

- Suggests a streamlined approach to incorporating small renewables in the offset system
- Large renewables will be dealt with through separate system

DESIGN ISSUES - Contribution

Should emission reductions projects be required to contribute to the national Kyoto target?

- equity issues: LFEs contribute through their targets; sinks projects contribute through BAU sinks (and sinks do not add to national emissions)
- the gap: Offsets used by LFEs for compliance are part of the 55 Mt LFE target. Broader scope for offset system may take potential away from TMs.
- contribution under consideration: 15% for all emission reduction projects. Treatment of renewables undecided.

DESIGN ISSUES - Surplus

Reductions/ removals awarded credits should be incremental to those resulting from other federal climate change measures

- Needed to ensure integrity of Plan accounting – no double counting

Implementation still an issue

- Direct effects of federal measures easier to deal with than indirect
- Implementation may vary somewhat across sectors
- Treatment of provincial/municipal requirements

DESIGN ISSUES - Baselines

Credits are awarded for the difference between "without project" emission baseline and the "with project" measured emissions

- agriculture: standard co-efficients would be used to establish baselines for some project types & project-specific estimates used for other project types
- forests: project-by-project approach would be used to establish baselines for individual project proponents
- renewables (small projects): credits awarded would be based on an emission intensity standard
- landfill gas: streamlined project-by-project approach under consideration

DESIGN ISSUES
Eligibility Date, Crediting Period, Registration

Project Eligibility Date - Jan 1, 2002 (eligible projects generate their initial reductions/removals on or after this date)

Crediting Period - Eligible projects can earn credits beginning Jan 1, 2008; no end date will be specified.

Registration

- Offset projects could be validated and registered as early as 2005/6 (assuming all the infrastructure is in place).
- Projects (including project baselines) reassessed for re-registration January 1, 2013, and every 5 years thereafter; eligibility criteria at the time of re-registration will be used.

DESIGN ISSUES - Non-permanence of Sinks

- Both temporary credits and permanent credits would be available to sinks proponents.
- LFE legislation would allow both temporary credits and permanent credits to be used for compliance.
- Temporary credit
  - represents storage of 1 tonne of CO2e for 1 year
  - LFE would be required to replace temporary credit after one year
- Permanent credit
  - represents permanent storage of 1 tonne of CO2e
  - liability for replacement if the sink is reversed will be shared between project proponent & government.

DESIGN ISSUES - Ownership, Unique

Ownership

- Project proponent is responsible for demonstrating that he/she is the party entitled to receive the offset credits.

Unique

- Reductions/removals can only be credited once under the offset system
- No restriction on eligibility of project for other systems (e.g., same reduction/removal could also earn a credit for use against Alberta requirements)

OTHER DESIGN ISSUES

Governance

- Options for institutional status of Program Authority still under review
- Expected that verification and operation of the offset registry will be contracted out to the private sector

Links with International

- Principles for Canadian Carbon Market established by IETA and federal government (October 23, 2003)
  - permanent domestic offset credits would be exchangeable for international Kyoto units
- JI rules would be at least as stringent as offset rules
  - project proponent could choose to apply for JI or offsets

ADMINISTRATION & TRANSACTION COSTS REPORT

- Examined administration and transaction costs under different potential design scenarios
  - inclusive approach taken to possible design scenarios so as to maximize knowledge base
- Findings suggest that costs reasonable under all system design scenarios
- Total system costs:
  - limited scenario (“project-by-project” baselines, limited scope): 1.54 - 1.74 $/tonne
  - broad scenario (“top-down” baselines, broad scope): 0.38 - 0.44 $/tonne
  - medium scenario (hybrid): 0.46 - 0.60 $/tonne

PROPOSED TIMELINE

- **Status report June 2004**
- **Working towards design proposal for review by Deputy Ministers/Ministers in summer/fall**
  - basis for further provincial/territorial and stakeholder review
- **Seeking Ministerial sign-off on broad system design by end 2004/early 2005**
- **Elaboration of detailed rules (e.g. quantification protocols) 2005-2006**
- **System fully operational 2006**