



# **CONSULTATIONS ON THE DESIGN OF A GREENHOUSE GAS OFFSET SYSTEM FOR CANADA – 2003**

***-- Summary Report --***

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## EXECUTIVE SUMMARY

**Background and Objectives** - The federal government's interdepartmental Working Group on Offsets (WGO) hosted a series of one-day consultation sessions in 6 cities across the country during the period of June 16-26, 2003.

The objectives of the consultation sessions were to:

- Inform provinces/territories and stakeholders on options and process for the development of an offset system;
- Foster exchange and discussion on the feasibility of an offset system, in the first commitment period;
- Obtain initial feedback on design considerations, elements and options; and
- Advise provinces/territories and stakeholders on how they can provide further input on the offset system design.

A total of 295 people participated in the sessions. Of the participants, approximately 75 represented industries that could be considered as potential “buyers” of offset credits; 62 represented industries and other activity-based organizations that could be considered as “sellers” of offset credits (including 13 municipal representatives); and 41 participants represented intermediary interests in the consulting, trading, insurance and finance sectors. The remaining 117 participants represented cross-cutting interests, including 42 provincial representatives, and 74 representatives from academia, environmental and other civil society organizations.

The session agenda included a series of presentations by the WGO (on the process for policy development of the offset system, cross-cutting design issues and options, and sectoral design issues and options) and opportunities for questions and comment using focus questions. Session Reports were prepared for each of the 6 sessions and were posted, in both official languages, on the Government of Canada's Climate Change Website at <http://www.climatechange.gc.ca>.

Provinces/territories and stakeholders were invited to provide written submissions on the Discussion Paper. A total of 76 submissions, from 73 different organizations / individuals, were received by July 31, 2003, in time for inclusion in this Summary Report. Submissions received after July 31, 2003 are also being considered by the Working Group on Offsets.

This Summary Report provides an overall summary of the key messages that were expressed by provinces/territories and stakeholders – herein referred to as participants – both during the sessions and in the written submissions. To the extent possible, this Summary Report, as well as the session-specific reports, have been written to reflect the views as they were expressed by participants and their interpretations of the *Offset System Discussion Paper* (Discussion Paper), or of other government policy proposals. They do not incorporate responses to participant questions by the WGO panel members who were involved in the sessions.

**General Views on the Concept and Process** - The discussions during the consultation sessions, and the written submissions provided to the WGO, were genuinely constructive. Participants were, in general, highly supportive of the concept of a greenhouse gas (GHG) offset system for

Canada. Amongst those expressing support, in principle, for the concept of a greenhouse gas offset system, the following concerns / issues were frequently raised:

- Exclusion of renewable energy and other indirect emission reduction activities;
- Fit with other elements of the *Climate Change Plan for Canada (Plan)*;
- Credit for early action;
- Suitability of proposed baseline estimation methodologies and Business As Usual projections;
- Complexity of proposed system;
- Need to recognize that alternate policy approaches might be effective;
- Need for international and domestic consistency; and
- Need to consider net project benefits.

**Comments on Principles** – Participants offered general support for the Principles as stated in the Discussion Paper. No clear hierarchy of principles was established. The largest number of interventions related to the principle of "open as practical". Most participants argued that the system should be designed to include participation from all sectors and activities outside the large industrial emitter system capable of delivering GHG emission reductions and/or removals. Many took particular note of the exclusion of renewable energy.

**Comments on Eligibility Criteria** - Participants expressed general support for the eligibility criteria as stated in the Discussion Paper. The largest number of interventions related to the proposed surplus criterion. Numerous participants suggested that the surplus criterion should be less restrictive and only exclude 1) those activities and projects initiated in response to regulatory requirements pertaining directly to GHG reductions/removals and 2) that portion of reductions/removals directly funded by the government.

Concerning the proposed crediting period, several participants expressed the view that the proposed five year crediting period (2008-2012) was too short and would limit investment in GHG offset projects. Strong support was voiced for consideration of an offset system that would allow for the use of emission reductions/removals banked from activities undertaken prior to 2008.

The eligibility criterion relating to ownership also came under scrutiny by several participants. Participants supported a range of approaches to ownership including rules-based, contract-based and a combination of the two.

Start date was also a commonly addressed eligibility criterion. The main message was that announcement of the start date of eligible projects was required as soon as possible to provide certainty for investors.

**Comments on Administrative Issues** – Participants expressed differing views on possible administrative structures and roles. Some support was expressed for a third-party and / or arms-length authority. There was also a strong view, however, that administration of the system would require active government involvement. In terms of roles, participants generally expressed the view that the program authority should rely, wherever available, on external expertise with respect to protocol development, reporting and verification.

With respect to issuance of offset credits, participants generally expressed support for an offset system that would allow for and encourage the establishment of an options / futures market to advance revenue to project proponents. Related to this, participants generally expressed the view that the risk of non-delivery should be managed through external, private contractual arrangements.

A number of participants noted that one important role for the Program Authority, or the WGO in the interim, would involve providing clarification on the issue of the legal nature of the offset credit.

**Comments on Design Issues** – Participant views on non-permanence issues were polarized. Some argued that the non-permanent nature of carbon removal activities should make them ineligible for consideration under the proposed offset system, and urged that any risk management approach adopted place a priority on avoiding public liability. Others argued that non-permanence was not a difficult issue to resolve and questioned why the Discussion Paper placed such an emphasis on it. Some participants expressed a general interest in the concept of a temporary crediting regime for risk management of carbon reversals, although others were opposed.

With respect to baselines issues, concern was expressed over the accuracy of the federal government’s Business as Usual (BAU) projections. Participants also expressed concern that the proposals identified for baseline determination methodologies and BAU projections at a project level were confusing and complex. Support was offered for a simpler system, whereby baselines and BAU projections are developed with consideration of regional and sectoral standard practices. However, participants expressed that the integrity of the offset system needs to be ensured. Participants also felt strongly that baselines, once established, should be fixed for the lifetime of the proposed project.

**Forestry Issues** – Participants representing forestry sector interests argued strongly in support of Canada including forest management activities within the national inventory and communicated support for including avoided emissions projects within the proposed offset system. Other participants, however, suggested that avoided emissions might be better managed via targeted measures, rather than through an offset system. A general, but not universal, preference was suggested for the “without project” approach to determining baselines described in the Discussion Paper.

Forestry sector participants were also concerned with the following issues:

- Lack of recognition of emission reduction potential in the sector;
- Baseline and BAU issues;
- Ownership issues – with respect to Crown and Aboriginal title and forest leasers / operators; and.
- Need to ensure net forest benefit and development of project proposals in accordance with Sustainable Forest Management principles and practices.

**Agriculture Issues** - Participants did not express a clear preference for either of the options for determining baselines proposed in the Discussion Paper (independent producer vs. pooling) and argued that both approaches should be available. With respect to the Pooling Approach,

stakeholders felt strongly that membership criteria and administration procedures should be left entirely to the discretion of project proponents and offset purchasers to address. Agriculture sector participants were also concerned with the following issues:

- Lack of recognition of emission reduction potential in the sector;
- No disadvantage for actions taken prior to the first commitment period;
- Baseline and BAU issues;
- Definition of the surplus eligibility criterion; and
- Ownership issues.

**Landfill Gas Issues** - Participants generally expressed a strong preference for accessing landfill gas emissions reduction potential through an offsets system as opposed to through regulation. Many participants expressed strong views against the concept of a required Kyoto contribution from landfill gas sector projects. Participants were also concerned with the following issues:

- Defining surplus criterion;
- Start date; and
- Eligibility of landfill gas use projects.

**Issues for Other Sectors** - Participants took strong exception to the Discussion Paper's proposals for eligibility / ineligibility of renewable energy and other indirect emission reduction projects. More generally, some participants argued that the Discussion Paper did not put enough emphasis on emission reductions in other sectors, compared to the emphasis placed on emission removals in the agriculture and forest sectors.

Participants identified the following design elements that could be implemented to facilitate the inclusion of projects in other sectors:

- Streamlined process for application, review, and verification of small projects;
- Opportunities to aggregate small projects; and
- Clear identification of a surplus criterion as it relates to targeted measures.

**Regional Issues and Variations** - The range and nature of messages heard were relatively consistent across the six consultation sessions. Each session did, however, involve a more detailed discussion and exploration of issues most prevalent to the respective regional economies. These are elaborated in the report.

**Next Steps** - The results of the consultation sessions and the written submissions will inform the development of a GHG offset system for Canada. In addition, analytical work is being undertaken to further develop offset system design. The next public document is expected to be available by early 2004. Further provincial/territorial and stakeholder input will be sought prior to finalization of the recommended offset system design.

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# 1. INTRODUCTION

## 1.1 BACKGROUND

On November 21, 2002, the Government of Canada released the *Climate Change Plan for Canada* (Plan). The Plan sets out a three-step approach for achieving Canada's Kyoto target of reducing annual Greenhouse Gas (GHG) emissions by 240 megatonnes (Mt). First, there are investments to date that will address one third of the total reduction (80 Mt). Second, the Plan defines a strategy for a further 100 Mt reduction. And finally, it outlines a number of current and potential actions that should enable Canada to address the remaining 60 Mt reductions.

Large industrial emitters (LIEs) play a significant role in the Plan's strategy. LIEs include the thermal electricity, oil and gas, and mining and manufacturing sectors, and are expected to produce about half of Canada's total GHG emissions by 2010. The Plan proposes that targets for emissions reductions -- totalling 55 Mt -- be established for LIEs through covenants with a regulatory or financial backstop. To provide LIEs with flexibility in achieving their targets, the Plan proposes access to emissions trading, international permits, and domestic offsets.

Agriculture, forests and landfills are identified in the Plan as having the potential to create offset credits for new activities to reduce emissions and increase sinks. The Plan proposes that agriculture and forestry sink enhancement can generate offset credits for sink increases beyond those from existing practices. The Plan also proposes consultations on whether emissions reductions from new capture and flaring or use of landfill gas should be regulated, or be eligible to generate offset credits.

A federal interdepartmental Working Group on Offsets (WGO), which includes representatives from Environment Canada, Natural Resources Canada, and Agriculture and Agri-Food Canada and the Department of Foreign Affairs and International Trade, was established to lead efforts on the design of a proposed offset system, and to consult with Canadians as appropriate.

In April 2003, the WGO summarized federal thinking to date on the key elements of a domestic offsets system in a *Key Elements Paper*, which was distributed to stakeholders and provinces / territories. This was followed by a more detailed *Offset System Discussion Paper* (Discussion Paper). The Discussion Paper served as the basis for the consultation sessions and was distributed to all invitees in early June 2003; it was also made publicly available on the Government of Canada's Climate Change Website (<http://www.climatechange.gc.ca>). The Discussion Paper addresses matters raised in the Plan with respect to agriculture, forestry and landfill gas potential, and broadens the scope of the proposed offset system to include other emission reduction potential across the economy and not covered by the backstop/covenant system for LIEs.

The federal government is continuing its development of a proposed offset system, taking into consideration the feedback received throughout the offset system consultations, the written submissions received subsequently, and analytical work.

## 1.2 OBJECTIVES OF SESSIONS

The objectives of the consultation sessions were to:

- Inform provinces/territories and stakeholders on options and process for the development of an offset system
- Foster exchange and discussion on the feasibility of an offset system, in the first commitment period
- Obtain initial feedback on design considerations, elements and options
- Advise provinces/territories and stakeholders on how they can provide further input on the offset system design

The sessions were not designed as a forum for negotiating positions, or pursuing consensus views amongst participants. Session participants and others unable to attend the consultation sessions were invited to provide more detailed input via written submissions.

## 1.3 APPROACH TO SESSIONS

One-day sessions were held in 6 cities across the country during the period of June 16-26, 2003. A common agenda was used for all sessions (see Appendix A). The sessions were organized, facilitated and reported by consultants from Marbek Resource Consultants and Stratos Inc., under contract to the WGO.

The sessions were hosted by the WGO, in the form of a panel with participants representing Environment Canada (Climate Change Economics Branch and National Office of Pollution Prevention), Natural Resources Canada (Large Industrial Emitters Group, Domestic Environment Policy Division and Canadian Forest Service) and Agriculture and Agri-Food Canada (Agriculture and Environmental Policy Analysis or Environment Bureau).

The agenda included a series of presentations to plenary by members of the panel based on material detailed in the Discussion Paper. The morning presentations involved an overview of the role of the proposed offset system within the Plan, and on the WGO's role and timelines for further development of the system. Additional presentations were made on cross-cutting topics, providing more detail on system principles, eligibility criteria, administration issues, and design considerations. Sector specific presentations were made in the afternoon and covered design options and issues for the forestry, agricultural, landfill gas, and other sectors.

Following the overview presentation, participants were given the opportunity to raise questions of clarification and make general interventions regarding the desirability of an offset system to assist in meeting the objectives of the Plan, and on the proposed approach for developing such a system.

Following the presentation on crosscutting topics, participants were again given the opportunity to raise questions of clarification and to make interventions on the focus questions related to these topics (see Appendix B) and / or other issues.

Following the presentations on sectoral issues and options, participants were asked to attend one of four sectoral breakout sessions. These breakout groups discussed the relevant focus questions



and other related issues and then reported back to plenary with a summary of the interventions made in relation to the focus questions. Participants were provided an opportunity to raise questions of clarification and / or make further interventions on the breakout groups' presentations.

Throughout the day, panel members participated by responding to requests for clarification, asking and answering questions, and highlighting key considerations.

Participants were encouraged to be open in sharing their views, on the understanding that there would be no attribution in the reports to follow. Participants were also asked to respect the “no attribution” rule in their public discussions of the sessions (e.g., with the media). While not directly invited, media were permitted to attend the sessions, provided that interventions made in plenary were not attributed without prior permission.

Given the time limitations, participants were encouraged to be brief (3-5 minutes) and to avoid formal presentations. Those who wished to provide written views on the focus questions raised in the consultation sessions or the key questions posed in the Discussion Paper (see Appendix C), were invited to do so by e-mail, regular mail, or fax, up to July 31, 2002. Those views have also been reflected in this report.

The individual Session Reports consisted of 7-8 page accounts of what was heard at each session. The reports do not provide a verbatim transcript, nor do they include a record of all views expressed. The Session Reports represent an attempt to capture views that, in the judgment of the rapporteur and the facilitator, were either widely held or were representative of the views of a sub-section of session participants. To the extent possible, the reports attempted to remain faithful to the views as they were expressed, and did not include either editorial influence or the replies of the panel members who attended the sessions.

The individual Session Reports and lists of participating organizations are reproduced in Appendix D.

#### **1.4 REPRESENTATION AT SESSIONS**

For the consultations to be successful, the number of participants needed to be manageable and reasonably balanced between stakeholder groups and provinces/territories. The first step was to develop a list of the categories of participants that needed to be represented, including provincial/territorial and municipal representatives, Non-Government Organizations (NGOs) and private sector. The second step was to categorize these individuals and organizations according to their interests / role in a possible offset system. This included categories of potential offset buyers, sellers and intermediaries, as well as those with more cross-cutting interests. The NGO list included environmental, health, financial, labour, aboriginal, consumer, municipal and academic organizations or representatives, the private sectors included business/industry associations, and energy, transportation, manufacturing, resource processing, agriculture, and forestry representatives, and consultants and intermediaries active in the field of climate change and market-based mechanisms. The invitation list was designed to ensure that, as far as possible, all of these categories were represented in the consultations.

A total of 295 participants attended the sessions. Appendix E provides a summary of attendance, including numbers for those who were invited and - for those who did attend - a breakdown by category.

## **1.5 WRITTEN SUBMISSIONS**

At the consultation sessions, participants were invited to provide written submissions on the Discussion Paper. The Government of Canada Climate Change web site was used as a forum to extend this invitation to a broader audience. A total of 76 submissions, from 73 different organizations / individuals, were received by July 31, 2003, in time for inclusion in this Summary Report. These are listed in Appendix F. Both the interventions made by participants at the sessions and views expressed in the written submissions are represented equally in this Summary Report. Although not represented in this report, policy developers will give consideration to all submissions received after July 31, 2003.

## **1.6 ABOUT THIS REPORT**

This Summary Report is based on the six Session Reports, as well as the written submissions received prior to July 31, 2003. Participants at sessions and authors of written submissions were stakeholders and provinces/territories, but will herein be referred to as participants for simplicity.

The report outlines the key messages heard at the consultation sessions and in the written views submitted, as well as highlights of regional issues and variations in the messages observed in the various jurisdictions. Like the Session Reports, the intention of this report is to succinctly and faithfully capture widely expressed views or representative views. It is important to note that, given the intention to provide a summary of the key messages heard from participants, responses provided by government panel members during the sessions (on questions of clarification and intent) are not included in this report.

## 2. KEY MESSAGES

### 2.1 GENERAL OBSERVATIONS

The discussions during the consultation sessions, and the written submissions provided to the WGO, were genuinely constructive. Stakeholder interventions were tightly focussed on recommendations for ensuring an effective and efficient GHG offset system for Canada.

The range and nature of messages heard were relatively consistent across the six consultation sessions. Each session did, however, involve a more detailed discussion and exploration of issues most prevalent to the respective regional economies. Section 3 below, provides a brief discussion of session-specific variances on the key messages summarized here.

While participants generally expressed their appreciation for the work of the WGO and congratulated the WGO, a small number of participants expressed concern with the tight timeframe involved in the consultations, noting that these timelines did not provide sufficient opportunity to consult fully with their own constituencies on the issues raised within the Discussion Paper.

### 2.2 GENERAL VIEWS ON THE CONCEPT AND PROCESS

Participants were, in general, highly supportive of the concept of a GHG offset system for Canada. This support extended to consideration of agricultural, forestry and landfill gas activities within such a system, as well as for emission reductions resulting from activities in other sectors.

Some stakeholders, in particular a few of those representing NGOs, expressed concern that offsets would, if not properly accounted for, replace real emission reductions and thereby reduce co-benefits, and threaten the integrity of the Plan and the achievement of the Kyoto target. In addition, some of these stakeholders expressed scepticism about the reality of durable GHG sequestration associated with proposed GHG sinks.

The following concerns / issues were frequently raised:

**Exclusion of renewable energy and other indirect emission reduction activities** – The most frequent objection made, through both the written submissions and the consultation sessions, was to the Discussion Paper's proposed exclusion of renewable energy and other indirect emission reduction activities from the offset system. This view was coupled with the position that offset credits provided for renewable energy and other indirect emission reduction projects should be awarded to those who invested in the projects, rather than to those entities that experience an induced reduction in their emissions as a result of those investments.

Session participants expressed the view that existing incentives were insufficient and expressed their desire for the inclusion of renewable energy projects (e.g., wind power, biomass energy, ground source heat, etc.) and demand side management/conservation activities in the offset system. Some interventions also suggested that other non-emitting energy sources should also be eligible, including hydroelectric and nuclear generation facilities.

While acknowledging the challenges (e.g., potential double counting) that inclusion of such activities would raise, the written submissions provided numerous and detailed recommendations for addressing such challenges.

A small number of written interventions, however, noted that renewable electricity and other indirect emission reduction activities were already being counted upon under the targeted measures portion of the Plan. In their view, such activities should only be considered for eligibility under the proposed offset system once the objectives established under the targeted measures have been fully realized.

**Fit with Other Elements of the Federal Climate Change Plan** – A frequent intervention topic concerned participants’ requests for clarification with respect to the overall fit between any greenhouse gas offsets system and other elements of the federal *Climate Change Plan*, including: the large industrial emitters (LIE) covenant/backstop system; existing and planned targeted measures, such as infrastructure funds and *Green Municipal Funds*, and the proposed partnership fund and innovation initiatives.

On numerous occasions during the consultation sessions, and within written submissions, participants called on the Government of Canada to conduct similar consultation exercises on other aspects of the Plan. Participants also frequently suggested that a single process or a set of parallel processes was needed for the design of all key Plan elements, to provide participants with confidence that nothing of importance would “fall through the cracks”.

**Credit for Early Action** – A widely made intervention involved participants’ concerns with respect to credit for early action in the proposed greenhouse gas offset system. While the need for the federal government to design a system capable of meeting Canada’s Kyoto commitment was acknowledged, participants argued that by not sufficiently rewarding action taken prior to the first commitment period, the proposed offset system would send the wrong signals. Participants noted that many projects required investment prior to 2008 to produce emission reductions/removals over the 2008-2012 period, and that these pre-2008 investments needed to be encouraged.

Several participants, in particular those in the forest and agricultural sectors, further noted that the achievement of the Plan’s BAU projections was dependent on ongoing maintenance activities and investments by actors in those sectors. These participants suggested that, in the absence of some suitable compensation for action taken prior to the first commitment period, perverse incentives could lead to existing and planned activities being postponed or not maintained prior to 2008 and/or through the 2008-2012 period, thus jeopardizing the BAU projections.

**Concerns about Business As Usual Projections and Baselines** – Stakeholder interventions also emphasized concerns with respect to several aspects of the Plan’s BAU emissions projections. In the absence of information on specific sector and/or activity-level breakdowns of the BAU projections, several stakeholders raised concerns regarding the credibility of the Plan and, in turn, Discussion Paper’s assumptions. Numerous interventions suggested that a top-down approach to BAU projections would lead to difficulties in terms of defining appropriate project-level baselines and emission reduction/removal projections. In both the consultation sessions and written submissions, detailed recommendations were made for alternate approaches to establishing baselines and BAU projections.

**Need for Environmental Integrity and Simplicity** – There was widespread support for ensuring the environmental integrity of the offset system and the credibility of offsets credits. However, there was varying views on the degree of complexity required achieve such a system.

A large number of interventions raised points of concern with the apparent complexity of the GHG offset system as proposed in the Discussion Paper. These participants called on the federal government to rethink the current approach and develop a simpler approach to determining project eligibility and baselines, reporting and verification requirements, etc. At the same time, these participants called on the federal government to establish the system's operation rules and procedures as soon as possible, to ensure investment is planned and underway prior to 2008. A significant number of interveners further suggested that the federal government should provide for the early phase-in of the offset system, starting in 2005 for instance, to provide actors with the necessary experience in working with the proposed system rules.

Others participants, such as some representing ENGO interests, argued that the system needed to be stringent, in order to ensure its environmental integrity and realization of the country's Kyoto commitment.

**Recognition of Alternate Policy Approaches** – Several interventions and written submissions noted that an offset system might not, in all cases, be the most appropriate means to incent emissions reduction/removal activities. Participants suggested that the application of targeted measures (e.g., regulations, provision of direct incentives, etc.) might be more suitable for some applications. In particular, a minority of stakeholders suggested that issues with respect to non-permanence of agricultural and forestry sequestration activities make these activities less suitable for inclusion in any offset system.

**Attention to Other Environmental Impacts and Co-Benefits** – Some participants expressed the view that the design of the offset system should favour activities capable of providing co-benefits with respect to human and environmental health. Others suggested that, at a minimum, eligibility under the proposed offset system should be contingent on proposed projects being subjected to an environmental screening exercise. Such an exercise would serve to quantify any unintentional negative impacts on the environment that might arise as a result of the proposed activity and assess these against the anticipated GHG reduction benefits.

**Need for Domestic and International Consistency** – A number of participants expressed support for the Discussion Paper's commitment to ensuring that credits obtained through investment in offset activities will be fully exchangeable with compliance units under other domestic (e.g., large industrial emitter covenant/backstop system) and international (i.e., Clean Development Mechanism, International Emissions Trading, Joint Implementation) systems. A number of interventions urged the WGO to go further and make maximum use of rules and procedures already being developed at the international level, a process in which Canada is playing a key role. Some participants raised concerns, however, about how system compatibility would be ensured, especially given the commitment to a per-tonne emission reduction price ceiling under the large industrial emitters covenant/backstop system.

Not all participants were supportive of the concept of compatibility between offsets and international compliance units. These participants felt that the GHG offset system for Canada

should include mechanisms that would clearly favour investment in Canada, rather than in foreign jurisdictions.

In addition to supporting the concept on international compatibility, a number of participants called on the WGO to work cooperatively with the provinces to ensure the development of compatible and integrated provincial and federal offset systems, with a preference expressed for a single national system. Harmonization between federal and provincial initiatives was stressed.

**Need for Certainty** – Another commonly made intervention stressed the need for investor certainty. It was expressed that certainty regarding at least some key elements of offset system design were required to encourage investment. Many participants noted that, in order for projects to produce reductions/removals during the 2008-12 period, investments had to be made now as investors were not apt to commit financing without some degree of certainty, and might direct their investment elsewhere, including in other countries.

## 2.3 VIEWS ON CROSS-CUTTING TOPICS

### 2.3.1 Principles

Participants in the consultation sessions and those that made written submissions offered general support for the principles as stated in the Discussion Paper. No clear hierarchy of principles was established.

A few interveners suggested that rather than principles, the statements made in the Discussion Paper appeared to be objectives. These participants called on the WGO to reflect on the key principles underlying the *Climate Change Plan for Canada* (e.g., regional and sectoral equity), and incorporate these into the design of the offset system.

Some stakeholders provided verbal and written suggestions for additional overarching principles for the governance of the offset system for Canada, including:

- A commitment to transparency and public involvement;
- Ownership determined on the basis of investment;
- A commitment to allowing risk to be negotiated through contractual arrangements; and
- A commitment to avoiding public liability for non-delivery or non-permanence of offsets.

**Open as Practical** – With respect to the principles documented in the Discussion Paper, the largest number of interventions related to the issue of openness. These participants took particular note of the exclusion of renewable energy and other indirect emission reduction projects and argued that the system should be designed to broaden participation to these sectors, as well as to any and all other sectors and activities capable of delivering GHG emission reductions/removals. Several participants suggested that the openness principle would contribute to satisfaction of other principles related to: encouraging investment in Canada, providing appropriate signals, and enhancing market liquidity.

Other participants raised objection to the openness principle, expressing concerns over potential double counting of indirect emission reduction activities. These participants suggested that the openness principle should be replaced by a commitment to “environmental integrity”, assuring that activities eligible under the proposed offset system would not jeopardize targets established for other aspects of the federal Plan.

**Enhancing Market Liquidity and Providing Appropriate Economic Signals** – During the consultation sessions, and within the written submissions, participants acknowledged the tension between the need for clear and effective rules and the desire for a workable system. The question of where to place emphasis, between these ends of the spectrum, was a point of debate amongst participants. Some participants, in particular those having clear interests as potential offset suppliers and/ or buyers, expressed strong preference for a system that was as simple as possible, capable of providing incentives for investment, leading to early investment and a high level of market liquidity. These participants sometimes noted that it was important to encourage action, and not focus on whether or not that action is part of the BAU forecast. Other participants, including ENGOs, placed a strong emphasis on careful design of the rules to encourage real emission reductions/removals and the avoidance of perverse incentives. Some also insisted on the establishment of clear and formal rules and opportunities for public involvement capable of contributing to a transparent system with a high degree of environmental integrity.

**Contribution to Achieving Canada’s Kyoto Commitment** – Opposing views were also noted on the principle of contributing to achieving Canada’s Kyoto target, either through BAU sinks or beyond BAU reductions. Some participants, often sellers, indicated their strong opposition to the concept of a Kyoto contribution within the offset system. These participants interpreted the proposed contribution as being equivalent to a tax that would increase transaction costs and would work to limit participation and market liquidity. Others, in particular those representing NGOs, strongly supported the concept, especially within their written submissions. These participants argued that it is necessary for all sectors to do their part in achieving the Kyoto target.

On a related issue, differing views were expressed on the appropriate time frame for the achievement of Canada’s climate change objectives. Some argued that the goal of the offset system should be to initiate widespread activity towards longer-term goals, rather than focusing on the Kyoto commitment of 2008-2012. Others stated their clear preference for a system that would ensure, in the first instance, that Canada’s Kyoto commitment in that period is satisfied, but also that a continued contribution past 2012 was justified.

**Incentive for Investment in Canada** – In general, participants expressed strong support for the principle relating to domestic investment. Some participants argued that the system needed to be intentionally designed to favour investment in domestic offsets over investment abroad.

### 2.3.2 Eligibility Criteria

Participants in the consultation sessions and those that made written submissions expressed general support for the eligibility criteria as stated in the Discussion Paper.

Overall, participants also stressed the importance of establishing clarity on the GHG offset system eligibility criteria as soon as possible, to facilitate decision making by potential project investors.

**Surplus** – The greatest number of interventions related to the proposed surplus criterion. Numerous participants suggested that the surplus criterion should not be too restrictive. These participants argued, for instance, that actions as part of voluntary initiatives should be eligible for offset creation. Likewise, the view was expressed that only actions taken as a result of specific regulation intending to address GHG emissions should be considered ineligible.

Many participants also expressed disagreement with the proposition in the Discussion Paper that reductions or removals resulting from targeted measures, or any other government climate change initiative, not be eligible for offset creation. A number of participants raised questions concerning the fairness and legality of this exclusion. For instance, a number of participants noted that participation in several of the targeted measures was undertaken on a voluntary basis.

These participants were also concerned that reductions/removals achieved with the help of even minor government contributions, whether through targeted measures, or even non-climate change related agricultural initiatives, could be excluded. In their written submissions, several participants suggested that only the percentage share of emission reductions/removals equivalent to the government's percentage share of investment should be excluded.

Relating to both the surplus and unique criteria, some participants called upon the WGO to cooperate with provinces that are in the process of developing their own climate change plans, so that the question of surplus / uniqueness does not become a “double jeopardy” issue for those required to make emission reductions under multiple systems.

Finally, and as noted earlier, participants expressed widespread concern about the proposed ineligibility of renewable energy projects and other projects capable of achieving indirect emission reductions. Written submissions provide the WGO with more detailed analysis concerning potential treatment of indirect emission reductions.

**Start Date and Crediting Period** –With respect to project start date, the majority of participants expressed a desire for a common start date across all project / activity types. A small number of participants suggested that a tiered approach, both between and within projects / sectors would be more appropriate. With respect to specific dates, stakeholders offering suggestions such as:

- Whichever date an offset system for Canada is formally launched;
- December 2002, reflecting Canada's ratification of the Kyoto Protocol;
- January 1, 2000, as per the Clean Development Mechanism;
- January 1, 1990, as consistent with the Kyoto Protocol;
- A date consistent with the start date proposed for the large industrial emitters covenant/backstop system.



Several participants expressed the view that the proposed five year crediting period (2008-2012) was too short and would limit investment in GHG offset projects. Strong support was voiced for consideration of an offset system that would award credits for emission reductions achieved prior to 2008. Support was also expressed for an extended post-2012 crediting period, given that some projects – such as forest ones - will require a much longer economic life to recover investments. Recognizing the level of uncertainty after the first commitment period and the limitations arising from the need to integrate the offset system with the covenant/backstop system, however, no clear proposals emerged on how to extend the crediting period beyond 2012.

In considering earlier GHG pilot initiatives, such as PERT, GERT and PERRL a number of interveners suggested that these should be given special consideration under the proposed offset system, especially if more restrictive start date and crediting period criteria are established. A small number of interveners argued that the pilot initiatives should not be given special consideration and should be subject to the same rules and eligibility criteria as all other projects.

**Ownership** –Some participants supported a rules-based approach, where ownership of reductions/removals would be specified in the offset system rules. One frequent example given was that the offset system rules should state that ownership would belong to the investor. Other stakeholders supported a contract-based approach, where those involved in the offset project would draw up contracts specifying ownership. Others still saw merit to a mixed approach, where general rules to ownership would be specified in the offset system rules, but project-specific details would be worked out through private contracts. Another view on the mixed approach was that ownership should be determined based on private contracts, but that the rules of the offset system should require project proponents to provide signed waivers from any parties that could be anticipated as having a potential ownership claim.

The varied views were often linked to project type. For example, participants considering indirect emission reductions projects favoured a rules-based approach stipulating that those investing in the project, rather than those experiencing the induced reduction in emissions, receive ownership of the offsets. Also, participants representing the agricultural community suggested that ownership should be directly tied to land ownership.

### 2.3.3 Administration

**Program Authority** – Participants expressed differing views on possible administrative structures and roles. Some support was expressed for a third-party and / or arms-length authority; however there was also a strong view that administration of the system would require active government involvement. In terms of roles, participants generally expressed the view that the program authority should rely on external expertise and systems as much as possible, and focus instead on establishing the broad rules and the framework under which the system will operate.

Participants identified the wide-range of experienced service providers, such as in the insurance and accounting fields, which are already accredited to conduct verification and

assurance activities under other government-regulated systems. The general view was that these service providers should be accredited to conduct similar verification and assurance activities under the proposed offset system. A few participants did question, however, whether a system based on external verification, by service providers engaged by project proponents themselves, would allow for sufficient levels of transparency and public participation. These participants generally argued that appropriate levels of public participation and transparency could only be guaranteed via verification through the Program Authority itself. Related to this, concerns regarding the manner by which the system will handle confidential business information emerged from both ends of the spectrum.

Some interveners also called on the WGO to rely on existing systems and service providers in other areas as well. For instance, a number of participants indicated support for reporting offset-related activities through an updated Voluntary Challenge and Registry (VCR) rather than through a new instrument. This view was not universally supported, however.

In considering the balance of administrative aspects, participants expressed their general support for an overarching system that is:

- As simple as possible – with low transaction costs;
- Internationally integrated - with those administrative systems and procedures under development for the Kyoto mechanisms; and
- Domestically harmonized - with offset/emissions trading systems under consideration at the provincial level.

Finally, some participants noted that one of the most important roles for the Program Authority, or the WGO in the interim, would involve providing clarification on the issue of the legal nature of the offset credit. Participants noted that this will be important in determining the rules by which the credit can be traded, including on what exchange and the degree of government involvement that will be appropriate.

**Early Issuance of Credits** – Participants generally expressed support for an offset system that would allow for / encourage the establishment of an options / futures market to advance revenue to project proponents. A few participants, in particular those representing forest sector interests noted the exceptionally long timeframes associated with project activities in that sector and noted their preference for a formal mechanism that would allow for early issuance of credits anticipated to accrue through 2012 and beyond.

**Risk of Non-Delivery** – Participants generally expressed the view that the risk of non-delivery should be managed through external, private contractual arrangements and offered, in their written submissions, a number of suggestions on how such arrangements could be constructed. For these participants, the role for the Program Authority would involve establishing requirements for each project to describe how the risk of non-delivery is being managed under that project.

### 2.3.4 Design Issues

Participants' comments with respect to design issues focused mainly on management of non-permanence with respect to carbon removal activities, and on project and sectoral baselines. Only limited input was provided with respect to issues concerning project leakage.

**Non-Permanence** – Participant views on the approach to non-permanence were polarized. Some ENGOs argued that the non-permanent nature of carbon removal activities should make them ineligible for consideration under the proposed offset system. At the other end of the spectrum, some participants representing forest and agricultural sector interests argued that non-permanence was not a difficult issue to resolve, and questioned why the Discussion Paper placed such an emphasis on it. Between these perspectives, other participants expressed support in principle for including carbon removal projects under the offset system, but cautioned that a liquid market in removal offsets would not emerge unless risk management systems for addressing non-permanence could be designed and implemented while keeping transaction costs low.

In terms of managing non-permanence, participants expressed general support for a system that would require project proponents to develop comprehensive risk management plans and demonstrate sufficient, third-party insurance coverage to manage risks of reversals. The possible role of commodity associations, exchanges, and other pools in the management of risk was also noted.

However, a small number of forestry and agricultural participants argued that, even if third-party insurance coverage were available, it might not cover all categories of risk and the government would need to be prepared to backstop / underwrite the system in the event of major catastrophic events such as forest fires and pest infestations.

Other participants, in particular environmental civil society associations, expressed a cautious view of the role of private contracts in managing risk and argued that the potential for off-loading liability to the public should be avoided at all costs.

Several participants expressed a general interest in the concept of a temporary crediting regime for risk management of carbon reversals. Participants representing forest sector interests, however, expressed polar views on the concept. While some expressed strong support, others suggested it had no place in a greenhouse gas offset system for Canada.

Within their written submissions, a small number of forest sector interests provided detailed feedback on other, more specific questions concerning non-permanence issues that were documented in the Discussion Paper.

**Baselines** – With respect to the overall estimates, participants sought clarification about what activities and emission levels were included in BAU projections in various sectors. Concern was expressed over the accuracy of the federal government's BAU projections.

At a project level, participants also expressed concern that the proposals identified for baseline determination and BAU projections were confusing and complex. Strong

support was offered for a simpler system, whereby baselines and BAU projections would be developed with consideration of regional and sectoral standard practices. Participants were also concerned with the option put forward in the Discussion Paper to recalculate baselines prior to the end of the first commitment period. Some participants felt strongly that baselines, once established, should be fixed for the lifetime of the proposed project. Interventions were also made suggesting that the offset system rules for baseline determination and BAU projections be made consistent with those being developed at the international level for the Kyoto Mechanisms.

The agricultural sector expressed concern that baselines based on BAU may result in a perverse incentive in the agricultural sector not to maintain a carbon removal practice – i.e., farmers may be incented to undertake reversals in order to ensure the ability to create offsets during the 2008-12 period.

## 2.4 VIEWS ON SECTORAL ISSUES

### 2.4.1 Forestry Sector

**Approach to Baselines** – During the consultation sessions, participants discussed the pros and cons of each approach to baseline determination proposed in the Discussion Paper (“without project” vs. “base period”). A general, but not universal, preference was suggested for the “without project” approach due to its overall flexibility. There was also a general preference for the “without project” approach where views were provided in the written submissions. Written submissions from forest sector interests also provided detailed views on the full range of questions posed in the Discussion Paper.

**Forest Management Activities and Avoided Emission Projects** – Participants representing forestry sector interests argued strongly in support of Canada including forest management activities within the national inventory and communicated support for including avoided emissions projects within the proposed offset system. Views differed, however, on the specific types of projects that should be considered eligible / ineligible. While some participants argued against inclusion of projects such as pest management, fire management, others argued that modeling and management tools were advanced enough for projects of this nature to be included. Other participants, however, suggested that avoided emissions might be better managed via targeted measures, rather than offsets.

**Lack of Recognition of Emission Reduction Potential** – Numerous participants commented on the Discussion Paper’s emphasis on emission removal activities in the sector, at the expense of emission reduction activities. These participants argued that emission reduction activities in the sector, such as use and promotion of forest-based bio-fuels, had the potential to make significant contributions and needed to be better explored.

**Baseline and BAU Issues** – Sectoral participants requested clarification with respect to the federal government’s BAU projections. In general, participants expressed concern that these top-down estimates would not be useful in developing project level baselines and projections.

**Ownership Issues** – Participants identified that the sector’s unique arrangements involving forest owners (i.e., Crown lands) and forest leasers / operators raised particular issues with respect to ownership of offsets. A number of participants also noted that the Discussion Paper was silent on the issue of potential Aboriginal Title issues.

**Ensuring Net Forest Benefit** – A number of participants commented on the need to ensure that forest sector projects are assessed based on their net impacts on the forest as a whole, and not solely on their basis to contribute carbon removals/reductions. In particular, it was suggested that forest sector offset projects must be undertaken in accordance with generally agreed Sustainable Forest Management principles and practices.

#### 2.4.2 Agriculture Sector

**Approach to Project Development** – With regard to the Discussion Paper’s two proposed options for project development, participants did not express a clear preference for either (independent producer vs. pooling) and argued that both approaches should be available. Participants generally felt that membership criteria and administration procedures for any project pools should be left to the discretion of project proponents and offset purchasers.

**Lack of Recognition of Emission Reduction Potential** – Numerous participants commented on the Discussion Paper’s emphasis on emission removal activities in the sector, at the expense of emission reduction activities. These participants argued that emission reduction activities in the sector, such as manure management and promotion of bio-fuels, had the potential to make significant contributions and needed to be better explored.

**No Disadvantage for Actions Taken Prior to the First Commitment Period** – Sectoral participants expressed frustration that best management practices adopted by early movers have been subsumed within the governments BAU projections. These participants identified the risk associated with these projections, arguing that they are dependent on the conduct of ongoing maintenance activities by sectoral interests. It was argued that, in the absence of sufficient compensation for actions taken prior to the first commitment period, the offset system would provide a perverse incentive for early movers to suspend maintenance activities, until at least 2008. Participants in the Regina session, along with a number of those that provided written submissions, offered recommendations on how the WGO could address this issue within the system design.

**Business As Usual** – Participants were concerned that the federal government's estimate of a BAU soil sink of 10 Mt in the *Climate Change Plan for Canada* has resulted in the government taking ownership of credits that, in their opinion, belong to the landowners undertaking the sequestering practice. In Regina, there were strong concerns expressed because a major portion of the BAU sink is in that province and therefore Regina participants felt they were being unfairly penalized. Some participants suggested that the government reconsider the BAU component of the Plan.

**Baseline and Start Date** -- Many participants encouraged an early start date (i.e., 1990) as well as baseline establishment tied to that start date such that early adopters of conservation practices would not be disadvantaged and would be eligible to benefit from participation in an offsets system. Also, participants noted that this approach would avoid a perverse incentive that would cause a delay in adoption of beneficial practices until 2008.

**Surplus Criterion** – Participants were also concerned with the proposed surplus criterion and how it would affect agricultural sector actors involved in programs such as *Green Cover*.

**Ownership Issues** – Whereas participants in other sectors argued that project investors should own the resulting offset credits, interests representing the agricultural sector identified the need to ensure landowners retain ownership of offsets in their sector.

**Risk Management** - Generally, participants felt that risk and liability need to be minimized, and managed in a cost-effective manner. Agricultural sector participants expressed a strong interest in receiving more information on temporary offset credit approaches to this issue.

### 2.4.3 Landfill Gas

**Offsets vs. Regulation** – Many participants expressed a strong preference for managing landfill gas emissions through an offsets system, identifying a number of the limitations of regulatory approaches. Other stakeholders, including some ENGOs, called on the WGO to make its decision on the basis of formal analysis of the two options.

**Contribution to Kyoto Target** – There was broad opposition from potential landfill gas operators to the proposition in the Discussion Paper of a required Kyoto contribution from landfill gas sector projects. The proposed contribution was seen as a tax that would work against the desire for liquidity and lowest-cost approaches for large industrial emitters. A few participants suggested that such a contribution, if required, should be invoked on a transparent and equal basis across projects in all sectors. Some other participants offered support for a contribution, as well as suggesting that landfill gas projects should not be eligible under the offsets system until the emission reductions identified for landfill gas within the *Climate Change Plan for Canada* had been achieved.

**Defining Surplus** – Some participants expressed concern that the proposed surplus criterion would lead to projects funded, in part, through initiatives such as the Federation of Canadian Municipalities Green Municipal Funds, the federal Infrastructure Program, or the pilot PERRL being considered ineligible under the offsets system. Participants recommended that rather than such broad exclusions only the share of emission reductions equivalent to the share of federal investments in such projects should be ineligible.

**System Start Date** – Participants noted that landfill gas capture activities in Canada had been initiated as early as 1992, in anticipation of a value being attached to the emission reductions. Generally, participants offered support for a start date of January 1, 2000

(Clean Development Mechanism start date) in cases where municipalities or other parties made investments in landfill gas capture.

**Eligibility of Landfill Gas Use Projects** – Participants expressed concern that the principles and eligibility criteria within the Discussion Paper would lead to only emission reductions from landfill capture and destruction being eligible for offsets, while any indirect emission reductions associated with practical application of landfill gas, such as for renewable energy electricity generation, would be ineligible.

#### 2.4.4 Other Sectors

**Eligibility** – As noted earlier, many participants took strong exception to the Discussion Paper’s proposals for the ineligibility of renewable energy and other indirect emission reduction projects. More generally, participants argued that the Discussion Paper placed too strong an emphasis on emission removals in the agriculture and forest sectors, at the expense of emission reductions in these and other sectors.

**Project Types with Greatest Potential** – Participants suggested a variety of project types that could make a substantial contribution within the proposed offset system. A large number of such activities were identified during the consultation sessions and within the written submissions, such as commercial transport sectors of road, rail and sea.

In some cases, the written submissions provided detailed estimates attempting to quantify the magnitude of emissions reductions that could result from projects in certain sectors.

Participants identified the following design elements that could be implemented to facilitate the inclusion of projects in other sectors:

- Streamlined process for application, review, and verification of small projects;
- Opportunities to aggregate small projects; and
- Clear identification of the surplus criterion as it relates to targeted measures.

### 3. REGIONAL ISSUES AND VARIATIONS

Although a number of fairly consistent key messages emerged from the sessions (as captured in the previous section), the individual sessions reflected some differences in circumstances (e.g., energy sources, industry base, socio-cultural environment) that were reflected in the discussion. Some of the variations are described below.

#### 3.1 TORONTO SESSION

- **Concerns about exclusion of renewable energy projects.** Several participants were concerned over the proposed exclusion of renewable energy and other indirect emission reduction projects from the proposed offset system. Although this was a message heard at all sessions, it was expressed most frequently and most strongly in Toronto and Calgary (see below).
- **Desire for real emission reductions.** The Toronto session included several interventions requesting that the WGO work to ensure the overall integrity of the proposed offset system, by developing rigorous rules to avoid double counting and to ensure that Canada's Kyoto commitment is satisfied. A number of participants also indicated support for an offset system capable of ensuring co-benefits, especially with respect to clean air in the region.

#### 3.2 MONTREAL SESSION

- **Concerns about credibility of projected BAU, Action Plan 2000, and incremental reductions and removals.** Several participants expressed scepticism concerning the modelling used to arrive at total amounts of tonnes of GHGs. In particular, there was concern about the accounting of the potential for new reductions/removals vs. reductions/removals included in the BAU projection and those associated with Action Plan 2000.
- **Concerns about exclusion of hydro-electricity.** As in other cities, several participants objected to the exclusion of renewable electricity generation. In Montreal, there was particular concern about the treatment of large hydro-electricity investments.

#### 3.3 HALIFAX SESSION

- **Concerns over scope and scale of proposed system.** Participants in the Halifax session were especially concerned that the offset system proposed in the Discussion Paper placed a general emphasis on the rules needed to manage a system comprised mainly of large projects, as well as on projects emanating from the forest and agriculture sectors. Participants called on the WGO to be mindful of the need to ensure that the system can support participation from a multitude of small projects, and to ensure that future work provides a more comprehensive discussion of how projects in other sectors will be treated. Some participants suggested that the offset system could be a useful alternative to targeted measures in promoting emission reductions in various sectors.



### 3.4 CALGARY SESSION

- **Concerns about exclusion of renewable energy projects.** Several participants from a range of sectors, including utilities and oil and gas, were concerned over the proposed exclusion of renewable energy and other indirect emission reduction projects from the proposed offset system.
- **Concerns over proper government role.** The Calgary session involved a great deal of discussion concerning the proper role for the government in a GHG offset system for Canada. Participants generally favoured a minimum role for government - focused on rule setting - and maximum use of existing service providers in areas relating to protocol development, registration, verification, insurance, etc.
- **Concerns regarding eligibility of municipal initiatives** - Municipal interests weighed in more heavily in the Calgary session than elsewhere. Municipal participants were especially concerned over the possible exclusion of activities they have been heavily involved in during the past number of years, including: renewable energy, electricity demand side management, waste management, and transportation demand management. Concern was also raised with respect to the potential exclusion of any projects, which may have been supported through the Federation of Canadian Municipalities' Green Municipal Funds.

### 3.5 VANCOUVER SESSION

- **Interest in other sector activities.** Vancouver participants identified a number of regionally important economic sectors having potential to deliver emission reduction offsets, including the commercial transport sectors of road, rail and sea. Several participants were concerned over the proposed exclusion of renewable energy and other indirect emission reduction projects from the proposed offset system.
- **Concerns over environmental aspects.** As in Toronto, the Vancouver session included several interventions requesting that the WGO work to ensure the overall integrity of the proposed offset system, by developing rigorous rules to avoid double counting and to ensure that Canada's Kyoto commitment is satisfied.
- **Broader interpretation of forest sector potential.** A number of Vancouver participants expressed concern that the forest sector portion of the Discussion Paper focussed on carbon removal activities. These participants noted the significant potential for emission reduction activities in the sector as well, especially in relation to the use of forest biomass as a fuel.

### 3.6 REGINA SESSION

- **Strong criticism of agricultural BAU projections.** Industry participants in Regina were particularly critical of the federal governments BAU projections concerning the agricultural sector. A number of participants noted that these projections were dependent on the conduct of ongoing maintenance activities, with respect to agricultural soils, by sectoral interests. These participants argued that such activities might be suspended and

the projections themselves put at risk should the offset system not include appropriate treatment of actions taken prior to the first commitment period for early adopters of sectoral best management practices.

- **Broader interpretation of agricultural sector potential.** A number of Regina participants expressed concern that the agriculture sector portion of the Discussion Paper focussed on carbon removal activities. These participants noted the significant potential for emission reduction activities in the sector as well, especially in relation to manure management and the use of agricultural biomass as a fuel.

#### **4. NEXT STEPS**

The results of the consultation sessions and the written submissions will inform the development of a GHG offset system for Canada. In addition, analytical work is being undertaken to further develop offset system design. The next public document is expected to be available by early 2004. Further provincial/territorial and stakeholder input will be sought prior to finalization of the recommended offset system design.

## APPENDIX A SCHEDULE OF CONSULTATION SESSIONS AND SAMPLE AGENDA

1. **Toronto**, Ontario – June 16, 2003
2. **Montreal**, Quebec – June 17, 2003
3. **Halifax**, Nova Scotia – June 18, 2003
4. **Calgary**, Alberta – June 23, 2003
5. **Vancouver**, British Columbia – June 24, 2003
6. **Regina**, Saskatchewan – June 26, 2003

### AGENDA

8:30	Opening Remarks (Plenary)
8:45	Overview Presentation on Discussion Paper and Initial Discussion (Plenary)
10:00	Break
10:15	Series of Presentations and Discussion on Crosscutting Topics (Plenary) <ul style="list-style-type: none"> <li>• Principles</li> <li>• Eligibility Criteria</li> <li>• Administration</li> <li>• Design considerations</li> </ul>
12:15	Lunch
1:15	Facilitator’s Summary of Morning Session (Plenary)
1:30	Presentations on Sectoral Issues (Plenary) <ul style="list-style-type: none"> <li>• Forestry</li> <li>• Agriculture</li> <li>• Landfill gas</li> <li>• Other sectors</li> </ul>
2:15	Breakout Groups by Sectoral Interest (Breakout rooms)
3:30	Break
3:45	Report by Breakout Groups and Final Discussion (Plenary)
4:45	Next Steps (Plenary)
5:00	End of Session

## **APPENDIX B CONSULTATION SESSION FOCUS QUESTIONS**

### **Focus Questions on Principles:**

- Are some principles more important than others?
- How should we make trade-offs if necessary?

### **Focus Questions on Eligibility Criteria:**

- What issues do these eligibility criteria raise and how can they be managed?

### **Focus Questions on Administration Issues:**

- What is the appropriate structure and role for the Program Authority/Authorities?
- Should offset credits be issued early?
- How should the risk of non-delivery be addressed?

### **Focus Questions on Design Considerations:**

- How should the project boundary be defined? When should leakage be addressed in the quantification of offsets?
- Which approach(es) to addressing non-permanence do you prefer and why?

### **Focus Questions on Forestry Options:**

- Which approach do you prefer for baselines and why?
- Should avoided emission projects (e.g., deforestation projects) be eligible?

### **Focus Questions on Agriculture Options:**

- Which approach do you prefer and why?
- Under the independent projects approach, how should changes in carbon stocks be determined?
- Under the pooling approach, what membership criteria should a pool have?

### **Focus Questions on Landfill Gas Options:**

- Which option do you prefer and why?
- Based on your preference, what do you think are the most important design factors for implementation?
- What should be the basis for determining the contribution?

### **Focus Questions on Options for Other Sectors:**

- Are the above proposals for eligibility/ineligibility reasonable?
- What project types (outside of landfill and forest/agriculture) have the most potential?
- What design elements could be implemented to facilitate the inclusion of new project types and/or small projects in the offset system?

## **APPENDIX C DISCUSSION PAPER FOCUS QUESTIONS**

### **Eligibility Criteria**

- What should be the start date for eligible offset projects? Should the same date be used for all project types? How should the start date of a project be defined?
- How should the projects that were reviewed in the PERT, GERT and PERRL pilots be treated?
- What is the preferred approach to ensuring clear ownership of emission reductions/removals?
- What project types do you think would be suitable as offset projects? What is the annual emission reduction/removal potential for such projects in Canada? Could other approaches achieve these reductions at lower cost?

### **Offset System Governance**

- What is the appropriate structure and composition of the Program Authority?

### **Review Process**

- Should government support be provided for the preparation of a quantification protocol for a new project type? If so, what type and level of support would be appropriate?
- Who should be responsible for verification - the Program Authority or accredited verification entities?
- Should offset credits be issued early? How should the risk of non-delivery be addressed?

### **Boundaries and Leakage**

- What is the appropriate definition of a project boundary and what sources of leakage should be identified and monitored?
- What is the most efficient and workable method for accounting for leakage in the quantification protocol?

### **Addressing Non-Permanence of Removals Projects**

- How should reversals prior to an offset credit issuance be addressed?
- Who should have liability for carbon sink reversals for which offset credits have been issued?
- How long must carbon remain sequestered to be considered equivalent to an emission reduction?
- Would a strict requirement for a risk management plan be an appropriate way to address non-permanence?
- If a tonne-year equivalence approach is used, how many tonne-years should be considered equivalent to a permanent reduction?
- If the insurance approach were to be used, how long should the insurance period be?
- What would constitute adequate insurance coverage, and would such coverage be offered commercially at a price that would enable sink projects to be viable?

- If temporary credits are used, should the validity period be fixed or variable, how long should it be, and should it be set to coincide with the commitment periods?
- Which approach(es) to addressing non-permanence should be accepted by the offsets system? If more than one approach is allowed by the rules, should the choice be left to the project proponents or be specified by the rules based on the project type?

### **Forests**

- Do avoided emission forest projects raise special or particularly difficult issues, for example with respect to baselines and leakage? Are there reasons to not include these projects in an offset system?
- How much potential is there for new forest sinks projects? What considerations in offset system design would help overcome the fact that much of the benefit of some forest projects may not occur for a long time?
- Do you agree that Option 1 - "Without Project" Baseline - is the preferred option for forest projects?
- What methodologies do you think are most appropriate for forest projects, and would be most used under the "without project" baseline approach? Why?
- How should changes in regulations be reflected in project baselines under this option, if at all?
- Would you prefer Option 2 - Base Period Baseline? If so, what do you think is an appropriate base period for which carbon stock change data are likely to be available?

### **Agriculture**

- How should changes in carbon stocks be determined for individual projects? If measurement is required what techniques should be used? What are the conditions (e.g., minimum area) under which statistical estimates are appropriate?
- How should the baseline account for the BAU increase in the net carbon stock?
- How should boundaries be specified for individual agricultural offset projects?
- Under the pooling approach, what form of public or private administration of the pool would work best?
- Under the pooling approach, what membership criteria should a pool have?
- Which approach for participation in the offset system do you think is preferable, and why? Should both approaches be available?

### **Landfill Gas**

- What do you think of the concepts of Option 1 and Option 2? What is your preference and why?
- Based on your preference, what do you think are the most important factors for implementation?
- What contribution - expressed as a percent of eligible reductions at a site – do you think would be reasonable?

**APPENDIX D**  
**SESSION REPORTS AND ATTENDANCE**



# **CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA**

**– SESSION REPORT –**

**Airport Marriott Hotel  
Toronto, Ontario  
June 16, 2003**

## **1. INTRODUCTION**

The first consultation session was held in Toronto on June 16, 2003. There were approximately 75 participants, including a range of industry sectors, business associations, ENGOs, individuals and service companies. Representatives from federal and provincial governments were also in attendance. The list of participating organizations is attached.

This report is a summary of views expressed at the Toronto consultation. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## **2. GENERAL VIEWS ON THE CONCEPT AND PROCESS**

There was general support for the concept of the offsets program, and support for including projects in sectors other than agriculture, forestry, and landfill gas.

Overall, there was recognition that offsets afford a link between emitters in the inventory who do not have emission reduction obligations and those that do. This inclusion is expected to harness creativity, allow a broad base of emission reductions to be accessed and therefore reduce overall compliance costs. Some opposition to the concept of the offset system was raised. Opposition centred on the view that the offset system enables large industrial emitters (LIEs) to avoid action at their own facilities and that the clean air co-benefits of emission reductions would be lost.

Although the open nature of the offset process was applauded, concerns were raised over the exclusion of certain sectors, and renewable energy (as a source of electricity) in particular. It was felt addressing renewable power under the backstop-covenant system placed too much market power with the LIEs, and significantly disadvantaged viable alternatives such as wind power and land fill gas (LFG) utilization.

Some participants questioned the commitment of the Government of Canada (GoC) to the concept of offsets. Specifically, if the offset system proved costly and cumbersome to administer and participate in, would an alternative be brought forward? Clarity on this point was sought and concern was raised that offsets may not be implemented.

With respect to the process, two themes emerged:

- **Integration with the Federal Plan.** There was a widespread view that it is difficult to comment on the offsets system as proposed without knowing more detail on the components of the overall climate change plan. There was widespread uncertainty on how the offset system would integrate with the other components of the federal plan and how offsets would complement the other actions, including interactions with targeted measures. Several participants enquired about plans for broader consultations on the LIE backstop/covenant system and the overall approach to targeted measures. Specifically, it was argued that focused, bilateral consultations or negotiations provided insufficient transparency and were unfair to the interests not represented.
- **Speed of Implementation.** Many participants argued that the offset system should recognize projects as soon as possible and that the rules and protocols should be published very soon so that investment decisions can be made with certainty. A number of participants felt that an acceptable trade-off would be speedy implementation with some design faults rather than a slower more methodical implementation. For example, it was argued that the offset system should not wait for a clarified BAU baseline and start developing protocols prior to 2004.

### 3. VIEWS ON CROSS-CUTTING TOPICS

#### 3.1 Principles

Several participants expressed support for the principles, however some suggested that higher order governance principles, such as sustainability, polluter pays, transparency, equity/fairness, harmonization, etc. were required. There was a suggestion that the proposed principles were in fact not principles, but objectives.

Several participants suggested that market liquidity should be viewed as the overriding principle to observe (implying that transaction costs needed to be kept to a minimum) whereas others viewed contribution to Canada's Kyoto commitment as the most important. Many suggested that the principles needed to be more specific in wording.

The exclusion of renewables was argued to be contrary to a number of principles. A related point was that the principles of "openness" and "provide the right signals" should be more broadly interpreted so that potential offset projects are not excluded.

It was also felt that "providing the right signals" suggested an early start date and some type of recognition for early action, in order not to penalize those who acted early.

The need for more provincial and federal harmonization of GHG reduction programs and initiatives was raised by a number of participants. For example, it was suggested that a consistent approach to measurement across all jurisdictions is required to encourage cooperation on administration of the system. However, given the significant regional differences in opportunities, it was also suggested that provinces could play a role in defining regional variations, within the federal system.

The point was raised that, to make the market work, a credit must be a commodity with validity, permanence and ownership clearly defined. However, the administrative complexity required to fully ensure these qualities contributes to transaction costs and therefore reduces the liquidity of the system. It was suggested that the system should be designed to balance these considerations.

### 3.2 Eligibility

The comments on eligibility criteria were focused on five of the criteria:

- **#2. Start Date.** There was concern about delaying the start date and recognition that incentives are required to promote early action prior to 2007. At the same time, questions were raised about how the early trading pilots (e.g., PERT, GERT, PEERL) will fit into the offset system.
- **#3. Crediting Period.** It was mentioned that eligibility criterion #3 introduces considerable uncertainty given the longer term planning horizon of most GHG reduction and investment projects. Currently there is not certainty with respect to offset credit outside the five-year first commitment period, and therefore no recognition of the planning horizon of long term investments (and longer term GHG reductions).
- **#5 and #6. Measurable and Verifiable.** It was noted that these criteria implied significant administrative burden and transaction costs that needed to be minimized, especially for small and medium enterprises (SMEs). At the same time, it was also pointed out that although scientific research will be required to support these eligibility criteria, the discussion paper gave insufficient attention to this need.
- **#7. Surplus.** Concern was raised that the intent and wording of the surplus criterion should not preclude actions that are voluntary or motivated by non-GHG regulations (e.g., action in response to NO<sub>x</sub> regulations that also reduces GHGs). Some participants suggested that excluding these actions would be contrary to a multi-pollutant emission management approach and would not send the right signals. Further clarity on the definition of surplus was requested.

## 4. ADMINISTRATION

The following comments were noted:

- **Examples for Clarity.** It was suggested that examples are required to enhance the understanding of the proposed offset system.
- **Estimating Transaction Costs.** It was felt that it would be helpful to have a general idea of the costs of administration on a project basis, in order to estimate project costs and the impact on project feasibility.
- **Public Review.** There was recognition that public review is required in the offset system. Some argued for public review at the project level (i.e., during validation) while others argued for review only during the elaboration of rules and protocols for validation and verification.

- **Early Implementation.** It was frequently mentioned that implementation should take place prior to 2007. Reasons cited included: creating a more certain investment climate; shifting investment flows earlier to implement projects; reducing the risk of non-compliance in the commitment period; creating experience for a market system; and providing an early basis for protocol development and refinement.
- **Verification Strategy.** It was suggested that an appropriate verification approach to reduce administration costs would be to adopt the income tax model and carry out audits on a subset of projects as opposed to verifying all projects.
- **Eligibility under the International System.** It was pointed out that credits created under the domestic offset system could be more constrained than credits created under the Kyoto Mechanisms but that the design should balance domestic needs with international compatibility.

## 5. DESIGN CONSIDERATIONS

The following areas were addressed:

- **Risk of non-delivery.** Assuming that contracts will provide the primary trading vehicle, it was argued that the offset system does not need to address issues of non-delivery between parties. Recourse provisions and quality requirements in contracts for non-performance are generally very specific and worked out between the buyer and seller.
- **Non-permanence of sinks.** There were many differing views on how to deal with the non-permanence issue. Some participants viewed the issue in the same context as any non-delivery scenario (see above), whereas others agreed with the idea that the risk associated with these credits needs to be accounted for in some manner (using one of the methods proposed in the Discussion Paper). It was argued that the risk of non-permanence would be too high, causing the liability to end up residing with the Government (resulting in a de-facto subsidy to the LIEs). In turn, the offset system should focus on emission reductions as opposed to sinks.
- **Boundaries.** It was stated that further discussion and clarity was needed concerning the crediting and accounting of emissions reductions related to co-generation outside of covered emissions.

## 6. VIEWS ON SECTORAL DESIGNS

### 6.1 Forestry

The breakout group examined the pros and cons of the two proposed baseline options and concluded that the preferable option was Option A – the “without project” baseline approach.

	<i>Option A: Without Project</i>	<i>Option B: Base Period</i>
Pros	<ul style="list-style-type: none"> <li>• Provides incentives for new activity for the first commitment period</li> <li>• Encompasses the “base period” concept for certain projects (e.g., afforestation)</li> <li>• Projects will be more tangible &amp; saleable</li> <li>• Models the approach in “other sectors”</li> <li>• Requires no assumption of linear trend in forest development from the base period</li> <li>• Can have a dynamic baseline</li> <li>• Can work for avoided emissions projects</li> <li>• No need to aggregate across landscapes</li> </ul>	<ul style="list-style-type: none"> <li>• Might provide more benefit over the longer term</li> <li>• Lower transaction costs</li> </ul>
Cons	<ul style="list-style-type: none"> <li>• May have high transaction costs</li> <li>• Requires extensive scientific information to establish a baseline</li> <li>• Review and verification requirements may be more rigorous and/or costly</li> </ul>	<ul style="list-style-type: none"> <li>• Need to aggregate across landscapes</li> <li>• Doesn’t work for avoided emission projects</li> <li>• Assumes continuation of a linear trend in forest level from base period</li> </ul>

In considering the eligibility of avoided emissions projects, the group suggested that proactive projects should be considered (e.g., pest control, fire protection, reduction in road right-of-way width) but that rules were needed to judge projects for possible eligibility. In general, the group thought that “do nothing” projects (e.g., not harvesting a forest) should not be eligible.

The following views were also raised:

- There is a need to establish the start date as soon as possible.
- There is a need to clarify carbon credit ownership. For example, do landowners (Crown/private) own offset credits?
- Aboriginal and treaty rights need to be recognized and considered in the system.
- There is a need to consider a backup plan in the event that the Kyoto Protocol does not come into force or if there is no second commitment period.
- There is a need to consider the implications of co-benefits (e.g., ecosystem integrity, etc.).
- With respect to the risk of reversal (e.g., insect infestations, fire), it may be best to implement risk-management using the best available science rather than buying insurance.
- The scale of a “disaster”/non-permanence event could be a factor for consideration.

### 6.2 Agriculture

The breakout group examined the two approaches – independent producer and pooling – and concluded that the two are not mutually exclusive. Comments included:

- The pooling approach makes sense when there are common practices.

- The independent project approach is useful where the sector is more diversified and can work with innovative concepts (e.g., new cultivators, anaerobic digesters).
- Although the pooling approach may avoid disincentives to early adoption, it does not address the issue of credit for early action.

Under the independent projects approach, the group considered how changes in carbon stocks should be determined. Comments included:

- The calculations should be based on the current state of knowledge.
- The implications of Best Management Practices (BMPs) should be validated using sound science.
- Calculations should be compatible with national GHG accounts (also applies to pooling).
- There is a need to quantify the potential value of offset credits for farmers.

Under the pooling approach, the group offered the following ideas:

- There could be different types of pools (e.g., regional or sectoral).
- Some BMPs may not be applicable everywhere and therefore adjustments will be required.
- Science based criteria are important for innovation, as well as measurement and verification.

The following views were also raised:

- There was strong support for the pooling concept and the open principle.
- It will be imperative to understand how the market will discount for non-permanence and risk.
- Risk management - if the pool is overly narrow (small) it may not be able to cope with the full implications of the risk. A sector pool may spread the risk more appropriately.
- The results of science and innovation regarding agricultural sinks need to be communicated to farmers and the industry.
- The challenge is to create incentives for action now, not just in the first commitment period.
- Livestock methane is an important emission, and the emission reduction potential may be underestimated.
- Only one or two of provinces monitor soil nitrogen – a possible opportunity for reductions.
- There is a need for consistent rules between offsets and the covenants system with respect to eligibility and credit for early action.
- There is a need for simple, clear and cost-effective rules to maximize incentives and ensure farmer participation.
- There is a need to clarify the roles, incentives and start dates soon so that investment decisions can be made. In particular, a number of emission reduction projects are longer than five years and need to begin well in advance of the first commitment period.

### 6.3 Landfill Gas

The breakout group examined the options of expanded regulation vs. offsets and expressed a clear preference for offsets. The following advantages were identified:

- Offsets will support domestic reductions and action.
- Offsets are more efficient from a proponent's perspective (i.e., offsets will spur a greater amount of emissions reductions).
- LFG offsets are Grade A - easy to implement with measurable and verifiable emission reductions.
- Offsets will result in low administrative and transaction costs.

Disadvantages of the regulation option were also identified:

- Regulations in this context are infeasible and impractical.
- Provinces are unlikely to support additional regulations.
- Federal jurisdiction to impose regulations is questionable.
- The administration costs of regulations are high.
- Regulations are inefficient from a proponent's perspective (i.e., only the surplus incremental to the reductions under the regulation may be sold as offsets).

In the view of group participants, the most important factors for implementation are:

- **Defining Surplus.** It was suggested that the wording be changed to "climate-change specific regulation" to clarify the intent.
- **Start Date of the System.** More certainty is required. The CDM start date of January 1, 2002 was suggested.
- **Start Date of the Project.** A definition of what constitutes the start date of the project is required (i.e., "shovel in the ground" or operations).

There was unanimous opposition from the group to the concept of a direct contribution to Canada's Kyoto commitments. The following reasoning was advanced:

- **Inequitable.** Requiring a contribution would disadvantage LFG projects relative to other domestic projects (agriculture, etc.) and international CDM/JI projects.
- **Inefficient.** Requiring a contribution would increase the price and cost of reductions and shift the demand to other projects.
- **Uncertain legality.** A contribution represents a fee that the government may not have the authority to implement.

The following views were also raised:

- The value of LFG utilization to displace other fuels should be fully recognized. Not doing so creates a perverse incentive for flaring instead of utilization.

- Participation in voluntary agreements and programs like EcoLogo should not preclude the crediting of offsets to LFG.

#### **6.4 Other Sectors**

The breakout group examined the eligibility proposal. The following views were raised:

- The exclusion of renewables is not reasonable and sends the wrong signal regarding the adoption of renewable power.
- Offsets credits should go to those who make the investment.
- Since renewables are excluded from the LIE discussions, they should be included in the offsets system.
- Clarification is needed for the meaning of “voluntary” actions that might be excluded.

The group considered that there was a large number of potential offsets projects in many sectors, including: renewables; biomass; freight energy use; vehicle efficiency; demand-side management (electricity and gas); trip reduction for employees; recycling and co-generation. Ultimately the group felt that the market should decide the most promising projects, and that the system should be as open as practicable.

To facilitate the inclusion of new and/or small projects, the group made the following suggestions:

- The rights and responsibilities of aggregators should be clarified.
- Rules for the post-2010 should be established as soon as possible.
- The system should be kept as simple as possible. Although consistency is required, the government should not try to design a perfect system.
- The system should be in place by 2004.
- A two-tier crediting system could be considered – discounting some offset credits based on criteria such as direct versus indirect.
- The cost of protocol development could be subsidized or a licensing/copyright system could be established to reward the initial applicants.
- There is a need to ensure that requirements for third party verification not be excessively onerous.
- An early clarification of the start date is needed.

The following views were also raised:

- Projects should not be ruled out on the expectation of high administration or transaction costs. The market should be left to decide.
- The exclusion of renewables and the associated uncertainty will mean that the US investment climate for renewables will be better than Canada’s. Therefore most investment will flow to the US.
- The inclusion of renewables in the LIE system encourages the existing market power of the fossil fuel-based electricity generators. This is inappropriate public policy.



## **7. CONCLUSION AND NEXT STEPS**

Many participants indicated that they would be forwarding written comments on the discussion paper.

A number of participants sought clarity on the integration of the federal plan (i.e., between offsets, Kyoto mechanisms, targeted measures and LIEs) prior to commenting on the specifics of the offset system.

With respect to next steps, the federal Government indicated that they are planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).

## **List of Participating Organizations - Toronto**

Alcan Global Greenhouse Gas Reduction Program  
BIOCAP Canada Foundation  
Canadian Chemical Producers Association  
Canadian Ecumenical Justice Initiatives  
Canadian Fertilizer Institute  
Canadian Gas Association  
Canadian Institute for Environmental Law and Policy  
Canadian Wind Energy Association  
Clean Air Canada Inc.  
Clean Power Income Fund  
Climate Action Network Canada  
Climate Change Central  
Climate Change Solutions  
CO2e  
Comcor Environmental  
David Suzuki Foundation  
Dow Chemical  
Draz Consulting  
Duke Energy  
E4 Inc.  
Earth Tech (Canada) Inc.  
Eastern Ontario Model Forest  
Eastern Power Ltd.  
Enbridge Gas Distribution  
EnQuest Power Corporation  
GCSI-Natsource  
Gowling LaFleur Henderson LLP  
Green Power Trade Show, Toronto  
ICF Consulting  
ICLEI Energy Services  
Independent Power Producers' Society of Ontario  
Jantzi & Associates  
Kinectrics Inc.

## **List of Participating Organizations - Toronto (continued)**

Macleod Dixon LLP  
Macviro Consultants Inc.  
Manitoba Hydro  
Margaree Consultants Inc.  
Mikro-tek Inc.  
Noranda Inc./Falconbridge Ltd.  
North American Carbon Inc.  
Ogilvy Renault  
Ontario Clean Air Alliance  
Ontario Corn Producers' Association  
Ontario Ministry of Agriculture and Food  
Ontario Ministry of Energy  
Ontario Ministry of Enterprise, Opportunity & Innovation  
Ontario Ministry of Natural Resources  
Ontario Ministry of the Environment  
Ontario Power Generation  
Osler, Hoskin & Harcourt LLP  
Pilkington Glass of Canada Ltd.  
Pollution Probe  
Probyn & Co.  
Protocol Energy/The Forest Bird Society  
RIS International Ltd.  
Ritwik Inc.  
Robert J. Redhead Ltd.  
T. Rotherham Forest Consulting Inc.  
Teletrips Inc.  
The Canadian Chamber of Commerce  
Toronto Hydro Corporation  
Trees Ontario Foundation  
Vestas-Canadian Wind Technology  
Walker Industries Holding Ltd.  
Woodrising Consulting Inc.

# CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA

– *SESSION REPORT* –

**Ramada Airport Hotel  
Montréal, Québec  
June 17, 2003**

## 1. INTRODUCTION

The Montréal consultation session was held on June 17, 2003. There were approximately 40 participants from a range of industry sectors such as forestry and agriculture, business associations, ENGOs, individuals and intermediaries (law firms, brokers, etc.). Representatives from the Quebec government and some municipalities were also in attendance, along with the federal team members. The list of participating organizations is attached.

This report is a summary of views expressed at the Montreal consultation session. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## 2. GENERAL VIEWS ON THE CONCEPT AND PROCESS

There was general support for an offsets trading system and there was broad support for the inclusion of sectors other than forestry, agriculture and landfill gas in the system.

A range of participants voiced concerns over the estimates of business-as-usual (BAU) and potential sinks and reductions related to agriculture, forestry and landfill gas. Participants made the following suggestions:

- The detailed economic modelling undertaken to arrive at these figures should be made public.
- The relationship between baselines, BAU and potential should be clarified.
- The estimates need to be reviewed and validated to provide more certainty in decision-making.
- Estimates should be prepared of the extent to which LIEs will rely on the offset system to reach their targets.
- The estimates need to be reconciled with other megatonne estimates in the Climate Change Plan. In particular, some participants were concerned that some sinks or reductions included in Action Plan 2000 were being counted twice.

It was suggested that there was a need for more clarity on the role of the offset system compared to targeted measures and other proposed tools.

Participants questioned the demand for a domestic offset system when international credits will be for sale at a guaranteed \$15 per tonne. The concern was that there would be insufficient incentive to purchase domestic offsets.

Several participants raised concerns regarding the exclusion of projects involving renewable electricity generation or electricity demand-side management. For example, hydro-electricity generation is not part of the large industrial emitters (LIE) group and therefore will not be receiving allowances – a participant noted that if they are also to be excluded from generating offset credits, hydro generators would be at a competitive disadvantage compared to thermal generators.

Several participants suggested that there was a need for more information on the roles of domestic emissions trading, offsets and the LIE covenants, and the relationship between these components. For example, one participant wondered if there would be single administrative body to deal with the LIE system and the offsets system.

### **3. VIEWS ON CROSS-CUTTING TOPICS**

#### **3.1 Principles**

Much of the discussion dealt with the principles of investor certainty and providing the appropriate signals. Some felt that the \$15 price cap was an important market distortion and that the possibility of targeted measures would also send the wrong signal by providing incentives for more costly actions. In general, there was concern that questions relating to offset credit ownership and project validation were creating investor uncertainty. On the latter, it was noted that it would be important to avoid baseline reassessments during the life of a project, as this would undermine investors' confidence in offset projects. Investor certainty is a prerequisite to the establishment of a futures market for offset credits.

One suggestion was that an additional principle be added, that of avoiding double counting. The view was that the risk of double counting is high enough to compromise the environmental integrity of the offset system, especially in light of the current potential for overlap between an offset system, LIE covenants, targeted measures, etc. Also, Canadian taxpayers should not have to pay twice for the same GHG reduction action.

There were comments on the principle of a contribution by offsets to Canada's Kyoto commitment, ranging from the view that this principle did not recognize the relationship of offsets to the LIE covenants, to the view that the principle was not conducive to long-term investment in Canada. A related point was the need for more certainty concerning the validity of offset credits in the post 2012 period in order to attract investment.

#### **3.2 Eligibility**

Comments centred on the criteria of start date and the crediting period, surplus, and ownership.

**Start date (#2) and Crediting period (#3).** There was broad support for an early start date for offset credit projects. As well, it was suggested that the crediting period should be the same as the applicable period for the LIE backstop/covenant system (possibly before 2008), although

there was also a view that the banking of pre-2008 credits should be avoided. The issue of the status of the Pilot Emissions Reduction Trading (PERT) and the GHG Emission Reduction Trading (GERT) pilot programs was raised. One view was that, although GERT projects could be considered eligible, PERT projects should not be considered because the validation process for those projects was neither transparent nor rigorous enough.

**Surplus (#7).** Comments were made on four issues:

- **Provincial regulations.** Several participants highlighted the need for a level playing field. The example of landfill gas was given – it is subject to differing levels of provincial regulation, therefore a standard national definition of surplus is needed. Agreement on a minimum regulation by all the provinces, or a federal framework with different provincial regulations, were two suggestions on how to manage this issue.
- **Voluntary agreements.** One participant questioned whether voluntary targets should be considered part of the baseline. The particular case of the commitments made under the Canadian Industry Program for Energy Conservation (CIPEC) was raised as an example of voluntary action to improve energy efficiency. The issue of the difficulty in separating out the impacts due to voluntary agreements in baselines was raised, as well as the potential perverse incentive it may cause.
- **Double counting.** The point was again raised that there must be certainty that offset credits are surplus, and have not been accounted for in other government emissions reductions programs. By making public the detailed modelling work that established the BAU figures, the public and industry would have a better idea of the actions from which reductions were calculated, and used to arrive at the targets outlined in the Climate Change Plan. If these actions were known with more certainty, there would be less risk of double counting. One participant noted that estimates for macroeconomic modelling are not necessarily suitable or reliable for more detailed analysis at the level of individual actions.
- **Additionality.** It was suggested that the definition of surplus be refined to ensure that baselines represent what would happen in the absence of the offset system as a whole (as opposed to the absence of the project) in order to ensure additionality.

**Ownership (#9).** There was broad support for the view that the federal government should develop default ground rules for ownership, but that, subsequently, parties would be able to sort out any sector-specific circumstances through the use of contracts.

## **4. ADMINISTRATION**

The following comments were noted:

### **4.1 Program Authority**

A number of participants held the view that a federal government department or agency should be designated as the Program Authority. The following reasons were noted:

- The Program Authority must be held accountable, and the federal government has the mechanisms to ensure this. It is also the jurisdiction that is accountable for Canada's commitment internationally.
- A government entity can ensure transparency by building in a public review process.
- A government entity avoids conflict-of-interest issues.
- Provincial governments lack the incentive to comply with Kyoto, as they are not directly responsible for Canada's target.

An alternative viewpoint was that the program authority be built on currently existing knowledge. The suggestion was that an entity such as the Voluntary Challenge Registry (VCR), which already engages industry on GHG emissions, would be a suitable choice as it encourages transparency about industry actions, and can expedite engagement without the administrative costs of a regulatory framework.

It was suggested that there could be a role for entities such as the VCR or BIOCAP, or provincial governments, in providing advice or coordination under the overall supervision of a federal authority. Several participants suggested that it was important for the government to play a role in ensuring the environmental integrity of the offset system, but that beyond this role, the market should be allowed to operate freely.

#### **4.2 Public Review**

There was some support for the view that the public should have some level of review of the process. Views differed, however, on the form of this review. One view held that a public review period of 60 to 90 days for each project should take place before approval, while another view was that providing public access to non-commercially sensitive information was sufficient, as any review process would cause an unacceptable delay in the issuance of credits. The question of differing levels of information housed in registries and available for public review was raised. In particular, it was noted that transparency was essential for the examination of credits used by LIEs to comply with their covenant targets.

#### **4.3 Early Issuance**

In response to the question of early issuance of credits and the risk of non-delivery, there was support for the view that credits should be available for early issuance, as such action increases market liquidity, reduces risk for investors and allows industry to plan for future purchases. At the same time, it was thought that a futures market should be capable of meeting most of these needs. Views on when early issuance could begin ranged, one consideration was the need by industry to produce inventories of its own emissions before it begins purchasing offsets.

#### **4.4 Risk of Non-Delivery**

One suggestion to reduce the risk of non-delivery was to introduce a criterion that judged the experience of the project developer in bringing credible projects to market. It was generally felt that the market would take care of non-deliverance through contractual arrangements between buyers and sellers. One participant expressed the concern that excessive monitoring and risk management activity could disadvantage small projects. A more general concern was that too

many constraints would increase transaction costs and make it difficult for offset credits to compete with international permits.

## **5. DESIGN CONSIDERATIONS**

### **5.1 Boundaries and Leakage**

In response to the questions of project boundary and leakage, one view was that the market would take care of project boundaries and leakage via risk management in contractual arrangements. In general, it was felt that there was a need for a balance between ensuring liability and promoting market liquidity.

### **5.2 Non-permanence**

With respect to non-permanence, there was some support for the view that temporary credits would offer the best protection against reversals.

## **6. VIEWS ON SECTORAL DESIGNS**

### **6.1 Forestry**

A considerable number of questions of clarification were raised. These questions related to the following topics:

- The inappropriateness of the definition of nonpermanence with regards to forestry sinks.
- The relationship/difference between avoided emissions offsets for domestic trading and the use of avoided emission allowances for international trading.
- The accounting required to demonstrate compliance with the cap on forest management sinks.
- The relationship between the national inventory and accounting on a project basis.
- The designation of harvesting as an emission under the Protocol and the intention to renegotiate this point at a later date.
- The attractiveness of CDM projects, as they currently appear to be a simpler avenue for obtaining credits.
- The possibility of provinces managing their own forestry pools, and acting as offset sellers and distributors of revenues.

In response to the question of which baseline measurement option was preferred (without-project vs. base period), there was broad agreement that each option had its advantages, and that in order for the forest sector to participate in an offset system, there was a need for as much flexibility as possible when making decisions about offset projects.

In response to the question of whether avoided emissions should be part of an offset system, the view was that the forestry sector would base its decisions on the economics of each project, and therefore it was in its interest to have all options available.



It was noted that if the decision on inclusion of Forest Management is not taken until 2006, then no or few Forest Management investments will be made for offsets during the first commitment period.

## **6.2 Agriculture**

In response to the question of which approach to projects was preferred (independent vs. pool), it was generally agreed that both options were viable in different situations, and that the market and cost would dictate the choice.

On the independent projects approach, it was recognized that the technology needed to determine changes in agricultural carbon stock is improving, and that in the meantime, the sector would rely on the best available tools.

On the pooling approach, participants agreed that the structure of pools should not be prescribed; and that it was likely that developers would take advantage of existing pooling structures (such as crop insurance agencies or the Wheat Pools) that offer the lowest administrative costs.

The following comments were also made:

- Government should provide the framework for the system, but the private sector should be left to carry it out.
- The question of how to deal with emissions reductions in periods of economic decline, and increasing emissions due to growth has still to be resolved.
- Concerns remain around how the BAU estimates are being calculated, and whether environmental integrity is being maintained.
- Agriculture requires good science and ongoing research to support its participation in an offset system.

## **6.3 Landfill Gas**

In response to the question of which option participants preferred (extended regulation vs. offset system), there was broad support for inclusion in the offset system, with the caveat that all emissions (and not just methane) be included in order to favour market liquidity. It was recognized that provincial regulations must be dealt with to address the surplus question.

In regards to design factors for implementation, the breakout group noted the following:

- The earliest start date possible should be selected.
- The definition of surplus should incorporate:
  - Eligibility of all emissions above provincially regulated levels.
  - A level playing field between the provinces.

In regards to the proposed contribution, views ranged from a contribution of 0% to 10-15%, which would reflect what is being proposed for other sectors.

The following comments were also made:

- The offset credit price will have an impact on the implementation of smaller landfill projects - economies of scale can be realised, and a higher price will encourage more projects;
- There should be an incentive to encourage renewable energy generation from landfill (and discourage flaring).

#### **6.4 Other Sectors**

In general, the group was in favour of the proposals for eligibility, except when it came to projects involving supply of renewable electricity or demand management, or projects involving off-site or downstream impacts. The group's view was that these types of projects presented significant opportunities and that they should not be ruled out unnecessarily. The group's view was that projects should be judged on their own merits against the eligibility criteria rather than being excluded as a group. It was proposed that the onus be on project proponents to demonstrate compliance with the criteria. For example:

- Electricity projects would have to demonstrate that the reductions are outside of those that would occur as a result of the LIE backstop/covenant system.
- Transportation demand projects would have to demonstrate that the avoided emissions are measurable and verifiable and that ownership is beyond challenge.
- Recycling projects would have to demonstrate that reductions are net of leakage associated with the transportation of the recycled materials.

It was recognized that the criteria would be difficult to meet and, in particular, the development of a credible baseline for determination of surplus reductions.

In regards to design elements that would encourage new and/or smaller projects in an offset system, participants suggested the following:

- Removing all restrictions on types of projects (incl. the restriction on electricity generation projects and upstream and off-site projects).
- Applying (strictly) the eligibility criteria
- Putting the onus on the project developer to prove that these criteria have been met, as above (e.g., ownership is clear, the project is surplus with respect to the LIE system and TMs, it is measurable and verifiable).
- Small project developers could either pool from among individuals and/or from among SMEs and others. The pooling of small reductions from the actions of individuals has the additional advantage of promoting greater awareness of the issues and a greater sense of ownership among citizens.

The group noted that the role of government is to recognize the small projects, expedite the process of their validation, and promote awareness.

## **7. CONCLUSION AND NEXT STEPS**

With respect to next steps, the federal government indicated that they are planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).

## **List of Participating Organizations - Montréal**

Abitibi Consolidated  
André Simard & Associés  
Bowater Canadian Forest Products Inc.  
Bureau sur les changements climatiques (Québec)  
Canadian Federation of Agriculture  
Canadian Pork Council  
Cement Association of Canada  
Conseil de l'industrie forestière du Québec  
Conseil Patronal de l'Environnement du Québec (CPEQ)  
Dairy Farmers of Canada  
Fasken Martineau Dumoulin LLP  
Forintek Canada Corp  
Gaz Métropolitain  
Grain Growers of Canada  
Group Alcan Métal Primaire, Division d'Alcan Inc.  
GSCI-Natsource  
Highland Energy Inc.  
ICF Consulting  
Kruger  
L'Union des Producteurs Agricoles  
McCarthy Tétrault  
McGill University  
Ministère des Ressources naturelles du Québec, Secteur énergie  
Ministère de l'Agriculture des Pêcheries et de l'Alimentation du Québec  
Ministère de l'Environnement du Québec  
Ministère du Développement économique et régional du Québec  
Ministère des Ressources Naturelles du Québec, Secteur faune et parcs  
Noranda Inc./Falconbridge Ltd.  
Paprican  
Pembina Institute  
Régie de gestion des matières résiduelles de la Mauricie  
Régie intermunicipale Argenteuil Deux Montagnes  
Tembec Inc.  
Tree Canada Foundation  
Union des municipalités du Québec (UMQ)

# **CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA**

*– SESSION REPORT –*

**Delta Barrington Hotel  
Halifax, Nova Scotia  
June 18, 2003**

## **1. INTRODUCTION**

The Halifax session was the third of six consultative sessions on the design of a greenhouse gas offset system for Canada. Approximately 30 stakeholders attended the workshop from a range of industries, business associations, non-governmental organizations, and intermediaries. Representatives from federal and provincial governments were also in attendance. The list of participating organizations is attached.

This report is a summary of views expressed at the Halifax consultation. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## **2. GENERAL VIEWS ON THE CONCEPT AND PROCESS**

In general there was broad support for the proposed greenhouse gas offset system. However, there were many questions of clarification regarding the elements of the proposed system. There were also questions about the relationship between elements of the Climate Change Plan (e.g., LIE system, targeted measures, etc.) and the roles of the different federal departments.

Many participants asked for clarification with respect to the definition and the starting date for the business as usual (BAU) scenario, and inquired as to whether or not past efforts would be rewarded under this system. The need to recognize and reward early action was emphasized, pointing to the fact that significant progress has been made in the past decade in reducing greenhouse gas emissions. The view was expressed that, in the absence of recognition for early action, those that have already achieved significant progress through the implementation of best practices will have few incentives for ongoing improvement, and could even be placed at a disadvantage relative to others that have not yet adopted similar practices.

Participants sought further clarification on the criteria that would be used to make the distinction between “normal business operations” and “exceptional new efforts” and also whether or not baselines could be changed in light of new information. There was support for the idea of defining standard practice within a specific sector, as well as for the concept of regional averages as a means for setting equitable baselines.

Most participants agreed that the federal government should provide incentives for creating domestic credits. This could take the form of either up front incentives (by subsidizing offset projects) or through the provision of end use incentives (government could be a purchaser of offsets). Providing incentives for domestic credit creation could also serve to decrease demand for compliance units from international sources.

While most participants supported the view that domestic credits should be available for trade in the international market, several individuals expressed concerns over the harmonization of domestic principles and price structures with international practices.

Other views presented included:

- A mechanism should be in place to ensure that there is no double counting between the offset system and the LIE backstop/covenant system.
- Administrative and transaction costs associated with targeted measures should be compared to those associated with the offset system.
- A formal governance structure should be established – including representation from all key federal departments – to provide oversight to the offset system.
- The proposal that projects designed to reduce electricity consumption from the grid would not receive credits would place several landfill gas projects at a distinct disadvantage.

### **3. VIEWS ON CROSS-CUTTING TOPICS**

#### **3.1 Principles**

In general, participants agreed with the five principles, but suggested that some principles appear to be in conflict with each other, and in conflict with other initiatives under Canada's climate change plan (e.g., LIE system). There was strong support for the fourth and fifth principles, which suggest that the offset system be designed to encourage investment in Canada, and to provide the right investment incentives. Several participants suggested that incentives (including an early start date) are needed to encourage investment in projects with long-term benefits, particularly for those that will not offer direct benefits until after the initial credit period. It was also noted that mechanisms should be in place to ensure that good practices are maintained in the short term, as there may be perverse incentives to lower current performance in order to obtain greater credit for future actions. Perverse incentives could also put at risk some of the assumed BAU credits, which are expected to contribute directly to Canada's Kyoto commitment.

It was also agreed that there should be consistency between the proposed offset system and other initiatives under Canada's climate change plan. As some current initiatives are designed to encourage early action the offset system should not only focus on future actions that are incremental to ongoing operations.

There was support for the principle of "open as practical", with one participant noting the significant potential for emission reductions in the transport sector that could generate credits for use by LIEs. Engagement of the private sector would be fundamental to the success of any reduction efforts.

## **3.2 Eligibility**

There was a mixed response to the proposed eligibility criteria, with many sector-specific concerns. Of particular concern overall was the lack of certainty with respect to project eligibility beyond 2012.

One participant emphasized the need to recognize the interconnection of projects – especially for vertically integrated entities that can apply their efforts to several components of the overall implementation plan (including the LIE process, offset system and targeted measures system).

It was also noted that the offset system should do more to promote and reward investment in renewable energy technology and reductions in electricity consumption.

It will be important to apply the surplus criterion carefully to avoid artificial barriers that could make it impossible to derive benefit for some actions. In particular, there were concerns raised over the application of the surplus criterion in the context of targeted measures involving relatively small contributions from the federal government. Some participants questioned the fairness of using an incremental approach as opposed to deducting a proportional share of the generated credits.

Participants identified a need to evaluate the relative effectiveness and cost efficiency of targeted vs. other measures (such as offsets eligibility) prior to deciding on the best strategy.

In general, participants agreed that early signals are needed with respect to projects that will be eligible for credit and that a high level of certainty will be needed well before the first commitment period begins.

One participant noted that the relationship between consumers and suppliers presented some opportunities. For example, the possibility of establishing producer-supplier relationships where real, measurable and verifiable offsets could be generated with clear (possibly shared) ownership.

A participant suggested that full life cycle accounting was required in order to consider the true effect on GHGs from both emissions and carbon sequestration. It was also recommended that the data collected through existing analysis reports could be applicable to the offset system.

## **4. ADMINISTRATION**

There was widespread support for keeping the system simple. For example, one participant emphasized the need to limit paperwork requirements.

Most participants felt that the process would have to be adjusted to reflect the unique conditions of each sector and region of the country. For example, there was some support for the idea of using existing mechanisms for pooling (e.g., crop insurance), however participants cautioned that conditions vary across the country (e.g., in the Maritimes less than 30% of crops are covered by crop insurance – so this mechanism has limited applicability).

Participants again emphasized the need to recognize early action, and indicated that the need for incentives could be best addressed through the creation of a futures market that would provide buyers with the opportunity to purchase credits for delivery at a later date. They also noted that one of the concerns with this mechanism is the issue of permanence: who is responsible for ensuring that credits sold in the futures market will actually be realized? One suggestion was that the risks associated with the futures market were significant, and that without greater certainty there would be a reluctance to purchase these credits.

Several participants suggested that a trial period be developed for this system. After the trial period, the government, in consultation with stakeholders, could review the proposed system and make any necessary adjustments prior to broad implementation. Potential participants in the system would also have the opportunity to test their quantification and verification protocols prior to the first commitment period.

With respect to reporting requirements, most participants agreed that it will be important to provide guidance to potential sellers as soon as possible. Much of the information required for reporting will take several years to collect, demonstrating the need for beginning this process at the earliest possible date.

It was also noted that responsibility for determining BAU/baselines and for reporting will not necessarily fall to the offset claimant. This may make it difficult to devote the resources necessary for the development of credible information (e.g., provincial governments may be responsible for forest inventories but may not be the primary beneficiaries of the sale of offsets).

Furthermore, in some jurisdictions where capacity is limited, it will be difficult to have third party verification. With a limited pool of available verification entities, there may be the possibility of conflict of interest, suggesting the need for other verification mechanisms. If third-party sources are not available, payment for verification could rest with either the project proponent or the federal government.

## **5. DESIGN CONSIDERATIONS**

Most participants agreed that additional guidance will be required with respect to determining project boundaries, and in addressing permanence issues.

An example was provided of how it would be difficult to account for forest sinks on a project-specific basis, and it was suggested that project boundaries be comparable to those already established to determine sustainable yield and timber supply. An exception to this is small afforestation projects, where it is possible to determine project-level impacts.

In regards to agricultural sinks, there was support for the view that determining boundaries on an independent project basis could be too administratively burdensome and that some sort of pooling might be appropriate.

Views on the use of temporary credits as a means of addressing issues of permanence were mixed – some favoured the approach, and others were opposed.



## **6. VIEWS ON SECTORAL DESIGNS**

### **6.1 Forestry**

Members of this discussion group suggested that the “without project” option provided the most fair and reasonable approach, whereas the base period option will produce both winners and losers depending on the state of the forest, rather than the nature of the project.

There are several issues associated with establishing baselines for private lands. In particular, and depending on the approach, it will be difficult to determine regional averages, company-specific BAU and history, and the impacts of provincial / crown regulations.

Other questions and views included:

- How will the Government ensure that early adopters are not penalized?
- How can perverse incentives be avoided?
- Regional averages will be useful, but dynamic baselines or periodic updates will be needed to account for change (e.g., pest outbreaks). In plenary, one of the session participants supported this view, but cautioned that it could result in the loss of offset credits, and could involve liability issues.
- Significant opportunities exist for improved forest management practices in Atlantic Canada, but it will be difficult to create incentives for investment in long-term projects.

In regards to avoided emission projects, members concluded that eligibility should depend on the project type. Furthermore, it will be difficult to set baselines for avoided emission projects.

The following views were also raised:

- Early decisions are needed with respect to the eligibility of forest management projects.
- Private woodlots have much in common with the agriculture sector and many design features being considered for that sector, such as pooling, might be applicable.
- The Canadian Council of Forest Ministers (CCFM) commitment to Sustainable Forest Management (SFM) requires the consideration of other values beyond carbon sequestration. These values must be protected in the design of the offset system.
- Third-party project certification should be considered, however a decision should be made soon.
- The first project will set a precedent for following projects, but the opportunity to change baseline determination procedures should exist for subsequent projects.

### **6.2 Agriculture**

In regards to the options pooling vs. the independent project approach, members of the agriculture discussion group concluded that both options presented unique opportunities and challenges.

The pooling approach could be designed in two ways: (1) membership could include all producers in a specific region; or (2) membership could be elective, where only those wishing to participate would become members of a pool. The first option would recognize early and late

adopters and could draw on existing data sets, but there would be losses in terms of unit cost. The second option would provide a higher reward for late adopters, and would be accompanied by high transaction costs. In plenary, it was suggested that the pooling approach could work across the supply chain and across different sectors and that there might be several advantages to expanding on supply chain management considerations.

The independent projects approach would reward early actors, but measurement on every farm would not be practical. Changes in carbon stock would be difficult to quantify due to the lack of historical data, the costs associated with project-based BAU determination, and the inadequacy of existing statistical modelling practices.

The following views were also raised:

- Carbon storage initiatives should be designed to promote other conservation objectives.
- The industry is interested in the establishment of temporary credits to address issues of permanence.
- There are concerns over whether or not adequate databases for farm practices are available.
- Action on climate change should not be segmented – it will be important to have interaction between sectors.
- The relative advantages of a whole farm vs. a commodity specific approach should be examined.

### **6.3 Landfill Gas**

The landfill gas discussion group concluded that the inclusion of landfill gases in the offset system was preferable to expanded regulation for the following reasons:

- The “carrot” approach is better than the “stick” approach.
- Actions to reduce emissions should be accompanied by the appropriate compensation, particularly given the limited resources available to municipally-owned landfills.

The group also agreed that one of most important design factors will be determination of an appropriate start date. The group recommended that projects begin as soon as possible (January 1, 2004, was the recommended start date), and that early trading be encouraged to provide a means of gaining the appropriate level of experience prior to implementation of the overall process. It was also suggested that credit be given for action prior to 2008. Underlying all design considerations should be principles of simplicity, clarity and transparency.

The group did not believe that landfill gas initiatives should contribute directly to the Kyoto Target. It was suggested that a direct contribution would create a disincentive for reduction, and that action by this sector would represent “expropriation without compensation” (i.e., the federal government will receive credit for private sector action without having to invest in actual reduction), resulting in a loss of revenues for owners of emission reductions.

The landfill gas discussion group also emphasized the need to promote sustainable waste management, organic diversion and source reduction. They also recommended that renewable energy use be considered for inclusion in the offset system.

## 6.4 Other Sectors

Members of the discussion group suggested that the success of the system will depend on (a) administrative feasibility; and (b) the ability to quantify and track emission reductions. The group also made note of the lack of incentives for renewable energy use, and emphasized the importance of making the offset system compatible with complementary federal and provincial initiatives.

The group recommended that the federal government take an open view to other projects, providing some flexibility in the early stages and introducing more rigour over time. One of the advantages of such a system would be the promotion of innovative technological solutions.

Project types identified as those with the most potential include:

- Residential fuel switching.
- Transportation (fleet conversion, fuel efficiency, road to rail).
- Community based initiatives.
- Solid waste diversion (organic management programs).
- Biofuels.
- Energy efficiency (generally).

Design elements that could be implemented to facilitate the inclusion of new project types and/or small projects in the offset system include:

- Simple screening for small projects.
- Aggregation of activities.
- A niche for community initiatives.
- Openness to innovative ideas.

Additional comments included:

- Offsets allow for more innovation than targeted measures, but are associated with a high degree of uncertainty.
- Regional flexibility should be included as part of the design.

## 7. CONCLUSION AND NEXT STEPS

With respect to next steps, the federal government indicated that they are planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).

## **List of Participating Organizations - Halifax**

Agriculture Producers Association of New Brunswick  
Alberta Sustainable Resource Development  
Atlantic Grains Council  
Canadian Agri-Food Research Council  
Canadian Manufacturers and Exporters  
Conservation Corps - Newfoundland and Labrador  
Eastern Canada Soil and Water Conservation Centre  
Ecology Action Centre  
Forest Products Association of Nova Scotia  
Highland Energy Inc.  
JD Irving  
New Brunswick Natural Resources and Energy  
Nova Scotia Department of Energy  
Natsource  
Neill and Gunter Ltd.  
New Brunswick Environment & Local Government  
New Brunswick Power  
Newfoundland and Labrador Department of Mines and Energy  
North Atlantic Refining Ltd.  
Nova Scotia Agricultural College  
Nova Scotia Power  
P.E.I. Agriculture & Forestry  
Stora Enso Port Hawkesbury Ltd.  
UPM-Kymmene

# CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA

– SESSION REPORT –

Marriott Hotel  
Calgary, Alberta  
June 23, 2003

## 1. INTRODUCTION

Approximately 70 stakeholders, representing a range of industry sectors, business and municipal associations, environmental NGOs, and provincial and municipal governments attended the Calgary session. This report is accompanied by a separate list of the organizations that participated in the meeting.

This report is a summary of views expressed at the Calgary consultation. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## 2. GENERAL VIEWS ON THE CONCEPT AND PROCESS

Participants in the Calgary session offered support, in principle, for the concept of a greenhouse gas offset system. This support was not universal, however. In addition, participants identified three key problematic areas:

- The lack of information on the boundaries between the offsets system and other elements of the federal *Climate Change Plan*;
- The proposed ineligibility of renewable electricity generation projects (in particular wind generation) and other projects involving indirect emission reductions; and,
- The lack of consideration for credit for early action.

**Fit with Other Elements of the Federal Climate Change Plan** - Participants raised several questions of clarification with respect to the overall fit between the offset system and other elements of the federal *Climate Change Plan*, including: the large industrial emitters Group backstop-covenant system; existing and planned targeted measures, such as Infrastructure Funds and Green Municipal Funds, and the proposed Partnership Fund and Innovation initiatives

Specifically, participants were concerned about the impact of these initiatives on Business as Usual (BAU) projections and sectoral/activity baselines, as well as the eligibility of different sectoral activities under the offset system. It was suggested that clarity needs to be provided in this area to motivate investment and activity prior to 2008, and also to ensure emission reductions are not double-counted.

Stakeholders also suggested that a single process, or a set of parallel processes was needed for the design of all key Plan elements and to provide stakeholders with confidence that nothing of importance would “fall through the cracks.”

**Exclusion of Renewable Projects and Other Indirect Emissions Projects** - Participants showed particular concern over the lack of clarity with respect to how investment in renewable electricity projects would be motivated under the federal Plan. A significant majority of participants indicated their desire for the inclusion of renewable energy projects in the offset system, including those involving wind power and biomass by-products of forestry and agricultural operations. In particular, participants expressed concern that the proposed approach to manage these incentives through the large industrial emitters backstop-covenant process did not reflect the realities of Alberta’s deregulated electricity system. Participants were equally concerned about the proposed exclusion of energy efficiency and demand side management activities that would likewise contribute to indirect emission reductions. Other stakeholders raised additional concerns focusing mainly on how the exclusion would be at odds with several of the Principles proposed in the Discussion Paper, including:

- Principle 1 (Enhance market liquidity)- it would exclude a significant portion of the lowest cost, most easily measurable, verifiable emission reductions;
- Principle 2 (Open as practical) - it would provide a disincentive to investment in renewable energy by small and medium sized operators and only provide a market signal to the large electricity generating utilities;
- Principle 4 (Invest in Canada) - reduce liquidity and increase reliance on less certain activities would lead buyers to look offshore for more certain reductions.
- Principle 5 (Provide right signals for action) - it would remove important incentives for municipalities to purchase renewable energy blocks;

Participants also noted that the existing Wind Power Production Incentive was significantly lower than similar incentives provided in the United States, and argued that this incentive alone would not lead to the creation of a robust renewable energy system in Canada. Participants suggested two other possibilities to provide clearer incentives for investment in renewable energy:

- Establishment of an offsets “set aside” for renewable energy projects; or
- Development of a tradable, renewable energy quota / portfolio system.

**Credit for Early Action** - A substantial number of participants raised concerns about lack of credit for early action in the proposed greenhouse gas offset system. While the need for the federal government to design a system capable of meeting Canada’s Kyoto commitments was acknowledged, participants argued that by not rewarding early action, the proposed offset system sent the wrong signals and provided only limited incentive to invest in emission reduction activities prior to 2008. Further, by not rewarding early action, the federal government’s BAU baselines might not be achieved, as perverse incentives could lead to existing and planned activities being postponed, or not maintained prior to 2008. Several interventions were made arguing for consideration of an industry/sectoral standard approach, so that companies that invest early and that are ahead of the baseline would not be unduly punished.

### 3. VIEWS ON CROSS-CUTTING TOPICS

#### 3.1 Principles

Several participants expressed their opinion that Principle 5 (Provide right signals for action) was the most important among the five listed in the Discussion Paper. These participants felt there was not enough certainty that BAU emission reductions would in fact be achieved, unless the proper signals were provided. Moreover, these participants favoured a plan capable of positioning Canada for its long-term goals, rather than being overly fixated on its Kyoto commitments.

While one participant suggested that Principle 3 (contribute to Kyoto commitment) be removed, as it would lead to increased transactions costs, others suggested that Principle 3 should be considered the most important principle. Participants voiced strong support for a greenhouse gas offset system capable of creating incentives for domestic investment (Principle 4).

Finally, individual participants suggested consideration of four additional principles when designing the greenhouse gas offset system:

- A commitment to transparency and public involvement, taking into account past experiences with quasi-voluntary systems;
- A commitment to ensuring that ownership of offsets should rest with those who invest;
- A commitment to allow risk to be negotiated through contractual arrangements; and
- A commitment to avoid public liability for non-delivery or non-permanence of offsets.

#### 3.2 Eligibility

A suggestion was made to include an additional criterion, requiring proposed offset projects to satisfy some form of environmental screening, assessing potential broader environmental impacts arising from the project.

**Criterion 2: Project start date** - Participants offered different suggestions:

- December 2002, reflecting Canada's ratification of the Kyoto Protocol;
- January 1, 2000, as per the Clean Development Mechanism;
- January 1, 1990, consistent with the Kyoto Protocol;
- Whichever date is consistent with the start date proposed for the large industrial emitters backstop-covenant system; and
- Other support was provided for a tiered start date.

**Criterion 3: Crediting Period** - Several participants expressed the view that the proposed five year crediting period (2008-2012) was too short and would work against the proposed Principle 1 (Increase market liquidity). Strong support was voiced for consideration of an early start date, perhaps involving some form of pilot program. Support was also voiced for an extended, post-2012 crediting period, given that some projects will require a much longer economic life to recover investments.

**Criteria 4, 5 and 6: Real, Measurable and Verifiable** - Participants noted that certain renewable energy projects and other projects involving energy conservation activities were amongst those capable of best satisfying these criteria.

**Criterion 7: Surplus** - Participants pointed out that determining surplus will depend on having a better understanding of what is and what is not included in the BAU baselines, and what is covered by other elements of the Plan. One participant suggested that surplus should not be determined by the level of emission reductions that would have occurred in the absence of the project, but rather those that would have occurred in the absence of the offset system.

**Criterion 8: Unique** - The federal government was called upon to cooperate with provinces that are in the process of developing their own climate change plans, so that the question of uniqueness does not become a “double jeopardy” issue for those required to make emission reductions under multiple systems.

**Criterion 9: Ownership** - Participants argued that it was crucial to provide clarity on ownership issues as soon as possible, in order to improve the prospects for market liquidity. Some participants suggested that ownership should be determined strictly on the basis of project investment by proponents.

#### **4. ADMINISTRATION**

**Governance Issues** - Participants expressed polar views on possible administrative structures and roles. While some support was expressed for a third-party, arms-length Authority, others suggested that administration of the system was too important to be left to a third party and would require active government involvement. In terms of roles, it was suggested that the Authority should allow those that are bearing risk to negotiate risk of non-compliance, with the Authority focusing on establishing the penalties for non-compliance

**Guidance for Project Proponents** - Participants offered considerable input on the issue of the proper level and form of guidance that should be provided by the government, or by another administrative authority. One participant cautioned against having unrealistic expectations with respect to the guidance that could be provided through standardized processes, given the range of project activities likely to emerge. Other participants suggested that the proper role of the government/authority would involve setting standards for protocol development by others. Others agreed with this view, but noted that the government/authority would need to find a means of compensating those who develop protocols, so that these can then be placed in the public domain and contribute to overall lower transactions costs across the offsets system. Support for development of protocols by entities other than the government/authority was not universal. A few participants questioned whether parties who have clear self-interest in project outcomes could develop fair and appropriate protocols. Participants agreed that development of domestic protocols should draw on work underway at the international level.

**Review Process** - Different views were offered on the issue of which entity should be responsible for verification. Some participants argued that existing, third party service providers (auditors, accountants, etc.) should be relied upon. Others stressed the need for transparency and the role of public involvement in the review process. A concern was raised that annual verification requirements might result in unacceptable transaction costs. Others suggested that verification



requirements should be consistent with those under development in the international system. In considering the link between verification and issuance of credits, one participant encouraged project proponents to set aside accrued revenues in a stand-alone, interest bearing account until fully verified/issued.

**Registries Issues** - One participant noted the importance of providing early clarity on registration requirements, so that information collection and analysis could be managed in a least-cost manner by building them into the project design at time of project start. Others noted the importance of compatibility with registries already in place or under development domestically.

**Trading and Links with International Systems** – Some participants expressed strong support for a domestic offset system that could be easily integrated with those under development for the Kyoto Mechanisms. In considering trading issues, the positive role that could be played by a futures market, in terms of dampening volatility and increasing liquidity, was highlighted.

**Other Administrative Issues** - One participant noted that clear penalty rules provide a strong incentive for purposefully doing things right, and a strong disincentive for doing things wrong, whether by intent or accidentally.

## **5. DESIGN CONSIDERATIONS**

**Baselines** - Participants sought clarification about what activities and emission levels were included in BAU projections across various sectors. The question of when BAU projections would be considered final, or whether they would be changing as the 2008 date approached, was also raised. Concern was expressed that the proposals for BAU projections and baselines were confusing and complex, especially as they attempted to take into account partial investments from other measures to determine the portion of reduction eligible for an offset. Interventions were also made suggesting that the offset system rules for BAU projections and baselines be consistent with, and take advantage of those being developed for the Kyoto Protocol.

**Non-Permanence of Removal projects** - Participants expressed an interest in receiving more information on how temporary crediting would work and how it would impact price. It was suggested that the insurance industry could also play an important role in managing non-permanence issues within private contract systems as long as the commodity was clearly known/defined. The possible role of commodity associations, exchanges, and other pools in the management of risk was also noted. Other participants expressed a more cautious view of the role of private contracts, arguing that, without proper public scrutiny, liability could be off-loaded to the public. As well, the need to address non-permanence issues in a manner consistent with the international system was also raised. One participant argued that before the private sector service providers in the insurance, tax and accounting sectors could play a role in the offsets system, clarity was required on whether offsets will be a commodity, a security, an environmental permit, or a service. In considering the difficulties of addressing the non-permanence issues associated with removal activities, interventions were made on the desirability of focusing investment in more certain emission reduction projects, including landfill gas, and low impact renewable energy.

## 6. VIEWS ON SECTORAL DESIGNS

### 6.1 Forestry

**Views on Proposed Baselines Approaches** - Participants discussed the pros and cons of each approach without offering a clear preference for either one. Participants noted that the without-project approach provides the most flexibility and would allow proponents to choose the most appropriate baseline for the project type. It was recognized, however, that with potential range of different project types and sizes involved, this approach could be complex and result in higher transaction costs.

Some participants identified a need to disaggregate the forestry BAU projection by region and activity, as such estimates might provide a useful and more cost-effective standard activity baseline against which proposed projects could be evaluated. It was also noted that such a regional averaging approach would contribute to rewarding early actors, and motivate additional investment and activity prior to 2008.

**Views on Eligibility of Avoided Emission Projects** - Participants agreed that avoided emissions projects should not be excluded as an entire class. Participants agreed, however, that avoided deforestation projects (e.g., improved low impact seismic lines, joint development of road networks with other sectors) were more suitable for consideration, while other types of avoided emission projects (e.g., fire and pest suppression) might be better approached through targeted measures rather than the offset system due to the complexities of establishing baselines and potential long-term ecological impacts.

**Views on Other issues** - Participants identified the need to focus on approaches for managing non-permanence. Finally, participants suggested that the design of the offset system needs to recognize that decisions involving forest management practices are ultimately determined by consideration of the value of forest fibre, and that proposed project activities involving consideration of carbon management alone would not be viable. The long-term nature of forestry investments also means that assurance of credits post-2012 is needed to motivate investment.

### 6.2 Agriculture

**Views on Proposed Approaches** - Participants did not express a clear preference for either of the proposed approaches (independent producer vs. pooling), as each was seen to have positive and negative attributes, some of which could provide perverse incentives and lead to gaming behaviours. The independent project approach, however, was considered to have a greater potential for addressing liability issues. The complexity and information needs for, determining baselines and BAU projections on a case-by-case basis, however, may result in independent with having unacceptable transaction costs. Some participants felt that the pooling approach could involve lower transaction costs, especially if top-down estimates for baselines and BAU projections were relied upon.

An alternative approach was put forward and received some support from other participants. This approach would involve the government providing “compensation,” or other incentives to ensure BAU activity is undertaken as anticipated. This would reward early actors, provide an incentive for additional investment pre-2008, and help to avoid gaming behaviour.

**Views on Criteria for Pool Membership** - Participants felt strongly that membership criteria should be left to project proponents and offset purchasers to address.

**Views on Other Issues** - Participants stressed the importance of emission reductions activities in the agricultural sector in areas such as livestock feeding, manure management, and biogas management. It was felt that such activities were significantly different from carbon removal activities involving agricultural soils, as they are more readily measurable and verifiable, and do not raise non-permanence issues. Participants also felt that other issues need to be more fully explored, including ownership issues, discussion of what activities are considered as BAU, and a focus on buyers needs in addition to those of sellers.

### **6.3 Landfill Gas Options**

**Views on Proposed Options** - Participants expressed a strong preference for managing landfill gas emissions through an offsets system, as opposed to regulatory processes. The group identified a number of shortcomings with the regulatory approach:

- It leads to minimum behaviour, rather than the maximum;
- It targets new and additional facilities and activities, rather than existing ones;
- It benefits neither project operator nor the Large Industrial Emitter;
- It is time consuming and resource intensive to develop;
- It is a provincial/territorial responsibility, not federal; and
- There is little confidence that a nation-wide regulation/series of regulations could be enacted in time.

In discussing their preference for an offsets approach, the group noted that:

- It would provide an important incentive for maximizing behavior;
- It would be a more effective and efficient approach to achieving methane reductions from existing landfill sites, during the 2008-2012 period; and
- It would benefit both the project operator and those in the large industrial emitters Group.

In recognizing that the provinces will continue to regulate landfill sites to address issues of safety and odour, participants suggested that any beyond regulation “surplus” activity should be eligible for consideration under the offset system.

**Views on Key Design Factors** – Participants noted the need to clearly define the reductions that would be eligible for offset creation through projects funded under the Green Municipal Funds or the federal Infrastructure Program (i.e., application of the surplus criterion). The group recommended that the portion of the project funded by the project proponents themselves, beyond that funded by the federal or provincial governments, be considered eligible.

System start date was also recognized as an important design issue. Two participants noted that landfill gas capture activities had been initiated as early as 1992, in anticipation of a value being attached to the emission reductions. In order to recognize and credit early action, the group suggested:

- Investments in landfill gas capture made by large industrial emitters should be considered on a case-by-case basis, during negotiation of the companies' covenants; and
- A generic start date of January 1, 2000 should be set (Clean Development Mechanism start date) in cases where municipalities or other parties other than large industrial emitters made investments in landfill gas capture. Participants suggested that proponents who had made investments in landfill gas capture prior to this date be provided an opportunity to argue exemptions, on a case-by-case basis.

**Views on Basis of Determining Contribution to Canada's Kyoto Target** - Participants argued that this contribution should be zero. They suggested that such a contribution was essentially a tax, and would work against the desire for liquidity and lowest-cost approaches for large industrial emitters. Participants added that if the federal government deemed such a contribution necessary, then the government itself should purchase and retire landfill gas offsets.

**Views on Other Issues** - Participants noted that project baselines need to be fixed as of the project start date and should not be subject to revision based on future regulatory activity, since investments are determined based on the project lifetime. Participants agreed that landfill gas used to displace fossil fuel use in non-Large Industrial Emitter Group facilities should be eligible for offsets, as proposed in the Discussion Paper. Participants also suggested that electricity generation from landfill gas should also be eligible for offsets, given that such offsets represent an important revenue stream, estimated at 5-10% of total project revenues.

#### **6.4 Other Sectors**

**Views on Eligibility** - Participants noted the potential for offset creation in other sectors. However, it was felt that the \$15 price cap set for the large industrial emitters may limit potential. Others noted that the federal government, not the participants, was likely better placed to conduct the price sensitivity analysis. Moreover, the view was raised in plenary that the potential of the offset system overall should be assessed before implementing this policy option as opposed to another.

Participants stated that rules should not, de facto, exclude any sector from the offsets system and indicated interest in having renewables and energy efficiency/Demand Side Management (DSM) made eligible. Consideration needs to be given to which instrument (offsets, targeted measures) is best suited to stimulate investment and activity in renewables and DSM, and this will need to consider market conditions and the situation in particular provinces. There is a need to ensure that the Wind Power Production Incentive provides a transition, rather than a barrier, to inclusion of wind power in the offsets system. The federal government needs, nonetheless, to set basic rules and penalties in the design of an offsets system. One participant cited an existing eco-efficiency municipal fund in Edmonton that has been designed, at least in part, to benefit from being able to sell offsets.

Participants identified project opportunities related to:

- Transportation sector (e.g., collective efforts to capture individual avoided emissions with such schemes as “teletrip” trading, and community initiatives to reduce auto travel);
- Oil and gas sector (e.g., flare gas capture);
- Municipal sector (e.g., pooled energy use reductions by citizens);
- Geological sequestration of CO<sub>2</sub>; and
- Wind electricity generation (25 MT potential was noted from the previous work of the Electricity Table).

One specific project type was elaborated upon – development and marketing of a new fuel additive with the potential to reduce emissions from vehicle tailpipes. To capture the offset, three conditions would need to be fulfilled:

- Clear investment in this modified fuel by a company or other entity;
- The ability to track sales (although it is not necessary to know what type of vehicle is using the modified gas); and,
- A guarantee that the producer of this fuel retains the right to offset credits.

A protocol developed for gasoline additives under the PERT (Pilot Emissions Reduction Trading Program) initiative was cited as providing a potentially useful model for such schemes.

**Design Conditions** - Participants noted the need to identify and assess the range of risks for each sector, and to consider how to cover them. It was suggested that government’s role should be to set basic rules on who gets credit for what and rules for a dispute resolution mechanism, but then to leave questions of ownership of specific offset credits to the market.

## 5. CONCLUDING REMARKS

Appreciation was expressed to the federal government for consulting stakeholders and for the opportunity to provide input on offset system design options. The government was urged to consult on all other elements of the plan.

One participant suggested that the main message heard during the day was that the federal government needed to send the right signals and provide credit for early action, rather than developing a complex and rules-bound system to strictly address contributions to Canada’s Kyoto commitment. It was suggested that appropriate signals, enabling early investment and actions, would lead to widespread activity capable of closing the Kyoto gap.

With respect to next steps, the federal government indicated that it is planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).

## List of Participating Organizations - Calgary

Agcert International, LLC  
Agrium  
Alberta Agriculture Food & Rural Development  
Alberta Department of Energy  
Alberta Environment  
Alberta Newsprint Company  
Alberta Urban Municipalities Association  
ALPAC  
Atco Gas  
ATCO Power  
BP Canada Energy  
Canadian Climate Exchange Inc.  
Canadian Association of Oilwell Drilling Contractors  
Canadian Cattleman's Association  
Canadian Energy Pipeline Association  
Canadian Wind Energy Association  
Canadian Association of Petroleum Producers  
City of Calgary  
Encana Corporation  
EnerStrategies  
ENMAX Corporation  
Enwest Inc.  
EPCOR  
Federation of Canadian Municipalities  
Genesis Projects Corp.  
Graymont Limited  
Green Energy Technologies  
Husky Energy  
ICF Consulting Canada Inc.  
Imperial Oil Reserves  
International Emissions Trading Association  
International Institute for Sustainable Development  
Jacques Whitford Environment Ltd.  
Lake Wabamun Enhancement & Protection Association

## **List of Participating Organizations - Calgary (continued)**

Luscar Ltd.  
Nabors Canada  
Natsource  
Nexen Canada Ltd.  
Nodelcorp Consulting Inc.  
Nova Chemicals Corporation  
Nova Chemicals Ltd.  
PCS Potash  
Pembina Institute  
Petro-Canada  
Pricewaterhouse Coopers  
Producer Services Consulting Inc.  
Pyecombe Consulting Services  
Ron Quick & Associates  
Saskatchewan Environmental Society  
Saskatchewan Soil Conservation Association  
Shell Canada, Oil Sands  
Suncor Energy Inc.  
Teletrips Inc.  
Transalta  
TransCanada Pipe Lines  
Valdrew Environmental Services Ltd  
VisionQuest  
Western Barley Growers Association

# CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA

– SESSION REPORT –

Sheraton Wall Centre Hotel  
Vancouver, BC,  
June 24, 2003

## 1. INTRODUCTION

The fifth consultation session was held in Vancouver on June 24, 2003. There were 44 participants, including a range of industry sectors, business associations, ENGOs, individuals and service companies. Representatives from federal, provincial and municipal governments were also in attendance. The list of participating organizations is attached.

This report is a summary of views expressed at the Vancouver consultation. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## 2. GENERAL VIEWS ON THE CONCEPT AND PROCESS

A number of perspectives found general agreement among participants with respect to the concept and process:

- There is general support for a domestic offset system that provides incentives to invest in Canada and to buy domestic reductions/removals of GHGs (and not international reductions/removals). As an example of support, one participant stated that in his sector offsets will be needed to help achieve cost-effective emissions reductions targets at the plant level.
- Concerns were raised about the need for clarity in the connections between the various elements of the Federal Plan (e.g., large industrial emitters (LIE) System, targeted measures (TM) and the offset system). As well, a question was posed as to the relative costs and opportunities of an offset system compared to other approaches such as targeted measures.
- There were questions raised regarding how the domestic offsets system (and other components of the Federal Plan) fit with the international CDM/JI systems. For example, it was observed that the offset system proposed in the Discussion Paper seemed distinct from the CDM rules on verification etc.
- It was noted by a number of participants that the offset system proposed in the Discussion Paper gave only limited attention to offset activities in sectors that are key to the B.C.



economy including sectors that are key to achieving GHG reductions in the province such as commercial transportation.

- A number of participants sought clarification specifically about the proposed surplus criterion and how it would be applied to regionally significant emitters (e.g., pipelines fugitive emissions, and commercial transportation (which is the largest single GHG emitting sector in B.C.); and to existing GHG initiatives (e.g., Federation of Canadian Municipalities (FCM) funding, green infrastructure financing). In particular, a specific comment noted that the FCM Green Municipal Infrastructure Fund (GMIF) financing is predicated on offset sales. It was then asked whether the Green Municipal Fund financial plan is in jeopardy under an offsets scheme and if GMIF participants could sell their emissions reductions as offsets.

One participant noted an additional point -- the majority of the participants at the session have an interest in flexible rules, since they will benefit directly from participating in an offset system, while fewer participants have an interest in emission reductions solely for environmental reasons. Thus, the session comments should not be weighted by the numbers of participants supporting flexibility. The participant also noted that it should be ensured that the government and citizens do not have to assume the liability if flexible measures do not produce sufficient GHG removals and reductions.

### **3. VIEWS ON CROSS-CUTTING TOPICS**

#### **3.1 Principles**

There was general support for the principles listed in the Discussion Paper. Some views that emerged during the principles discussion included:

- There is a need for rigorous rules in the offset system to ensure that conflicts between the principles do not result, and to ensure credibility of Canadian offsets (To foster liquidity).
- There was strong support but not full support for Principle #3 (Contributing to the Kyoto commitment) and some participants argued that it should be the overarching principle for the offset system. That said, clarity about the meaning of equity within the context of the contribution to Kyoto between the sectors was sought. Another participant argued that there is no interest in a system that does not relate the offset credits directly to a real emission reduction in the national inventory.
- On the liquidity principle, one participant noted that scrutiny is required when applying the liquidity principle to ensure offset system credibility.
- Principle #4 (Incentive to invest in Canada) was supported by a number of participants. Regarding this principle, several points were raised:

The incentive to invest in Canada is already in place (i.e., with the 55 Mt LIE obligation) and that the offset system should not diminish this incentive.

It was noted that domestic action generates positive GDP impacts. Therefore, the federal government's position should be biased against the importation of international credits to ensure that the Canadian GDP impact stemming from domestic offsets is maximized.

There is a need to avoid artificial barriers to domestic investment in designing the offsets system.

- A new principle was proposed: minimize risk and maximize certainty. For example, it was pointed out that LIEs do not want to invest in purchase credits that have a higher risk than emission reductions in their own activities (operations). Therefore the offset system should not be designed to provide incentives for certain projects in certain sectors where the risks maybe high (i.e., offsets with non-permanence issues). If the system is designed to promote high risk offset projects, the LIEs will likely look to lower risk reductions using other mechanisms, including purchases of CDM reductions internationally.
- It was stated that there is a need for co-operation between the federal government and provincial and municipal governments in the design and implementation of an offsets system.

### 3.2 Eligibility

A number of participants noted problematic issues around **Start Date** and **Crediting Period**.

- It was suggested by a number of participants that the crediting period of 2008-2012 proposed in the Discussion Paper does not provide credit for early action and therefore results in a perverse incentive that will likely postpone investment action until 2008. It was suggested that the challenge for the offset system is to encourage early action and to reward early actors (including projects under such pilots as PERT/GERT). If this can be accomplished, it was argued, perverse incentives can be avoided. It was mentioned that it is difficult at this time to determine if a potential project should be implemented under existing programs such as PERRL, or if the investment should be postponed until it can be implemented under the offset system (which would have a different set of rules).
- It was noted that it would be useful to establish a crediting period so that projects with longer-time horizons that are already in the process of being initiated can be optimized to reduce GHGs. With respect to crediting beyond 2012, it was observed that many investments have longer time horizons, and the offset system should attempt to provide eligibility security beyond 2012, especially for projects (i.e., forestry projects).
- One participant suggested that the date of Canadian ratification of the Kyoto Protocol should serve as the start date.

With respect to the **Unique** criterion, it was stated that the offset system has the potential for double-counting, and that clarity is required to avoid this occurring.

With respect to **Ownership**, comments were:

- The ownership question as presented in the Discussion Paper is unclear.
- Contractual arrangements addressing ownership should have public oversight to ensure that the public interest is maintained.

- In the case of municipalities, buyers and sellers dispose of public resources, so the issue of ownership with respect to who has paid for what and when needs to be addressed in the offset system.
- It was argued that ownership of offsets should rest with the investor.

With respect to the eligibility criteria in general, it was suggested that having more sector and project types eligible would mean that there are fewer options for reducing Mt outside the 55 Mt target for LIEs.

Some participants argued that the scope of the offset system as proposed in the Discussion Paper is problematic. Specifically, the exclusion from the offset system of indirect emission reductions from demand side management (DSM), energy efficiency and co-generation projects was a source of concern. One participant argued that an offset system based on a least cost approach would need to include projects such as DSM and energy efficiency.

#### **4. ADMINISTRATION**

It was stated by a number of participants that existing systems should be used when designing the offset system, to ensure that transaction costs are minimized. For example, it was suggested that the system should mirror the CDM rules for international offsets to ensure the least amount of differences between trading systems; or that the Voluntary Challenge Registry (VCR) system could be upgraded for reporting purposes. This would reduce project transaction costs and ensure compatibility between mechanisms/systems. Another view was that the VCR is not an adequate model since the offset system would also require administrative authorities that do not exist in the current VCR.

A number of participants stated that there is a need to clarify the role and level of public involvement. On this point, there were differing views on the administrative role of the government versus the private sector in the design and implementation of the offset system. For example,

- Some argued that the role of government is to set up and audit the system and allow the private sector to administer as much of the system as possible with respect to verification and quantification.
- One participant suggested that a multi-stakeholder body be responsible for conducting project reviews, as was in the GERT process, would be preferred.
- Another participant expressed the need for the federal government to serve as a fully accountable offset authority. For example, only the federal government would be able to exchange the offset units for international valued units. Therefore, there is a need for federal government involvement at a level greater than just rule making and verification.
- One participant stated that a system open to public scrutiny would ensure credibility and promote self-corrections in the offset system over time.
- It was observed that increased certainty in the timing of an offset review process (including verification), and the need to credit annually, are both essential to ensure investment certainty. Therefore, the role of government should be to ensure an adequate structure to support the review process (e.g., clear criteria upon which to approve or reject a project proposal). There is a need for clear timelines for project review, comment

and decision-making. The clear set of timelines in the CDM process was noted as an example.

- With respect to information provided by proponents of offsets project and the question of confidentiality, one participant argued that there is a need to ensure as much information as possible is public, for example, with respect to baselines.

Further, some participants noted that the project review process should allow for feedback and modification during the review in order to keep the applications moving through the system. As well, it was argued that each project proposal should not be subject to multiple review processes, which would be inefficient and add uncertainty to investments. In addition, rules for an appeal process should be outlined.

## 5. DESIGN CONSIDERATIONS

It was noted that most of the calculations and rules for the offset system seem to be for large projects, but the size of eligible proponents in BC are small. Thus the system should recognize the differences in scale of projects. It was also noted that even under pooling, the transaction costs will likely be higher than for single emitters, and therefore, the system design must account for transaction cost burdens for pools or groups of offset sellers.

With respect to **non-permanence**, a number of differing views were raised touching on the question of liability:

- It was strongly stated by some participants that liability for non-permanence should not rest with the public. Under a public liability scheme, there is the potential for a significant downstream public subsidy with risky projects, such as those which provide non-permanent offsets. These participants emphasized that the buyers or sellers of offsets should be responsible for addressing non-permanence. It was suggested that if a subsidy is contemplated, it should be applied under targeted measures and not an offset system given that the transaction costs under the targeted measures are likely lower relative to offsets.
- Another participant stated that neither the buyer nor government should have to be concerned with non-permanence – the risk should fall solely on the seller.
- A different view was that government will need to guarantee approved offsets to foster investment.

In terms of managing non-permanence, participants showed an interest in temporary offsets and asked for further analysis and information on how such a system would work. One participant suggested that a replacement requirement would be the best means for addressing non-permanence.

A number of participants did not support the concept of a **contribution** by each offset sector/project to Canada's Kyoto target as proposed in the Discussion Paper. One reason cited is that such a contribution would involve double counting for the LIEs, where the LIEs would pay for their 55 Mt reduction plus the contribution from landfill gas and other sector offset reductions. As well, it was stated that such a contribution would create a perverse incentive for investments to be made internationally and not domestically.

## **6. VIEWS ON SECTORAL DESIGN**

### **6.1 Forestry**

On the question of which approach to baselines is preferred, the group felt that there is no clear preference for the without project versus base period approach. That said, most of the discussion centered on the without project approach, and three design considerations in particular:

- The without project approach provides appropriate incentives;
- Tools are available which can use existing information (i.e., managed versus unmanaged yields); and,
- Significant issues exist, including;
  - Developing realistic baselines; and
  - Ensuring appropriate oversight.

Under the base period approach, it was pointed out that the change in carbon stocks over time is not always clear and definable.

There was general support that avoided emission projects related to avoided deforestation should be included. However, concerns were raised over including other types of projects such as pest management and forest fire protection where baselines are difficult to establish. Finally, it was agreed that offsets may not be the best mechanism to motivate avoided emission projects and in particular, targeted measures or regulations may be more effective to encourage action.

With respect to the treatment of non-permanence, there was interest in the temporary credits option. However, it was stated that there is a need to better understand the impacts on project economics, including the impact of lower prices per tonne of carbon and deferred liability. As well, the offsets system needs to differentiate between non-permanence for planned reversals (harvest) versus unplanned (fire, insects) reversals. Other mechanisms may be of interest to address non-permanence, such as conservation easements and sustainable forest management liens.

Participants stated that there is a need for clear differentiation between implementation of Article 3.3 of the Kyoto Protocol (afforestation, reforestation and deforestation) and Article 3.4 (forest management) and that this separation should be clear in the Design Paper.

Finally, there is also a need for more discussion on non-carbon values and impacts such as biodiversity. Incorporation of Sustainable Forest Management (SFM) principles into offsets projects would help. One participant also noted that forest management projects should include a commitment to sustainable forest management.

### **6.2 Agriculture**

With respect to pooling versus independent producer options, it was noted that both approaches are desirable, and offset projects should not be limited to either one. Ideally, the decision to pursue either approach would be made at the farm level, and would be based on a farm level cost-benefit type assessment. Specific aspects of the two approaches include:

Positive	Negative
<b>Pooling</b>	
<ul style="list-style-type: none"> <li>• Spreads risk</li> <li>• Lower transaction costs including easier BAU estimates</li> <li>• Early adopter compensated for maintenance</li> </ul>	<ul style="list-style-type: none"> <li>• Lower return</li> <li>• Lower incentive for late adopters</li> </ul>
<b>Individual</b>	
<ul style="list-style-type: none"> <li>• Full financial benefit of action</li> <li>• Big farm size results in lower transaction costs</li> <li>• Captures changes in practices – measures baseline changes with new practices</li> </ul>	<ul style="list-style-type: none"> <li>• No record of BAU practices thus high transaction costs associated with BAU verification and validation at the farm level</li> </ul>

With respect to **membership criteria**, the membership in pools should not be limited or constrained. The reasons cited for open membership:

- Participation in the pools will only work if it is voluntary and farmers can assess the benefits. Therefore there is no need to apply criteria that limits membership;
- There is no common template that would fit all pools and circumstances;
- There is much precedence for pools and other groupings of farmers (i.e., co-ops) in agriculture, therefore lots of viable models;
- There is a range of possible types of aggregation in pools (e.g., by geography, farm type etc.) therefore limits should not be placed;
- Challenges of other provincial structure might complicate pooling membership (e.g., licenses and sharing equipment for vehicle licensing and shared ownership); and,
- Pool contracting can be effective at dealing with issues of exit/entry/non-performance etc.

A number of observations were made with respect to the independent producer approach and how changes in carbon stocks should be determined. These included:

- More tools are required to measure carbon stocks at the farm level;
- The average producer will be challenged to measure carbon stock independently. Therefore there is a role here for the federal, provincial and municipal governments to assist with protocol development and training; and,
- Farm size will influence the overall cost of completing stock assessments at the farm level (i.e., large farms will be able to achieve lower transaction costs per units of reduction/removal).

A number of additional comments were noted by the breakout group:

- With respect to the 60 Mt unallocated gap in the Federal Plan, it was argued that there is an opportunity for sinks and targeted measures for sinks to be used to help address the unallocated gap. This is particularly the case since the market may not demand the sinks offsets, and therefore targeted measures may be required to encourage sinks action outside of the offset system.
- Ownership of offsets is a significant issue given that land management and land ownership are highly separated in agriculture. Consequently, the ownership of offsets must be clarified.
- With respect to the risk of non-permanence, it was stated that leasing may be viable while insurance may not be feasible.

### 6.3 Landfill Gas

There was a strong preference for using an offset system rather than regulation of GHGs from landfills, given that this provides a market incentive for efficient reductions (i.e., a profit opportunity for landfills and least cost reductions for LIEs). It was also stated that designing regulations for the landfill sector would be complex and this is likely a provincial jurisdiction. Therefore, regulation of GHGs from this sector is not desired. The participants did suggest a complementary option that would involve financial incentives for LFG electricity generation.

A number of important design factors were identified:

- Options for a preferred start date ranged from when the LIE system is promulgated to crediting offsets immediately;
- With regard to the **surplus criterion**, it was agreed that clarity is required around the treatment of reductions under the pilots;
- Providing the rights **signals for action now** was agreed as an important principle of the offset system. It was stated that there is a high potential for reductions now and that offset system uncertainty is hindering the capture of more gas in the near term;
- Participants had different opinions regarding the principle of **contribution to Kyoto target**. Some felt it is a key principle while others argued to remove the principle on efficiency grounds; and,
- Different views were voiced on the basis for determining the **contribution level**. Some argued that there should be no direct contribution from the landfill gas sector to the Kyoto target since it conflicts with efficiency and is a disincentive to investment. Others argued that the contribution is valid and should be expressed as a percentage of the reduction so that small projects are not disadvantaged. As well, all sectors should be subject to the contribution to ensure equity.

Participants raised additional comments, including:

- Offsets are just one policy instrument, and there is a need to determine if different instruments are more cost effective; and,
- There is concern around administration costs that may be a barrier to small and rural municipalities to enter the offset system.

### 6.4 Other Sectors

The Other Sectors group expressed concern and confusion over the complexity of the offset system design proposed in the Discussion Paper and the exclusion of certain sectors and types of projects. For example:

- It is not clear which sectors are or are not covered by the covenants system and clarity is sought on this issue;
- With respect to ownership, a question was raised about who owns the credits generated under reduced energy demand projects. It was also noted that the distinction between electricity generation and other sectors does not reflect commercial realities; and,

- Finally, the start date and crediting period proposed in the Discussion Paper are both distant in the future, and it is likely that only large integrated firms can plan effectively for the offset system.

A number of specific project types were identified to have the greatest potential under the offsets system:

- Commercial transport – reverse trend from rail to road and provide emission reductions through inter-modal transportation;
- Forestry – biomass use (1-2 Mt available annually in BC);
- Offset internal emissions in integrated firms, including through small hydroelectricity generation;
- Off grid generation – diesel in remote communities;
- Urban energy efficiency and pooled transportation projects;
- Tree planting/conversion of built surfaces to carbon sinks;
- Green roofs/urban sinks; and,
- Municipal government DSM.

A number of important design elements or themes were identified including:

- There is interest in defining the contribution of targeted measures (existing and new) by sector to clarify the application of the surplus criterion and the inclusion of projects in the offset system;
- It was noted that innovation should be left to the market, and specifically, those who will buy and sell the offsets; and,
- The system should be cost-effective with low administrative and transaction costs; the feasibility of some projects will be determined by the burden of administration and compliance costs.

## **7. CONCLUSION AND NEXT STEPS**

With respect to next steps, the federal government indicated that it is planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).



## **List of Participating Organizations - Vancouver**

BC Agriculture Council  
BC Hydro  
BC Ministry of Forests, Economics & Trade Branch  
CarbonCorp Management  
Carbonforest  
Chemical Lime Company of Canada  
Crane Management Consultants  
CSQ Environmental Technologies  
David Suzuki Foundation  
Duke Energy Gas Transmission  
Environmental Intelligence  
Facet Decision Systems  
Fasken Martineau DuMoulin LLP  
GEMCO  
Global Change Strategies International  
Greater Vancouver Regional District  
Howe Sound Pulp & Paper  
Lamorna Enterprises Ltd.  
Lorax Environmental  
Lynn Ross Consulting  
Manitoba Department of Energy, Climate Change Branch  
McCarthy Tétrault  
NorskeCanada  
Regional District of Comox-Strathcona  
Regional District of Fraser-Fort George  
Sierra Club of Canada  
Soil Conservation Council of Canada  
Terasen Gas  
Timmenga & Associates Inc.  
University of British Columbia  
Vista Group  
West Fraser Timber Co. Ltd.  
Weyerhaeuser Company Ltd.

# CONSULTATIONS ON THE DESIGN OF A GHG OFFSET SYSTEM FOR CANADA

– *SESSION REPORT* –

**Delta Regina Hotel  
Regina, Saskatchewan  
June 26, 2003**

## **1. INTRODUCTION**

The Regina session was the final of six consultative sessions on the design of a greenhouse gas offset system for Canada. Approximately 40 stakeholders attended the workshop from a range of individual companies, industry associations, and non-governmental organizations. Representatives from federal, provincial and municipal governments were also in attendance. The list of participating organizations is attached.

This report is a summary of views expressed at the Regina consultation. No attempt has been made to edit or interpret those views.

The purpose of the consultation was to obtain the input of the varied participants in attendance. There was no attempt to reach a consensus among participants, though the report notes areas of general agreement.

## **2. GENERAL VIEWS ON THE CONCEPT AND PROCESS**

In general there was substantial support for a greenhouse gas offset system. However, some participants noted that significant clarification is needed with respect to various options and proposals for elements of the system described in the Discussion Paper. Several participants, including from the agriculture sector, indicated concern around the uncertainty surrounding the calculation of Business as Usual (BAU). Also, concern was voiced around the lack of recognition for offset projects beyond 2012. It was noted that a crediting period ending in 2012 will work against innovation and will make it difficult for proponents to plan and obtain financing for projects. It was emphasized that investors and company boards of directors need more certainty on longer-term returns.

Concern was expressed over the complexity of the offset system detailed in the Discussion Paper. Participants stated that the proposed system should be both simple and flexible, and some argued that the government role in administering the program should be limited. Program flexibility would provide incentives for innovation, and would encourage adoption of cost efficient solutions.

A proposal was made to provide transparency and equal treatment in determination of the BAU: to take a set percentage of existing GHG reductions or removals for each sector as the government's share – essentially as an “energy tax” – apply it transparently and evenly across sectors and sets of activities within a sector. This would provide clarity on reductions/removals

eligible for offset credits in past and existing activities and would provide a basis from which the market could operate more efficiently.

### 3. VIEWS ON CROSS-CUTTING TOPICS

#### 3.1 Principles

In general, there was wide support for the proposed principles of the offset system. However, several participants noted greater elaboration is required before the system can be made operational. Principles 2 (Open as practical) and 5 (Provide right signals for action) were regarded as being highly important to the overall success of the system, with strong support also being expressed for the third principle (Contribute to Kyoto commitment).

The following views on specific principles/concepts were also presented:

- **Enhance Market Liquidity** - With respect to the first principle, one participant emphasized the importance of ensuring fungibility among domestic and international markets, including the establishment of consistent trading rules. The market should also encourage participation from all scales and levels, even if the contributions appear small. The government should also recognize the environmental benefits in addition to GHG reductions/removals that can be achieved through private sector investment in offsets.
- **Open as Practical** - It was suggested that the rules associated with the offset system be developed and adapted over time to reflect actual market conditions as sectors become more adept at creating credits and as improved understanding is obtained through system operation.
- **Contribute to Kyoto Commitment** - One participant suggested that this is the most important underlying principle for the offset system.
- **Create Incentives for Investment in Canada** - It was recommended that the offset system be designed to encourage investment in the province/region and in Canada.
- **Provide Right Signals for Action** - One participant stressed the importance of avoiding perverse incentives, indicating that sectors with sinks capabilities have the potential to make positive or negative contributions.
- **Tradeoffs** - It was suggested that when contemplating tradeoffs, due consideration should be given to “maximizing the potential” reductions/removals of the system, with the greatest efforts being directed at options that will produce the greatest paybacks.

Several participants also recommended that additional principles or elaboration of the principles be adopted. These included:

- The principles for the proposed offset system should be consistent with and reflect the overriding principles of Canada’s Climate Change Plan, as well as the principles agreed to by federal and provincial/territorial ministers.
- The system should be *simple*, as a simpler administrative process would broaden and diversify participation in the offsets system, including for smaller businesses.
- The benefits of *pollution prevention*, as opposed to pollution management, should be stressed.

- Of particular importance is *uncertainty and risk* – particularly with respect to BAU calculation (e.g., what is BAU? What behaviours are and are not included? How can the correct signals be sent to proponents and the public?).
- The system needs to emphasize the importance of *equitable burden sharing* across geographical regions and to minimize unfair burden by any region. This is of particular importance for Saskatchewan, which will play a significant role in agricultural sinks creation.
- All sectors should be treated *fairly*; companies and/or individuals within each sector should also be treated fairly.
- The principles should support that a range of objectives being met, including the prevention and management of climate change in order to avoid negative impacts and create benefits to Canadian industry, improvements to quality of life and ecological integrity.

### 3.2 ELIGIBILITY

A wide range of views was presented with respect to the proposed eligibility criteria.

It was argued that the proposed limited credit period – 2008 to 2012 – raises serious investment issues. Many participants wanted to see early action recognized under the offset system and there was general agreement that perverse incentives should be removed in order to encourage proponents to invest in early action. It was cautioned that a short crediting period such as 2008-2012 could result in action avoidance prior to the 2008–2012 period. Some participants indicated that incentives are required to encourage immediate investment in long term offset projects, including the option of investment in futures markets. They proposed that project proponents be provided with the appropriate incentives for initial investment if the return on investment in a carbon offset project is uncertain beyond 2012.

There was considerable discussion about the surplus criterion and most participants agreed that greater clarity was required. Some of the key questions included:

- Will projects that receive partial funding from provincial and municipal governments be ineligible under the proposed system? Or, will eligibility be contingent upon the level of funding received (e.g., if 25% of the project is funded by municipal government, is 75% of the project still eligible under the offset system)?
- How can surplus actions be disaggregated from BAU activities?
- Should the effects of perverse incentives be recognized in baseline calculations?
- Are non-CO<sub>2</sub>e reductions that contribute to climate change objectives eligible under this system (e.g., water vapour)?

With regards to the surplus criterion, one key area of discussion was the relationship between voluntary programs and the carbon offset system. The Green Cover program, for example, is directed at agricultural operations, and is designed to contribute to larger biodiversity and environmental quality objectives. However, participation in this program may require participants to forfeit their rights to sell carbon credits in the future, and it was suggested that this would place some of the more innovative farming operations at a distinct disadvantage in the offset market. Several agricultural operations have signed contracts to undertake actions designed to meet environmental objectives, but parties to these agreements are, for the most part,

not aware of the implications for offsets with respect to their participation in the Green Cover program. To resolve this issue, it was suggested that farmers be informed of the implications of their participation in the Green Cover program in the context of the offsets system, and that contracts should explicitly state the number of carbon credits that will be created through participation in the Green Cover program. Increasing transparency associated with participation in the Green Cover program will allow farmers to (i) determine what activities will qualify as surplus in the future; and (ii) compare the benefits of participation in the Green Cover program with the potential benefits of participation in the carbon offset market.

One participant suggested that the criterion related to ownership will form the foundation of the carbon offset system and is the most important criterion. The system will create a new type of property that should be accompanied by appropriate ownership mechanisms, and efforts should be made to graft this new type of property into existing property registry systems. Legal clarity is needed on what type of property will be created by the offset system. With respect to options for ownership, one participant advised that a contract-based approach should be used.

The need for cooperation among levels of government – municipal, provincial/territorial, and federal – was raised. Such cooperation would be needed to avoid “double jeopardy” in terms of regulatory requirements.

#### **4. ADMINISTRATION**

**Governance** - A number of participants recommended a mixed approach to governance. This model would place primary responsibility for arranging transactions with the private sector, with government setting rules and providing an oversight role, as required. It was suggested that verification should be conducted by third parties, and dispute resolution and enforcement mechanisms should be established by government to ensure effective operation of the system. There was also some preference expressed for a coordinated national system rather than a federal plus a series of provincial systems.

**Registries** - Several participants emphasized the need to integrate existing provincial and territorial programs (e.g., Alberta’s system for coal generators) within a larger national program. In contrast, one participant suggested that jurisdictional sub-units should be permitted to operate their own systems. One suggestion was to upgrade the VCR registry system.

**Early Issuance of Credits** - Several participants expressed concerns over the option in the Discussion Paper of early issuance of credits. Of paramount concern was the risk of non-delivery within the crediting period, and the lack of certainty beyond 2012. One participant suggested that the risk of non-delivery could be reduced by including carbon credits as property in land titles/securities systems.

**Transition** - There was support expressed for an initial voluntary period/lead up program to be established prior to 2008 to provide both government and industry with the opportunity to test the program and make necessary adjustments before the system is finalized.

## **5. DESIGN CONSIDERATIONS**

Non-permanence of sinks was seen as an important issue to address. Some participants, particularly from the agriculture sector, expressed support for the establishment of temporary credits, largely because of the limited liability timeframe. They also suggested that temporary credits could be attractive to buyers of offsets among the large industrial emitters – particularly if a facility will be able to reduce its emissions in the future by installing new technology or modifying industrial processes. Under this scenario, an industrial facility would be interested in purchasing a temporary credit to maintain compliance until it has made the necessary reductions in emissions. However, an opposing view was also presented: one participant indicated that the transaction costs associated with purchasing a temporary credit would outweigh the benefits. It was suggested that the market be left to cope with non-permanence, although there was also a view that government may have to provide a backstop for unforeseen events.

Participants also requested clarification regarding leakage, the treatment of indirect emissions within baseline calculations, as well as the eligibility of fuel switching projects. There was also a question concerning the eligibility of a mechanism capable of removing CO<sub>2</sub> directly from the atmosphere (i.e., can credit be received for activities that fall outside of reduction or removals activities?).

One participant also recommended that the transportation sector, as a significant sector in climate change, be included in the broader discussion – particularly with respect to indirect emission contributions.

## **6. VIEWS ON SECTORAL DESIGNS**

### **6.1 Forestry**

Members of the forestry discussion group focussed their discussion on baselines in afforestation and reforestation projects. They suggested that the “without project” approach represented the best option for baseline determination (most flexibility; equitable; allows for adjustment of base period). It was proposed that the “without project” approach include a base period method as one of the possible methods that could be used under this approach.

With respect to eligibility of avoided emission projects, it was noted that these projects could face particular difficulties in establishing baselines, but the discussion group recommended that these projects not be excluded from the system. Proponents should be provided with the opportunity to develop credible methodologies capable of quantifying changes resulting from these projects. If successful, the projects should be eligible for credit under the proposed system.

In addition, the group agreed that a wide range of approaches was necessary to address issues associated with permanence. There was mixed views on temporary vs. replacement credits, with some participants demonstrating a clear preference for temporary credits, and others showing support for replacement credits. However, it was generally agreed that both credit types have their respective strengths, depending on the specific situation.

The group also had a lengthy discussion concerning the establishment of suitable timeframes for replacement and insurance. It was agreed that further clarification is needed before the system is finalized.

The following views were also raised:

- The system should recognize the full range of forest values, rather than focusing solely on carbon. One participant suggested that forest management projects will never be done solely for carbon benefits, so it is important that other forest values are included in consideration of these projects. Land management plans should include mechanisms to enhance and/or maintain all resource values, including biodiversity, economic development and water quality.
- Incentives should be provided to encourage investment in projects with long-term benefits.

## **6.2 Agriculture**

Most members of the group expressed a preference for the pooling approach (as opposed to the independent producer approach). Pooling offers lower transaction costs, and can draw on existing institutional structures (e.g., crop insurance). It was also suggested that pooling could help solve issues associated with permanence, saturation and perverse incentives. Membership criteria could be established by privately developed pools, and could include protocols related to specific conservation objectives.

Although pooling was the preferred method, it was also suggested that the independent producer approach should remain an option. Aggregation is still possible under this alternative, and could include the establishment of standard protocols (e.g., regional averages).

Concern was also raised that the proposed system might encourage early adopters to switch back to conventional practices prior to the first crediting period. To counter these concerns, it was suggested that: (i) an early start date be established; and (ii) payment be provided for maintenance (using 1990 as a baseline).

The group noted that the BAU projections in the federal government's analysis for agricultural sinks are dependent upon the continued performance of maintenance activities through agricultural and soil management practices. As currently prepared, the offsets system would not provide credit for such maintenance activities.

The group therefore considered a third option, which places an emphasis on "maintenance". This option is designed to:

- Remove perverse incentives
- Include activities that have already been completed (since 1990)
- Raise awareness of other programs/Targeted measures (TMs).

The essence of this option is that BAU sinks would be eligible for offset credits, while sinks that go beyond BAU would be used against Canada's Kyoto target.

Participants also considered that offset credits could be divided into: permanent offsets (e.g., reduction of emissions); and non-permanent offsets (e.g., sequestration, avoidance of emissions).

The following views were also raised:

- Clarity is needed on whether liability will be associated with the land, or the owner of an offset credit.
- When calculating changes in carbon stocks under the independent producer approach, consideration should be given to non-CO<sub>2</sub> reductions.
- Biotechnology is an extension of the agricultural sector, and its inclusion is vital if the whole system is to work. If the industry cannot be supported through the offset system, then support should be provided through some other mechanism(s).
- Further research on sequestration options is also encouraged.

### **6.3 Landfill Gas**

There was broad support for including landfill gas activities in the offset system, rather than regulating GHGs from landfills. Inclusion in the offsets program would provide incentives for innovation, as well as revenue opportunities for municipal landfills. Inclusion in the offset program was also noted to be better suited to encourage the participation of small and medium sites.

It was recognized that provincial authorities would continue to regulate safety and odour issues associated with landfill sites.

There was concern that the crediting period is too short relative to the lifespan of landfill emission projects. Furthermore, it was noted that there should be certainty surrounding the start date (as early as possible), and that recognition should be given for early action (failure to reward early action will create perverse incentives).

The following views were also raised:

- If a contribution to meeting Canada's Kyoto target is to be applied, it should be applied equitably across all sectors earning offsets.
- Other options for the landfill gas sector, including waste management and pollution prevention approaches, should be eligible and encouraged through the provision of incentives

### **6.4 Other Sectors**

In general, participants felt that all relevant sectors should have an opportunity to participate in the offsets system. The system should be simple enough to allow other sectors and project types not described in the Discussion Paper to be eligible for offsets. This could include projects such as:

- Biomass in the forestry sector – both as a fuel in internal generation and for electricity generation
- Co-generation
- Waste heat



- Integrated forest industry/activities not covered by the LIE covenants (e.g., related to the transportation of product)
- Community-based housing initiatives (group of homeowners pooling reductions and selling as offsets)

Greater clarity is needed with respect to the structure of the federal plan, and how all components fit together. There should be a clear understanding of how targeted measures will fit into the overall plan, and how administrative costs will be minimized in order to facilitate broad participation, particularly for SMEs that may require additional incentives.

The following views were also raised:

- Credit for early action should be included in the offset system; and
- Fuel economy and other transportation contributions should be recognized under this system.

## **7. SUMMARY COMMENTS**

General comments from participants concerning the day's proceedings included:

- A number of participants expressed appreciation and satisfaction with the consultation process.
- The focus should be on moving the climate change agenda forward, rather than just using credits as incentives for action.
- Saskatchewan should not be systematically disadvantaged in the common goal of reducing emissions.
- Companies should not be penalized (in terms of losing access to offset credits) for actions they take to meet provincial government regulations or for participation in provincial climate change programs beyond that which is included in the Climate Change Plan.
- Integrated systems analysis should be included within the offset system.
- Renewables should be recognized within the offset system.
- Canada should establish rules and approaches that allow for linkages to the U.S. approach at the federal and state levels.
- Participants from the agricultural sector were encouraged by the proposed flexibility associated with carbon sequestration projects, as it provides incentives for investment.
- There should be incentives for domestic credit creation.
- The private sector, as buyers, will play an important role in validating offset projects; government should refrain from over-regulating this process.
- Early action should be encouraged, regardless of whether or not it will be included in the offset system.
- Research and data requirements should be defined up front to encourage investment in research and development.
- The offset system should be supported by adequate training and investment in resources.

## **8. CONCLUSION AND NEXT STEPS**

With respect to next steps, the federal Government indicated that they are planning to integrate stakeholder inputs over the summer into a detailed proposal for the design of an offset system. Written comments are invited and encouraged, and should be submitted to [consultations2003@ec.gc.ca](mailto:consultations2003@ec.gc.ca). More information on submitting written comments can be found at [www.climatechange.gc.ca](http://www.climatechange.gc.ca).

## **List of Participating Organizations - Regina**

AgCert International, LLC  
Agricultural Producers Association of Saskatchewan Inc.  
Centre for Studies in Agriculture, Law and the Environment  
City of Regina  
Ducks Unlimited Canada  
EBA Engineering Ltd.  
IMC Potash  
International Institute for Sustainable Development  
Keystone Agricultural Producers  
Louisiana-Pacific Canada Ltd.  
Pulse Canada  
Saskatchewan Agriculture, Food and Rural Revitalization  
Saskatchewan Association of Rural Municipalities  
Saskatchewan Environment  
Saskatchewan Government Relations and Aboriginal Affairs  
Saskatchewan Industry and Resources  
Saskatchewan Mining Association  
Saskatchewan Potash Producers Association  
Saskatchewan Power Corporation  
Saskatchewan Soil Conservation Association  
Saskatchewan Urban Municipalities Association  
Saskatchewan Executive Council  
Soil Conservation Council of Canada  
TransAlta Corporation  
University of Saskatchewan

## APPENDIX E SUMMARY OF SESSION ATTENDANCE

	<b>Sellers</b>				<b>Buyers</b>	<b>Intermediaries</b>	<b>Xcutting</b>	<b>Provincial Government</b>	<b>Totals</b>
	<b>Forestry</b>	<b>Agriculture</b>	<b>Landfill</b>	<b>Other</b>					
<b>Toronto</b>	3	1	1	6	21	16	20	7	<b>75</b>
<b>Montreal</b>	6	5	2	1	5	5	5	8	<b>37</b>
<b>Halifax</b>	4	3	0	0	7	1	5	9	<b>29</b>
<b>Calgary</b>	2	3	3	3	31	9	16	5	<b>72</b>
<b>Vancouver</b>	6	1	3	0	5	8	20	3	<b>46</b>
<b>Regina</b>	1	4	4	0	6	2	8	11	<b>36</b>
<b>Totals</b>	22	17	13	10	75	41	74	43	<b>295</b>

## **APPENDIX F LIST OF WRITTEN SUBMISSIONS**

1. Ontario Clean Air Alliance
2. Voluntary Challenge & Registry Inc.
3. Marion Hill
4. Regie de gestion des matières résiduelles de la Mauricie
5. Independent Power Producers' Society of Ontario
6. Sempa Power Systems Ltd.
7. ecoStrategic Group
8. Ville de Québec
9. Teletrips Inc.
10. Saskatchewan Association of Rural Municipalities
11. Government of Alberta - Sustainable Resource Development
12. Climate Change Central
13. Alberta Urban Municipalities Association
14. Vestas Canadian Wind Technology, Inc.
15. J.D. Irving, Ltd.
16. K.J. Plourde
17. Landfill Gas Industry Alliance
18. Natural Forces Technologies Inc.
19. Manitoba Hydro
20. Canadian Climate Exchange Inc.
21. Suncor Energy Inc.
22. Ducks Unlimited Canada
23. North American Carbon Canada Inc.
24. Canadian Gas Association
25. Peter Ormand, Mohawk College
26. Saskatchewan Power Corporation
27. Sea Breeze Energy Inc.
28. Computare
29. Earth First Energy Inc.
30. Earth Energy Society of Canada
31. Clean Air Renewable Energy Coalition
32. Independent Power Producers Society of Ontario (#2)
33. Federation of Canadian Municipalities
34. Green Municipal Funds Council
35. Siobhan Baker
36. Just Geothermal Systems
37. Agricultural Producers' Association of Saskatchewan
38. AgCert Canada
39. AgCert Canada (#2)
40. Mancini, Saldan & Associates Ltd.
41. Forest Carbon Management (FCM) Pilots Series
42. Canadian Wind Energy Association
43. Nova Scotia Power Inc.
44. Canadian Association for Renewable Energies
45. Climate Change Solutions

46. Shell Canada Limited
47. Clean Air Canada Inc.
48. Climate Action Network – Canada
49. Bruce Power
50. Canadian Fertilizer Institute
51. Pollution Probe
52. Pembina Institute
53. Forest Products Association of Canada
54. BC Hydro
55. Pristine Power Inc.
56. Canadian Cattlemen’s Association
57. BIOCAP Canada Foundation
58. Canadian District Energy Association
59. Canadian District energy Association (#2)
60. David Suzuki Foundation
61. Canadian Association of Petroleum Producers
62. David Tamblyn
63. Canadian Hydropower Association
64. Carl Chaplin
65. CellFor Inc.
66. Saskatchewan Soil Conservation Association
67. Western Canadian Offsets Team
68. Independent Power Producers Association of BC
69. MCW Consultants ltd. And Borealis Infrastructures Management Inc.
70. UPM-Kymmene Inc.
71. Government of Nova Scotia – Department of Energy
72. Lorax Environmental
73. EPCOR
74. Ed Lohrenz
75. Ontario Waterpower Association
76. JFBioEnergy Inc.