

Carbon Market North America

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NEWS

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EPA ruling pressures Congress, makes waves in Copenhagen

Hours after negotiators descended upon Copenhagen's Bella Centre for the start of UN climate change negotiations Monday, Environmental Protection Agency (EPA) Administrator Lisa Jackson made waves across the pond when she announced her agency is now "authorised and obligated" to regulate greenhouse gas emissions under the Clean Air Act.

The EPA officially determined Monday that greenhouse gases pose a threat to public health, a move that gives it the ability to use the existing federal regulations to regulate the heat-trapping emissions.

"These long-overdue findings cement 2009's place in history as the year when the US government began addressing the challenge of greenhouse-gas pollution and seizing the opportunity of clean-energy reform," Jackson said at a press conference Monday.

But she emphasised that EPA rules are no substitute to the passage of comprehensive energy and climate legislation.

"Legislation is the best way to move our country forward on a clean economy," Jackson said, noting it gives businesses "absolute certainty" needed for their investments.

"I do not believe this is an either/or proposition. I see this as a both/and," the administrator added.

Jackson added EPA rules on carbon dioxide would be designed to "complement" a comprehensive climate cap-and-trade bill.

"We look forward to working with Congress to get a bill to the president's desk," she said.

The administrator added the endangerment finding serves as the "legal foundation" for finalising regulations proposed this spring that would require automakers to set higher fuel economy standards for their new fleet of vehicles.

It also supports a proposed regulation, expected to be finalised next spring, that would require mobile sources of

greenhouse gases to use the "best available control technology" for carbon when they build or expand new operations.

Senator John Kerry, a Democrat who is seeking to propel bipartisan climate legislation (see page 3), said Monday that the EPA announcement gives Congress a shot in the arm.

"The message to Congress is crystal clear: get moving," he said in a statement. "Given the potential for agency regulation, those who now aim to grind the legislative process to a halt would later come running to Congress to secure the kinds of incentives we can pass today."

The ability of the EPA to regulate CO2 and other greenhouse gases as a backstop measure if legislation doesn't materialise can strengthen the US position at the UN climate summit, others contended.

"In addition to the (US) target, the other thing the president brings to Copenhagen is the EPA and its authority under law to regulate to stop global warming emissions. It's a very powerful tool," Senator Joe Lieberman said.

Angela Anderson, programme director for the US Climate Action Network who is currently in Copenhagen said: "In the absence of US legislation, the administration is working hard to make clear to nations gathered in Copenhagen that it has the will and a way to meet its commitments to reduce its global warming pollution."

But the main opponent of climate change legislation in the US Senate, Republican Senator James Inhofe, remarked that EPA regulation of greenhouse gas emissions would be a job killer in the US.

"The administration's endangerment finding will lead to a wave of new regulations and bureaucracy that will wreak havoc on the American economy, destroy millions of jobs, and force consumers to pay more for electricity and gasoline," the senator said

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RGGI exchange snapshot (\$)

Exchange	Contract	Settle	Change
CCFE	Dec 09	2.08	0.02
CCFE	Dec 10	2.02	-0.07
Nymex	Dec 09	2.08	0.02

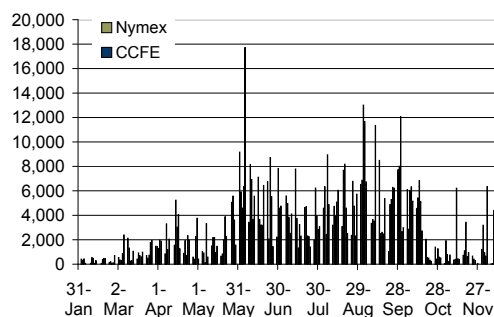
Point Carbon RGGI OTC assessment (\$)

Contract	Best bid	Best offer	Close	Change
Dec 09	2.07	2.10	2.08	0.03

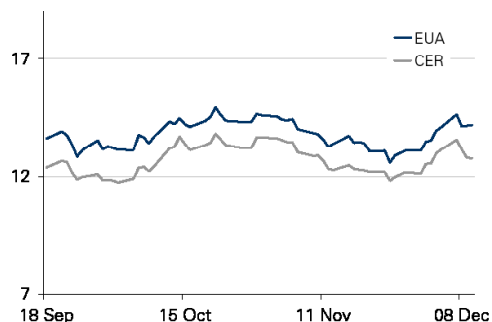
Source: Evolution Markets, Icap and TFS.

Quoted prices are \$US per short ton of at close of market each Thursday as per Point Carbon's RGGI assessment methodology. Changes refer to the last issue of Carbon Market North America.

For methodology, see www.pointcarbon.com/news/methodology

Exchange volumes ('000) all RGGI contracts

Source: CCFE and Nymex

2009 European and CER prices (€)**Market comment**

RGGI rose 1 per cent following last week's higher-than-expected allowance auction results. The benchmark December 2009 contract closed at \$2.08 on the Chicago Climate Futures Exchange (CCFE), up 1 per cent on its close a week ago.

The contract's brokered bid and offer were \$2.07 and \$2.10, respectively.

The price of RGGI benchmark allowances has hovered in the \$2.08-\$2.12 range following the release of last Wednesday's quarterly allowance auction results.

On Friday, RGGI announced its member states had sold all of the 28.6 million 2009 allowances that were up for auction for \$2.05. They also sold a portion of vintage 2012 allowances for the minimum bid price of \$1.86.

The auction was oversubscribed with demand for 2009 allowances 2.6 times higher than available supply.

The clearing price for the 2009 allowances was slightly higher than market participants expected. Many had predicted the 2009 allowances would clear at or close to the minimum bid price of \$1.86.

Some analysts had also forecast the auction would be undersubscribed given the fall in emissions in the RGGI region.

RGGI benchmark allowances rallied 3 per cent to \$2.13 after the release of the results.

A broker said the current bid support for December 2009 allowances reflects the slightly bullish results of last week's auction.

"There is bid support at these levels because the auction result was a little higher than people thought," said the broker.

The bulk of this week's trading volumes consisted in spread trades between the December 2009 and December 2010 (vintage 2009) contracts.

Many market participants continue to roll out of the December 2009 contract, which expires at the end of this month, to buy the December 2010 contract in order to lock in the spread between the two. The current spread between the two contracts is around 5 cents.

The majority of contracts changed hands last Friday and Wednesday and Thursday this week.

Meanwhile, trading activity was extremely low on Monday and Tuesday with only 52,000 allowances changing hands on the CCFE.

RGGI states will sell their next batch of allowances in the next quarterly auction on 10 March 2010.

UN unveils new texts, no market rulings

Two texts issued at the UN climate summit in Copenhagen by the chairs of the two main negotiation tracks are positive for the continuation of key elements of the Kyoto protocol.

The chairs issued the working texts Friday morning, and made a pledge to cut emissions from industrialised countries by between 25 and 45 per cent under 1990 levels by either 2018 or 2020.

The Kyoto protocol text (KP), which was introduced by the chair of the group John Ashe, suggests that countries with a target under the 1997 pact should cut "their overall emissions... within the range of [30 to 45] per cent below 1990 levels."

The brackets in the text indicate they are yet to be agreed by all parties, something that needs to occur before the end of next week if the proposals are to survive.

Meanwhile, Michael Zammit Cutajar, the chair of the UN track that includes the US (LCA), presented a working text that states industrialised nations as a group should cut their emissions slightly lower - between 25 and 45 per cent under 1990 levels by 2020.

The text states global emissions should be cut by at least 50-95 per cent under 1990 levels by 2050, with developed countries cutting their emissions 75-95 per cent over the same time period.

However, the document does not set a mandate to negotiate a legally binding treaty, leaving the option open that the US may not be legally bound under the UN to cut greenhouse gases.

Martin Kaiser Greenpeace International's climate policy advisor, said: "It is imperative that they strengthen it considerably and fill in the gaps so that it produces the legally binding deal that averts climate chaos."

There is no mention of individual country targets in either paper, but the LCA draft states targets pledged by countries with goals under the Kyoto text will be enshrined in this draft, suggesting the survival of the treaty.

A US target will also be published.

For developing countries, the text states they should ensure a "substantial deviation in emissions [in the order of 15-30 per cent by 2020]" under business as usual levels.

To help them do so it says developing nations should undertake "national appropriate mitigation actions"; and it also suggests that these actions should be registered in an international registry.

The drafts are the first working texts to come out of the negotiating streams and much is still to be discussed before they can be adopted by leaders next week.

Kaiser said the text left the door open for a legal outcome, which, along with the numbers, is what negotiators must now focus on.

Under the Kyoto draft, the proposal makes reference to a raft of key decisions on whether to include carbon capture and storage, nuclear, standardised baselines and discount factors in the clean development mechanism.

However, the paper gives at least two options for each of the issues – mainly whether to accept or reject them.

The Kyoto paper also leaves open the option of whether to limit the banking of government emission rights from the first commitment period ending in 2012 into a second period.

It also makes no decision on whether to extend the share of proceeds levy, currently applied to the CDM, to the issuance of assigned amount units (AAUs), although it has bracketed text suggesting that between a levy of 0.5-8 per cent should be applied.

It now appears that any decision on sectoral approaches will be made in the negotiating stream that includes the US, giving the world's second biggest emitter more of a say in the development of future markets.

The LCA document states all decisions on market mechanisms and measures to cut emissions on shipping and aviation have still to be elaborated on.

For more on the UN climate treaty negotiations currently underway in Copenhagen, please follow Point Carbon News at <http://www.pointcarbon.com/news/post2012>.

Kerry-Graham-Lieberman bill to set 17% GHG target

A compromise bill under development by Democratic Senator John Kerry, Republican Lindsey Graham and Independent Joe Lieberman would set a 17 per cent emission reduction target below 2005 levels by 2020.

The target is 3 per cent lower than the one set in the cap-and-trade bill Kerry co-authored with environment committee Chairwoman Barbara Boxer, which passed out of her committee in November.

The 17 per cent target matches the one in the House-passed Waxman-Markey bill, and mirrors the target proposed by the Obama administration at the UN climate treaty negotiations underway in Copenhagen.

The 17 per cent target means the US can emit 640 million more tonnes of CO₂e between 2012 and 2020 than it would have under the 20 per cent target, according to Point Carbon Research.

The legislative trio is currently drafting a compromise energy and climate change bill that can attract at least 60 votes in the Senate.

On Thursday they released the "legislative framework" of their future bill, which is expected to incorporate an energy bill that already passed out of the energy committee, and the cap-and-trade bill that passed out of the environment panel.

Kerry told Point Carbon News that the senators agreed to soften the Kerry-Boxer target due to concerns raised by finance committee Chairman Max Baucus that a 20 per cent target was too ambitious.

Earlier in the week, a Senate staffer said Baucus had planned to propose an amendment that would lower the target in the Kerry-Boxer bill from 20 to 17 per cent when the bill was being debated in early November.

But if other major emitting countries are deemed by the US president to be taking comparable action to reduce their emissions, the target would be raised to 20 per cent.

"The idea is to establish a two-tiered carbon reduction target," said the staffer, who noted the idea is based on policy already adopted by the EU.

The EU has said it will up its 2020 target from 20 to 30 per cent below 1990 levels if it determines other countries are making strides to slash emissions.

Baucus' finance panel is one of three Senate committees Kerry expects will contribute to the bill.

His committee, as well as the agriculture and commerce committees, are all expected to hold hearings on climate and energy legislation early next year, Kerry said.

Another senate staffer said it was still unclear whether any of those committees would write additional pieces to contribute to the bill, or simply provide input into the work being done by Kerry, Graham and Lieberman.

The senators also sent a letter to President Barack Obama telling him that momentum was growing in the Senate toward passage of a comprehensive energy and climate legislation.

"Well over 60 members of the US Senate are in play," Lieberman said, but noted they had "a lot of work to do" before they secure the votes for the bill.

Kerry said Senate Majority Leader Harry Reid would bring the bill up for debate on the Senate floor in "early spring".

The White House released a statement Thursday commending Kerry, Graham and Lieberman for taking "another significant step in the effort to pass comprehensive energy reform" with the release of their framework.

"The president believes this is a positive development towards reaching a strong, unified and bipartisan agreement in the US Senate," White House Press Secretary Robert Gibbs said.

EPA regulation should enable offset use, experts say

Even if Congress fails to pass a climate law, offsets can still play a role in a regulatory system, US climate policy watchers contend.

The Environmental Protection Agency's (EPA) determination this week that greenhouse gases (GHG) endanger public health (see front page) moves the agency a step closer to policing emissions from power plants, factories and oil refineries that emit more than 25,000 tonnes of GHG emissions per year.

Kyle Danish, an attorney with Van Ness Feldman, said if the regulations take effect, the EPA could preserve the offset system proposed in bills pending in Congress by allowing facilities to use offsets to meet EPA requirements.

First, he said facilities approaching the EPA's 25,000-tonne threshold could be allowed to purchase offsets to avoid triggering regulation of their facility.

Danish also said the EPA could allow facilities that emit more than 25,000 tonnes to use offsets to count towards their best available technology (Bact) requirement, an obligation the EPA is likely to enforce.

The EPA has not yet said what constitutes Bact for GHGs. Technologies like carbon capture and sequestration for power plants are not yet commercially viable.

"For many types of facilities, there are no control technologies that are commercially available," Danish said. "In those cases, allowing the facility to use offsets ensures that the programme will still generate emission reductions."

Danish, who is also counsel for the Coalition for Emission Reduction Projects (Cerp), said the offset lobby group may raise these ideas when it submits comments to the EPA in the coming weeks.

But he added that even if the EPA adopted those recommendations, offset demand would be less than it would be under any of the major bills before Congress. The EPA did not return calls seeking comment.

David Hunter, director of public policy for the International Emissions Trading Association, said the EPA would come under pressure from businesses to allow offsets to lower compliance costs if the agency were to regulate GHGs.

"The EPA will be under a lot of pressure to include cost-control provisions, the primary of which is offsets," he said. "The EPA is not looking to come out with a rule that will increase costs for consumers or businesses."

A spokeswoman for American Electric Power (AEP), one of the nation's largest emitting utility companies, said the company would back efforts to allow for the use of offsets

for compliance under an EPA regulatory system.

"It doesn't make sense to spend more money to achieve the same environmental benefit," said Melissa McHenry. "If you can do that less expensively through offsets than through the retrofit of a power plant, then that makes sense to us."

But some policy watchers are sceptical that the EPA would ever be open to a proposal like Danish's.

"In our view, offsets are as close to a mechanism for fraud as you can possibly get," said David Bookbinder, chief climate counsel for green group the Sierra Club.

"The idea that you would use these things to escape regulation or to meet compliance obligation is just nonsensical," he said, adding there was "no way in hell" the EPA would agree to those terms.

Canada seeks to change Kyoto baseline

Canada said countries should use "more contemporary" base years to measure emission cuts at a working group on rich country commitments in Copenhagen this week.

Canada proposed changing the legal baseline year for reducing global GHGs from 1990 to later years.

Michael Martin, Canada's chief climate negotiator, said in a conference call this week that Canada is proposing a 2006 legal baseline year by which to measure GHG reductions, while other parties have put forward other later baselines.

"There have been discussions in an ad hoc working group on how to define commitments to follow 2012," said Martin, referring to the year the Kyoto protocol runs out.

"In the Kyoto system, these would translate into an absolute [emission reduction] amount," he said.

When the Kyoto protocol was created in 1997, 186 countries agreed to reduce their emissions by an average of 5 per cent between 2008 and 2012 using 1990 as a baseline. Canada agreed to a 6 per cent cut but has already conceded it would not try to meet the treaty's goal. In 2007, Canada's emissions already soared 33.8 per cent above its Kyoto target of 558 million tonnes.

In talks on a successor treaty to Kyoto, some countries have proposed scrapping the 1990 baseline year in favour of an agreement that includes a range of baseline years for targets enshrined in countries' mitigation plans.

Canada's proposal to use 2006 as a baseline year, when it emitted 718 million tonnes of CO₂e, would make it much easier to meet its pledge to cut emissions 20 per cent by 2020. This target equates to only a 3 per cent reduction below 1990 levels by 2020.

Canada's 2020 target is in line with the US proposal to cut emissions 17 per cent below 2005 levels by 2020, which also translates roughly into a 3-4 per cent cut below 1990.

Canada is seeking to align its environmental regulations with those of the US and will not enact domestic regulations until the US passes its own climate legislation.

RECENT GLOBAL CARBON POLITICS

The European commission formally rejected the national allocation plans (NAPs) of **Poland and Estonia** and requested Friday that they to come up with revised plans, according to the EU executive's web site. The commission wants the new NAPs to use 2008 data, which could mean the countries end up with a lower emissions cap under the 2008-2012 phase of the EU emissions trading scheme (ETS) than previously.

Over the past 18 months, **fraudulent transactions** in the EU ETS resulted in losses of around €5 billion (\$7.4 billion) for several national treasuries, European police agency Europol said in a statement this week. And in some countries, up to 90 per cent of the whole market volume was caused by fraudulent activities.

At UN climate talks in Copenhagen this weeks, the EU's most forested countries, Austria, Finland and Sweden,

pushed for new rules on how they account for changes in **forestry and land-use**, such as logging, wood-burning and farming practices. If accepted, the rules would enable them to meet binding emissions targets more easily, green groups warn, and could have a negative impact on future carbon prices. The countries are pushing for alternative accounting systems where countries will not be responsible for planned emission increases from land use, land-use change and forestry (**Lulucf**). The proposal has also gained support from other rich countries with large forests.

The EU pledged it will contribute €2.4 billion (\$3.6 billion) annually over the next three years to **kick-start climate aid** to poor and vulnerable nations in order to help secure a post-2012 climate pact. The EU has called for an annual global contribution of €7 billion (\$10.3 billion) per year between 2010 and 2012.

Australia's opposition Liberal party said there is no guarantee it will back the government's carbon reduction target even if the ongoing UN climate talks prove successful. "The agreements are one thing, what the countries actually do when they get home is something else," said Barnaby Joyce, a key party member. "We don't honour anything until we see the details."

New Zealand has proposed calculation methods for issuing free permits to industry under the ETS. The final rules could mean millions of dollars won or lost for industrial companies, because not every industry will be given free permits under the emissions trading scheme. Emission-intensive industries exposed to international trade will receive either 90 per cent or 60 per cent of their needed permits for free.

GUEST COMMENTARY

Clash of the environmentalist and anti-capitalist agendas

By James Emanuel, commercial director at CantorCO2e

During the UN Climate Change Conference (COP 15) in Copenhagen this week we have witnessed climate activists criticising carbon trading as the mechanism of choice for achieving emission reductions.

Such views are not uncommon. Only last month, Sarah Jayne-Clifton of the NGO Friends of the Earth published a report in which she launched a scathing attack on the carbon market claiming that "Carbon trading is failing dismally at reducing emissions!"

Similarly, Angie Viands of Rainforest Action Network claimed that "Carbon Trading ... acts as a dangerous distraction from the real climate solutions we urgently need"

"The air is not for sale!" declared Abigail Singer of the Mobilization for Climate Justice. "Cap-and-trade plans are an unprecedented and opportunistic attempt to privatise the atmosphere!"

According to Kevin Smith from Climate Justice Action, "The carbon markets cannot really be trusted to reduce emissions."

Such disparagement only serves to highlight a fundamental misunderstanding of the cap-and-trade mechanism.

The fact of the matter is that carbon trading is NOT designed to reduce emissions.

The quantitative reduction of emissions is determined by governments in setting the carbon cap. The trading is the subsequent mechanism designed to afford industry with maximum flexibility in complying with the prescribed carbon caps: hence the name "cap and trade".

Once the cap has been set, the

carbon market acts as a very useful barometer of the economy's achievement in relation to its emission abatement target: the lower the market price, the closer the economy is to attaining the prescribed cap and, all else being equal, the market price will be zero when the cap is finally achieved.

If NGOs are not happy with the quantity of emission reductions presently being achieved, then criticism should be directed towards the level at which the caps were set by legislators in the first instance.

Moreover, NGOs ought to know better than to irresponsibly criticise carbon trading without suggesting any better alternative. Destructive criticism from NGOs only serves to undermine the credibility of the best compliance mechanism available to us presently.

Indeed, I would argue that there is no viable alternative to carbon trading. The arguments in favour of the introduction of a carbon tax have imploded and so cap and trade is, de-facto, the only game in town.

Four good socioeconomic reasons exist for not favouring a carbon tax over a cap-and-trade solution:

- A "one size fits all" tax would require an impossible calculation of the average cost of reducing emissions over a given period of time. Compare this to an emission trading system that works on the free floating marginal cost of emission abatement
- Taxes are levied locally and so are impossible to properly administer on a global scale. A global carbon market price is perfectly pervasive
- Unlike carbon trading, a carbon tax does not provide a forward

market in which to hedge the long-term risk of emission abatement investments. Without a forward market, investment in large scale projects would be inhibited

- Tax cannot guarantee a reduction in greenhouse gas emissions: emitters could opt to pay the tax and continue emitting at will. Conversely, a cap-and-trade solution introduces an absolute carbon ceiling and the price acts as no more than a useful barometer of how close we are to achieving that goal: prices will move to zero as the requisite level of emission reductions are achieved.

The latter point dispels the political myth that "we need to establish a carbon price"

Why does it matter if we achieve the necessary quantity of emission abatement at \$2 per tonne of CO₂ or at \$50 per tonne of CO₂?

Politicians should not be focussing any attention on carbon pricing. All focus at the summit should be on setting a satisfactory carbon cap: the price will determine itself.

Let us not lose sight of the fact that the goal is to achieve an environmental objective while carefully balancing the pervasive political objective of protecting the economy. A priori, emission abatement may only be optimised if the impact on the economy is minimised. Therefore, all of those in favour of maximising the reduction of greenhouse gas emissions ought to welcome the mechanism that best mitigates the consequential cost to the economy: a cap-and-trade solution.

My message to the environmental lobby is that "recycling old arguments will not save the planet!"

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