By Senator Carlyle
[A.1]

P2SSB 5126 (S-2069.2/21) - S COMM AMD
By Committee on Ways & Means

On page 2, line 24, after "(5)" insert "The legislature further finds that by exercising a leadership role in addressing climate change, Washington will position its economy, technology centers, financial institutions, and manufacturers to benefit from national and international efforts that must occur to reduce greenhouse gases. The legislature intends to create climate policy that recognizes the special nature of emissions-intensive, trade-exposed industries by minimizing leakage and increased life-cycle emissions associated with product imports. The legislature further finds that if appropriate climate policies are not enacted, leakage can occur that results in net increases in global greenhouse gas emissions and increased negative impacts to those communities most impacted by environmental harms from climate change. The legislature further intends to encourage these industries to continue to innovate, find new ways to be more energy efficient, use lower carbon products, and be positioned to be global leaders in a low carbon economy.

(6)"

Beginning on page 27, line 13, after "INDUSTRIES." strike all material through "retired." on page 30, line 3, and insert "(1) A covered entity must receive an allocation of allowances under this subsection at no cost if the entity is classified as emissions-intensive and trade-exposed, as determined by being engaged in one or more of the processes described by the following industry descriptions and codes in the North American industry classification system:

(a) Metals manufacturing, including iron and steel making, ferroalloy and primary metals manufacturing, secondary aluminum smelting and alloying, aluminum sheet, plate, and foil manufacturing, and smelting, refining, and alloying of other nonferrous metals, North American industry classification system codes beginning with 331;

(b) Paper manufacturing, including pulp mills, paper mills, and paperboard milling, North American industry classification system codes beginning with 322;

(c) Aerospace product and parts manufacturing, North American industry classification system codes beginning with 3364;

(d) Wood products manufacturing, North American industry classification system codes beginning with 321;

(e) Nonmetallic mineral manufacturing, including glass container manufacturing, North American industry classification system codes beginning with 327;

(f) Chemical manufacturing, North American industry classification system codes beginning with 325;

(g) Computer and electronic product manufacturing, including semiconductor and related device manufacturing, North American industry classification system codes beginning with 334;

(h) Food manufacturing, North American industry classification system codes beginning with 311;

(i) Cement manufacturing, North American industry classification system code 327310;

(j) Petroleum refining, North American industry classification system code 324110;

(k) Asphalt paving mixtures and block manufacturing from refined petroleum, North American industry classification system code 324121;

(l) Asphalt single and coating manufacturing from refined petroleum, North American industry classification system code 324122; and

(m) All other petroleum and coal products manufacturing from refined petroleum, North American industry classification system code 324199.

(2) By July 1, 2022, the department must adopt by rule objective criteria for both emissions' intensity and trade exposure for the purpose of identifying emissions-intensive, trade-exposed manufacturing businesses during the second compliance period of the program and subsequent compliance periods. An entity covered by subsection (1)(a) through (m) of this section is considered an emissions-intensive, trade-exposed entity and is eligible for allocation of no cost allowances as described in this section. In addition, any covered party that is a manufacturing business that can demonstrate to the department that it meets this criteria, is also eligible for treatment as emissions-intensive, trade-exposed and is

eligible for allocation of no cost allowances as described in this section.

(3)(a) For all compliance periods prior to December 31, 2034, the annual allocation of allowances for direct distribution to an entity identified as emissions-intensive and trade-exposed must be equal to the covered entity's proportional obligation of the program budget under section 8 of this act, multiplied by 100 percent.

(b) The department shall by rule provide for emissions-intensive and trade-exposed facilities to apply and receive from the department an adjustment to the allocation for direct distribution of allowances based on a facility-specific carbon intensity benchmark as calculated in this subsection. If the department determines that the net quantity of no cost allowances awarded pursuant to (a) of this subsection is lower than the facility-specific carbon intensity benchmark, the department shall award additional no cost allowances up to the facility-specific carbon intensity benchmark. The department shall adjust the no cost allocation of allowances and credits to an emissions-intensive and trade-exposed facility to avoid duplication with any no cost allowances transferred pursuant to sections 13 and 14 of this act, if applicable.

(i) For the purpose of this section, "carbon intensity" means the amount of carbon dioxide equivalent emissions from a facility in metric tons divided by the facility specific measure of production including, but not limited to, units of product manufactured or sold, over the same time interval.

(ii) If an emissions-intensive and trade-exposed facility is not able to feasibly determine a carbon intensity benchmark based on its unique circumstances, the entity may elect to use a mass-based baseline that does not vary based on changes in production volumes. The department shall establish a comparable compliance obligation and no cost allowance allocation under this section between an entity utilizing a carbon intensity benchmark and a mass-based baseline. If a facility elects to use a mass-based baseline, it may not later convert to a carbon intensity benchmark during the first three compliance periods.

(c)(i) By April 1, 2022, the department must convene a work group of the emissions-intensive, trade-exposed facilities defined in this section, and their affiliated trade associations, and independent experts in emissions regulation, industrial practices, or other related fields.

(ii) By July 31, 2022, the work group shall establish procedures for calculating carbon intensity benchmarks. The carbon intensity benchmark must be based upon data from 2015-2019, unless the emissions-intensive, trade-exposed facility can demonstrate that there have been abnormal periods of operation that materially impacted the facility and the baseline period should be expanded to include years prior to 2015.

(iii) By September 15, 2022, each emissions-intensive, trade-exposed facility shall submit its carbon intensity benchmark for the first compliance period to the department. The calculation must be consistent with the work group established procedures.

(iv) By November 15, 2022, the department shall review and approve each emissions-intensive, trade-exposed facility baseline carbon intensity benchmark.

(d) For each year in the first four-year compliance period that begins January 1, 2023, each emissions-intensive, trade-exposed facility will calculate its facility-specific carbon intensity benchmark by its actual production.

(e)(i) For the second four-year compliance period that begins January 1, 2027, the second period benchmark for each emissions-intensive, trade-exposed facility is three percent below the lower of the first period benchmark or the 2015-2019 benchmark.

(ii) For the third four-year compliance period that begins January 1, 2031, the third period benchmark for each emissions-intensive, trade-exposed facility is three percent lower than the second period benchmark.

(f)(i) Prior to the beginning of either the second or third compliance periods, an emissions-intensive, trade-exposed facility may make an upward adjustment in the next compliance period's benchmark based on a demonstration that additional reductions in carbon intensity or mass emissions are not technically or economically feasible. An emissions-intensive, trade-exposed facility may base its upward adjustment in the next compliance period on the facility's best available technology analysis. The department shall by rule provide for emissions-intensive, trade-exposed facilities to apply to the department for an adjustment to the allocation for direct distribution of no cost allowances based on its facility-specific carbon intensity benchmark or mass emissions baseline. The department shall make adjustments based on:

(A) A significant change in the emissions use or emissions attributable to the manufacture of an individual good or goods in this state by an emissions-intensive, trade-exposed entity based on a finding by the department that an adjustment is necessary to accommodate for changes in the manufacturing process that have a material impact on emissions;

(B) Significant changes to an emissions-intensive, trade-exposed facility's external competitive environment that result in a significant increase in leakage risk; or

(C) Abnormal operating periods when an emissions-intensive, trade-exposed facility's carbon intensity has been materially affected so that these abnormal operating periods are either excluded or otherwise considered in the establishment of the compliance period carbon intensity benchmarks.

(ii) For the purpose of this section, "best available technology" means a greenhouse gas emissions limitation determined by the department on a case-by-case basis taking into account the fuels, processes, equipment, and technology used by facilities to produce goods of comparable type, quantity, and quality, that will most effectively reduce those greenhouse gas emissions for which the source has a compliance obligation. Best available technology must be technically feasible, commercially available, economically viable, not create excessive environmental impacts, and be compliant with all applicable laws while not changing the characteristics of the good being manufactured.

(4)(a) Beginning January 1, 2035, and each year thereafter, the annual allocation of no cost allowances for direct distribution to an entity identified as emissions-intensive and trade-exposed must reduce by an equal amount each year between 2035 and 2050 such that in 2050 the facility's proportionate share of the allowance budget is equal to the share in 2035. The annual allocation must decline from the average of the facility's annual allocation of no cost allowances from 2031-2034. If the emissions-intensive, trade-exposed facility can demonstrate that there have been abnormal periods of operation that materially impacted the facility, then the baseline period should be expanded to include years prior to 2031.

(b) By December 1, 2030, the department shall provide a report to the appropriate committees of the senate and house of representatives that describes alternative methods for determining the amount and a schedule of allowances to be provided to each covered entity designated as an emissions-intensive, trade-exposed manufacturing business. The report must include a review of global best practices in ensuring against emissions leakage and economic harm to businesses in carbon pricing programs and describe alternative methods of emissions performance benchmarking and mass-based allocation of no cost allowances. In developing the report, the department shall form an advisory group that includes representatives of the manufacturers listed in subsection (1) of this section.

(5) If the actual emissions of an emissions-intensive, trade-exposed facility exceed the facility's no cost allowances assigned for that compliance period, it must acquire additional compliance instruments such that the total compliance instruments transferred to its compliance account consistent with section 19 of this act equals emissions during the compliance period. The department shall limit the use of offset credits for compliance by an emissions-intensive, trade-exposed facility, such that the quantity of no cost allowances plus the provision of offset credits does not exceed 100 percent of the facility's total compliance obligation over a compliance period.

(6) The department must withhold or withdraw the relevant share of allowances allocated to a covered entity under this section in the event that the covered entity ceases production in the state and becomes a closed facility. In the event an entity curtails all production becoming a curtailed facility, the allowances are retained but cannot be traded, sold, or transferred and are still subject to prescribed emission reductions had the facility not curtailed. An operator of a curtailed facility may transfer the allowances to a new operator of the facility that will be operated under the same North American industry classification system codes. If the curtailed facility becomes a closed facility, then all unused allowances will be transferred to the emissions containment reserve. A curtailed facility is not eligible to receive free allowances during a period of curtailment. Any allowances withheld or withdrawn under this subsection must be transferred to the emissions containment reserve."

<u>EFFECT:</u> Corrects an erroneous NAICS reference to the wood products manufacturing sector.

Adds NAICS references for asphalt paving mixtures and block manufacturing; asphalt single and coating manufacturing; and all other petroleum and coal products manufacturing from refined petroleum.

Provides that the emissions-intensive, trade-exposed (EITE) status is permanent for listed NAICS references.

Directs the department of Ecology (Ecology) to identify additional EITEs by rule prior to the first compliance period.

Provides that for all compliance periods prior to December 31, 2034, EITEs receive 100 percent no-cost allowances proportional to the cap decline.

Directs Ecology to allow EITEs to apply and receive an adjustment to their allocation of allowances based on a facility-specific carbon intensity (CI) benchmark.

Provides that for the first compliance period, EITEs may apply to receive additional free allowances up to the CI benchmark, for the second compliance period the CI benchmark declines by 3 percent, and for the third 4-year compliance period the CI benchmark declines by an additional 3 percent.

Provides that if an EITE facility is not able to feasibly determine a CI benchmark, it may elect to use a mass-based baseline that does not vary based on changes in production volumes.

Directs that beginning January 1, 2035, the annual no cost allowance allocation must decline annually between 2035 and 2050 based on the facility's proportionate share of the program budget in 2035.

Requires Ecology by December 1, 2030, to provide a report to the legislature describing alternative methods and best practices in ensuring against emissions leakage.

Requires EITEs to purchase allowances and or offset credits for their emissions above their assigned no cost allowances.

Allows Ecology to limit offset credit use if no cost allowances plus offset credits exceed one hundred percent of total compliance.

Clarifies that a curtailed facility can retain, but not trade, sell, or transfer, allowances except to transfer to a new operator of the facility operating under the same industrial classification.

Requires all unused allowances to be transferred to the emissions containment reserve if the curtailed facility becomes a closed facility. A curtailed facility is not eligible to receive free allowances during a period of curtailment.

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