

Issue Overview:

Role of Offsets in Cap and Trade



On January 15, 2009, the U.S. Climate Action Partnership (USCAP) issued the *Blueprint for Legislative Action* – a detailed framework for legislation to address climate change. This brief discusses the importance of offsets in a cap-and-trade program. It should be considered in the context of our *Blueprint*, which includes interconnected and interdependent recommendations on climate protection legislation.

Background

Unlike many types of pollution, the location or source of greenhouse gas (GHG) emissions does not significantly affect its environmental impact because GHGs spread quickly in the atmosphere, where they remain for decades to centuries. Since the total accumulation of GHGs determines the climate impact, reducing a ton of emissions from one source has the same climate impact as reducing a ton of emissions from any other source. The interchangeability of emission reductions in a cap-and-trade system helps manage costs since the cheapest reductions are likely to be made first.

USCAP's Recommendations

USCAP recommends a cap-and-trade program with a broad scope of coverage. However, some sources and activities that contribute GHG emissions will necessarily remain outside the cap. USCAP recommends the establishment of an “offset” program that would allow covered sources to purchase measurable and verifiable emissions reduction credits from sources that remain outside the cap.

- A well-designed offsets program significantly improves the cost effectiveness of achieving the environmental goals of the program by including a broader scope of low- and moderate-cost emissions reduction opportunities. In doing so, it ensures that a broader segment of the economy has an incentive to respond to a carbon price signal.
- USCAP recommends including only high-quality domestic and international offsets in a cap-and-trade program. Assuring that offsets are of high quality ensures the climate benefits of the overall program will be achieved and enables offsets to trade on equal terms with other types of emission reductions.
- To ensure offset quality, USCAP recommends that criteria be established to ensure that all offsets are environmentally additional, verifiable, permanent, measurable and enforceable. USCAP recommends that the Environmental Protection Agency (EPA), should be directed to establish an offset program within 18 months of enactment that would identify specific categories of offsets that would be eligible to participate in the program. To assure greater consistency and efficiency, the EPA should develop standard methodologies for evaluating offsets in each category, and guidance should be created for offset developers with clear certification procedures.

USCAP recommends Congress place limits on the use of offsets for compliance.

- An initial annual limit of two billion metric tons could be increased to a maximum of three billion metric tons by a Carbon Market Board established by Congress in order to avoid undue economic harm from excessively high allowance prices.
- Within these overall limits, Congress should set maximum upper limits of 1.5 billion tons each on the use of either domestic or international offsets in any year.

International offsets can play an important role in forging a global climate protection agreement by providing incentives for more countries to undertake significant actions to reduce emissions. Global deforestation, for example, accounts for 20 percent of global GHG emissions, more than the entire global transportation system. Creating a program to allow measurable and verifiable offsets from reductions in deforestation can, along with

other mechanisms, be a critically important tool for successfully fighting climate change. USCAP recommends that the EPA should establish a schedule to assure that over time, international offsets result in incremental reductions beyond a nationally appropriate country or sector-specific emissions reduction commitment. Such a commitment should cover a suitable share of that countries' emissions, consistent with the global goal of avoiding dangerous climate change.

As part of our cost containment recommendations, USCAP calls for the establishment of a Strategic Offset and Allowance Reserve Pool that would release offsets into the market, at or above the auction threshold price, to prevent excessive carbon prices. To assure effective cost containment, USCAP recommends that a very large number of offsets be maintained in the Reserve Pool. The supply of offsets in the Reserve Pool is expected to include reductions from avoided deforestation, whether provided via government-to-government agreements or by private developers, as well as from other qualifying offset projects. All offsets released from the Reserve Pool must meet the same quality criteria as those used for normal compliance and they can be used by covered sources for compliance without limitations.

The use of real and verifiable offsets has multiple benefits.

- High-quality offset projects stimulate emission reductions and technology innovation in uncapped sectors and result in emission reductions – that have the same climate benefit as equivalent reductions within a capped sector – that would not otherwise occur.
- Offsets reduce costs to the U.S. economy by allowing firms to purchase emission reductions that occur outside the cap when they are more cost-effective, just like a cap-and-trade program allows firms to purchase allowances from other capped firms that can reduce emissions more cheaply.
- Given the emission reduction targets recommended by USCAP, offsets provide a critical transition period for industry to meet their compliance obligation while still developing and deploying emerging low-carbon technologies, thereby helping to safeguard the economy from drastic shocks in fuel use and prices.

To learn more about the USCAP *Blueprint for Legislation Action*, please visit www.us-cap.org.

The U.S. Climate Action Partnership is a non-partisan coalition composed of 25 major corporations and five leading environmental organizations that have come together to call on the federal government to quickly enact strong national legislation requiring significant reductions of greenhouse gas emissions. USCAP has issued a landmark set of principles and recommendations to underscore the urgent need for a policy framework on climate change.