Fuels Sectors: Considerations for Covered Entities and Compliance Instrument Distribution

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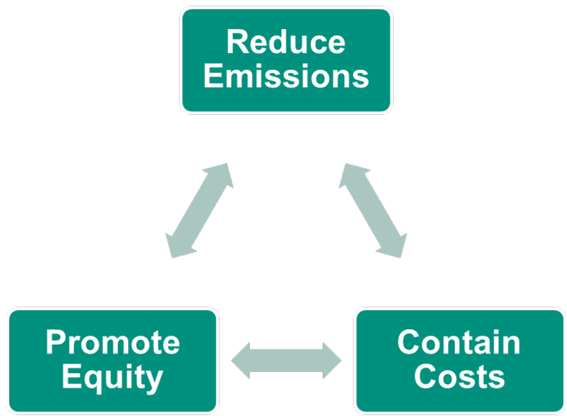
DEQ is a leader in restoring, maintaining and enhancing the quality of Oregon's air, land and water.

Overview

The Climate Protection Program will limit and reduce greenhouse gas emissions from some of the most significant sources in Oregon. The program aims to:

- Achieve significant emissions reductions
- Promote benefits and alleviate burdens for environmental justice and impacted communities
- Contain costs



This brief reviews some key considerations for regulating non-natural gas fuel suppliers and natural gas utilities.

1. Determining which entities are covered by the program and which are not.
2. Distributing compliance instruments.

DEQ believes the program should have a predictable process to determine covered entities, which will also inform compliance instrument distribution. This approach will provide certainty for businesses in order to achieve significant emissions reductions while limiting program costs.

Determining which non-natural gas fuel suppliers are covered

The point of regulation for non-natural gas fossil fuels, such as gasoline, diesel, propane and kerosene, is the fuel supplier that first has title to the fuel outside of a fuel terminal or otherwise owns the fuel as it is imported across the state border. An emissions threshold will be used to determine which fuel suppliers would be regulated. Any fuel supplier with emissions at or above the threshold would be covered under the program.

The companies importing these fuels and the quantities they supply vary annually, particularly among smaller companies. A company's market share can change significantly from year to year. A fuel supplier could have emissions above the selected threshold one year, but not in future years. This could occur regardless of the threshold level selected but would occur more frequently at a lower threshold.

DEQ discussed potential thresholds of 5,000, 25,000 and 300,000 metric tons at the March 2021 Rulemaking Advisory Committee meeting and received multiple comments from advisory committee members. Many advisory committee members and public commenters requested a lower threshold to ensure regulation of a greater percentage of total emissions covered under the program and to limit in-state leakage from larger fuel suppliers to smaller fuel suppliers. Other commenters requested a higher threshold to avoid regulating smaller entities, since they may face challenges such as less administrative capacity or higher compliance costs. Regardless of the threshold selected for the program, DEQ seeks to limit annual variability about which entities are above the threshold.

Using an evaluation cycle

One way DEQ could accommodate this sector's variability and reduce uncertainty, would be to evaluate emissions over a multi-year period to determine which entities meet or exceed the threshold. For example, an entity could be covered if its emissions exceeded the threshold during any year of the evaluation period or if its average emissions exceed the threshold. The determination about whether the entity is covered could apply for one compliance period, multiple compliance periods, or indefinitely. DEQ believes that reducing uncertainty could help fuel suppliers plan for compliance, and also potentially help limit unnecessary cost increases for consumers.

As an example, DEQ could evaluate historical emissions from a three-year period to determine which entities are above the threshold. Any fuel supplier with average emissions above the threshold would be a covered fuel supplier. These entities would then need to comply with program requirements for the next six years (two, three-year compliance periods). DEQ would conduct a new evaluation with updated data every three years, as shown in Table 1.

Table 1: Example schedule for evaluating applicability for non-natural gas fuel suppliers

Emissions years for evaluation period	Year in which evaluation occurs to determine if entity is covered	Applicable compliance periods for which entity becomes a covered fuel supplier (both periods):	
		First period	Second period
2017-2019	2021	2022-2024	2025-2027
2020-2022	2024	2025-2027	2028-2030
2023-2025	2027	2028-2030	2031-2033
Each subsequent three-year period	Every third year (the year prior to the start of a new compliance period)	Each subsequent three-year period	Each subsequent three-year period

How often should thresholds be evaluated?

DEQ understands entities seek clarity around which future years they will be regulated based on historical emissions compared to a threshold.

To minimize fluctuation in which entities are covered over time, DEQ would seek to make this determination no more than once per compliance period. This could support more clarity in the distribution of compliance instruments.

Additionally, an entity could be covered for multiple compliance periods. This would further provide long-term certainty regarding whether an entity is covered once its emissions exceed the threshold. However, this also means that if an entity's emissions eventually fall below the threshold, there will be a longer period of time before it is no longer covered.

What years should be used in the threshold evaluations?

DEQ could evaluate emissions across multiple years to help minimize the effects of annual variability, but if the emissions are too far in the past, the emissions may not properly reflect fuel supplier's present emissions or upcoming compliance period emissions. However, if emissions are too recent, then fuel suppliers would have less time to plan for compliance.

Based on the greenhouse gas emissions reporting and verification schedule, emissions data for a given year are not available for analysis until late fall of the following year.

- One approach would be calculate the emissions thresholds immediately prior to the start of a compliance period in order to incorporate the most recent year of emissions data. However, this allows little time for covered entities to plan for compliance with a year in which their emissions are regulated beginning in a few short months.

- Another approach is to calculate the emissions average earlier in the year that is prior to the first year of a compliance period. However, in this case, the emissions data used would be further removed from the compliance period, as shown in the example in Table 1. In this approach, the most recent year of emissions data is in the next evaluation for a later compliance period.

Regulating natural gas utilities

DEQ's current leaning is to regulate all natural gas emissions at the three natural gas utilities without setting a threshold.

Distributing compliance instruments to natural gas utilities and non-natural gas fuel suppliers

DEQ will set an annual limit of allowable emissions in the Climate Protection Program measured in metric tons of carbon dioxide equivalent (MT CO_2e). The limit would decline each year toward emissions reduction targets established in the program rules. The limit would apply to natural gas utilities and non-natural gas fuel suppliers, also called covered fuel suppliers.

One compliance instrument would represent one allowable MT CO_2e of covered emissions. Annually, DEQ would generate a number of compliance instruments equal to the limit and distribute those compliance instruments to covered fuel suppliers. DEQ has previously stated it favors distributing compliance instruments annually based on historically reported emissions by covered entities. This could be done by assessing a covered fuel supplier's proportional share of emissions to determine their distributed share of compliance instruments. For example, if a covered fuel supplier reported one percent of historical emissions, they could receive one percent of compliance instruments. This approach raises several key considerations.

Timing of DEQ determination of shares of compliance instruments

If DEQ uses a cyclical process to determine which fuel suppliers are covered, as described above, this could mean that the list of covered fuel suppliers is constant within a compliance period. DEQ could determine the distribution of compliance instruments at the same time, or immediately after identifying covered fuel suppliers for an upcoming compliance period. DEQ could hold that percentage share of compliance instruments constant throughout the compliance period. This approach could provide clarity about the number of compliance instruments each covered fuel supplier would receive.

Evaluation period and schedule

Tradeoffs for selecting an evaluation period may be similar to those outlined above for threshold evaluations for non-natural gas fuel suppliers. There may be advantages to using the same evaluation period as shown below in Table 2, though it is not necessary to align. Some additional considerations include:

- If DEQ bases compliance instrument distribution fully on historically-reported emissions, then for each compliance period, a fuel supplier would know what percentage of compliance instruments they can expect to receive prior to the beginning of the next compliance period. However, the emissions data used may not correspond to future emissions that may occur during the compliance period.

- DEQ could base compliance instrument distribution in part on emissions that are reported during the compliance period. For example, DEQ could wait to distribute any compliance instruments until after emissions from the first year of the compliance period are reported and verified. However, this means that covered fuel suppliers would not know how many compliance instruments they would receive until late in the second or third year of a three-year compliance period. This would create uncertainty for those regulated under the program. Additionally, this approach may mean that covered entities may be hesitant to reduce emissions during the first year of the compliance period if higher emissions might result in receiving a greater share of compliance instruments.

Table 2: Example schedule for evaluating distribution of compliance instruments

Emissions years for evaluation period	Year in which evaluation occurs to determine distribution of compliance instruments	Compliance period for which the determined distribution methodology applies
2017-2019	2021	2022-2024
2020-2022	2024	2025-2027
2023-2025	2027	2028-2030
Each subsequent three-year period	Every third year (the year prior to the start of a new compliance period)	Each subsequent three-year period

Calculation of share

A simple approach to distribute compliance instruments to each covered fuel supplier would be based on their proportional share of emissions relative to total covered emissions. For example, if an entity produced 1 percent of covered emissions, it could receive one percent of compliance instruments. However, this approach may not address the needs of each entity. Among fuel suppliers with smaller total emissions, a change in the number of compliance instruments received could be a comparatively large percentage of emissions.

For example, if a covered fuel supplier has 50,000 MT CO_2e of emissions and it needs 1,000 more compliance instruments in order to comply, this is a much larger percentage of its emissions than a 1,000 compliance instrument shortage for a covered fuel supplier with 1 million MT CO_2e of covered emissions. A possible way to address this could be to group fuel suppliers (based on sector, range of emissions, or other category). DEQ could then distribute a percentage of compliance instruments to a group first. The instruments could then be divided among the entities within the group in proportion to their emissions. This may mean that an entity's distribution is less affected by the activities of those outside of their own group. This could limit variability within groups, although DEQ would need to determine what percentage to distribute to each group and determine how often to update those percentages.

Discussion questions

1. How often should DEQ evaluate who is above the program threshold?
    a. How many years of historical emissions data should be used in an evaluation?
    b. For how many years or compliance periods should entities be covered based on evaluation of historical emissions data?
2. What are the advantages and disadvantages of using an evaluation cycle to determine distribution of compliance instruments?
    a. What tradeoffs are important to you when considering using historical or more current emissions data, relative to a compliance period?
    b. Should the evaluation cycle align with determination of applicability? Why or why not?
    c. Should DEQ establish specific percentages of compliance instruments to distribute to groups of entities? Why or why not?

Alternative formats

DEQ can provide documents in an alternate format or in a language other than English upon request. Call DEQ at 800-452-4011 or email deqinfo@deq.state.or.us.