

# US GHG Markets – January - February 2010 (1/2)

## Monthly Market Update



### Federal

#### Volatility Persists on Federal Climate Change Legislation

The months of January and February were notable for the constant change in the federal climate change legislation debate. One important milestone over the course of the two months included the Massachusetts special election in which Republican Scott Brown won the former Senator Ted Kennedy's seat. The election led to the dissolution of the Democratic Party's filibuster-proof super majority voting bloc in the Senate. While this led to increased malaise over the prospects for passing climate change legislation, the tri-partisan partnership of John Kerry (D-MA), Lindsay Graham (R-SC) and Joseph Lieberman (I-CT), continued to exhibit support for passing legislation this Congress. While these Senators showed continued support, several key Democratic Senators were reported to state that a climate change bill was dead this year, including one key vote, Max Baucus (D-MT).

It has been the plan all along to include several Republicans in the negotiation process as comprehensive energy and climate change legislation has always been a bi-partisan effort. The trick in the Senate is to find the right mix of incentives to get the 60 votes. Kerry, Graham and Lieberman have always maintained open-mindedness to putting a price on carbon and addressing America's energy independence challenge. Through this position, the Senators have received several suggestions on how to craft a bill which will attract the necessary votes. The framework that is most likely could include:

- an electricity sector cap only starting in 2012
- phase in the manufacturing sector under cap by 2018,
- carbon tax on oil and gas,
- provisions for increased domestic oil and gas drilling and
- financial support for nuclear power.

The new framework, which differs significantly from the House passed Waxman-Markey bill, is being designed to fold Senators from States tied to conventional fuels into the debate. The three Senators hope phasing in the manufacturing sector could attract votes from "Blue Dog" Democrats in the Midwest whose constituencies are tied to the manufacturing base in those areas of the country. Taxing oil and gas will provide better certainty on the costs of the legislation to oil and gas producing companies, thereby attracting votes from the South such as Mary Landrieu (D-LA). While the bill is far from certain, there does appear to be surviving momentum on climate change legislation, despite the further divisions created through the healthcare reform bill.

#### Disapproval Resolution Introduced by Alaskan Senator

In late January, Republican Senator Lisa Murkowski (R-AK) introduced a disapproval resolution which is aimed at nullifying the EPA's authority to regulate greenhouse gas (GHG) emissions. If passed in both the Senate and House, the resolution would preclude the EPA from regulating GHGs under the Clean Air Act. While the measure is strongly opposed by Senate Democratic leadership and the White House, three Democratic Senators have signed on to the measure including Senator's Lincoln (D-AR), Landrieu (D-LA) and Nelson (D-FL). The resolution would require only 51 votes to pass the Senate and would be required to be passed in the House, which is unlikely.

In February, Murkowski called for a senate floor vote on the resolu-

tion for early March, At this writing a date for consideration of the resolution has not yet been set.

Also of note, the White House called for \$47 million in new funding in its 2011 budget to enable the EPA to regulate GHG emissions. While speculation abounds that this EPA will use this funding to investigate a regulatory cap and trade program, EPA officials denied it and continue to be non-committal on the issue.

#### SEC Issues Guidance for Disclosing Material Climate Change Risks

In late January, the Securities and Exchange Commission (SEC) issued guidance on how companies should report material climate change risks. The SEC voted along party lines (3-2) to issue an Interpretive Release, which clarifies disclosure requirements related to "business or legal developments relating to the issue of climate change." While not a rule or regulation, the guidance interprets how climate change risk should be addressed under existing SEC Regulation S-K, which outlines areas of disclosure for registration statements and periodic reporting filed under the Securities Acts of 1933 and 1934. Specifically, the Release implies risks associated with climate change exist for business, including physical impacts such as water supply shortages or hurricane risks, as well as impact associated with regulation such as financial liability associated with emissions control requirements.

The Guidance cited four climate change risks which business must now consider when reporting:

1. Impact of legislation and regulation,
2. Impact of international accords,
3. Indirect consequences of regulation or business trends, and
4. Physical impacts of climate change

### California

#### Ballot Initiative in California

Republican Assemblymen Dan Logue and Congressman Tom McClintock have teamed with conservative activists in California to launch a ballot initiative to suspend California's Global Warming Pollution Reduction Act, also known as Assembly Bill 32. The initiative was filed with the Attorney General's office in February. The initiative aims to suspend implementation of the bill until such time as the unemployment rate in the State is 5.5% or less for four consecutive quarters. In order for this initiative to make it on to the midterm election ballot this November, the proponents of the effort must collect 433,971 valid signatures by April 16, 2010. As of this writing, no counties have submitted signatures supporting the initiative.

According to the Sacramento Bee, Texas-based oil company Valero Services Inc. donated \$500,000 to support the signature collection efforts. According to documents filed with the State, other contributors to the initiative include Howard Jarvis, Taxpayers Association (\$100,000), and three other oil companies including Tesoro Cos., Tower Energy Group and World Oil Group (\$360,000).

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The title that was prepared by the Attorney General of California (Jerry Brown):

“SUSPENDS AIR POLLUTION CONTROL LAWS REQUIRING MAJOR POLLUTERS TO REPORT AND REDUCE GREENHOUSE GAS EMISSIONS THAT CAUSE GLOBAL WARMING UNTIL UNEMPLOYMENT DROPS BELOW SPECIFIED LEVEL FOR FULL YEAR.”

Evolution Markets is closely monitoring developments with the ballot initiative. If you have any questions, please feel free to call our San Francisco carbon desk at 415.963.9137.

### ARB Revokes Climate Action Reserve Protocols; Could Re-Adopt Pursuant to CEQA Review Process

At a Board meeting in February, the California Air Resources Board (ARB) revoked two previously adopted offset quantification protocols by the Climate Action Reserve (CAR). The Livestock Methane Project Protocol and the Forest Project Protocols were revoked. The two protocols will now be subject to environmental review under the California Environmental Quality Act (CEQA). The revocation of the protocols injected further uncertainty into a fragile pre-compliance offsets market. The act by ARB was tempered with upbeat remarks for both Mary Nichols (ARB Chairman) and Linda Adams (CalEPA Secretary) on the ultimate fate of the protocols in a California cap and trade program.

Point Carbon reported Linda Adams stated she is “very confident” that CAR offset protocol will be approved for compliance under AB 32. Adams told Point Carbon she feels “very confident that since [ARB] has adopted the most stringent standard in the world, it’s highly likely that these projects will be given credit for early action.”

The upbeat remarks have provided some buoyant confidence Climate Reserve Tonnes (CRTs) will be useable in a California cap and trade program. The Board remarked that CEQA review of the protocols is planned to occur along the same timeline of the Final Regulation, which is expected to be adopted by the Board in October 2010. This means the market could see certainty on offsets in October.

### WCI

#### Arizona Drops Out of WCI

Late in February, Arizona made it clear it would not participate in of the Western Climate Initiative (WCI) when Republican Governor Jan Brewer issued an executive order. The order cited concerns related to the economy and the cost of the program. While Arizona is not rescinding its status as a WCI Partner, the order did state Arizona will not participant in a cap and trade program starting in January 1, 2012.

Benjamin Grumbles, director of the Arizona Department of Environmental Quality told the Arizona Republic “It’s very important for the state to stay engaged, to be at the table, but it’s also important to convey clearly our position on how to make progress. Right now, given the economic downturn, given the complexity of cap and trade scheme being developed, we’re not going to be supportive of it.”

Arizona is a founding member of the WCI. The WCI requires each of its Partners to pass legislation authorizing each Partner to participate in the trading program. At this point, California, British Columbia, Quebec and Ontario are the only Partners with the required legislation in place.

#### New Mexico Plans to Pass Cap and Trade Law

Earlier this month, New Mexico’s environmental department sent an outline of its cap and trade program to its governor-appointed Environmental Improvement Board. If passed, the plan would establish a pathway for New Mexico to participate in the WCI starting in 2012. At this stage, California, British Columbia, Ontario and Quebec are the only members that have passed the legislation required to participate in the WCI. There has been considerable doubt raised over whether other member states will be able to participate, such as Oregon, Washington, Arizona, Utah and others.

According to Sarah Cottrell, the State’s delegate to the WCI committee, New Mexico legislature does not have to pass legislation authorizing it to begin emissions trading in the program in 2012. The State currently has laws that mandate a reduction in greenhouse gas emissions from stationary sources such as power plants. However, the State would need to approve participation in the second phase of the WCI which would establish a cap on greenhouse gas emissions from the heating and transportation fuel sectors.

### Verified Emission Reductions (VERs) Offers

▼ TYPE	▼ COUNTRY	▼ SIZE (tons CO@e)	▼ VINTAGE	▼ BID/ASK	▼ PRODUCT
Livestock Methane	Western USA	50k/year	2009-2015	\$5.00 / \$8.50	Climate Action Reserve (CRT’s)
Landfill Gas	Midwest USA	75k/year	2009-2013	\$3.50 / \$6.50	Climate Action Reserve (CRT’s)
Forestry	California	100k	2009	\$6.00 / \$8.75	Climate Action Reserve (CRT’s)
Wind	Midwest	70k	2009	\$3.50/\$7.00	Voluntary Carbon Standard (VCUs)
Coal Mine Methane	Western USA	150k	2007	\$1.50 / \$3.00	Voluntary Carbon Standard (VCUs)
Ozone Depleting Substances	California	125k	2010	\$2.50 / \$5.50	Climate Action Reserve (CRTs)
Landfill Gas	USA	100k	Pre-2009	\$0.30 / \$0.60	Registered Chicago Climate Exchange (CCX) Offsets

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