

MIDWESTERN GREENHOUSE GAS REDUCTION ACCORD
PRELIMINARY RECOMMENDATIONS OF THE ADVISORY GROUP

INTRODUCTION

On November 15, 2007, the Governors of Illinois, Iowa, Kansas, Michigan, Minnesota and Wisconsin, and the Premier of Manitoba entered into the Midwestern Greenhouse Gas Reduction Accord (the "Accord"). The Accord calls for the establishment of "targets for GHG emission reductions and timeframes consistent with states' targets" and the development of a regional cap-and-trade program design. In early 2008, the Governors and Premier convened an Advisory Group consisting of a diverse group of individuals representing varied interests from across the region, including representatives from state and provincial governments, business, energy and environmental advocacy groups, and academia.

The Advisory Group was charged with making recommendations for the establishment of targets for emissions reductions in the region, and for the design of a regional cap-and-trade program. After lengthy deliberation and consideration of the various options for the participating jurisdictions, the Advisory Group has arrived at the preliminary recommendations contained below.

DESIGN PRINCIPLES

In setting the regional reduction target and designing the cap-and-trade program, the Advisory Group considered the following design principles:

- Ensure that the system is equitable, administratively simple for government and private participants, minimizes administrative costs, and has a clear compliance path;
- Cover as many sources as is practical, while encouraging emissions reductions beyond the capped sources and sectors;
- Assure a transparent and robust data gathering and accounting system that will measure and report emissions accurately and consistently across all sectors and throughout the region;
- Distribution of allowance value should support the goals of the program, including compensating for disparities and impacts caused by the program;

- Enable linkage to systems in other jurisdictions with similarly rigorous accounting in order to create economies of scale and to increase market efficiencies, diversity and liquidity, while reducing costs;
- Maximize economic, employment, energy diversity, environmental and public health benefits, while minimizing any transitional job losses and energy and other cost impacts;
- Reduce the potential for emissions leakage, including the shifting of economic activity to non-covered sources and to non-participating jurisdictions;
- Stimulate investment, especially in low-carbon technologies, and reward innovations that will lead to near and long-term, permanent greenhouse gas reductions;
- Credit qualified past and present actions to reduce GHG emissions;
- Require any offsets to be real, surplus/additional, verifiable, permanent and enforceable, and appropriately address additionality and permanence;
- Allow flexibility for participating jurisdictions to meet specific policy needs and objectives, while maintaining regional program uniformity;
- Demonstrate leadership toward, and enable incorporation into and harmonization with, any future federal program, while ensuring the capability of the regional program to stand on its own, if necessary. (Revised significantly from Accord); and
- Reduce the potential for and scale of unintended economic consequences of the policy, while maintaining an appropriate price signal.

THE RECOMMENDATIONS

1.0 EMISSIONS REDUCTION TARGET.

- 1.1 Reduction Targets: The Advisory Group recommends the following emissions reduction targets for the participating jurisdictions.
 - 1.1.1 2020 Target. The Advisory Groups has requested modeling analysis of a target that reduces emissions by 15, 20, and 25 percent below 2005 levels by 2020
 - 1.1.2 2050 Target. The Advisory Group recommends a reduction consistent with that recommended by the scientific community, or 60-80 percent below 2005 levels by 2050.

1.1.3 The Advisory Group also recommends that the targets be revisited and adjusted from time to time based on future scientific findings, technology developments, and program results, and recommends the establishment of a mechanism to conduct this review.

2.0 PROGRAM SCOPE

- 2.1 Sectors and Fuels. The Advisory Group recommends that the program cover the following sectors:
- 2.1.1 Electricity generation and imports.
 - 2.1.2 Industrial combustion sources
 - 2.1.3 Industrial process sources will be included to the extent credible measurement & monitoring protocols exist or can be developed prior to inclusion.
 - 2.1.4 [Transportation fuels]
 - 2.1.5 [Fuels serving residential, commercial and industrial buildings not otherwise covered in 2.1.1 or 2.1.2 above.]
- 2.2 Greenhouse Gases. The program should cover the following greenhouse gases, as appropriate: carbon dioxide, methane, nitrous oxide, hydro-fluorocarbons, perfluorocarbons, and sulfur hexafluoride.
- 2.3 Points of Regulation. The following are the recommended points of regulation for each sector:
- 2.3.1 For electricity, the first deliverer of electricity.
 - 2.3.2 For industrial combustion emissions, the emissions sources
 - 2.3.3 For industrial process emissions, the emissions sources.
 - 2.3.4 If transportation fuels are included, where the fuels enter the market in the participating jurisdictions; generally at the terminal rack, final blender or distributor.
 - 2.3.5 If residential, commercial and industrial combustion emissions not covered at 2.3.1 and 2.3.2, where the fuels enter the market in the participating jurisdictions; generally at the terminal rack, final blender or distributor.
- 2.4 Threshold for coverage. The emissions threshold for coverage at individual covered sources will be established on a sector-by-sector basis with the goal of including between 85 and 95% of the emissions in each sector. For the electricity sector, the threshold for coverage should be [25MW nameplate capacity][25,000 tons of carbon dioxide on an annual basis].

- 2.5 Cap-and-Trade Reductions. The reduction to be achieved in the covered sectors should be [equal to the regional reduction target], provided the cap-and-trade program, together with the complementary policies to be undertaken in the states and province, should at least achieve the recommended reduction goal set out in 1.0 above.
- 2.6 Complementary Policy Reductions. The recommendations on the scope of the cap-and-trade program assume that other policies will be implemented to ensure that comparable reductions will be achieved in those sectors not recommended to be part of the cap-and-trade program so that, taken together, the cap-and-trade program and the other policies will achieve the regional goal equitably across the economy.
- 2.7 Linking. The Advisory Group recommends that the participating states and province seek to link the MGGA cap-and-trade program to the:
 - 2.7.1 Northeast Regional Greenhouse Gas Initiative covering ten northeastern and mid-Atlantic states;
 - 2.7.2 Western Climate Initiative, covering seven western U.S. states and four Canadian provinces;
 - 2.7.3 European Emissions Trading System; and
 - 2.7.4 Other mandatory greenhouse gas reduction programs as appropriate.

3.0 ALLOWANCES

- 3.1 State and Provincial Allowance Budgets. Apportionment refers to how the total regional allowance budget is divided into participating jurisdictions' allowance budgets.¹ The Advisory Group recommends that the state and provincial allowance budgets should be established based primarily on absolute emissions allowed in each state and province, calculated in a uniform manner. Some portion of the state and provincial allowance budget should be apportioned based on other criteria, such as GHG emissions per capita; baseline year for allocation (i.e. adjustments to allow reward for early action); population and economic growth in the participating jurisdictions; and new sources or projected new sources.
- 3.2 Reduction Path. Allowance apportionment will decline in line with the targets trajectory over time.

¹ This is distinct from allowance distribution, which describes how jurisdictions choose to distribute their share of allowances into the market.

3.3 Allowance Distribution: Purposes. Allowances should be put toward climate-related purposes, not other purposes. The program will entail a significant economic transition. The Subgroup recognizes the need to mitigate the costs and maximize the benefits associated with this transition. Climate-related purposes include three categories: (1) accelerating transformational investment; (2) mitigating transitional adverse impacts of the program, and (3) addressing harmful impacts due to climate change. These recommendations are made on the assumption that strong complementary policies are enacted and additional funding is provided outside of the cap and trade program.

3.3.1 *Accelerating Transformational Investment.* Allowance value should be distributed to accelerate:

3.3.1.1 Commercial development and deployment of low-carbon technologies, infrastructure, and strategies primarily for sectors covered by the C&T Program. Distribution should be especially focused on those initiatives covered by the MGA platform, with emphasis on the recommendations of the Tier II Advisory Groups, and where potential GHG emissions reduction benefits are substantial and a lack of funding is a key barrier to success.

3.3.1.2 The retooling, conversion, and/or re-use of existing industrial and manufacturing infrastructure in the midwest region, particularly in the transportation sector.

3.3.2 *Mitigating Transitional Adverse Impacts:*

3.3.2.1 Consumers:

3.3.2.1.1 Allowance value should be distributed to mitigate cap-and-trade program cost impacts to consumers (particularly low-income consumers), including energy price impacts.

3.3.2.1.2 The distribution of allowance value, together with complementary policies, should minimize net cost increases to consumers by promoting investment in conservation and efficiency programs.

3.3.2.1.3 The MGGRA Advisory Group strongly recommends that the Tier II Advisory Group, and all jurisdictions participating in the MGGRA Accord and Energy

Platform process, pursue and implement aggressive conservation and efficiency policies in the very near term, with a particular focus on those policies that provide assistance to low-income consumers by minimizing increases in energy bills.

3.3.2.1.4 Any allowance value put towards efficiency should be additional to, and not a substitution for, utility conservation and efficiency programs and complementary policies.

3.3.2.2 Industry:

3.3.2.2.1 Allowance value should be distributed to mitigate cap-and-trade program cost impacts (including energy price impacts) to industrial entities in the region, particularly for those in industries that are GHG-intensive and have a limited ability to pass costs on to consumers of their products. Eligible industries will be determined based on further analysis, but may include: fabricated metals, food processing, primary metals, nonmetallic minerals, wood and furniture, chemicals and plastics, paper and printing, textiles, motor vehicles, and miscellaneous manufacturing. Such impacts can be related to carbon-intensive energy purchased or generated, and process emissions.

3.3.2.2.2 Allowance value should be distributed to ease worker and community transition.

3.3.2.2.3 Allowance value should be distributed to minimize leakage of emissions, jobs, and industry to regions outside of the area covered by the program.

3.3.2.3 Workers: Allowance value should be used to support a robust regional worker training and education program that includes incorporation of existing or underutilized human capital in all sectors, taking into account areas of particular Midwestern importance and strength as well as

how such a program might supplement similar efforts and funding proposals at the federal level.

- 3.3.3 Addressing adverse impacts of climate change on communities, human health, and natural resources.
 - 3.3.3.1 *Mitigating climate change impacts on communities and human health, with an emphasis on investment in infrastructure to offset, for example, urban heat-related and other climate-related health impacts, urban and rural flooding, etc., and investment in adaptation planning, anticipation, and response.*
 - 3.3.3.2 *Minimizing adverse impacts of climate change on natural resources.* Allowance value should be distributed to:
 - 3.3.3.2.1 Develop and administer comprehensive regional and state natural resource climate adaptation strategies; ensure dedicated funding to implement these strategies for climate-related ecosystem protection, with a focus on critical regional resources including: the Great Lakes; the Mississippi river basin; and the Great Plains.
 - 3.3.3.2.2 Enhance scientific capacity of the state environmental and resource agencies to evaluate and address the impacts of climate change on fish, wildlife, and ecosystems.
- 3.3.4 The Advisory Group will explore and recommend the categories within each purpose towards which allowance value may be distributed, a process for estimating a potential range of allowance value that may be appropriate to dedicate to each of the purposes outlined above, and the mechanisms through which these purposes may best be met. Once the Tier IV modeling results are complete, the Advisory Group will seek to reach consensus on recommended ranges.
- 3.4 Allowance Distribution: Methodology. The Advisory Group recognizes that the decision on whether to auction or allocate allowances will depend on the purposes to be achieved through the

allowance value or portion of the allowance value. Accordingly, the Advisory Group recommends a hybrid approach to allowance distribution, including some auctioning, some free allocation, and some allocation at a small fixed fee. Those objectives best achieved through direct allocation to affected entities should be so allocated. Those purposes best achieved through distribution of the revenue from an allowance auction should receive the allowance value after auction.

The Advisory Group recommends that most of the available allowances during a transition period be distributed to affected sectors as described below. The transition period should be [ten years] or [defined based on the availability of new technologies]. A reasonable portion of available allowance value should be retained each year to support the Regional Low-Carbon Technology Commercialization Fund described in section 1.5.2 below. The Group notes that if transportation is not included in the cap and trade program scope, we will need to find a funding mechanism for promoting transformational investment in transportation.

3.4.1 The Subgroup recommends establishing mechanisms in order to safeguard allowance value and ensure it is not diverted to non-climate related purposes. To the extent that auctioning is used, legal mechanisms must be put in place to ensure that auction revenues are not diverted to non-climate related purposes.

3.4.1.1 *Utility sector.* In order to safeguard allowance value and ensure that it is directed towards the purposes identified above rather than diverted towards other purposes, the Subgroup recommends direct allocation of [some share of] allowances to local distribution companies and load-serving entities, with conditions attached so as to ensure that

3.4.1.1.1 Receipt of allowances is contingent upon performance in energy efficiency and conservation (i.e. demonstrating energy and cost savings achieved through investment in efficiency programs) that benefits end-use consumers (particularly low-income consumers and energy-intensive industries).

3.4.1.1.2 Allowance value flows directly to end-use consumers including energy-

intensive industries, or is otherwise used in a manner that indirectly flows through to the benefit of consumers through investments that lower GHG emissions and compliance costs (including appropriate incentives to maximize utility performance).

3.4.1.1.3 The recipients of the allowances are subject to firm and effective regulatory oversight.

3.4.1.2 *Industrial Sector:* Some share of total allowance value will be allocated freely to energy-intensive or otherwise particularly vulnerable industries in order to mitigate adverse economic impacts of the program on industrial competitiveness and workers, and to help these industries transition to a low-carbon future. Distribution of these allowances is contingent on implementation of mechanisms to achieve the industrial sector purposes laid out in section 1.3.2.2 above, including protecting workers. The precise quantity of allowance value to be freely allocated will be determined as follows:

3.4.1.2.1 To mitigate adverse economic impacts to particularly vulnerable or competitively disadvantaged industries, allowances could be distributed using some methodology that would provide firms transitional assistance to enable them to move towards a lower-carbon future. Evaluating the effects from a carbon price on industrial profitability can help in determining how many free allowances might be required to provide appropriate levels of transitional assistance.

3.4.1.2.2 The impact of a carbon price on the competitiveness of a given industry or firm in the MGGRA region is tied to 1) the energy/carbon intensity of that industry or firm and 2) the extent to which that industry or firm is capable of passing additional costs on to consumers (dependent on the ability of

consumers to turn to lower-carbon product substitutes or imported products). This information can be used to assess the vulnerability of particular industries to adverse economic impacts, and the degree to which these impacts will need to be mitigated. After identifying estimates of energy costs as a share of total costs for particular industries, this data on industries' energy and emissions intensity of production can be used to calculate the likely impact of a carbon price on those industries.

3.4.1.3 *Transportation sector:*

3.4.1.3.1 In order to help facilitate technological transition in vehicles, fuels, and other transportation technologies, some share of allowance value should go towards supporting a regional fund to which project bids are submitted on a competitive basis using a "reverse auction" format (see section 1.5.2 below). Transportation project funding should be broken down into at least three categories: vehicle efficiency, low carbon fuels, and transportation system efficiency/VMT reduction, including retooling and conversion of existing infrastructure.

3.4.1.3.2 Some share of allowance value should be distributed to help fund development of local-level planning by municipalities that includes VMT reduction objectives, then distribute allowance value (on a competitive basis) to support implementation of these plans, including improving physical infrastructure.

3.4.1.3.3 To help mitigate gas price impacts on vulnerable individuals, communities, and businesses. allowance value should be used to provide assistance to low income consumers to help mitigate gas

price impacts resulting from the program including consumer rebates and short-term assistance (including incentives to purchase more efficient equipment) to industries (e.g. taxis, trucking) disproportionately affected by gas price increases.

3.4.1.3.4 Any allowance distribution method should supplement existing low-carbon transportation policy and incentives and support complementary policies that are structured to align with GHG reduction and economic & equity goals. To the degree that complementary policies are designed federally or in states, they should be structured to complement and not to undermine the objectives set out in MGGRA and allowance policy. MGGRA should advocate mechanisms in federal and state vehicle efficiency/fuel economy legislation that promote domestic manufacture of the most fuel efficient vehicles or components.

3.4.2 Consistent with our principles, the Advisory Group recommends that the basis for any free or fee-based allocation will be determined based on addressing economic harm (including mitigating energy price impacts during a transition period), accelerating transformational investment, and avoiding intra-regional competitive impacts. The Advisory Group will work on devising methods for achieving these objectives. This will apply to both existing and new emissions sources.

3.5 Regional Distribution of Allowance Value, or by Jurisdiction. The Advisory Group recommends a hybrid approach for the distribution of allowance value across the region. Some decisions over allowance distribution should be left to each jurisdiction, while other decisions should be harmonized across participating jurisdictions. The Advisory Group recommends that the hybrid approach seek to achieve the maximum achievable level of harmonization and consistency across participating jurisdictions in order to help minimize inter-jurisdictional economic competitiveness issues and ensure the most level playing field.

- 3.5.1 Decisions that should be harmonized across jurisdictions to the maximum extent possible include:
 - 3.5.1.1 To the extent allowances are allocated, consistent procedures should be employed with the objective of minimizing intra-regional competitive concerns and anticompetitive outcomes.
 - 3.5.1.2 Treatment of new entrants. Covered entity entrants to the cap-and-trade program should be treated similarly across all participating jurisdictions to the maximum extent possible.
 - 3.5.1.3 The minimum percentage of allowances to auctioned, for price discovery and to help ensure market liquidity in the early years of the program
- 3.5.2 *Regional Low-Carbon Technology Commercialization Fund.* The MGGRA Advisory Group recommends establishment of a cost-effective competitive regional fund that is supported by allowance value in order to foster low-carbon technology demonstration, deployment and commercialization based on the shared technology priorities of this Advisory Group and the three MGA Energy Security and Climate Stewardship Platform advisory groups.
 - 3.5.2.1 The fund will:
 - 3.5.2.1.1 Ensure availability of investment funding needed under a cap and trade program;
 - 3.5.2.1.2 Maximize regional coordination of R&D efforts, including coordination among research universities, and help attract capital investment to the region;
 - 3.5.2.1.3 Award funds to projects based on a reverse auction to maximize the cost-effectiveness and performance of the overall investment portfolio. Under a reverse auction, project bidders commit to certain operational outcomes at a particular price based on the established performance criteria of the auction.
 - 3.5.2.1.4 Provide for separate auctions within the overall fund in order to allow commercially riskier projects (e.g. higher levels of CO₂ capture or less tested technologies) to compete for support

based on different performance and eligibility criteria.

- 3.5.2.2 Fund Purposes. Demonstration, deployment and commercialization purposes for a competitive fund should be based on MGA Platform priorities, including: 1) CCS technologies; 2) advanced biomass conversion technologies for biomass to liquids, SNG, and power; 3) other advanced low-carbon energy technologies; 4) combined heat and power applications in the electric power and industrial sectors; 5) electricity storage; and 6) advanced low-carbon transportation technologies, including low-carbon fuels, advanced vehicle batteries, and others. While separate auction pools will be maintained for each of these high-priority technology areas, the MGGRA jurisdictions will also consider how the regional fund can be leveraged to strengthen links between sectors, such as the utility and transportation sector, by targeting cross-cutting technologies or infrastructure.
- 3.5.2.3 Sources of Fund Revenues. The fund may initially be supported using revenues from a carbon-based wires charge and/or another sector-specific or broader fee mechanism and initial allowance auction revenue. Over time, the fund will be increasingly supported by a transition to allowance value obtained either through auction or direct allocation of allowances.
- 3.5.2.4 Awarding of funding. Based on their reverse auction bids, winners will receive fixed annual performance-based payments per: 1) ton of CO₂ sequestered (for technologies and projects involving CO₂ capture and storage); 2) MWhrs of electricity or Btus of liquid fuels, syngas or SNG produced for renewable or near zero-carbon energy projects; or 3) other appropriate measure applicable to technology type. Performance-based payments will be made annually over 10 years from commencement of operations.
- 3.5.2.5 Program Management. The MGGRA jurisdictions will jointly manage the fund, including developing appropriate funding categories and amounts, deadlines, eligibility and performance criteria. The

jurisdictions will establish and revise technology goals based on the evolving status of emerging technologies and emissions reductions needs in different sectors, and the availability of alternative sources of technology funding.

- 3.6 Compliance Period. A compliance period is the length of time for which covered sources must submit allowances equivalent to their emissions, or face a penalty for failing to do so. The Advisory Group recommends that each compliance period should be 3 years in length.
 - 3.7 Banking. The Advisory Group recommends that the cap-and-trade program should allow unlimited banking of allowances and offsets credits. Allowances or offsets received or purchased in one year, therefore, can be banked and used in any subsequent year of the program.
 - 3.8 Borrowing. The Advisory Group recommends that limited borrowing should be allowed from no more than two years beyond the end of the current compliance period, provided borrowed allowances should be paid back with some “interest”.
 - 3.9 Early Action Credit. The Advisory Group recommends that early action should be recognized in the cap-and-trade program through a hybrid approach that rewards early actions using credits at the regional level, as well as allowing individual jurisdictions to further reward early action using allowances out of their own allowance budget. Two types of early action credit are recommended:
 - 3.9.1 *Early reduction by covered entities*. Covered entities should be able to earn early reduction allowances in addition to the starting allowance budget by reducing emissions at covered facilities. Emissions reductions achieved between the release of the final cap-and-trade program Model Rule and the program’s commencement date will be eligible to receive early action credit.
 - 3.9.2 *Other early action*. The Advisory Group also recommends that to the extent participating jurisdictions wish to reward early action that does not qualify for allowances under 1.9.1, those reductions should be awarded allowances out of (and not in addition to) the jurisdiction’s allowance budget.
- 4.0 OFFSETS
- 4.1 Offsets Program. The Advisory Group recommends that the states and province develop an offsets component as part of the cap-and-trade program.

- 4.2 Offsets Requirements. Offsets must be real, additional, verifiable, permanent, and enforceable so that they do not compromise the integrity of the cap-and-trade program:
- 4.2.1 *Real*. Offsets must represent actual emission reductions and not artifacts of incomplete or inaccurate accounting. The effects of a project on GHG emissions must be comprehensively accounted for, and “leakage” in emissions must be factored into the quantification of emission reductions. Conservative assumptions should be used where there are uncertainties in quantifying emission reductions or removals.
 - 4.2.2 *Additional*. The reductions resulting from offset projects must be shown to be “in addition to” reductions that would have occurred without the incentive provided by offset credit. To be eligible for offsets, offset projects cannot be required by law or regulations, and must exceed baseline criteria. The baseline should use standardized criteria (including but not limited to, performance standards, financial feasibility criteria, market penetration, and project start date) that serve to exclude “business as usual” projects from eligibility.
 - 4.2.3 *Verifiable*. Offsets must result from projects or programs whose performance can be readily monitored and verified, and whose effects can be measured with reasonable precision and certainty.
 - 4.2.4 *Permanent*. Emission reductions or removals must be backed by guarantees if they can be reversed, i.e., re-emitted to the atmosphere. For emission reductions or sequestration activities that can be reversed, adequate safeguards should be established to minimize the risk of reversal, or a mechanism should be provided for the replacement of those tons.
 - 4.2.5 *Enforceable*. Offsets must be consistent with regulations and administrative rules that define their creation, provide for transparency, and meet defined standards of ownership to avoid double counting.
- 4.3 Regional Coordination and Reciprocity
- 4.3.1 The offsets program must be consistently implemented from jurisdiction to jurisdiction. To facilitate this, a regional organization should be formed to help jurisdictions evaluate project types, offset protocols, and individual offset project applications. However, participating jurisdictions should make all final decisions.

- 4.3.2 All offset protocols used by participating jurisdictions must be reviewed and approved through a regional process. However, each participating jurisdiction reserves the right to select the regionally approved offset protocols for which it will provide application support, review and approval.
- 4.3.3 Offsets awarded by any participating jurisdiction should be eligible in every other participating jurisdiction.
- 4.4 Offset Protocol Development. The offset program should employ standards-based protocols to reduce the administrative burden of the program, and improve certainty for project developers. Initial offset project categories and evaluation protocols should be established before program launch. The following mechanism should be used to establish this initial list, and to incorporate additional categories and evaluation criteria over time.
 - 4.4.1 Category evaluation and protocol development should be spearheaded by strong technical and scientific advisory committees.
 - 4.4.1.1 Technical Committees would be established for each offset category being considered by signatory states and provinces. Technical Committees would be comprised of subject matter experts and would be tasked with drafting offset project protocols. The Technical Committees should report their findings to the Scientific Committee.
 - 4.4.1.2 The Scientific Committee is a standing body of scientists and experts with an in-depth understanding of climate science and offset program principles and implementation challenges. The Scientific Committee can accept, reject, or suggest modifications to the Technical Committees.
 - 4.4.1.3 In developing those protocols, the Technical and Scientific Committees should consider the Offset Program Design Principles, Carbon Offset Requirements, and other guidelines agreed to by the signatory states and provinces.
 - 4.4.2 In the interest of promoting transparency, protocols approved by the scientific committee should be made available for public comment.
 - 4.4.3 Agency Heads of participating states and provinces would collectively consider, through a collaborative process, those

public comments when deciding whether or not to adopt a protocol throughout the region.

- 4.4.4 At any time, anyone may propose protocols for new types of projects to the regional organization, for consideration pursuant to the procedures in 4.4.
- 4.4.5 Protocols for quantification of emission reductions/removals and for project monitoring should be as standardized to the extent possible, while ensuring accuracy. Ideally, there should only be one approved protocol for each type of project, but additional protocols may be adopted if warranted.
- 4.4.6 Offsets Types. Initial project categories should be identified and prioritized for protocol development under section 4.3 to the extent that they meet the following criteria:
 - 4.4.6.1 Offsets easily and credibly meet the Offset Program Design Principles and Carbon Offset Requirements;
 - 4.4.6.2 Offsets can incentivize new technologies or new practices;
 - 4.4.6.3 It is unlikely that a project category would be unregulated under a Midwestern cap-and-trade program, or by complementary policies developed through the Greenhouse Gas Accord process;
 - 4.4.6.4 It is unlikely that a project category would be unregulated under a federal cap-and-trade program;
 - 4.4.6.5 There is stakeholder support for project categories;
 - 4.4.6.6 There is a high quantity of cost-effective reduction opportunities;
 - 4.4.6.7 There are environmental and economic co-benefits;
 - 4.4.6.8 Protocols already exist that employ standardized benchmark criteria for evaluating project categories;
 - 4.4.6.9 There is administrative simplicity for project developers and state regulators; and,
 - 4.4.6.10 Any other criteria adopted by the region.
- 4.5 Limits on Use of Offsets. The use of offsets should be constrained to [10 to 50 percent of the emission reductions to be achieved by

the program when compared to business as usual projections]. Modeling results should inform the determination of usage constraints, and any determinations regarding the need and price of triggers that would expand usage limits.

4.6 Geographical Location of Offsets.

4.6.1 Initially, the geographic scope should be constrained to MGA GHG Accord signatory jurisdictions and those states and provinces that have entered into an MOU with the MGA GHG Accord signatory jurisdictions.

4.6.1.1 At a minimum that MOU should require the state or province to carry out certain administrative tasks related to evaluation of offset projects.

4.6.1.2 States and provinces not apart of the MGA GHG Accord could also be required to have a GHG regulatory program of comparable or greater stringency than that established by the MGA GHG Accord.

4.6.2 As the program evolves, states and provinces should consider incorporating the Clean Development Mechanism (CDM) and Joint Implementation (JI) programs.

4.6.3 Any determination about whether to allow offset credits from other regulatory offset programs should follow the procedures for adding offset project categories. Therefore, such decisions should be made by Agency Heads, and only after thorough consideration by the Technical and Scientific Committees and public comment.

4.7 Offsets Project Review.

4.7.1 To maximize certainty for project developers, a two-step review process should be adopted for individual projects. The first step – a consistency determination – provides for preliminary review before project commencement. The second step – monitoring and verification – is the application for offset allowances equal to the actual emissions reductions or sequestrations demonstrated to have occurred at the project location.

4.7.2 Applications for consistency determinations and applications for monitoring and verification must be verified by accredited, independent, third-party verifiers.

4.7.3 Third-party verified applications must be reviewed by states or provinces.

- 4.7.4 To ensure rigor, periodic auditing should be performed by states, provinces, or the centralized administrative body.
- 4.7.5 It is critical that the regional offset program be consistently implemented from jurisdiction to jurisdiction.
- 4.7.6 Project applications should be filed in accordance with the following guidelines:
 - 4.7.6.1 For an offset project located in one participating jurisdiction (in whole or in part), the consistency application must be filed with the appropriate regulatory agency in that jurisdiction.
 - 4.7.6.2 For an offset project located wholly outside all participating jurisdiction, the consistency application may be filed with the appropriate regulatory agency in any one participating jurisdiction, provided a copy of the consistency application is also filed with the cooperating regulatory agency in the jurisdiction where the offset project is located.
 - 4.7.6.3 For an offset project located in more than one participating jurisdiction, the consistency application must be filed in the participating jurisdiction where the larger part of the CO₂ equivalent emissions reduction or carbon sequestration due to the offset project is projected to occur.
 - 4.7.6.4 If the jurisdiction of primary location does not provide services for a particular offset category, a project may apply to any jurisdiction that provides such services.

5.0 MANDATORY EMISSIONS REPORTING

- 5.1 Start Date. Mandatory reporting of emissions for the six families of greenhouse gases included under the cap (carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride) will commence in January 2011 for all entities and facilities subject to reporting (with data collection beginning in 2010). [Reporting should begin at least one year before cap compliance obligations begin.]
 - 5.1.1 Prior to the start of the mandatory reporting program, the MGGRA jurisdictions will establish the essential requirements for reporting by all entities and facilities required to report in each MGGRA jurisdiction.

- 5.1.2 For purposes of converting emissions to CO₂e, it is recommended that the values listed in the GWP table contained in the TCR General Reporting Protocol, Version 1.1 be used.
- 5.2 Threshold for Reporting. The entities and facilities subject to reporting are:
 - 5.2.1 Facilities with [nameplate capacity >= 25MW or] annual emissions equal to or greater than [10,000] metric tons of CO₂e. This includes all entities included under the cap as well as some below the cap threshold.
 - 5.2.1.1 Level of Reporting Required. Only direct, stationary combustion and process emission sources are required to report. Sources within a facility with minimal contribution to the facility's emissions profile may be exempted from reporting.
 - 5.2.1.2 Reporting of Emissions from Biomass. Reporting will required even if emissions are not covered under the cap.
 - 5.2.2 [Pending scope group decision on inclusion of upstream fuels: Entities producing or blending fuels, pending scope group determination on coverage of fuels in cap]
 - 5.2.3 As each MGGRA jurisdiction collects additional emissions data from entities and facilities required to report, data will be made available to all MGGRA jurisdictions for review and consideration for possible expansion of the cap-and-trade program to include additional sources and gases, as appropriate given confidentiality concerns.
 - 5.2.4 Nothing in the MGGRA program design would limit any state or province's discretion to require reporting earlier, at lower thresholds, or for entities and facilities not covered by the cap-and-trade program.
- 5.3 Reporting Authority. The Advisory Group recommends using a version of the Climate Registry Information System (CRIS) (hosted and managed by TCR), modified to support mandatory reporting, to collect and manage MGGRA's regional database of emissions information. In addition, jurisdictions may use the CRIS Common Reporting Framework to meet their individual jurisdictional database needs for emission collection, verification, and compliance.
- 5.4 Verification. MGGRA jurisdictions will require third party verification of reported emissions from entities and facilities that will be included under the cap.

- 5.5 [Subject to EPA determination on mandatory reporting at federal level.] For sources subject to reporting but not covered by the cap, third party verification will not be required, although reporters could be subject to agency review.
- 5.6 Costs will be taken into account when considering verification requirements.
- 5.7 Standards: Verification and accreditation should be consistent with ISO 14064-3 and ISO 14065 standards.
- 5.8 Accreditation of verifiers: [internal/external]
MGGRA will develop programs to promote voluntary reporting to TCR (which includes entity-level verification).

6.0 COMPLIANCE AND ENFORCEMENT RECOMMENDATIONS

- 6.1 Each participating jurisdiction will retain and/or enhance its regulatory and enforcement authority and responsibilities to enforce compliance with the cap-and-trade program within its own jurisdiction.
- 6.2 Each covered entity or facility will demonstrate compliance with the cap-and-trade program by surrendering sufficient allowances following the end of each compliance period. To ensure transparency and maintain public confidence, certain data from the emissions reports, allowances, and offsets that are used for compliance will be made public in a timely manner.
- 6.3 If by the deadline for demonstrating compliance a covered entity or facility does not have sufficient allowances to cover its emissions for the previous compliance period, it shall be required to surrender [XX allowances and/or \$YY] for every metric ton of CO₂e not covered by an allowance at the deadline. This does not preclude other penalties allowed under individual state or provincial laws.
- 6.4 The MGGRA jurisdictions recognize that during the first compliance period, both they and the entities and facilities covered by the cap-and-trade program will likely encounter issues that arise in the implementation of any new program. Consequently, the MGGRA jurisdictions are committed to providing appropriate technical and other compliance assistance to the program participants.
- 6.5 The participating jurisdictions will ensure accounting systems are in place to prevent using allowances, tradable units, and offsets more

than once for compliance.

7.0 PROGRAM IMPLEMENTATION, COORDINATION, AND REVIEW

- 7.1 The cap-and-trade program will launch starting January 1st, 2012.
- 7.2 A Regional Administrative Organization will be established to reduce administrative costs and improve program transparency and consistency. The Organization will include a Board staffed by representatives from each participating jurisdiction, and may also employ additional staff. While the Organization will provide market oversight in addition to oversight provided by participating jurisdictions, it will be a technical assistance organization only and will not possess regulatory or enforcement authority itself. At a minimum, the Organization will:
 - 7.2.1 Coordinate the regional auction of allowances;
 - 7.2.2 Track emissions and provide public information on progress towards the MRGGA regional goal;
 - 7.2.3 Monitor and report on market activity, including any potential market manipulation;
 - 7.2.4 Serve as a forum for MRGGA Partner jurisdictions to update one another on program progress;
 - 7.2.5 Coordinate review and adoption of protocols for offsets;
 - 7.2.6 Coordinate review and adoption of updated reporting protocols;
 - 7.2.7 Coordinate review and issuing of offset credits; and
 - 7.2.8 Suggest criteria and means to accredit service providers to deliver validation and verification services.
 - 7.2.9 Facilitate and coordinate periodic, comprehensive program reviews.
- 7.3 Program Review. The cap-and-trade program will undergo, on a regular basis, periodic comprehensive review and revision, coordinated through the Regional Administrative Organization. This review will include a full assessment of the program and a determination of whether adjustments need to be made to the program based on its environmental results and market performance, as well as future scientific findings and technology developments. In particular, the review process will:
 - 7.3.1 Revisit and revise program emissions targets and trajectories;

- 7.3.2 Assess market prices and trends, including unanticipated price volatility and impacts, and adjust the program accordingly through revision of cost containment measures;
- 7.3.3 Consider adjustments to program scope of coverage, thresholds for inclusion and/or reporting, and point of regulation;
- 7.3.4 Consider the inclusion of new partner jurisdictions;
- 7.3.5 Revise compliance and enforcement provisions;
- 7.3.6 Revise offsets protocols;
- 7.3.7 Revise allowance distribution methodologies;
- 7.3.8 Considering revision of existing complementary policies, and determine whether additional complementary policies are required to help meet program goals.