

# Replacement Liability Provisions of California's Compliance Offset Program

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California Air Resources Board

April 7, 2011 Electric Power Research Institute Offsets Workshop

# Main Topics

- **Defining Replacement Liability**
- **Existing Provisions**
- **Alternatives**

## Replacement Liability

- **Invalidation of offset used for compliance**
  - **Entity that used the offset for compliance obligation must retire a compliance instrument**
  - **Entity does not face a penalty if it replaces the invalidated credit in time**
- **Types of eligible compliance instruments**
  - **Allowance**
  - **Valid compliance offset**

## Rationale for User Replacement Liability

- **Capped entities located in California and directly regulated under cap-and-trade**
- **Makes clear responsible party**
- **Offset Buyers**
  - **Assign and manage risk through private contracts**
  - **Encourages due diligence by project developers, verifiers, and buyers**
- **Ensures environmental integrity**

## Enforcement Provisions

- **Offset developers, verifiers, and OPRs attest to the accuracy and completeness of all information provided to ARB**
- **Attestations allow ARB to pursue direct enforcement against offset developers, verifiers, and offset project registries.**
- **Penalties pursuant to Health and Safety Code 38580**

## Stakeholder Comments

- **Stakeholders have told us that the current provisions on User replacement liability:**
  - **Have too long a time horizon to allow risk quantification**
  - **Have a time horizon too long to be consistent with market participants' risk management (reserve) policies**
  - **Raise the cost of using offsets, negating the cost containment purpose of offsets**

## Alternatives

- **Clarify under what circumstances an offset could be invalidated**
  - **What are the specific conditions?**
  - **What is the evidence threshold?**
- **Clarify process for invalidation**

## Finite Review Period Features

- **ARB would pursue User for replacement if offset invalidation occurred less than X years from issuance of the offset**
- **The period must be long enough to ensure multiple verifications by different verifiers**
- **ARB could pursue replacement or penalty against others involved in offset production (e.g. verifiers, project operators)**
- **ARB would still invalidate all offsets not yet used for compliance**
- **Holders of invalidated offsets would still have to seek recourse against project operators or registries through contractual arrangements**

## Finite Review Period (Continued)

- **Does the proposal address the concern?**
- **What length of period is needed?**
- **What other mechanisms could reduce invalidation risk?**

# Offset Reserve

**Stakeholders are considering reserves against invalidation**

- **Who would operate the reserve?**
- **Who would fund the reserve?**
- **Who would draw from the reserve? Under what rules?**
- **Is there moral hazard associated with reserves?**
- **Should there be separate reserves for sequestration and non-sequestration projects?**
- **What role for registries in the reserve**

## Additional Information

- **For upcoming meetings and events related to cap-and-trade please visit:**

**<http://www.arb.ca.gov/cc/capandtrade/capandtrade.htm>**

- **Join the cap-and-trade listserve at:**

**[http://www.arb.ca.gov/listserv/listserv\\_ind.php?listname=capandtrade](http://www.arb.ca.gov/listserv/listserv_ind.php?listname=capandtrade)**

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# Questions

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