State of Oregon

# Department of Environmental Quality

March 11 2021

**To:** Members of the Joint Committee on Transportation

**From:** Oregon Department of Environmental Quality

**Subject:** Program and policy implications of HB 3056

**This memo responds to questions and concerns raised during the Public Hearing for HB 3056. The Department of Environmental Quality appreciates the efforts of all entities – including Cherriots Transit District – to adopt the use of Cleaner Fuels. However, the proposal to exchange expired tax credits for Clean Fuels Program credits sets a concerning precedent that stands to undermine the Clean Fuels credit market and the environmental integrity of the program.**

**Clean Fuels credits are a regulatory tool used by fossil fuel suppliers to comply with the program. Issuing credits as proposed in HB 3056 will allow fossil fuels companies to comply with the program without achieving any real reduction in the carbon footprint of transportation fuels.**

## *HB 3056 Description*

As DEQ understands HB 3056, the agency would be required to issue to Cherriots a number of Clean Fuels Program credits, which represent tons of emissions reduced, equivalent to the value of expired tax credits that the transit agency was unable to monetize. Each Clean Fuels credit represents one ton of greenhouse gas emissions reduced, and their prices are not fixed or set by the program the way a tax credit is. Rather, the prices are set by private and some public parties trading credits in the program's credit market, and are generally based on the supply and demand for credits based on parties' understanding of the program and expectations about how compliance will be achieved in the future.

## *HB 3056 Impacts to the Clean Fuels Market*

According to information provided by Cherriots, the transit district has $5,928,184 in expired tax credits. Based on the current average Clean Fuels Program credit price ($125.74 in February 2021), Cherriots' tax credits would equate to 47,146 CFP credits. This is a significant infusion of credits into the Clean Fuels market with no associated reduction to the carbon intensity of Oregon's transportation fuels.

As of the end of the third quarter of 2020, the entire program-wide credit bank (all credits available to those needed for compliance) was 732,083 credits. Under the bill, DEQ would be required to generate approximately 47,000 new credits – or 6.5% of the program's total bank. This infusion of credits represents 40 times the number of credits Cherriots has generated in total over the last five years.

As the regulator of this environmental market, DEQ is careful to not forecast credit prices or comment on its expectations of future credit prices. However, it is understandable that participants may react to the sudden infusion of these additional credits and the added supply to the market. Action taken under the proposed bill may also lead to market uncertainty because of a belief or expectation that the legislature is willing to infuse additional credits in the future. This undermines the certainty that companies need to invest in lower carbon fuel technologies.

*Policy and Program Concerns*

The bill sets new precedent for the Clean Fuels Program in ways that are concerning and should be carefully considered. Specifically:

**HB 3056 awards credits without reducing the carbon intensity of transportation fuels**
In response to Representative Power's question during the public hearing, the legislature defined credits in the Clean Fuels Program as follows in ORS 468A.265(4):

> "Credit" means a unit of measure generated when a fuel with a carbon intensity that is less than the applicable low carbon fuel standard is produced, imported or dispensed for use in Oregon, such that one credit is equal to one metric ton of carbon dioxide equivalent.

This means that a credit in the Clean Fuels Program is created when enough of a low-carbon fuel is used in Oregon that it reduced a ton of carbon emissions. According to testimony provided by Cherriots Transit District, their expired tax credits were earned for investments made to operate and expand fixed-route bus services. While expanding transit service certainly provides social and environmental benefits, it does not reduce the carbon intensity of Oregon's transportation fuels, nor is it eligible for credits as defined by the legislature.

**HB 3056 awards credits for activities that occurred before the program was established**
Based on information provided by Cherriots, the transit investments were made before the establishment of the Clean Fuels Program. The program relies on a baseline standard set in 2015. That standard already considers and accounts for any activity that occurred prior to the program – meaning even if providing transit services was eligible for Clean Fuels Program credits, the investment or activities would need to occur *after* the baseline in order to generate credits under the program.

**HB 3056 stands to undermine the environmental integrity of the Clean Fuels Program**
Together, these actions – awarding credits with no associated transportation fuel greenhouse gas benefits *and* for activities that occurred before the program was established - stand to undermine the integrity of the Clean Fuels Program. These changes also create uncertainty in the market due to speculation about what future legislatures may allow to generate credits.

When the credits generated under the proposed HB 3056 are sold by Cherriots, it will allow regulated parties – namely fossil fuel suppliers - to comply with the program without achieving any carbon intensity reductions, leading to the state underachieving its environmental targets for the program in that year.

The Clean Fuels Program can play a prominent role in incentivizing a transit agency's decision to electrify their fleet. DEQ is ready to support Cherriots ongoing and good work to adopt lean fuels. A few opportunities in the near-term:

- DEQ will propose rules to our commission next week that allowing for upfront or "advanced" crediting of transit bus electrification.
- Additionally, the department will soon begin awarding grants with Volkswagen Settlement funds. Grant criteria provided preferences for projects that switch from conventional diesel engines to "cleaner fuels" including electricity. These grants can cover 100% of project costs for public entities (including most school and transit districts).

**Questions**

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