

FINAL BILL REPORT

E3SHB 1091

PARTIAL VETO C 317 L 21 Synopsis as Enacted

Brief Description: Reducing greenhouse gas emissions by reducing the carbon intensity of transportation fuel.

Sponsors: House Committee on Transportation (originally sponsored by Representatives Fitzgibbon, Slatter, Berry, Dolan, Bateman, Ramos, Simmons, Ramel, Senn, Peterson, Duerr, Ryu, Valdez, Callan, Kloba, Chopp, Ormsby, Frame, Macri, Pollet, Goodman and Bergquist; by request of Office of the Governor).

House Committee on Environment & Energy
House Committee on Appropriations
House Committee on Transportation
Senate Committee on Environment, Energy & Technology
Senate Committee on Ways & Means

Background:

Greenhouse Gas Reporting Requirements and State Limits.

The United States Environmental Protection Agency (EPA) and the Department of Ecology (Ecology) identify carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride as greenhouse gases (GHGs) because of their capacity to trap heat in the Earth's atmosphere. According to the EPA, the global warming potential (GWP) of each GHG is a function of how much of the gas is concentrated in the atmosphere, how long the gas stays in the atmosphere, and how strongly the particular gas affects global atmospheric temperatures. Under state law, the GWP of a gas is measured in terms of the equivalence to the emission of an identical volume of carbon dioxide over a 100-year timeframe (carbon dioxide equivalent or CO₂e).

Under the federal Clean Air Act, GHGs are regulated as an air pollutant and are subject to several air regulations administered by the EPA. These federal Clean Air Act regulations

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not part of the legislation nor does it constitute a statement of legislative intent.

include a requirement that facilities and fuel suppliers whose associated annual emissions exceed 25,000 metric tons of CO₂e report their emissions to the EPA. At the state level, GHG reporting is regulated by Ecology under the state Clean Air Act. This state law requires facilities, sources, and sites whose emissions exceed 10,000 metric tons of CO₂e each year to report their annual emissions to Ecology. Distributors of gasoline, diesel, and aircraft fuel whose GHG emissions exceed 10,000 metric tons and who pay fuel taxes to the Department of Licensing (DOL) must use the fuel sale information submitted for the DOL fuel tax purposes to report to the state the GHG emissions associated with the fuel.

Ecology and the Department of Commerce must report to the Governor and Legislature by December 31 of even-numbered years regarding total GHG emissions and GHG emissions by source sector in Washington. According to the most recent Ecology data, as of 2018 the total annual GHG emissions in Washington were estimated at 99.6 million metric tons (MMT) of CO₂e. Of these emissions, a total of 44.73 MMT CO₂e were attributable to transportation sources, of which on-road gasoline accounted for 22.33 MMT CO₂e and on-road diesel accounted for 8.87 MMT CO₂e.

In 2008 Washington enacted legislation that sets a series of limits on the emission of GHGs within the state. Ecology is responsible for monitoring and tracking the state's progress toward the emission limits. In 2020 the limits were updated to the following:

- By 2020, reduce overall emissions of GHGs in the state to 1990 levels, or 90.5 MMT.
- By 2030, reduce overall emissions of GHGs to 45 percent below 1990 levels, or 50 MMT.
- By 2040, reduce overall emissions of GHGs in the state to 70 percent below 1990 levels, or 27 MMT.
- By 2050, reduce overall emissions of GHGs in the state to 95 percent below 1990 levels, or 5 MMT, and achieve net-zero GHG emissions.

State Clean Air Act.

Ecology and seven local air pollution control authorities (local air authorities) have each received approval from the EPA to administer aspects of the federal Clean Air Act in Washington. Local air authorities have primary responsibility for administering the state and federal Clean Air Acts in counties which have elected to activate a local air authority or to form a multicounty air authority. In other areas of the state, Ecology is responsible for administering state and federal Clean Air Act programs.

Under the federal Clean Air Act, each state maintains a State Implementation Plan (SIP) that describes how the state implements clean air programs to achieve the federal National Ambient Air Quality Standards (NAAQS) for certain air pollutants, known as criteria pollutants. If the state does not achieve NAAQS in a portion of the state for a particular criteria pollutant, that area is considered to be in nonattainment, and the state must revise its SIP with the goal of regaining attainment with NAAQS. Areas that have previously been designated as nonattainment areas but that subsequently regained NAAQS compliance are

considered to be maintenance areas. In maintenance areas, the SIP must be revised to incorporate local maintenance plans designed to prevent those areas from relapsing into nonattainment status. Areas in Washington covered by maintenance plans for various criteria pollutants as of January 1, 2021, include areas of King, Pierce, Spokane, and Thurston counties, as well as the cities of Vancouver, Yakima, and Wallula. No areas of Washington are currently designated with nonattainment status.

Violations of Clean Air Act requirements are punishable by a variety of criminal and civil penalties. Civil penalties of up to \$10,000 per violation are authorized by the state Clean Air Act.

Fuel Content.

The state Motor Fuel Quality Act (MFQA), enacted in 1990, adopted motor fuel standards, authorized the Washington State Department of Agriculture (WSDA) to set state fuel standards, and established a sampling, testing, and enforcement program administered by the WSDA. Under the MFQA, it is unlawful to deceive the purchaser of fuel as to its nature or quality, among other aspects. Violations of this prohibition are enforced by the WSDA. Washington's Renewable Fuel Standard was enacted in 2006 as a component of the MFQA, and establishes requirements for the biodiesel content of diesel fuel, and the ethanol content of gasoline:

- Special fuel licensees must provide evidence that at least 2 percent of diesel fuel annually sold in Washington is biodiesel or renewable diesel fuel. This requirement will increase to at least 5 percent if the WSDA determines that both in-state feedstock and oilseed crushing capacity can satisfy a 3 percent requirement. The WSDA has not certified that the state has met this threshold.
- Motor vehicle fuel licensees must provide evidence that at least 2 percent of the total gasoline sold in the state is denatured ethanol. This ethanol requirement may be increased if the WSDA determines an increase would not jeopardize the state's continued attainment of federal Clean Air Act standards, and that the state can economically support the production of higher ethanol blends.

Clean Fuel Programs in Other States.

California and Oregon have each instituted policies that require reductions in the GHG emissions associated with transportation fuels, as measured against a standard unit of fuel energy (carbon intensity). California's program, which began in 2010, requires a 10 percent reduction by 2020 and a 20 percent reduction by 2030 in the carbon intensity of gasoline and diesel fuel, in conjunction with the use of fuels that serve as substitutes for those fuels. Oregon's program, which began in 2015, currently requires a 10 percent reduction by 2025 in the carbon intensity of transportation fuels, although additional targets for Oregon's program have been set for 2030 and 2035 by executive order but have not yet been adopted into program rules.

Both the California and Oregon programs function by assigning compliance obligations, also known as deficits, to persons associated with the production or import of fuels that exceed an average carbon intensity of fuel based on a baseline year. In tandem with the assignment of deficits, the programs provide for the generation of credits that denote the production or import of fuel with a carbon intensity of less than the baseline carbon intensity. Since 2019 California's program has allowed the generation of credits for certain other activities with a nexus to the transportation fuel supply chain, such as for the installation of electric vehicle charging infrastructure. The programs of both states measure the carbon intensity of transportation fuels based on a lifecycle analysis of direct and indirect GHG emissions associated with the production, distribution, and consumption of the fuels. Programs in both states provide exemptions for certain categories of transportation fuels.

2015 Transportation Revenue Package.

In 2015 the Legislature enacted a bill that raised revenue for transportation purposes from a variety of transportation-related sources ("Transportation Revenue Package"). Among other sources of revenue, the Transportation Revenue Package generated revenue by increasing fees for:

- enhanced and commercial driver's licenses; and
- vehicle weight fees that apply to passenger vehicles and motor homes.

In general, the enhanced and commercial driver's license fees are deposited into the Highway Safety Fund (used for driver's license implementation, driver improvement, and financial responsibility, among other programs), while the vehicle weight fees are deposited into a combination of the Multimodal Transportation Account (used for transportation purposes) and the Freight Mobility Multimodal Account (used for certain freight mobility projects approved by the Freight Mobility Strategic Investment Board). However, if a clean fuel standard policy is adopted by rule or otherwise initiated by a state agency prior to July 1, 2023, the additional revenue raised from the driver's license and vehicle weight fee increases in the 2015 Transportation Revenue Package would be redirected from the Highway Safety Fund, Multimodal Transportation Account, and Freight Mobility Multimodal Account, and would instead be deposited into the Connecting Washington Account (an account which is used for projects that have been identified in a transportation appropriations act as "Connecting Washington" projects or improvements).

Biofuel Refinery Siting.

The energy facility site evaluation council (EFSEC) is responsible for making certification recommendations to the Governor for certain new energy facility construction or existing facility expansion proposals. Facilities capable of processing at least 25,000 barrels per day of biofuel into refined products must use the EFSEC certification process for siting, unless the production takes place in an existing industrial facility. Energy facilities of any size that exclusively use alternative energy resources, such as wind power, can also opt into the

EFSEC review and certification process.

Summary:

Program Goal.

The Department of Ecology (Ecology) is directed to adopt a rule establishing a Clean Fuels Program (CFP) limiting the greenhouse gas (GHG) emissions attributable to each unit of transportation fuel (carbon intensity) to 20 percent below 2017 levels by 2038. The rule must reduce the overall, aggregate carbon intensity of transportation fuels used in Washington. The rule may only require aggregate carbon intensity reductions, and may not require a reduction in carbon intensity to be achieved by any individual type of transportation fuel. The rule must establish a start date for the program of no later than January 1, 2023, but the program may not begin assigning compliance obligations or allowing the generation of credits until the Legislature enacts an increase in the state motor vehicle and special fuel tax of at least five cents per gallon.

In reaching the carbon intensity reduction of 20 percent below 2017 levels by 2038, Ecology's rules must reduce the carbon intensity of transportation fuels each year relative to the previous year of the CFP by no more than:

- 0.5 percent in 2023 and 2024;
- 1 percent in 2025, 2026, 2027;
- 1.5 percent in 2028, 2029, 2030, and 2031; and
- 0.0 percent in 2032 and 2033.

In addition, Ecology may not increase the carbon intensity reductions required under the CFP by more than 10 percent until:

- there is at least a 15 percent net increase in in-state liquid biofuel production and the use of foodstocks grown or produced in Washington;
- at least one new or expanded biofuel production facility representing at least 60 million gallons of biofuel production or production capacity per year has received all siting, operating, and environmental permits and any timely and applicable appeals of such permits have concluded. At least one new facility producing at least 10 million gallons of biofuel production or production capacity must be part of achieving this threshold; and
- a Joint Legislature Audit and Review Committee (JLARC) report on the first five years of program operations has been completed, and the 2033 regular legislative session has adjourned.

Covered and Exempt Fuels.

Electricity and liquid and gaseous fuels are within the scope of the CFP, so long as the fuels or electricity are used to propel motor vehicles or are intended for transportation purposes

(transportation fuels). Excluded from the CFP carbon intensity reduction requirements are the following:

- transportation fuel that is exported or otherwise not used in Washington;
- transportation fuel that is used for the propulsion of all aircraft, railroad locomotives, or vessels;
- military tactical vehicles and tactical support equipment;
- transportation fuels that are used in volumes below thresholds adopted by rule by Ecology; and
- any other fuels that Ecology may adopt rules to exempt in order, with respect to similar GHG or low carbon fuel programs, to avoid mismatched incentives, fuel shifting between markets, or other outcomes counter to the intent of the CFP.

Until January 1, 2028, the following fuels are also exempt from the CFP's carbon intensity reduction requirements:

- special fuel used off-road in vehicles used primarily to transport logs;
- dyed special fuel used in vehicles that are not designed to transport persons or property, not designed to be operated on highways, and that are used primarily for construction work, including timber harvest and mining; and
- dyed special fuel used for agricultural purposes that are exempt from state fuel taxation.

Mechanics of the Clean Fuels Program.

The rule adopted by Ecology to implement the CFP must include:

- standards for assigning levels of GHG emissions attributable to transportation fuels based on a lifecycle analysis that considers emissions from the production, storage, transportation, and combustion of the fuels, and associated changes in land use. Ecology must establish separate carbon intensity standards for gasoline and its substitutes and diesel and its substitutes;
- processes for assigning and verifying bankable, tradeable credits for the production, import, or dispensation for use of transportation fuels with associated lifecycle GHG emissions that are less than the 2017 baseline carbon intensity levels established by Ecology, or when other specified activities are undertaken that support the reduction of GHG emissions associated with transportation in Washington;
- a requirement that producers or importers of transportation fuels that are ineligible to generate credits must register in the CFP;
- the option to elect to register and earn credits in the CFP for: (1) persons associated with transportation fuels with a carbon intensity below the carbon intensity standard; and (2) persons associated with exempt transportation fuels, including electricity and fuel used to propel vessels, railroad locomotives, or aircraft;
- a determination of the carbon intensity of electricity supplied by electric utilities participating in the CFP based on the mix of generating resources used by each electric utility, and mechanisms that allow for the certification of electricity that has a carbon intensity of zero, but that do not require electricity to have a carbon intensity

- of zero in order to be eligible to generate credits;
- mechanisms that allow for the assignment of credits to an electric utility for, at minimum, residential electric vehicle charging or fueling;
- cost containment mechanisms that are harmonized with other states with similar CFP requirements. Ecology must consider a credit price cap or other cost-containment measures if necessary to harmonize market credit costs with other states with similar CFP requirements; and
- a credit clearance market, in which regulated parties that have a net deficit balance at the end of a compliance period must participate. The credit clearance market must provide an opportunity for regulated parties to purchase credits pledged by credit sellers at no more than a maximum price of \$200 in 2018 dollars for 2023, adjusted for inflation.

Except where inconsistent with specific statutory direction from the Legislature, Ecology's CFP rule must seek to harmonize with similar programs that have been adopted by other states with significant amounts of transportation fuel supplied to or from Washington.

Ecology may require electric utilities and transportation fuel suppliers to submit GHG emissions data and information that is different from the types of data currently submitted to the state by those entities. Ecology may also require periodic reporting on CFP activities from producers and importers of transportation fuels. Transactions that transfer ownership of fuels required to be covered by the CFP must be accompanied by documentation assigning compliance responsibility for the fuels. To the extent practicable, CFP reporting rules for persons associated with the supply chains of transportation fuels must be consistent with the reporting procedures of similar clean fuels programs in other states and with other state programs that require similar information to be reported by regulated parties, including electric utilities.

Ecology must conduct a biennial review of innovative technologies and pathways to reduce carbon and generate credits, and must modify rules or guidance as needed to maintain stable credit markets.

Alternative Credit-Generating Mechanisms.

In addition to the provision of transportation fuel with a carbon intensity below the Ecology-established standard, Ecology's CFP rules may allow the generation of credits from specified activities related to the reduction of GHG emissions associated with transportation, including:

- specified carbon capture and sequestration projects, including crude oil production projects, project-based refinery mitigation, and direct air capture;
- deployment of machinery and equipment used for certain nonfossil feedstocks;
- the fueling of electric vehicles by commercial, public, and nonprofit entities that are not electric utilities; and
- the use of smart vehicle charging technology that results in electric vehicle fueling during times of comparatively low carbon intensity of the electric grid.

Ecology's rules must allow the generation of credits based on capacity for zero emission vehicle infrastructure, and may allow the generation of credits from the provision of low-carbon fuel infrastructure. Ecology's rules may establish limits on the number of credits available from alternative credit-generating mechanisms, and any limits on refueling infrastructure credits must consider the return on investment necessary for a credit-generating activity to be financially viable.

Ecology's rules must also allow the generation of credits from 10 categories of state transportation investments, but must limit the number of credits earned each year from state transportation investments to 10 percent of total CFP credits.

Public Reporting Requirements.

Beginning in 2025, Ecology must submit a report to the Legislature every year on May 1 detailing certain information regarding the previous year's CFP activities, including volumes of credits and transportation fuels. An estimate of probable costs or cost savings per gallon of gasoline and diesel attributable to the CFP must be prepared annually by an independent consultant under contract to Ecology, and must be announced to the news media in a press release when the annual report is submitted to the Legislature. Ecology must also contract for a one-time forecast to be submitted to the Legislature by July 1, 2022, and that estimates, using multiple methodologies, probable costs or cost savings per gallon of gasoline and diesel from the CFP. In annual reports or other public documents or communications that refer to assumed public health benefits from the CFP, Ecology must distinguish between pollutant reductions from the CFP and those reductions primarily attributable to vehicle emission standards.

The Department of Commerce must develop a periodic fuel supply forecast to project the availability of fuels and credits necessary for compliance with CFP requirements. This forecast must be finalized no later than 90 days before the start of a CFP compliance period.

By December 1, 2030, the Joint Legislative Audit and Review Committee is required to perform an analysis of the first five years of the CFP. This analysis must include the costs and benefits of the program and an evaluation of the information summarized by Ecology in their annual reports.

Emergency and Forecast Program Deferrals.

If the Department of Commerce's periodic fuel supply forecast predicts that there will not be sufficient credits during an upcoming compliance period, Ecology must issue a forecast deferral of CFP compliance obligations.

Ecology must issue an emergency deferral of the CFP in the event that extreme or unusual circumstances exist that prevent fuel distribution and result from specified causes, including

a natural disaster.

Ecology's emergency or forecast deferral orders must specify the duration of the deferral, the type of applicable fuel, and the applicable methods for deferring compliance with CFP requirements, which may include temporary adjustments to the carbon intensity standard, the carryover of deficits accrued during a deferral, or a suspension of deficit accrual.

Ecology may also issue or renew a full or partial deferral for one calendar quarter applicable to a person if the person cannot comply with CFP requirements for reasons beyond the person's reasonable control.

Other Provisions.

The current distribution is retained for revenues granted by the 2015 Transportation Revenue Package, eliminating changes that would have been triggered as a result of the establishment of the CFP.

Ecology may require that persons electing or required to participate in the CFP pay a fee to cover the direct and indirect costs to Ecology and the Department of Commerce for developing and implementing the CFP. If Ecology elects to require program participants to pay a fee, it must adopt rules to set a payment schedule and the amount of the fee, and must enter into an interagency agreement with the Department of Commerce and complete a biennial workload analysis. Fees are deposited into a Clean Fuels Program Account (Account) used to carry out the CFP.

Ecology must establish and consult with a forestland and agricultural landowner stakeholder advisory panel to solicit input on how to incentivize the sequestration of GHGs on forest and agricultural lands through program credit allotment.

Violations of CFP requirements are subject to civil and criminal penalties under state Clean Air Act authority. Penalties collected from CFP violations must be deposited into the Account.

Fifty percent of revenues earned by electric utilities from electricity supplied to retail customers to generate credits under the CFP must be used for transportation electrification, which may include the production and provision of hydrogen. Of this 50 percent, 60 percent of the transportation electrification projects must be in or directly benefit federal Clean Air Act maintenance or nonattainment areas, areas at risk of maintenance or nonattainment designation, areas designated as maintenance or nonattainment, or areas identified by the Department of Health as disproportionately impacted communities, if such areas are within the service area of the utility. For the other 50 percent of revenues, each electric utility must spend revenues on programs or projects selected from a list developed jointly by Ecology and the Department of Transportation. The list must be developed based on greenhouse gas emission impacts and transportation sector decarbonization potential,

and must include at least four categories of projects or programs, including the provision of zero emission vehicles at no cost or a discount to certain entities and grid capacity expansions to enable transportation electrification investments.

The generation, purchase, sale, transfer, or retirement of CFP credits is not subject to the business and occupation tax. A tax preference performance statement is not required for this exemption from the business and occupation tax.

All CFP rulemaking must meet the standards that apply under the Administrative Procedure Act to significant legislative rules, which includes evaluating the costs and benefits of the proposed rule and identifying least burdensome alternatives.

Biofuel refineries capable of producing between 1,500 and 25,000 barrels per day of biofuel may elect to receive site certification as an energy facility through the Energy Facility Site Evaluation Council (EFSEC) siting process.

Ecology, in coordination with other agencies as appropriate, must develop recommendations for potential permitting process improvements for industrial projects that would contribute to achieving state emission limits. Ecology must provide increased clarity on areas of the state that may be suitable for siting projects with a lower potential for negative environmental impacts, and must recommend potential improvements and any additional studies needed. Ecology must convene stakeholders in this process and must consult with tribes. Ecology and the Department of Commerce must submit an interim progress report with initial policy recommendations by December 1, 2021, and a final report by December 1, 2022.

To the extent that the CFP conflicts with the state Motor Fuel Quality Act and its biofuel requirements, the CFP's requirements supersede.

A null and void clause is included. A severability clause is included, accompanied by specific instruction that in the event of litigation on the provisions related to the delay in the decrease in carbon intensity requirements based on biofuel facility siting or feedstock availability or any other CFP provisions, it is the Legislature's intent that the CFP continue to be enforced.

Votes on Final Passage:

House	52	46	
Senate	27	20	(Senate amended)
House			(House refuses to concur in Senate amendments/asked Senate to recede from amendments)
Senate			(Senate insisted on its position/asked House for a conference)

Conference Committee

Senate	26	23
House	54	43

Effective: July 25, 2021

Partial Veto Summary: The Governor vetoed the provision that prohibited the Department of Ecology from assigning compliance obligations or allowing the generation of credits under the Clean Fuels Program until the Legislature enacts an increase in the state motor vehicle and special fuel tax of at least 5 cents per gallon.