
HOUSE BILL 1659

State of Washington

68th Legislature

2023 Regular Session

By Representatives Dye and Klicker

Read first time 01/30/23. Referred to Committee on Environment & Energy.

1 AN ACT Relating to preventing carbon market price manipulation;
2 amending RCW 70A.65.290 and 70A.65.100; adding a new section to
3 chapter 43.09 RCW; creating new sections; and providing an expiration
4 date.

5 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

6 NEW SECTION. **Sec. 1.** (1) The legislature recognizes that
7 following the stock market crash of 1929, the public lost confidence
8 in United States markets. In 1933, congress passed the securities act
9 and in 1934 it passed the securities exchange act. The purpose of
10 these laws was to require companies offering securities for sale to
11 the public to be truthful and transparent about their business, the
12 securities they are selling, and the risks involved in investing in
13 those securities. The laws also required those who sell to treat
14 investors fairly and honestly. The securities exchange act
15 established the securities and exchange commission as an independent
16 regulator to protect investors, maintain fair and efficient markets,
17 and facilitate capital formation. Reflecting on this history, the
18 legislature wishes to maintain, and never lose, the confidence of the
19 public in the functioning of Washington state's first multibillion
20 dollar market of regulatory compliance instruments, which has been
21 created under the climate commitment act. The legislature wishes to

1 study how an independent oversight agency might be best structured to
2 maintain public confidence and prevent market manipulation and bidder
3 collusion. The legislature also wishes to study whether the early
4 years of carbon market operations result in any suboptimal outcomes
5 that would negatively impact Washington consumers in the form of
6 artificially or inordinately high energy and consumer good prices,
7 beyond the substantial price increases that the programs, even when
8 functioning as intended, have been forecast to cause.

9 (2) The legislature is concerned that the department of ecology
10 is not well suited to police the market and proactively report on any
11 shortcomings that may arise. The department of ecology, consistent
12 with the express and unequivocal priorities of the governor, has
13 advocated before the committees of the legislature for the
14 establishment of the cap and invest program it is now tasked with
15 overseeing and will gain dozens of new full-time equivalent employees
16 to administer this program. It is understandable that department of
17 ecology employees may find it difficult to report news about the cap
18 and invest program that may reflect poorly on its administration of
19 the program or the success of a featured policy initiative championed
20 by those that fund and administer the department. Furthermore, the
21 legislature observes that the department of ecology has no expertise
22 in regulating a billion dollar market in tradeable compliance
23 instruments. It is due to this very lack of expertise that the
24 department of ecology is contracting with a third-party entity to
25 actually run the allowance auctions. For these reasons, it is the
26 intent of the legislature to:

27 (a) Establish and structure an independent agency for oversight
28 of the market, and integrate it into the existing cap and invest
29 program;

30 (b) Study mechanisms to guard against bidder collusion and market
31 manipulation;

32 (c) Thoroughly audit the program's functioning at the conclusion
33 of the first compliance period; and

34 (d) Ensure that the existing exemption from public disclosure
35 under the climate commitment act does not preclude the release of key
36 information that will allow the public to judge whether the carbon
37 market is functioning with integrity and in a manner that does not
38 result in artificial inflation of consumer prices.

1 NEW SECTION. **Sec. 2.** (1) By December 1, 2024, the Washington
2 state institute for public policy must submit a report to the
3 appropriate committees of the legislature that:

4 (a) Recommends criteria for the legislature to consider in the
5 future establishment of an office, agency, or entity independent from
6 the department of ecology that will be assigned duties for the
7 regulation and oversight of the compliance instrument auctions and
8 markets created by chapter 70A.65 RCW. The primary mission of such an
9 office, agency, or entity is to ensure fair, efficient, and orderly
10 functioning in the markets created by chapter 70A.65 RCW. The
11 recommendations for the establishment of an office, entity, or agency
12 must consider how to maximize its independence from other
13 environmental regulatory agencies and ensure its neutrality with
14 respect to the greenhouse gas emissions reduction policy outcomes
15 intended to be achieved by the program; and

16 (b) (i) (A) Addresses how other jurisdictions with greenhouse gas
17 emission trading programs balance public transparency with the
18 interests of market participants in confidentiality; and

19 (B) Identifies any rules or other policies these other
20 jurisdictions have established to prevent agency employees who obtain
21 knowledge of market trading activities exempt from public disclosure
22 under RCW 70A.65.100(9) from accepting employment from or otherwise
23 working to provide advantage or insider information to market
24 participants after leaving state service; and

25 (ii) Identifies best practices that provide the greatest degree
26 of public information and market oversight without detracting from
27 allowance market participation or other efficient auction or trading
28 market functioning.

29 (2) The report to the legislature must assess whether the rules
30 adopted by the department of ecology to guard against bidder
31 collusion and minimize the potential for market manipulation are
32 consistent with best practices employed by other jurisdictions with
33 market-based trading programs similar to the program established by
34 chapter 70A.65 RCW for balancing the competing public interests of:

35 (a) Public disclosure and transparency; and

36 (b) The need to guard against bidder collusion and minimize the
37 potential for market manipulation.

38 (3) The report to the legislature may include recommendations for
39 changes to chapter 70A.65 RCW or the rules adopted by the department

1 of ecology under chapter 70A.65 RCW in light of the findings
2 contained in the report.

3 NEW SECTION. **Sec. 3.** A new section is added to chapter 43.09
4 RCW to read as follows:

5 (1)(a) The legislature finds that a performance audit of the
6 effectiveness and efficiency of the cap and invest program created in
7 chapter 70A.65 RCW, which is currently anticipated to collect as
8 state revenue more than \$3,600,000,000 in its first five years, is
9 appropriate for accountability, program improvement, and oversight.
10 The legislature observes that performance audits differ from
11 financial and accountability compliance audits in that performance
12 audits evaluate the efficiency and effectiveness of government
13 programs with the goal of making them work better. Performance audits
14 compare what an agency is doing versus leading practices and look for
15 improved outcomes that could include saving money or better processes
16 for delivering the same service to the public.

17 (b)(i) The legislature intends for a state auditor's office
18 performance audit to occur and finds it appropriate for several
19 reasons: The legislature finds that public trust and confidence in
20 the audit will be enhanced if it is conducted by a separately elected
21 statewide official who has no constituency that relies on the funding
22 that the auctions under chapter 70A.65 RCW provide, and no
23 constituency that has to pay for the compliance instruments and other
24 program costs, but is instead neutral on whether the program is
25 characterized as having been successfully implemented.

26 (ii) It is the intent of the legislature that the performance
27 audit provide, at a minimum, a comparative view of pertinent program
28 effectiveness and efficiency including, but not limited to, costs per
29 metric ton of greenhouse gas reduced under chapter 70A.65 RCW
30 compared to costs per metric ton of greenhouse gas reduced under
31 other greenhouse gas emissions reduction programs, the relative cost
32 of program administration born directly or indirectly by regulated
33 entities, and whether state oversight of the third-party auction
34 provider is consistent with best practices.

35 (iii) The state auditor's office performance audit team may make
36 such recommendations as are consistent with government accounting
37 standards for similar audits.

38 (2) After December 31, 2026, the state auditor shall conduct a
39 comprehensive performance audit of the cap and invest program

1 established by chapter 70A.65 RCW covering the first compliance
2 period of the program.

3 (3) The state auditor shall complete the audit and publish a
4 report with its findings by December 31, 2027.

5 (4) This section expires July 1, 2028.

6 **Sec. 4.** RCW 70A.65.290 and 2021 c 316 s 32 are each amended to
7 read as follows:

8 (1) By December 1, 2029, the joint legislative audit and review
9 committee must analyze the impacts of the initial five years of
10 program implementation and must submit a report summarizing the
11 analysis to the legislature. The analysis must include, at minimum,
12 the following components:

13 (a) Costs and benefits, including environmental and public health
14 costs and benefits, associated with this chapter for categories of
15 persons participating in the program or that are most impacted by air
16 pollution, as defined in consultation with the departments of ecology
17 and health and as measured on a census tract scale. This component of
18 the analysis must, at a minimum, assess the costs and benefits of
19 changes in the following metrics since the start of the program:

20 (i) Levels of greenhouse gas emissions and criteria air
21 pollutants for which the United States environmental protection
22 agency has established national ambient air quality standards;

23 (ii) Fuel prices; and

24 (iii) Total employment in categories of industries that are
25 covered entities. The categories of industries assessed must include,
26 but are not limited to, electric utilities, natural gas utilities,
27 oil refineries, and other industries classified as emissions-
28 intensive and trade-exposed;

29 (b) An evaluation of the information provided by the department
30 in its 2027 program evaluation under RCW 70A.65.070(3);

31 (c) A summary of the estimated total statewide costs and benefits
32 attributable to the program, including state agency administrative
33 costs and covered entity compliance costs. For purposes of
34 calculating the benefits of the program, the summary may rely, in
35 part, on a constant value of the social costs attributable to
36 greenhouse gas emissions, as identified in contemporary
37 internationally accepted estimates of such global social cost. This
38 summary must include an estimate of the total statewide costs of the

1 program per ton of greenhouse gas emissions reductions achieved by
2 the program; (~~and~~)

3 (d) An evaluation of the impacts of the program on low-income
4 households; and

5 (e) An evaluation of whether the rules adopted by the department
6 to guard against bidder collusion and minimize the potential for
7 market manipulation have been successful at achieving those outcomes.

8 (2) This section expires June 30, 2030.

9 **Sec. 5.** RCW 70A.65.100 and 2022 c 181 s 3 are each amended to
10 read as follows:

11 (1) Except as provided in RCW 70A.65.110, 70A.65.120, and
12 70A.65.130, the department shall distribute allowances through
13 auctions as provided in this section and in rules adopted by the
14 department to implement these sections. An allowance is not a
15 property right.

16 (2)(a) The department shall hold a maximum of four auctions
17 annually, plus any necessary reserve auctions. An auction may include
18 allowances from the annual allowance budget of the current year and
19 allowances from the annual allowance budgets from prior years that
20 remain to be distributed. The department must transmit to the
21 environmental justice council an auction notice at least 60 days
22 prior to each auction, as well as a summary results report and a
23 postauction public proceeds report within 60 days after each auction.
24 The department must communicate the results of the previous calendar
25 year's auctions to the environmental justice council on an annual
26 basis beginning in 2024.

27 (b) The department must make future vintage allowances available
28 through parallel auctions at least twice annually in addition to the
29 auctions through which current vintage allowances are exclusively
30 offered under (a) of this subsection.

31 (3) The department shall engage a qualified, independent
32 contractor to run the auctions. The department shall also engage a
33 qualified financial services administrator to hold the bid
34 guarantees, evaluate bid guarantees, and inform the department of the
35 value of bid guarantees once the bids are accepted.

36 (4) Auctions are open to covered entities, opt-in entities, and
37 general market participants that are registered entities in good
38 standing. The department shall adopt by rule the requirements for a
39 registered entity to register and participate in a given auction.

1 (a) Registered entities intending to participate in an auction
2 must submit an application to participate at least 30 days prior to
3 the auction. The application must include the documentation required
4 for review and approval by the department. A registered entity is
5 eligible to participate only after receiving a notice of approval by
6 the department.

7 (b) Each registered entity that elects to participate in the
8 auction must have a different representative. Only a representative
9 with an approved auction account is authorized to access the auction
10 platform to submit an application or confirm the intent to bid for
11 the registered entity, submit bids on behalf of the registered entity
12 during the bidding window, or to download reports specific to the
13 auction.

14 (5) The department may require a bid guarantee, payable to the
15 financial services administrator, in an amount greater than or equal
16 to the sum of the maximum value of the bids to be submitted by the
17 registered entity.

18 (6) To protect the integrity of the auctions, a registered entity
19 or group of registered entities with a direct corporate association
20 are subject to auction purchase and holding limits. The department
21 may impose additional limits if it deems necessary to protect the
22 integrity and functioning of the auctions:

23 (a) A covered entity or an opt-in entity may not buy more than 10
24 percent of the allowances offered during a single auction;

25 (b) A general market participant may not buy more than four
26 percent of the allowances offered during a single auction and may not
27 in aggregate own more than 10 percent of total allowances to be
28 issued in a calendar year;

29 (c) No registered entity may buy more than the entity's bid
30 guarantee; and

31 (d) No registered entity may buy allowances that would exceed the
32 entity's holding limit at the time of the auction.

33 (7)(a) For fiscal year 2023, upon completion and verification of
34 the auction results, the financial services administrator shall
35 notify winning bidders and transfer the auction proceeds to the state
36 treasurer for deposit as follows: (i) \$127,341,000 must first be
37 deposited into the carbon emissions reduction account created in RCW
38 70A.65.240; and (ii) the remaining auction proceeds to the climate
39 investment account created in RCW 70A.65.250 and the air quality and
40 health disparities improvement account created in RCW 70A.65.280.

1 (b) For fiscal year 2024, upon completion and verification of the
2 auction results, the financial services administrator shall notify
3 winning bidders and transfer the auction proceeds to the state
4 treasurer for deposit as follows: (i) \$356,697,000 must first be
5 deposited into the carbon emissions reduction account created in RCW
6 70A.65.240; and (ii) the remaining auction proceeds to the climate
7 investment account created in RCW 70A.65.250 and the air quality and
8 health disparities improvement account created in RCW 70A.65.280.

9 (c) For fiscal year 2025, upon completion and verification of the
10 auction results, the financial services administrator shall notify
11 winning bidders and transfer the auction proceeds to the state
12 treasurer for deposit as follows: (i) \$366,558,000 must first be
13 deposited into the carbon emissions reduction account created in RCW
14 70A.65.240; and (ii) the remaining auction proceeds to the climate
15 investment account created in RCW 70A.65.250 and the air quality and
16 health disparities improvement account created in RCW 70A.65.280.

17 (d) For fiscal years 2026 through 2037, upon completion and
18 verification of the auction results, the financial services
19 administrator shall notify winning bidders and transfer the auction
20 proceeds to the state treasurer for deposit as follows: (i)
21 \$359,117,000 per year must first be deposited into the carbon
22 emissions reduction account created in RCW 70A.65.240; and (ii) the
23 remaining auction proceeds to the climate investment account created
24 in RCW 70A.65.250 and the air quality and health disparities
25 improvement account created in RCW 70A.65.280.

26 (e) The deposits into the carbon emissions reduction account
27 pursuant to (a) through (d) of this subsection must not exceed
28 \$5,200,000,000 over the first 16 fiscal years and any remaining
29 auction proceeds must be deposited into the climate investment
30 account created in RCW 70A.65.250 and the air quality and health
31 disparities improvement account created in RCW 70A.65.280.

32 (f) For fiscal year 2038 and each year thereafter, upon
33 completion and verification of the auction results, the financial
34 services administrator shall notify winning bidders and transfer the
35 auction proceeds to the state treasurer for deposit as follows: (i)
36 50 percent of the auction proceeds to the carbon emissions reduction
37 account created in RCW 70A.65.240; and (ii) the remaining auction
38 proceeds to the climate investment account created in RCW 70A.65.250
39 and the air quality and health disparities improvement account
40 created in RCW 70A.65.280.

1 (8) The department shall adopt by rule provisions to guard
2 against bidder collusion and minimize the potential for market
3 manipulation. A registered entity may not release or disclose any
4 bidding information including: Intent to participate or refrain from
5 participation; auction approval status; intent to bid; bidding
6 strategy; bid price or bid quantity; or information on the bid
7 guarantee provided to the financial services administrator. The
8 department may cancel or restrict a previously approved auction
9 participation application or reject a new application if the
10 department determines that a registered entity has:

11 (a) Provided false or misleading facts;

12 (b) Withheld material information that could influence a decision
13 by the department;

14 (c) Violated any part of the auction rules;

15 (d) Violated registration requirements; or

16 (e) Violated any of the rules regarding the conduct of the
17 auction.

18 (9) (a) Records containing the following information are
19 confidential and are exempt from public disclosure in their entirety:

20 ~~((a))~~ (i) Bidding information as identified in subsection (8)
21 of this section;

22 ~~((b))~~ (ii) Information contained in the secure, online
23 electronic tracking system established by the department pursuant to
24 RCW 70A.65.090(6);

25 ~~((c))~~ (iii) Financial, proprietary, and other market sensitive
26 information as determined by the department that is submitted to the
27 department pursuant to this chapter;

28 ~~((d))~~ (iv) Financial, proprietary, and other market sensitive
29 information as determined by the department that is submitted to the
30 independent contractor or the financial services administrator
31 engaged by the department pursuant to subsection (3) of this section;
32 and

33 ~~((e))~~ (v) Financial, proprietary, and other market sensitive
34 information as determined by the department that is submitted to a
35 jurisdiction with which the department has entered into a linkage
36 agreement pursuant to RCW 70A.65.210, and which is shared with the
37 department, the independent contractor, or the financial services
38 administrator pursuant to a linkage agreement.

39 (b) The following records are not exempt from public disclosure
40 under (a) of this subsection:

1 (i) Records containing information pertaining to the contents of
2 holding accounts that is required to be displayed under RCW
3 70A.65.090(7)(b);

4 (ii) Records pertaining to bidding information as identified in
5 subsection (8) of this section that pertains only to concluded
6 allowance auctions. The records referenced in this subsection (9)(b)
7 include all records contained in the post auction public proceeds
8 report and communications to the environmental justice council
9 required under subsection (2)(a) of this section;

10 (iii) Records pertaining to the public roster made public on the
11 department's website under RCW 70A.65.090(10);

12 (iv) Other records containing information that is expressly
13 required to be made public under this chapter; and

14 (v) Records necessary for the joint legislative audit and review
15 committee to complete and publish the analysis required under RCW
16 70A.65.290(1)(e) or for the state auditor to complete and publish the
17 audit required by section 3 of this act.

18 (10) Any cancellation or restriction approved by the department
19 under subsection (8) of this section may be permanent or for a
20 specified number of auctions and the cancellation or restriction
21 imposed is not exclusive and is in addition to the remedies that may
22 be available pursuant to chapter 19.86 RCW or other state or federal
23 laws, if applicable.

24 (11) The department shall design allowance auctions so as to
25 allow, to the maximum extent practicable, linking with external
26 greenhouse gas emissions trading programs in other jurisdictions and
27 to facilitate the transfer of allowances when the state's program has
28 entered into a linkage agreement with other external greenhouse gas
29 emissions trading programs. The department may conduct auctions
30 jointly with linked jurisdictions.

31 (12) In setting the number of allowances offered at each auction,
32 the department shall consider the allowances in the marketplace due
33 to the marketing of allowances issued as required under RCW
34 70A.65.110, 70A.65.120, and 70A.65.130 in the department's
35 determination of the number of allowances to be offered at auction.
36 The department shall offer only such number of allowances at each
37 auction as will enhance the likelihood of achieving the goals of RCW
38 70A.45.020.

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