

July 24, 2009

**Steve Borg**  
**Project Manager**  
**Ministry of the Environment**  
**Integrated Environmental Policy Division**  
**Air Policy Instruments and Programs Design Branch**  
**135 St. Clair Avenue West, Floor 4**  
**Toronto, Ontario, M4V 1P5**

**Dear Mr. Borg:**

**RE: Feedback on the Discussion Paper, “Moving Forward: A Greenhouse Gas Cap-and-Trade System for Ontario”**

On behalf of Canada’s Industry-Provincial Offset Group (IPOG), please accept the following comments in response to the Government of Ontario’s release of the discussion paper “Moving Forward: A Greenhouse Gas Cap-and-Trade System for Ontario” (the “Discussion Paper”). IPOG is a multi-stakeholder group with a membership that includes four provincial governments, large industry and offset developers. IPOG members represent over 60% of industrial greenhouse gas (GHG) emissions in Canada. Our work on the development of offset protocols represents a broad range of industry participants, including non-governmental organizations (NGOs). IPOG focuses on issues and governance considerations in developing sound offsets markets.

We would like to express where we have concerns with the offset system contemplated in the Discussion Paper and where we are aligned. We will also respond to the questions provided in the Discussion Paper, with our thoughts on how a successful and robust offset system could be implemented. Due to the nature of our organization and its membership, the comments provided will be limited to those areas of the discussion paper that are relevant to offsets and are organized according to the headings provided in the discussion paper.

We have found it effective in the past to consider five principles when considering an offset system:

1. Maximize the volume of emission reductions while maintaining the environmental integrity of the system. To promote innovation and technology development, the system should not limit project types, nor restrict market sectors that can participate in the system. Rather, by prescribing clear rules around eligibility, the system should encourage the development of new, sound project types that are relevant to Ontario and our reduction opportunities.
2. Minimize the administrative burden where possible. One way in which this can be achieved is to adopt best practices, protocols and policies from other compatible jurisdictions.
3. To promote immediate investment, the system should provide clear guidance and long-term certainty to system participants, and reward early action efforts.
4. Align the system with other provincial systems and the proposed Federal program. This will increase the efficiency of project developers leading to faster GHG reductions.
5. The system needs to be cost effective. If it is overly burdensome on project developers it will not generate significant volumes and thus not contribute to the reduction of greenhouse gas emissions.

IPOG has found it helpful in the past to compare proposed policies with these principles when trying to determine the correct balance between technical perfection and achievable results.

### **Discussion Paper Feedback**

#### Program Authority

We agree with the comments cited by the offsets expert group with regards to both the need for government certification of offsets and the concerns expressed with a government managed program authority.

IPOG also encourages the Ontario government to allocate adequate resources to the system's design and implementation, in order to avoid potential backlogs and process delays. Investment will flow to jurisdictions with the best regulatory clarity and least regulatory friction. Proper resource allocation early on will ensure that Ontario's offset system is as efficient as possible.

#### Protocol Development

Successful protocols have been created in other jurisdictions, providing Ontario the opportunity to begin an offset system with a significant number of pre-approved protocols. Collaboration with existing systems will be very important to share best practices and reduce the resource requirements for the Ontario offset system. This has already been demonstrated with Ontario participating actively within the Western Climate Initiative (WCI). Tremendous work has been done in other systems within and outside of Canada and this should be leveraged to the extent possible, while ensuring that the protocols meet the requirements of the program authority. Regular meetings between program authorities in different jurisdictions are encouraged and the ability to use approved protocols from other systems as base protocols within the Ontario system would reduce the resource requirements in Ontario. By freeing up resources, Ontario could then focus more time and energy on the long term needs of the market, for example, providing criteria and guidance to the private sector to assist them in developing additional protocols.

#### Project Types

We believe that both a broad and deep market is required to reduce emissions to maximum extent possible while also providing an alternative compliance option to industry. The government of Ontario has expressed a desire to promote a broad innovation agenda, especially in the areas of clean and green technologies. To be consistent with this mandate, and to unleash creativity and innovation across the province, we see no need to create a definitive list of approved project types. Prescribing a limited list of eligible project types will have the opposite effect of what is desired, choking off a strong financing tool that could be leveraged by Ontario's clean technology entrepreneurs. Project developers should be able to provide offset protocols on any project that reduces GHG emissions and does not include capped emission sources, to avoid double counting.

#### Treatment of Renewable Energy and Energy Conservation Projects

We agree with the offset experts group that treatment of renewable energy and conservation projects under the cap and trade should coordinate with the Feed-In Tariff under the Green Energy Act, 2009, to reduce overlap between the two policies. We believe that the emission reductions created both directly and indirectly by renewable energy projects and energy

conservation projects should be recognized. The form of recognition will depend on the overall design of the two policies.

#### Offsets Outside of Ontario

To increase the liquidity of the market, we would suggest accepting approved emission reductions from compatible offset systems and which meet the criteria and principles set by the Ontario program authority. As the offset system develops and the program authorities from different jurisdictions collaborate, we anticipate a general aligning of principles and protocols. This will ease the resource requirements to approve credits from other offset systems. We would further suggest that there should be no arbitrary limit on the use of offsets generated in compatible offset systems. Limits inhibit the decrease of GHG emissions and create barriers to trade which increase the cost of the program and decrease the efficiency of government resources used to support it.

#### Additionality

As stated in the Discussion Paper, additionality is a difficult requirement for offset projects, but one we feel can be efficiently and effectively managed. We generally agree with the suggestions put forth by the experts group as detailed below.

Offset projects should surpass all regulatory requirements except in the case where an adjusted baseline approach is taken, which then implicitly accounts for actions taken prior to the system start date. In the case where an adjusted baseline approach is not used, any project which exceeds the regulatory requirement should be able to receive offset credits for the portion of the project which exceeds the requirements.

A project start date and a project crediting date should be established. Both dates should occur several years prior to the start of the program, to account for investments made in projects in good faith with the expectation of receiving offset credits, and to not unfairly punish groups that have taken a leadership role in reducing emissions across Ontario. The principles discussed in the Credit for Early Action section apply equally to offset projects, to recognize past investments in offset projects and incent further action prior to the start of the offset system. This measure will also ensure liquidity during the initial market start-up date.

IPOG opposes the use of financial additionality as a requirement for offset projects. Several years of experience has been gained by the international community in the development of offset projects under the Clean Development Mechanism. We believe this experience clearly shows that it is very difficult, if not impossible, to provide a fair, transparent, and consistent set of criteria whereby a developer or a verifier can determine if a project meets this type of criteria. We believe that this has not been a failing of the program authority, but an inherent problem with the concept of trying to show that a project is financially additional, and therefore we recommend that it not be included as one of the criteria in the Ontario offsets system.

We also believe that projects that receive some type of GHG government incentive should still qualify as an offset project. GHG government incentives should be defined as those government programs which clearly indicate that the government is providing funding to secure the GHG environmental attributes of the projects. In this case a pro-rata approach should be taken whereby the incentive is compared with the overall cost of the project, with the project receiving offset credits relative to the portion of the project that was self financed and the remaining

environmental benefits accruing to the government. Consistency with the proposed Federal program in terms of "qualifying reductions beyond other climate change incentives." would be beneficial.

#### Addressing Reversals and Permanence

IPOG supports a risk-based approach to managing reversals and permanence issues. A risk-based approach is commonly used in insuring other products and processes (e.g. automobiles, houses and health from fire, flood, hurricanes, etc.). Statistical estimates of risk, based on historical data or other means (reliable prediction tools), are used to devise actuarial tables and risk premiums. Similar techniques can and are already being applied to offset projects.

IPOG recommends the use of a government approved assurance factor embedded in the relevant protocol. Choosing a conservative factor, which guarantees more carbon reserves than the level of risk assessment, would serve to ensure that future reversals are reasonably accounted for. Regular monitoring and recalibration to adjust the assurance factor and the resulting size of the reserve based on actual loss experience would be desirable. The reserve would never be returned to the offset pool. This assurance mechanism will offer the credibility and environmental integrity of the sink offsets, as well as provide the incentive and management flexibility required for commercializing a new project by providing permanent offsets to the project developer.

#### Offset Limits

We currently see no need to limit the use of offsets. An offset credit, if created in a conservative and transparent manner, is exactly equivalent to the same reduction at a capped entity. Thus, if the environment is seeing the same benefit from both activities there should be no preference for either and no restrictions on the creation or use of either. We would propose that there be no limit.

In addition, we expect supply will be constrained as offset projects begin to be developed. From the time that a protocol is established, an average project still requires between one to two years to secure capital, finish construction, and become operational. These offsets must then be verified and certified before being sold to a compliance buyer. The process creates a multi-year delay between the approval of a protocol and when the first offsets are available for purchase. Further, it will take a significant amount of time for new protocols to be developed and then to develop projects based on the new protocols – therefore, the development time cycle insures a constrained project pipeline eliminating the need for limits. This approach is far superior to the concept of temporary credits that, in IPOG's opinion, is a flawed approach to reversal and permanence risk and should be avoided.

#### Banking

For the reasons stated in the Discussion Paper, IPOG fully supports 100% banking of offset credits with no discount applied to their use in future compliance periods.

#### Alignment with Other Programs

We believe that the Ontario offset system should be aligned with the currently proposed Federal offset system and other provincial systems. Having synchronized offset protocols and approval

processes will reduce offset developer costs, reduce the resource requirements for the government and increase the fungibility of Ontario-based offset credits.

### Looking Ahead

Thank-you for another opportunity to provide feedback. We have appreciated the Government of Ontario's participation within IPOG and we hope that you will be able to incorporate our suggestions into the Ontario offset framework. As a further contribution, IPOG has developed several papers on many of the topics discussed in this paper and would be pleased to share them with the Government of Ontario.

IPOG and its members offer our expertise, experience and knowledge to the Government of Ontario. Should you have any questions or would like to discuss further steps associated with IPOG's engagement in this policy process, please feel free to contact the undersigned at your earliest convenience.

We appreciate your time and consideration and look forward to hearing from you.

Sincerely,



Skip Willis  
IPOG Co-Chair



Nathan Maycher  
IPOG Co-Chair