



To: Surabhi Subedi
Environmental Planner

From: Kevin Tempest
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RE: Comments on Cap-and-Invest Program Updates - House Bill 1975 Public
Workshop Questions for Feedback

General Comments

Clean & Prosperous (C&P) appreciates Ecology's continued work to clarify and streamline the rule, smoothing the path to an eventual linkage agreement with the California-Québec carbon market. Linking these markets will provide substantial near-and long-term benefits aligned with the Climate Commitment Act (CCA) goals, as we have mentioned in previous comments.

As we move closer to the end of the first compliance period, looking ahead, C&P encourages Ecology to move expeditiously to update the allowance budget and the Allowance Price Containment Reserve (APCR) rules, as required by HB 1975. Providing clarity on these elements is essential for covered entities to plan effectively, manage compliance obligations, and maintain confidence in the program's long-term integrity.

Importance of Implementing HB 1975

Emissions limits (December 31 limits)

The annual allowance budget and stringency of the cap remain ambitious even as they are amended to align with original legislative intent as informed by statutory emissions limits. **Our recommendation is to true up the full allocation consistent with Emissions Limits as soon as possible, and certainly in time to reflect the completion of the First Compliance Period (2023-2026, with full compliance required by November 2027).** This enhances the long-term durability, more closely couples the budgets of the Climate Commitment Act with the proportional share of statutory emissions limits, and serves as

the key price stabilization approach before Washington potentially links with the California-Québec carbon market.

Since the original CCA rulemaking and Regulatory Analysis, C&P has consistently emphasized that adjusting the alignment of the cap with statutory targets is critical for the integrity and price stabilization of the program.¹ HB 1975 clarifies that the allowance budget must reflect the state limit of halving emissions over eight years (annual emissions through 2030) to meet the proportion of statutory target emissions reduction as covered under the cap. This adjustment in volume of allowances preserves the original legislative intent and integrity of state limits. By our calculations, nearly 4 million additional allowances would be backfilled from 2023-25 allowance budgets alone, growing to over 6 million through 2026 and 22 million through 2030. A portion of these will enter through the APCR that Ecology is obligated to expand under HB 1975.

This volume is particularly relevant to covered parties who must purchase allowances for compliance, as reflected primarily in the price at auction. This is because much of the freely distributed allowance volume is fixed irrespective of the total allowance budget relative to 2015-19 emissions baselines (in the case of EITEs) or Clean Energy Transformation Act requirements (in the case of the power sector). Therefore, additional allowances primarily enter through the auctions.

Number of future vintage allowances placed in APCR and when APCR allowances introduced

The recommendation from C&P is to maintain the 5% APCR set aside for 2023-2030 (including increased volumes due to the Emissions Limit adjustment to annual allowance budgets) and start the lower bound (2%) from 2031-2040 allowance budgets. At minimum, the additional 2023-2030 APCR should be released before the first compliance period compliance event, depending on price triggers, while additional volumes can be released based on certain predefined price triggers, as they have previously, and market price evolution in California-Québec ahead of any linkage agreement. This gives Ecology most, if not all of 2026, to define those volumes and price triggers for APCR volume release as needed to contain prices through the first quadrennial compliance event.

Ecology recognized price stability as a primary design consideration in its initial rulemaking by making a substantial allocation to the APCR. To date, allowance prices

¹ As noted in Clean & Prosperous Institute comments during draft rulemaking: The cap decline rate is influential on program costs and compliance obligations. C&P's review indicates that a 7% rate of decline, as set in the proposed rule, exceeds the amount necessary for consistency with statutory targets based on a proportional reduction from baseline emissions levels.

have remained below projected ranges that forecast a greater reliance on the APCR, demonstrating that the market is working efficiently and effectively to beat the most rigorous cost estimates.² Given this track record, and especially in light of the continued steps towards linkage that offer a likely path to price moderation and stability, C&P continues to caution against overreliance on the APCR.³

The APCR borrows allowances from future allowance budget years. When more APCR allowances are leveraged early, this decreases volumes available for auction in future years. This requires balance, because unlike adjusting Emission Limits timing, this does not increase the overall pool of allowances.

The current APCR sets aside nearly 19 million allowances, of which over 14 million will have been available for purchase by the end of 2025. Some additional APCR may be demanded in 2026, the last year of the first compliance period (2023-26), but the extent of that demand remains to be seen and remains dependent on other price stabilizing efforts built into the original law: The impact of additional allowances through Emissions Limit adjustments and the details of potential linkage.

Adjusting the emissions limits through 2030 alone – with 5% set-aside for the APCR through 2030 – brings forward another 1.1 million allowances to earlier auctions. Adding just 2% of 2031-2040 is another 5.7 million allowances into APCR whereas 5% brings another 14.2 million forward in time. Given these additional volumes, a cautious approach should be applied to borrowing even more from future allowance budgets. This approach can include careful evaluation of the impact of linkage by monitoring market prices and price forecasts for California-Québec. It is likely easier to decide to increase the APCR allocation in the future than it is to reduce it. Therefore, we suggest maintaining the 5% set-aside in the APCR through 2030 and initially setting aside 2% of the 2031-2040 budget.

² Prices forecast at \$58.31 in 2023, \$61.21 in 2024, \$64.76 in 2025 including nearly 19M APCR allowances through 2025. Actual prices have been lower in each year to date (average of all allowances sold is \$46.35) while APCR volumes have also been lower (14.4M will be offered through end of 2025).

³ C&P review of the preliminary regulatory analysis (PRA) indicates that the case for additional price containment mechanisms is less pressing than the scenarios presented by Vivid Economics may suggest. C&P finds that a more realistic set of assumptions significantly lowers the anticipated range of allowance prices,” (Regulatory Analysis comments, 2022)

Tier 2 price revision

To the extent that a Tier 2 price may be utilized (all APCR allowances are to be sold at Tier 1 prices currently), a clear consideration of Tier 2 prices may be necessary. In the view of C&P, we do not see Tier 2 prices are currently relevant, but believe a price step between Tier 1 and the Price Ceiling is a reasonable starting point. This assumes that the Tier 1 price does not see any downward adjustment, but is maintained at its current level and set rate of increase. C&P believes that the Tier 1 price is working as intended and should not be adjusted when considering where to set the Tier 2 price.

Additional feedback

With the anticipated increase in allowance volumes, emphasizing the availability of a significant share of these well in advance to the first quadrennial compliance event, there is an anticipated increase in revenue. This will be somewhat balanced out by lower allowance prices. Ecology should provide the Legislature a clear picture of the anticipated revenue reflecting the implementation of HB 1975 requirements. In turn, the Legislature will have the ability to more effectively appropriate and allocate Climate Commitment Act revenue to better deliver on the intent of the program.

Conclusion

The recommendation from C&P is to true up the full allocation consistent with Emissions Limits as soon as possible, and certainly in time to reflect the completion of Compliance Period 1 (end of 2026, with full compliance required by November 2027).

The recommendation from C&P is to maintain the 5% APCR set aside for 2023-2030 (including increased volumes due to the Emissions Limit adjustment to annual allowance budgets) and start with the lower bound (2%) set-aside from 2031-2040 allowance budgets. At least the additional 2023-2030 APCRs should be made available, depending on price triggers, before the first compliance period compliance event, while additional volumes can be released based on certain predefined price triggers, as they have previously, and market price evolution in California-Québec ahead of any linkage agreement.

To the extent that greater allowance volumes, primarily under the change to Emissions Limits but also due to greater APCR availability in the upcoming one to two years, Ecology should account for this early in the budgeting process so that any changes in revenues can be planned for appropriately.