

Insights and Commentary from Dentons

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This document was authored by representatives of McKenna Long & Aldridge prior to our combination's launch and continues to be offered to provide our clients with the information they need to do business in an increasingly complex, interconnected and competitive marketplace.

Carbon Developments in the United States

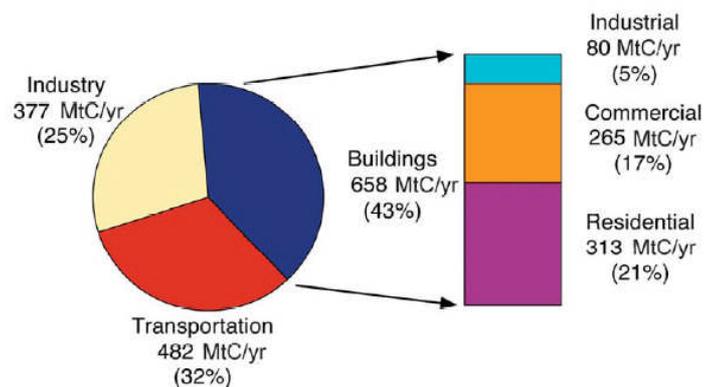
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USGBC Capital Chapter Carbon Workshop
June 25, 2008 – Washington, DC

McKenna Long
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Attorneys at Law

CO2 Emissions from Fossil Fuel Combustion By End-Use Sector



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Topics to be Covered

1. Capitol Hill: Update on Climate Change
2. Developments in the Voluntary Carbon Market
3. Verified Emissions Reduction Purchase & Sale Agreement and Other ACORE-ABA Projects

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Capital Hill Update

Senate Side

- Lieberman-Warner "Climate Security Act of 2008" (S.3036) is dead (but not buried)
 - Would have established cap-and-trade regime
 - Title VIII ("Efficiency and Renewable Energy") created green building incentives: \$51 million in emission allowances allocated to fund an "efficient buildings program"
 - Those allowances would be distributed to projects resulting in "verifiable, additional and enforceable" improvements, specifically -
 - **New or renovated buildings** that achieve Energy Star score of 75 or equivalent score under another benchmarking tool
 - **Retrofitted existing bldg** that improve by at least 30 points
 - Lieberman-Warner died when it became clear that the sponsors could not get 60 votes needed to close debate on the bill

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Capital Hill Update *(cont'd)*

House Side

- Multiple cap-and-trade bills to be considered in Energy & Commerce Committee hearings this Fall:
 - The Investing in Climate Action and Protection Act" (H.R. 6186) (authored by Re. Markey)
 - Lieberman-Warner Security Act of 2008 (S.3036)
 - The Safe Climate Act of 2007 (H.R. 1590) (authored by Rep. Waxman)
- All three bills have some incentives for green building projects but this is largely a symbolic exercise as the Senate will not be taking up climate change again this year

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Capital Hill Update *(cont'd)*

Predictions

- Conventional wisdom was always that there was no chance of passing cap-and-trade leg. in 2008
- Cap-and-trade in 2009? Much improved given likelihood of larger Dem. majority in Senate and a president who supports climate change. Nevertheless, 50-50 is my prediction.
- By 2010? Perhaps 70%.
- Carbon tax? No chance.
- "Sectoral approach" is possible for regulating CO₂ emissions from regulated industries that compete overseas, e.g., steel, cement, etc.

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Voluntary Carbon Market Developments: RGGI

New Opportunities for Green Building Owners to Profit From by Reducing CO₂ Emissions:

1. Regional Greenhouse Gas Initiative

- Goes into effect Jan. 1, 2009
- Establishes cap-and-trade for CO₂ emissions for 10 northeastern and mid-Atlantic states, including Maryland
- Applies only to fossil fuel burning utilities which must hold CO₂ emissions steady through 2014, and then reduce emissions 2.5% annually through 2018 (10% total)
- **Green Building angle?** Utility can offset 3.3% of its emissions using five project types, including “reduction or avoidance of CO₂ emissions from natural gas, oil or propane end-use combustion **due to energy efficiency**”

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Voluntary Carbon Market Developments: CCX

2. Chicago Climate Exchange (“CCX”)

- Background:
 - Phase I: Members committed to reduce GHG emissions 1% annually 2003-2006 (total of 4% below baseline).
 - Phase II: members commit to additional 2% of reductions below baseline by 2010 (total of 6% from 2003-2010).
 - If unable to reduce operational emissions, member can
 - purchase emission reduction credits to meet obligation
 - purchase offsets
- CCX offsets include green building CO₂ reductions:
 - New or retrofitted bldg. can earn tradable CCX emission offsets **only if** it surpasses Energy Star efficiency minimum std.
 - Offset issued annually on the basis of the following: modeled emissions for minimum Energy Star bldg. minus actual emissions

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Voluntary Carbon Market Developments: CCX (cont'd)

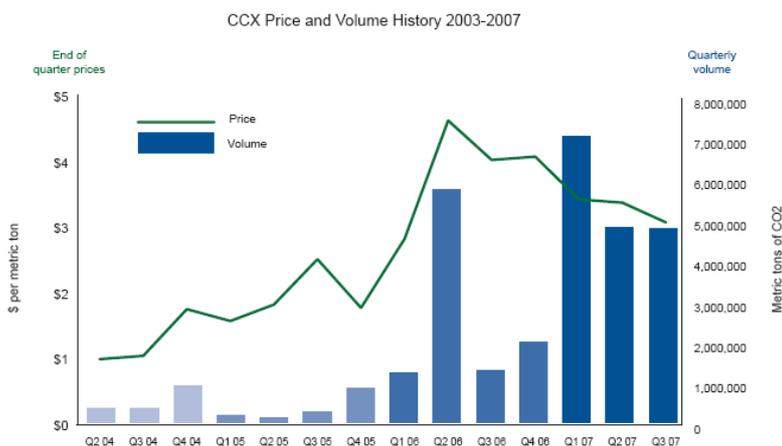
- **Problem:** Emission reductions achieved by individual green building projects may not warrant the cost of joining CCX and meeting requirements for listing offset credits for sale
- **Potential solution:** “Aggregation.” Emission reductions from multiple green building projects could be bundled and for sale on CCX by “aggregator”
- North Dakota Farmer’s Union model: farmers aggregated CO₂ emission reductions achieved through no-till farming, and collected over \$1 million from CCX sales of the aggregated offsets
- Green building owners could pursue similar strategy
- **Other market opportunities:**
 - Oregon Climate Trust (RFP structure)
 - NYMEX Green Exchange

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Voluntary Carbon Market Developments: CCX



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Verified Emissions Reduction Purchase & Sale Agreement

- Developed jointly by ABA and ACORE
- Intended to facilitate carbon transactions in the voluntary market
- Why should USGBC members care about this Agreement?
 - No need to wait for cap-and-trade legislation to cash in on green buildings
 - Voluntary GHG emission reductions achieved by making buildings energy-efficient can generate GHG emission reduction credits that can be bought and sold in established markets like CCX or "over the counter"

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Verified Emissions Reduction Purchase & Sale Agreement (cont'd)

- Buying and selling GHG emission reductions has been characterized as the "Wild West" because of the lack of standards, regs, federal oversight, etc.
- In the absence of such standards, the contract takes on immense significance
 - defines the right being sold,
 - who bears the risk in the event the project does not perform as expected
 - point at which CER is transferred, etc.
- ABA/ACORE attempt to standardize the contract is an attempt to reduce uncertainty which in turn increases value

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Verified Emissions Reduction Purchase & Sale Agreement (cont'd)

- Basic elements for enhancing chances that an emission reduction credit has market value: reduced emissions must be (1) "additional" and (2) verified in order to generate a VER
 - "Additional" - means that activity is not required by law, voluntary, differs from "business as usual"
 - "Verified" means quantified using accepted methodology by an independent auditor
- Note: requirement under Kyoto Protocol for carbon reduction transactions are much more demanding:
 - Must satisfy numerous requirements under either "Clean Development Mechanism" or "Joint Implementation" schemes
 - ***But even a Kyoto offset project will need a Verified Emission Reduction Purchase and Sale Agreement***

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Verified Emissions Reduction Purchase & Sale Agreement (cont'd)

- Other Joint ABA/ACORE Activities of interest: series of educational seminars and teleconferences on renewable energy and climate change, e.g.:
 - *Green Buildings and Community Development-Getting the Rules, Incentives and Financing Right (TODAY !!)*
 - *Risk Management, Mitigation, and Technologies: From Insurance, Contracting to Sophisticated Finance (5/21/08)*
 - *Carbon: Policy Options for the US in A Global Market (4/16/08)*
 - *Honing the Cutting Edge: Strategies and Challenges in Scaling Up Cleantech and Renewables (3/19/08)*
 - *Carbon Trading Markets and the Verified Emissions Reduction Purchase and Sale Agreement (2/20/08)*
 - *Emerging Capital Sources for Renewables (1/16/08)*

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