

Comments To The FTC On Marketing Claims Regarding Carbon Offsets

January 25, 2008

Prepared On Behalf Of Hydrodec North America LLC

Re: Federal Trade Commission's request for public comment published at 72 Fed. Reg. 66094 (Nov. 27, 2007), entitled "Carbon Offset Workshop - Comment, Project No. P074207."

This comment is in response to the FTC's question: "What is the relationship between the concept of 'additionality' in carbon offset markets and the FTC's standard for deception under the FTC Act?" 72 Fed. Reg. 66094, 66097 (Nov. 27, 2007) and is based in part on statements made at the public workshop hosted by the FTC on January 8, 2008.

To the extent that the FTC concludes that guidance on the question of additionality is warranted, the FTC should not prescribe a policy straight-jacket for additionality. Instead, the FTC should require claimants to (1) be clear with consumers about what type of additionality, if any, their "carbon offsets" actually provide, and (2) to maintain substantiation for any additionality claims. This approach would be consistent with the FTC's basic principles for addressing deceptive and unfair practices and it would ensure that consumers have truthful information on which to base their decisions. At the same time, this approach would maintain the incentives for new technology and other innovations that offsets can provide. Consumers could therefore have more choices than they might otherwise have if a particular test for additionality were required, and the environment would be helped through the development and use of technologies and other measures that reduce harmful emissions.

I. We Support The FTC's Effort To Protect Consumers

We commend the FTC for taking steps to incorporate the issue of carbon offsets into its Guides for the Use of Environmental Marketing Claims ("Green Guides"), and recognize that the concept of additionality is important to individual consumers who purchase offsets voluntarily in hopes of making a difference to the environment. We also recognize the FTC's role in this matter and we commend the FTC's efforts to ensure that consumers are not misled when purchasing offsets. For the same reasons that the FTC has said that unspecific claims such as "environmentally friendly" are inherently misleading, "carbon offsets" that do not specify in what particular sense they represent reductions of carbon emissions are also inherently misleading. The avoidance of consumer confusion in the carbon offset market is of particular importance because, in addition to the risk to consumers due to misinformation, there is also the potential to incorrectly quantify national and global progress towards stabilizing climate change.

We would urge the FTC, however, to remain firm in its plan not to develop environmental performance standards for carbon offsets and to use care not to do so directly or indirectly on the issue of additionality through the issuance of guidance on the subject. Carbon markets are just beginning to operate and the issue of how these markets will treat "additionality" is controversial. Moreover, U.S. policy on how to best respond to the realities of climate change is still developing. As such, the FTC should not exceed its mandate.

II. Hydrodec North America LLC Is A Start-up Business In The Oil Re-Refining Industry

Hydrodec North America LLC ("Hydrodec") is a start-up company that is currently entering the oil re-refining business in the United States, after piloting its technologies in Australia. It has already broken ground on a facility in Canton, Ohio and hopes to begin construction on another in Laurel, Mississippi shortly. Hydrodec's current focus is on

transformer oil, of which up to 150 million gallons is consumed each year. This oil is refined from naphthenic crude oil, a limited resource often imported from politically unstable countries. Hydrodec intends to buy used transformer oil, which is often contaminated with PCBs, and re-refine it to specifications equaling or exceeding ASTM new oil standards, while also meeting standards promulgated by the U.S. Environmental Protection Agency ("EPA") for PCB destruction. Hydrodec believes that within several years, it could potentially supply up to half of the nation's transformer oil requirements, all from the re-refining of used oil that would otherwise be burned as waste oil. In the process, it will allow for a significant reduction in indirect greenhouse gas emissions, both from the reduction in new oil refining, which produces large quantities of greenhouse gases, and to a lesser extent, reduced emissions from incineration. Hydrodec's process is unique and exhibits far greater environmental benefits than older re-refining technologies, which have relied on dangerous chemical re-agents while often producing sub-par oils along with significant hazardous emissions. Hydrodec's process is better for industry, local communities, and the environment.

III. In Adopting A Particular Viewpoint On Additionality, The FTC Would Create Disincentives For Innovators While Increasing Oversight Burdens For Itself

Hydrodec is concerned about the issue of additionality as it relates to carbon offsets because as a start-up company that is pioneering environmental technologies, it faces major hurdles to achieving success. The final determination of what constitutes additionality for purposes of generation of carbon offsets could have a significant impact on Hydrodec's bottom line. At the same time, the FTC would face great hurdles in regulating claims regarding carbon offsets if it were to adopt a view of additionality before a national standard is set.

While the question of additionality -- essentially, would the project or emissions reduction have happened anyway -- appears simple, the question is really rather complicated. As

indicated in the literature and in the FTC's January 8, 2008 workshop, there are numerous ways to determine additionality, and the various methods each have their benefits and drawbacks. One type, mentioned by various presenters at the FTC's workshop, is whether a project would have occurred in a hypothetical "business as usual" scenario. As explained by commenter Ed Holt, President of Ed Holt & Associates, one test for additionality would be whether without offsets, a project would offer insufficient financial returns or face insurmountable structural barriers - hence, these types of additionality are often referred to as "**financial**" or "**barriers**" tests. As commenter Matthew Clouse, Director of EPA's Green Power Partnership, noted, however, the problem with this test is that it is impossible to determine which source of funding made a difference, or put another way, put the project over the top. An alternative type is the "**performance**" additionality mentioned by commenter Maurice LeFranc, Senior Policy Analyst in EPA's Climate Change Division, who explained that this methodology examines whether a technology represents a level of performance that allows for emissions reductions that are better than the average of recently undertaken practices in a relevant geographic area, which Mr. LeFranc mentioned has been adopted by EPA's Climate Leaders program. A variation on this is the "**common practice**" test, which simply examines whether a technology or practice is in common use within an area.

Commenter Anja Kollmus of the Stockholm Environment Institute noted that while some critics might want to move beyond a discussion of additionality, it is a "very complex issue and . . . needs to be discussed." Even the "**regulatory**" additionality test, which would disallow offsets if a project is required by government regulation, is not as simple as it might first appear. As commenter Wiley Barbour, Director of Environmental Resource Trust, noted, projects can be governed by multiple regulations, and the issue of whether a particular technology investment

was required by regulation can be difficult to answer in such scenarios. As Ms. Kollmus noted, regulatory additionality also discourages regulation at the state and local level in order to afford local businesses the opportunity to generate offsets. A final variation on additionality is the “**timing**” test, in which only those projects started after a given date will be considered for offsets. An unfortunate result of this test would be that much-needed investments might be delayed until an offset system is put in place. A complete review of various forms of additionality is Michael Gillenwater, “Redefining RECs (Part 1): Untangling attributes and offsets,” at 8, Aug. 2007, available at: http://www.princeton.edu/~mgillenw/REC-OffsetPaper-PartI_v2.pdf.

While many examples could be provided, even just the two below illustrate plainly the pitfalls that innovators would face if specific types of additionality were required in marketing claims:

(1) Under a “financial” additionality test, an innovator who has developed a more advanced process that is both more efficient and exhibits fewer environmental impacts may instead decide to implement a less efficient method, because the promise of carbon offsets for the less efficient method could give a business better overall financial returns on the margin than the more advanced alternative would without offsets.

(2) Under the “common practice” test, an innovator who is particularly successful at bringing a superior environmental technology to market will be stripped of the incentive to expand that offsets provide simply because the technology has become common in a particular geographic area.

IV. **It Would Be Premature For The FTC To Determine Whether Marketing Claims Must Take Account Of Additionality, Given EPA’s Pending Jurisdiction In The Matter**

While there is currently no federal law determining whether additionality will apply in carbon offset markets in the U.S., EPA is specifically tasked in the draft language of pending climate bills to address additionality and it is therefore premature for the FTC to determine whether marketing claims must take account of additionality. For instance, in the Lieberman-Warner bill (s. 2191) currently being considered by the United States Senate, Sections 2401-2411 specify that the EPA Administrator will develop standardized methods for addressing additionality and uncertainty. Given that the Congress intends to delegate rule-making authority on the issue of additionality to EPA, it would neither be appropriate nor productive for the FTC to take a stance on the issue before a national regulatory system is put in place by the United States Congress and the EPA.

V. **If The FTC Needs To Address Additionality At This Time, It Could Simply Require Marketers To Make Clear Whether Their Carbon Savings Would Be Considered “Additional”**

While we understand the FTC’s need, even in the absence of a national system for regulating emissions and offsets, to explore the marketing of carbon offsets and potentially to provide guidance on the matter, it is our belief that the FTC could simply require that marketers explain their claims as to carbon offsets in their marketing material in light of the various definitions of additionality. The potential for deception of the consumer would be greatly minimized, while maintaining incentives for innovators to accelerate their development of technological solutions to global climate change.

In the event the FTC were to determine that guidance on additionality is needed, we would recommend that the FTC amend the Green Guides, at § 260.7 - “Environmental Marketing Claims,” to add guidance on carbon offsets, incorporating the following language:

In the absence of a national system of greenhouse gas regulation and an accepted standard for determining when carbon offsets are “additional” or beyond “business-as-usual,” in order to prevent the marketing of offsets

from being deceptive, the marketer should disclose clearly to consumers the standard by which additionality was determined. Marketers should identify at least one test by which their technology represents additional carbon savings beyond business-as-usual from among the following tests: (1) the Regulatory Test - the offsets were not generated by emissions reductions required by regulation; (2) the Financial Test - the savings would not have come about without the sale of offsets due to insufficient financial returns; (3) the Barriers Test - the savings would not have occurred without the sale of offsets due to a lack of infrastructure; (4) the Common Practice test - the savings would not have been generated without the incentive provided by offsets because the technology involved was a new and unique practice that had not yet been accepted in the market; (5) the Initiation Date test - the savings were generated after a particular date, indicating that the offsets therefore acted as an incentive; or (6) the Performance Benchmark test - the project produces exceptional savings not common among its competitors.

Adapted from: Michael Gillenwater, "Redefining RECs (Part 1): Untangling attributes and offsets," at 8, Aug. 2007, available at: http://www.princeton.edu/~mgillenw/REC-OffsetPaper-PartI_v2.pdf.

VI. The Concept Of Credits For Indirect Emissions Reductions Generated By Recyclers Also Requires Careful Consideration

Another area of concern for Hydrodec is the issue of "indirect" emissions reductions. Hydrodec is building its plants from the ground up, and therefore has no initial carbon footprint in the United States on which to be benchmarked. It therefore cannot reduce its direct emissions, as is the case with most companies engaged in recycling. In re-refining transformer oil, Hydrodec will displace millions of gallons of oil refined from virgin crude oil, a highly-intensive industrial process that emits large quantities of greenhouse gases. Hydrodec would urge that the FTC not take any action that would prohibit Hydrodec and others from claiming they reduce carbon emissions where the reductions occur through displacement of more carbon intensive activities by third parties. It is Hydrodec's opinion that it should be able to make marketing claims about the environmental attributes of its process and the concomitant emissions

reductions at oil refineries or waste disposal facilities, and we would anticipate that recyclers will certainly wish to make similar claims about their processes.

We understand that a concern to the FTC is that it is not always clear to consumers where offsets come from. To address this concern, we would urge that the FTC require claimants to be clear about what species or type of carbon offsets is involved. For example, the FTC could provide in its guidance that: **“claims should identify how the carbon emissions reductions are derived, such as ‘carbon offsets derived from recycling’, ‘carbon offsets derived from low intensity manufacturing’ or ‘carbon offsets derived from energy efficiency’.”**

Respectfully submitted,

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