

DRAFT CLEAN HEAT STANDARD RULE COMPANION STATUS REPORT

by the Vermont Public Utility Commission

October 1, 2024

I. Introduction and Summary of the Clean Heat Standard

In 2023, the Vermont General Assembly passed Act 18 of 2023,¹ which details a Clean Heat Standard program and requires the Vermont Public Utility Commission (“Commission”) to provide a Clean Heat Standard rule to the Legislature by January 15, 2025. The Act states that “it is the intent of the General Assembly that the Clean Heat Standard be designed and implemented in a manner that achieves Vermont’s thermal sector greenhouse gas emissions reductions necessary to meet the requirements of [the Global Warming Solutions Act of 2020], minimizes costs to customers, protects public health, and recognizes that affordable heating is essential for Vermonters.”

The purpose of the Clean Heat Standard (“CHS”) is to reduce greenhouse gas emissions from the thermal sector through the implementation of clean heat measures. The CHS does this by requiring any company that imports heating fuels for ultimate consumption in Vermont to retire a certain amount of clean heat credits each year. The CHS calls these companies “obligated parties.”² An obligated party must obtain and then retire (*i.e.*, not sell or save) a certain number of clean heat credits every year based on its share of fossil-based heating fuels delivered into Vermont.³ These businesses can pay a default delivery agent (“DDA”) appointed by the Commission to procure the credits they are obligated to retire in any given year, deliver clean heat measures themselves, or purchase credits from other entities doing that work. Credits are created by delivering clean heat measures such as weatherization, heat pumps, advanced wood heat systems, and biofuels. A clean heat credit is a tradeable, nontangible commodity representing the amount of greenhouse gas reduction attributable to a clean heat measure. The DDA(s) will work on behalf of obligated parties to help meet the annual clean heat credit requirements.

More information on the Commission’s work on the potential Clean Heat Standard, as well as updates on the Commission’s processes and procedures, can be found on our Clean Heat Standard website at <https://puc.vermont.gov/clean-heat-standard>. The Commission’s work is in ePUC; our work relating to the development of the rule and other policy decisions is in Case No. 23-2220-RULE; our work relating to DDA(s) is in Case No. 23-2221-INV.

¹ The bill as enacted is available at <https://legislature.vermont.gov/Documents/2024/Docs/ACTS/ACT018/ACT018%20As%20Enacted.pdf>. The relevant sections of the law can also be found at <https://legislature.vermont.gov/statutes/fullchapter/30/094>.

² 30 V.S.A. § 8123(12). This also includes any entity that produces, refines, manufactures, or compounds heating fuel within Vermont for ultimate consumption within the state.

³ 30 V.S.A. § 8124(a)(2).

At the highest level, Chapter 94 of Title 30 of the Vermont Statutes Annotated requires the Commission to “adopt rules and [] issue orders to implement and enforce the Clean Heat Standard program.”⁴ The Legislature specifically directed the Commission to draft a rule and a checkback report to submit to the General Assembly no later than January 15, 2025. After the rule is submitted, the Legislature determines whether, and in what form, the rule will be adopted. Put differently, the Legislature must still decide whether and how to implement the Clean Heat Standard.

Additionally, the Commission is charged with the following tasks to set up the Clean Heat Standard:⁵

- Devise a registration system and facilitate the registration of Vermont fuel dealers, beginning in January 2024.
- From the 2024 registrants, determine which entities are obligated parties and set each obligated party’s annual clean heat credit requirement for the first compliance year and projected requirement for the next 10 years.
- Establish a system of tradeable clean heat credits earned from the delivery of clean heat measures that allows for the registration, verification, trading, banking, and retirement of those credits.
- Provide for the development and implementation of statewide clean heat programs and measures by one or more default delivery agents appointed by the Commission.

This status report serves as a companion document to the Commission’s draft rule to provide context for how the draft rule fits into the work that the Commission has engaged in since Act 18 was passed by the Legislature in 2023. Over the last year and a half, the Commission has hired full-time staff to work on the design of the CHS and appointed the members of both statutorily required advisory groups: the Technical Advisory Group and the Equity Advisory Group. These advisory groups have met regularly since December 2023. The Commission has also issued orders and straw proposals for comment, hired a consultant to facilitate public engagement, hired an emissions analyst consultant, adopted and implemented a registration platform for Vermont fuel dealers and collected year one registration and reporting data, and engaged with other State agencies to carry out the work the Commission was tasked with by Act 18.

This status report is organized into sections.

- Section I provides an introduction and a summary of the Clean Heat Standard.
- Section II gives an overview of the Commission’s draft rule.

⁴ 30 V.S.A. §§ 8122(d), 8126(a), 8126(b) (“The requirements to adopt rules and any requirements regarding the need for legislative approval before any part of the Clean Heat Standard goes into effect do not in any way impair the Commission’s authority to issue orders or take any other actions, both before and after final rules take effect, to implement and enforce the Clean Heat Standard.”).

⁵ There are numerous tasks the Commission is charged with if the Clean Heat Standard program is implemented after the 2025 legislative session. Some of those tasks include managing the annual reporting of Vermont fuel dealers, determining annual obligated parties, and adjusting annual clean heat credit requirements.

- Section III outlines the other components of the Clean Heat Standard.
- Section IV describes when the Commission intends to provide information on the estimated costs of the Clean Heat Standard.
- Section V briefly describes an alternative to the Clean Heat Standard.
- Section VI identifies the process for public input on the Commission’s draft rule.
- Section VII concludes the status report.
- Appendix A summarizes each section of the draft rule.

II. Overview of the Draft Rule

As highlighted above, Act 18 contemplates that the Commission will develop and implement the Clean Heat Standard via multiple tools, including rules and orders. Throughout the first year, the Commission has reviewed the various tasks required by Act 18 to determine what aspects of the potential program fit into rulemaking, Commission proceedings that culminate in orders, internal procedures or informal processes, and other forms of Commission work. The rule that is due to the Legislature on January 15, 2025, will not include every aspect of the Clean Heat Standard because not all components of the potential Clean Heat Standard program fit into a rulemaking.

The Vermont Administrative Procedure Act defines a “rule” as “each agency statement of general applicability that implements, interprets, or prescribes law or policy.”⁶ In the context of the Clean Heat Standard, the focus of the Commission’s draft rule is on the responsibilities of the obligated parties that the Commission would be charged with regulating under the potential CHS program. Fuel dealers — many of which are small businesses — have never before been regulated by the Commission, so there is a need to prescribe the process for when and how the obligated parties would engage with the Vermont Department of Public Service (“Department”) and the Commission if this program is adopted by the Legislature.

As an appendix to this status report, we provide a guide to the draft rule to facilitate greater understanding of what each section of the draft rule does. This guide can be read in conjunction with the draft rule for context.

III. Other Components of the Clean Heat Standard

The purpose of this section of the status report is to provide an overview of the other elements of the Commission’s Clean Heat Standard work. Because our draft rule is aimed at the newly regulated entities and because a rule is inflexible once it is adopted, the Commission has determined that these tasks are better accomplished using other tools, such as orders, contracting processes, reports, or consultation with State agencies and experts.

⁶ 3 V.S.A. § 801(b)(9).

A. The Default Delivery Agent

The Commission is required to appoint at least one default delivery agent (“DDA”).⁷ The DDA will be responsible for obtaining credits that the DDA will retire on behalf of obligated parties who have contracted with the DDA to satisfy their credit requirements, in whole or in part.⁸ The Commission has determined that the DDA will primarily perform a program-administrative role under a performance-based regulatory structure.⁹ The DDA will serve a crucial role in the Clean Heat Standard program, if adopted by the Legislature in a form that requires one or more DDAs, by coordinating the flows of available funds, work, and credit creation and distribution.

On September 6, 2024, the Commission issued a request for information (“RFI”) to further refine the scope of work for the DDA and gather information concerning the appointment of a DDA.¹⁰ Responses to the RFI are due by December 6, 2024. If the General Assembly approves the Clean Heat Standard with a provision for appointing one or more DDAs, the Commission will appoint one or more DDAs according to the requirements of the enacted legislation. Currently, statute requires the Commission to approve the first DDA three-year plan and budget by September 1, 2025; the DDA(s) must be appointed or contracted before that date. The Commission intends to proceed with a request for proposals (“RFP”) and eventually to issue an Order of Appointment to one or more organizations to serve as DDA(s) if the Legislature approves a Clean Heat Standard program that requires a DDA.

The Order-of-Appointment process is its own stand-alone component of the Commission’s work on preparing for the potential Clean Heat Standard program. As recognized in Act 18, in other contexts, such as in appointing the electric efficiency utilities (“EEUs”), the Commission has used a similar process.¹¹ In our EEU work, we do not have a rule for the appointment, management, reporting, regulation, and budget-setting of EEUs. We are taking that approach for the DDA as well.

⁷ 30 V.S.A. § 8125(b).

⁸ Public comments on the role, number, and status of default delivery agents for the potential Clean Heat Standard were requested in December 2023 and summarized in the Commission’s April 2024 order on that topic. *See Order on the Role, Number, and Status of Default Delivery Agent(s) in the Potential Clean Heat Standard Program*, Case No. 23-2221-INV, Order of 4/26/24.

⁹ *See id.*

¹⁰ Case No. 23-2221-INV, RFI issued 9/6/24. The Commission was required by Act 18 to open a proceeding “to establish the default delivery agent credit cost or costs and the quantity of credits to be generated for the subsequent three-year period.” 30 V.S.A. § 8125(e)(1).

¹¹ *See* 30 V.S.A. § 8125(b) (“An existing order of appointment issued by the Commission under section 209 of this title may be amended to include the responsibilities of the default delivery agent.”).

B. Technical Aspects of Administering the Clean Heat Standard

The Commission has determined that several technical aspects of the Clean Heat Standard do not fit within a rulemaking. The Commission will instead issue orders detailing these aspects of the potential program's implementation. The areas that will be covered in Commission orders are:

- Registration of fuel dealers – process, guidance, and enforcement;
- The pacing process for credit retirement;
- Establishing obligated parties and their annual clean heat credit requirements;
- Setting the clean heat credit retirement schedule;
- Setting declining carbon intensity values for liquid and gaseous clean heat measures;
- Determining the minimum percentage of clean heat credits being retired each year that must result from the implementation of clean heat measures for customers with low and moderate income;
- Deciding how early action credits will be awarded and valued; and
- Assessing the Clean Heat Standard's interaction with other programs (such as Tier 3 of the Renewable Energy Standard) as well as inter-eligibility requirements.

The Commission has issued or anticipates issuing orders before January 15, 2025, regarding all the bullets above. Further work on these topics will be required if the Legislature adopts the Clean Heat Standard program.

C. A Credit Platform

Other jurisdictions, such as California, Oregon, and Canada, have developed digital platforms to manage data and processes related to the implementation of low-carbon fuel standards like the Clean Heat Standard.¹² These platforms facilitate fuel pathway certification approval; fuel transactions reporting and recordkeeping; and credit generation, banking, sale, transfer, and trading. Non-regulated entities, such as brokers, may also participate in these platforms, which are therefore open to participants beyond obligated parties and fuel dealers. Although such platforms can reduce administrative complexity over time, they are costly to develop and maintain. The costs can remain high when they are not shared regionally, nationally, or even internationally. Thus, the cost is dependent on the development of a marketplace for the credits and adoption of similar low-carbon policies in other jurisdictions.

¹² Vermont has the related experience of interacting with the New England Power Pool Generation Information System (NEPOOL GIS) for purposes of regulating compliance with the Vermont Renewable Energy Standard ("RES"). NEPOOL GIS is the entity that issues and tracks the renewable energy credits (RECs) that Vermont distribution utilities use to show compliance with the RES.

Given the complexity and cost of developing a credit platform, the Commission is holding off on creating or recommending a platform until the Legislature has determined whether and, if so, in what form the Clean Heat Standard will continue to be developed. If the Legislature adopts the Clean Heat Standard program, the creation or adoption of a credit platform would not be part of the Commission's rule. A credit platform would likely be something operated independently by a third-party vendor. Such platforms typically have their own manual for engagement with the platform.¹³ For these reasons, the Commission's draft rule does not include the details of a credit management platform but does reference the existence of such a platform.

D. The Checkback Report

Also due on January 15, 2025, is the Commission's second checkback report to the Legislature. The Commission is required to include the following in its report:

estimates of the impacts of the Clean Heat Standard on customers, including impacts to customer rates and fuel bills for participating and nonparticipating customers, net impacts on total spending on energy for thermal sector end uses, fossil fuel reductions, greenhouse gas emission reductions, and, if possible, impacts on economic activity and employment. The modeled impacts shall estimate high-, medium-, and low-price impacts. The report[] shall recommend any legislative action needed to address enforcement or other aspects of the Clean Heat Standard, including how to ensure fuel use that occurs outside the thermal sector is not impacted under the program.¹⁴

In addition to the economic study required by Act 18 for this second checkback report, the Commission intends to report on the following:

- The context for thermal sector greenhouse gas emission reductions, including the Greenhouse Gas Inventory, Global Warming Solutions Act, and existing thermal programs and funding;
- An overview of the Commission's implementation of the Clean Heat Standard to-date;
- An updated funding proposal per Act 18, Section 6(h); and
- Underlying issues with implementing the Clean Heat Standard program as envisioned by the current legislation.

The Commission's vision for the second checkback report is to inform the Legislature's decision about the Clean Heat Standard. Because the Commission has been engaged in implementing the

¹³ See, e.g., California Environmental Protective Agency Air Resources Board, *Low Carbon Fuel Standard User Guide* (v. 1.2), available at https://ww2.arb.ca.gov/sites/default/files/classic/fuels/lcfs/guidance/lrt_cbts_userguide.pdf; Environment and Climate Change Canada, *Clean Fuel Regulations Credit and Tracking System: User Guide for Primary Suppliers, Registered Creators, and Foreign Suppliers* (v. 2.1), available at <https://www.canada.ca/content/dam/eccc/documents/pdf/climate-change/clean-fuel/regulations/cats/CFR-Credit-Tracking-System-User-Guide-Primary-Suppliers-Registered-Creators-Foreign-Suppliers-v2-1.pdf>.

¹⁴ Act 18, § 6(i).

early stages of a potential program, we want to provide meaningful feedback on the obstacles to implementation and areas of concern that have come to light in the early stage of development.

Further, the Commission will provide a proposed alternative mechanism for accomplishing the same legislative aims as the Clean Heat Standard. This alternative proposal seeks to address some of the major pitfalls that the Commission has encountered in attempting to work through the Clean Heat Standard as originally conceived. These roadblocks include: the overall complexity and significant administrative costs, lack of a robust and liquid market for clean heat credits, and inconsistencies with the accounting performed in the Greenhouse Gas Inventory.

IV. Costs

The Commission recognizes that many participants in the Clean Heat Standard proceedings, the advisory groups, and members of the public have requested detailed cost projections. The Vermont Department of Public Service's potential study includes some potential costs of the Clean Heat Standard as currently conceived.¹⁵ Using the Department's potential study as well as other cost modeling, the Commission will provide additional cost analysis in its checkback report that will be submitted to the Legislature on January 15, 2025. The Commission also understands that the Vermont Legislative Joint Fiscal Office endeavors to perform additional cost analysis.

The Commission is not providing a cost estimate at this time. However, we do point out in several places in this status report the types of administrative costs associated with the Clean Heat Standard as currently conceived.

V. An Alternative to the Clean Heat Standard

The Commission has previously been asked to study other mechanisms for reducing thermal sector emissions. Given the regulatory complexity and administrative costs of the Clean Heat Standard, the Commission reiterates its findings of its final report required by Act 62 of 2019:

The basic policy question — how to fund energy efficiency and fuel switching in the world of unregulated fuels — has been studied for many years. A long list of studies — going back over a decade — from a variety of stakeholders all recommend that the Legislature establish a stable and sizable stream of funding for thermal and transportation efficiency and fuel switching. At current funding levels, Vermont

¹⁵ Vermont Department of Public Service, Clean Heat Standard Assessment of Thermal Sector Carbon Reduction Potential in Vermont (Sept. 1, 2024), available at <https://publicservice.vermont.gov/sites/dps/files/documents/NV5%20-%20VT%20Act%2018%20Clean%20Heat%20Standard%20Potential%20Study%20Report.pdf>.

will fail to achieve its ambitious goals to reduce energy usage and greenhouse gas emissions.¹⁶

As detailed in the Commission's Act 62 preliminary report, programs currently in place span electric efficiency, thermal energy, electrification, electric load management, transportation, and cross-cutting efficiency.¹⁷ Programs such as the Weatherization Assistance Program ("WAP"), Vermont Gas Systems, Inc.'s residential and commercial energy efficiency programs, Efficiency Vermont's and the City of Burlington Electric Department's Thermal-Energy and Process-Fuel Efficiency ("TEPF") services, and advanced wood heating initiatives provide proven and straightforward mechanisms for decarbonizing Vermont's thermal sector. The issue is simply insufficient funding to meet the requirements of the Global Warming Solutions Act.

The Clean Heat Standard as currently conceived requires substantial additional costs and regulatory complexity above the funding needed to accomplish Vermont's greenhouse gas emission reduction goals. For example, the Clean Heat Standard would require establishing a credit marketplace managed by what is likely to be a costly credit platform, the potential for fraud and market manipulation, the appointment of new or varied default delivery agents with administrative costs of their own, and the participation and regulatory engagement of hundreds of fuel dealers and other actors — *e.g.*, companies and individuals that install clean heat measures — not currently or historically regulated by the Commission.

Our work over the past year and a half on the Clean Heat Standard demonstrates that it does not make sense for Vermont, as a lone small state, to develop a clean heat credit market and the associated clean heat credit trading system to register, sell, transfer, and trade credits. Because the Clean Heat Standard introduces these additional regulatory hurdles and costs, the Commission is considering other options to achieve Vermont's greenhouse gas emission reduction goals for the thermal sector.

One option, as advanced in the Commission's Act 62 final report, is a new thermal energy benefit charge on the sale of fuel oil, propane, and kerosene.¹⁸ Similar to the long-standing electric efficiency charge, the Commission would set the thermal energy benefit charge based on statutory criteria, including the need to provide sufficient funding to meet the Global Warming Solutions Act requirements. The funds raised could be spent directly on fossil-fuel-reduction projects such as weatherization and electrification, avoiding the complexity and high administrative costs of a thermal credit market in which only Vermont participates. We intend to develop this alternative concept in the checkback report and will solicit feedback later this year.

¹⁶ Vermont Public Utility Commission, Act 62 – Final Report on All-Fuels Energy Efficiency (Jan. 15, 2021) at 1 (citations omitted), available at https://puc.vermont.gov/sites/psbnew/files/doc_library/act-62-final-report-amendment-020321.pdf.

¹⁷ Vermont Public Utility Commission, Act 62 – Preliminary Report on All-Fuels Energy Efficiency (Jan. 15, 2020) at 20-36, available at https://puc.vermont.gov/sites/psbnew/files/doc_library/Act%2062_PreliminaryReport%201.15.20.pdf.

¹⁸ Vermont Public Utility Commission, Act 62 – Final Report on All-Fuels Energy Efficiency (Jan. 15, 2021) at 13-15.

We recognize that current programs will need to be developed further to achieve Vermont's greenhouse gas emission reduction goals. For example, discussion regarding the Clean Heat Standard has illuminated one area where existing programs may need to be augmented — expanding the use of biofuels, which is likely to be one of the more cost-effective strategies to meet the requirements of the Global Warming Solutions Act. The Commission will be reviewing clean fuel programs currently implemented by a handful of other states and will recommend a path forward in this area in the checkback report.

VI. Process for Public Input on the Draft Rule

Act 18 requires a 30-day comment period on the Commission's draft rule. The Commission is issuing the draft rule and this companion document on October 1, 2024, and providing 30 days for public comment. During this public comment period, the Commission will be hosting a workshop and a public hearing to discuss the draft rule. On October 7, 2024, we will hold a technical workshop to talk through the details of the draft rule. On October 30, 2024, we will hold a public hearing on the draft rule. Details for each of these meetings are included in the order that issued with this status report. Notices will be issued for both the workshop and the public hearing.

After the deadline for comments on the draft rule, the Commission will compile and summarize the comments and evaluate what changes to the draft rule should be made before preparing a final proposed rule for submission to the General Assembly, pursuant to Act 18. If necessary, the Commission will seek clarification or additional comments on the changes.

In sum, the draft rule builds on 18 months of information requests, straw proposals with comment, Technical Advisory Group meetings and feedback, Equity Advisory Group meetings and feedback, public engagement sessions, State agency engagement, and informal information gathering. It is the culmination of all the work since Act 18 was passed by the Legislature in 2023.

VII. Conclusion

This status report serves as a companion document to the Commission's draft rule to provide context for how the draft rule fits into the work that the Commission has engaged in since Act 18 was passed by the Legislature in 2023. To date, the Commission's work has required flexibility and ingenuity to carry out the development-phase directives in Act 18. If the Legislature adopts the Clean Heat Standard program, the Commission will be tasked with many aspects of the Clean Heat Standard that build on, modify, or potentially even undo some of this early work. It is in that environment that the Commission has drafted a rule that establishes the core, outward-facing components of the potential program so that affected entities, particularly those who would now come under the Commission's regulation, can understand when and how they are expected to engage in the regulatory process.

Appendix A: Guide to the Draft Rule

PART I: GENERAL PROVISIONS

8.101 Purpose and Background

Explains the purpose of the draft rule, what prompted the Commission to write it, and the general goals of the Clean Heat Standard.

8.102 Authority

Provides the statutory authority for the Commission to create, modify, and enforce the draft rule and other aspects of the potential Clean Heat Standard program.

8.103 Definitions

Provides a list of relevant terms used in the draft rule and their intended meanings. All terms defined in Act 18 have been included.

PART II: REGISTRATION, OBLIGATED PARTIES, AND COMPLIANCE PATHWAYS

8.104 Fuel Dealer Registration and Reporting Requirements

Explains when and how fuel dealers must register with and report to the Commission and retain relevant documentation.

8.105 Determining Obligated Parties

States what data the Commission will use to determine whether a fuel dealer is an obligated party and that the Commission will calculate how many clean heat credits obligated parties owe for each compliance year.

8.106 Clean Heat Standard Compliance, Waiver Process, and Credit Fulfillment Plans

Explains that the Commission will establish the number of clean heat credits that each obligated party must retire each calendar year, and how those obligations will be treated if an obligated party is acquired or goes out of business. Provides two pathways for obligated parties to meet their obligation based on whether an obligated party uses a default delivery agent. Establishes a deadline for obligated parties to report a plan for credit fulfillment for the next compliance year.

PART III: CLEAN HEAT MEASURES

8.107 Process for Approval of Clean Heat Measures

Explains who may propose new clean heat measures, how they should do so, the process for approval, and the status of unapproved measures. Describes how renewable natural gas and similar measures are to be reported to the Commission to qualify as a clean heat measure.

8.108 Clean Heat Measure Group

Details how the credits generated by each registered clean heat measure will be assigned to a clean heat measure group as required by Act 18.

PART IV: EMISSIONS ACCOUNTING

8.109 Updating the Emissions Table

Explains when the emissions table of lifecycle emission rates for heating fuels and any fuel that is used in a clean heat measure will be updated and how it can be updated outside of the regular review schedule.

PART V: CLEAN HEAT CREDITS

8.110 Carbon Equivalency of Clean Heat Credits

States the CO₂e value of a clean heat credit.

8.111 Registering and Tracking Clean Heat Credits

Explains who can register clean heat measures, what information is necessary to create a potential clean heat credit when a measure is registered, how clean heat credits will be time stamped, when a clean heat credit can be traded or retired, and how credits will be tracked.

8.112 Verifying Clean Heat Credits

States who verifies a clean heat measure and that the act of doing so changes the status of the credit.

8.113 Measure Attributes and Credit Ownership

Sets out how initial credit ownership is determined for different types of clean heat measures. Restricts how the initial measure owner can transfer their measure attributes. Explains how clean heat credits can be traded.

8.114 Demonstrating and Verifying Annual Compliance

Determines where obligated parties will retire their credits to fulfill their annual obligation, what it means to retire credits, and the conditions under which credits are eligible for retirement. Explains how annual compliance will be verified, the schedule on which obligated parties must demonstrate compliance, and the Department of Public Service's role in verifying compliance. Outlines the process the Commission will use to determine whether an obligated party is in compliance and to assess non-compliance penalties or directives. Provides a method for obligated parties to pursue a waiver for noncompliance.

8.115 Banking Clean Heat Credits

Provides the ability for entities to bank clean heat credits.

8.116 Disclosures and Representations Regarding Clean Heat Credits

States the requirement of providing disclosures with clean heat measures and where to find sample disclosures.