January 20, 2017

Clerk of the Board
California Air Resources Board
1001 I Street
Sacramento, CA 95812

Submitted Electronically:
https://www.arb.ca.gov/lispub/comm2/bccommlog.php?listname=ct-amendments-ws

RE: Proposed 15-Day Modifications to the Cap-and-Trade Regulation

Dear Chairwoman Nichols and Members of the Board:

Agricultural Council of California (Ag Council) and Dairy Institute of California appreciate the opportunity to submit comments in response to the December 21, 2016 Proposed 15-Day Modifications to the Cap-and-Trade Regulation (Modified Regulation).

Ag Council is a member-supported organization advocating for more than 15,000 farmers across California, ranging from small, farmer-owned businesses to some of the world's best-known brands. Ag Council works tirelessly to keep its members productive and competitive, so that agriculture can continue to produce the highest quality food for the entire world.

The Dairy Institute is a California dairy processor trade association founded in 1939. Dairy Institute represents milk and dairy processors on legislative, regulatory and economic policy.

A number of our member companies participate in the cap-and-trade program, and as a result, we wanted to take the opportunity to comment on several key points:

- First, we continue to request the California Air Resources Board's (ARB) consideration of adjusting the food processing industry assistance factor to reflect high leakage and provide 100 percent allocation in the third compliance period.
- Second, we strongly oppose the ARB proposed post-2020 approach to allowance allocation that uses the non-peer reviewed results of two academic studies and continues to categorize food processing in the medium leakage category.
- Third, we continue to emphasize additional concerns regarding benchmarks raised in previous comments.

Assistance Factor for 2018-2020

In recognition of the potential for emissions leakage, Assembly Bill 32 compels ARB to minimize leakage "to the extent feasible" in its operation of the cap-and-trade program. Consequently, and in order to facilitate the transition to emissions pricing, ARB has freely distributed emissions allowances to covered entities according to their production levels and leakage risks. ARB presently infers leakage risk from calculations of industry-specific emissions intensity and trade exposure.

In "Appendix E: Emission Leakage Analysis," released August 2, 2016, ARB staff states that no changes are proposed to the 45-day regulatory proposal for the third compliance period.[1] In joint comments by Ag Council and the Agricultural Energy Consumers Association on September 19, 2016, we stated that providing 100 percent free allowances would minimize the potential harm to the agricultural sector and avoid simply shifting emission to other locations outside of California. In response to stakeholder comments, staff responded in the December 21, 2016 Notice of Public Availability and Modified Text Document:

> *"In response to the 45-day regulatory proposal, some stakeholders requested that ARB modify third compliance period assistance factors to retain the 100 percent assistance factors for sectors in the medium and low leakage risk categorizations. These stakeholders argue that these sectors are at high risk of leakage and therefore require 100 percent allocation to prevent emissions leakage. These requested changes are outside of the scope of the current regulatory changes, as the 45-day regulatory proposal did not address assistance factors for those sectors during the third compliance period. Therefore, no changes to those assistance factors are being proposed within this rulemaking package. Further, leakage analyses performed for the initial Regulation in 2010/2011 and those performed for the current regulatory changes demonstrate that all sectors currently in the medium- and low-leakage risk categorizations do not require 100 percent allocation to protect them from emissions leakage. The assistance factors proposed for the post-2020 period (Table 8-3 of this 15-day proposal) demonstrate that the third compliance period assistance factors are either at the level needed to prevent against emissions leakage or they are higher than needed."*[2]

In Section 95870 of the Modified Regulation, Table 8-1 is adjusted to include new leakage risk categorizations and assistance factors.[3] For example, Wet Corn Milling was determined to have high leakage risk and was assigned a 100 percent third compliance period assistance factor. We understand this change was included in the Modified Regulation because it was identified in the scope of the 45-day regulatory proposal. However, we disagree with the assertion that all sectors currently in the medium leakage do not require 100 percent allocation in the third compliance period. As stated in our November 4, 2016 comment letter, the main reason ARB commissioned additional research on leakage was because there were doubts that ARB had correctly measured the energy intensive and trade exposed nature of our members.[4] In previous comment letters we have continued to ask ARB to conduct more analysis and advocate that the food processing sector should be moved to the top Industry

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[1] https://www.arb.ca.gov/regact/2016/capandtrade16/appe.pdf (page 3)
[2] https://www.arb.ca.gov/regact/2016/capandtrade16/15daynotice.pdf (page 15)
[3] https://www.arb.ca.gov/regact/2016/capandtrade16/attacha.pdf (page 157)
[4] https://www.arb.ca.gov/lists/com-attach/29-ct-amendments-ws-VGYBN11tWD1SeQk4.pdf (page 2)

Assistance Factor tier of “high” and receive 100 percent free allowances due to price pressures from domestic and international markets. Given the previous examples of the peach industry import pressures, coupled with the already existing problems of California dairies leaving the state, leakage has been demonstrated within California agriculture due to the competitive disadvantages we are experiencing in our current regulatory environment. This impending cap-and-trade regulation is bound to exacerbate this issue, as we are the only state in the nation with this law.

Having a reliable and stable supply of safe, high quality, and affordable domestic supply of food should be a public policy priority. California produces food in the most environmentally sound, socially conscious state in the nation. ARB should protect our food supply by reducing the cost of this regulation to the best of its ability. Furthermore, food processors are economic drivers in many disadvantaged communities across the state. For these reasons ARB should designate food processors as high risk for leakage.

Post-2020 Industry Assistance Factor Calculations

In contemplating leakage mitigation efforts beyond 2020, ARB directed staff to “investigate potential improvements” to its system of allowance allocation in order to better minimize leakage. Appropriate allocation of emission allowances is critical to ARB’s mandate to minimize leakage and, indeed, to the success of California’s climate-change program. The determination of leakage potential across industries and of mitigation measures is essential for the effective implementation of additional regional climate-change policies.

As ARB considers both the third compliance period and post-2020 assistance factors for food processing, it is important to note that this industry has historically been influenced by not only supply, but also with the opportunities for cost-efficient processing. Food processing facilities have been built in locations where market access is conducive to lower manufacturing and shipping costs. Conversely, product supplies have moved and expanded to meet the processing capacities of those facilities. Equipment in one plant can be moved to a new location to serve another more lucrative market.

As with other California industries now regulated under cap-and-trade, food processing was built to meet domestic and international demand. Export markets have grown to meet California’s product output. As we have stated in earlier comments, domestic and international markets are dynamic and volatile, driven by competitiveness in product price. Product prices are based upon costs.

The importance of accuracy in the calculation of assistance factors, before or post-2020 cannot be overstated. Calculations applied to the food processing sector should be enhanced by readily available data. For example, the California Department of Food and Agriculture compiles useful data in its annual manufacturing cost study for dairy. For comparison and determination of emissions leakage, a variety of cost comparisons can be made using a variety of comparable cost information for other dairy manufacturing regions within the United States. Recognizing that the product mix is not uniform across domestic manufacturers, this cost data would give the fuller picture of the California dairy industry and its competitive placement against domestic dairy product manufacturers.

In Attachment B of the Modified Regulation, staff proposes a framework whereby percent assistance factors will be assigned for each manufacturing industry by summing an international leakage mitigation assistance factor based upon the University of California Berkeley study[5] and a domestic leakage mitigation assistance factor based upon the Resources for the Future study.[6] Currently, staff is not proposing to use the data from the Cal Poly San Luis Obispo food processing leakage study.[7] Staff states in Attachment B that they, "appreciate the difficulty of obtaining results given limited aggregated data of these food processing industries," and that staff, "will continue to evaluate the potential to incorporate the study into development of AFs for these four sectors."[8] Substantial public sector funds were spent to support this study and after many years of research, we urge ARB to revisit and review its findings. If the study was updated, it will likely demonstrate the inability to pass on the cost of this program in the food processing industry.

Benchmarks

In the 45-day regulatory proposal, staff proposed eliminating the benchmark for tree nut manufacturing because emissions per unit of product are highly variable. In absence of a benchmark, staff suggested that covered entities conducting this activity would receive allowance allocations under the energy-based methodology. In joint comments by Ag Council and the Agricultural Energy Consumers Association on September 19, 2016, we recommended, "reinstating the benchmark for tree nut manufacturing and refining the product-based benchmark to reflect updated data and efficiency trends."[9] In the Modified Regulation staff expresses that the benchmark review is ongoing and staff may propose further changes. We are committed to keeping the Almond Processing and Pistachio Processing Benchmark intact. We hope to find a resolution that works for both ARB and covered entities.

We appreciate your consideration and the opportunity to comment. Our intention in these comments is to avoid simply shifting emissions to other locations outside of California. Should you have any questions or need anything further from us, please contact either Rachael O'Brien at (916) 443-4887 / Rachael@agcouncil.org or Rachel Kaldor at (916) 441-6921 / RKaldor@dairyinstitute.org.

Respectfully,

Emily Rooney
President
Agricultural Council of California

Rachel Kaldor
Executive Director
Dairy Institute of California

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[5] https://www.arb.ca.gov/cc/capandtrade/meetings/20160518/ucb-intl-leakage.pdf
[6] https://www.arb.ca.gov/cc/capandtrade/meetings/20160518/rff-domestic-leakage.pdf
[7] https://www.arb.ca.gov/cc/capandtrade/meetings/20160518/calpoly-food-process-leakage.pdf
[8] https://www.arb.ca.gov/regact/2016/capandtrade16/attachb.pdf (page 17)
[9] https://www.arb.ca.gov/lists/com-attach/73-capandtrade16-UTIGYVEgVSsKbQNt.pdf (page 7)