



To: Mary Nichols, Chair
California Air Resources Board

Fr: Climate Change Policy Coalition

Date: September 19, 2016

Re: California Air Resources Board's Consideration of the
Proposed Amendments to the Cap-and-Trade Regulation

The Climate Change Policy Coalition (CCPC) is a coalition of business and taxpayer groups working for effective implementation of California's climate policies (AB 32 and SB 32). CCPC represents regulated entities subject to the cap-and-trade program, and our goal is to provide a constructive voice in how program improvements are proposed and design element updates are adopted by the California Air Resources Board (ARB).

CCPC believes that the cap-and-trade program can become an effective regulatory program to reduce emissions in a cost effective manner that maintains the competitiveness of California's businesses – but how that's done can make or break California's economy.

Currently, the cap-and-trade regulation contains numerous issues that need resolution prior to the next time the Board considers the final proposed amendments to the cap-and-trade Regulation. These issues include design flaws, which should be addressed in the regulatory amendments.

ARB is on questionable legal ground by generating auction revenue from an effective tax on carbon absent the necessary legislative vote. We ask the Board to be cognizant of the outstanding legislative and legal issues that could affect the outcome of the current program.

ARB Lacks Statutory Authority to Set Post-2030 Allowance Budgets

SB 32 (Pavley) does not authorize the Governor or the ARB to establish a greenhouse gas emissions limit that would be applicable after 2030 – and in passing this legislation, lawmakers made clear that they shall have oversight of climate change policies going forward. We recommend that ARB remove post-2030 caps from this rulemaking.

Lack of Post-2020 Design Detail Impedes Stakeholder Input

CCPC objects to the lack of critical regulatory detail regarding several 2030 design elements in the proposed regulation. There is no way to analyze the economic impacts of the proposed 2020-2030 cap due to the lack of information on trade exposure status, holding limits or other cost containment policies (besides APCR).

The mix of covered entities and the amount of emissions will change over time and the new 2030 goal is very stringent, the rationale for the cap number should be more robust than simply that ARB applied the same percentage as in 2010's rulemaking. It is not clear why it is necessary to make the cap for cap-and-trade more stringent than the overall state goal of 256.6.

This current and ambiguous approach limits stakeholder input and may constrain the scope of what ARB can consider in subsequent 15-day changes.

Additional Trade Exposure Protection is Necessary

In the last round of amendments to the cap-and-trade regulation ARB extended full industry assistance factor into the second compliance period. Today, California's market remains largely isolated from other

markets where more cost-effective reductions exist, as it was in the 2013-2014 timeframe. Accordingly, an extension of the same full industry assistance is still warranted until such time that leakage risk is eliminated, both to maintain the environmental integrity of the program and to protect California jobs and the state economy.

Reductions in GHGs are driven by the cap, not by allowance allocation. Reductions in GHGs are improved if the state minimizes leakage as required in AB 32 38562(b)(7) because leakage causes emissions outside of the cap to increase. The program can better meet California's climate goals by extending the full industry assistance factor. Emission reductions will continue to occur because industry does not receive allowances over the cap. For these reasons, we recommend that ARB extend full industry assistance factor into future compliance periods.

Offsets Must Be Expanded to Capture Additional Cost Containment and Emissions Reduction Benefits

Offsets are a proven and cost-effective means of meeting AB 32 compliance obligations. They are also an effective means of achieving significant GHG emissions reductions in other jurisdictions which lack GHG regulatory programs. Expanded and expedited use of offsets is consistent with ARB's statutory obligation to achieve the maximum technologically feasible and cost-effective GHG emissions reductions. For example, authorization of sector-based offsets will be critical to ensuring adequate offset supply in future compliance periods, and as ARB has observed, should be incorporated into the cap-and-trade regulation in advance of the third compliance period.

Allowance Price Containment Reserve (APCR) Design Increases Costs and Decreases Liquidity Conflicting with ARB's Objectives

A new proposed provision allows ARB to transfer unsold allowances from the Current Auction, if unsold for 24 months after their initial sale date, to be transferred to the APCR and made available through a Reserve Sale. This process would come into effect January 1, 2018.

ARB's proposed method of continuing allowance diversions from annual budgets and proposing to funnel unsold allowances into the APCR is concerning.

Artificially raising costs conflicts with AB 32's statutory objective to develop market mechanisms as cost-effectively as possible. It could lead to a very large APCR decreasing liquidity in the overall market. ARB's stated desire to increase market liquidity (*ISOR Executive Summary, pp. 7*) conflicts with the APCR changes. ARB should continue to return unsold allowances to the auction.

Emission Reductions and Relative Cost-Effectiveness of Each Measure

Robust and regular oversight and informational hearings must accompany any post-2020 climate policies. We believe ARB should, at a minimum, review each current regulation resulting from AB 32 and determine if, (1) the regulation has accomplished the intended GHG reduction objectives or, (2) if the regulation has failed to achieve its goal and may simply have placed undue burdens on California's businesses and consumers without reducing our GHG emission levels, and (3) if there were a more effective means of achieving the intended reduction. Each measure adopted in the 2030 Target Scoping Plan and accompanying regulations should be held to the same standards of accountability.

Appendix F

The regulations and implementation of the provisions of California's greenhouse gas policies will have significant impact on businesses within the state, particularly those in the industrial sector that are directly affected by a mandate to report GHG emissions levels or participate in the cap-and-trade program. As such it is important that the early and sustained input from a representative group of industrial entities be a part of ARB's process to develop regulations in this area. ARB must take the step to establish an "Industrial Advisory Council"

(IAC) to meet on a regular basis to evaluate and provide feedback to ARB staff during the regulatory development process in this formal capacity.

The California Global Warming Solutions Act of 2006 (AB 32) directed ARB to form the Economic and Technical Advisory Committee to “to advise the state board on activities that will facilitate investment in and implementation of technological research and development opportunities.” In a similar fashion, the IAC would advise ARB regarding activities that will support industrial activity toward achieving California’s overall GHG reduction goals. Taking this step would improve the regulatory development process.

CCPC looks forward to finding solutions and working with ARB staff to improve the cap-and-trade program and amendments necessary to ensure we have a program in place that meets the goals of AB 32 while protecting the stakeholders being held accountable for the system to be a success. Should you have any questions or need anything further from us, please feel free to contact Shelly Sullivan at (916) 858-8686

cc: California Air Resources Board Members
Dr. Steve Cliff, Senior Advisor to the Chair
Richard Corey, Executive Officer
Edie Chang, Deputy Executive Officer