

August 11, 2011

California Air Resources Board  
1001 I Street  
Sacramento, CA 95814  
*Submitted electronically*

Dear Chair Nichols and Members of the Board:

The Nature Conservancy (TNC) appreciates the opportunity to submit comments on the July 25th 15-day rule modification to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms Regulation, including Compliance Offset Protocols (cap-and-trade program). As we have stated in previous workshops and public comments, TNC remains supportive of the overall cap and trade program, its success, and California's goal to reduce greenhouse gas emissions. With this in mind, we offer the following recommendations related to definitions, liability, forest biomass and renewable energy, and use of allowance revenue.

### **Definitions § 95802**

- 1) *The definition of "forest owner" should be clarified to focus on those "owners" with an interest in real property that would impact forest offsets and be refined further to eliminate the reference to liability.*

The current definition of forest owner is expansive and includes an entity(ies) that holds *any* interest in the real property involved in the forest offset project. The definition, in Subarticle 2, § 95802(a)(103), of the regulation states the following:

*"Forest owner" means the owner of any interest in the property involved in a forest offset project. Generally, a Forest Owner is the owner in fee of the property involved in a forest offset project. In some cases, one entity may be the owner in fee while another entity may have an interest in the trees or the timber on the property, in which case all entities or individuals with an interest in the property are collectively considered the Forest Owners, however, a single Forest Owner must be identified as the Offset Project Operator. All Forest Owners are ultimately responsible for all commitments associated with a forest offset project.*

For clarity, the definition should be simplified as it is currently overbroad and confusing. The definition goes beyond a simple regulatory definition and identifies the responsibility of forest

owners (see last sentence of definition). This last sentence causes some confusion with the liability sections that are addressed in future sections of the regulation (e.g., Subarticle 13, §95981 et al.). Therefore, TNC recommends that this last sentence be deleted from the definition, as it is not necessary in this section.

For a number of reasons, including liability, it is important for the regulation to clarify that a single forest owner must be identified as an Offset Project Operator in instances where there is more than one “forest owner.” While it is helpful to have such a statement also included in the definition, this type of directive should be stated in the other provisions of the regulation where applicable (e.g., Forest Protocol) to avoid confusion.

The definition should also clarify that the “interest” referenced in the definition relates to real property versus property in general, as it could be interpreted to include personal property. Furthermore, TNC recommends that the definition be narrowed to specify that the interest in real property should be constrained to those that directly impact forest offsets, such as the fee owner, easement holder, and the owner of timber or carbon rights.

- 2) *The forest owner definition in the Compliance Offset Protocol for Forests should be adjusted to be internally consistent and consistent with the cap and trade regulations*

The Compliance Offset Protocol for Forests contains two different forest owner definitions on pages 10 and 82. The former definition is consistent with the definition in the cap and trade regulations, Subarticle 2, § 95802(a)(103). However, the latter definition is inconsistent and excludes conservation easement holders from the forest owner definition. This definition needs to be amended, and TNC recommends that the definition in the Protocol be adjusted to reflect our recommendations stated in section 1.

## **Forest Offset Credit Reversals, Invalidation and Liability §§ 95983 – 95985**

- 1) *ARB should refine forest offset liability associated with invalidation and intentional reversals by identifying the Offset Project Operator as the party initially responsible for invalidation of forest offsets*

According to sections 95983 and 95985 of Subarticle 13, the forest owner is responsible for replacing offsets whether it’s due to invalidation or an intentional reversal. However, as stated previously, the forest owner is broadly defined to include any entity that has an interest in the property involved in the forest offset. The result of this broad definition creates significant uncertainty regarding who among the “forest owners” would be responsible for replacing offsets.

The forest owner definition also states that only one entity who qualifies as a forest owner can be the Offset Project Operator. According to Subarticle 2, §95802 (a) (172), an “Offset Project Operator” is the “entity(ies) with legal authority to implement the offset project.” If the Offset Project Operator (OPO) has the legal authority to implement the offset project and those who qualify as forest owners must identify only one OPO, it would be consistent and more clear to identify the OPO as the party, at least initially, who would be responsible to replace forest offsets in the event of forest offset invalidation and intentional reversals. ARB could also include a separate provision as it does in §95985(h) that retains the authority of California to pursue enforcement action against any party in violation of the article. Doing so would provide more certainty to forest owners, market participants and regulated entities regarding the chain of liability that ARB would seek in an enforcement action and allow these parties to more thoughtfully address these risks in contracts.

- 2) *ARB should use the forest offset buffer pool for invalidation of forest offsets in the same manner it relies on the pool for intentional reversals to avoid inconsistencies*

In the event of an intentional reversal of forest offsets, the current draft of the regulation (Subarticle 13, § 95983(c)(3)) requires the forest owner to replace these reversed tons with valid offset credits or other compliance instruments. For reasons stated earlier in this document, TNC recommends that this replacement responsibility be assigned to the OPO since this party, according to the “forest owner” definition, is effectively the forest owner.

In instances where intentionally reversed forest offsets are not replaced within 90 calendar days, ARB relies on the forest buffer account to replace the reversed tons. In the case of forest offsets, there may be instances where there is little difference between an intentional reversal and the invalidation of a forest offset. For instance, a party may intentionally harvest timber in a forest offset project area that effectively reverses (or reduces) offset credit that has already been attributed to a compliance obligation. This action could qualify as an intentional reversal, triggering the remedial process of § 95983(c)(3). At the same time, this intentional reversal could also qualify for offset credit invalidation pursuant to § 95985 (b)(1) or(b)(2) as the reversal could be characterized as information that was not accurate or as a data report that overestimated the amount of GHG removal enhancements. While this instance could qualify for either scenario, the processes for addressing this issue in the regulations are different with one using the forest buffer as a fall back option (intentional reversal) and the other not using the forest buffer account at all (invalidation).

To avoid this inconsistency and likely future conflict in regulatory interpretation, TNC recommends that ARB utilize the same remedial process to address forest offset credit

invalidation and intentional reversals. The forest buffer account should be used as security in instances where the OPO does not replace the invalidated or intentionally reversed forest offsets within 90 days. To ensure that the forest buffer account maintains sufficient offsets to remedy reversals and invalidation, ARB could adjust the forest buffer risk rating in the Forest Protocol (see Appendix D of the Compliance Offset Protocol for U.S. Forest Projects) to include invalidation risk.

3) *ARB should continue to provide additional clarification regarding the basis for and extent of offset credit invalidation*

TNC commends ARB for providing additional clarification in the regulations to identify the circumstances under which offset credits may be invalidated. Such clarity will help encourage investments in offset projects as market participants (forest owners, OPOs, capped entities, etc.) will have greater certainty and ability to manage risk. TNC recommends that ARB provide additional clarification to § 95985(b) by identifying the extent to which offset credits may be invalidated. For instance, subsection (b)(2) indicates that credits may be invalidated when the Offset Project Data Report overstates the amount of GHG reductions or removals by more than 5 percent. It is unclear from this provision whether all credits or just the portion that is overstated would be invalidated. Additional detail regarding the scope of invalidation or the process that will be used to determine the scope of invalidation for this subsection as well as the others in this provision would be useful.

## **Treatment of Biomass Energy and Adaptive Management §95852.2**

1) *TNC urges ARB to continue to monitor the upstream carbon impacts related to the use of forest biomass for renewable energy*

As stated in a previous letter submitted to ARB on April 8, 2011, while TNC acknowledges that there may be atmospheric and ecological benefits associated with the use of forest biomass for energy and fuels, such use may not be “carbon neutral” and may not always be ecologically beneficial. The current cap and trade regulations effectively treat forest biomass (woody biomass) as carbon neutral by not requiring a compliance permit for this type of energy. We urge ARB to continue to monitor this issue closely as part of ongoing efforts to maintain the integrity of the cap and trade program and its impacts. In response to our comments and the comments of colleagues, ARB has made adjustments to the Mandatory Reporting Rule (MRR) to gather information that could help assess the carbon impact of forest biomass use for energy. We commend ARB for taking these actions, support those provisions, and will provide additional constructive comments on the MRR in a separate letter.

As part of ARB's policy commitment to adaptive management, we urge ARB to adopt a process to periodically review the treatment of forest biomass for energy in the cap and trade program, including its greenhouse gas impacts and impacts to ecological sustainability. Furthermore, we request that ARB review the recommendations that will be developed for forest biomass through the Low Carbon Fuel Standard Sustainability Workgroup process and consider their application for forest biomass in the cap and trade program.

### **Use of Allowance Revenue**

- 1) *ARB should work with the legislature to establish a program that commits use of allowance revenue to the investment categories identified by the Economic Allocation and Advisory Committee and supported by Board resolution last December*

While TNC acknowledges that ARB may not have full authority to determine how allowance revenue may be used, we urge ARB to work with the legislature to develop an infrastructure that facilitates the investment of allowance revenue consistent with the recommendations of the Economic Allocation and Advisory Committee, published in March 2010, and subsequently endorsed by the Board in its December 16, 2010 resolution (Resolution 10-42). These categories supports funding for, among other things, adaptation of natural systems to climate change (e.g., nature-based adaptation), land use and transportation, job training, disadvantaged communities and regional and local governments. Investments in these categories are critical to facilitate additional greenhouse emission reductions and help nature and people adapt to the unavoidable impacts of climate change.

Once again, TNC commends the Air Resources Board and staff for its extensive work to develop a statewide greenhouse gas reduction program. It's a tremendous effort, and we will continue to provide constructive input to help ensure the cap and trade program is a success. If you have any questions related to our comments, please contact Michelle Passero at [MPassero@tnc.org](mailto:MPassero@tnc.org).