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June 27, 2012

Steven Cliff, Chief of Climate Change Markets Branch
California Air Resources Board
1001 I Street, Sacramento, California

Submitted via weblink at: ***http://www.arb.ca.gov/cc/capandtrade/comments.htm***

Re: Comments on the Proposed Cap-and-Trade Linking Regulation

Dear Mr. Cliff and the California Air Resources Board:

These comments are submitted on behalf of the Center for Biological Diversity regarding the Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms to Allow for the Use of Compliance Instruments Issued by Linked Jurisdictions ("the regulation"), and the associated Staff Report: Initial Statement of Reasons ("ISOR"), released May 9, 2012.[1]

Our primary concern is that the regulation linking California's greenhouse gas cap-and-trade program with partner jurisdictions will force California to accept carbon offset credits from projects with low or no environmental standards, thereby leading to substantial negative environmental impacts. This is of particular concern with respect to forest offset projects, which, if not developed pursuant to environmentally rigorous standards, can impair forest ecosystems, wildlife habitat, and water quality, even in cases when those forest projects may provide climate benefits. California's cap-and-trade program should not contribute financial incentives that would drive forest ecosystem degradation in other states and provinces. California must ensure that our greenhouse gas reduction efforts do not rely on projects that result in ecosystem degradation to our forests or outside the state in order to reduce the costs of compliance for industrial polluters in California.

These overarching concerns are presented in our comment letters submitted in response to the announcement of the development of the regulation and the discussion draft.[2] Our review of the proposed regulation further identified the following concerns: 1) The regulation commits California to accept offsets generated under future regulations not yet written in other jurisdictions; 2) The regulation would force California to accept offset credits with low or no environmental standards; 3) Accepting lower quality offsets would undermine California's authority to achieve the mandate of AB 32 to maximize co-benefits to public health and the environment**;** 4) Accepting lower quality offsets threatens to allow project developers to choose

[1] The proposed regulation is posted at http://www.arb.ca.gov/regact/2012/capandtrade12/appendixa2.pdf. The ISOR is posted at http://www.arb.ca.gov/regact/2012/capandtrade12/isormainfinal.pdf

[2] Incorporated here by reference are the Center for Biological Diversity comment letters dated February 29, 2012, and April 13, 2012.

among different protocols to select one with the lowest standards; and 5) The ISOR fails to analyze potential environmental impacts of projects that will generate offset credits that become part of the California market. These issues are addressed here in turn.

1. The regulation commits California to accept offsets generated under future regulations not yet written in other jurisdictions.

The regulation requires California to accept any offset credit accepted by any linking partner. *"Once a linkage is approved, a compliance instrument issued by the linked jurisdiction may be used to meet a compliance obligation in California."* § 95942 (e) at page 75.

This regulation would commit California now to accepting in the future offset credits from protocols that have not yet been developed yet by partner jurisdictions, as well as any offset credits issued by any other jurisdictions to which we link our cap-and-trade program in the future. California cannot rationally agree to offsets when we do not yet know the content of the protocols for those offsets. It is impossible for ARB to ensure that these as-yet-undeveloped protocols will meet AB 32 standards and other applicable laws, particularly AB 32's requirement that ARB maximize environmental co-benefits in developing market-based greenhouse gas reduction programs. It is not possible even to know the environmental costs of these protocols, much less maximize their environmental benefits, when they do not yet exist. ARB must first determine what the protocols are for any offset it wishes to potentially accept, and then must conduct environmental review of those protocols and receive public comment. ARB cannot and should not commit California to buying offset credits out of this "black box" of potential future protocols.

Furthermore, because we do not yet know the content of the protocols of other jurisdictions, ARB is creating a situation that could lead to contradicting protocols. In the future, when other jurisdictions establish their own protocols, those protocols may or may not be consistent with the protocols California has established. Also, it is not possible for the public to meaningfully comment on protocols that do not yet exist. Only after other jurisdictions establish their protocols can the public meaningfully examine and analyze those protocols.

2. The regulation would force California to accept offset credits with low or no environmental standards.

While the regulation requires California to accept any offset credit accepted by any linking partner, there is no mention in the regulation or the ISOR of any review of offset protocols adopted by other jurisdictions, any consideration of the environmental impacts of offset projects, or any mechanism for reducing California's reliance on offset credits generated by projects with negative environmental impacts. Furthermore, Québec's cap-and-trade regulation contains no environmental criteria for offsets or the adoption of offset protocols.[3]

[3] "The following emission allowances may be traded through the system and used for compliance purposes: (1) every emission unit and early reduction credit referred to in this Title; (2) every offset credit issued by the Minister pursuant to subparagraph 2 of the first paragraph of section 46.8 of the Environment Quality Act; (3) every emission allowance issued by a government other than the Gouvernement du Québec, with which an agreement has been entered into in accordance with section 46.14 of the Act." Québec cap-and-trade regulation § 37.

Under this provision, California would be forced to accept offset credits generated under offset protocols with lesser environmental standards than the offset protocols adopted by California for the same project types (e.g. forest projects), even when the offset projects in other jurisdictions result in significant negative environmental impacts. And while the regulation requires ARB to ensure that all offsets accepted as compliance instruments in California's cap-and-trade are real, permanent, quantifiable, verifiable, and enforceable, it does not provide for any determination of the environmental impacts.

These agreements similarly exclude any determination of environmental impacts. The WCI agreements, to which ARB is a party but which have not been adopted under any California regulatory process, contain no environmental criteria for offset projects or the approval of offset protocols except for the practically meaningless requirement that "projects must meet all applicable local environmental regulations and be in compliance with all applicable laws."[4] The WCI agreements acknowledge that offset projects have "the potential to impact the environment or social environment in which the project is located,"[5] but sets neither standards for ensuring that offset projects do not result in negative environmental impacts nor thresholds for allowable levels of environmental impacts.[6] Furthermore, the WCI agreements explicitly reject the notion of setting standards to achieve environmental or social benefits: "WCI Partners recognize the environmental, social, economic and health benefits that may arise from an offset project and the offset system will focus on those benefits directly related to mitigating climate change. A WCI offset project is required only to result in a greenhouse gas emission reduction or removal."[7]

In December 2011, WCI adopted a process for the approval of offset protocols by WCI partner jurisdictions.[8] Under that process, if a protocol is found to be consistent with WCI

[4] "WCI offset projects must meet all applicable local environmental regulations and be in compliance with all applicable laws in the jurisdiction where the project is located. If environmental or socioeconomic assessments of the proposed project have been done, the project's registration application should reference this work and include a summary of the findings. WCI offset protocols for specific offset project types may require analysis of environmental and socioeconomic impacts beyond what the local jurisdiction would otherwise require and may require additional mitigation of potential negative impacts." WCI *Offset System Essential Elements Final Recommendations Paper* § 8.3, Assessment of Environmental or Social Impacts.

[5] "Offset projects are intended to reduce or remove greenhouse gas emissions. However, any project activity has the potential to impact the environment or social environment in which the project is located." WCI *Offsets Committee White Paper, Task 1: Offset System Essential Elements, Offset Definition (Task 1.1) and Eligibility Criteria (Task 1.2) white paper*, July 2009, at 42.

[6] WCI encourages offset projects to reference environmental impact reviews required under local laws and acknowledges that offset protocols could potentially require analysis and mitigation of environmental impacts beyond what the local jurisdiction would otherwise require. "WCI offset projects must meet all applicable local environmental regulations and be in compliance with all applicable laws in the jurisdiction where the project is located. If environmental or socioeconomic assessments of the proposed project have been done, the project's registration application should reference this work and include a summary of the findings. WCI offset protocols for specific offset project types may require analysis of environmental and socioeconomic impacts beyond what the local jurisdiction would otherwise require and may require additional mitigation of potential negative impacts." WCI *Offset System Essential Elements Final Recommendations Paper* § 8.3. Assessment of Environmental or Social Impacts. http://www.westernclimateinitiative.org/document-archives/Offsets-Committee-Documents/Offsets-System-Essential-Elements-Final-Recommendations/

[7] WCI *Offset System Essential Elements Final Recommendations Paper* § 3.2.3, underline added.

[8] WCI *Final Offset Protocol Review and Recommendation Process*, December 19, 2011.

principles (which do not include environmental criteria or standards), the protocol would be available for use by any of the WCI partners. [9] The WCI process thus appears to require California to accept any offset credits accepted by a WCI partner, and it does not appear to allow California to object to a protocol used by a WCI partner based on negative environmental impacts.[10]

3. The regulation would undermine California's authority to achieve AB 32's mandate to maximize environmental co-benefits.

AB 32 mandates that market-based compliance mechanisms, such as this one, must maximize environmental co-benefits.[11] However, by explicitly committing to accept offsets from any future protocols yet to be written and providing no conditions on their acceptance, the regulation not only makes it impossible to maximize environmental co-benefits, it forfeits any opportunity to analyze, assess, or reduce negative environmental impacts of future protocols. The regulation should explicitly require ARB to analyze the environmental impacts of any offset protocol that generates offset credits that can be used as compliance instruments in California. In addition, the regulation should include provisions that explicitly require that all offsets used for compliance in California must maximize environmental benefits, and that all offset projects in linked jurisdictions meet or exceed the standards of protocols adopted by ARB for similar offset types.

The Center for Biological Diversity has repeatedly expressed concerns over the potential for offset projects to result in negative environmental impacts. This is of particular concern with forest offset projects, which can result in substantial impacts to forest ecosystems, wildlife habitat, and water quality. In order to ensure that California's cap-and-trade program does not rely on or result in the degradation of forests and ecosystems elsewhere, the regulation should not allow credits from forest protocols adopted by any linked jurisdictions to be sold into California's cap-and-trade system absent meaningful minimum protections (e.g. provisions to ensure maintenance of native species, diverse age classes, structural diversity, wildlife habitat, water quality, and other natural resources).

4. Accepting lower quality offsets would allow project developers to choose among different protocols to select one with the lowest standards.

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[9] *Id*. at 3. "The candidate protocol will initially be evaluated against the WCI criteria as defined in the WCI *Offset System Essential Elements Final Recommendations Paper* and the WCI *Detailed Design*: Definition of project scope; Eligibility/additionality requirements; GHG quantification method; GHG emissions reduction method; Monitoring and verification method; Permanence; Leakage."

[10] "Once a Partner jurisdiction determines that another program meets the criteria in section 9.1, the Partner jurisdiction and the other jurisdiction will mutually acknowledge that their programs are compatible and will …Allow the mutual recognition of compliance instruments issued to meet compliance obligations;" WCI *Design for the WCI Regional Program*, July 2010, at 45. http://www.westernclimateinitiative.org/component/remository/general/program-design/Detailed-Design/

[11] "Prior to the inclusion of any market-based compliance mechanism in the regulations, to the extent feasible and in furtherance of achieving the statewide greenhouse gas emissions limit, the state board shall do all of the following: (1) Consider the potential for direct, indirect, and cumulative emission impacts from these mechanisms, including localized impacts in communities that are already adversely impacted by air pollution…(3) Maximize additional environmental and economic benefits for California, as appropriate." Calif. H.S.C. § 38570.

The regulation does not expressly prevent offset developers and projects located in U.S. states outside of California (or even within California) from choosing among offset protocols offered by other linked jurisdictions; therefore, a project can select the option that offers the lowest standards. Furthermore, the WCI agreements specifically allow any WCI partner to "issue offset certificates for projects located…outside the WCI Partner Jurisdictions within North America."[12] This obviously includes U.S. states outside of California.

A WCI partner could propose a forest offset protocol with lower environmental standards than the protocol adopted by ARB, other WCI partners would be able to adopt the protocol with lower standards, and California would be forced to accept offset credits generated under those less stringent protocols. This scenario could place California in a position that violates the letter and intent of AB 32, which gives ARB the sole authority to adopt offset protocols, and specifically requires ARB to verify and enforce the quality of offsets used for compliance in California.[13] Also, even if California were to reject credits generated under less stringent protocols—in fact, even if WCI were to reject a protocol, and a protocol was acknowledged only within a single partner jurisdiction—the fungible nature of offset credits in an auction system means that those credits still would effectively become part of California's compliance market.

5. The ISOR fails to acknowledge or analyze potential environmental impacts of projects that will generate offset credits that become part of the California market.

The ISOR implies that because Quebec has not adopted a forest protocol, there is no need to analyze potential impacts to forest resulting from linking. "*The proposed amendments to the cap-and-trade regulation would not change how entities would comply as evaluated in the FED for California's cap-and-trade regulation. Therefore, implementation of the Proposed Amendments to the cap-and-trade regulation would not result in any potentially significant agricultural and forest resources impacts, as evaluated and disclosed in the FED summarized above*." ISOR at 53.

However, this ignores the possibility that Quebec may develop a forest protocol in the future, and under the regulation California would be committed to accepting offset credits from that protocol. This also ignores the fact that British Colombia, also a WCI partner, has already adopted a forest offset protocol that fails to ensure the value of the reductions and fails to protect forest environmental values.[14]

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[12] "A WCI Partner jurisdiction may issue offset certificates for projects located within its own jurisdiction as well as jurisdictions outside the WCI Partner Jurisdictions within North America. A WCI Partner jurisdiction will accept offset certificates issued by other WCI Partner jurisdictions. As described in section 9.8 of WCI's design document, WCI Partner jurisdictions may also accept offset certificates from outside North America." WCI *Offset System Essential Elements Final Recommendations Paper* S 3.2.3. Geographic limits. WCI *Offset System Essential Elements Final Recommendations Paper* S 3.2.3. Co-benefits.

[13] "The state board [ARB] shall adopt methodologies for the quantification of voluntary greenhouse gas emission reductions. The state board [ARB] shall adopt regulations to verify and enforce any voluntary greenhouse gas emission reductions that are authorized by the state board for use to comply with greenhouse gas emission limits established by the state board." Calif. H.S.C. § 38571.

[14] The "Protocol for the Creation of Forest Carbon Offsets in British Columbia, Version 1.0" was adopted by BC in November 2011. In general, the BC forest protocol lacks a requirement that in-forest carbon stocks are maintained or increase over the life of the project, allows the project baseline to be manipulated to include unintentional

Rather than analyze the potential environmental impacts of forest offset protocols issued by other jurisdiction, the ISOR largely defers to the environmental analysis in the FED for the cap-and-trade regulation. *"The environmental analysis for the proposed amendments to California's cap-and-trade regulation relies on the analysis conducted for the cap-and-trade regulation FED and the environmental analysis for the Landfill Regulations to the extent that the environmental impacts of the proposed amendments would be consistent with the impacts addressed in those prior documents*." ISOR at 44. At the same time, the ISOR does acknowledge that forest offset programs have the potential for significant adverse environmental impacts, and that linking to partner jurisdictions could increase demand in California for offset credits generated in other jurisdictions.[15]

However, the FED explicitly stated that it did not analyze the potential impacts of linking. "*No linkages are proposed at this time; however, future linkages are anticipated. Each linkage would be approved by the Board and subject to its own environmental review*." FED at 33 "*Each compliance response project implemented by a covered entity in California, offset protocol adopted by ARB, or linkage agreement approved by ARB, that constitute a "project" as defined by CEQA, section 21065, would be subject to CEQA environmental review*." FED at 130.

Furthermore, the FED, in its analysis of potential environmental impacts of forest offsets, acknowledged the need for environmental criteria. The FED also acknowledged that linking to jurisdictions with lower environmental criteria could result in discrepancies in the environmental quality of offsets. Also, the FED acknowledged the need for comprehensive environmental standards to apply to protocols in all linked jurisdictions. "*A linkage program with comprehensive environmental protection standards adopted as conditions of approval would create the opportunity to gain GHG reduction benefits while avoiding or minimizing the potential for other environmental impacts. Protocols could be established to require achievement of environmental standards, including definition of the standards, monitoring procedures, regular reporting of monitoring results to California, and adaptive environmental management for refining the standards and approaches for their achievement over time. Variations in the approvals of linkages could influence environmental impacts of allowances and offset credits created under other linked programs. A primary question related to the environmental impacts of linked programs is the degree of environmental review and protection/mitigation requirements in the other jurisdictions where linked programs would be approved. California environmental laws are typically more protective than the laws of other states and nations. If linkage was restricted to California programs only, the state's environmental laws would maintain protections through environmental impact assessment of public agency actions (under CEQA) and other laws protecting natural resources. Restricting linkage to California may have some advantages for environmental protection; however, the capacity to develop emissions credits would be substantially limited. Also, the overall cap-and-trade program includes accepting offset projects from outside California, so a geographic limitation on linkage would not result in a*

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reversals, counts benefits of storage for less than 100 years, and lacks any requirements to promote natural forest structure. http://www.env.gov.bc.ca/cas/mitigation/fcop.html

[15] [T]he Forest Protocol has the potential for significant adverse impacts to biological resources and land use." ISOR at 45. Depending on relative price and availability, linkage with Québec could incent California-covered entities to seek offset credits from projects in Québec." ISOR at 50.

substantial environmental advantage on its own. A linkage program with comprehensive environmental protection standards adopted as conditions of approval would create the opportunity to gain GHG reduction benefits while avoiding or minimizing the potential for other environmental impacts. Protocols could be established to require achievement of environmental standards, including definition of the standards, monitoring procedures, regular reporting of monitoring results to California, and adaptive environmental management for refining the standards and approaches for their achievement over time." FED at 387.

The FED offers a list of reasons it fails to provide a good-faith, reasoned analysis of the regulation's environmental impacts as required by CEQA, *see* CEQA Guidelines[16] sections 15144, 15151. None are valid.

First, the FED seeks to rely on the environmental document prepared for the overall cap-and-trade regulation. Such reliance ("tiering" in CEQA parlance) is appropriate, however, only to the extent that the specific environmental impacts associated with the linkage regulation were already identified, analyzed, and mitigated to the extent feasible in the FED for the cap-and-trade regulation. The current FED makes no real attempt to demonstrate whether, or to what extent, this is the case. Indeed, the linking regulation may have a number of impacts not identified in the prior FED simply because it anticipates acceptance of credits under protocols developed—or, in many cases, not even developed yet—by partner jurisdictions. To the extent that these protocols incent activities that may have environmental impacts, those impacts could not have been discussed in the cap-and-trade FED. Therefore, they must be disclosed and analyzed here.

Second, however, the FED claims that it need not analyze these impacts because they cannot be determined with any specificity. ISOR at 45 ("The FED relied on the agencies with local permitting authority to analyze site- or project-specific impacts because the programmatic FED could not determine with any specificity the project-level impacts . . . ."). Again, this is incorrect. ARB, must make a good-faith effort to disclose all it reasonably can about these projects. Where protocols exist, and underlying environmental standards are ascertainable, ARB must do its best to forecast the reasonably foreseeable environmental consequences of offset projects. These are not projects that would happen anyway; indeed, if any of these projects are truly additional—which the linking regulation ostensibly requires—they would not happen but for the incentives created by the linking regulation. Accordingly, the environmental consequences of these projects are, if not direct, then at least indirect effects of the regulation. Nor may the FED simply state that all projects are expected to comply with legal standards applicable in the host jurisdiction. The fact that a project may comply with legal standards alone does not relieve a lead agency of its obligation to determine whether its environmental impacts are significant. *See, e.g., Californians for Alternatives to Toxics v. Dept. of Food & Ag.* (2005) 136 Cal. App. 4th 1.

Third, the FED argues that it is a "program" document and thus lacks specificity. Again, the argument fails. Under CEQA, a program environmental document still must disclose all reasonably available information, and is most helpful if "it deals with the effects of the program as specifically and comprehensively as possible." CEQA Guidelines § 15168(c)(5). Indeed, a program document can provide "an occasion for a more exhaustive consideration of effects and

[16] All references to the "CEQA Guidelines" are to title 14 of the California Code of Regulations.

alternatives that would be practical" in analyzing individual actions. *Id.*, § 15168(b)(1). This is especially the case here, where *only* at the programmatic level can all of the incentives governing underlying project activities be disclosed and considered.[17] Rather than prepare a program-level document in accordance with these CEQA principles, ARB has largely declined to offer any meaningful analysis at all. This is improper.

Finally, ARB claims it has no authority to require mitigation. ISOR at 45 ("ARB does not have the authority to require project-level mitigation for specific projects carried out to comply with California's cap-and-trade regulation or protocols.") Again, the claim is patently false. Program-level review specifically allows agencies to "consider broad policy alternatives and programwide mitigation measures at an early time when the agency has greater flexibility to deal with basic problems or cumulative impacts." *Id.*, § 15168(b)(4). ARB cannot plausibly claim that it has no role in mitigating the environmental harm potentially caused by offset projects that would not occur absent the linking regulation. ARB is designing the regulation and has ultimate responsibility under AB 32 for adopting methodologies and protocols governing these projects. ARB therefore has both legal and practical authority to condition the acceptance of offsets in a way that minimizes minimize and avoid environmental impacts. ARB has not shown that its own mitigation measures are legally infeasible. It cannot simply abdicate its responsibility to consider feasible mitigation measures for projects *entirely* subject to its own design, authority, and control.

CEQA requires that ARB act with full knowledge of the environmental consequences of its actions. Because of the extraordinary nature of this regulation—seeking to commit California to accepting offset credits from protocols that do not yet exist—the review of environmental impacts will need to be extraordinarily conservative and circumspect. If linking to a partner jurisdiction commits California to accepting offset credits even when the offset protocols lack even the insufficient environmental safeguards of protocols adopted by ARB, it will not be possible to dismiss the effects of future offset projects in those jurisdictions as too speculative for analysis.

Thank you for considering these comments.

In conclusion, the regulation fails to ensure that carbon offsets generated in other jurisdictions will not result in negative impacts to forest ecosystems, will not undermine the integrity of California's cap-and-trade program, and will not contradict the mandate of AB 32 to maximize environmental co-benefits. The regulation should include environmentally rigorous standards and require affirmative determination by ARB that offset protocols in other jurisdictions—and in California—will not result in negative environmental impacts. We hope these comments help ARB reconsider and revise the proposed regulation. Please contact me if you have any questions.

Sincerely,

[17] Later environmental review—such as, for example, review of a timber harvesting plan associated with a forest project—may not capture the entire constellation of environmental consequences that flow from adoption of the regulations that create incentives to undertake that project.

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