

To: CARB Staff
From: Andy Katz, **Breathe California**
Tam Hunt, **Community Environmental Council**
Mike Sandler, **Climate Protection Campaign**
Shankar Prasad, **Coalition for Clean Air**
Daniel Emmett, **Energy Independence Now**
Jason Barbose, **Environment California**
Kristin Grenfell, **Natural Resources Defense Council**
Bill Magavern, **Sierra Club California**
Christopher Busch, **Union of Concerned Scientists**
Re: Cap and Trade Program Design in Draft Scoping Plan
Date: August 4, 2008

We support the Draft Plan's proposal that California will need a broad array of reduction efforts to meet its GHG reduction goals. A well-designed cap and trade program could be one important part of the state's package of policies, and could serve as a complement to other regulations by achieving emissions reductions beyond what other regulations alone would achieve (p.18). We focus our comments here on how to design an effective cap and trade program, because any cap and trade program must be well-designed in order to be an effective policy tool which we would support.

Any cap-and-trade program must meet the objectives of AB 32.

We support the Draft Plan's statement that CARB will only adopt a cap and trade program if it meets all the requirements of AB 32 (p.15). By law, the program should achieve the following objectives:¹

- Distribute allowances in an equitable manner;
- Seek to minimize costs and maximize total benefits to California;
- Encourage early action to reduce GHG emissions;
- Not disproportionately impact low-income communities;
- Provide appropriate credit for voluntary early action;
- Design the program to prevent any increase in emissions of toxic or criteria air pollutants; and
- Minimize administrative burden and leakage.

A tight cap should be set over as many sectors as practicable

A tight cap that covers as many sectors as possible will provide more certainty that California will meet AB 32's emission limit. A broad scope will also create a more stable and more liquid market, thus allowing the cap and trade program to be more effective. We agree with the CARB proposal that the cap and trade program should cover the electricity, industrial, natural gas, and transportation sectors (p.17).

¹ California Health and Safety Code §38562 (b)

Allowances should be auctioned

Allowances are valuable permits to pollute the public atmosphere, and their value should be distributed in the public interest. The simplest and fairest way to do this is to auction the allowances and use the revenue to further the purposes of AB 32. If any allowances are freely allocated, their value should be earmarked for purposes that further the goals of AB 32.

We appreciate the Draft Scoping Plan's recognition that WCI suggests that a majority of allowances should eventually be auctioned (p.18). However, this does not go nearly far enough. California should commit now to auction all allowances and use the value of allowances in the public interest from the start of the program. The staff's Proposed Scoping Plan to be released in October 2008 should demonstrate a strong commitment to auctioning, independent of WCI.

Auction revenue should be used in the public interest

Auction revenue should be used to further the goals of AB 32. We believe that CARB should create explicit guidelines for uses of auction revenue. As CARB is well aware, there must be a close nexus between the use of the fee revenue and the purposes of AB 32.² The primary purpose of AB 32 is to reduce greenhouse gas emissions,³ but the bill also describes several other goals, including maximizing environmental and economic co-benefits,⁴ complementing efforts to reduce air pollution and toxic contaminants,⁵ transforming the state's energy infrastructure,⁶ and maximizing overall societal benefits.⁷

The Draft Scoping Plan repeats ETAAC's suggested uses for auction revenues but does not lay out any guidelines or categories of its own (p.46). We believe that the Proposed Scoping Plan should specify that auction revenue should be used for the following purposes:

- Reduce costs to consumers, particularly low-income consumers, for example through investments in end-use efficiency beyond the state's existing programs, and possibly through direct payments.
- Support investments in, and deployment of, technologies and strategies to reduce GHG emissions, such as energy efficiency, renewable energy and transit, as well as RD&D of innovative technologies to reduce GHG emissions;
- Provide economic opportunities to low-income and disadvantaged communities, as well as small businesses, schools, affordable housing associations, and other community institutions;
- Support air and toxic pollution reduction efforts and enforcement programs, particularly in environmental justice communities; and
- Support development of "green collar" jobs through training and outreach.

² *Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 877-878

³ Health and Safety Code § 38501 (h)

⁴ Id. at § 38501(h)

⁵ Id. at § 38562(b)(4)

⁶ Id. at § 38501(h)

⁷ Health and Safety Code § 38562 (b)(6)

If they are allowed, offsets should be limited

We agree with the Draft Scoping Plan's statement that a limit on offsets might be necessary to prevent weakening the cap and trade program (p.19). However, the suggested limit of 10% of compliance obligations from offsets is a wholly inadequate limitation because it would mean that *all* of the reductions from a cap and trade program could be achieved through offsets.

CARB expects to set the cap at 365 MMTCO_{2e} in 2020, meaning that it will distribute 365 MMTCO_{2e} of allowances (p.17). Capped entities will need to surrender a combination of allowances and offsets equal to their emissions. If capped entities use offsets to account for 10% of their emissions, they will emit a total of 406 MMTCO_{2e} in 2020, accounting for these emissions by surrendering 365 MMTCO_{2e} of allowances (90% of their compliance obligations) and 40.6 MMTCO_{2e} of offsets credits (10% of their compliance obligations). However, CARB expects that the cap and trade program will only account for 35.2 MMTCO_{2e} of reductions in 2020 (p.11). Therefore, if capped entities purchase 40.6 MMTCO_{2e} of offsets, there will be no reductions in the capped sectors beyond what is already required by other regulations.

We believe that the vast majority of the reductions accounted for by a cap and trade program should be achieved through on-site reductions by capped entities, and that offsets should account for only a minority. We also believe that one of the main benefits of a cap and trade program is that it can push emissions even further below what is already being accomplished by other regulations. Offsets cannot be allowed to undermine this benefit. We urge staff to clarify in the Proposed Scoping Plan, to be released in October 2008, that offsets should account for no more than *10% of the reductions* to be achieved by cap and trade. Ten percent of 35.2 is 3.5 MMTCO_{2e}, or approximately *1% of total allowances* in 2020.

Program should provide benefits to communities that suffer greatest cumulative impacts of air pollution

CARB should strive to achieve air quality co-benefits from greenhouse gas emission reductions measures to provide near term public health benefits, especially in communities that have suffered the greatest cumulative impacts of air pollution. We are pleased to see that CARB has committed to conducting evaluations of public health and environmental benefits for measures under consideration in the scoping plan and to use the results of those evaluations to refine the overall program design (p.60). We concur with the EJ Advisory Committee recommendation that outside health experts should be consulted to assist with the assessment of health impacts.

CARB should also state in the Proposed Scoping Plan how it plans to accomplish the more detailed screenings that are required to determine whether each proposed regulation and market mechanism will comply with all the requirements of AB 32.⁸ CARB's plan should include a clear schedule for developing and updating analytic tools and data sets that will be needed for these analyses, acquiring outside technical expertise if needed, gathering input from stakeholders, and conducting the analyses.

⁸ These screenings are spelled out in Health and Safety Code § 38562 (b) (1-9) and 38570 (b) (1-3))

Strict standards should be met before California links with WCI

We agree that California's ultimate goal should be to be part of strict regional, national, and international efforts to reduce GHG emissions (p.15; p.C-14). However, we urge California to move forward with achieving its own reductions and to carefully judge whether to link with other programs. Before linking, California must first ensure that other programs have a comparably stringent program, including a comparably strict cap, comparable verification and reporting requirements, comparable limits on offsets, and comparable enforceability. The WCI draft released July 23, 2008 suggests that the regional cap be set at BAU levels in 2012,⁹ and does not make clear how much reduction, if any, will be required in 2015.¹⁰ California should commit to achieving reductions below business as usual from the outset, and should not link with a program that does not make a similar commitment.

Reporting must be transparent

The program should make data on emissions, allowances, trades, prices, and evaluations of compatibility with air quality and toxic reduction efforts transparent and publicly available by source and sector in a timely manner to establish a well-functioning program. In addition, we request that CARB amend the mandatory reporting requirements to require entities to submit data used to calculate emissions and supporting documentation to CARB so that it can also be made available to the public. Making emissions data available, along with the underlying documentation, and information about allowances, prices, and concurrent air and toxic pollutants will help the market function better and will build public confidence in the program.

Penalties must be meaningful

The proposal that non-complying entities would have to surrender allowances "equal" to those they over-emitted is inadequate (p.C-18). If a capped entity does not surrender sufficient allowances at the end of a compliance period, it must be required to surrender a multiple of the allowances, as well as being subject to fines, civil and criminal penalties.¹¹ The penalty should be large enough that no rational entity would choose to pollute and accept the penalty.

Multi-year compliance periods and banking, but not safety valves, should be used to contain costs

Trading of allowances, banking, and a multi-year compliance period are preferred methods to provide flexibility and lower the costs of the program. A price cap on allowances, or "safety valve", should not be included because it would break the program's cap and allow emissions to increase.

⁹ WCI "Draft Design of a Regional Cap and Trade Program" (July 23, 2008), §6.2.

¹⁰ Id. at 6.3

¹¹ California Health and Safety Code § 38580(b)(1) states that violations are subject to penalties set forth in § 4200. Section 4200 *et. seq.* states that violators are guilty of a misdemeanor and subject to fines and imprisonment.