

Economic and Allocation Advisory Committee

Allocation Report

Allocation Design Issues

Allowance Distribution Mechanism: How much auctioning vs. free allocation?

Allowance Value Provision: Who receives what portions of allowance value?

Importance of Allocation Design Issues

Allowance Distribution Mechanism: How much auctioning vs. free allocation?

- **Can significantly affect overall costs of cap and trade**

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Importance of Allocation Design Issues

Allowance Distribution Mechanism: How much auctioning vs. free allocation?

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Allowance Value Provision: Who receives what portions of allowance value?

- **Much at stake: total allowance value may be \$7-\$22 billion in 2020**
- **But note that allowance value is not same as overall cost (overall cost is much less)**

Criteria for Evaluating the Options

- Cost Effectiveness
- Fairness
- Environmental Effectiveness
- Simplicity

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These connect closely with stated objectives of AB 32. The Act stipulates that regulations should be designed in a way that ...

- Seeks to minimize costs; minimizes the administrative burden
- Designs the regulations in a manner that is equitable; ensures that compliance with the regulations does not disproportionately impact low-income communities; directs public and private investment toward the most disadvantaged communities in California
- Minimizes leakage; ensures overall social benefits, including reductions in other air pollutants

Recommendations and Justifications

Allocation Mechanism

- Rely principally on auctioning
 - Advantages:
 - transparent, reveals costs of abatement
 - can lower overall costs substantially
 - In most cases, consumers face same prices under auctioning and free allocation
 - In principle, auction proceeds can provide same compensation as free provision
 - Is free allocation needed/warranted to protect stockholders? managers? employees?
- Use free provision only as necessary to address emissions leakage
 - Specifically, use output-based free allocation to prevent cost-disadvantage with out-of-state competition (if border adjustments not feasible)

Recommendations and Justifications - 2

Allowance Value Provision

- \$7-\$22 billion involved in 2020
- Earmarked:
 - Addressing emissions leakage
 - Avoiding disproportionate impact on low-income households
 - Financing contingency fund to address any adverse local environmental impacts
- Remainder (lion's share):
 - Roughly 75% recycled to households, 25% to finance various government expenditures (R&D investments, adaptation, job-training, state&local land-use policies)

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 - Roughly 75% recycled to households, 25% to finance various government expenditures (R&D investments, adaptation, job-training, state&local land-use policies)
- *Committee did not achieve consensus on how to recycle auction revenues to households*
 - rebate checks (salience) vs. avoided taxes (lower costs)

Final Comments

Relying nearly exclusively on auctioning poses political challenges

- Urge Board to counter false claims (auctioning causes higher prices, hurts employment, involves greater aggregate costs)
- If apply free provision, do so conservatively -- avoid overcompensation