

**State of California
Environmental Protection Agency
AIR RESOURCES BOARD**

Topics Subject to Potential Regulatory Amendments

California Cap-and-Trade Regulation (2013)

April 2013

Background

The California Cap-and-Trade Regulation (Regulation) was formally adopted by the Air Resources Board (ARB or Board) in 2011. In 2012, the Board adopted a limited set of amendments focused on implementation of the Regulation. In response to Board direction and further discussions with stakeholders, staff will begin a public process to propose additional amendments for Board consideration in fall 2013. This document provides a summary of the topics that staff will consider for new amendments. Amendments to the Cap-and-Trade Regulation may also require modifications to the Mandatory Reporting Regulation (MRR) and the Fee Regulation.

Starting this spring, staff will hold workshops focused on specific topics that are the subject of potential amendments to the Regulation. Staff invites stakeholders to participate in workshops and provide comments on the development of proposed new amendments. Staff will announce workshops using the Cap-and-Trade (capandtrade) list serve. To sign up for the list serve, please visit:

http://www.arb.ca.gov/listserv/listserv_ind.php?listname=capandtrade.

All informal staff proposals and proposed regulatory amendments that may have market implications will be shared with stakeholders through a transparent and coordinated process to ensure all stakeholders receive information at the same time. As part of these activities, ARB will also continue to collaborate on program design with other jurisdictions implementing similar programs.

Tentative Schedule for 2013 Rulemaking Activities

March: New Offset Protocol Workshop

May: Universities, Legacy Contracts, and “But For” Combined Heat and Power Workshop

May: Cost Containment, Information Disclosure, and CITSS Workshop

June: Natural Gas Supplier Workshop

June: Release Draft Proposed Amendments to Regulation

July: Draft Proposed Amendments to Regulation Workshop

September: Release 45-day Proposed Draft Amendments to Regulation and New Offset Protocols

October: Board Hearing

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Topics for Potential Rulemaking in 2013:

Resource Shuffling

Per Board Resolution 12-33, the Board directed staff to continue to work with the Emissions Markets Advisory Committee (EMAC), the California Independent System Operator (CAISO), State agencies and stakeholders to provide certainty to the electricity market about how the Regulation will address resource shuffling. The Board also directed staff to further refine the definition of resource shuffling and to identify situations that ARB would not consider resource shuffling. Recommended actions were presented to the Board at the October 2012 Board meeting. Based on these recommended actions, staff developed guidance for the definition of resource shuffling, and identified “safe harbors” that ARB does not consider resource shuffling. Staff will propose clarifying amendments to the Regulation consistent with the previously recommended actions and published guidance regarding the definition of resource shuffling and the identified safe harbors, and present additions to definitions in the Regulation, as necessary.

Legacy Contracts

Per Board Resolution 12-33, the Board directed staff, in coordination with the California Public Utilities Commissions (CPUC), to develop a methodology that provides transition assistance to covered entities that have a compliance obligation cost that cannot be reasonably recovered due to a legacy contract. Staff will evaluate and propose a methodology that provides transition assistance to those with legacy contracts. Staff will also propose clarifications and additions to definitions in the Regulation, as required.

Combined Heat and Power

Per Board Resolution 12-33, the Board directed staff to work with the CPUC, the California Energy Commission (CEC), and stakeholders to develop a methodology that exempts the steam and waste heat emissions for all facilities that would not be included in the Cap-and-Trade program “but for” their investment in combined heat and power (CHP). Staff will propose a methodology and regulatory language that provides for a process to quantify emissions eligible for the exemption.

Emissions Leakage

Per Board Resolutions 12-33 and 11-32, the Board directed staff to continue to evaluate trade exposure categorization and, if necessary, modify the leakage risk determinations to be implemented prior to the allocation of allowances for the second compliance period. The Board further directed staff to complete current studies of leakage risk and evaluate options for ensuring the competitiveness of California industries. Staff will evaluate and may propose new leakage classifications for rare earth mineral extraction activities, acid battery recycling activities, and liquid hydrogen production in 2013. Additional modifications to existing leakage risk determinations based on the results of current studies under contract to ARB will be presented to the Board in a subsequent rulemaking, if necessary, prior to the allocation of allowances for the second compliance period.

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Universities

Per Board Resolution 12-33, the Board directed staff to develop a methodology to allocate allowances to California universities that recognizes early actions to reduce greenhouse gas (GHG) emissions, and invest in energy efficiency and CHP. Staff will propose a methodology for the direct allocation of allowances to California universities that are covered entities as a result of early action GHG reduction activities. Staff will also propose clarifications and additions to definitions in the Regulation, as required.

Offset Program Implementation

Staff will evaluate and clarify processes related to offset program implementation. These amendments may address project listing requirements, monitoring and reporting requirements, verification body requirements, conflict of interest requirements, compliance offset credit issuance, timing and deadlines, and roles of air quality districts. Staff may also propose changes to clarify that invalidation requirements are consistent for all project types. Staff may also propose clarifications and additions to definitions, as required.

New Offset Protocols

Staff will propose quantification methodologies for two new proposed compliance offset protocols: coal mine methane and rice cultivation practices.

Cost Containment

Per Board Resolution 12-51, staff will evaluate and propose amendments to ensure that allowance prices will not exceed the highest price tier of the Allowance Price Containment Reserve while minimizing the impact on existing allowances and maintaining the environmental integrity of the Program.

Product-Based Benchmarks

Per Board Resolution 11-32, the Board directed staff to identify and propose new benchmarks and allowance allocation for manufacturing of new products in California. Staff will propose new product benchmarks for dry gas extraction activities, rare earth mineral extraction activities, acid battery recycling activities, and for any other entities for which product data was not collected through MRR 2011 reporting but which may be eligible for free allocation. Staff will also propose new product benchmarks for the following activities currently under the energy-based methodology of allowance allocation: eight food processing sectors, foundries, metal casting, metal forging, and ethanol production. Staff will reassess and may propose modifications to the existing product-based benchmarks for the following activities: thermal and non-thermal oil and associated gas extraction, natural gas extraction, petroleum refining, hydrogen production, coke calcining, flat glass and container glass manufacturing, recycled boxboard manufacturing, and tissue product manufacturing.

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Allowance Allocation

Per Board Resolution 11-32, the Board directed staff to continue to work with stakeholders to further develop the allowance allocation approach for the petroleum refining sector in the second and third compliance period. Staff will evaluate and may propose modifications to the true-up methodology, and if necessary the allocation methodology, associated with refinery allowance allocation. Staff will evaluate the current exemption of offshore oil and gas extraction activities and propose modifications, as needed. Staff will also evaluate the option of allocation for suppliers of natural gas, which will have a compliance obligation beginning with the second compliance period.

Waste-to-Energy

Per Board Resolution 12-33, the Board directed staff to develop regulatory amendments to exempt waste-to-energy facilities from the program for the first compliance period. Staff will propose an exemption of emissions from waste-to-energy facilities, and propose modifications to require the retirement of allowances associated with the exempted emissions.

Renewable Energy Credits

Staff will evaluate and may clarify requirements for the retirement of Renewable Energy Credits (REC's) in order to ensure that REC's are not used to account for zero emissions in multiple programs. Staff will propose modifications to ensure the retirement requirements are consistently applied to both in-state and out-of-state electrical generation facilities.

Implementation of Auction and Trading Requirements

Staff will evaluate and may propose modifications related to the implementation of the auction and trading provisions within the Auction Platform and Compliance Information Tracking Services System (CITSS). Staff will also reevaluate and may propose modifications to the current schedule for auctions and reserve sales.

Compliance Instrument Tracking System Service and Information Disclosure

Staff will evaluate and may propose modifications to the existing information disclosure requirements to ensure rigorous oversight of the market program and of actions taken in the tracking system. Staff may propose additional information disclosure requirements to help ARB monitor relationships between consultants and market participants.

Market Rules

Staff will evaluate and may propose modifications, as needed to aid implementation, to the existing information requirements related to CITSS instrument transfers. These requirements may be used to monitor the market and provide public reports for program transparency. Staff will also evaluate any need to modify the current auction purchase limits.