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June 22, 2009

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Kevin Kennedy, Chief
Program Evaluation Branch
Office of Climate Change
California Air Resources Board
1001 J Street
Sacramento, CA 95814

Subject: WSPA Comments on AB 32: Reviewing and Approving Offset Projects and Protocols in a Cap and Trade Program

Dear Mr. Kennedy,

The Western States Petroleum Association (WSPA) is a non-profit trade association representing twenty-eight companies that explore for, produce, refine, transport and market petroleum, petroleum products, natural gas and other energy supplies in California and five other western states.

WSPA member companies own and operate facilities that include oil and natural gas production properties, refineries, marketing terminals, pipelines and retail gasoline outlets. The companies produce fuels and other products that will all be impacted by the implementation of AB 32.

As we have previously indicated, it is critically important that the California Air Resources Board (ARB) clearly describe how the AB 32 program will interact with future programs. This includes federal and other programs such as international carbon markets, other regional efforts or state programs.

WSPA also reiterates our belief that a market-based mechanism, such as a cap and trade program, provides the dual benefits of environmental action and cost-effectiveness to achieve the emission reduction goals of AB 32.

We are submitting the following comments in response to your solicitation for stakeholder input at the May 21 Public Meeting on AB 32: Reviewing and Approving Offset Projects and Protocols in a Cap and Trade Program.

Need for a Robust Offset Program

WSPA continues to believe that a robust offset program is essential to ensuring that AB 32 is implemented in a cost-effective manner. Cost-effective implementation will buttress ARB's objective of ensuring that California's program is credible outside of the state.

Development of a quality offset generation program is integral to the success of a cap and trade market. ARB must ensure that necessary offsets are available when the cap and trade program begins in 2012.

ARB must also balance the timely availability of the offsets with regulatory requirements under the cap and trade regulation, such as a compliance timeline, to ensure the cap and trade program as a whole is feasible.

Recommendation ó ARB should evaluate the variables that affect the availability of offsets by investigating the offset market within existing cap and trade programs.

ARB must consider offset availability based on the elements of the offset program that California develops, as part of an integrated cap and trade program to ensure that the cap and trade program is feasible and cost effective. Without considering the whole program, the offset program could contribute to economic leakage

Development of a linked offsets program

Compatible and cost-effective approaches to GHG emission reductions will encourage innovation and also provide the impetus for early reductions needed to meet California's short-term goals. Cost effective reductions, as well as innovation, can provide an ancillary benefit of keeping jobs within the State.

According to economic studies by both the US EPA¹ and Charles Rivers Associates, offsets that are compatible globally will dampen the overall compliance costs and save up to 80% of the costs to the participants and to the California economy. Use of offsets will ensure the cost-effective reduction of GHG emissions in California and around the globe, thereby greatly reducing the risks of leakage and other adverse impacts.

An open and robust offsets program linked globally with other programs appears to be the ARB's single largest cost containment opportunity under AB 32

Beyond the cost effectiveness benefits of a linked offsets program, the limited time interval between the start of the cap and trade program and the full development of the ARB cap and trade regulations² necessitates that the AB 32 program seamlessly link with other GHG programs. To accomplish this task, ARB must recognize quality offsets and other GHG credits developed through existing regional and international GHG reduction programs. This action will maximize the availability of offsets and the feasibility of the cap and trade program .

Recommendation ó ARB should recognize the global scope of the GHG emissions issue and the potential benefits of reduction of GHG emissions anywhere in the world. Hence, approvals of offsets and protocols must not be California-centric. Instead, they must be usable nationally and

¹ <http://www.epa.gov/climatechange/economics/pdfs/WaxmanMarkeyExecutiveSummary.pdf>

² e.g., *offset regulations and the implementation of the offset protocols, certification organization, trading organization and the actual offset projects*

internationally. Development of a State-only program would burden California with unnecessary costs, trigger development of duplicative protocols, and create an unnecessary and costly bureaucracy to manage the State's efforts.

California should avoid the temptation to develop state-specific project methodologies and seek instead, to harmonize with other existing international and domestic programs. This will allow developers to leverage experience with protocols/methodologies across jurisdictions. It will also allow ARB to use its scarce resources on more critical aspects of the cap and trade program.

ARB should develop a matrix of other key GHG reduction program offset and credit programs with the criteria that they used to generate the offsets. This matrix should be used to review and analyze programs for compliance with AB32 requirements. We believe this will dramatically improve transparency and understanding for stakeholders.

It is critical that a list of recognized programs, whose offsets, credits and protocols are recognized as valid and useable for AB32 compliance purposes, be published well before offsets are needed in 2012.

WSPA is supportive of a system that:

- i) is established or recognized by federal, State or tribal law or regulation, or founded on recognized standards, or any offsets program, or parts thereof, that has proven to be compatible with the programs that meet specified criteria;
- ii) is developed through a peer review or public consultation process or has developed offset project-type standards, methodologies and protocols through a peer review or public consultation process;
- iii) uses publicly published standards, methodologies and protocols that require credited emission reductions or sequestration programs that are real, permanent, additional, verifiable and enforceable;
- iv) requires all emission reductions or sequestration be verified by a state regulatory agency or an accredited third-party independent verification body; and,
- v) requires that all credits issued are authorized for use by ARB and registered in a publicly accessible registry, with individual serial numbers assigned for each ton of carbon dioxide equivalent emission reductions or sequestration.

Enforcement of Offsets

Once offsets are determined to be valid and useable for AB 32 compliance purposes, users of these "certified" offsets and credits must not be liable for enforcement actions in the event the generator of the offset later fails to comply with applicable requirements. Without certainty of the validity of the credits, the risks will compromise the usefulness of the offsets and thwart the offset market.

"Certifying" the offset credits as valid and useable for AB 32 compliance purpose does not mean ARB approves each offset credit. We believe a hybrid process can be developed that includes specific ARB approval for offsets from unique California generated offsets and ARB recognition of 1) California generated offsets using ARB approved protocols and 2) credits established by other regional or international credits generated by programs recognized by ARB.

Recommendation ó ARB must öcertifyö or otherwise indicate that the offset credits are valid and useable for AB 32 compliance purposes. Users of these öcertifiedö offsets and credits must not be subject to enforcement actions in the event the generator of the offset later fails to comply with applicable requirements.

No limitations on Offsets

It seems clear that a robust offset program with unlimited offsets³ is the most cost-effective approach to a functional cap and trade program for GHG emissions. Cap and trade programs without geographic or quantity restrictions allow market participants to trade with the greatest flexibility so that costs are minimized.

Placing limits on use of offsets may also delay or defer participation by offset providers and can result in reducing the ability of the cap and trade program to achieve mandated reductions at the least cost. In previous letters, we highlighted a number of studies showing that limiting offsets can lead to significant adverse cost impacts to California business and consumers. (See comments filed May 27.)

Recommendation ó ARB should not limit offsets in early stages of market development ó either quantitatively or geographically ó because such an action will reduce innovation, decrease allocation trading and therefore, delay appropriate carbon cost setting.

ARB should re-evaluate the current interpretation of the stated limit on the use of offsets based on the 49% of required reductions. Aside from WSPA's previously-stated concern with any quantitative limit placed on the use of offsets, as well as a concern around limits based on a percentage of required reductions, staff's current interpretation of this limit severely and unreasonably further restricts the use of offsets.

As required under the Scoping Plan Adoption Resolution, ARB should conduct an economic impact analysis on the Agency's proposal limiting the use of offsets. This study should be initiated as soon as possible and be completed before any quantitative limits for offsets are determined. Completing the study consistent with this schedule will enable ARB to receive the most up to date information on the issue.

Clarity in Requirements

Implicit in the listing of some key program elements above, is a provision that ARB publishes a list of protocols to be developed. The protocol should specify a process where project sponsors can petition for inclusion of their technology as a candidate offset measure as well as an appeals process should the petition or certification of offsets be denied.

Recommendation ó Protocol methodology development should be prioritized in the following order: i) existing protocols authorized by other regions; ii) projects/project types that have the potential to generate significant quantities of offsets and, iii) projects/project types that promote commercialization of innovative technologies.

Terminology that is used in the State program should be consistent with prevalent terminology. For example, the word öregistrationö is typically synonymous with ARB's use of the word öcertification.ö

³ *No limitations quantitatively or geographically*

Thank you for considering our comments. We look forward to continuing working with you and ARB staff to ensure the success of this challenging endeavor.

If there are any questions, please contact me at this office or Mike Wang of my staff at (626) 590-4905.

Regards,

A handwritten signature in blue ink that reads "Cathy A. Boyd". The signature is fluid and cursive, with the first name "Cathy" being the most prominent.

cc: Mike Schieble, ARB
Lucille Van Ommering, ARB
Mike Wang, WSPA