

State of California
AIR RESOURCES BOARD

**Notice of Public Availability of Cap-and-Trade
Discussion Draft and Workshop**

ARB staff is holding a public workshop to discuss draft changes to the greenhouse gas cap-and-trade and mandatory greenhouse gas reporting regulations.

DATE: Friday, July 15, 2011

TIME: 9 am to 3 pm

LOCATION: Byron Sher Auditorium, 2nd Floor, Cal/EPA HQ Building,
1001 "I" Street, Sacramento

WEBCAST: <http://www.calepa.ca.gov/broadcast/?BDO=1>

During the workshop, stakeholders may email questions to ccworkshops@arb.ca.gov. A discussion draft including proposed changes to the cap-and-trade regulation is now available for download on the program webpage at:

<http://www.arb.ca.gov/cc/capandtrade/capandtrade.htm>

Special Accommodations or Language Assistance:

If you require a special accommodation or need these documents in an alternate format or language, please contact the Office of Climate Change at (916) 322-2037 as soon as possible. TTY/TDD/Speech to Speech users may dial 711 for the California Relay Service.

Background

At its December 16, 2010 public hearing, the Air Resources Board (ARB or Board) endorsed the proposed finalization of sections 95800 to 96022, title 17, California Code of Regulations (CCR), which comprise the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanism Regulation, including Compliance Offset Protocols.

At the hearing, the Board considered the California cap-and-trade program Initial Statement of Reasons Staff Report released on October 28, 2010, and adopted Resolution 10-42 directing several modifications proposed by staff. The Board did not endorse the regulations as written and advised staff that additional changes were necessary. Resolution 10-42 and other regulatory documents for this rulemaking action are available online at the cap-and-trade program website referenced above.

Some revisions in this notice reflect clarifications to better align California's cap-and-trade program with rulemaking efforts in other Western Climate Initiative (WCI) jurisdictions to allow for future linkage to support a broader, regional cap-and-trade program. A broader program will provide more cost containment benefits to California-covered entities and ensure greater reductions in regional emissions of greenhouse gases (GHGs) to the atmosphere.

The discussion draft of the cap-and-trade regulation is being released alongside a discussion draft of the Mandatory Greenhouse Gas Reporting Regulation (Subchapter 10, Article 2, sections 95100-95199, title 17, California Code of Regulations), which provides the emissions data that are the basis for determining both inclusion in the cap-and-trade program and a covered entity's compliance obligation. Proposed revisions to the Mandatory Reporting Regulation have been harmonized with both the federal greenhouse gas reporting requirements and these proposed revisions to the cap-and-trade regulation.

In accordance with Government Code section 11346.8, in Resolution 10-42 the Board directed the Executive Officer to take final action to adopt the proposed regulations, with the modifications identified in the Resolution and other such conforming modifications as may be appropriate, after making the modified language and any additional supporting documents available to the public for a comment period of at least 15 days. The Board also directed the Executive Officer to consider such written comments as may be submitted during this period and to make such modifications as may be appropriate in light of the comments received. ARB expects to release for public comment revisions to the regulation before the end of July 2011 pursuant to Government Code section 11346.8. This discussion draft will be the basis for those revisions and the subject of the July 15, 2011 workshop. As part of finalizing the regulation staff will be finalizing the associated environmental document and developing additional details about the adaptive management component of the cap-and-trade program. Staff is seeking comment on this component. The finalized regulation must be filed with the California Office of Administrative Law (OAL) by October 28, 2011. Please note that while comments are appreciated and can be submitted to this workshop, this workshop is not part of the formal rulemaking process pursuant to the Administrative Procedure Act (APA). ARB will release changes pursuant to the APA for 15 days as required by Government Code section 11346.8(c) separately from this notice. In order for comments on the proposed changes to be included in the rulemaking file, comments must be submitted again once the 15-day notice is published.

Summary of Proposed Modifications

The following sections detail the changes from the October 28, 2010 proposal that are included in the discussion draft. Appended to this notice are documents describing in greater detail the electrical distribution utility (Appendix A) and industrial producer (Appendix B) allocation analysis and methodologies.

Staff has modified the regulation in many places to reflect a proposal to begin the compliance obligation in 2013, while conducting two auctions in 2012. As written, many sections in the regulation refer to the beginning of the compliance obligation or of compliance periods when describing the requirements for market participants. In this draft discussion document, the allocation, auction, trading, and other activities will begin in 2012 before the start of the compliance obligation and the first compliance period. Staff acknowledges that some additional modifications will need to be made prior to finalizing the proposal. Staff is requesting comment on which program elements should begin in 2012 and what advantages there are to phasing in various components during 2012.

Staff is also investigating ways to ensure that large industrial sources subject to the recently finalized Energy Efficiency and Co-Benefits Audit regulation be required to take all cost-effective actions identified under those audits. We are seeking stakeholder input on how to implement this policy.

The staff's proposed modifications in this discussion draft to the originally proposed regulations are summarized below and are set forth in detail in Attachment 1 to this notice. All references to sections 95800, 95801, 95802, 95810, 95811, 95812, 95813, 95814, 95820, 95821, 95830, 95831, 95832, 95840, 95841, 95850, 95851, 95852, 95852.1, 95852.2, 95852.3, 95853, 95854, 95855, 95856, 95857, 95870, 95890, 95891, 95892, 95893, 95910, 95911, 95912, 95913, 95914, 95915, 95920, 95921, 95922, 95940, 95941, 95942, 95943, 95970, 95971, 95972, 95973, 95974, 95975, 95976, 95977, 95978, 95979, 95980, 95981, 95982, 95983, 95984, 95985, 95986, 95987, 95988, 95990, 95991, 95992, 95993, 95994, 95995, 95996, 95997, 95998, 96010, 96011, 96012, 96013, 96020, 96021, and 96022 are to title 17, CCR. The following summary does not include modifications to correct typographical or grammatical errors, changes in numbering or formatting; nor does it include all of the non-substantive revisions made to improve clarity. For a complete account of all modifications in the proposed regulations, please refer to the underline and strikeout sections in the discussion draft.

A. Modifications section 95801. Purpose.

No modifications made to this section.

B. Modifications to section 95802. Definitions.

A number of definitions were added or modified. Many of the new or modified definitions are necessary to implement the "first deliverer" approach for the electricity sector as well as to implement the benchmarking approach for distribution of allowances for several different sectors. Definitions were also added or modified to improve clarity and to ensure that the terms used in the cap-and-trade regulation are consistent with those used in the Mandatory Reporting of Greenhouse Gas Emissions Regulation (MRR). Adding these definitions was required to ensure that all terms contained in the regulation have the same meaning to the regulated public.

Section 95802 was modified to include a definition for “carbon dioxide supplier,” “geologic sequestration,” and “process unit” to reflect changes to sections 95812(c) and 95852.

C. Modifications to section 95810. Covered Gases.

No modifications made to section 95810.

D. Modifications to section 95811. Covered Entities.

Section 95811 specifies which entities are covered by the rule. One modification was made to section 95811(g) which specifies that suppliers of carbon dioxide (CO₂) will be referred to as carbon dioxide suppliers for purposes of the rule. This change was made to simplify the regulation such that only one term would be used for carbon dioxide suppliers instead of multiple terms (e.g., suppliers of carbon dioxide, suppliers of CO₂, carbon dioxide suppliers, CO₂ suppliers), thus making it easier to search for this supplier category within the regulation.

E. Modifications to section 95812. Inclusion Thresholds for Covered Entities.

Section 95812(a) was modified to specify that reported and verified annual emissions must be reported and verified pursuant to the verification sections of the MRR. This modification is necessary to be consistent with the MRR, and to clarify that a covered entity’s annual emissions must both be reported and verified.

Section 95812(b) was modified to specify that an entity will be classified as a covered entity if the reported or reported and verified annual emissions in any data year from 2008 to 2011 exceed the thresholds identified in sections 95812(c) and (d), and to remove the term ‘aggregated.’ This modification is necessary to be consistent with the MRR.

Section 95812(c)(2) was modified to clarify the existing applicability thresholds for covered entities.

Section 95812(c)(3) was modified to replace the original section 95812(c) and specify that the inclusion threshold for carbon dioxide suppliers is based on the amount of CO₂ captured from production process units and production wells, and supplied for commercial application or geologic sequestration. This change was required to ensure that all CO₂ created and potentially emitted in California by carbon dioxide suppliers would be covered, and to align with the federal greenhouse gas reporting regulation.

A new section 95812(c)(4) was inserted to be consistent with how MRR categorizes these sources for reporting purposes.

Section 95812(d) was modified to include assigned emissions levels consistent with MRR. This section is necessary so covered entities that do not receive a positive verification are still included in the regulation.

Section 95812(d)(2) was modified to be consistent with section 95812(c)(2).

Various other minor and non-substantive clarifications were also made to section 95812.

F. Modifications to section 95813. Opt-In Covered Entities.

Minor and non-substantive clarifications were made to section 95813 to better organize the section and otherwise clarify who can be an opt-in covered entity.

G. Modifications to section 95814. Voluntarily Associated Entities and Other Registered Participants.

New section 95814(a)(3) creates a new type of voluntarily associated entity (VAE) that will take only temporary control of compliance instruments when it provides clearing services for transactions. Defining this new VAE allows ARB to specify a new type of account that can only be used by that type of entity, which ARB can then conditionally exempt from the holding limit. This section specifically adds derivatives clearing organizations registered with the U.S. Commodity Futures Trading Commission as eligible. Staff is requesting comment on whether the new VAE category captures the types of clearing entities expected to be active in carbon markets.

Section 95814(b)(1)(D) was modified to specify that entities approved as Early Action Offset Programs, pursuant to subarticle 14, do not qualify to hold compliance instruments, but may qualify as a Registered Participant. This modification was necessary to ensure consistency between Offset Project Registries and Early Action Offset Programs, as, in many cases, they may be the same entities.

H. Modifications to section 95820. Compliance Instruments Issued by the Air Resources Board.

Minor and non-substantive clarifications were made to section 95820 to correct cross references within the regulation.

I. Modifications to section 95821. Compliance Instruments Issued by Approved Programs.

Minor and non-substantive clarifications were made to section 95821 to add consistent terminology and correct cross references within the regulation.

J. Modifications to section 95830. Registration with ARB.

Section 95830(b) was modified to delete references to linking to external programs approved by ARB. This text was deleted because any additional registration requirements will be addressed in subarticle 12 at the time the regulation is modified to include linkage.

New section 95830(c)(1)(F) exempts entities registering to provide clearing services from having to meet the information disclosure requirements of 95830(c)(1)(D) for compliance instruments it holds for the purposes of clearing transactions. This provision was added to avoid burdening entities providing clearing services with the burden of reporting information on transactions that ARB will be getting directly from the entities involved in a transaction.

New section 95830(f) adds the requirement that registered entities must update their registration information within ten days of a change in that information. The section allows ARB to revoke, suspend, or restrict an entity's registration or impose penalties if an entity fails to update its registration information. This section is necessary because ARB will rely on registration information to conduct market oversight and enforce rules on holding and purchase limits. These efforts will be undermined if entities are not required to update the information.

New section 95830(g) adds provisions concerning the confidentiality of the information gathered through registration. Section 95830(f)(1) identifies beneficial holdings disclosures and information on the identity of real persons as information that should be treated as confidential. Section 95830(f)(2) allows for other registration information to be made public. ARB is proposing these conditions to balance the need for market transparency with the protection of information on individuals.

K. Modifications to section 95831. Account Types.

New section 95831(a)(4)(B) was added to allow a publically owned utility to transfer allowances from their holding account to the compliance account of joint powers agency of which the publically owned utility is a member. Adding this provision alleviates the concern that some small publically owned utilities raised about being required to consign allowances when a joint powers agency purchases electricity on behalf of the publically owned utility.

New section 95831(a)(5) creates a new type of holding account, called an Exchange Clearing Holding Account, for entities supplying exchange clearing services. Entities transfer instruments to clearing entities on a temporary basis while a transaction is being cleared. The clearing entity then transfers the instruments to the designated account of the entity receiving the allowances as part of the transaction being cleared. Creating this account will allow ARB to exempt an entity clearing transactions from the holding limit.

Original section 95831(b) was moved to new section 95921(f), because the text deals with account restrictions that may be imposed for rule violations while subarticle 11 deals with the conduct of trading.

Original section 95831(c)(5), now section 95831(b)(5), was modified to clarify how the Forest Buffer Account functions and when ARB may place ARB offset credits into the Retirement Holding Account from the Forest Buffer Account. These changes were made for clarification purposes and to align these requirements with the updated requirements in section 95983.

New section 95831(b)(6) creates a holding account under the control of the Executive Officer called the Voluntary Renewable Electricity Reserve Account. This provision is needed to implement section 95870(c). The Executive Officer will place allowances into the account, which may then be retired as part of the voluntary renewable energy set-aside. The account will be closed when the allocation of allowances is depleted.

Various other minor and non-substantive clarifications were made to section 95831 to add and correct cross references within the regulation.

L. Modifications to section 95832. Designation of Authorized Account Representative.

Sections 95832(a)(4), 95832(a)(6), and 95832(d) were modified to specify that an authorized account representative and any alternative account representative must attest to the validity of their application for an account with the accounts administrator under penalty of perjury and under the laws of the State of California. This addition is necessary to ensure that all information submitted is true and complete under penalty of perjury.

Various minor and non-substantive clarifications were also made to section 95832 to correct cross references within the regulation and fix numbering.

M. New section 95833. Disclosure of Direct and Indirect Associations.

New section 95833 is composed generally of modified text that originally appeared as sections 95914(a) through (d). In addition to moving these sections, staff made two changes to the original text. The section requires all registered entities to identify if they share specific types of relationships with other registered entities. This information is needed to monitor for suspicious activity in the market program and ensure market rules are not circumvented.

New section 95833(a)(2) was modified from original text to clarify an existing requirement that an entity holding compliance instruments on behalf of another entity in a beneficial holding relationship is considered to have a direct corporate association with the other entity. New section 95833(a)(4) was added on the advice of counsel to exempt from the corporate association requirements any

entities already subject to state or federal rules which prohibit the sharing of market information between entities that have a formal corporate affiliation.

New sections 95833(d)(1) through (4) were moved from section 95914. No substantial changes were made to this text.

N. New section 95834. Disclosure of Beneficial Holding.

New section 95834 provides detailed provisions for an existing requirement that any entity holding compliance instruments on behalf of another entity disclose the relationship to ARB. New section 95834(a)(1) defines when a beneficial holding relationship exists. It also defines an agent as the entity holding allowances owned by a second entity, which is defined as the principal.

New section 95834 (a)(2) creates a type of beneficial holding relationship for electric distribution utilities which may need to hold compliance instruments on behalf of entities with whom they have long term electricity delivery contracts which may not explicitly determine which party to the contract has the responsibility to surrender compliance instruments. ARB has held extensive discussions with electric utilities on this issue, and is requesting comment on whether the proposed requirements address this concern.

Section 95834(a)(3) allows entities which have disclosed a corporate association pursuant to section 95833 to utilize the beneficial holding arrangements.

Section 95834(b) contains requirements for the disclosure of beneficial holding relationships. Section 95834(c) contains requirements applying to an entity which may serve as an agent for more than one principal. The requirements are intended to prevent the disclosure of market information between market participants, to prevent opportunities for collusion.

O. Modifications to section 95840. Compliance Instruments.

Section 95840(a) was modified to exclude 2012 from the first compliance period and accommodate the new compliance obligation start date of January 1, 2013.

P. Modifications to section 95841. Allowance Budgets Calendar Years 2012-2020.

Section 95841 was modified to remove the allowance budget for 2012 to accommodate the new compliance obligation start date of January 1, 2013.

Q. New section 95841.1. Voluntary Renewable Electricity.

New section 95841.1 was added to clarify the treatment of voluntary renewable electricity, reflecting the intended changes identified in Resolution 10-42 and in Attachment B of the Resolution. Staff worked with stakeholders to clarify the role of voluntary renewable electricity in reducing GHG emissions after the cap-and-

trade program is in place, in order to support increased voluntary investment in renewable resources. Voluntary renewable electricity refers to renewable electricity that, unlike renewable electricity used for the Renewable Portfolio Standard, is not the subject of a mandate. Once the cap is set, voluntary renewable electricity can only reduce GHG emissions if it is tied to a reduction in the total amount of allowances. New section 95831(b)(6) explains that a Voluntary Renewable Electricity Reserve Account will be set up to hold allowances that may be retired to account for voluntary renewable electricity. This section explains what is required to demonstrate that Renewable Energy Credits (RECs) or renewable electricity is eligible to count toward the retirement of allowances from this account.

New section 95841.1(a) explains the reporting requirements for voluntary renewable electricity, including a required attestation that the operator of a renewable generator or a marketer of RECs claiming credit under the cap-and-trade regulation is not also claiming credit for the same renewable electricity in any other program. This section also describes the reporting required to demonstrate the claimant's ownership of the renewable electricity or RECs.

New section 95841.1(b) explains the requirement for either retirement of RECs or attestation pursuant to section 95841.1(a)(1) in order for renewable electricity to be counted toward retirement of allowances. New section 95841.1(c) requires that RECs for voluntary renewable electricity must be associated with electricity that is delivered directly to the California electricity grid, and that the claimant must report the same information required of first deliverers or facilities pursuant to MRR. New section 95841.1(d) requires that the generator of voluntary renewable electricity be registered as eligible for the RPS with the California Energy Commission to ensure that it meets the same standards required for the RPS.

New sections 95841.1(e) and (f) describe what must be included in an application to retire allowances from the Voluntary Renewable Electricity Reserve, and how the amount of allowances to be retired is calculated. New section 95841.1(g) provides that a generator or REC marketer will fulfill the attestation requirements of section 95841.1(a)(1) if it participates in a tracking system that will be developed by ARB, once the tracking system is approved by the Executive Officer.

R. Modifications to section 95850. General Requirements.

New section 95850(b) was added to specify that a covered entity's compliance obligation is based on their verified emissions, rounded to the nearest whole ton, or their assigned emissions pursuant to MRR. This modification is necessary to clarify that an entity's compliance obligation will be based on their verified emissions rounded to the nearest whole ton in the case that an entity reports their emissions in decimal form.

Section 95850(c) was changed from requiring a 10-year data retention period to a 7-year period to be consistent with the WCI essential reporting requirements. Stakeholders also commented that a 10-year period is too long, given how much reporting data they must hold on to.

New section 95850(c)(4) requires that covered entities retain their detailed verification reports as required pursuant to MRR for at least 7 years. This was included to require that a covered entity retain all records associated with reporting and compliance obligations.

Various minor and non-substantive clarifications were made to section 95850 to ensure consistent terminology within the regulation.

S. Modifications to section 95851. Phase-In of Compliance Obligation for Covered Entities.

Various minor and non-substantive clarifications were made to section 95851.

T. Modifications to section 95852. Emission Categories Used to Calculate Compliance Obligations.

Section 95852(a) was divided into subsections and modified to specify that a covered entity has a compliance obligation for assigned emissions. This modification was made to specify that if ARB has assigned emissions for the sources subject to a compliance obligation, then the facility will have a compliance obligation equal to the value of every metric ton of CO₂e assigned emissions. New section 95852(a)(2) was included to specify that beginning in 2015, combustion emissions resulting from burning specific fuels are not included when calculating an entity's compliance obligation. This modification was made to specify that the compliance obligation for these specified fuels is at the supplier level in 2015. This is the case only for stationary combustion and not suppliers.

Section 95852(b) was modified to specify how the compliance obligation is calculated for electricity marketers and retailers that import electricity and for natural gas suppliers – who will subtract out the fuel supplied to entities subject to the cap (e.g., electricity generators) and whose obligation is based on the end user's combustion of the fuel. This modification was necessary to clarify the reference to the applicability section, and to explain that electricity deliveries are subject to the new provision prohibiting resource shuffling. In addition, the reference to thresholds is added to clarify that first deliverers incur compliance obligations only if they exceed the applicable threshold.

New section 95852(b)(1) was added to prohibit resource shuffling and minimize the potential for leakage. Leakage occurs if a first deliverer switches what resources are deemed to serve California to claim a lower compliance obligation, while total actual emissions within the interconnected western electricity grid are not reduced. New sections 95852(b)(1)(A) and (b)(1)(B) are the attestations that

first deliverers must sign and deliver to ARB to certify that their deliveries do not include any resource shuffling. These sections works in conjunction with the newly added definition of resource shuffling in section 95802.

New section 95852(b)(2) clarifies that, in order to make a specified delivery claim, a first deliverer must report pursuant to MRR, including reporting the facility's assigned identification number, and that first deliverers must have ownership rights with a clear link to the source of the electricity delivered. This section was added to clarify what is required for a first deliverer to claim a facility specific emission factor for an electricity delivery.

New section 95852(b)(3), in conjunction with a new definition for replacement electricity in section 95802, sets out requirements for claiming the emission factor of a variable renewable resource (wind, solar, or run-of-the-river hydroelectric) for "substitute" electricity that is delivered in place of the real-time generation. This provision was added to address utility concerns about the treatment of renewable electricity, and to strike a balance between recognizing the value of variable renewable electricity and limiting the possibility for double counting of emission reductions in cases where electricity from a variable renewable resource cannot be directly delivered to California.

New section 95852(b)(4) requires "direct delivery", newly defined in section 95802, for electricity with a facility specific emission factor lower than the default emission factor. This section is needed to ensure that claims for electricity from a specific facility are for electricity that is actually delivered to serve California load, and is not used to serve load outside of California. This requirement is among those needed to prevent resource shuffling and leakage.

New section 95852(b)(5) requires that electricity generated from biomethane, in order to receive a zero emission factor, must meet reporting requirements pursuant to MRR. This is added to ensure that claims for electricity from biomethane are supported by the reporting of all data necessary to demonstrate that the electricity is not subject to a compliance obligation.

In conjunction with a new definition of qualified exports, new section 95852(b)(6) allows a credit against a first deliverer's compliance option based on emissions from electricity that is exported at the same time that the first deliverer is importing electricity. This provision addresses stakeholder concerns regarding "simultaneous exchanges" and recognizes that this kind of exchange is similar to the wheeling of electricity through California, in that not all of the electricity being imported is actually used to serve California load.

New sections 95852(c)(1) through (c)(4) were included to specify that suppliers of natural gas must report emissions delivered to all end users in California. ARB will then calculate the metric tons CO₂e of GHG emissions for natural gas delivered to covered entities. The emissions will comprise the CO₂e emissions that received a positive or qualified positive emissions data verification statement

or the assigned emissions from natural gas delivered to the covered entity by the supplier of natural gas. These sections were added to clarify how the compliance obligation will be determined for suppliers of natural gas.

New section 95852(c)(3) specifies that ARB will provide the supplier of natural gas a listing of all customers and aggregate natural gas volumes and emissions calculated from the supplier's natural gas delivered to covered entities. Following the verification deadline, the supplier of natural gas will be notified of their compliance obligation. This section is needed to clarify that ARB will provide suppliers of natural gas with the data used to determine their compliance obligation.

Section 95852(d) was modified to specify that suppliers of petroleum products have a compliance obligation for every metric ton CO₂e of GHG emissions that would result from full combustion or oxidation of the quantities of the following fuels that are removed from the rack in California, sold to entities not licensed by the California Board of Equalization as a fuel supplier or imported into California except for products for which a final destination outside California can be demonstrated. This modification is necessary to specify that the obligation is not only for imports into or deliveries into California.

Section 95852(g) was modified to specify that carbon dioxide suppliers have a compliance obligation only for CO₂ produced in-state and either (1) supplied for in-state utilization, or (2) exported out-of-state for geologic sequestration. The compliance obligation for in-state supply of carbon dioxide was added because it was mistakenly omitted in the regulation. CO₂ supplied for geologic sequestration can only be exempt from a compliance obligation if it is verified to be geologically sequestered through use of a Board-approved quantification methodology. Imports from carbon dioxide suppliers were excluded because CO₂ imports are relatively small and those imports would need free allocations to ensure similar treatment as in-state production of supplied CO₂. Instead of providing free allocation of allowances for a relatively small amount of CO₂, ARB chose to monitor imports; if CO₂ imports increase, ARB will re-assess its treatment of imported CO₂. Exports were, for the most part, excluded from a compliance obligation because the potential emission of CO₂ would occur out of state. An exception is made for CO₂ exported for purposes of geologic sequestration (i.e., this CO₂ *will* have a compliance obligation) because ARB does not want to incentivize out-of-state geologic sequestration without rigorous assurance that the CO₂ will remain underground.

Original section 95852(h) was deleted and moved to new section 95852(i) to incorporate the correct numbering structure and put it at the end of section 95852.

New section 95852(h) was added to specify emissions categories used to calculate compliance obligations for oil and gas producers. The operator is the operating entity listed on the state well drilling permit, or the state operating

permit for wells where no drilling permit is issued by the state, who operates onshore petroleum and natural gas production wells and controls by means of ownership (including leased and rented) and operation (including contracted) stationary and portable equipment located on all well pads within a single hydrocarbon basin as defined by the American Association of Petroleum Geologists (AAPG) three-digit Geological Province Code (published 1991) holds a compliance obligation. This addition was necessary to be consistent with MRR for purposes of entities that report and hold a compliance obligation.

U. Modifications to section 95852.1. Compliance Obligations for Biomass-Derived Fuels.

Section 95852.1 was modified to specify that emissions from biomass-derived fuels must be reported and verified pursuant to the MRR. Source categories that are not listed under section 95852.2 or that have not received a qualified positive or positive verification statement must be reported as other biomass CO₂. This modification is necessary because emissions that cannot be verified pursuant to section 95131(i) of MRR are not considered biomass derived and will hold a compliance obligation.

V. New section 95852.1.1. Eligibility Requirements for Biomass-Derived Fuels.

New section 95852.1.1(a) was added to require emissions from biomass-derived fuels to be verified based on requirements in section 95131(i) of the MRR. The verification body is subject to specified requirements under this section when verifying biomass-derived fuel that is not subject to a compliance obligation. These requirements were originally found in MRR section 95131(i)(1)(A); however, staff have moved them into this section in the cap-and-trade regulation so that all provisions defining a compliance obligation are in one regulation.

New section 95852.1.1(a)(1) specifies that the contract shuffling date for purchasing any biomass-derived fuel must be in effect prior to January 1, 2012 and remain in effect or have been renegotiated with the same California operator within one year of contract expiration. This section is necessary to prevent contract shuffling through which contracts are being diverted to California by entities seeking to avoid a compliance obligation for fossil fuels. Contract shuffling could allow fossil emissions to increase in states where the biofuel was previously combusted, resulting in a potential no net change in emissions and emissions leakage. The January 1, 2012 date was changed from the original date in the MRR of January 1, 2010 in response to stakeholder comments that staff need to allow time for contracts to go through the California Energy Commission (CEC) process for RPS certification.

New sections 95852.1.1(a)(1)(A) and (B) were added to provide the requirements that biofuel has to meet once there is a signed contract in place. These sections

are necessary to clarify how new and increased production for purposes of contract shuffling will be treated.

New section 95852.1.1(a)(2) was added to specify that fuel provided under any contracts after January 1, 2012 must be for additional biomass-derived capacity and not for increases in other biomass that would have a compliance obligation. This section is necessary to prevent increased production of other biomass.

New section 95852.1.1(a)(3) was added to specify that the biomass fuel must meet the requirements in sections 95852.1.1(a)(1) and (a)(2) and a verifier must be able to track the fuel back to a previous contract. This section is necessary to track where the fuel is coming from and to prevent double counting of the fuel in case it is under another contract.

New section 95852.1.1(a)(4) specifies that once a certification program is in place, a fuel which meets the requirements of sections 95852.1.1(a)(1) and 95852.1.1(a)(2) will always be considered to have met the requirements in section 95852.1.

New section 95852.1.1(a)(5) specifies that if the biogas or biomethane is used at the site of production, and not transferred to another operator thus not requiring a contract, then the operator must demonstrate that the fuel has been used or combusted in California prior to January 1, 2012. This section is necessary to make sure that the fuel was not previously used to produce useful energy transfer.

Section 95852.1.1(b) specifies that as part of a biomass-derived fuel's eligibility to avoid a compliance obligation no party may sell, trade, give away, claim or otherwise dispose of any of the carbon credits, carbon benefits, carbon emissions reductions, carbon offsets or allowances, howsoever entitled, attributed to the fuel production that would prevent the resulting combustion from not having a compliance obligation. This section was necessary to specify that Generation of Renewable Energy Credits is allowable and will not prevent a biomass-derived fuel that meets the requirements in this section from being exempt from a compliance obligation.

W. Modifications to section 95852.2. Emissions without a Compliance Obligation.

Sections 95852.2(a) was modified to further clarify which types of waste sources do not have a compliance obligation. This is merely a clarification and does not exclude any sources that would have been included in the original regulation. Also in this section, staff deleted text that would not allow biogas from digesters to be exempt from a compliance obligation. This change was made based on staff's recommendation endorsed by the Board under Attachment B of draft Resolution 10-42.

New section 95852.2(b) was modified to specify that emissions from geothermal generating units and geothermal facilities do not hold a compliance obligation. Stakeholders submitted comment letters stating that emissions from geothermal facilities should not be classified as fugitive or process emissions, and should therefore not have a compliance obligation. Based on stakeholder comments, staff concluded that although geothermal facilities must report, they will not hold a compliance obligation. ARB will monitor their activities via the CEC renewable programs.

Sections 95852.2(c) through (r) were included to align with the WCI Reporting Committee's revised list of "reporting only" emissions sources. This updates the sources listed in the Final Essential Requirements for Mandatory Reporting. Emissions data from these source types will be submitted for information only, and will not be subject to a compliance obligation.

Section 95852.2(s) excludes emissions from facilities that directly combust municipal solid waste to energy in an existing permitted facility. This provision was added because including emissions from these facilities in cap-and-trade would cause statewide GHG emissions to increase as a result of diversion of waste to landfills. This exclusion is based on staff's analysis of the potential economic impacts created by a cap-and-trade program and the potential increase in methane emissions resulting from diversion of waste to landfills even after the implementation of early action measures. Staff also believes this provision is consistent with recognition of one facility as Renewable Portfolio Standard eligible and with similar provisions in the European Union Emissions Trading System (EU-ETS) and the Regional Greenhouse Gas Initiative (RGGI) where these facilities have no compliance obligations.

Various minor and non-substantive clarifications were also made to section 95852.2 to include the correct hierarchy in the numbering structure and consistency with the terminology used in the MRR for these sources.

X. Deletion of section 95852.3. Effect of Status of Verification Statement on Calculation of Compliance Obligations.

This section was removed from the regulation because it is duplicative of language that exists in MRR section 95103.

Y. Modifications to section 95853. Calculation of Covered Entity's Triennial Compliance Obligation.

Sections 95853(a), (b), (c), and (d) were modified to clarify that an entity's compliance obligation is calculated as the total of the emissions that received a positive or qualified positive emissions data verification statement, or were assigned by the Executive Officer. When a reporting entity that holds a compliance obligation under the cap-and-trade regulation fails to submit an emissions data report or fails to obtain a positive or qualified positive emissions

data verification statement by the applicable deadline, the Executive Officer will develop an assigned emissions level for the reporting entity as specified in section 95131(c)(5)(A) through (C) of the MRR.

Z. Modifications to section 95854. Quantitative Usage Limit On Designated Compliance Instruments—Including Offset Credits.

New section 95854(a) was originally expressed as part of the “O” term in the equation in this section and was moved into its own section to make it more clear which compliance instruments are subject to the quantitative use limit. This original text was also modified to include a reference to ARB offset credits (section 95820(b)), which was inadvertently omitted from the original regulatory text.

The text in what is now section 95854(b) now references section 95854(a), which clarifies which compliance instruments are subject to the quantitative usage limit so that it is made clearer. This text, as well as the modified text in the O_o and S terms of the equation, establishes that the quantitative usage limit applies to the triennial compliance obligation and not the annual compliance obligation. This modification was made in response to stakeholder comments. Staff agrees with stakeholders, who have indicated that applying the limit to each annual surrender is overly complicated and there is no benefit to the program applying it annually.

Section 95854(c) was added to clarify that sector based offset credits may only be used for up to 25 percent of the 8 percent total limit on designated compliance instruments, increasing to one half of the 8 percent in the second compliance period. This reflects the intended changes identified for this section in Attachment B of Resolution 10-42.

AA. Modifications to section 95855. Annual Compliance Obligation.

Section 95855 was modified to be consistent with section 95853 and MRR.

BB. Modifications to section 95856. Timely Surrender of Compliance Instruments by a Covered Entity.

Section 95856(a) and (d) were modified to provide additional time for an entity to meet its annual surrender obligation. Changing the date to November 1, provides consistency between the annual surrender and triennial surrender. The extended deadline will also allow allocations to be distributed for the following year based on verified data.

Minor and non-substantive clarifications were also made to section 95856 to add consistent terminology and correct cross references within the regulation.

CC. Modifications to section 95857. Untimely Surrender of Compliance Instruments by a Covered Entity.

Section 95857(b)(4) was modified to provide a covered entity time to acquire compliance instruments from an auction or reserve before being required to provide ARB the number of compliance instruments assessed for an untimely surrender. This change is necessary because several commenters were concerned that the originally proposed regulation did not allow enough time to acquire excess compliance instruments and the immediacy of the surrender would create an unstable market. By extending the untimely surrender obligation to be due after an auction and a reserve sale, ARB expands an entity's ability to comply with the excess emissions surrender obligation without resorting to the secondary market.

Section 95857(c) was rewritten to outline the consequence of not meeting the untimely surrender obligation: subsection (c)(1) indicates that ARB will determine the number of violations, (c)(2) indicates the entity will have a new untimely surrender obligation that includes the original untimely surrender obligation which has not been satisfied. This new obligation is due immediately. These changes are necessary because a new time frame is created by the changes to 95857(b)(4), and additional rules regarding the calculation of the obligation is necessary in the event of a partial surrender. This section is necessary to inform all regulated parties of the consequences of missing the untimely surrender obligation deadline.

Minor and non-substantive clarifications were also made to section 95857 to add consistent terminology and correct cross references within the regulation.

DD. New Section 95858. Compliance Obligation for Under-Reporting in a Previous Compliance Period.

New section 95858 was added to address cases when the Executive Officer finds there had been under-reporting by an entity after they submitted compliance instruments to meet their compliance obligation. These provisions are necessary so entities with a compliance obligation know what action the Executive Officer would take in the event they are found to have under-reported their emissions.

New section 95858(a) provides that entities that are found to have under-reported their emissions by less than five percent must not take any further action to replace the deficient compliance instruments. This corresponds with the requirements for reporting.

New section 95858(b) provides that entities that are found to have under-reported their emissions by more than five percent must turn in compliance instruments in the amount calculated pursuant the formula in this section. This amount equals for the difference in what was initially reported and verified and what is determined by the Executive Officer. Requiring entities that under-report emissions by more than would be allowed under the reporting requirements to make up these emissions ensures the environmental integrity of the program.

New section 95858(c) was added to provide entities that must turn in compliance instruments for under-reported emissions a six month period to submit them to ARB. Staff included a six month period to give covered entities enough time to acquire sufficient compliance instruments and avoid any short-term shocks to the market. This section also specifies which compliance instruments may be used to meet this requirement and provides that if the entity turns in all of the compliance instruments within the six month period they are not subject to the excess emissions obligation under section 95857. They are not subject to excess emissions because if they turn them in within the six months ARB considers the submittal to be a timely surrender.

EE. Modifications to section 95870. Disposition of Allowances.

Section 95870(a) was modified to change the date of creation of the Allowance Price Containment Reserve to July 18, 2012. Section 95870(b) was modified to change the date at which the Executive Officer would transfer future vintage allowances to the Auction Holding Account. Both changes are necessary to reflect the change in dates of the first auction and reserve sales.

Section 95870(b) was modified to increase the amount of future vintage allowances auctioned each year from 2% to 10% of future allowance budgets. This change is required to respond to stakeholder concerns about preparing for the second compliance period when there is an increase in the size of the program due to the addition of the transportation fuels and upstream natural gas sectors. The increase in the advance auction will allow covered entities to accumulate allowances for the second compliance period while diminishing the need for banking allowances from the first compliance period, which might otherwise tighten the market in the first compliance period more than is optimal.

New section 95870(c) was added to include new language as directed in Resolution 10-42 to specify how many allowances will be set aside for Voluntary Renewable Electricity reductions.

The number of allowances available for allocation to electrical distribution utilities was increased. Appendix A explains how this value was derived.

Additionally, Table 8-1 has been updated to clarify the relationship between activities that produce products at risk for leakage and the sectors in which these activities occur.

FF. Modifications to section 95890. General Provisions for Direct Allocations.

Section 95890 was modified to improve clarity on how verification impacts eligibility for free allocation.

GG. Modifications to section 95891. Allocation for Industry Assistance.

Section 95891(b) was modified to change the timing of output data to respond to stakeholder concerns about prolonged exposure to recessionary output levels. A “true-up” term was added to the equation to ensure that the amount of allocation received for a given year is corrected to actual production for that year. The assistance factor (determined by leakage risk) and the cap decline factor were clarified to be a function of activity rather than of sector.

The product benchmarks for industrial activities, as presented in Table 9-1 of section 95891(b), were added per Resolution 10-42, to allow allowances to be allocated under the product-based approach. The product outputs used to establish the product benchmarks were altered from the proposal outlined in staff’s Initial Statement of Reasons (ISOR) as necessary. For a description of the benchmark development see Appendix B.

The name of the “thermal energy based allocation calculation methodology” in section 95891(c) was renamed the “energy based allocation calculation methodology” to more explicitly recognize the impact of electrical energy carbon costs and cost recovery. A new term was derived from a heat rate based on the pending Public Utilities Commission Qualified Facility settlement to quantify the expected carbon cost recovery in the price of power sold from an industrial facility. Equivalent adjustments were made when establishing the values of the product-based benchmarks (see Appendix B). The formula was also altered to show how any combined heat and power facilities allocated to under this approach will receive allowances. In section 95891(c)(1) text was added to explain that under the energy based approach the baseline annual amount of California GHG Allowances directly allocated to each eligible entity will be representative of current activity but provide appropriate credit for early voluntary reductions in greenhouse gas emissions. The descriptions of data sources that ARB will use to allocate under this methodology were clarified and it was explained that, if necessary, the Executive Officer will solicit additional data to allocate under the energy based approach.

The cap decline factor table (Table 9-2), in section 95981(c), was altered slightly to show that this factor impacts the allocation to electrical distribution utilities, as well as to industrial facilities, and to remove the year 2012 to accommodate the change in compliance obligation start date.

In addition to the industrial sectors identified in regulation for industry assistance to trade exposed sectors, additional sectors have also requested direct allocation of all or a portion of their allowances. Staff have reviewed the requests from these stakeholders and determined that some of these sectors are not at risk of emissions leakage, and therefore, do not qualify to receive assistance based on the risk for leakage due to the cap-and-trade program.

HH. Modifications to section 95892. Allocation to Electrical Distribution Utilities for Protection of Electricity Ratepayers.

This section was modified to show how many allowances each electrical distribution utility will receive as a portion of the total electricity sector allocation created in section 95870. This allocation to each utility is presented in Table 9-3 of section 95892(a). Appendix A explains how these values were derived.

Additionally, section 95892(a) was added to include the specific allocation of allowances to individual electrical distribution utilities.

Section 95892 was modified to delete the existing requirement that electrical distribution utilities offer all allowances in their limited use holding accounts to auction within the year they were received. New section 95892 requires that one sixth of all 2013 vintage allowances in limited use holding accounts must be consigned to auction in each of the two auctions scheduled for 2012. Section 95892(c)(2) recreates the existing consignment requirement for auctions taking place in calendar years after 2012. The changes were needed to accommodate the decision to have two auctions of vintage 2013 allowances take place in 2012 before the beginning of the first compliance period.

The Department of Water Resources, the Metropolitan Water District and the State Water Contractors have requested direct allocation of allowances to cover their emissions obligation and the potential cost burden of purchasing electricity to convey water from the State Water Project and the Colorado River Aqueduct. Staff has reviewed these requests and does not recommend direct allocation to the water utilities consistent with the October 2010 proposal. Since the allowance allocation provided to electrical distribution utilities as described in Appendix A includes allowances associated with electricity used to convey water, staff believes that the electrical distribution utilities are the appropriate conduit for the return of allowance value associated with electricity generation to ratepayers.

As detailed in footnote 22 of the Initial Statement of Reasons for the cap-and-trade regulation, some generators and industrial steam producers have reported that some existing contracts do not include provisions that would allow full pass-through of cap-and-trade costs. Staff is evaluating this issue to determine whether some specific contracts may require special treatment on a case-by-case basis. In several cases, staff is aware and encouraged that parties are in the process of or already have negotiated new contracts to resolve this issue. Staff believes that bilateral contract negotiations would provide the best resolution of this issue. Should contract renegotiation not be possible in all cases, staff will continue discussions with counter-parties to consider how this issue should be resolved in the regulation.

II. Modifications to section 95893. Reserved for Allocation to Natural Gas Distribution Utilities for Protection of Natural Gas Ratepayers.

No modifications made to section 95893.

JJ. Modifications to section 95910. Auction of California GHG Allowances.

Section 95910(a) was modified to match the new schedule of auctions and reserve sales. This was necessary to accommodate covered entities' verification deadlines in MRR and the decision to have two auctions in 2012 and four in 2013 onwards.

Section 95910(c)(1) modifies an existing provision that one fourth of allowances allocated for auction each year by ARB will be sold at each auction to reflect the decision to begin such auctions in 2013.

Section 95910(c)(2) was modified to have the existing requirements for advance auction begin in 2013 not 2012. For 2012, one half of the 2015 vintage allowances allocated to the advance auction will be sold at each of the two auctions taking place in 2012.

Section 95910(d)(4) was modified to reflect the change in the auction schedule. The existing text requires that allowances must be consigned to the auction at least 75 days prior to the auction in order for the number of allowances auctioned to be included in the auction notice. For the two auctions in 2012, the consignments need occur only 10 days before the auction because the number of allowances to be consigned is set in regulation and will be known in time to be included in the auction notice.

KK. Modifications to section 95911. Format for Auction of California GHG Allowances.

Section 95911(b)(3) was modified to provide a corrected reference and to clarify that when there are insufficient bids to sell all consigned allowances, the administrator will sell an equal proportion of the consigned allowances from each source.

Section 95911(b)(4)(A) was added to clarify that unsold, non-consigned allowances at auction will be allocated equally to the three tiers of the allowance price containment reserve. Any allowances remaining after this division will be deposited in the lowest price tier. Section 95911(b)(4)(B) was added to clarify that unsold future vintage allowances will be returned to the Auction Holding Account for sale at the next auction.

Section 95911(b)(6) modifies the effective dates of the reserve price and the reserve price escalator to reflect the new schedule for auctions.

Section 95911(c)(1) removes a reference to provisions on disclosable bidding associations. ARB removed the existing provisions for disclosable bidding associations after changes to corporate associations and beneficial holding rules rendered the bidding association provisions unnecessary.

Section 95911(c) is reorganized for clarity. In addition, the section clarifies that the original text does not apply to the advance auction. Rather, the purchase limit for the advance auction will be 25 percent. A higher purchase limit was chosen for the advance auction because staff concluded that there is a lower risk of market manipulation at the advance auction compared with the current vintage auction, due to the lower proportion of each year's allowance budget sold at the advance auction and the fact that future vintage allowances cannot be used for current compliance.

LL. Modifications to section 95912. Auction Administration and Registration.

Section 95912 was modified to allow the Executive Officer to designate a financial services administrator to execute the financial transactions required for the implementation of the market program. Clarifications were also made regarding the confidentiality of auction related data. These changes were necessary because it is highly probable the Executive Officer will contract for these services.

Various other minor and non-substantive clarifications were also made to section 95912. Text on the protection of confidential information (section 95912(d)) and provision of false information (section 95912(e)) was moved to sections 95914(d) and (c), respectively, along with other provisions regarding auction participation and prohibited behavior because it was more contextually appropriate..

MM. Modifications to section 95913. Sale of Allowances from the Allowance Price Containment Reserve.

Section 95913 was modified to provide clarification on the sale of allowances from the allowance price containment reserve.

Section 95913(a) was modified to clarify that a financial services administrator will conduct the financial transactions for sales from the Allowance Price Containment Reserve Account. This is necessary to make clear that ARB will not actually be conducting financial transactions and they will occur only through a third party.

Section 95913(c) was modified to clarify that only covered entities, as defined in the regulation, that are registered shall be eligible to purchase allowances from the Allowance Price Containment Reserve Account. This clarification and limitation is necessary because the purpose of the Allowance Price Containment Reserve Account is to protect covered entities from the possibility of allowances being unavailable. If all registered participants were able to purchase from the Allowance Price Containment Reserve Account, the policy of ensuring allowances are available would be substantially undermined.

Staff made two changes to accommodate the change in start date for the compliance obligation in the cap-and-trade program. In section 95913(c)(3)(A)

the date of the first reserve sale was changed from 2012 to 2013. In section 95913(d) staff changed the effective dates for setting the prices in each tier, as well as the price escalation mechanism, to reflect the new compliance obligation start date.

At the suggestion of stakeholders, section 95913(f)(3) was modified to implement a new process for determining the number of allowances purchased from the Allowance Price Containment Reserve. This change was made in response to stakeholder comments that the original bid process in original section 95913(e)(1) was unnecessarily cumbersome and together with the tie-breaking procedure in section 95913(f)(4) could result in bidders paying too much for or not getting the allowances they need. Some stakeholders recommended that ARB replace bidding on specific tiers of the reserve with a process in which bidders specify a quantity and a maximum price, and the bids are filled with the lowest priced allowances available. Staff agreed with the comments and is proposing this change. ARB requests comment on whether this process represents a simplification and reduces uncertainty.

Section 95913(e)(2) was modified to include the role of a financial services administrator in the processing of the bid guarantee.

Various other minor and non-substantive clarifications were also made to section 95913.

NN. Modifications to section 95914. Disclosure of Direct and Indirect Corporate Associations.

Section 95914 was renamed Auction Participation and Limitations and modified to move text regarding disclosable corporate associations to new section 95833 in subarticle 5. Text regarding the application of corporate associations to the holding limit was moved to section 95920. Text was also added to clarify how the corporate and bidding association rules are applied to the purchase limit at auction. Text relating to provision of false information and protection of confidential information was moved from section 95912. These changes were necessary to place the language in the appropriate context within the regulation.

OO. Deletion of section 95915. Identifying Disclosable Bidding Associations.

Section 95915 has been deleted. The expanded requirements on corporate associations in new section 95833 and beneficial holdings in new section 95834 have made the existing requirements on disclosable bidding associations unnecessary. Parts of section 95915(e) were moved to section 95914.

PP. Modifications to section 95920. Trading.

Section 95920(a) on general prohibitions on trading was moved to section 95921. Text on the holding limit (originally in section 95920(b)) was significantly rewritten

for clarity, and several new subsections added. New section 95921(a) changes the reference to the definition of corporate association to new section 95833.

New section 95921(b) adds new provisions that the holding limit does not apply to allowances contained in a limited use holding account. In addition, allowances held by a clearing entity will be counted against the holdings of the entity to whose account the instruments will be transferred when the transaction has been cleared. The section adds a requirement that if a transaction is discovered to violate the holding limit after the transaction has been discovered, then the transaction may be reversed and a penalty applied.

New section 95920(c) was added to clarify that the holding limit will be applied separately to allowances which can be used for current compliance and to allowances from future vintages which cannot be used for current compliance.

New section 95920(d)(1) contains the existing holding limit formula to be applied to allowances which can be used for current compliance. New section 95920(d)(2) contains an extensive clarification of the calculation of the existing limited exemption from the holding limit in section 95920(d)(1). Stakeholders had commented that the language did not convey that the exemption was cumulative through the compliance period nor was it clear how the exemption would be calculated based on emissions reports.

New section 95920(e) contains a formula for calculating the holding limit for future vintage allowances which cannot be used for current compliance. The formula is similar to the one in section 95920(d)(1), except that the “base” parameter was multiplied by three and the formula is calculated using the entire compliance period budget rather than a single budget year.

QQ. Modifications to section 95921. Conduct of Trade.

Section 95921(a) was rewritten to address the handling of violations that are detected before the transaction is registered as well as those that are detected after the transaction is registered. Specifically, the section now addresses the consequences of violating the requirements of subarticle 11 at two possible times: if the violation is discovered before the transaction is recorded (section 95921(a)(1)(A)) and if the violation is discovered after the transaction is recorded (section 95921(a)(1)(B)). These clarifications were necessary to inform covered entities and participants in the cap-and-trade program of the consequences of violating the various restrictions in subarticle 11. New section 95921(a)(3) was added to clarify that the account numbers to be used in transactions between registered entities are those of holding accounts.

A new section 95921(b)(3) was added to make explicit that violations of subarticle 11 also subject participants in the cap-and-trade program to penalties pursuant to section 96013. This addition is necessary to make explicit the scope of the penalties available to ARB in the event of a violation of the restrictions of

subarticle 11, and to make clear that the specific actions of sections 95921(a)(1) and (a)(2) are not exclusive.

RR. Modifications to section 95922. Banking, Expiration, and Voluntary Retirement.

No modifications were made to section 95922.

SS. Modifications to section 95940. General Requirements.

No modifications were made to section 95940.

TT. Modifications to section 95941. Procedures for Approval of External GHG ETS.

No modifications were made to section 95941.

UU. Modifications to section 95942. Approval of Compliance Instruments from External GHG ETS.

No modifications were made to section 95942.

VV. Modifications to section 95943. Reserved for Linkage.

No modifications were made to section 95943.

WW. Modifications to section 95970. General Requirements for ARB Offset Credits.

Section 95970 was modified to distinguish between an ARB offset credit and a registry offset credit and establish the requirements that each must meet. These clarifications were necessary because the originally proposed language could have been interpreted to mean that any offset credit could be used in the cap-and-trade program without limiting them to ARB issued offset credits.

Various minor and non-substantive clarifications were also made to section 95970.

XX. Modifications to section 95971. Procedures for Approval of Compliance Offset Protocols.

No modifications were made to section 95971.

YY. Modifications to section 95972. Requirements for Compliance Offset Protocols.

Section 95972 was modified to require that all Compliance Offset Protocols must specify the geographic location where they are applicable. This requirement clarifies that compliance offset protocols can only be applicable in North America.

This change was necessary because stakeholders were confused about the possible location of the offset projects for which ARB would issue ARB offset credits.

Section 95972 was also modified to require that Compliance Offset Protocols include standardized methods. As discussed in the ISOR, this ensures a consistent implementation of all offset projects within a project type.

ZZ. Modifications to section 95973. Requirements for Offset Projects Using ARB Compliance Offset Protocols.

Section 95973 was modified to address stakeholder comments by clarifying the eligibility criteria for offset projects. The text was also modified to address requirements that unintentionally would prohibit early action offset projects from being able to transition to Compliance Offset Protocols based on the offset project commencement date. A new section 95973(c) now makes it clear that early action offset projects may have commencement dates prior to December 31, 2006, which is consistent with the requirements in section 95990.

Section 95973(d) was added to clarify that offset projects developed on lands related to federally-recognized Indian tribes are eligible only if the Offset Project Operator or Authorized Project Designee demonstrates the existence of a limited waiver of sovereign immunity between the Tribe and ARB, entered into pursuant to section 95975 of this article. This modification also clarifies the categories of lands to which this requirement applies. This new provision is needed to ensure Offset Project Operators or Authorized Project Designees meet the requirements for listing in section 95975.

Various minor and non-substantive clarifications and updates were also made to section 95973.

AAA. Modifications to section 95974. Authorized Project Designee.

Section 95974 was modified to clarify when an Offset Project Operator may identify an Authorized Project Designee in response to stakeholder comments and correct and add several cross references within the regulation.

BBB. Modifications to section 95975. Listing of Offset Projects Using ARB Compliance Offset Protocols.

Section 95975(a)(3) was deleted and moved to section 95975(b) to place the language in the appropriate context within section 95975.

Language was added to section 95975(c)(2) to specify that all Offset Project Operators or Authorized Project Designees specifically submit to California's jurisdiction to resolve any disputes regarding enforcement of the regulation against the Offset Project Operator or Authorized Project Designee. This change is necessary to make clear to Offset Project Operators or Authorized Project

Designees that by participating in California's cap-and-trade program in this capacity, they will be subject to California's jurisdiction regardless of the physical location of the offset project.

New section 95975(c)(3) was added to include additional attestations that must be made when an offset project is listed. Original section 95975(c)(4) was deleted and moved to section 95975(d) to place the language in the appropriate context within section 95975.

New section 95975(c)(5) requires that an Offset Project Operator or Authorized Project Designee disclose any offset credits issued for the same project for any other purposes in any other program. This is to address stakeholder concerns regarding any double counting of the GHG reductions or GHG removal enhancements in multiple programs.

New section 95975(l) was added to clarify that a Tribe, in addition to meeting the other offset project listing requirements, must also enter into a limited waiver of sovereign immunity with ARB related to the Tribe's participation in the cap-and-trade program prior to the listing of any offset project being developed on lands related to the Tribe as specified in section 95973(d). This ensures ARB's ability to pursue judicial remedies, if necessary, regarding these offset projects when enforcing the requirements of the Compliance Offset Protocols and the cap-and-trade regulation.

Various minor and non-substantive clarifications were also made to section 95975 to ensure consistency in terminology and references throughout the regulation.

CCC. Modifications to section 95976. Monitoring, Reporting, and Record Retention Requirements for Offset Projects.

Section 95976(d) was modified to address stakeholder concerns about a calendar year reporting period with a fixed annual "verification period." The new requirements cover a reporting period that is not tied to the calendar year to address these stakeholder concerns.

The record retention requirements in section 95976(e)(2) were changed to 15 years following the issuance of ARB offset credits due to stakeholder concerns about an unnecessarily long record retention requirement for forestry projects.

Various minor and non-substantive clarifications were also made to section 95976.

DDD. Modifications to section 95977. Verification of GHG Emission Reductions or GHG Removal Enhancements from Offset Projects.

Section 95977(e) was moved to a new section 95977.1 in response to stakeholder comments that the references in original section 95977 throughout the regulation were very lengthy and hard to follow. Additional modifications were made to the timing for the schedule for verification (sections 95977(b) and (c)) and the submittal of Offset Verification Statements (section 95977(d)) to be consistent with the new offset reporting schedule in section 95976(d) and clarify the verification cycle.

Various minor and non-substantive clarifications were also made to section 95977 to ensure consistency in terminology throughout the regulation.

EEE. New section 95977.1. Requirements for Offset Verification Services.

New section 95977.1 was added in response to stakeholder comments that the references in original section 95977 throughout the regulation were very lengthy and hard to follow.

Original section 95977(e)(1), now new section 95977.1(a), dealing with rotation of verification bodies was modified to make it clear that the rotation of verification bodies must occur on an offset project basis. The intent of the language was not changed. These clarifications were made in response to stakeholder comments that it was unclear if the rotation of verification bodies every six years applied at the individual offset project level or Offset Project Operator level.

Original section 95977(e)(2)(C)(iv), now new section 95977.1(b)(3)(D), dealing with site visits for offset projects was modified to allow site visits to be conducted at least once every six years for those forest offset projects approved for less intensive verification. These changes were made in response to stakeholder comments that annual site-visit verifications for forest projects are cost-prohibitive and unnecessary. Staff agrees that as long as on-site verification is conducted at least once every six years there is reasonable assurance.

A new requirement was added to original section 95977(e)(2)(C)(iv)(a.), now new section 95977.1(b)(3)(D)(1.), that requires the offset verification team to review the listing information submitted by the Offset Project Operator or Authorized Project Designee. This requirement is needed to ensure the offset verification team is satisfied that all of the correct documentation was submitted by the Offset Project Operator or Authorized Project Designee.

Original section 95977(e)(2)(C)(xvii), now new section 95977.1(b)(3)(Q), was modified to change the term “errors” to “discrepancies” in the formula for calculating offset material misstatement. This change was necessary because the definition of offset material misstatement uses the term “errors” twice with two different meanings and the terminology for the calculation of offset material misstatement in this provision needs to be consistent with the revised definition.

Original section 95977(e)(2)(C)(xviii)(d)(i), now new section 95977.1(b)(3)(R)(4.)(a.), was modified to require that a verification body must submit verification reports to Offset Project Registries with the Offset Verification Statement. This provision is necessary to ensure that the Offset Project Registries possess all pertinent information regarding the offset project.

Original section 95977(e)(2)(C)(xviii)(d)(iii), now new section 95977.1(b)(3)(R)(4.)(c.), was modified to disallow the use of Qualified Positive Offset Verification Statements for certain project types, if specified in the Compliance Offset Protocol. The revisions to Compliance Offset Protocol U.S. Forest Projects disallows the use of Qualified Positive Offset Verification Statements because for forest projects ARB must ensure all protocol requirements are met, including sustainable harvesting requirements.

Original sections 95977(e)(2)(C)(xix)(a.) through (c.) were modified and/or deleted and replaced with new sections 95977.1(b)(3)(R)(5.) through (7.). These changes reflect the deletion of Offset Project Registries from the appeals process for Adverse Verification statements. This was clarified to be consistent with the MRR and reflects stakeholder comments that the appeals process should only be limited to determinations made by the Executive Officer of ARB and that ARB should be the only one to make these determinations.

Various minor and non-substantive clarifications were also made to original section 95977(e) that are now part of section 95977.1. These include general clarifications to ensure consistency of terminology and correct section references within the regulation.

FFF. New section 95977.2. Additional Project Specific Requirements for Offset Verification Services

New section 95977.2 was added to replace original section 95977(f) in response to stakeholder comments that the references in original section 95977 throughout the regulation were very lengthy and hard to follow. No substantive changes were made to the actual text.

GGG. Modifications to section 95978. Offset Verifier and Verification Body Accreditation.

Various minor and non-substantive changes were made to section 95978 for consistency in terminology within the regulation.

HHH. Modifications to section 95979. Conflict of Interest Requirements for Verification Bodies for Verification of Offset Project Data Reports.

Section 95979 was modified to include new Board directed text in Resolution 10-42 that clarifies the conflict of interest requirements as they pertain to air districts. Changes were also made to include personal or family relationships as a medium

for potential for conflict of interest to strengthen the conflict of interest requirements between verifiers and Offset Project Operators and Authorized Project Designees. This is also consistent with the MRR.

Various minor and non-substantive clarifications were also made to section 95979 for consistency in terminology within the regulation.

III. Modifications to section 95980. Issuance of Registry Offset Credits.

The process for issuance of registry offset credits and ARB offset credits was clarified by revising sections 95980 and 95981 and adding new section 95980.1 and 95981.1. Sections 95980 and 95980.1 apply specifically to the issuance of registry offset credits; sections 95981 and 95981.1 apply specifically to the issuance of ARB offset credits.

Section 95980 was modified to apply only to the issuance registry offset credits issued by an Offset Project Registry. Registry offset credits are not allowed to be used for compliance in the program, because only compliance instruments issued by ARB or an approved program for linkage may be used for compliance.

Various minor and non-substantive clarifications were also made to section 95980 to ensure consistency of terminology and correct section references within the regulation.

JJJ. New section 95980.1. Process for Issuance of Registry Offset Credits.

New section 95980.1 was added to clarify the process by which a registry would issue registry offset credits. The processes for issuing both registry and ARB offset credits were originally in section 95981. This new section and new section 95981.1 were added to establish the difference between the processes for issuing a registry offset credit and an ARB offset credit and provide clarity.

KKK. Modifications to section 95981. Issuance of ARB Offset Credits

Section 95981 was modified to apply only to the issuance of ARB offset credits. ARB offset credits can only be issued by ARB because they are able to be used for compliance. The issuance of both ARB and registry offset credits were originally in section 95980. This modified section and modified section 95980 clarify the difference between the issuance of ARB and registry offset credits. In addition, new attestations that must be made by Offset Project Operators and Authorized Project Designees were added to the process for issuing ARB offset credits (new section 95981(c)). This will help to ensure all the requirements of the program are met before ARB offset credits are issued.

LLL. New section 95981.1. Process for Issuance of ARB Offset Credits.

New section 95981.1 was added to clarify the process by which ARB would issue ARB offset credits. The processes for issuing both registry and ARB offset credits were originally in section 95981. This new section and new section 95980.1 were added to establish the difference between the processes for issuing a registry offset credit and an ARB offset credit and provide clarity.

MMM. Modifications to section 95982. Registration of ARB Offset Credits.

Section 95982 was modified to include minor and non-substantive clarifications and consistency in terminology.

NNN. Modifications to section 95983. Forestry Offset Reversals

Section 95983(a) was modified to delete text that was duplicative of text in section 95983(a)(3). Text in section 95983(a)(3) was revised for clarity purposes without changing the intent.

The timing for Offset Project Operators or Authorized Project Designees to notify ARB of an intentional reversal was changed in section 95983(b) from six months to 30 days. Staff believes since the notification is based on the discovery of the reversal as opposed to its occurrence that 30 days is sufficient for notification. Section 95983(b)(1)(A) was moved to section 95983(b) and section 95983(b)(1)(B) was moved to section 95983(b)(1) to provide clarity without changing the intent of the original text. Section 95983(b)(2) was modified to clarify how ARB offset credits are retired from the Forest Buffer Account in the event of an unintentional reversal and removes an inaccurate citation.

Sections 95983(c)(1) and original section 95983(c)(2) were modified and/or deleted to clarify the process for notifying ARB of an intentional reversal. ARB will not notify the Offset Project Operator or Authorized Project Designee of its determination because the occurrence of an intentional reversal is required to be verified in new section 95983(c)(2) within one year of the occurrence of an intentional reversal. This verification will determine if there is an intentional reversal.

New section 95983(c)(3) replaces original section 95985(e) which requires that Offset Project Operators or Authorized Project Designees replace ARB offset credits with valid compliance instruments in the case of an intentional reversal. The original replacement timing was 30 days and staff changed it to 90 days to give entities enough time to acquire allowances at auction, or purchase additional ARB offset credits in the market. A new requirement was added to section 95983(c) that says ARB offset credits will be retired from the Forest Buffer Account if the reversed tons are not replaced by the Offset Project Operators or Authorized Project Designees within the 90 days. This ensures that the system

is made whole and that the environmental integrity of the program is intact. If the Offset Project Operator or Authorized Project Designee does not replace the ARB offsets within the 90 days and ARB offset credits are retired from the Forest Buffer Account, ARB will assess penalties pursuant to section 96014. This allows the program to be made whole and still requires that the “bad actors” are appropriately penalized for not making the program whole.

New section 95983(c)(4) was added to clarify what happens in the case of an early forest project termination. These provisions were added to deter forest project owners from terminating their offset projects early given permanence requirements that require the sequestration of carbon for 100 years. If there is an early project termination, ARB will retire ARB offset credits from the Forest Buffer Account and notify the Offset Project Operator or Authorized Project Designee of the retirement. This ensures that the system is made whole and that the environmental integrity of the program is intact. The Offset Project Operator or Authorized Project Designee must replace all of the reversed tons calculated pursuant to Compliance Offset Protocol, U.S. Forest Projects to ARB within 90 calendar days. If the Offset Project Operator or Authorized Project Designee does not replace the ARB offsets within the 90 days and ARB offset credits are retired from the Forest Buffer Account, ARB will assess penalties pursuant to section 96014. This allows the program to be made whole and still requires that the “bad actors” are appropriately penalized for not meeting the requirements of this article and not making the program whole.

Sections 95983(d) and (e) were modified and deleted respectively, to combine the requirements for the disposition of forest offset projects in one section dealing with all reversals. This change was made because there was no need to have two sections. New section 95983(d)(3) was added to replace the text in original section 95983(e)(2), which was deleted for reasons stated above.

Various minor and non-substantive clarifications were also made to section 95983 to provide consistency in terminology and correct references within the regulation.

OOO. Modifications to section 95984. Ownership and Transferability of ARB Offset Credits.

Section 95984 was modified to specify for which purposes an ARB offset credit can be used. These changes were needed to make it clear to market participants how an ARB offset credit can be used within the cap-and-trade program. Additionally, a numbering structure was added to this section for readability.

Various minor and non-substantive clarifications were also made to section 95984.

PPP. Modifications to section 95985. Invalidation of ARB Offset Credits.

Section 95985(a)(2) was deleted and moved to section 95985(a). Section 95985(a)(1) was deleted because it was mistakenly included in the original regulation. All offsets will be retired once they are used for compliance, therefore we cannot require that all retired offsets be invalidated.

Section 95985(b) was modified in response to stakeholder comments to include a statute of limitations within which ARB would be able to invalidate an ARB offset credit. Staff determined that an 8 year time limit was sufficient to allow two verification bodies to review all the related offset project documentation, since verification bodies must be rotated once every six years. This gives ARB sufficient time to review all verification related material.

Original section 95985(b)(1) was deleted because the reversals and replacement of forest related offsets is being handled in section 95983. Original section 95985(b)(2), now section 95985(b)(1), and new sections 95985(b)(2) through (b)(4) clarify the conditions under which ARB would invalidate an ARB offset credit. These changes were made in response to stakeholder concerns that they are unable to quantify the risk of invalidation because the conditions were too broad.

Original section 95985(c) was deleted and moved to new section 95985(e) to provide the correct sequencing in this section due to the inclusion of new sections 95985(c) and (d). New section 95985(c) was pulled out of original sections 95985(d) and (e) and identifies the current holder or retiree of the ARB offset credits in question. This was added because this party is referenced several times in this section and allows staff to reference this section as opposed to writing it out in each provision. New section 95985(d) provides a dispute resolution process to allow entities to submit additional information to ARB before a final determination is made for invalidation. These provisions were added in response to stakeholder comments that there should be a notification and due process associated with invalidations.

As mentioned above, new section 95985(e) was moved from original section 95985(c). These provisions are generally the same except that new section 95985(e)(2) was added to allow for the dispute resolution process mentioned above.

Original section 95985(d), now section 95985(f), was modified to change the replacement timing from 30 days to 90 days to give entities enough time to acquire allowances at auction, or purchase additional ARB offset credits in the market.

Original section 95985(e) was moved to section 95983(c)(3) for reasons discussed in chapter NNN of this notice. Original section 95985(f) was deleted

because it is duplicative of requirements in section 95983(a) and replacements of ARB offsets due to reversals in the forest sector are now all handled in section 95983.

Various minor and non-substantive clarifications were also made to section 95985 to provide consistent terminology and section references within the regulation.

QQQ. Modifications to section 95986. Executive Officer Approval Requirements for Offset Project Registries.

Section 95986(c) was modified to remove the requirement that an Offset Project Registry apply for a holding account. This provision was mistakenly included in the original regulation because according to section 95814, Offset Project Registries may not hold compliance instruments.

Section 95986(c)(1)(E) was modified to change the amount of professional liability insurance that Offset Project Registries must maintain from fifty million to five million dollars. This change reflects stakeholder comments that the dollar amount was too high and that insurance was not offered at that level of coverage. Sections 95986(c)(2)(A)(1.) and (2.) were modified to specify what type of conflict of interest policies Offset Project Registries must have. These changes were made to clarify the types of policies that are acceptable by ARB.

New section 95986(c)(2)(F) was added to clarify how the Offset Project Registry application process applies to large organizations that may have a dedicated subdivision that wants to provide registry services. This is in response to stakeholder comments that potential Offset Project Registries could be part of a larger organizational structure, and the original language could preclude them from meeting the requirements for application.

Section 95986(c)(3)(C) was modified to remove the requirements that Offset Project Registries track prices and counter parties. This was removed in response to stakeholder comments that Offset Project Registries do not have the capability to track them.

Section 95986(d)(1) was modified to make it clear that Offset Project Registries cannot be Offset Project Operators or Authorized Project Designees for those offset projects developed under Compliance Offset Protocols. This change was made in response to comments that Offset Project Registries should be able to act in this capacity for those projects that are voluntary and will not come in to the compliance offset program.

New section 95986(d)(3) was added to be consistent with the new text added in section 95986(c)(2)(F).

The changes to section 95986(h) and the addition of new section 95986(i) clarify the level of expertise and training that Offset Project Registries and their staff

must have to be approved. These changes were necessary to clarify the requirements for stakeholders who plan to apply to be an approved Offset Project Registry.

The Offset Project Registry approval process was also strengthened to require that their staff take training and demonstrate knowledge about ARB Compliance Offset Protocols and regulatory requirements.

Original section 95986(j), now section 95986(k), was modified to clarify what happens to offset projects that reside at an Offset Project Registry, whose approval has been suspended or revoked. These offset projects may transfer to another approved registry and continue its current crediting period. This change was necessary because stakeholders were concerned that their offset projects could be ineligible if an Offset Project Registry's approval was suspended or revoked.

Various minor and non-substantive clarifications were also made to section 95986 to provide consistent terminology and section references within the regulation.

RRR. Modifications to section 95987. Offset Project Registry Requirements.

Section 95987(a) was modified to clarify that Offset Project Registries can also list offset projects not developed using Compliance Offset Protocols. Offset projects developed under non Compliance Offset Protocols would not be eligible to be issued ARB offset credits and the Offset Project Registry must make it clear that these offset projects do not qualify for compliance. This change was made in response to comments that Offset Project Registries should be able to act in a registry capacity for those projects that are voluntary and will not come in to the compliance offset program.

Section 95987(c) was modified to add a timing component of 15 days for an Offset Project Registry to submit any new conflict of interest documentation to ARB once it receives it from an Offset Project Operator and Authorized Project Designee. This text was added because it was unintentionally omitted from the original regulation.

Section 95987(e) was modified to change the number of in-person audits that Offset Project Registries must perform from 20 percent to 10 percent. Staff reduced the number of in-person audits because ARB will also have its audit program that will include in-person audits in addition to those performed by Offset Project Registries. ARB will also have access to the audit results collected by Offset Project Registries.

Section 95987(f) was added to require Offset Project Registries to review each verification report before accepting a verification opinion for an offset project listed using a Compliance Offset Protocol. This text was added to provide

greater assurance to ARB and Offset Project Registries that the verification opinions are accurate.

Various minor and non-substantive clarifications were also made to section 95987 to provide consistent terminology and section references within the regulation.

SSS. Modifications to section 95988. Record Retention Requirements for Offset Project Registries.

Section 95988 was modified to change record retention requirements for Offset Project Registries to 15 years. This change was made to be consistent with the new record retention requirements for Offset Project Operators and Authorized Project Designees in section 95976.

TTT. Modifications to section 95990. Recognition of Offset Credits for Early Action.

Original section 95990(a) was moved to new section 95990(b) for purposes of providing clarity within this section.

Original section 95990(c) is now new section 95990(a). These sections were moved to provide clarity within section 95990. New section 95990(a), original section 95990(c), was modified to change the dollar amount of professional liability insurance that Early Action Offset Programs must hold from two million to one million. This change was made in response to stakeholder comments that currently operated voluntary registries only hold one million dollars. This section was also modified to remove the requirements that Early Action Offset Programs track prices and counter parties. This was removed in response to stakeholder comments that Early Action Offset Programs do not have the capability to track them.

New section 95990(a)(3) now includes requirements for Early Action Offset Programs that are similar to requirements identified in section 95986(d) for Offset Project Registries. These requirements are necessary since both types of entities will be fulfilling similar functions within the offsets program and many of these entities may be acting in both capacities.

Original section 95990(b) is now new section 95990(c). These sections were moved to provide clarity within section 95990. New section 95990(c)(3) was added to the list of original requirements. This section requires that GHG reductions or GHG removal enhancements must result from an early action offset project listed prior to January 1, 2013. Originally the timing was tied to the offset project commencement date of January 1, 2012. Staff made this change because the acceptance of early action offset credits is tied to vintage years as opposed to offset project commencement. The date was changed from 2012 to 2013 because the offsets program will not be implemented by January 1, 2012. Original sections 95990(b)(5)(D) and (E) were combined into new section

95990(c)(5)(D), original section 95990(b)(5)(E)(i) was deleted and original section 95990(b)(5)(E)(ii) was moved into new section 95990(c)(5)(D). These changes were made because once the requirement to have a conservation easement was deleted, the requirements for all the forest projects are the same and do not need to be in separate provisions. The requirement for conservation easements was deleted because it is not needed since all projects are required to contribute to the Forest Buffer Account.

Original section 95990(d) was moved to new section 95990(j). New section 95990(d) was added to require that Offset Project Operators and Authorized Project Designees register with ARB. All entities implementing an offset project must register with ARB to ensure the agency has all necessary information about the owners of an offset project. These requirements are similar to those for offset project coming in directly under an ARB Compliance Offset Protocol.

Original section 95990(e) was moved to new section 95990(h)(6). New section 95990(e)(1) was added to include listing requirements for early action offset projects. These requirements are similar to those required of Offset Project Operators and Authorized Project Designees bringing in a compliance offset project under an ARB Compliance Offset Protocol. Listing is necessary to ensure that ARB has access to all information regarding early action offset projects. New section 95990(e)(2) was added to require Early Action Offset Programs to make specific information regarding early action offset projects publicly available. This is necessary to ensure that the public has access to all information regarding early action offset projects.

The changes to this section also clarify what happens to the crediting periods of early action offset projects once they transition to ARB Compliance Offset Protocols.

Section 95990(f) was modified to clarify the requirements for regulatory verification of early action offset projects. New section 95990(f)(1) includes new requirements that the verifier performing the re-verification services must be different than the one that did the initial verification for the Early Action Offset Program. This ensures that the review is completely independent and unbiased. The new requirements include a desk review of each Offset Project Data Report (new section 95990(f)(3)) by an ARB accredited verification body based on all original early action offset project documentation. A desk review by an independent body that is accredited by ARB is sufficient to determine if the information originally submitted regarding the offset project is complete and accurate. Staff has also included provisions to allow all Offset Project Data Reports for an individual offset project to be included in one desk review (new section 95990(f)(3) in response to stakeholder concerns that re-verification costs may be exceedingly high.

Section 95990 was further modified to include a threshold based on offset material misstatement in section 95990(f)(4) that, if found to be exceeded during

the desk review, would trigger full offset verification services for the Offset Project Data Reports that exceed the threshold. Staff set this threshold at 3 percent or more or 25,000 metric tons CO₂e, whichever is smaller. The 25,000 threshold is the same as the threshold for inclusion of covered entities in the cap-and-trade program and staff anticipates that three percent would be around this level as well. This provision allows for the same verifier that performed the desk review to conduct the full verification services because at this point in the process staff feels that the review by the same verifier is still independent and unbiased however, it may not be done by the verification body that did the initial verification under the Early Action Offset Program for reasons mentioned above. This provision also allows all Offset Project Data Reports that exceed the threshold and must undergo full offset verification services to be done as one verification service. This was included in response to stakeholder concerns that re-verification costs may be exceedingly high. Sections 95990(f)(4)(A) through (E) replace original sections 95990(f)(3) and include all the requirements that must be met to ensure that the early action offset credits are verified according to regulatory verification requirements of all ARB offset credits as found in section 95977.1.

Staff is seeking stakeholder comments on potential ways to facilitate the regulatory verification of early action offset credits that is efficient, does not require multiple verifiers to look at the same offset project data, and potentially provides a single, shared cost for verification services for an Offset Project Data Report.

New section 95990(g) was moved from original section 95990(f)(2) and modified so that conflict of interest is now assessed only against any party that holds more than 30 percent of the early action offset credits issued in each data year. Originally the regulation required that conflict of interest be assessed against all holders of the early action offset credits. Staff made this modification to reflect stakeholder concerns that applying conflict of interest to all early action offset credit holders is unnecessary and overly burdensome.

New section 95990(h) was added to clarify the criteria that early action offset credits must meet to be issued ARB offset credits. These requirements are similar to the issuance requirements for ARB offset credits in new section 95981. New sections 95990(h)(1), (3), (4) provide that ARB offset credits will be issued for those early action offset credits that meet the requirements of sections 95990(c), (e), and (f). New section 95990(h)(2) requires that all the GHG reductions or removal enhancements must be achieved by December 31, 2014. This is because beginning on January 1, 2015 all offset projects must use Compliance Offset Protocols and are no longer eligible to be brought into the compliance program if they are using Early Action Offset Program protocols approved pursuant to this section. New section 95990(h)(5) requires that Offset Project Operators and Authorized Project Designees of early action offset projects submit multiple attestations to ARB before any ARB offset credits are issued to GHG reductions or GHG removal enhancements achieved by their

offset projects. ARB requires these attestations in new section 95981.1 as well. These attestations are needed to specify that all Offset Project Operators or Authorized Project Designees specifically submit to California's jurisdiction to resolve any disputes regarding enforcement of the regulation against the Offset Project Operator or Authorized Project Designee. This change is necessary to make clear to Offset Project Operators or Authorized Project Designees that by participating in California's cap-and-trade program in this capacity, they will be subject to California's jurisdiction regardless of the physical location of the offset project. New section 95990(h)(6) was moved from original section 95990(e).

New section 95990(i) was added to clarify the process for how ARB offset credits will be issued for purposes of early action. New sections 95990(i)(1)(A) through (C) specify that one ARB offset credit will be issued for each early action offset credit that meets the requirements of section 95990(h) if the offsets occurred under the identified protocols in these sections. New section 95990(i)(1)(D) identify conditions that must be met for an ARB offset credit to be issued if the projects are using one of the identified protocols in this section. New section 95990(i)(1)(D)(i) requires that a portion of offset credits calculated pursuant to Compliance Offset Protocol U.S. Forest Projects be placed into the Forest Buffer Account. Like compliance offset projects, early action forest projects are also subject to reversals; therefore, these projects must also contribute ARB offset credits into the account to cover any potential losses. New section 95990(i)(1)(D)(ii) specifies that the ARB offset credits may come from a buffer account that is already being run by an Early Action Offset Program or may be subtracted from the total ARB offset credits issued at the time of conversion. The first case is identified because stakeholders have made ARB aware that some voluntary registries have already required their forest projects to contribute to a buffer account. If those registries will release the offsets to ARB, they will be accepted to meet this requirement. The second case is designed to cover those offset projects that have not contributed to a buffer account already or cannot get the offsets released to ARB by the voluntary registry. New sections 95990(i)(1)(D)(3.) and (4.) were included to identify what happens in the event that there is a reversal from an early action forest offset project. These provisions treat reversals the same way as they are treated for compliance offset projects pursuant to section 95983. This ensures that all forest offset credits are meeting the same standards.

New section 95990(i)(1)(E) provides the requirements that early action offset projects using Climate Action Reserve Forest Project Protocol, Version 2.1 must meet only if they plan to transition their early action offset projects to Compliance Offset Protocol U.S. Forest Projects. If the offset project will not transition to the compliance program, they would follow the rules in section 95990(i)(1)(D). Offset projects transitioning into the compliance system must recalculate their baseline based on the requirements in Compliance Offset Protocol U.S. Forest Projects. If they would have been issued more early action offset credits after they recalculate their baseline, ARB will issue them ARB offset credits in that additional amount, otherwise they will be issued ARB offset credits on a 1:1

basis. These provisions are necessary because the project baselines for offset projects using Climate Action Reserve Forest Project Protocol, Version 2.1 need to be recalculated as averaged baselines.

New section 95990(i)(2) through (4) outline the process that ARB will use to notify the Early Action Offset Program that ARB offset credits have been issued to replace their early action offset credits. These provisions are necessary so these programs can retire the appropriate offsets in their own systems, to avoid the same GHG reductions or GHG removal enhancements being credited twice in multiple systems.

New section 95990(j) was moved from original section 95990(d) and modified to include a timeframe of 15 days for ARB to notify the original holders of the early action offset credits that they have been issued ARB offset credits. This section further requires that those claiming that the early action offset credits belong to them must prove they own them and register for ARB. These steps ensure ARB has transferred the ARB offset credits to the correct parties, and that ARB can track their participation in the market.

New section 95990(k) was added to clarify how early action offset projects transition to compliance offset projects. New sections 95990(k)(1)(A) through (C) specify that early action offset projects using Early Action Offset Program protocols identified in the provisions must use the specified Compliance Offset Protocols and must begin using the Compliance Offset Protocols by December 31, 2014. These provisions are necessary so Offset Project Operators and Authorized Project Designees know which Compliance Offset Protocols they must use and the timing for when they must transition. New section 95990(k)(1)(D) specifies that early action offset projects using Climate Action Reserve Forest Project Protocol version 2.1 must recalculate their baselines pursuant to Compliance Offset Protocol U.S. Forest Projects. This provision is necessary to ensure consistency across all forest projects in the compliance program. New section 95990(k)(1)(E) requires that all early action offset projects using Climate Action Reserve Forest Project Protocol versions 3.0 through 3.2 subtract any optional pools that are excluded from Compliance Offset Protocol U.S. Forest Projects beginning with the last reporting period. This provision is necessary to ensure consistency across all forest projects in the compliance program because these pools will be excluded for any new projects coming into the program beyond December 31, 2014.

New section 95990(k)(2) was added to clarify that all early action offset projects which transition to a Compliance Offset Protocol will begin a new crediting period. This provision was included to provide clarify for stakeholders on the length of eligibility for transitioned offset projects.

New sections 95990(k)(3) and (4) was added to require that once an early action offset project transitions it must meet all the requirements that all compliance offset projects must meet if they begin under Compliance Offset Protocols.

These requirements can be found in sections 95973, 95975, 95976, 95977 through 95978, 95980.1, and 95981.1. These provisions are necessary to ensure consistency across all offset projects in the compliance program beginning in the second compliance period, 2015.

New section 95990(l) was added to provide that ARB offset credits issued to non-forestry early action offset projects are also subject to the invalidation provisions in section 95985. These provisions are necessary to ensure that there are replacement measures in place in the event an ARB offset credit is found to be invalid, and also ensure consistency across all offset projects in the compliance program beginning in the second compliance period, 2015.

Various minor and non-substantive clarifications were also made to section 95990 to provide consistency in terminology and ensure correct references within the regulation.

UUU. Modifications to section 95991. Sector-Based Offset Credits.

No modifications were made to section 95991.

VVV. Modifications to section 95992. Procedures for Approval of Sector-Based Crediting Programs.

No modifications were made to section 95992.

WWW. Modifications to section 95993. Sources for Sector-Based Offset Credits.

No modifications were made to section 95993.

XXX. Modifications to section 95994. Requirements for Sector-Based Offset Crediting Programs.

No modifications were made to section 95994.

YYY. Modifications to section 95995. Quantitative Usage Limit.

No modifications were made to section 95995.

ZZZ. Modifications to section 95996. Reserved for Sector-Specific Requirements.

No modifications were made to section 95996.

AAAA. Modifications to section 95997. Reserved for Approved Sector-Based Crediting Programs.

No modifications were made to section 95997.

BBBB. Modifications to section 96010. Jurisdiction.

No modifications were made to section 96010.

CCCC. Modifications to section 96011. Authority to Suspend, Revoke, or Modify.

No modifications were made to section 96011.

DDDD. Modifications to section 96012. Injunctions.

No modifications were made to section 96012.

EEEE. Modifications to section 96013. Penalties.

Section 96013 was modified to include minor clarifications.

FFFF. Modifications to section 96014. Violations.

Section 96014(b) was modified to clarify that each compliance instrument not surrendered on the appropriate surrender date is a single separate violation. The section was also clarified to allow the violation to accrue every 45 days instead of each day the compliance instruments remain unsurrendered. These changes were made in response to stakeholder concerns about market volatility if a covered entity was required to obtain a significant number of allowances in a very short period of time, as initially drafted. These changes allow greater time to obtain the compliance instruments and thus maintain stability of the market.

Section 96014(c) was added to the regulation to clarify that any act of deception in working with ARB will subject an entity to additional penalties under the provisions of this regulation. Section 96014(c) lists specific violations that may be contained in records submitted to ARB that will result in additional penalties against an entity that does not comply with the provisions of this regulation.

GGGG. Modifications to section 96020. Severability, Effect of Judicial Order.

No modifications were made to section 96020.

HHHH. Modifications to section 96021. Confidentiality.

No modifications were made to section 96021.

IIII. Modifications to section 96022. Jurisdiction of California

Section 96022 was modified to include a provision that clarifies that any entity that participates in the market program is subject to California's jurisdiction.

JJJJ. New section 96023. Reserved Provisions.

Section 96023 was added to reserve subsequent sections for any future rulemaking needs.

1. Modifications to Compliance Offset Protocol Urban Forest Projects.

Minor, non-substantive changes were made to this protocol to ensure consistency between the regulatory requirements for offsets and the compliance offset protocols.

This protocol was also modified to clarify that offset projects on lands related to federally-recognized Indian tribes are eligible under this protocol only if the tribes enter into a waiver of sovereign immunity with ARB related to the tribes' participation in the requirements of this protocol and the Cap-and-Trade Regulation. This ensures ARB's ability to pursue judicial remedies, if necessary, regarding these offset projects when enforcing the requirements of this protocol and the Cap-and-Trade Regulation, similar to ARB's ability to pursue judicial remedies regarding all other offset projects commenced under this protocol.

2. Modifications to Compliance Offset Protocol Livestock Projects.

Minor, non-substantive changes were made to this protocol to ensure consistency between the regulatory requirements for offsets and the compliance offset protocols.

This protocol was also modified to clarify that offset projects on lands related to federally-recognized Indian tribes are eligible under this protocol only if the tribes enter into a waiver of sovereign immunity with ARB related to the tribes' participation in the requirements of this protocol and the Cap-and-Trade Regulation. This ensures ARB's ability to pursue judicial remedies, if necessary, regarding these offset projects when enforcing the requirements of this protocol and the Cap-and-Trade Regulation, similar to ARB's ability to pursue judicial remedies regarding all other offset projects commenced under this protocol.

3. Modifications to Compliance Offset Protocol Ozone Depleting Substances Projects.

This protocol was modified to add CFC 113 as an eligible refrigerant and a carbon ratio was added for CFC 115. The leakage rate was changed to include the impact of California's Refrigerant Management Program. Staff also clarified that a third-party must verify compliance with the United Nations Technical and Economic Assessment Panel TEAP requirements.

This protocol was also modified to clarify that offset projects on lands related to federally-recognized Indian tribes are eligible under this protocol only if the tribes enter into a waiver of sovereign immunity with ARB related to the tribes' participation in the requirements of this protocol and the Cap-and-Trade Regulation. This ensures ARB's ability to pursue judicial remedies, if necessary, regarding these offset projects when enforcing the requirements of this protocol

and the Cap-and-Trade Regulation, similar to ARB's ability to pursue judicial remedies regarding all other offset projects commenced under this protocol.

Minor, non-substantive changes were made to this protocol to ensure consistency between the regulatory requirements for offsets and the compliance offset protocols.

4. Modification to Compliance Offset Protocol U.S. Forest Projects.

This protocol was clarified to require that the 10-year look-back at management activities on project lands is independent of past ownership to avoid crediting of regrowth of trees that were recently harvested.

Staff made clarifications to the protocol that state forest projects are not eligible to receive qualified positive offset verification statements, specifying the number of sample plots to be measured and which statistical tests to use, requiring that the project acreage to be verified, requiring that the verification team include a person with demonstrated competence in forest biometrics and modeling, and including requirements for less intensive verification, which requires site visits once every six years after initial verification.

This protocol was also modified to clarify that offset projects on lands related to federally-recognized Indian tribes are eligible under this protocol only if the tribes enter into a waiver of sovereign immunity with ARB related to the tribes' participation in the requirements of this protocol and the Cap-and-Trade Regulation. This ensures ARB's ability to pursue judicial remedies, if necessary, regarding these offset projects when enforcing the requirements of this protocol and the Cap-and-Trade Regulation, similar to ARB's ability to pursue judicial remedies regarding all other offset projects commenced under this protocol.

Minor, non-substantive changes were made to this protocol to ensure consistency between the regulatory requirements for offsets and the compliance offset protocols.