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California Air Resources Board
Senate Select Committee on Environment,
Economy & Climate Change
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Thank You Senator Pavley and Members of the Committee. It's a pleasure to be here today.

I'd like to start this afternoon by discussing how the cap and trade regulation fits within the overall AB 32 policy framework. Then I'll turn to some of the major details of the program, and I'll conclude with some discussion about where we are in the process of finalizing the details of the regulation and starting the program.

Under AB 32, California is required to cut its greenhouse gas emissions to 1990 levels by 2020. As part of this effort, ARB developed a Scoping Plan in partnership with many of our sister agencies and with the input and expertise of stakeholders and experts from across the spectrum.

The plan reflects the comprehensive approach our state is taking to cut emissions and drive the transition to a clean energy economy. It also reflects the recognition that these actions will deliver major public health and air quality benefits for Californians, something that has for more than forty years been at the core of ARB's mission.

Major elements of the plan include our now statutorily required 33% Renewable Electricity Standard; our Clean Vehicle Standards; our Energy Efficiency Standards for buildings and appliances; the Low-Carbon Fuel Standard; and Senate Bill 375.

There are a number of other targeted strategies to cut emissions, and we have in place an extensive emissions inventory and reporting system.

All of these rules and regulations are important, and many are designed to achieve not just climate goals, but other energy, economic, public health, and transportation related goals.

In addition to these key components, a cap and trade regulation provides two additional elements that are needed to support our efforts toward the development of a clean energy economy: a hard and declining cap on emissions, and a price on carbon.

The cap and trade regulation is projected to achieve about 20 percent of the total reductions needed to meet the AB 32 target. In fact, other policies like the Clean Cars Rule and the Renewable Electricity Standard are responsible for a greater percentage of the overall reductions.

But the hard and declining cap will cover about 85% of total statewide emissions, meaning that even if other policies underperform, regulated entities will nonetheless be required to take the necessary actions to reduce emissions sufficiently to meet the 2020 target. How they choose to do so is up to them, which significantly increases cost-effectiveness. But they have to do it.

The other key element of a cap and trade regulation is the economy-wide economic incentive it creates for the development and deployment of clean energy technologies. In California, as in most other places in the world, investment in clean energy technologies is stifled. Why? Because until the true cost of our current approach to doing business is accounted for, there's simply no motivation to do otherwise.

The money is out there. The inventive and entrepreneurial minds are out there. The research institutions and technology centers are out there. In fact, we have all of these right here in California in spades. But until the right economic and policy signals are sufficiently in place, we will not see the necessary focus and scale of investment in clean energy technologies that we both need and will greatly benefit from.

That is what an economy-wide price on carbon does. It sends a crystal-clear signal that we are serious about powering our economy with clean, less-carbon intensive technologies, and that investment in and development of them will be rewarded.

I'd now like to discuss some of the major elements of the cap and trade regulation. The regulation establishes a hard and declining cap on about 85 percent of total statewide emissions, including those from all major sources like refineries, cement plants, and the electricity sector. Starting in 2015, the transportation fuel and residential and commercial natural gas sectors would also be covered.

We have designed our regulation to carefully ensure that the initial price on carbon is strong enough to begin immediately sending the right signals without creating economic shockwaves. We have done this through the design of the allocation system, which relies on both free allocation and auction of allowances at the outset. The provisions for free allocation in the regulation are designed to encourage greater efficiency of production, which means that there are simply no incentives for regulated entities to increase emissions as a means to receive more allowances.

We have also incorporated rigorous offset provisions into the regulation, which will both enable regulated entities to meet their compliance obligations cost-effectively and help drive the development of additional technologies, methods, and practices to reduce emissions, especially from sectors not subject to greenhouse gas regulations. I think it is safe to say that the offset provisions in the regulation are the strictest, most rigorous provisions in existence anywhere in the world.

The rule also includes detailed provisions to prevent gaming or other activities that would compromise the effective functioning of the program. These include registration, reporting, and certification requirements, as well as provisions that establish limits on the amount of allowances entities can purchase or hold.

In addition, ARB will be establishing a Market Monitor Group and a Market Surveillance Committee, both of which will serve important roles in overseeing market activity and producing regular publicly available reports. We are also working with both the State Attorney General and the Commodity Futures Trading Commission to ensure all necessary provisions are in place to monitor activity in secondary markets and prevent any fraudulent or gaming types of activities.

And, we continue to work closely with the Western Climate Initiative, which includes other U.S. states and several Canadian provinces, toward the potential linkage of our regulation with those of other partners. Just as we have taken care to ensure that our own rule is defined by rigorous standards, we will ensure that other any programs we choose to link with adhere to similar standards before we do so.

Before I conclude, I’d like to briefly discuss where we are in the implementation process for the cap and trade regulation. Last

December, ARB considered the cap and trade rule, which includes the programmatic details I've mentioned here today. As part of the Board's action in December, we directed staff to continue working to finalize the necessary elements of the regulation. We are continuing to move forward within the timeline the legislature assigned us under AB 32 and the program is on track to begin in 2012.

However, in light of the importance of this regulation to the success of California's climate change program and the need for all necessary elements to be in place and fully functional, we are proposing to initiate the program in 2012, but start the requirements for compliance in 2013. This would not affect the stringency of the program or change the amount of emission reductions that the program will achieve, keeping us on track to meet the 2020 target required by AB 32.

In the next few weeks, ARB staff will hold a public workshop to discuss and receive input on this proposal and other elements needed to finalize the regulation. Prior to the workshop, staff will release a discussion draft of the regulation to enable all stakeholders to continue to fully participate in helping establish the final details of the program.

Staff will also be 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.

As I believe many of you know, in March of this year a trial court in San Francisco reached the conclusion that ARB had not sufficiently analyzed alternatives to the cap and trade regulation as part of the required analysis under CEQA for the 2008 Scoping Plan. We did not agree with court's decision and last week the First District Court of

Appeal granted our request to continue working on the development of the cap and trade regulation pending the final outcome of the appeal.

However, in light of our interest in maximizing both public participation and informed decision-making by our Board, ARB recently released a revised alternatives analysis for the Scoping Plan, which lays out several potential alternatives to the cap and trade regulation as a means to achieve the objectives of AB 32. The document reflects both regulatory and economic developments that have occurred since 2008, and is currently open for the 45-day public comment period. After considering and responding to all public comments, the Board will consider for adoption the revised alternatives analysis and the Scoping Plan on August 24th.

There have been many critiques of cap and trade. Some have come from those who are committed to designing and implementing the best possible program. These critiques are welcome. In fact, they are key to ensuring that we pursue the best possible approach for California – one that does in fact deliver the public health and economic benefits that AB 32 envisions.

Yet others have attacked cap and trade for altogether different reasons, including those interests that are merely hoping to forestall any meaningful actions to address climate change. We saw this in Washington not long ago. And as result, we have no national program. Not only did our country fail to take advantage of the opportunity to make major strides in reducing greenhouse gas emissions, we squandered the opportunity to reap major public health, air quality, and economic benefits.

Fortunately, in California we already have in place a number of key policies to cut emissions and drive clean energy. And moving forward, we will have even more information that will help inform our decision about the best possible way to design and implement our program. But we cannot afford to lose sight nor let up in our efforts.

Thank You and I’d be happy to answer any questions.