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December 14, 2010

Clerk of the Board
Air Resources Board
1001 I Street
Sacramento, CA 95814

File No. 043053-0000

**Re: California Climate Coalition Comments on
Proposed Cap and Trade Regulation**

Dear Chair Nichols and Members of the Board:

The California Climate Coalition is a coalition of California industries and cleantech companies who have joined together to develop recommendations for California's AB32 program. Since the fall of 2006, the Coalition has provided input to the ARB staff regarding design approaches that can accelerate low-carbon technology deployment in California and reduce greenhouse gas emissions in a cost-effective manner.

Our comments fall into three categories. The first set of comments contains recommendations for the Board's adopting resolution. The recommended provisions would ensure that the staff takes the necessary steps promptly to fill existing gaps in the current proposal, to issue guidance that covered entities will need to comply with the program, to evaluate and improve market design and to avoid duplicative regulation of California businesses by obtaining US EPA's determination that California's program will be considered equivalent to emerging federal regulations. The second set of comments recommends specific revisions or additions to the program to ensure that, as implemented, it is affordable and efficient. The third set of comments recommends actions that the Board should take beyond the adoption of the AB32 cap and trade program to accelerate cleantech investment and deployment.

I. The Board's Adopting Resolution

The California Climate Coalition has several concerns regarding the implementation of the proposed AB32 program that are best addressed through the adopting resolution. These concerns are noted below.

- A. Availability of Regulatory Tools and Guidance** - We are concerned that the proposal remains significantly incomplete and lacks sufficient regulatory guidance for timely compliance when the AB32 program commences. Much of the unfinished business includes material components of the program, including the allocation of allowances to the power, fuels and industrial sectors; the

selection of emission factors for various source types (particularly as the ARB intends to use both higher-tier emission factors than EPA uses for its reporting program as well as highly-conservative missing data provisions); the allowance tracking system; the auction system; the registration process; and various other critical components.

Recommendations:

- (1) The Board's resolution should commit to provide for one or more additional public hearings, or to reopen the record, prior to the commencement of the program, to enable stakeholders to comment further as more information becomes available regarding key program components;*
- (2) The Board should direct the staff to prepare a plan that specifies:*
 - (a) the tools and guidance that covered entities will need to comply with the regulations, including such components as the allowance tracking system, the registration process, the leakage assistance allocation, the auction process and the process by which the Executive Officer shall determine emissions in the event positive or qualified positive verification is not attainable, among other components;*
 - (b) the compliance activities affected by these tools and guidance,*
 - (c) the timeline, milestones and deadlines for staff development of these tools and guidance, and*

The resolution should further provide that the identified aspects of the AB32 program shall not commence unless the necessary tools and guidance are available to covered entities no less than six months prior to the date on which covered entities will need such information to commence operation under the cap and trade program.

- B. Evaluation of Proposed Market Design** – We remain concerned that the market, as currently proposed, is too dependent on as-yet-unknown future contingencies, including the degree of linkage to other jurisdictions (if any), the actual availability of verifiable offsets, the extent to which consumer demand will respond as predicted to carbon price increases and similar contingencies that the staff have recognized will ultimately determine the carbon price in California. We strongly recommend that further market analysis be conducted by independent third parties and that the staff consider and present to the Board for

adoption any necessary program adjustments or protections prior to program commencement.

Recommendation:

The Board's resolution should provide for a prompt independent market evaluation to test areas of potential market vulnerability, including the role of linkages, offsets, anticipated demand response and the functioning of the auction and price containment reserve and for the staff to return to the Board with proposed program revisions, as warranted.

- C. Integration with and Equivalency to EPA's Emerging Greenhouse Gas Program** – We remained highly concerned that California businesses will become subject to costly and time-consuming duplicative regulation. At present it appears likely that, without further action by ARB and US EPA, major California businesses will be regulated by (1) the ARB's AB32 cap and trade program; (2) by the federal Best Available Control Technology (BACT) program implemented by California air districts, by EPA or by both; and (3) by EPA's emerging new source performance standard (NSPS) program, which may address greenhouse gas emissions from both new and existing sources. Many of these businesses also will directly or indirectly be subject to one or more of the ARB's several complementary measures (e.g., low carbon fuel standard, renewable electricity standard, etc.). Duplication of agency oversight and program content¹ will impose unnecessary costs on California businesses without yielding any material corresponding environmental benefit. Such duplicative programs are very likely to discourage new investment in the state, including the very cleantech and energy efficiency investments on which we depend for the long-term success of the AB32 program.

Recommendation:

The Board's resolution should state the Board's intention that the AB32 program, as a robust economy-wide carbon cap and trade program, provides the best approach to regulate California's greenhouse gas emissions and to encourage strategic low-carbon technology development and that the overlay of federal greenhouse gas regulation would be neither necessary nor beneficial, particularly in light of the additional

¹ Despite best efforts, at this time California and the Western Climate Initiative staff also have yet to convince EPA to harmonize greenhouse gas monitoring, recordkeeping and reporting. Duplicate reporting also will add material unnecessary costs.

cost, time delay and multiple agency administrative resources that implementation of such duplicative federal regulations would require.

We are not seeking a delay in the December 16 adoption of the proposed regulation. We do believe that it is paramount, however, for the Board to recognize that successful completion of the above unfinished tasks is absolutely necessary to ensure that the AB32 program operates as desired. We further recommend the following elements for inclusion in the Board's adopting resolution.

Recommendation:

The Board should establish working groups of covered entities to assist the staff in identifying potential compliance and market operational problems that should be addressed before the program commences.

The Board resolution also should provide for periodic reports back to the Board on each of the items identified above (e.g., the availability of necessary regulatory tools and guidance, the results of the independent market evaluation, the determination of the equivalency of California's program with EPA regulations, and the identification and resolution of potential compliance and market operational problems identified by the covered entity troubleshooting work group recommended above).

II. Specific Program Design Recommendations

We make the following further recommendations regarding the content of the AB32 cap and trade program to ensure that it will function fairly and efficiently.

- A. Independent Dispute Resolution Board** – We strongly recommend that the Board direct staff to develop regulations for the operation of an independent administrative dispute resolution board. The sole purpose of this entity would be to adjudicate those factual, legal and jurisdictional disputes that will inevitably arise in the implementation of the AB32 program. While there are a variety of disputes that could arise under the program, as an illustration, among the first will be disputes regarding actual emissions from covered entities. These may arise as the ARB staff attempts to apply different emission factors or missing data assumptions to covered entity operations. Another area of potential dispute may be whether offsets have properly been verified and, if so, what level of emission reductions they represent. There are innumerable situations under such a comprehensive regulatory program in which such factual, legal and jurisdiction disputes will arise. The absence of an expert administrative dispute resolution body will not avoid controversy. Controversies will arise and, if there is no administrative mechanism for dispute resolution, then parties will simply direct such disputes to courts of law, likely resulting in significant unnecessary litigation, increased cost of compliance, excessive uncertainty and delay.

- B. Fair and Consistent Application of Auction Revenues** – While the details of auction revenue application will matter, in general we believe that the Board should embrace the following principles for applying auction revenues. Auction revenues
- i) from any sector should be applied primarily to greenhouse gas emission reductions from within that sector;
 - ii) from all sectors should be used for comparable purposes; and
 - iii) to the extent consumer rebates are offered, similar rebates should be available to consumers of fuels and other consumer products as well as electricity.
- C. Allowance Holding Limit** – The Board should remove or significantly increase the proposed holding limit. As currently proposed, the holding limit will severely restrict the ability of companies to trade economically, which will both materially increase costs and reduce liquidity.
- D. Price Containment Reserve** – The Board should amend the Price Containment Reserve to replenish the Reserve with offsets, obtained from third-party approved entities, if it becomes oversubscribed so as to provide for higher-confidence cost containment and to avoid depleting future allowance pools.
- E. Offsets** – The Board should amend the offset provisions by:
- (i) removing the limit on offset use for compliance purposes. The ARB's complementary measures directly ensure appropriate California investment in strategic low carbon fuels and technologies. In such a context, limiting offset use will simply increase the cost of the program unnecessarily. The regulation should use appropriate integrity criteria to assure that offsets are verified, surplus and otherwise worthy of use in the program; but should not otherwise limit offset access or use.
 - (ii) shielding from liability any good faith purchaser of verified offsets. Imposing liability on offset purchasers would unfairly penalize covered entities who have relied on the offset verification process and otherwise fully adhered to program requirements.
- F. Enforcement** - We understand that the staff did not intend for covered entities to be subject both to the market remedy for non-compliance (e.g., 4:1 offset relinquishment) and the daily penalty provisions. We believe that as drafted the regulation could subject covered entities to both sanctions. The Board should direct the staff to make appropriate revisions to the enforcement provisions to provide that:

- (i) covered entities would not be subject to both excess emission penalties and to civil and criminal penalties under the HSC, and
- (ii) civil/criminal penalties would not apply to each compliance instrument that has not been surrendered.

III. Rapid Cleantech Deployment

Consistent with prior CCC recommendations (see www.caclimate.org), the Board should establish an Executive Office level position the primary responsibility of which is to ensure that the very cleantech and facility investments anticipated by the AB32 program and its complementary measures (e.g., the low carbon fuel standard, the renewable electricity standard and motor vehicle technologies, among other measures) are expedited by the ARB and its sister departments, commissions, agencies and air districts. This responsibility should include appropriate reform of CEQA and air quality regulations so that low carbon fuels and technologies rapidly receive required product or facility performance verifications, certifications and permits. The responsible ARB Executive should submit periodic reports to the Board regarding obstacles, proposed solutions and degree of success.

We looking forward to working further with the ARB staff to ensure that the AB32 program becomes a success, that it operates fairly and efficiently and that it serves as a model for the nation. We hope that its implementation will create the confidence necessary to reduce the existing barriers to energy investments in the state.

Very truly yours,

Robert A. Wyman
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