CE2 Capital Partners
clean energy + clean environment

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Via Electronic Submission

The Honorable Mary Nichols, Chair
California Air Resources Board
Attn: Kevin Kennedy, Ph.D
Chief, Office of Climate Change
1001 I Street
Sacramento, CA 95812
http://www.arb.ca.gov/lispub/comm/bclist/php

Re: Comments on Proposed Regulations to Implement the Cap-and-Trade Program Under AB32

CE2 Capital Partners (CE2) appreciates the opportunity to comment on California Air Resources Board's (CARB) Proposed Regulation Order. A well-defined cap-and-trade program is essential to helping California meet its 2020 emissions targets.

Since its founding in 2005, CE2 has become one of the largest U.S.-based investors focused on global environmental markets. CE2 has closely followed the development of a cap-and-trade program in California and lauds the steps CARB has taken to provide a strong carbon market framework.

Outlined below are several comments to CARB's proposed regulation:

Offsets

Eligible Project Types

CARB has indicated that currently it will only accept four project types as offset credits: Forestry, Livestock, Urban Forestry, and Ozone Depleting Substances (ODS). Given the small scale of Livestock and Urban Forestry, CARB is highly dependent on the supply of credits provided by Forestry and ODS. This could severely limit offset supply, as few landowners have thus far agreed to the 100-year forest management commitment and there are other competing uses for ODS. In order to provide adequate cost containment, we believe that CARB should include easily measurable and verifiable coal mine methane and landfill methane projects as eligible offset types.

Early Action

Similar to eligible project types starting in 2012, CARB has limited early action credits. By only allowing Climate Action Reserve credits issued under Forestry, Livestock, Urban Forestry, and ODS protocols, CARB is hampering its ability to contain costs in the early years since there are few CAR credits currently issued under those protocols. CARB should encourage early investment in offset projects by expanding its eligible early action credits to include landfill and coal mine projects, and to allow credits from other scientifically rigorous registries such as the Voluntary Carbon Standard and the America Carbon Registry.

CARB has also indicated that it will only accept vintages from 2005-2014 as eligible early action credits. This artificially limits the crediting period of early action offset projects and hampers investment. Numerous offset projects were started with the expectation of an already established crediting period that extends beyond 2014. For example, most early action forestry projects were commenced on the expectation that they would receive credit for greenhouse gas removals through the end of an established crediting period (typically 30 years). CARB's cut off only makes sense if there is a clear procedure to transition projects from other program standards to CARB standards without significant additional cost and without changing the eligibility rules under which the project was originally registered. CARB has not yet provided any guidance on such a procedure, and needs to do so in order to encourage early investment in offset projects. Developers need certainty that their credits will seamlessly transfer from current existing protocols to the future CARB program in order to invest time and money.

Offset Supply

CARB's projections for offset supply rely heavily on ODS and forestry. However, there are several parameters in CARB's forestry protocol that will limit the development of forestry offset projects. First, CARB only provides a 25-year crediting period for forestry projects, yet requires a 100-year maintenance period following the last credit issuance. Although CARB indicates that it will provide crediting period renewals, it is uncertain whether eligibility requirements may change after the initial crediting period. Project developers will be wary of putting capital at risk if there is a burden and liability beyond the crediting period. We believe that the crediting period for forest projects should be commensurate with the permanence requirement. The second roadblock for developers is the 100-year permanence requirement following the issuance of the last offset credit. This restriction imposes a long tail of legal liability to project developers, one that extends well beyond AB32's market design. This imposes obligations on forestry offset projects well beyond those of industrial and power sectors.

Banking

Similar to allowances, CARB should identify that offsets have no expiration. This will help keep offset prices consistent with allowance prices and encourage long-term investment in offset projects. Without such clarity, investments in offsets projects will be dramatically curtailed given the slow ramp of the program and concerns around supply of and demand for offsets.

REDD

Additionally, CARB has been considering but has not yet adopted a program for REDD-based projects. It is important that CARB proceed to promptly outline a process for developing REDD crediting rules and to commit to a timetable to complete this process in 2011. Further, we would be particularly interested in additional clarity regarding the interaction between this process and the on-going process to define specific linkages with the states of Chiapas in Mexico and Acre in Brazil announced on November 17, 2010 by the Governor's Climate and Forests Task Force. We welcome the opportunity to participate in any working group or public comment process on this matter.

The comments above are of particular interest to CE2 based on our experience as an investor and project developer in environmental commodities markets throughout the US, as well as internationally. We welcome the opportunity to continue to participate in a robust, public process to develop a cap-and-trade program in California that will enable us all to meet the environmental and economic goals of the California Global Warming Solutions Actgre.

Thank you.

Sincerely,

Gregory Arnold
Managing Partner
CE2 Capital Partners LLC

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