



Graphic Packaging International, Inc.  
2600 De La Cruz Blvd  
Santa Clara, CA, 95050

January 20, 2017

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

[https://www.arb.ca.gov/lispub/comm/bcsubform.php?listname=capandtrade16&comm\\_period=1](https://www.arb.ca.gov/lispub/comm/bcsubform.php?listname=capandtrade16&comm_period=1)

Subject:

Comments to Assistance Factors, Approach, and Data for the Paperboard Sector

Reference:

ARB 15-Day Cap and Trade Amendments, Comments Due January 20, 2017, 5PM  
Graphic Packaging International, Inc., Santa Clara Paper Mill,  
CITSS ID CA1275 and ARB ID 100147  
2600 De La Cruz Blvd., Santa Clara, California

To the Clerk of the Board:

This letter provides comments to the ARB's proposed assistance factors, approach, and data for our sector, the paperboard sector (NAICS Code 322130). The data and approach used by ARB to determine the assistance factors for the paperboard industry does not adequately describe our sector. Therefore, the proposed assistance factors are inappropriate. In this letter, we describe key attributes of our sector, indicating where the ARB approach and data falls short and propose alternative approaches and data that would result in a more accurate characterization of our sector with fair assistance factors. Please give these comments your strongest consideration in finalizing these cap and trade amendments.



### **Trade Exposure**

ARB underestimates the trade exposure for paperboard sector at 11% to 14%. In actuality, nearly 60% of paperboard sold in California comes from outside California. This number is projected to increase to nearly 67% during the period from 2020 to 2030. In this sector, there is a significant level of competition from both international competitors and US firms outside of California, despite the additional cost they bear in shipping to our state. As a result, the threat of leakage is very high. These competitors have cheaper labor costs, lower raw material costs, and lower regulatory burdens, including no cap and trade costs. ARB's heavy reliance on just import and export data generate the misleading conclusion that trade exposure for this sector is only a moderate threat. It is in fact a very high threat, one where increased cap and trade costs can cause further leakage of business outside California. We strongly recommend that the trade exposure for this sector be revised upward to no less than 67% to accurately reflect our market situation and the very real threat of leakage.

One significant threat is Chinese paperboard firms. In previous discussions with ARB staff, staff have discounted the threat Chinese firms present in our sector, based China's pledge to reduce greenhouse gas emissions under the Paris accord. This is no guarantee. Past pledges by the Chinese government underscore this. There is no guarantee that greenhouse gas emissions reductions would come from their paperboard mills. To date, our market intelligence has not indicated emission controls at Chinese paperboard mills; nor was it expected. China has actually pledged to reduce greenhouse gas emissions only after 2025. Note that even if they started reducing greenhouse gas emissions in 2026, the Chinese mills will have far greater greenhouse gas intensities (closer to US firms in 2007) making it extremely difficult for California mills with significant greenhouse gas reduction investments to compete. Our market intelligence does indicate that they are increasing the capacity of their paperboard mills, fired on coal and other fossil fuels. We expect them to be a stronger competitor in the 2020-2030 decade than they are now. We expect increased leakage to China with their low cost structure and lack of environmental regulations, including no cap and trade. Similar arguments can be made for our competitors in North and South Korea and Mexico.

We support ARB's effort to expand the jurisdiction of cap and trade by linking with other states and Canadian provinces. This levels the playing field in the sector, reducing the concerns over trade exposure and leakage. Unfortunately, there have been no linkages with other states at this time, as each state continues to pursue separate agendas on addressing climate change and greenhouse gas emissions. At this time, we ask that ARB not bank on securing further linkages for cap and trade when constructing these amendments and recognize that other states, including Utah, Washington, Texas, several Midwest states, and many East Coast states, are a serious threat in our sector. Leakage to these states is a real concern as we do not compete on even footing in areas such as regulatory requirements, including cap and trade.



### **Sector in Decline**

The paperboard sector is currently in decline, with product demand down nearly 3% from 2010 to 2015. Several consumer buying factors are driving this decline, including preferences for fresh foods over dry grocery, package and product optimization that eliminates packaging material, and packaging substitution that results in switching to plastic containers. Furthermore, state and national extended producer responsibility (EPR) policies, including California, have created further uncertainty for the paperboard sector. Enacting these EPR policies may have the unintended consequence of increasing costs for paperboard while allowing plastic packaging with poor recyclability to become a competitive alternative. All of these trends are not temporary but a permanent part of the changing paperboard market driven by the sustainability movement. As such, we expect our sector to see continued decline through 2030. The assistance factor analyses ARB has conducted thus far has yet to account for market trends. With our sector facing severe headwinds in a permanent decline in demand, we ask that ARB realize that greenhouse gas emissions will be reduced in this secular decline, but please do not exasperate the extremely tough market environment with a reduction in the assistance factor for this sector.

### **Applicability of Regression Analysis**

ARB incorporated a regression analysis in the development of both international and domestic assistance factors for the paperboard sector. While the effect was minimal in for the international assistance factor, the regression analysis had a surprisingly significant impact of reducing the domestic assistance factor by more than 25%. ARB states that the purpose of the regression analysis is to "harmonize" the assistance factor component "across different sectors with similar attributes." However, the regression analysis was conducted across all sectors with no attempt to identify sectors that have similar attributes that logically might act in a similar fashion. As members of the paperboard sector, we see no logical reason that our sector should act like or have any relation to the petroleum and natural gas sector, petroleum refining sector, beet sugar sector, coal products manufacturing, wet corn milling, fruit and vegetable canning, all dairy product manufacturing, breweries, wineries, turbine and turbine generator manufacturing, aircraft manufacturing, guided missile and space vehicle manufacturing, automobile and other motor vehicle parts manufacturing, and many other covered sectors under cap and trade. The attributes in the paperboard sector, including commodity pricing, international competitors, non-California US competitors, energy intensity, and market trends, are vastly different than the other covered sectors under cap and trade. If a regression analysis is to be utilized, it can only be used when similar attributes between sectors are identified, providing rationale for harmonization between like-sectors. No rationale exists today, as ARB has not conducted an effort to identify similar attributes between sectors. As such, there is no rationalization for the 25% drop in the domestic assistance factor for our sector from 0.8 to 0.55. Based on this, we ask that ARB omit the regression analysis from all assistance factor analyses done for the paperboard sector.



## Recommendations

After a great deal of review of ARB's assistance factor analyses and proposed assistance factor for the paperboard sector, we recommend that:

1. The trade exposure for the paperboard sector be raised to at least 67% to accurately reflect the highly competitive market that exists with international and non-California US paperboard firms.
2. The regression analysis be omitted for the determination of all assistance factors as there is no rationale for or identification of similar attributes between the paperboard sector and any other covered sector under cap and trade.
3. ARB recognize that all other states in the union may never link to California's cap and trade system and are therefore a leakage threat to California businesses. For the paperboard sector, firms from other states, which have lower cost structures and lower regulatory burdens including cap and trade, are a significant threat to leakage.
4. ARB not consider Chinese paperboard mills on par with California paperboard mills. They are not. In the period from 2020 to 2030, if Chinese paperboard mills begin reducing greenhouse gas emissions after 2025, their emission intensity will be significantly higher than California paperboard mills.
5. ARB incorporate market trends into the assistance factor analyses. Such trends give a vital perspective on a sectors ability to absorb a reduced assistance factor. The paperboard sector is in decline and is expected to continue this decline through 2030, making it extremely difficult to absorb the additional burden of a reduced assistance factor under cap and trade.

We appreciate the opportunity to provide these comments to ARB in order to improve the characterization of our paperboard sector and the development of fair and appropriate assistance factors under cap and trade. We would be happy to discuss any or all of these recommendations with the ARB team detail, subject to confidentiality. Let us know if further discussion is needed. Please contact me at (408) 496-5080 should you have any questions regarding these comments.

Sincerely,

A handwritten signature in black ink, appearing to read "Rick Horne".

Rick Horne  
Human Resources and Environmental Manager

Copies:

Andrew Johnson, VP Government Affairs and Sustainability  
William Buchan, Market Potential, Inc.