

October 22, 2018

**To: Rajinder Sahota**  
**Assistant Division Chief**  
**Industrial Strategies Division**  
**California Air Resources Board**  
**1001 I Street**  
**Sacramento, California 95814**

Online submission: <http://www.arb.ca.gov/lispub/comm/bclist.php>

## **COMMENTS ON PROPOSED REVISIONS TO THE CAP-AND-TRADE REGULATION**

Dentons US LLP, on behalf of Foam Supplies, Inc. and True Manufacturing Co., Inc., submits the following comments with respect to the proposed revisions to the cap-and-trade regulation published on September 4, 2018. In these comments we focus on two particular topics in the Proposed Regulation and Initial Statement of Reasons, the Direct Environmental Benefit in the State (“DEBS”), and the Price Containment Units.<sup>1</sup> We appreciate the outreach by CARB staff to solicit informal comments before beginning the formal rulemaking process.

### **Price Containment Units**

We support the approach taken in proposed §95915 with respect to the use of Price Containment Units (PCUs) should prices exceed the price ceiling.

- To preserve the integrity of the GHG reductions used for PCUs, we recommend the use of verified offsets created under approved compliance or voluntary protocols/methodologies.
- Design the program to invest in a reserve PCUs through the purchasing of compliance and voluntary offsets sooner than later. This advance investment would have the benefit of providing funding to incentivize more in-state offset project development from existing CARB protocols and other voluntary protocols.
- We recommend the minimum price CARB may purchase offsets to meet this obligation be set at the auction price floor. We recommend CARB consider using an offset purchase ratio greater than one offset to one PCU to provide additional environmental benefits to the program.

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<sup>1</sup> We stand by our prior comments in the public workshops held earlier this year and our recent comments to IEMAC. (attached).

Additionally, in our comments to the Independent Emission Advisory Committee (“IEMAC”) we provided a recommendation to maintain more allowances in the “speed bumps” and “price ceiling” reserves to reduce allowance supply in the active market and safely test how this effects the market and prices (see Attachment A).

## **Offsets: Direct Environmental Benefits in the State**

We support the approach taken in the propose rule. Offset projects which are undertaken in a State clearly have direct environmental benefits to the State. The Initial Statement of Reasons contains very specific examples of the environmental benefits from projects using one of the six approved compliance offset methodologies.

We agree that projects undertaken outside the State, may also have direct benefits in California. The proposed rule allows for certain categories of information to be submitted in support of a claim that a project outside California has direct in-state environmental benefits: scientific peer reviewed information or reports, governmental reports such as the Intergovernmental Panel on Climate Change, and “monitoring or other analytical data...results in the reduction or avoidance of any pollutant in the State.” See §95989(b)(3).

The June 21 staff presentation demonstrated: [1] that some individuals and groups are using the DEBS language to restrict the applicability of accepted methodologies and even criticize in-state projects because all the reduced GHG emissions are just being used to offset in-state emissions - they are not additional; and [2] of all the offset credits issued to date from the six existing authorized methodologies, only about 20% come projects that are located in-state and clearly meet DEBS criteria (forestry and livestock). We suggest this demonstrates the need for additional protocols to be adopted that can generate DEBS.

## **Overlapping Policies**

- We support the assertion by others that there are regulatory policies that overlap with the cap-and-trade program by targeting the same regulated entity more than once. Regulatory policies dictate how reductions must be met while cap-and-trade does not. How an entity meets their emissions allocation is up to them and, therefore, this does not restrict reductions from a regulatory policy being used to meet cap-and-trade obligations and result in double-counting, reducing the demand for allowances, lowering allowance prices, and affecting the ability for California to meet its reduction targets. For example:
  - If regulatory policies also target 20% of AB32 covered source emissions, this could lead to both programs incorrectly reporting success in meeting their annual reduction goals. Total reductions required from both cap-and-trade and regulatory programs to meet California’s 2030 goal are 1.72b tonnes (32% (620m tonnes) from cap-and-trade and 68% (1.1b tonnes) from regulatory policies). If both sides report meeting their 2030 goals, 220m tonnes (1.1b x 20%) could be double counted.
- We recommend CARB consider requiring compliance entities to include the volume of reductions that resulted from their compliance with regulatory policies to start understanding the impact of overlapping policies.

**Conclusion**

We appreciate the opportunity to make these suggestions for enhancement of the cap and trade rule.

Respectfully,

*Susan E Wood*

Susan Wood, Senior Advisor

*Jeffrey Fort*

Jeffrey Fort, Partner

*Matthew Adams*

Matthew Adams, Partner

October 1, 2018

To: IEMAC

## COMMENTS ON IEMAC SUBCOMMITTEE REPORTS

We appreciate the time and effort devoted by the Independent Emission Advisory Committee (IEMAC) in the development of the subcommittee reports and also thank you for allowing an open discussion at the September 21, 2018 committee meeting. The following comments are provided as a follow up to the verbal comments made by Susan Wood during the meeting.

### SUBCOMMITTEE REPORT ON OFFSETS

1. Offset prices are linked to allowance prices in that they trade at a slight discount to the allowance price. However, the cost of high-quality offset prices (especially anaerobic digestors) is generally higher than the current price of allowances and is limiting the number of projects being developed in other protocols. If the price of allowances continues to trade at the auction price floor, the forward price curve still does not provide the appropriate price incentive for offset projects (see comments on overallocation report).
2. We support the recommendation of the language to clarify how a project qualifies for DEBS designation and suggest the following additional language (in italics) just to remove any ambiguity.
  - a. ...to qualify as an offset credit providing direct environmental benefits in state, a project must reduce or avoid not only greenhouse gas emissions but at least one additional air *pollutant in the state* or water pollutant that “could have an adverse impact on waters of the state.”
3. See attached white paper (“A Case for Offsets”) authored by Dentons in March 2017 for additional comments and information.

### SUBCOMMITTEE REPORTS ON MANAGING ALLOWANCE SUPPLY & ALLOWANCE OVERALLOCATION

1. We agree that there is likely an oversupply of allowances in the market currently and in the future (post-2020). Following the 9-21-18 meeting, we were provided with additional data from IEMAC on this subject and we agree that further investigation or a more detailed explanation of future projected supply by CARB is warranted.
2. We support IEMAC’s recommendation to reduce the post-2020 active market allowance supply by moving allowances into the post-2020 “Reserve Tiers” and “Price Ceiling” (Section 4(4)(a) of the Subcommittee Report on Managing Allowance Supply”).
3. Some additional thoughts on why the market seems overallocated:



- a. A clear sign indicating that there has been a historical and current oversupply of allowances in the market is that allowances have continually traded at or near the auction price floor.
  - b. Prior to 2013, allowance prices were much more volatile and traded based on industry and regulatory news. However, since program implementation, the allowance price has traded near the auction price floor and any industry or regulatory news has had very little effect on allowance prices.
  - c. The market has become complacent and seems comfortable that there is an adequate allowance supply now, and in the future, and has very little concern that allowance prices will rise to any significance above the auction price floor.
4. By reducing allowance supply post-2020 and forcing allowance prices to trade based on the true supply and demand in the market, as opposed to just trading around the auction floor price, this should provide CARB with a better indication of the actual state of over or under-supply in the market at any given time.
  5. An increased and more volatile allowance price will incentivize compliance entities and market participants to participate more actively in the market and strongly consider offsets and investing in offset projects as a path towards compliance. The majority of compliance entities do not use offsets for compliance due to the complications associated with contracting and guarantees with the project developer. Additionally, because offsets trade at such a small discount to allowances, there is not an incentive for buyers to take the risks associated with offsets.

#### **SUBCOMMITTEE REPORT ON PRICE CEILING CONSIDERATIONS**

1. We support the recommendation that offsets to be used for price containment units (PCUs) should the price ceiling be reached and allowances available at that price are exhausted.
2. We recommend the use offsets from the voluntary registries (ACR, CAR, & Verra) be used to meet this obligation.
3. We support the recommendation for CARB to “design the program so that investments in a reserve of emissions to account for the possible use of price ceiling units occurs before they might be brought into the program. This advance investment would have the indirect benefit of identifying new protocols for out of market emissions reduction opportunities.”
4. We recommend the minimum price CARB may purchase offsets to meet this obligation be set at the auction price floor.
5. We support the recommendation of using “...a ratio greater than ton per ton...” of offsets.

#### **SUBCOMMITTEE REPORT ON OVERLAPPING POLICIES**

1. We support the recommendation that there are policies that overlap with the cap-and-trade program by targeting the same regulated entity more than once.

2. We support the conclusion that this overlap can lead to an oversupply of allowances that may dampen prices in the cap-and-trade market.
3. We also suggest that the overlapping policies affect the ability for CA to meet its reduction targets.
  - a. For example: Total reductions required to meet 2030 goal are 620m tonnes (38%) from cap-and-trade and 1.1b tonnes (68%) from regulatory policies. Assuming both programs meet their goals but 20% ( $1.1b \times 0.20 = 220m$ ) of the regulatory policy reductions comes from cap-and-trade covered sources, this reduces cap-and-trade's net contribution to 400m ( $620m - 220m$ ) even though it will be recorded as a 620m reduction.
4. Regulatory policies dictate how reductions must be met while cap-and-trade does not. How an entity meets their emissions allocation is up to them and, therefore, this does not restrict reductions from a regulatory policy being used to meet cap-and-trade obligations and result in double-counting.
5. We recommend CARB consider requiring compliance entities to report their GHG reductions resulting from compliance with regulatory policies other than cap-and-trade.

We appreciate the opportunity to submit these comments to the IEMAC. If you have any questions, please do not hesitate to call (203-561-9116) or email ([swood1234@gmail.com](mailto:swood1234@gmail.com)) Susan.

Respectfully,

*Susan E Wood*

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*Jeffrey Fort*

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