



Ms. Rajinder Sahota
California Air Resources Board
1001 I Street
Sacramento, CA 95814

October 27, 2017

Submitted electronically via: www.arb.ca.gov/cc/capandtrade/meetings/meetings.htm

RE: Public Workshop on Cap-and-Trade Regulation Post-2020 and AB 398 Implementation held October 12, 2017

Dear Ms. Sahota:

Environmental Defense Fund commends ARB for engaging stakeholders early on the important topic of cap-and-trade design post-2020 as it relates to adapting the regulation to comply with AB 398 and we want to thank ARB for their informative workshops and this opportunity to comment.

Price Ceiling

Work with the Legislature to consider a “rainy day” fund that could be used at the price ceiling. Given that California must implement a hard price ceiling per the direction in AB 398, the ideal would be to have a pool of reductions available ahead of time to replenish the Allowance Price Containment Reserve should it become exhausted. AB 398 provides ARB with the authority to purchase reductions with revenue raised for instruments sold above the price ceiling but is silent on any earlier expenditures. Therefore ARB would likely have to work closely with the Legislature to fully implement a “rainy day fund” for reductions. A number of questions would have to be addressed with the Legislature including: when should California begin to develop a rainy day fund? How could revenue best be used so that developing a rainy day fund does not interfere with the other important expected investments from the Greenhouse Gas Reduction Fund especially investments in disadvantaged communities?

However, there are a number of steps ARB could take in order to facilitate this discussion with the Legislature. It is important that ARB clearly identify potential sources of reductions that could be used to back up instruments sold at the price ceiling. This includes developing a clear process for how the agency will consider and approve these reductions ahead of time in order to send a signal to those markets. ARB could also compile relevant information on these approved sources of reduction including current supply and time required for new project

development. ARB may also be able to utilize the expertise of the new offsets task force to help answer these questions as well. Armed with this information, ARB could make recommendations to the Legislature through regular Cap and Trade reporting or presentations to the relevant committees, recommending how much advanced time the state might need in order to secure a pipeline of reductions that would be able to protect the environmental integrity of the price ceiling. This would allow the Legislature to consider important questions like should a percentage of the revenue from the price containment points be used to secure reductions in advance?

Factors to consider in setting the price ceiling.

Overall EDF believes that the goal should be to set the price ceiling at a level that provides the certainty required by AB 398 but ultimately at a level that California is unlikely to reach and that allows the carbon market to operate to set the carbon price needed to achieve the state's goals. AB 398 includes a number of important considerations on setting the price ceiling and we concur with ARB's addition of how to best incentivize research, development and deployment of GHG reducing technologies. We also want to emphasize the importance of coordinating with linked jurisdictions and those that might potentially link in the future. ARB recognized this during the workshop and it was helpful to have Ontario and Quebec included in the proceedings. Consideration of the needs of linked jurisdictions is worth adding to the list of important considerations in setting the price ceiling. For example, it is critical that the level of the price ceiling works with any federal requirements imposed on linked jurisdictions by the Canadian government.

Future Linkages

Creating a pathway for a sectoral, one-way linkage with Acre, Brazil is more important than ever.

EDF has submitted many comments in support of California's consideration of a link between California's program and the extensive and well established effort in Acre, Brazil to further the social justice movement started by Chico Mendes to reduce large-scale deforestation and forest degradation in order to protect indigenous peoples' rights and support sustainable livelihoods for forest communities. As previously described we believe this is an important step in the evolution of California's global climate leadership.

The global importance of California's action has not diminished; but now more than ever we believe that California needs the high integrity instruments that Acre can offer to protect the environmental integrity of California's program as the state implements a hard price ceiling. AB 398 requires ARB to implement a hard price ceiling and to offer instruments for compliance at a set price if the Allowance Price Containment Reserve is exhausted. Importantly, AB 398 also requires ARB to use all revenue from the sale of instruments sold above the cap to purchase reductions on at least a ton-for-ton basis. Because of the new limitations in AB 398 on offsets, which could chill the market for further offset development, the supply of offsets within already approved protocols could very likely be insufficient to meet any potential future need California

has for purchasing reductions to protect the environmental integrity of the price ceiling¹. Thus, creating a linkage with Acre, which could provide an ample supply of high quality instruments if California needs them, is of paramount importance.

Time is of the essence for establishing this linkage. First, there are several international actors who could potentially look to Acre and other tropical forest states and countries for GHG reductions. Because of California's long relationship with Acre and extensive work in this area, California is best positioned to develop the standards for this type of international reduction credit in a transparent way that sets a very high bar of environmental integrity and social and environmental safeguards. California must act relatively quickly to continue to lead in this area, however. Similarly, California cannot simply wait until prices begin to approach the price ceiling in order to act. It takes time to create the pipeline of credits and Acre needs to know whether they can count on California's partnership. Slightly more intangible but no less important, research is showing that the ongoing climate impacts California will continue to experience have a close link to the Amazon rain forest. For example, complete deforestation of the Amazon could cause a 50% reduction in snowpack in the Sierra Nevada².

ARB has done extensive work in this area including holding many informative workshops. We urge ARB to move into the regulatory development phase for this important linkage as soon as possible and definitely before the end of the third cap-and-trade compliance period.

Other 398 Considerations

Cap should be adjusted to reflect expected emissions in 2020 and as a response to AB 398 changes.

The current regulation sets the 2021-2030 cap based on a straight-line reduction between 2020 and 2030. Emissions are expected to be below capped levels in 2020, however, and for a number of reasons articulated in previous comments, EDF believed that ARB should have set the post-2020 cap based on a step-down to expected emissions in 2021 rather than a straight-line. In the final regulation, ARB compromised by placing the allowances that made up the difference between these two methodologies in the Allowance Price Containment Reserve.

EDF believes that changes made in AB 398 provide even stronger justifications for retiring or otherwise eliminating these allowances. Before AB 398 these additional allowances could perhaps be justified as providing additional price protection given the soft price ceiling. However, the new hard price ceiling will provide absolute price protection. Pre-2020 APCR allowances will provide a buffer before ARB needs to begin issuing new instruments above the

¹ The authors of [Balancing Risks from Climate Policy Uncertainties: The Role of Options and Reduced Emissions from Deforestation and Forest Degradation](#) have recognized this potential role for REDD+ on a global scale.

² [Simulated Changes in Northwest U.S. Climate in Response to Amazon Deforestation](#).

cap and these post-2020 APCR allowance are not needed. AB 398 also directs ARB to consider oversupply and banking. These post-2020 APCR allowances meet the definition of oversupply and can be easily removed from the program without impacting incentives or disrupting consistency and expectations of the program since advanced 2021 vintage allowances have never been sold.

Banking

We agree with the ARB summary of the benefits of banking and see banking as an important feature of California's program. In addition, banking can create incentives for earlier emissions reductions, creating a benefit for the atmosphere. We believe that eliminating post-2020 APCR allowances would be the appropriate response to the direction in AB 398 rather than making any adjustments to banking rules or based on banking behavior pre-2020.

Offsets

EDF believes that offsets play an important role in the cap-and-trade program. They provide opportunities to uncapped sectors to participate in emissions reductions, provide pathways for lowering compliance cost and therefore opportunities for increasing ambition, and importantly the cost-containment they provide can also help California avoid triggering its new hard price ceiling post-2020. Therefore we urge ARB to continue considering new offset protocols as we approach 2020. We also believe that ARB's interpretation of the direction in AB 398 about half of offsets providing direct environmental benefits is correct. This should be interpreted to mean that a compliance entity can meet up to two percent and then up to three percent (after 2025) with any approved offsets and in order to access the full four or six percent of offsets they must procure offsets that provide a direct environmental benefit to California.

Sincerely,

A handwritten signature in cursive script that reads "Erica Morehouse".

Erica Morehouse
Senior Attorney, Global Climate