April 5, 2013

VIA E-MAIL

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

Electronic submittal: www.arb.ca.gov/lispub/comm/bclist.php

Re: **Proposed Amendments to the California Cap and Trade Rule**
Amendments to Allow the Use of Compliance Instruments Issued by Linked Jurisdictions
Subchapter 10, Climate Change, Article 5
3rd Notice of Public Availability
Comments from Valero

Gentlemen:

The Valero Companies ("Valero") appreciate this opportunity to provide comments regarding the California Air Resources Board ("ARB") proposed amendments to the California cap on greenhouse gas emissions and market-based compliance mechanisms, as posted for public comment on March 22, 2013. Valero subsidiaries own and operate two refineries in the state of California, and one in the Province of Quebec, with a combined throughput capacity of over 540,000 barrels per day and market our products on a retail and wholesale basis through an extensive pipeline distribution system. Due to our presence in both jurisdictions under discussion in this proposal, Valero is providing the following comments and observations.

As stated in our June 27, 2012 comments, we reiterate that Valero does not support linkage of the California and Quebec programs at this time due to differences between the two cap-and-trade programs and the high potential for inequitable treatment of covered entities. The California program is significantly more prescriptive than Québec's which will result in inconsistent interpretation and application of the program requirements on affected businesses and create adverse impacts for California facilities. Before considering linkage, we again stress that ARB and Québec should allow both cap-and-trade programs to be fully developed and implemented separately. After both programs have been operational for a reasonable period of time, ARB and Québec will be in a position to truly evaluate program performance and cross program equity so as to avoid adverse impacts to business. While these comments focus on linkage with Québec, the same logic holds true for any trading partners that may potentially link with ARB's program in the future. A well planned and evaluated linkage will help to ensure the success of multiple linked programs by ensuring availability of credits, fluidity of the market and reasonable pricing.

We incorporate herein our comments on the original linkage draft rule dated June 27, 2012, and January 8, 2013. To the extent that ARB eventually finalizes amendments pertaining to linkage, we offer the following comments on the third public notice.

- Linkage to External GHG ETS. The regulatory record for justifying linkage between the California Cap-and-Trade program and other jurisdictions fails to provide a defensible argument as to how linkage will not overstep constitutional limits on states engaging in foreign affairs. In *Massachusetts v. Environmental Protection Agency*, 549 U.S. 497, 519 (2007), The Supreme Court wrote: "Massachusetts cannot invade Rhode Island to force reductions in greenhouse gas emissions, [and] it cannot negotiate an emissions treaty with China or India." There are a number of constitutional doctrines that ARB has not sufficiently addressed to justify program linkage to foreign entities, including but not limited to constitutional doctrines of preemption, the dormant foreign affairs power, the Compact Clause, or the dormant Commerce Clause. Thus the potential for litigation appears to be a distinct possibility, creating significant uncertainty in the market and potentially jeopardize participants with significant capital investments in a linked program

- Linkage through WCI, Inc. It has been Valero's understanding that the process of "linking" Cap-and-Trade programs from varying jurisdictions was to occur through WCI, Inc. We note that nowhere in the proposed revisions does ARB mention WCI, Inc: all mention of linkage is in the context of a direct relationship with the external GHG ETS. Valero contends that this is inappropriate in light of the statements ARB has made with regards to the process of linkage, particularly in regards to the constitutional limitations mentioned above. WCI, Inc. will play a pivotal role in the linkage process. ARB has stated that all GHG ETS systems are ultimately linked only to WCI, Inc., and it is through this linkage the participating jurisdictions have coupled programs. Valero contents that ARB should revise the proposed language to reflect the linkage process as occurring through the entity of WCI, Inc., and not directly with external GHG ETS.

- The 3rd 15-day notice fails to address significant issues regarding offsets between programs. Page 4 of the second 15-day notice states that the Quebec compliance offset program is equivalent to the California program. This is not true in at least two important aspects: **reciprocity** and **liability**. While Quebec has revised some language to clarify which offsets in California will be honored, there is still a lack of mutual reciprocity between the jurisdictions. For example, Quebec stated for the destruction of ozone depleting substances protocol that only materials extracted from equipment in Canada would be eligible for offset credit under their program. In addition, the liabilities for invalidated offsets are not the same: California leaves the covered entity responsible for replacing invalidated offsets, whereas the Quebec program has a pool from which covered entities can pull valid replacement offsets. In this third 15-day notice, there is no discussion at all about offsets, the verification protocol for offsets, and the liability for invalidated offsets. ARB should revise this proposal to address these issues.

- Specification of Currencies: §95911(c)(3)(C)-(D) contains language specific to Canadian currency but should either remain general for the currencies of any linked jurisdiction or be left out altogether.

Additional Regulatory Citations:

- §95913(i) does not allow an entity registered in an external GHG ETS to purchase from the California Reserve. While it may make sense to prevent a Canadian company without any related entities in California to buy up California reserve allowances, this requirement would preclude a company with entities in both Quebec and California from optimizing its compliance strategy. All aspects of the market should be uniform and open to entities in all linked jurisdictions. Similarly, section 95942(d)-(e) should include reserve allowances.

- §95921(6) should be expanded to state that price disclosure is also not required for secondary market transactions.

- §95830(h)(2): This section requires clarification as to the definition of "entity" in that if "entity" is defined as the "corporation", then registering in any other jurisdiction other than California would be prohibited, regardless of the presence of operations in linked jurisdictions.

- §95833(f)(3)(D) and 95920(g): Significant clarity is needed around how the holding limits will apply to entities with operations in multiple jurisdictions. Statements regarding "opting-out" of consolidation notwithstanding, we request that ARB provide concise regulatory language regarding how the holding limits will apply under these circumstances.

- §9511(c)(3)(e): Valero contends that it is inappropriate for the auction administrator to set the auction reserve price to the highest market value of any participating jurisdiction. Unforeseen market circumstances that artificially inflate market prices in one jurisdiction should not penalize all other participants. ARB should explore other approaches to setting the reserve price that reflect the market signals from all linked jurisdictions.

Valero strongly urges ARB to consider and address the issues outlined above before moving forward with linkage to the Québec cap-and-trade program. As proposed, we believe the methodology used to develop linkage between the California and Québec cap-and-trade programs are fundamentally flawed and do not ensure equitable treatment for covered entities, potentially causing harm to businesses in both jurisdictions. We hope that ARB can work with us in a manner that is reasonable, technically feasible, cost effective, and considers the practical impact of AB32 on jobs, the economy, and the consumer. Please contact me at (210) 345-4620 should you have any questions or need clarifications concerning our comments.

Sincerely,

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