California Air Resources Board Staff
Cap and Trade Program
Sacramento, CA

March 21st 2018

On behalf of the California Environmental Justice Alliance (CEJA) and the Asian Pacific Environmental Network (APEN), we respectfully submit these comments related to the California Air Resources Board (CARB)'s Preliminary Discussion Draft of Potential Changes to the Regulation for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanism ("Discussion Draft"). CEJA is a statewide coalition of grassroots, community-based organizations that represents tens of thousands of low-income communities and communities of color across California. APEN organizes with the Asian Pacific Islander communities in Oakland and Richmond to achieve environmental justice.

Introduction and Summary

CARB's greenhouse gas program should be designed to effectively reduce our state's greenhouse gas emissions to meet the mandates in Senate Bill 32 (SB 32), while analyzing and addressing any disproportionate impacts in our state's disadvantaged communities. CEJA believes the best, and likely only, way to accomplish this is by requiring direct emission reductions and aggressively expanding complimentary climate programs outside of cap and trade. However, given CARB's large reliance on cap and trade for reductions, CEJA and APEN are providing the below recommendations for strengthening the cap and trade program in response to CARB's Discussion Draft.

Whether California achieves our greenhouse gas emission reduction requirements in actual terms is a critical issue for the state's most disadvantaged communities. Environmental justice communities are on the frontlines of climate change.[1] Low-income communities and communities of color are disproportionately located near the state's largest sources of greenhouse gas emissions (GHG), including both industrial facilities and major transportation corridors,[2] as well as oil and gas infrastructure.[3] The communities where CEJA's members and partners work are already facing the impacts of climate change, from suffering most acutely during extreme weather events to bearing the burden of drought or exacerbated air quality impacts. Minimizing further climate change is critical to the long-term health and well-being of low-income communities and communities of color across the state.

Additionally, there are ongoing concerns that as designed, California's cap and trade program will have disproportionate impacts on environmental justice communities. If sources are not reducing their actual emissions because of cap and trade design features such as an

[1] *See* SB 32, Section 1(c) (2016) (describing how disadvantaged communities "are affected first, and, most frequently, by the adverse impacts of climate change").
[2] *See* L. Cushing, et. al, *A Preliminary Environmental Equity Assessment of California's Cap-and-Trade Program*, pg. 2, 4, 5.
[3] *See generally id.*

oversupply of allowances, allowance banking, and offsets, it directly impacts disadvantaged communities – both in terms of localized GHG and co-pollutant emissions, and our state's overall ability to aggressively curb GHG's and thus slow climate change.

Recent data underscores the need for continued analysis and action on these EJ concerns. The 2016 Cushing et. al Report highlighted preliminary findings that showed emission increases in certain sectors under the cap and trade program.[4] The 2016 cap and trade compliance data also showed similar patterns: certain sectors, such as refineries, have actually increased emissions.[5]

While CARB is relying heavily on implementation of AB 617 to address air quality issues in EJ communities, it still has a clear statutory authority to analyze EJ impacts within the cap and trade program and take corrective actions if disproportionate impacts continue to be documented. AB 398 requires CARB to "[e]nsure that activities undertaken to comply with the regulations do not disproportionately impact low-income communities."[6] SB 32 further requires CARB to "achieve the state's most stringent greenhouse gas reductions in a manner that benefits the state's most disadvantaged communities."[7]

In sum, whether California actually achieves our GHG reduction goals, and where those reductions take place, is a critical environmental and climate justice issue that needs to be thoughtfully addressed. To do this, in response to questions raised in the Discussion Draft, CEJA recommends changes to strengthen the cap and trade requirements, as discussed below.

(1) The Regulations Should Require that the State Meet Annual Targets, Not Solely the 2030 Target.

CEJA recommends that the regulations require the State to meet annual targets, not solely the 2030 target. A focus solely on 2030 would not provide sufficient oversight to ensure the SB 32 requirements are met. This is especially relevant given the current oversupply of the market, discussed below.

To best ensure compliance with SB 32, entities should be required to comply with the cap each year. An annual compliance period is important for several reasons. Initially, it helps ensure that entities are making efforts to comply with GHG requirements every year and exploring ways to directly reduce emissions and reduces potential for procrastination. In addition, an annual compliance period increases transparency of process and allows for the public to see how entities are complying with cap and trade year to year. Finally, an annual compliance period is likely to lead to greater overall reductions and may smooth out emissions from year to year.

Notably, other programs with a market-based system require compliance every year. For example, EPA's Acid Rain requires each source to hold allowances equal to the amount of its

[4] L. Cushing, et. al, *A Preliminary Environmental Equity Assessment of California's Cap-and-Trade Program* (2016).
[5] https://calmatters.org/articles/californias-emissions-dip-climate-policies-get-less-credit-weather/?utm_source=CALmatters+Newsletter&utm_campaign=fdcb7a06db-RSS_WEELKY_SUB_EMAIL&utm_medium=email&utm_term=0_faa7be558d-fdcb7a06db-150198313
[6] Cal. Health & Safety Code § 38562(b)(2). This provision is not limited to economic impacts, which CARB analyzes in Appendix E. As written, it includes all potential impacts including environmental impacts.
[7] Senate Bill 32, Section 1(d) (Pavley, 2016).

emissions each year or during ozone season.[8] In other words, the compliance period is either an annual period or a seasonal period. In addition, the European Union Emissions Trading System requires companies to surrender enough allowances to cover all its annual emissions, otherwise fines are imposed.[9]

At the very least, the cap and trade requirements should not have compliance periods any longer than 2 years, similar to the first compliance period from 2013-2014. For all these reasons, CEJA urges CARB to require compliance with the cap and trade regulations on an annual basis.

(2) The Price Signal Should Prioritize Early Action.

CEJA recommends that the price signal be set to prioritize early action. Early action will be essential for meeting our climate requirements and protecting disadvantaged communities, and early action can lead to greater reductions overall. As SB 32 states:

> Continuing to reduce greenhouse gas emissions is critical for the protection of all areas of the state, but especially for the state's most disadvantaged communities, as those communities are affected first, and, most frequently, by the adverse impacts of climate change, including an increased frequency of extreme weather events, such as drought, heat, and flooding. The state's most disadvantaged communities also are disproportionately impacted by the deleterious effects of climate change on public health.[10]

SB 32 further provides that CARB "shall achieve the state's more stringent greenhouse gas emission reductions in a manner that benefits the state's most disadvantaged communities." One way to best protect disadvantaged communities is to set a price signal that will motivate early reductions. Without a high price signal, it is unlikely that Cap and trade, by itself, will change greenhouse gas emissions, especially in the early years.

In addition, a high price signal is consistent with the trajectory that the state has set for itself. SB 32 requires that greenhouse gas levels are reduced to "*at least* 40 percent below the statewide" GHG level from 1990.[11] In addition, Executive Order S-03-05 requires the State to achieve 80 percent below 1990 greenhouse gas levels in 2050. The greenhouse gas reduction path mandated by these authorities does not impose an artificial stopping point at the SB 32 mandate, but rather directs state agencies to fundamentally change the our state into one that does not rely on fossil fuels.

A higher price signal is also consistent with requirements for CARB to consider the social cost of carbon. When establishing the price ceiling, CARB is required to consider, among other things: "[t]he full social cost associated with emitting a metric ton of greenhouse gases."[12] Therefore, CARB is correctly considering that the "[a]cademic study that found the existing social cost of carbon is too low and could be closer to $220 ($2015)."[13] Given this, the value of $150 in 2030

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[8] *See* https://www3.epa.gov/airmarkets/progress/reports/index.html
[9] *See* https://ec.europa.eu/clima/policies/ets_en
[10] SB 32 (2016).
[11] *See* Cal. Health & Safety Code § 38566.
[12] Section 4, AB 398.
[13] https://www.arb.ca.gov/cc/capandtrade/meetings/20180302/ct_workshop_3-1-18.pdf at Slide 14.

may very well be too low.[14] CARB should maintain the high end of the proposed price ceiling in 2030 and conduct additional economic modeling with independent experts.

(3) CARB should take early and transparent action to identify allowance oversupply issues.

We strongly recommend that CARB use a transparent process to take early action in reducing the current overallocation of allowances in the cap and trade market, including creating requirements to retire pre-2021 banked allowances after 2020. The current oversupply of allowances has been documented by multiple analyses. An analysis conducted by Energy Innovation found that an estimated "cumulative oversupply through 2020 for the combined WCI market at 270 million metric tons (MMT) with an uncertainty interval of 200-340 MMT."[15] The Legislative Analyst's Office has shared a similar analysis.[16]

Overallocation and oversupply of allowances will hinder California's ability to achieve its SB 32 mandate, as many legislative and independent analyses have shown. As the Senate Environmental Quality committee stated in their July 12th analysis, "When there is overallocation cap-and-trade ceases to be an effective tool as the allowances replace the need to reduce emissions."[17] The analysis further found that:

> Allowing for an overreliance on allowances and offsets results in delays of true emission reductions. If ARB focuses on cumulative reductions in the Scoping Plan and cap-and-trade design processes, oversupply and banking will lead to delays in control measures being adopted, ultimately resulting in statewide emissions being substantially above the target in 2030.[18]

AB 398 requires CARB to: "[e]valuate and address concerns related to overallocation in the state board's determination of the number of available allowances for years 2021 to 2030, inclusive, as appropriate."[19] We have yet to see a substantive proposal from CARB to address the well-established overallocation concerns, as directed in AB 398. CARB should develop such a proposal, which should include establishing requirements for the retirement of pre-2021 banked allowances after 2020.

(4) CARB should retire additional allowances, rather than include them reserve tiers.

CEJA recommends that no additional allowances should be put into reserve tiers or the Allowance Containment Price Reserve. In the Discussion Draft and the Staff's March 2, 2018 presentation, staff requests additional comments on whether it would be appropriate to distribute additional allowances.[20] With the already existing overallocation, adding new allowances would only exacerbate the challenges to achieving annual emission targets. Therefore we recommend that no additional allowances be put on the market.

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[14] https://www.arb.ca.gov/cc/capandtrade/meetings/20180302/ct_workshop_3-1-18.pdf at Slide 14.
[15] http://energyinnovation.org/wp-content/uploads/2018/02/WCI-oversupply-grows-February-update.pdf at p. 3.
[16] July 12, 2017 Senate Environmental Quality Analysis (citing LAO letter).
[17] July 12, 2017 Senate Environmental Quality Analysis.
[18] July 12, 2017 AB 398, Analysis from the Senate Environmental Quality, available at https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201720180AB398.
[19] Cal. Health & Safety Code § 38562(c)(2)(D).
[20] *See* March 1, 2018 Presentation, Slides 20-21.

(5) The IAF Should Not Be Adjusted to a Higher Level from 2018-2020.

CARB proposes to adjust the industrial assistance factor from 2018-2020. CEJA is strongly opposed to this recommendation, and requests that CARB does not adjust the 2018-2020 emission factors for several reasons.

AB 398 does not require this adjustment. In fact, AB 398 only provides direction to assistance factors commencing in 2021. Specifically, AB 398 requires CARB to:

> Set industry assistance factors for allowance allocation commencing in 2021 at the levels applicable in the compliance period of 2015 to 2017, inclusive. The state board shall apply a declining cap adjustment factor to the industry allocation equivalent to the overall statewide emissions declining cap using the methodology from the compliance period of 2015 to 2017, inclusive.[21]

Resetting the 2018-2020 assistance factors is not required by this statutory language, and it is inconsistent with previous CARB determinations that the assistance factors could be decreased. Industry has been aware of decreasing industrial assistance factors for the 2018-2020 compliance period for years. CARB has provided no concrete or substantive rationale for why the proposed IAF increase is needed, citing only the need for a "smooth market," with no supporting analysis.

In addition, reducing the industrial assistance is an important way to ensure greater compliance with AB 197 and ensuring that the cap and trade program does not exacerbate environmental justice issues. In recent years, the total amount of free allowances has been nearly half of all the allowances.[22] If CARB continues to give away the majority of allowances under this program, it will undermine the state's ability to prioritize direct emission reductions as mandated in AB 197. Furthermore, since a majority of facilities covered by cap and trade are located in disadvantaged communities,[23] the allocation of IAF's has a direct impact on disproportionately burdened communities. By increasing IAFs, it is contrary to the mandate of AB 197, which directs CARB to prioritize direct emission reductions in overburdened communities.

(6) ARB Needs a Tighter Definition of Environmental Benefits Related to Offsets.

As Staff correctly notes, AB 398 requires that "no more than one-half [of offsets] may be sourced from projects that do not provide direct environmental benefits in the state."[24] AB 398 further defines "direct environmental benefits in the state" ("DEBS") as "the reduction or avoidance of emissions of any air pollutant in the state or the reduction or avoidance of any pollutant that could have an adverse impact on waters of the state."[25]

As the Assembly Floor Analysis notes, questions have arisen for "how offsets, particularly from sources outside the state, might meet AB 32's. . . requirements or otherwise produce benefits in

[21] Cal. Health & Safety Code § 38562(c)(2)(G).
[22] For example, in 2016, the total free allowances was 192,960,667 with a 4,781,633 true-up value, while the total allowances in 2016 was 382.4 million.
[23] L. Cushing, et. al, *A Preliminary Environmental Equity Assessment of California's Cap-and-Trade Program* (2016).
[24] Cal. Health & Safety Code § 38562(c)(2)(E).
[25] Cal. Health & Safety Code § 38562(c)(2)(E).

California."[26] Given these concerns, it is not surprising that the statutory language in AB 398 was intended to "[d]evelop approaches to increase offset projects in the state. . . .".[27] Notably, the Senate Floor Analysis states that AB 398 "[r]equires 50% of all offsets to be in California."[28]

CARB staff proposes to use the same statutory definition of DEBS in their rule-making, and also create a process by which individual projects could provide additional information to show that their out of state project has DEBS for California.[29] The proposed process should be rejected as vague and inconsistent with the language of the statute; it will conceivably create a loophole by which nearly all offsets could qualify. It is also opaque in its compliance with the legislative direction provided by AB 398, which clearly requires an avoidance or reduction of air pollution in the state or the avoidance or reduction of a pollutant impacting the state's waters.

It should be noted that just because an offset project is located in-state, it does not necessarily have DEBS to California. An example would be projects under the Ozone Depleting Substances protocol – destruction of these materials in state would provide no real environmental benefits to California, even though a facility may be located in state.

CARB staff should also clarify that net avoided GHG emissions cannot be used be used to qualify as a DEB. Offsets do not result in net climate benefits; for every offset, CARB issues credits that are eventually used by emitters. Offsets are an inherently indirect way of saving GHGs. It is contrary to legislative intent and introduces extreme environmental uncertainty into the program to create a pathway whereby indirect mechanisms can be qualified as having "direct benefits." It is also in contradiction of the AB 32 definition of "direct emission reduction," which states that: ""Direct emission reduction" means a greenhouse gas emission reduction action made by a greenhouse gas emission source at that source."[30] Creating such a definition and pathway could have negative repercussions on other proceedings at CARB, such as AB 197 implementation. Thus, under the proposed definition of a DEB, "any air pollutant" should clearly be identified pollutants outside of GHGs.

(7) General Comments

According to the Final 2030 Scoping Plan, the cap and trade market will have to achieve 43 percent of the total reductions needed to achieve the 2030 target. In CEJA's comment letter on the 2030 Final Scoping Plan, we note that there has yet to be clear analysis to show how the cap and trade market will achieve the additional reductions, how new prescriptions may or may not necessitate changes in market design, nor what other measures might be needed if the market cannot achieve the emissions outlined. We encourage CARB to model how different design scenarios for the cap and trade market will impact California's ability to meet the 2030 emission reduction goals. This should include, but is not limited to, modeling various pricing options, including the price ceiling, price floor and price containment points, strategies to

[26] AB 398 July 2017 Assembly Floor Analysis, p. 7-8.
[27] AB 398 July 2017 Assembly Floor Analysis, p. 2; see also July 2017 AB 398 Senate Floor Analysis (stating that AB 398 "[r]equires ARB to develop approaches to increase offset projects in the state. . . .").
[28] July 2017 AB 398 Senate Floor Analysis, p. 5.
[29] Discussion Draft, pp. 18-19.

[30] AB 32, Chapter 3, section 38505

addressing the issue of overallocation, and what the impacts by sector will be on actual emission trends.

Given the significant work the cap and trade market is expected to do, we urge CARB to continue developing additional complimentary emission reduction policies and programs. This will help reduce the pressure on the cap and trade market, and it would also help achieve more clear compliance with AB 197, which requires prioritization of direct emission reductions. It would also help CARB develop a more clear regulatory path to reducing vehicle emissions, also needed to achieve environmental justice as well as meet our 2030 targets.

Finally, we recommend CARB identify a clear process to identify possible mechanisms to reduce fossil fuel production in California to achieve our 2030 and 2050 GHG reduction targets. When it adopted the 2030 Scoping Plan, CARB also resolved to "continue to evaluate and explore opportunities to achieve significant cuts in greenhouse gas emissions from all sources, including supply-side opportunities to reduce production of energy sources." CARB has yet to clearly outline what such a process will entail, but this will be a critical step to ensuring that our state has the needed policies in place to meet our 2030 and 2050 GHG reduction goals.

We appreciate the opportunity to submit these comments. We look forward to working with the CARB staff in achieving our shared goals of environmental justice, improved air quality, and meeting our climate change goals.

Sincerely,

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