

Coalition for Sustainable Cement Manufacturing & Environment

1107 9th Street, Suite 930 | Sacramento, CA 95814 | (916) 447-9884

April 10, 2018

Ms. Mary Nichols
Chair
California Air Resources Board
1001 "I" Street
Post Office Box 2815
Sacramento, California 95812

Subject: Comments on the Establishment of the Cap Adjustment Factor under the Post-2020 Cap-and-Trade Program

Dear Chairman Nichols:

The Coalition for Sustainable Cement Manufacturing and Environment ("CSCME"), a coalition of all five cement manufacturers in California,¹ provides these comments regarding the California Air Resources Board's ("CARB's") establishment of cap adjustment factors ("CAFs") for the post-2020 Cap-and-Trade Program. In particular, these comments address the requirements under AB 398 and CARB's Preliminary Discussion Draft of Potential Changes to the Regulation for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms ("PDD").

AB 398 directs CARB to "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." According to CARB:

The criteria that CARB originally set in considering sector eligibility for the alternate cap adjustment factors are as follows: over 50 percent of total emissions are from process emissions; the sector has a high leakage risk classification; and the sector has high emissions intensity, defined as 5,000 MTCO₂e per million dollars value added.

In its PDD, CARB indicated that it will "continue to evaluate whether alternate cap adjustment factors for these sectors are appropriate post-2020." CARB also stated that "{s}taff plans to work with affected sectors to gather new data for use in calculating, if necessary, post-2020 alternate cap adjustment factors." CARB's statements regarding whether alternate CAFs are appropriate to certain sectors and calculating if necessary post-2020 alternate CAFs not only directly contradicts the plain language of AB 398, but sidesteps the critical issue of how alternate CAFs will be set to achieve fundamental obligations under AB 32 – in particular, minimizing leakage.

CSCME believes that alternate CAFs are not only appropriate, but necessary to minimize leakage in certain industries. Allowance allocation is likely to remain CARB's primary tool for minimizing leakage for the

¹ The Coalition includes CalPortland Company, Cemex, Inc., Lehigh Southwest Cement Company, Mitsubishi Cement Corporation, and National Cement Company of California Inc. There are ten cement plants located in California, eight of which are currently operating.

foreseeable future, and an industry's CAF is a critical determinant of its allowance allocation rate. An industry with a high leakage risk not only merits a high assistance factor, but also merits special consideration when it comes to the design and application of a CAF. In short, the question of "whether" such industries should receive alternate CAFs has already been answered by both the plain language of AB 398 and the fundamental rationale that underpins CARB's approach to minimizing leakage.

The critical question is not "whether" but "how" CARB will use the upcoming regulatory development process to refresh its approach to alternate CAFs so that it more closely aligns with the objective of minimizing leakage. Although CSCME endorses CARB's basic approach to establishing alternate CAFs, we believe that there are opportunities to refine and improve upon that approach for the post-2020 program. Specifically, we recommend that CARB take three steps to improve the approach used for establishing post-2020 alternate CAFs for certain industries.

(1) Use Best Available Data to Establish CAFs

An industry's eligibility for an alternate CAF is determined, in part, by the ratio of process emissions to total emissions. However, an industry's process emissions share can change substantially over time, especially if it systematically reduces its combustion-related emissions (consistent with the goals of the Cap-and-Trade Program). Accordingly, CSCME recommends that CARB refresh its process emission share calculations using more recent data as part of its establishment of alternate CAFs.

(2) Make an Industry's CAF Proportional to the Share of Process Emissions

As stated by CARB in the PDD, the principle rationale for the current practice of applying alternate cap adjustment factors is that some high-risk sectors also have limited abatement options for reducing GHG emissions due to the presence of process-related emissions. Accordingly, an industry with a higher share of process emissions should receive a more favorable CAF, and vice versa. However, presumably due to data limitations at the time, CARB assigned all industries with more than 50 percent process emissions the same CAF. Now that better data is available, CARB should consider a methodology that scales an industry's CAF to reflect its process emissions share.

(3) Establish CAF Floors Consistent with an Industry's Process Emissions Share

For the post-2020 program, CARB is proposing an overall cap that declines at roughly 4% per year. This aggressive reduction means that the allowance allocation rate will decline substantially for all industries over time, even if they qualify for a high assistance factor and alternate CAF. This raises the possibility that some industries, including but not limited to cement, will eventually receive allowance allocations that begin to approach or fall below those needed to cover their process emissions.

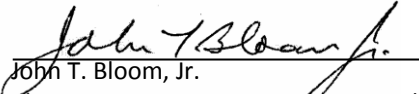
In such instances, these industries would effectively relinquish any ability to positively respond to the program's incentives by reducing emissions that are reasonably within their control. Instead, they will be forced to either curtail production or accept a competitive disadvantage by absorbing the cost of the program – both of which would result in emissions leakage.

Accordingly, CSCME recommends that CARB establish CAF "floors" that reflect the fact that certain industries cannot reduce their GHG footprint below a certain level without causing significant and

unsustainable leakage. These floors would provide owners and investors with the assurance needed to continue operating in California even as the overall allocation rate declines. The floor would presumably be eliminated if and when: (1) an incremental border adjustment is implemented to level the incremental costs of the program between domestic and imported product and/or (2) technology for substantially reducing process emissions (e.g., carbon capture and sequestration) is deemed to be both commercially available and cost-effective at prevailing carbon prices. We recommend that CARB establish clear criteria for monitoring and determining whether either of those objectives have been achieved.

CSCME welcomes the opportunity to provide additional information on the proposed steps set forth above and appreciates CARB's continued diligence in implementing California's Cap-and-Trade Program consistent with the requirements under AB 32, including minimizing leakage.

Sincerely yours,


John T. Bloom, Jr.
Chairman, Executive Committee, Coalition for Sustainable Cement Manufacturing & Environment

CC: *Steven Cliff, California Air Resources Board*
Richard Corey, California Air Resources Board
Rajinder Sahota, California Air Resources Board
Jason Gray, California Air Resources Board
Derek Nixon, California Air Resources Board