COMPRESSED GAS ASSOCIATION
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January 11, 2010

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

Subject: The Compressed Gas Association's Comments regarding Preliminary Draft Regulation for a California Cap and Trade Program

Dear Ms. Nichols:

Thank you for the opportunity to comment on the Preliminary Draft Regulation for a California Cap-and-trade Program. The Compressed Gas Association (CGA) represents over 125 member companies involved in the production and delivery of industrial gases located in the United States, Canada, and around the world. Industrial gases are pure gases such as oxygen, hydrogen, nitrogen, and other specialty gases that are used by industry to make products more efficiently and with less impact on the environment.

CGA is an American National Standards Institute (ANSI) accredited Standards Development Organization with a mission to advance safe and environmentally sound practices in the industry. For almost 100 years, CGA has brought the field's best engineers and scientists together to produce standards that are broadly accepted by the industry and government. CGA's standards have been adopted by the U.S. Occupational Safety and Health Administration, the U.S. Department of Transportation, Transport Canada, Health Canada, as well as domestic and international fire and building code organizations. CGA also supports the United States delegation in the development of United Nations model regulations affecting the safe use and transport of hazardous materials.

The industrial gases industry helps manufacturers improve productivity and efficiency in cleaner, more environmentally sound ways, thereby strengthening overall economic and environmental competitiveness. Consequently, CGA believes the industrial gases industry can and should play an instrumental role in meeting the goals of A.B. 32 through the application of existing technologies and the development and adoption of new technologies to ensure the competitiveness of industries as we transition to a carbon-constrained world.

There is no question that the industrial gases industry is energy intensive (around 70% of the variable cost of producing industrial gases is energy), however, the products are of relatively low cost and cannot be economically distributed long distances. As such, industrial gases are generally produced locally and are not considered trade intensive.

Potential for Market Distortions

The business model of industrial gases companies is based on the use of gases in a wide range of applications and industries, combined with the efficient aggregation of demand and the out-sourcing of production by the end user. Many industrial gas production facilities are physically located at the customer site and integrated with their industrial processes. In fact, CGA member companies operate many such on-site facilities within the State of California.

Under a Cap-and-Trade program, the potential for market distortions exists because large consumers of industrial gases can produce industrial gases themselves or purchase gases from an industrial gases supplier.   This creates a unique situation in which the industrial gases producer is competing with the economics of self-production by its customers, in addition to competition from other industrial gas suppliers. Often, customers operate industrial gases production facilities and purchase from third parties at the same facility. Through a model of aggregation and economies of scale, and efficiency, industrial gas producers have been able to compete successfully with these less efficient internal production options.

Market distortions will occur between an industrial gases company and its customers if the industrial gases suppliers are required to bear higher costs related to direct or indirect CO2 emissions without receiving the same allocated allowances given to their customers. Such customers would experience a perverse financial incentive to “in-source” the production of the industrial gases needed in their processes resulting in:

- Reduction of economic and carbon-emission efficiencies of the overall supply chain.
- Reduction in the utilization of energy and environmentally efficient industrial gases applications.
- Increased carbon emissions from operating smaller “internal” plants instead of larger third-party multi-customer facilities.
- Increased costs to other industries that currently benefit from aggregation of their industrial gases requirements.

It is important that the industrial gases industry be included in allocation of allowances under the Cap-and-Trade system being developed. Failure to include the industrial gases industry could undermine the intent of the program and result in two unintended consequences:

- First, an unintended and counter-productive incentive is created for the major eligible industries to in-source the production of industrial gases needed for their industrial processes, forsaking the economies of scale created by the industrial gases industry, and resulting in overall decreased efficiency and increased carbon emissions.
- Second, healthcare, food, and manufacturing industries within California would face substantial cost increases for the products supplied by the industrial gases industry.

To protect California consumers and jobs, it is imperative that the industrial gases industry be included in any allocation of allowances to energy intensive or trade exposed industries. We stand ready to work with you to address this important issue.

Respectfully submitted,

Marc J. Meteyer
President and CEO
Compressed Gas Association