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January 11, 2009

**Re: EcoSecurities' Comments on the AB 32 Preliminary Draft Regulation**

Dear Secretary Adams:

On behalf of EcoSecurities, a world leader in the development of greenhouse gas (GHG) emission reduction projects with offices in California, we thank you for the opportunity to comment on the Preliminary Draft Regulation (PDR) for AB 32. We acknowledge that development of this regulation has and will continue to be a significant task, and we applaud you for your diligent work and transparent processes to date. We hope our efforts will contribute to the development of climate policies in California that are environmentally effective and administratively straightforward.

Our comments focus on four areas of the Preliminary Draft Regulation: the quantitative limits that AB 32 imposes on offsets, offset geographical scope, the offset project eligibility date for additionality, and offset project types.

**1) Quantitative Limits on Offsets**

EcoSecurities believes the existing quantitative offsets limits as outlined in the PDR are too low at their current limit of 4%. EcoSecurities opposes quantitative offset limits in theory but understands the importance of using offsets as a supplemental tool to reduce emissions occurring at the source of a capped entity. Nevertheless, offsets also play a critical role in reducing overall costs to the economy associated with implementing a cap-and-trade system. We applaud California's perseverance in proceeding with the implementation of the nation's first economy-wide cap-and-trade system, especially given the fragile state of the global economy. Given the circumstances, however, we believe it is in the best interest of California to create a cap-and-trade system that promotes the maximum environmental benefits at the lowest costs. The stringent limits that California has proposed for offsets risk undermining the ability of offsets to lower costs and moderate market spikes.

Additionally, the presence of stringent limits on offsets in California is likely to dry up offset supply entirely. As a project developer, EcoSecurities is familiar with the costs to

develop projects under new rules and in new jurisdictions. If the allowable pool of offsets in California is too small, there will be little incentive to build capacity to access it, and capital will flow elsewhere. EcoSecurities would encourage California to expand the allowable use of offsets in the State.

The anticipated environmental benefits of imposing such stringent quantitative offset limits come at a very high cost to California's economy. We believe California could achieve much greater environmental benefits (albeit across a larger geographic region) at a lower cost by allowing more offsets. Having stringent standards will ensure that only additional, high-quality offsets can be used for compliance. High standards will in turn provide a natural limit on the total number of offsets allowed, as a result of market forces. The introduction of such stringent limits undermines the flexibility of the emissions reduction program, unnecessarily increasing overall compliance costs.

Finally, arbitrary quantitative limits reduce the size of the offsets pool, but do nothing to change the proportion of low-quality credits that get through. The objective of reducing emissions would be far better served by holding an unrestricted pool of credits to rigorous standards, thereby increasing the number of high quality offsets representing real emissions reductions. This would enhance the environmental integrity of the system while avoiding harmful perversions of the market.

## **2) Geographical Scope of Offsets**

Limiting offsets geographically constricts their supply, thereby increasing their cost and undermining their ability to function as a cost-containment mechanism. Rather than placing limits on offsets geographically or quantitatively, EcoSecurities would encourage only high quality standards for offsets across the board. This would increase the quality of offsets accepted on the whole, instead of simply shrinking the pool of eligible credits. California could also very easily guarantee that offsets from outside its borders meet the State's rigorous additionality requirements by linking only with other cap-and-trade systems whose offsets and crediting systems meet California's requirements.

## **3) Offset Project Start Date**

EcoSecurities believes that robust offset projects established after January 1, 2001 should be eligible for offset credits under California's cap-and-trade program. According to the Preliminary Draft Regulation a project must have commenced after December 31, 2006 in order to receive offset credits. This arbitrary restriction will prevent a significant number of high-quality offsets from entering an already limited supply pool, thereby driving up the overall costs of the cap-and-trade program.

For the purposes of harmonizing California's cap-and-trade program with other carbon systems, a project start date of January 1, 2001 more closely resembles the eligibility

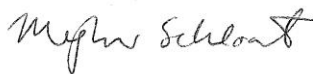
requirements used by a number of respected offset standards. Many of the methodologies under the Climate Action Reserve (CAR) use or have used in the past a project start date of January 1, 2001, while the American Carbon Registry (ACR) uses an even earlier start date of January 1, 2000. We also observe 2001 project start dates imbedded in climate legislation at the federal level. Both the Kerry-Boxer bill and the stand-alone Stabenow bill list a 2001 project start date for early offsets and all offsets, respectively.

#### **4) Offset Project Types**

EcoSecurities believes that ARB should establish an initial “positive list” of pre-approved project types for the California cap-and-trade program. Including such a list would provide a much needed market signal to the offset investment community, and would create greater market certainty by encouraging early emissions reductions from known project categories. In the absence of a positive list, investment in carbon offset projects would stagnate until more project clarity is offered, and offset’s primary purpose of mitigating costs during the early years of the cap-and-trade program would be undermined. A positive list would also be extremely beneficial to offset project developers, who could then begin pursuing emission reductions as soon as possible. In order for offsets to properly serve as a mechanism for cost-containment and allowance price stability, offset project developers must be given forward insight as to the types of projects that will be allowed into the system.

We appreciate the thoughtful consideration of the aforementioned issues by the Air Resources Board, and we look forward to seeing a robust, administratively reasonable offset system constructed by the State of California. If EcoSecurities can provide more detailed information, research, or other guidance with respect to offsets either in person or in writing, we would be happy to do so in the future. Thank you for your attention and for this opportunity to contribute our thoughts on this important process.

Sincerely,



Meghan Schloat  
Manager, U.S. Regulatory Affairs