

COALITION FOR SUSTAINABLE CEMENT MANUFACTURING & ENVIRONMENT
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August 30, 2012

Mr. James Goldstene
Mr. Steve Cliff
California Air Resources Board
1001 "I" Street
Post Office Box 2815
Sacramento, California 95812

Subject: Comments on CARB's Leakage Monitoring And Research Proposals

Dear Mr. Goldstene and Mr. Cliff:

The Coalition for Sustainable Cement Manufacturing and Environment ("CSCME"), a coalition of all six cement manufacturers in California,¹ submits the following comments on the proposal of the California Air Resources Board ("CARB") to develop a leakage monitoring program and conduct leakage-related research. CSCME commends CARB for focusing on leakage at its May 30, 2012 and July 30, 2012 workshops and for recognizing the importance of avoiding leakage resulting from the implementation of AB 32.

Despite CARB's allowance allocation system, the vast majority of industrial facilities will continue to face significant compliance costs throughout the three compliance periods. Absent effective action from CARB, these costs, which are not borne by competitors outside California, may lead to leakage in certain industries. As CARB is aware from CSCME's prior comments, several factors make the California cement industry particularly vulnerable to leakage resulting from the implementation of AB 32, including but not limited to the fact that the greenhouse gas ("GHG") intensity of cement production is far higher than that of all other industries and the extremely limited GHG abatement opportunities available to cement manufacturers.

As a result of our industry's particular vulnerability to leakage, CSCME members are highly motivated to assist CARB in effectively anticipating, identifying, and addressing leakage. These comments are intended to be an initial step in that process, setting forth (1) principles related to program design that CSCME believes are essential to conducting useful leakage research and developing an effective leakage monitoring program, (2) an outline of the type of leakage monitoring program that would likely prove effective across affected industries, and (3) important considerations regarding the confidentiality of data submitted to support CARB's efforts to address leakage.

¹ The Coalition includes CalPortland Company, Cemex, Inc., Lehigh Southwest Cement Company, Mitsubishi Cement Corporation, National Cement Company of California Inc., and Texas Industries, Inc. There are ten cement plants located in California, eight of which are currently operating in the aftermath of the recent recession and uneven economic recovery.

A. PROGRAM DESIGN PRINCIPLES FOR ADDRESSING LEAKAGE

- 1. A one-size-fits-all approach to leakage monitoring or leakage research is likely to be ineffective**

The risk of leakage in a particular industry is highly dependent on a variety of industry-specific factors, including the nature of the product, market structure, trade exposure, investment cycles, and other conditions of competition. Given the complex interaction of these factors, a "one-size-fits-all" approach to leakage monitoring and research is likely to result in a "one-size-fits-none" result. For this reason, CARB's focus should be on obtaining as much information as possible from various industry participants and developing a flexible approach to leakage monitoring and research that allows CARB to work closely with each affected industry to understand their unique characteristics and accurately account for significant differences between industries.

- 2. CARB's approaches to both leakage monitoring and leakage research should recognize the need for predictability**

Given existing regulatory costs within California and the long-term planning that is required in capital-intensive industries such as cement manufacturing, lingering uncertainty regarding future compliance obligations will chill long-term investment in the state. Such uncertainty could influence decisions regarding, among other things, whether to upgrade equipment and where to locate a new or expanded production facility. Accordingly, it is critical that CARB take sufficient action to avoid leakage and give industry participants as much advance notice as possible regarding how it plans to address leakage. In particular, because cement manufacturers are already making decisions relating to production in 2015, CARB should ensure that it is able to effectively prevent leakage during the second compliance period, and should provide as much clarity as possible regarding its plans to do so in order to allow market participants to plan accordingly.

B. BASIC OUTLINE OF LEAKAGE MONITORING PROGRAM DESIGN

With respect to leakage monitoring, time is of the essence. There is likely to be a significant lag between the collection of industry data, analysis of that data, and the decision to implement leakage-preventing measures. Thus, as a practical matter, CARB's measures of leakage are likely to be lagging indicators. The importance of detecting and addressing leakage in real time is heightened by the fact that leakage may result in largely irreversible effects, including plant closures and decisions not to make capital investments to modernize and expand capacity in California. Consequently, a key characteristic of an effective leakage monitoring program is that it promptly identifies likely leakage and promptly responds when leakage has been confirmed.

1. CARB Should Ensure That It Promptly Identifies Instances Of Leakage

We propose that CARB create the following two-step process for identifying and responding to leakage. First, CARB should make preliminary determinations of whether there is a reasonable indication of leakage or imminent threat of leakage based on either (a) ongoing analysis of trends in a discrete list of factors or (b) consideration of industry petitions. Second, where CARB has made a preliminary determination that there is a reasonable indication of leakage or imminent threat of leakage, CARB should immediately release allowances to affected producers in order to minimize the impact of any leakage. Such determination should also trigger a full leakage investigation that considers more detailed information for a longer period and considers input from interested parties in order to make a final determination of whether leakage is occurring or is imminent. If CARB determines that leakage is not occurring or imminent, the recipient would return the allowances to CARB.

Notably, CARB does not have to develop this type of investigation process from scratch. The U.S. International Trade Commission ("ITC") has developed factors and methodologies to determine whether a domestic industry is materially injured or threatened with material injury by reason of dumped or subsidized imports. Such factors and methodologies could inform CARB's assessment of whether lower-priced imports (resulting from the avoidance of AB 32 compliance costs) are causing or threatening imminent leakage to the California cement industry. CSCME is still completing its analysis of which factors considered by the ITC are most relevant for leakage purposes, but we believe that the ITC's work and methodologies will be valuable resources as CARB develops a system like the one proposed below for identifying and responding to instances of leakage.

a. CARB should develop a short list of economic indicators of leakage that can be monitored continuously

As stated above, time is of the essence regarding both CARB's collection of data indicating leakage and CARB's response to indications of likely leakage. Due to this time sensitivity, CARB should ensure that its leakage monitoring process is as simple as possible so that it makes preliminary leakage determinations promptly. This can be accomplished by identifying the most relevant economic factors to monitor on a continuous basis. This list of factors to monitor continuously should be kept to a manageable size and should preferably include only factors for which data are publicly and timely available to CARB and that companies are otherwise required to report to local, state, or federal government agencies.

In developing this brief list of factors, CARB should keep in mind that this is only an initial test for likely leakage. As a result, the objective should not be to develop a perfectly comprehensive set of factors to analyze, but instead to identify a short list of factors that companies can reliably, inexpensively report in a timely manner and that CARB can process and analyze in a short period of time. In addition to saving time, this approach will prevent unnecessary expense and alleviate some data confidentiality concerns that might exist if CARB instead requested ongoing reporting of a broad set of data.

- b. CARB should develop a historical baseline for each factor it monitors for each industry so that likely leakage will automatically be identified if those indicators reach certain levels**

CARB's preliminary investigation of leakage monitoring data should be swift and decisive. The best way to ensure this is to develop baselines for each of the monitored factors for each industry. Such baselines would be based on historical relationships between the most salient data points (e.g., production, import market share). As soon as one of the key factors rises above the expected divergence from the baseline level, CARB staff would closely monitor that factor. If such a trend continued for a certain period of time, CARB would automatically make a preliminary determination of a reasonable indication of leakage or imminent threat of leakage.

- c. CARB should also create a petition process that would allow California industries to establish a reasonable indication of leakage or imminent threat of leakage**

It is possible that a simple monitoring system would fail to detect all instances of leakage. To account for this possibility, CARB should also create a petition process through which California industries could provide data and information to CARB showing a reasonable indication of leakage or imminent threat of leakage. This petition process would allow CARB to keep its standard monitoring system simple while also ensuring that CARB can receive and consider broader information from California industries about apparent leakage that is not captured by the monitoring system. Industry participants are well placed to identify the impact of imports from unregulated or less regulated jurisdictions on their own economic positions.

As with the standard monitoring process, CARB's analysis of industry petitions should be swift and decisive. Although judgment will be required to weigh data related to a wide variety of relevant factors, CARB should set a short timeframe within which it must consider a petition and make a preliminary determination. If the preliminary determination is negative, that would end the investigation. If the preliminary determination is affirmative, CARB would promptly initiate a full investigation. Recognizing that a full investigation is still to come, the intent of a preliminary investigation should be to determine whether the industry has presented evidence showing a reasonable indication of leakage or an imminent threat of leakage. The ITC's procedures for preliminary and final injury investigations in antidumping and countervailing duty cases could provide a useful template for CARB's preliminary and final leakage investigations.

- d. Affirmative preliminary determinations of leakage or imminent threat of leakage should automatically be followed by a full leakage investigation**

Every preliminary determination of leakage or imminent threat of leakage, whether through the standard monitoring system or the industry petition process, should then be followed by a more extensive full leakage investigation intended to accomplish at least three things: (1) provide an

additional period of time for CARB to collect and analyze data and receive input from interest parties; (2) allow time for consideration of a broader set of factors and associated data trends; and (3) provide an opportunity to conduct a more comprehensive objective assessment of whether leakage is occurring or is likely to occur absent CARB's intervention.

2. CARB's Response To Identified Instances Of Leakage Should Be Automatic And Effective

- a. A reasonable indication of leakage or imminent threat of leakage should automatically result in CARB releasing additional allowances to California producers in the affected industry**

CARB's leakage monitoring program will only be effective if it results in prompt action to counteract identified leakage. Thus, as soon as likely leakage is identified through one of the two processes discussed above, adequate allowances should be released to affected California producers in the relevant industry. The prompt release of these allowances should give California producers confidence that adequate allowances are available to address any actual leakage promptly and adequately and to mitigate the risks of further leakage going forward.

- b. After a full leakage investigation is complete, the additional allowances should be either kept by the affected producers or returned to CARB**

As discussed above, CARB (or a body it designates) would conduct the full investigation. At the conclusion of the investigation, a decision would be made on whether leakage is occurring or is imminent. If such an affirmative finding is made, the allowances that were released would be kept by producers in the affected California industry. If the full investigation resulted in a finding of no leakage or imminent threat of leakage, the allowances would instead be returned to CARB.

C. LEAKAGE MONITORING DATA CONSIDERATIONS

1. Data Confidentiality

At its May 30 workshop, CARB stated that it will ensure that any leakage monitoring data will be maintained as confidential. At its July 30 workshop, CARB referenced California Code of Regulations sections 91000-91022 and U.S. Census methods for handling confidential data but did not otherwise specify how it will ensure confidentiality of sensitive data submitted to support leakage monitoring efforts. If data are required for each individual facility, as CARB has proposed, confidentiality is essential. CSCME has commented regularly during the development of several regulations under AB 32 about the particular importance of data confidentiality in the cement industry due, in part, to the fact that emissions and energy efficiency data can reveal sensitive information about the cost of production at a given plant. CSCME reiterates these concerns and looks forward to working with CARB to ensure

that only necessary data are collected for leakage monitoring and that essential controls are in place to ensure absolute confidentiality of these data.

2. Ensuring Data Are Only Used For Leakage Monitoring

Any data submitted as part of CARB's leakage monitoring program should only be used for leakage monitoring. CARB's leakage monitoring program should be narrowly focused on leakage issues and should be designed to allow CARB to identify leakage promptly, analyzing leakage issues as directly as possible. Such an approach, including a well-defined "ring fence" around the data within CARB, should prevent the collection of unnecessary data and minimize the potential for inadvertent and highly damaging disclosures.

3. Enforcement And Verification Provisions

CARB officials stated at the May 30 workshop that they have not yet determined whether submission of leakage monitoring data will be mandatory or voluntary. CARB staff added, though, that it might be difficult to obtain adequate data if submission of leakage monitoring data were voluntary. CSCME considers that more information is needed about the structure and scope of the program and the associated data requirements before assessing the nature of any data reporting obligations.

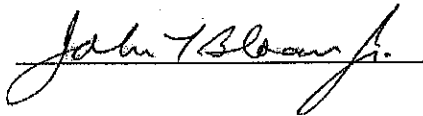
In any event, CARB should ensure that any related enforcement and verification provisions strike an appropriate balance of ensuring the reliability of submitted data without imposing egregious penalties for inadvertent and/or minor reporting errors. Importantly, the entire reason for leakage monitoring is to identify and avoid negative effects resulting from costs imposed by AB 32 on California producers but not on competitors outside the state. It would therefore be counterproductive to impose additional costs on California producers through excessive reporting, enforcement and verification provisions related to leakage monitoring.

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D. CONCLUSION

As stated above, CSCME commends CARB for recognizing the continuing risk of leakage, particularly in the cement industry. To address this challenge, we look forward to assisting CARB in developing effective leakage research and leakage monitoring programs that address the important concerns outlined above.

Sincerely yours,

A handwritten signature in cursive script, reading "John T. Bloom, Jr.", written over a horizontal line.

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