To: Kevin Kennedy, CARB Office of Climate Change

From: Shelly Sullivan, Executive Director

Subject: AB 32 Implementation Group Comments – 'Update on Offsets and Linkage in a California Cap-and-Trade Program' Workshop -- June 22, 2010

Date: July 13, 2010

The AB 32 Implementation Group is a coalition of business and taxpayer groups advocating for AB 32 regulations and policies that will support a growing and healthy California economy.

We appreciate the opportunity to comment on the proposals for cost containment and offset policy during the June 22 workshop.

Cost Containment

The June 22 workshop introduced concepts for cost containment and offsets in the cap-and-trade program. The topics are vitally important - AB 32 itself directs CARB to minimize leakage, maximize cost-effectiveness and ensure technological feasibility. A failure to satisfy these goals could threaten success of the program, both on the environmental front through leakage of emissions to other states, regions and countries, and on the economic front through declining private investments and reduced employment.

The first step to containing costs and achieving environmental goals should be achieved through the design of the program. Making the right decisions about market design issues to avoid high prices, including offset policies, is the first and best cost-containment approach. But we also need mechanisms that will operate when necessary to ensure that affordable allowances will be always be available for current operations and expansions in California. The reserve function outlined in the workshop could provide this assurance.

We note the observation in the Analysis Group comments that the marginal cost abatement curves are significantly uncertain and that the curve rises steeply as the quality of emission reduction needed to meet emission targets increase. To tame a market that may rapidly rise out of acceptable bounds, a robust reserve should include all possible options, including borrowing and using offsets to fill the account. Since the market will respond to the prospect of future shortages in the case of borrowing, truly increasing the supply of allowances through the use of offsets is a necessary solution. The less likely the reserve will be needed, and the more effectively investors anticipate it will operate, the more likely they will make long term capital commitments and hiring in the state.

Offsets

We urge CARB to adopt a policy to broadly allow the use of offsets from the very beginning of the program. A 4% limit is unacceptably low. Governor Schwarzenegger urged in his March 24 letter to CARB Chair Mary Nichols that we should have an "ample supply of high quality offsets" available in the program. By this, we believe the Governor was directing CARB to revisit the unnecessarily restrictive 4% quantitative limit on the use of offsets. The cost containment potential for the broad use of offsets is undeniable, and we should be encouraging development of a healthy offset development market in the state. Strict limits will dampen enthusiasm and investment in these valuable and innovative projects.

Given that climate change is a global challenge requiring a global solution, it is critical that a global, fungible market for high-quality offsets emerges. CARB's suggestion that they would need to approve all offset credits would result in a very restrictive, de-facto geographic limit on offsets. Staff also discussed a number of requirements for offset project approval, including requiring "regulatory additionality" and "substantial co-benefits" in order for certain offset credits to be accepted.

We are concerned about CARB's thinking that offset projects should be limited to projects in California and elsewhere in North America where these projects have not been developed under any other accepted protocols. Adding or imposing California-only requirements will result in fewer offsets available for use in California and will make it less likely that California could link with other programs unwilling to accept these restrictive requirements. It would also add the unintended consequence of substantial leakage. CARB should agree to accept credits (that can be periodically audited) from existing programs that are widely accepted elsewhere in the world.

Thank you for allowing us to comment on the June 22, 2010 'Update on Offsets and Linkage in a California Cap-and-Trade Program' workshop. We look forward to attending and participating in additional workshops to ensure California's cap-and-trade market system is developed in a way that protects California's consumers and businesses while achieving the greenhouse gas emission reduction goals set forth in AB 32.

Should you have any questions, please feel free to contact me at (916) 858-8686.

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