



Western States Petroleum Association
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Catherine H. Reheis-Boyd
Executive Vice President and COO

November 19, 2008

Ms. Mary Nichols, Chair
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Subject: **AB 32 Implementation – Proposed Scoping Plan**

Dear Ms. Nichols:

The Western States Petroleum Association (WSPA) is pleased to submit the following comments regarding the AB 32 Proposed Scoping Plan. The Plan will be discussed at the Air Resources Board hearing on November 20, 2008 for adoption at the Board meeting in December.

WSPA is a non-profit trade association representing twenty-seven companies that explore for, produce, refine, transport and market petroleum, petroleum products, natural gas and other energy supplies in California and five other western states.

WSPA member companies own and operate facilities that include oil and gas production properties, refineries, marketing terminals, pipelines and retail gasoline outlets. They produce fuels and other products that will all be impacted by the implementation of AB 32.

It has been nearly two years since CARB staff held the first Scoping Plan workshop on January 22, 2007. At that time and throughout the process, WSPA has been committed to engage constructively with ARB and other stakeholders to ensure the successful implementation of AB 32 in accordance both with its terms and with all other applicable California and federal laws.

Throughout the Scoping Plan development process, WSPA also has consistently stated that successful implementation of AB 32 requires embracing several key program elements. These include: efficiency; sound science; cost-effectiveness; technological feasibility; fairness and equity; stimulation, innovation and investments; adequacy, reliability and affordability of fuels; and, protection of the economy and the environment.

In particular, WSPA believes the Board should acknowledge the importance of ensuring that adequate, reliable and affordable energy supplies are available to consumers while the State moves to a low carbon future. We believe this can best be accomplished by working with the California Energy Commission (CEC) to ensure California's energy demands are being met as the scoping plan is fully implemented.

Using this approach will give consumers comfort that as AB 32 is implemented, they will still be able to turn their lights on, heat and cool their homes and drive where they need to go, even if the form of transportation evolves over time.

The proposed Scoping Plan being reviewed on November 20th contains a complex menu of proposed measures that includes a potentially workable cap and trade instrument, plus so-called “complementary” command and control measures and performance standards. Most of the measures are also interrelated and have the potential to be overlapping and/or conflicting.

Petroleum industry facilities and products are covered by a number of programs and measures, including for example: the cap and trade program; proposed specific control measures at oil fields and refineries; the LCFS for transportation fuels; and potentially local regulatory programs, including local applications of the California Environmental Quality Act (CEQA).

In addition, other California agencies are working on related programs that ARB anticipates will work in conjunction with or in a complementary manner with the Scoping Plan measures. For example, the CPUC is working on a RPS for alternative electricity generation and other initiatives, like a solar roofs program.

The CEC and ARB are developing regulations to implement the AB 118 Air Quality Improvement Program that in many areas overlap with the Scoping Plan. WSPA recently submitted comments on this process. We have asked that GHG emission reductions pursuant to the AB 118 program be reflected in the Scoping Plan, taking into account the legal restrictions on the use of reductions generated under the AB 118 Air Quality Improvement Program.

Further, California is committed to participating in the Western Climate Initiative (WCI) with all its potentially conflicting recommendations. Given the complexity of the multiple regulations in the area of climate change, and given the timeline for adoption in 18 months, the task before us is certainly daunting. As WSPA has said in many previous comments, “We must get this right, there is too much at stake to get it wrong.”

Therefore, we urge the Board to develop and publish a detailed, written and public work plan for adoption of priority regulations. If industry is to implement and comply with forthcoming rules to implement the Scoping Plan, it is critical that we all start working to develop, in a systematic manner, all the necessary regulations and policy guidance that must be in place to ensure the timely implementation of the measures that will be needed to achieve GHG reductions. And, everyone must know the schedule for implementation.

The work plan should be an outline and timeline to develop at a minimum the following:

1. Policies to assess cumulative impact of all the regulation on businesses’ capital, resources, etc.;
2. Enforcement provisions such as variances, breakdowns, compliance fees, etc.;
3. Permit facilitation regulations/policies so that GHG reductions can proceed in a timely manner under CEQA and other state and federal laws;

4. Regulations/policies to address unnecessary barriers to GHG objectives such as barriers to the expanded use of CHP;
5. A process to handle conflicts arising from duplicative/conflicting regulations from multiple state, local and federal agencies; and,
6. Policies to support RD&D.

We appreciate that the proposed Scoping Plan includes the potential of a workable cap and trade instrument. As you move forward to develop the details of a cap and trade program, we feel it is important that a well designed cap and trade program must include the following elements:

- It minimizes auctions - ARB should not initially use auctioning as this will create an uneven playing field that will disadvantage industries within California compared to industries in the US and the world. We also believe an auction program requires additional legislative authority since it operates as a tax. WSPA recommends a phase-in approach using reasonably set compliance periods where the allocation methodology and other factors are reviewed and reassessed, as AB 32 implementation progresses through its phased compliance periods.
- The program is designed to be compatible with and link to future regional and federal programs;
- It includes a robust offsets program without geographic or quantity limitations that links to regional, federal and international markets. We believe the offset limitations as described on page 37 of the proposed Scoping Plan are too restrictive, unwarranted and will lead to added and unnecessary costs to California.

Further, we note in the proposed Scoping Plan (Table 5) the emission reductions for the cap and trade program are those needed to reduce from "business as usual" growth to 2020. Yet, as we read Figure 2 on page C-22 of Appendix C, the offset limitations seem to be based on a 2012 baseline. Offset limitations based on a 2012 baseline as opposed to "business as usual" reductions would more severely restrict offsets, making the program even more costly to California. We urge as you move forward, that you clarify the offset limitations are based on the business as usual baseline.

- It is a broad market-based program that minimizes command and control direct regulation of sources under the cap and trade program and allows the market to identify and achieve the lowest cost emission reductions over time. Imposing current command and control regulatory measures on sources already under the cap will not lead to additional emission reductions, only potentially higher cost reductions that lock in current technologies and do not reflect emerging technologies.

Command and control measures should be targeted to those instances where demonstrated market failures occur. Those types of market failures are not likely to occur when the sources under the cap are large energy users like those covered by the proposed Scoping Plan. We urge, as you move to implement the Scoping Plan, that ARB frequently evaluate the technological feasibility and cost-effectiveness of the proposed direct measures.

- Where command and control is used, the program ensures the measures are technologically feasible and cost-effective as required by AB 32. It is important that the cost-effectiveness evaluation and criteria are separate from any co-benefit issues so that one goal does not deter from the other, and that the measures meet the requirements of the Health & Safety

Code, California Administrative Procedures Act, CEQA and other California and federal requirements that may apply to particular topics such as fuels regulation.

WSPA urges that ARB embrace the above principles and elements as it moves to implement the proposed Scoping Plan.

The proposed Scoping Plan includes a significant discussion on auctions and the use of revenues from those auctions. But as noted above, AB 32 does not provide ARB with the authority to impose “carbon fees” beyond those necessary to cover the administrative costs of the program. Therefore, auctions as discussed in the proposed Scoping Plan require additional legislative authority for ARB to assess and raise/allocate/distribute funds generated by such auctions/fees.

The Scoping Plan also includes a number of measures that would apply to petroleum industry facilities, including an energy efficiency assessment requirement. The Plan proposes that these facilities be under the cap and trade program, hence they will have a strong market incentive to improve energy efficiency. We therefore recommend that as you move forward, those measures be re-evaluated as part of, and in light of, the cap and trade regulation.

The Plan also embraces energy efficiency and combined heat and power (CHP). These programs and others will likely require facilities to implement projects that modify facility operations. To ensure efficient and timely implementation of these programs, we urge you direct staff to:

- Work with the CPUC to address and ultimately to remove the economic and regulatory barriers and hurdles for timely implementation of CHP projects;
- Provide CEQA guidance and permit streamlining in implementing the final Scoping Plan for CHP and other implementation projects; and,
- Ensure that the program to implement the local government targets does not duplicate, overlap and double count or conflict with the industrial sector program.

WSPA is encouraged that the plan includes a discussion of carbon capture and storage (CCS) (as is required by AB 32 – H&SC §38561(f)) as we believe CCS is critical to the success of this program. We urge that in implementing the Scoping Plan, ARB should work with the CEC, CDOGGR, US EPA, US DOE, US DOI and others to promote research, develop and demonstrate CCS in California, and ensure that an adequate framework is in place to provide credit for CCS projects when appropriate.

The proposed Scoping Plan envisions the Low Carbon Fuel Standard (LCFS) as a major contributor to achieving the AB 32 emission reduction goal. The LCFS will be a major undertaking requiring the use of breakthrough innovations that have not yet been discovered and/or developed.

Further complicating the fuel situation is the lack of clarity about how California’s LCFS will work with the federal EISA requirements that are now law. As mentioned above, the recently submitted WSPA comments on the implementing regulations for AB 118 highlight the need to have a coordinated and consistent policy for accounting and use of reductions and credits with AB 118, the LCFS and the Scoping Plan (all consistent with legal mandates in AB 118 and AB 32). Please see and consider WSPA’s comments in our November 13, 2008 WSPA letter on the AB 118 program and our November 19, 2008 WSPA letter on the LCFS.

In addition to the LCFS, ARB is proposing the inclusion of transportation fuels in the cap and trade scheme in 2015. Although we understand this proposal is consistent with the WCI – to which California is committed, we strongly urge ARB to carefully assess the pros and cons of including transportation fuels under the cap and trade program, taking into account the other regulatory programs for fuels like the RFS under EISA.

We urge ARB to evaluate other potential mechanisms and the potential overall program design in 2015, before making any final decision on how to additionally handle transportation fuels. The same would apply to the proposal for natural gas.

We also note that WCI committed to study the pros and cons of transportation fuels under the cap and trade program prior to making their recommendation. In fact, the WCI has never conducted that evaluation. WSPA urges the ARB to perform this evaluation before California takes that step on transportation fuels and natural gas. The final implementation of the Scoping Plan must not inhibit or prevent consumer access to adequate, reliable and affordable supplies of energy.

At the June 26 Board hearing, a mandatory five year review and update was highlighted as required by AB 32. We believe this review and update are critical program features allowing all of us to ensure we are on the right track and to make any needed course corrections.

However, there is little in the proposed Scoping Plan about the mandatory review or the criteria for this evaluation. We urge that for the implementation phase, you direct ARB staff to develop and adopt these important criteria for the five year review – especially the criteria for maximum technologically feasible and cost-effective reductions as required by AB 32 and the need for additional economic analysis of the plan as it is being implemented and updated.

There is nothing in the proposed Scoping Plan regarding tracking mechanisms or early indicators that will identify and disclose the effect of the plan on energy supply and its impact on the economy. We recommend that for the implementation phase, you direct ARB staff to develop and adopt such tracking mechanisms or early indicators that will allow ARB to identify needed course corrections on an ongoing basis - the five year review is the minimum required by AB 32.

It will be important for ARB to collaborate with the CEC/CPUC to ensure under the Scoping Plan that adequate, reliable and affordable energy sources and transportation fuels can be maintained.

The AB 32 Implementation Group has provided significant comments and recommendations on the need for a robust, comprehensive and well-designed economic study of the implementation of AB 32. WSPA endorses and supports those comments and urges that as ARB implements the Scoping Plan, an economic analysis be completed and used for decision-making.

We understand the Scoping Plan is a flexible document that ARB will review and can adjust in the future. In particular, we understand ARB has fully retained all of its options to adjust the amount of GHG reductions assigned initially to direct regulation relative to the amount of GHG reductions assigned to a cap-and-trade program.

We strongly urge ARB to exercise its authority to make adjustments like this, as additional economic studies are completed and the staff performs detailed technological feasibility and cost-effectiveness analyses of specific Scoping Plan measures as required by AB 32.

Ultimately, California consumers will be the judge of the program's success. California will still need adequate, reliable and affordable supplies of energy, including electricity, natural gas and transportation fuels. ARB needs to ensure that both goals, of adequate energy supplies and addressing climate change, can be achieved as we move to a lower carbon future.

Thank you for considering our comments. If there are any questions, please do not hesitate to contact me at 916-498-7752.

Sincerely,

A handwritten signature in black ink, reading "Cathi A. Boyd". The signature is written in a cursive style with a large, stylized initial "C".

cc: Linda Adams, CALEPA
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