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

Subject: ConocoPhillips Comments - California Climate Change Draft Scoping Plan

Dear Ms. Nichols,

ConocoPhillips supports the State of California in its effort to advance the goal of environmentally effective and economically efficient climate change policy in the United States. Our hope is that state government efforts to address climate change will hasten the development of a mandatory national framework with international linkages which we believe will be the most effective approach for achieving a meaningful impact on global greenhouse gas emissions.

ConocoPhillips has significant operations in California including oil refineries, crude oil and petroleum product pipelines and terminals, and retail marketing outlets. We are a member of the California Climate Action Registry and started voluntary reporting of our emissions with CY2006. As the third largest US energy company, we also have important operations and investments in other Western Climate Initiative states, throughout the US and worldwide. As such we are keenly interested in the development of California climate policy in its own right and because we believe your efforts will have important implications for the development of climate policy elsewhere in the US and the world. We support the eventual harmonization of state-level policy with national and international climate frameworks.

ConocoPhillips is the only US-based oil and gas company to publicly call for the development of a mandatory US national framework to address greenhouse gas emissions, a position we have held since April 2007. We are committed to playing a proactive and positive role in the development of efficient, equitable and environmentally effective climate change policy. Attached you will find our comments on California's Climate Change Draft Scoping Plan as well as our position on climate change.

We welcome this opportunity to submit comments on the Draft Scoping Plan. Feel free to contact us with additional questions, clarifications and feedback.

Sincerely,

A handwritten signature in dark ink, appearing to read 'S. L. Cornelius', written in a cursive style.

Cc: Linda Adams, Secretary Cal-EPA  
Cindy Tuck, Under Secretary Cal-EPA  
CARB Board Members  
Chuck Shulock, CARB  
Edie Chang, CARB  
Darren Bouton, Deputy Cabinet Secretary for Governor Schwarzenegger

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# **California Climate Change Draft Scoping Plan**

**Stakeholder Comment**

**ConocoPhillips**

**Submitted to the California Air Resources Board  
August 1, 2008**

## **Summary of Key ConocoPhillips Recommendations**

**Inclusion of Transportation Fuels in the California Cap-and-Trade Program:** We recommend that CARB remove transportation fuel emissions from the State cap-and-trade system and instead apply a carbon fee on these GHG emissions should CARB determine that vehicle and fuel performance standards are inadequate to deliver targeted reductions from the transportation sector.

**California Cap-and-Trade Program Linked to Western Climate Initiative:** We recommend that CARB include in the Scoping Plan specific recommendations for harmonizing California climate policy with any future Federal climate change program as it has with the Western Climate Initiative.

**Use of Offsets for Compliance:** We recommend that the use of offsets from projects outside California be limited only by quality rather than by geography or by arbitrary volume thresholds.

**Low Carbon Fuel Standard (LCFS):** We recommend that CARB adheres to the principle of fair and equitable treatment of all feedstocks (including heavy oil) for transportation fuels consumed in the California market when developing the LCFS.

**Energy Efficiency and Large Industrial Sources:** We recommend letting the market price of carbon determine the GHG reduction opportunities each facility chooses to pursue. California should not adopt a command-and-control approach to facility GHG emission regulation and energy efficiency measures.

**Co-Benefits:** We recommend the CARB take a cost-benefit approach to co-benefits that carefully weighs the value of any potential environmental and economic co-benefits against the potential increased cost of the entire climate program that could result from additional command-and-control style regulation.

**Carbon Fees:** We recommend that CARB not use a carbon fee as a means of sending an additional price signal to entities already covered by the cap-and-trade program.

**Use of Possible Revenues:** We recommend that any revenues flowing to the State as a result of implementation of AB32 be used to directly address the impacts of climate change and climate change policy rather than for general tax relief.

**CO2 Capture and Storage (CCS):** We recommend that CARB specifically address the practice of CCS in the Scoping Plan.

**Cost and Benefit Analysis:** We recommend that CARB evaluate the cost-effectiveness of reducing GHG emissions by comparing any options to be evaluated against a cap-and-trade program with the unrestricted import of high-quality offsets, unencumbered by additional regulation.

## **Introduction**

The comments that follow are directed at specific elements of the Draft Scoping Plan. We have made every effort to explain our position and where appropriate recommend changes to the Draft Scoping Plan that we believe will improve the prospects of successfully achieving the goals of AB32. Our comments are arranged roughly in the order in which the design elements appear in the Draft Scoping Plan.

## **Inclusion of Transportation Fuels in the California Cap-and-Trade Program**

*Capped sectors would include electricity, transportation fuels, natural gas, and large industrial sources. Emissions or energy use from most of the sectors covered by a cap-and-trade program would also be governed by other measures, including performance standards, efficiency programs, and direct regulations*

ConocoPhillips: We recognize the importance of addressing greenhouse gas (GHG) emissions from transportation fuels within the California climate change policy. We also understand the challenge of including emissions from millions of transportation fuel consumers within a cap-and-trade system. A variety of policy options are available other than cap-and-trade to reduce GHG emissions from the transportation sector, some of which are already included or are being considered in the Draft Scoping Plan (e.g. LCFS, vehicle emission standards, carbon fees). Inclusion of transportation fuels within the cap-and-trade program could send a weak and inconsistent price signal to consumers<sup>1</sup>, would increase the administrative complexity of the system and could increase the market price of emission allowances for all the other capped sectors.

*Recommendations:* We recommend removing transportation fuel emissions from the State cap-and-trade system and instead applying a carbon fee on these GHG emissions should CARB determine that vehicle and fuel performance standards are inadequate to deliver targeted reductions from the transportation sector. Such a fee should be applied at the point of consumption of transportation fuels.

## **California Cap-and-Trade Program Linked to Western Climate Initiative**

*Implement a broad-based cap-and-trade program that links with other Western Climate Initiative Partner programs to create a regional market system. Ensure California's program meets all applicable AB 32 requirements for market-based mechanisms.*

ConocoPhillips: We fully support California's intent to harmonize its climate program with the Western Climate Initiative (WCI) while maintaining the ability to meet the goals established under AB32. We agree with CARB's assessment of the value of this larger program especially as a means of limiting "leakage" of economic activity and emissions out of California. We believe there are two other key values of a regional program:

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<sup>1</sup> The cost of carbon applied to transportation fuels via a cap-and-trade approach that consumers would experience would necessarily track the cost of emission allowances. In addition, each \$10 increment in the cost of allowances translates to approximately a \$0.10 increase in the cost of gasoline. We believe these factors could lead to an inconsistent and weak price signal for consumers.

1. Increased administrative efficiency and therefore lower administrative costs
2. Increased access to lower cost, high quality emission reduction opportunities

As a company with multi-state and multi-national operations we believe these benefits extend to the Federal level as well, hence our support for a national GHG regulatory framework with international linkage. We believe a robust Federal climate change policy is now a question of “when and what” rather than “if”.

*Recommendation:* We recommend at a minimum the Scoping Plan describes California’s intent to link with a future US Federal climate program as it has with the WCI. Further, we urge CARB to include in the Scoping Plan specific recommendations for harmonizing California climate policy with any future Federal program.

### **Use of Offsets for Compliance**

*The rulemaking would also need to establish appropriate rules for use of offsets. A limit on offsets, such as 10 percent of the compliance obligation for an individual firm, would allow ARB and WCI to test the viability of the offset system while limiting the risk that unconstrained offsets could weaken the stringency of the overall cap-and-trade program.*

ConocoPhillips: Extensive modeling of climate change policy by a variety of stakeholders has concluded that access to significant volumes of high quality GHG offset credits for use towards compliance will result in a significantly lower market cost of emission allowances and therefore a lower cost for reaching the environmental targets of cap-and-trade program. Therefore, expanded opportunity to use offset credits from qualifying emission reduction projects outside of California should lower the total cost of implementing AB32 for California taxpayers and consumers.

*Recommendation:* ConocoPhillips supports unlimited use of high quality offsets for compliance with any cap-and-trade program. High quality offsets are defined as environmentally additional, verifiable, permanent and enforceable. We recommend that access to offsets should be limited only by quality rather than by geography or by arbitrary volume thresholds.

### **Low Carbon Fuel Standard (LCFS)**

*Develop and adopt the Low Carbon Fuel Standard.*

ConocoPhillips: The LCFS has been identified as a discrete early action item with implementation starting in 2010. Success of the program will be highly dependent upon its construct and timing. ConocoPhillips has a strong interest in how the LCFS develops in California. We are a significant fuel producer and supplier in California and we have extensive research efforts underway to identify cost effective and renewable low carbon intensity fuel solutions to meet anticipated future demand. In addition, we have a major position in Canadian oil sands development and publicly support the Canadian government policy efforts aimed at reducing GHG emissions from oil sands production.

*Recommendation:* ConocoPhillips strongly recommends that CARB adheres to the principle of fair and equitable treatment of all feedstocks (including heavy oil) for transportation fuels consumed in the California market. We suggest adoption of a LCFS that does not differentiate between fuels derived from conventional and unconventional petroleum resources. If the LCFS includes that differentiation, full credit should be given for GHG reductions made at facilities that extract or process unconventional resources.

While we support the concept of reducing fuel carbon intensity, we urge CARB to fully address timing and feasibility issues brought forth by the fuel supply industry as it establishes the timing and scope of the program implementation. Specifically, regulatory language has not yet been established for an LCFS and many unknowns remain around life-cycle assessments for potential fuels. With investments and permits likely to be needed for any identifiable approach, initial years of the program should be narrow in scope and associated with achievable targets. As advanced biofuels commercialize, more aggressive targets and expansion of the program could be considered. Early years of the program should incentivize next generation biofuels via appropriate multipliers to help accelerate their needed technological development.

Finally, the Federal government has recently mandated an aggressive and comprehensive Renewable Fuel Standard (RFS) with GHG delimited requirements. This mandate includes California. It is critical that CARB recognize this Federal RFS overlay and harmonize the LCFS with it to the greatest extent possible.

### **Energy Efficiency Audits for Large Industrial Sources**

*Require assessment of large industrial sources to determine whether individual sources within a facility can cost-effectively reduce GHG emissions and provide other pollution reduction co-benefits.*

ConocoPhillips: We continue to improve the energy efficiency of our operations in California, nationally and internationally. For example, as a participant in the US EPA Climate Action Challenge, ConocoPhillips is targeting a 10% improvement in the energy efficiency of our U.S. refining system between 2002 and 2012, as measured by the Solomon Energy Efficiency Index. In addition we continue to evaluate other opportunities for reducing GHG emissions in our refineries including process changes and CO2 capture and storage. ConocoPhillips is willing to discuss our successes and plans regarding energy efficiency improvement with CARB.

*Recommendation:* We support the inclusion of facilities above a de minimis GHG emission threshold within the California cap-and-trade system and recommend that CARB let the market price of carbon determine the GHG reduction opportunities each facility chooses to pursue. Such an approach will drive GHG reduction investment dollars towards the most cost-effective solutions thereby lowering the overall cost of the program to the California economy. We recommend against adopting a command-and-control approach to facility GHG emission regulation and energy efficiency measures.

### **Co-Benefits**

ConocoPhillips: The desire on the part of regulators to capture potential co-benefits of GHG reduction may lead to a command-and-control approach to GHG regulation. We believe such an approach, which could mandate reductions from specific types of equipment and/or at specific facilities and locations, could undermine the effectiveness of the cap-and-trade program to drive GHG reduction investment towards the most cost-effective solutions. The result could be increased cost of GHG reduction in the State and net increase in the cost to California.

*Recommendation:* We recommend the CARB take a cost-benefit approach to co-benefits that carefully weighs the value of potential environmental and economic co-benefits against the potential increased cost of the entire climate program that could result from a command-and-control style of regulation.

### **Carbon Fees**

*Carbon fees can play two distinct roles in implementing AB 32. Fees can be used as a powerful tool to incent emission reductions by affecting the relative prices within the economy. Fees would also provide a source of revenue to pay for reductions or achieve other goals related to the program.*

ConocoPhillips: We support limited auctioning of emission allowances within a cap-and-trade program during the transition to a full auction as our recommended approach to allowance value allocation. As a general rule we support resourcing the administrative cost of climate policy implementation from those auction proceeds. We do not believe that an additional fee *expressly for the purpose of creating a price for carbon* should be charged to entities already covered by a cap-and-trade program. Such an overlay on the carbon market would definitely add to the administrative cost of the program and could increase the overall cost of compliance. The use of a carbon fee may be appropriate for emission streams *outside* the cap-and-trade system. In particular, such a fee may be a more appropriate approach to applying a cost of carbon to transportation fuels than including transportation fuel emissions under a cap. This type of fee should be applied as close to the point of emission (i.e. end-use energy consumer) as possible.

*Recommendation:* CARB should not use a carbon fee as a means of sending an additional price signal to entities *already covered* by the cap-and-trade program. As stated previously, we recommend removing transportation fuel emissions from the State cap-and-trade system and instead applying a carbon fee on these GHG emissions should CARB determine that vehicle and fuel performance standards are inadequate to deliver targeted reductions from the transportation sector. Such a fee should be applied at the point of consumption of transportation fuels.

### **Use of Possible Revenues**

*Revenues may be generated from the implementation of various components of the Scoping Plan, including by the use of auctions within a cap-and-trade system, adoption*



*of carbon fees, or through the imposition of more targeted measures like public goods charges on water. These revenues could be used to support AB 32 requirements for GHG emission reductions and associated socio-economic considerations.*

ConocoPhillips: We support the use of government revenues generated during implementation of a climate change program specifically for addressing the impacts of climate change and climate change policy. We recommend that any revenues be directed towards three general categories of activity:

- Assist consumers, workers and impacted businesses with the transition to a low-GHG economy;
- Promote the acceleration of technology development and deployment;
- Address climate change impacts on communities and the environment;

We are pleased to see that many of the possible uses for revenue generated under the California program and listed in the Draft Scoping Plan are aligned with these categories.

*Recommendation:* CARB should ensure that any revenues flowing to the State as a result of implementation of AB32 be used to directly address impacts of climate change and climate change policy rather than for general tax relief. We recommend taking a cautious approach to government management of carbon market volatility via the buying and selling of credits<sup>2</sup>. A variety of policy tools could be adopted to address issues related to allowance value in the early days of a cap-and-trade program (e.g. banking and borrowing) that would require less government intervention in the market.

### **CO2 Capture and Storage**

ConocoPhillips: We believe that CO2 capture and storage (CCS) represents a key set of technologies and practices that will play an important role in meeting state, regional, national and global GHG reduction requirements while maintaining and strengthening the ability of society to provide abundant and affordable energy. Widespread deployment of CCS will require legislation or regulation that establishes a value for carbon emissions, supports technology research and development, provides incentives for early movers, and creates a regulatory and legal framework that provides the certainty necessary for long-term investment while letting market forces drive the most cost-efficient and environmentally effective CCS solutions. Further, we think California could be a major proving ground for CCS. Broad agreement exists that widespread deployment of CCS is critical to achievement of long-term GHG emission reduction goals. However, given the relatively immature state of the industry and its relatively high cost, rapid deployment of CCS will require incentives to spur advances in three stages of CCS development – R&D, demonstration and deployment.

*Recommendation:* In order for CCS to play a significant role in mitigating GHG emissions in California in a timely fashion, it is important for the State to start now to support CCS development and deployment. Therefore we recommend that CARB specifically address the practice of CCS in the Scoping Plan. Recognizing that it may be

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<sup>2</sup> Draft Scoping Plan Page 46 – “Manage the early carbon market and mitigate price volatility, purchasing credits and selling them or retiring them as needed,”

some time before the market price of CO<sub>2</sub> is high enough to make CCS commercially viable, California should develop a CCS incentive program aimed at proving up key elements of CCS technology and supporting early-mover projects in the State. Funding for such an incentive program could come from climate program revenues. In addition, California should work to address non-commercial barriers to CCS deployment (e.g. permitting, regulatory framework, community opposition).

### **Cost-Benefit Analysis**

ConocoPhillips: We commend CARB for the scope of the cost-benefit analysis being carried out and look forward to seeing the results of the analysis when it becomes available. CARB correctly points out that “the cap-and-trade program is expected to encourage the lowest-cost emission reductions to be implemented” to meet the cap and “the reductions that are achieved would likely be the cheapest ones”. As such, we believe CARB does not make a strong case as to the need for additional GHG regulations which would likely increase the overall cost of AB32 to the California economy.

CARB quotes the results of recent economic modeling studies which attempt to assess the impact of the proposed S.2191 legislation and draws the conclusion that the impact on GDP will be small. From our own analysis of the same studies we found that GDP in General Computable Equilibrium models tends to be insensitive to any policy changes absent any major constraints on the ability to meet the reduction goal (e.g. the pace at which new nuclear plants can be built or the substitutability of one form of transportation fuel for another). We also found that, even though the scenarios that were chosen to be modeled used outdated and understated capital cost assumptions for CO<sub>2</sub> reduction technologies, the promotion of those technologies was, nevertheless, critical to achieving the GHG reductions at the lowest cost.

We feel that the CARB definition of “cost-effectiveness” does not adequately consider that GHG reduction is a global problem and that the most cost-effective reductions could take place in locations other than California. The GHG price required to meet the cap in a well-designed, efficient cap-and-trade system, which allows the import of high-quality offsets, should provide the baseline definition of cost-effectiveness in meeting GHG targets. Any cost benefit analysis should be carried out on an incremental basis to be compared to this base case. In this manner the cost-benefit analysis of the decisions to add further regulation or to the limit the import of offsets can be evaluated against the incremental benefits obtained.

*Recommendation:* We recommend that CARB evaluate the cost-effectiveness of reducing GHG emissions by comparing any options to be evaluated against a cap-and-trade program with the unrestricted import of high-quality offsets, unencumbered by additional regulation. We also recommend that CARB ensure that the assumptions used in any cost-benefit analysis of GHG reduction technologies take into account the recent capital cost inflation being experienced by the economy.

## APPENDIX A

### **ConocoPhillips Climate Change Position**

ConocoPhillips recognizes that human activity, including the burning of fossil fuels, is contributing to increased concentrations of greenhouse gases in the atmosphere that can lead to adverse changes in global climate. While uncertainties remain over the extent of human contributions and the timing and magnitude of future impacts, we are committed to taking action to expand our business planning processes to address greenhouse gas (GHG) emissions and to develop greenhouse gas targets for our operations. Our commitment to sustainable development will provide the foundation for our actions.

Concerns continue to grow regarding the possible environmental and financial impacts of climate change. We recognize these concerns, and in the context of our business we face uncertain costs and outcomes associated with:

- Developing technology, products and operating practices which reduce or avoid GHG emissions.
- Responding to altered patterns of demand for products due to regulations designed to combat climate change, actual climate changes or changes in consumer attitudes toward products based on their associated GHG emissions.
- Complying with government-mandated action.
- Adapting our facilities or operational practices due to the physical consequences of changing climate.

No one entity can address these issues on its own, but ConocoPhillips will show leadership in finding pragmatic and sustainable solutions. In addition to taking actions within our own sphere of influence, we intend to play a constructive role in public policy dialogue to devise practical, equitable and cost-effective approaches to stabilize the concentration of GHG in the atmosphere. It is our view that mandatory national regulatory frameworks which link to international ones are most likely to achieve meaningful global GHG reductions. We will seek to encourage policy measures which deliver the following principles:

- Slow, stop and ultimately reverse the rate of growth in global GHG emissions.
- Establish a value for carbon emissions, which is transparent and relatively stable and sufficient to drive the changed behaviors necessary to achieve targeted emissions reductions.
- Provide long-term certainty for investment decisions.
- Encourage the development and deployment of innovative technology to help avoid or mitigate GHG emissions at all stages of the product life cycle.
- Realistically match the pace and stringency of policy to the rate at which new technology or infrastructure changes can be developed and deployed.
- Encourage energy efficiency at all stages of the product life cycle.
- Inform and influence consumer preference toward less GHG-intensive consumption.
- Encourage the deployment of carbon capture and storage as a practical near-term solution.

- Avoid placing a disproportionate burden on any one business sector or consumer segment.
- Support equitable international competition.
- Ensure that early actions are not disadvantaged.
- Avoid undue harm to the economy.

As economies around the world continue to develop, the growing global demand for energy must be met in concert with responsible actions on climate change. Balancing supply and demand will require more efficient use of energy and the full utilization of both conventional and innovative sources of energy into the foreseeable future. This will include renewable sources such as wind, solar, hydro, thermal and biomass, together with nuclear power and continued use of hydrocarbons in ways that lower the GHG impacts of oil, gas and coal.

Meeting the twin challenges of taking action on climate change and providing adequate and reliable supplies of energy will require technical innovation, resource commitments and responsible stewardship by energy producers and consumers alike. ConocoPhillips intends to meet these challenges.