TITLE 17. CALIFORNIA AIR RESOURCES BOARD

NOTICE OF PUBLIC HEARING TO CONSIDER AMENDMENTS TO CALIFORNIA CAP ON GREENHOUSE GAS EMISSIONS AND MARKET-BASED COMPLIANCE MECHANISMS TO ALLOW FOR THE USE OF COMPLIANCE INSTRUMENTS ISSUED BY LINKED JURISDICTIONS

The Air Resources Board (ARB or Board) will conduct a public hearing at the time and place noted below to consider proposed amendments to California greenhouse gas emissions cap-and-trade program and market-based compliance mechanisms to allow for the use of compliance instruments issued by linked jurisdictions.

DATE: June 28, 2012

TIME: 9:00 a.m.

PLACE: California Environmental Protection Agency
Air Resources Board
Byron Sher Auditorium
1001 I Street
Sacramento, California 95814

This item may be considered at a two-day meeting of the Board, which will commence at 9:00 a.m., June 28, 2012, and may continue at 8:30 a.m., on June 29, 2012. This item may not be considered until June 29, 2012. Please consult the agenda for the hearing, which will be available at least 10 days before June 28, 2012, to determine the day on which this item will be considered.

INFORMATIVE DIGEST OF PROPOSED ACTION AND POLICY STATEMENT OVERVIEW

Sections Affected: Proposed amendments to California Code of Regulations, title 17, to sections 95802, 95814, 95830, 95831, 95832, 95833, 95834, 95856, 95870, 95910, 95911, 95912, 95913, 95920, 95921, 95942, 95943, 96010, and 96022.

Background:

The California Global Warming Solutions Act of 2006 (Assembly Bill 32; Stats. 2006, Chapter 488) (AB 32) authorizes ARB to implement a comprehensive, multi-year program to reduce greenhouse gas (GHG) emissions in California. AB 32 required ARB to develop a scoping plan to reduce GHG emissions in California to 1990 levels by 2020. ARB's adopted Scoping Plan includes a comprehensive set of actions designed to reduce GHG emissions in California, improve the environment, reduce dependence on foreign oil, diversify energy sources, save energy, create new jobs, and enhance public health. Meeting the goals of AB 32 requires a coordinated set of strategies to reduce GHG emissions throughout the economy that work within a comprehensive tracking, reporting, verification and enforcement framework. The Scoping Plan includes

a variety of measures to achieve AB 32 goals, including direct regulations, performance-based standards, and market-based mechanisms. Many of the measures in the Scoping Plan complement and reinforce each other.

The Scoping Plan directed ARB staff to develop a cap-and-trade regulation, which is a type of market-based compliance mechanism. As envisioned in the Scoping Plan, the cap and trade program would eventually be linked with cap and trade programs operating in other states and provinces. The cap-and-trade regulation provides a fixed limit on GHG emissions from the sources responsible for about 85 percent of the state's total GHG emissions. The cap-and-trade regulation reduces GHG emissions by applying a declining aggregate cap on GHG emissions, and creates a flexible compliance system through the use of tradable instruments (allowances and offset credits). The regulation is designed to link up with partners in other jurisdictions, beginning with the Western Climate Initiative (WCI). The cap-and-trade regulation went into effect January 1, 2012.

In 2007, California helped establish the Western Climate Initiative, a cooperative effort of seven U.S. states and four Canadian provinces (the "partners") that are collaborating to identify, evaluate, and implement policies to reduce GHG emissions, including the design and implementation of a regional cap-and-trade program. WCI developed two design documents that describe a template for state and jurisdiction cap and trade programs that could be linked to form a regional market. WCI consulted extensively with stakeholders in the development of these two documents. Since 2007, WCI has held 130 public discussions via public meeting, teleconference, discussion papers and webinars. The details of WCI's public consultation are included in Appendix B. ARB worked closely with the partners in formulating the cap-and-trade regulation, and anticipated linking to programs promulgated by the partners as they are adopted. California and Québec are currently the two WCI partner jurisdictions with enforceable cap-and-trade regulations.

ARB staff conducted an extensive public process during the development of the California cap-and-trade regulation. From 2009 through 2011, staff developed the overall options for program design and development. ARB staff conducted extensive public consultation, including more than 40 public meetings, to discuss and share ideas with the general public and key stakeholders on the appropriate structure of the cap-and-trade program. In many of these public meetings, staff discussed the concept of linking California's' cap and trade program with that of other WCI partner jurisdictions. Staff also met regularly with individual stakeholders to hear their concerns and recommendations. ARB staff collected public comments during each public workshop, which focused on key topics and program design components.

In developing these proposed cap-and-trade regulation amendments, staff held two workshops and released discussion draft regulation amendments for public comment. ARB received more than 15 written comments on the discussion draft amendments and met regularly with stakeholders to discuss concerns and recommendations. In addition, WCI held a public meeting on January 12 to discuss plans to develop a North American greenhouse gas emissions trading program through linkage with partner programs.

Description of the Proposed Regulatory Action, Objectives and Benefits

After considering the comments received, ARB staff is proposing amendments to the cap-and-trade regulation that would establish the details for common allowance auctions between California and Québec and would allow acceptance of Québec compliance instruments for compliance with California's cap-and-trade regulation. These amendments include requirements for a linked compliance instrument registry and associated registration requirements. Details regarding the proposed amendments are included in Chapter II: Summary of Proposed Action and in Appendix A of the staff report.

Linking to Other Cap-and-Trade Programs

The cap-and-trade regulation includes general requirements for linking to other programs. Establishing linkage, as proposed in these amendments, with other programs requires ARB approval under the California Administrative Procedure Act (APA) before allowances and/or offset credits from an external program can be used for compliance with California's regulation. The proposed amendments would establish linking with Québec under the framework included in the existing cap-and-trade regulation. Other WCI Partner jurisdictions will be evaluated for linking as those programs become available for review when new programs are established. Québec's cap-and-trade regulation is being amended to include auction rules in common with California's amendments proposed in this rulemaking and to establish a linkage with California. Although Québec has not yet published any documents on which staff may rely, staff is confident that Québec's amended cap-and-trade regulation will be consistent with the amended California regulation based on ongoing discussions with Québec officials and the agreed upon WCI process. ARB staff is also confident, based on these discussions, that Québec's offset provisions will follow WCI recommendations regarding offset regulations and offset process, and will be consistent with California's requirements for offsets. Québec is also anticipated to make some minor revisions to their mandatory GHG reporting regulation to address areas related to data quality. Additionally, staff anticipates Québec's amended cap-and-trade and mandatory GHG reporting regulations and new offset provisions will become publicly available during the pendency of this rulemaking. ARB will add these documents to the rulemaking file pursuant to the provisions of the APA and will make these documents available for 15-days for review once these new regulations are available.

Know Your Customer (KYC) Requirements

The proposed regulation will limit registrants to individuals with a primary residence in the United States or Canada to enhance the ability of ARB to enforce the regulation. If an entity's account representative does not have an address in Québec or California, the regulation will require an agent for service of process in either jurisdiction. Canadian entities will be required to register in Québec and US entities will be required to register in California. Those with a criminal conviction constituting a felony in the US or Canada within the last 5 years will be excluded from registration.

Auction Process

New text is proposed to allow a single auction to be conducted simultaneously in two currencies, as would be the case with a linked program between California and Québec. It is important that auction participants in each jurisdiction have equitable access during the bidding process.

CONSISTENCY AND COMPATIBILITY WITH EXISTING STATE REGULATIONS

Staff does not believe the proposed regulation is inconsistent or incompatible with existing state regulations

MANDATED BY FEDERAL LAW OR REGULATIONS

This regulation is not mandated by federal law or regulations.

COMPARABLE FEDERAL REGULATIONS

This regulation is not mandated by federal law or regulations, and there are no comparable federal regulations.

AVAILABILITY OF DOCUMENTS

ARB staff has prepared a Staff Report: Initial Statement of Reasons (ISOR) for the proposed regulatory action, which includes a summary of the economic and environmental impacts of the proposal. The report is entitled: Proposed Amendments to The California Cap On Greenhouse Gas Emissions And Market-Based Compliance Mechanisms To Allow For The Use Of Compliance Instruments Issued By Linked Jurisdictions.

Copies of the ISOR and the full text of the proposed regulatory language, in underline and strikeout format to allow for comparison with the existing regulations, may be accessed on ARB's website listed below, or may be obtained from the Public Information Office, Air Resources Board, 1001 I Street, Visitors and Environmental Services Center, First Floor, Sacramento, California, 95814, (916) 322-2990, on May 9, 2012.

AVAILABILITY OF FINAL STATEMENT OF REASONS

Upon its completion, the Final Statement of Reasons (FSOR) will be available and copies may be requested from the agency contact persons in this notice, or may be accessed on ARB's website listed below.

AGENCY CONTACT PERSONS

Inquiries concerning the substance of the proposed regulation may be directed to Mr. Steve Cliff, Chief of the Climate Change Program Evaluation Branch, at (916) 322-7194 or Ms. Rajinder Sahota, Manager of the Climate Change Program Monitoring Section at (916) 323-8503.

Further, the agency representative and designated back-up contact persons, to whom nonsubstantive inquiries concerning the proposed administrative action may be directed are Ms. Lori Andreoni, Manager, Board Administration and Regulatory Coordination Unit, at (916) 322-4011, or Ms. Amy Whiting, Regulations Coordinator, at (916) 322-6533. The Board staff has compiled a record for this rulemaking action, which includes all the information upon which the proposal is based. This material is available for inspection upon request to the contact persons.

INTERNET ACCESS

This notice, the ISOR and all subsequent regulatory documents, including the FSOR, when completed, are available on ARB's website for this rulemaking at http://www.arb.ca.gov/regact/2012/capandtrade12/capandtrade12.htm

FISCAL IMPACT

The determinations of the Board's Executive Officer concerning the costs or savings necessarily incurred by public agencies and private persons and businesses in reasonable compliance with the proposed regulations are presented below.

ECONOMIC IMPACT ASSESSMENT/ANALYSIS

Linking with other jurisdictions will increase emission reduction opportunities and improve the liquidity of the emissions trading market. Depending on factors such as the size of the California market relative to the other jurisdictions, the stringency of the cap in the other jurisdiction, the cost of reductions in the other jurisdictions, and the availability of offsets in the other jurisdictions, the resulting allowance price may increase or decrease relative to a California-only cap-and-trade program. Linking with other jurisdictions could also provide gains from trade as a result of expanded reduction opportunities – further reducing emissions, facilitating innovative technologies, and creating the jobs to support them.

The analysis investigates the possible economic impacts to California of a cap-and-trade program that links with Québec, Canada. Québec is the first of the Western Climate Initiative partners ready to link with California. This analysis is based on an energy supply and demand model (ENERGY 2020) and E-DRAM, a model ARB uses to estimate the macroeconomic impacts on the California economy. These models are not designed to evaluate potential investment of funds in California from linked jurisdictions and their potential economic benefits, as could occur under linkage with Quebec.

The Energy 2020 model was used to estimate the potential GHG emission reductions and the changes in investment and fuel use. The Environmental Dynamic Revenue

Analysis Model (E-DRAM) was used to estimate the macroeconomic impacts of the proposed linkage regulation on the statewide economy including impacts on gross state product, personal income, and employment, based in part on outputs from Energy 2020. These analyses are presented in 2007 dollars and focus on the impacts of the proposed regulation in 2020. The analysis builds on the analysis for the 2010 cap-and-trade regulation and examines differences in impact between the proposed regulation and the current California only cap-and-trade regulation.

Under the proposed regulation, projected economic growth would continue virtually on par with current forecasts. The 2010 cap-and-trade economic analysis indicated likely allowances prices of $15 to $30 per metric ton CO2e in 2020. The impact of linkage on California allowance price in 2020 is estimated to result in no change or a slight increase. Thus, gross state product will remain virtually unchanged relative to the expected impact from a California-only program. Impacts on long-term projected growth rates in personal income and employment are similarly small. The allowance price in the cap-and-trade program creates a price incentive to reduce the consumption of energy. Reductions in the use of energy created by this price incentive may offset some or all of the potential small increases in the cost of electricity, natural gas and gasoline. Linking with other jurisdictions could provide additional gains from trade as a result of expanded reduction opportunities and a more liquid market.

ARB's economic analysis cannot predict the increased growth in sectors that could result because of new opportunities created by imposing a carbon price, such as those that design or manufacture renewable technologies, or predict the creation of so called "green jobs." This analysis can therefore be considered a conservative estimate of the potential statewide impacts from the imposition of a California cap-and-trade program linked with Québec that does not consider the potential statewide benefits from the linked program.

The economic analysis also focuses exclusively on the economic effects in California of linking the California cap-and-trade program with Québec's cap-and-trade program, and does not consider the avoided costs of inaction. The potential effects of climate change that are expected to occur in California, such as increased water scarcity, reduced crop yield, sea level rise, and increased incidence of wildfires, could cause severe economic impacts. While California has developed a Climate Adaptation Strategy to help alleviate these potential costs, the risk of potentially high economic costs from climate change in California remains real.

COSTS TO PUBLIC AGENCIES AND TO BUSINESSES AND PERSONS AFFECTED

The determinations of the Board's Executive Officer concerning the costs or savings necessarily incurred by public agencies and private persons and businesses in reasonable compliance with the proposed regulation are presented below.

Costs to State Government and Local Agencies

The Executive Officer has determined that the proposed regulatory action would create costs or savings, as defined in Government Code sections 11346.5(a)(5) and

11346.5(a)(6), to State agencies or in federal funding to the State. The proposed regulatory action would create costs and would impose a mandate on some State and local agencies, but would not create costs or impose a mandate on school districts. At least eight California public universities, several municipal utilities, two correctional facilities and the California Department of Water Resources would have a compliance obligation under the proposed regulation, as they do under the current cap and trade program. These entities would be required to surrender allowances or offsets equal to the amount of their GHG emissions during the compliance period. The expected costs to these entities ranges from no impact to slightly greater compared with the expected costs presented in the 2010 cap-and-trade regulation analysis due to the slightly higher expected allowance price with linkage. Because the regulatory requirements apply equally to all covered entities and unique requirements are not imposed on local agencies, the Executive Officer has determined that the proposed regulatory action imposes no costs on local agencies that are required to be reimbursed by the State pursuant to part 7 (commencing with section 17500), division 4, title 2 of the Government Code, and does not impose a mandate on local agencies or school districts that is required to be reimbursed pursuant to section 6 of Article XIII B of the California Constitution.

Costs to Businesses and Private Individuals

In developing this regulatory proposal, ARB staff evaluated the potential economic impacts on representative private persons or businesses. The Executive Officer has determined that representative private persons and businesses would be affected by the cost impacts from the proposed regulatory action. Representative private persons and businesses that do not exceed the emissions threshold would not be directly regulated under the proposed action, but would be indirectly affected by changes to the cost of using fossil-fuel based energy. Pursuant to Government Code section 11346.5(a)(7)(C), the Executive Officer has made an initial determination that the proposed regulatory action would not have a significant statewide adverse economic impact directly affecting businesses, and little or no impact on the ability of California businesses to compete with businesses in other states.

Regulated businesses may face additional indirect costs due to slightly increased energy and input prices, and some businesses might be impacted based on the compliance path they choose to meet their obligations under the proposed regulation. However, the proposed regulation would not impose sufficient direct or indirect costs to eliminate businesses in California. It is not possible to quantify the number of businesses that will be created in response to additional investment opportunities that arise as a result of the proposed regulation. However, staff believes that startups in emerging sectors such as renewable energy and biofuel production could represent significant numbers of new, small and medium sized businesses.

STATEMENT OF THE RESULTS OF THE ECONOMIC IMPACT ASSESSMENT PREPARED PURSUANT TO GOVERNMENT CODE SEC. 11346.3(b)

A detailed assessment of the economic impacts of the proposed regulatory action can be found in the Economic Impact Analysis in Chapter V of the ISOR.

In accordance with Government Code section 11346.3, the Executive Officer has determined that the proposed regulatory action would not eliminate existing businesses within the State of California, but would affect the creation of new businesses or the expansion of existing businesses currently doing business in California. The proposed regulatory action would not eliminate jobs within the State of California, but would affect the creation of jobs within California.

ARB estimates that 360 businesses or covered entities would participate in the cap-and-trade program from the year of initial implementation through 2020. These businesses include: electricity generators; electricity importers; industrial facilities including cement plants, cogeneration facilities, hydrogen plants, petroleum refiners, and general stationary combustion facilities; and many fuel providers including wholesalers of gasoline, distillate, propane, and natural gas.

In general, most small businesses in regulated sectors would not be subject to the proposed regulation because their total GHG emissions are below the GHG reporting threshold, thereby exempting them from compliance obligations under the proposed regulation. However, small businesses may experience similar cost impacts as consumers. Cost impacts on consumers would result from no change to a potential slight increase in energy prices. Households and small businesses that consume less energy (directly by reducing their consumption of energy or indirectly by utilizing goods and services that are produced using less energy) will be less affected by higher prices than those that consume more energy. Incentive programs available to small businesses and consumers will provide access to funds for investing in energy efficient technologies, which includes low interest loans, rebates and credits. Energy savings from efficiency improvements are likely to partially offset or fully mitigate the impact of any increase in electricity prices and could mean decreased energy bills. Most California businesses will likely pass along the small cost increases to consumers in the form of slightly higher prices for their products or services.

ARB staff has considered whether any proposed alternatives would lessen potential adverse economic impacts on businesses. The alternatives that staff has considered are described in more detail in Chapter VI of the Initial Statement of Reasons.

In accordance with Government Code sections 11346.3(c) and 11346.5(a)(11), the Executive Officer has found that the reporting requirements of the proposed regulation which apply to businesses are necessary for the health, safety, and welfare of the people of the State of California.

Before taking final action on the proposed regulatory action, the Board must determine that no reasonable alternative considered by the Board, or that has otherwise been identified and brought to the attention of the Board, would be more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons than the proposed action.

SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS, INCLUDING ABILITY TO COMPETE

The Executive Officer has made an initial determination that the proposed regulatory action would not have a significant statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states, or on representative private persons.

ALTERNATIVES

Before taking final action on the proposed regulatory action, the Board must determine that no reasonable alternative considered by the Board, or that has otherwise been identified and brought to the attention of the Board, would be more effective in carrying out the purpose for which the action is proposed, or would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provisions of law. ARB considered four alternatives to the proposed action including: no linkage, waiting to link with additional WCI states or jurisdictions, linkage with no Québec offsets and linkage with restricted Québec offsets. A detailed analysis of alternatives is presented in Chapter VI of the initial statement of reasons.

ENVIRONMENTAL ANALYSIS

In accordance with ARB's certified regulatory program, California Code of Regulations, title 17, sections 60006 through 60007, and the California Environmental Quality Act, Public Resources Code section 21080.5, ARB has conducted an analysis of the potential for significant adverse and beneficial environmental impacts associated with the proposed regulatory action. The environmental analysis of the proposed regulatory action can be found in Chapter IV of the Initial Statement of Reasons.

SUBMITTAL OF COMMENTS AND WRITTEN COMMENT PERIOD

Interested members of the public may also present comments orally or in writing at the meeting, and comments may be submitted by postal mail or by electronic submittal before the meeting. The public comment period for this regulatory action will begin on May 14, 2012. To be considered by the Board, written comments, not physically submitted at the meeting, must be submitted on or after May 14, 2012 and received **no later than 12:00 noon on June 27, 2012**, and must be addressed to the following:

Postal mail: Clerk of the Board, Air Resources Board
1001 I Street, Sacramento, California 95814

Electronic submittal: http://www.arb.ca.gov/lispub/comm/bclist.php

You can sign up online in advance to speak at the Board meeting when you submit an electronic board item comment. For more information go to:
http://www.arb.ca.gov/board/online-signup.htm

Please note that under the California Public Records Act (Gov. Code, § 6250 et seq.), your written and oral comments, attachments, and associated contact information (e.g., your address, phone, email, etc.) become part of the public record and can be released to the public upon request.

ARB requests that written and email statements on this item be filed at least 10 days prior to the hearing so that ARB staff and Board members have additional time to consider each comment. The Board encourages members of the public to bring to the attention of staff in advance of the hearing any suggestions for modification of the proposed regulatory action.

Additionally, the Board requests but does not require that persons who submit written comments to the Board reference the title of the proposal in their comments to facilitate review.

STATUTORY AUTHORITY AND REFERENCES

This regulatory action is proposed under the authority granted in Health and Safety Code, sections 38510, 38560, 38562, 38564, 38570, 38571, 38580, 39600 and 39601. This action is proposed to implement, interpret, and make specific sections 38530, 38560.5, 38564, 38565, 38570 and 39600 of the Health and Safety Code.

HEARING PROCEDURES

The public hearing will be conducted in accordance with the California Administrative Procedure Act, Government Code, title 2, division 3, part 1, chapter 3.5 (commencing with section 11340).

Following the public hearing, the Board may adopt the regulatory language as originally proposed, or with non-substantial or grammatical modifications. The Board may also adopt the proposed regulatory language with other modifications if the text as modified is sufficiently related to the originally proposed text that the public was adequately placed on notice and that the regulatory language as modified could result from the proposed regulatory action; in such event, the full regulatory text, with the modifications clearly indicated, will be made available to the public, for written comment, at least 15-days before it is adopted.

The public may request a copy of the modified regulatory text from ARB's Public Information Office, Air Resources Board, 1001 I Street, Visitors and Environmental Services Center, First Floor, Sacramento, California, 95814, (916) 322-2990.

SPECIAL ACCOMMODATION REQUEST

Special accommodation or language needs can be provided for any of the following:

- An interpreter to be available at the hearing;
- Documents made available in an alternate format or another language; or

- A disability-related reasonable accommodation.

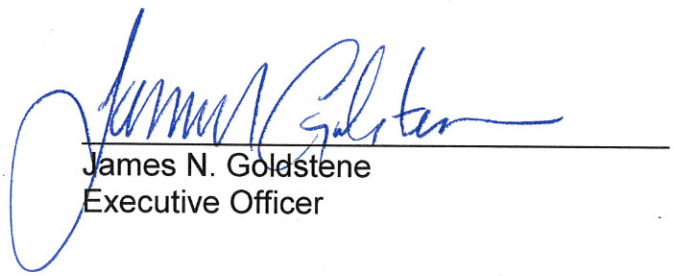
To request these special accommodations or language needs, please contact the Clerk of the Board at (916) 322-5594 or by facsimile at 916) 322-3928 as soon as possible, but no later than 10 business days before the scheduled Board hearing. TTY/TDD/Speech to Speech users may dial 711 for the California Relay Service.

Comodidad especial o necesidad de otro idioma puede ser proveído para alguna de las siguientes:

- Un intérprete que esté disponible en la audiencia.
- Documentos disponibles en un formato alterno u otro idioma.
- Una acomodación razonable relacionados con una incapacidad.

Para solicitar estas comodidades especiales o necesidades de otro idioma, por favor llame a la oficina del Consejo al (916) 322-5594 o envíe un fax a (916) 322-3928 lo más pronto posible, pero no menos de 10 días de trabajo antes del día programado para la audiencia del Consejo. TTY/TDD/Personas que necesiten este servicio pueden marcar el 711 para el Servicio de Retransmisión de Mensajes de California.

CALIFORNIA AIR RESOURCES BOARD



James N. Goldstene
Executive Officer

Date: May 1, 2012

The energy challenge facing California is real. Every Californian needs to take immediate action to reduce energy consumption. For a list of simple ways you can reduce demand and cut your energy costs, see our website at www.arb.ca.gov.