State of California
AIR RESOURCES BOARD

Amendments to California Cap-and-Trade Program - Linkage

Resolution 13-7

April 19, 2013

Agenda Item No.: 13-4-1

WHEREAS, sections 39600 and 39601 of the Health and Safety Code authorize the Air Resources Board (ARB or Board) to adopt standards, rules, and regulations and to do such acts as may be necessary for the proper execution of the powers and duties granted to and imposed upon the Board by law;

WHEREAS, the California Global Warming Solutions Act of 2006 (AB 32; Chapter 488, Statutes of 2006; Health & Safety Code section 38500 et seq.) declares that global warming poses a serious threat to the economic well-being, public health, natural resources, and environment of California and creates a comprehensive multi-year program to reduce California's greenhouse gas (GHG) emissions to 1990 levels by 2020;

WHEREAS, AB 32 added section 38501 to the Health and Safety Code, which expresses the Legislature's intent that ARB coordinate with State agencies and consult with the environmental justice community, industry sectors, business groups, academic institutions, environmental organizations, and other stakeholders in implementing AB 32; and design emissions reduction measures to meet the statewide emissions limits for greenhouse gases in a manner that minimizes costs and maximizes benefits for California's economy, maximizes additional environmental and economic co-benefits for California, and complements the State's efforts to improve air quality;

WHEREAS, section 38501(c) of the Health and Safety Code declares that California has long been a national and international leader on energy conservation and environmental stewardship efforts, and the program established pursuant to AB 32 will continue this tradition of environmental leadership by placing California at the forefront of national and international efforts to reduce GHG emissions;

WHEREAS, section 38501(d) of the Health and Safety Code confirms that national and international actions are necessary to fully address the issue of global warming, but action taken by California to reduce GHG emissions will have far reaching effects by encouraging other states, the federal government, and other countries to act;

WHEREAS, section 38501(e) of the Health and Safety Code states that by exercising a global leadership role, California will also position its economy, technology centers, financial institutions, and businesses to benefit from national and international efforts to

reduce emissions of greenhouse gases. More importantly, investing in the development of innovative and pioneering technologies will assist California in achieving the 2020 statewide limit on emissions of greenhouse gases and will provide an opportunity for the state to take a global economic and technological leadership role in reducing emissions of greenhouse gases;

WHEREAS, section 38510 of the Health and Safety Code designates ARB as the State agency charged with monitoring and regulating sources of GHG emissions in order to reduce these emissions;

WHEREAS, section 38560 of the Health and Safety Code directs ARB to adopt rules and regulations in an open public process to achieve the maximum technologically feasible and cost-effective GHG emissions reductions from sources or categories of sources;

WHEREAS, section 38562(a) of the Health and Safety Code requires ARB to adopt GHG emissions limits and emissions reduction measures by regulation to achieve the maximum technologically feasible and cost-effective reductions in GHG emissions in furtherance of achieving the statewide GHG emissions limit, to become operative beginning on January 1, 2012;

WHEREAS, section 38564 of the Health and Safety Code directs ARB to consult with other states, and the federal government, and other nations to identify the most effective strategies and methods to reduce greenhouse gases, manage greenhouse gas control programs, and to facilitate the development of integrated and cost-effective regional, national, and international greenhouse gas reduction programs;

WHEREAS, California is participating in the Western Climate Initiative (WCI), with other Partner jurisdictions considering implementation and linkage of GHG Cap-and-Trade programs;

WHEREAS, over the course of 6 years, the WCI Partner jurisdictions have coordinated on developing recommendations for greenhouse gas reporting, compliance offsets, and cap-and-trade as models for jurisdictions to develop their own programs;

WHEREAS, the WCI Partner jurisdictions developed recommendations in a public and transparent manner with over 130 public documents, 86 stakeholder meetings, webinars, and calls, and received comments on 48 occasions;

WHEREAS, by linking California's Program to WCI Partner jurisdictions, the combined Programs will result in more emission reductions, generate greater potential for lower cost emissions reductions, enhance market liquidity, and will increase opportunities for GHG emissions reductions for covered sources more than could be realized through a California-only program;

WHEREAS, establishing and implementing a California and regional GHG Cap-and-Trade Program requires ARB and WCI Partner jurisdictions to harmonize specific

regulatory and operational provisions, including, but not limited to, sources subject to compliance obligations, emissions reporting requirements, cost-containment mechanisms, evaluation of regulatory baselines for existing offset protocols, procedures for developing new offset protocols, compliance instrument tracking system development and operation, auction services, financial services, and market monitoring and oversight;

WHEREAS, ARB and the WCI Partner jurisdictions established a regional administrative organization in November 2011, similar to other regional Cap-and-Trade Programs, called Western Climate Initiative, Inc. to meet the goal of regionally coordinated administration of cap-and-trade services;

WHEREAS, the Board adopted the Final Regulation Order establishing a GHG Cap-and-Trade Program for California after a three-year development process that included hundreds of stakeholder meetings, workshops, and comments; the regulation became effective January 1, 2012, and includes the following elements:

Addresses emissions of carbon dioxide (CO_2), methane (CH_4), nitrous oxide (N_2O);

Identifies the Program scope: starting in 2012, electricity, including imports, and large industrial facilities are included; starting in 2015, distributors of transportation fuels, natural gas, and other fuels are included;

Establishes a declining aggregated emissions cap on included sectors. The cap starts at 162.8 million allowances in 2013, which is equal to the emissions forecast for that year. The cap declines approximately 2 percent per year in the initial period (2013–2014). In 2015, the cap increases to 394.5 million allowances to account for the expansion in Program scope to include fuel suppliers. The cap declines at approximately 3 percent per year between 2015 and 2020. The 2020 cap is set at 334.2 million allowances;

Provides for distribution of allowances through a mix of direct allocation and auction in a system designed to reward early action and investment in energy efficiency and GHG emissions reductions; allowances will be distributed for the purposes of price containment, industry transition and assistance, and fulfillment of AB 32 statutory objectives;

Establishes a market platform for allowance auction and sale;

Establishes cost-containment mechanisms and market flexibility mechanisms, including trading of allowances and offsets, allowance banking, a two year compliance period and two 3-year compliance periods, the ability to use offsets

for up to 8 percent of an entity's compliance obligation, and an allowance reserve that provides allowances at fixed prices to those with compliance obligations;

Establishes a mechanism to link with other GHG trading programs and approve the use of compliance instruments issued by a linked external GHG trading program;

Establishes requirements and procedures for ARB to issue offset credits according to offset protocols adopted by the Board;

Includes four offset protocols adopted by the Board as part of the regulatory package;

Establishes a mechanism to include international offset programs from an entire sector within a region;

Establishes a robust enforcement mechanism that will discourage gaming of the system and deter and vigorously punish fraudulent activities; and

Provides an opt-in provision for entities whose annual GHG emissions are below the threshold to voluntarily participate in this program.

WHEREAS, staff has proposed amendments to the Cap-and-Trade Regulation set forth in Attachment A hereto that includes the following elements:

The use of allowances and compliance offsets from a linked jurisdiction by California entities for compliance in the Cap-and-Trade Program;

The use of California issued allowances and compliance offsets for compliance by entities in a linked jurisdiction;

Joint quarterly auctions that include allowances from California and its linked jurisdictions;

Adjustments to the "Annual allowance budget" used in the calculation of the holding limits to include allowances from California and its linked jurisdictions;

Mechanisms to allow for auction bidding and settlement in two currencies;

Requirements for each covered entity to register in its jurisdiction;

Requirements for all voluntary participants located in the United States to register with California and voluntarily submit themselves to the jurisdiction of the State of California; and

Requirements where only covered entities in California would be eligible to participate in the California Allowance Price Containment Reserve sales.

WHEREAS, staff held two public workshops on the linkage amendments and also participated in numerous other meetings with various stakeholders to provide additional opportunities for participation in the regulatory development process;

WHEREAS, the Board believes the success of a Cap-and-Trade Program is predicated on GHG regulations that are clear, consistent, enforceable, and transparent;

WHEREAS, staff prepared a document entitled "Staff Report: Initial Statement of Reasons for the 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" (ISOR), which presents the rationale and basis for the proposed regulation and identifies the data, reports, and information relied upon;

WHEREAS, the proposed regulatory language was made available to the public at least 45 days prior to the public hearing to consider the proposed regulation, with three subsequent comment periods of 15 days to add documents to the record and propose additional modifications to the regulatory text;

WHEREAS, Senate Bill 1018 (Government Code section 12894(f)) was enacted requiring state agencies to notify the Governor that the agency intends to take action to link with another greenhouse gas emissions trading program; and the Governor must make specified findings prior to the agency taking action to approve the linkage;

WHEREAS, on February 22, 2013, the Executive Officer sent a letter to the Governor requesting the Governor's consideration of the four findings that are necessary before ARB can adopt a regulation that would link the greenhouse gas emissions trading programs developed by California and the Province of Québec;

WHEREAS, on April 8, 2013, the Governor provided ARB a letter stating that the four requirements of Government Code section 12894(f) have been satisfied and describing additional steps the Board will take prior to implementing linkage with the Québec Cap-and-Trade Program;

WHEREAS, in consideration of the ISOR, written comments, and public testimony it has received to date, the Board finds that:

> The goal of the Québec's 2020 greenhouse gas emissions target is at least as stringent as California's 2020 greenhouse gas emissions target;
> The scope of Québec's Cap-and-Trade Program is consistent with the scope of California's Program;
>
> Québec's greenhouse gas reporting program is rigorous and will provide accurate greenhouse gas emissions data to support a Cap-and-Trade Program;
>
> Québec's greenhouse gas reporting program verification requirements are consistent with California's requirements;

Québec's Cap-and-Trade Program is designed with mechanisms consistent with the California Program to prevent the ability of entities to exert market power;

Québec's auction mechanics are consistent with those in California's Program and will enable the administration of joint auctions;

Québec's identity verification requirements are consistent with those in the California Program;

Québec's compliance offset program design is consistent with California's Program requirements;

Québec's offset criteria are consistent with AB 32 and California's Program;

Québec's offset verification requirements are consistent with those recommended by WCI and included in California's Program;

Québec's offset protocols for the destruction of ozone depleting substances and livestock digesters are based on and consistent with ARB's Compliance Offset Protocol Ozone Depleting Substances Projects and ARB's Compliance Offset Protocol Livestock Projects;

Québec's offset protocol for small landfills requires the capture and destruction of landfill methane similar to ARB's landfill early action measure;

Québec's offset protocol for small landfills would not give compliance offset credit to large landfills which would be subject to the landfill early action measure in California and is therefore harmonized with California's Program;

The staff's proposed regulatory text meets the statutory requirements identified in section 38562 of the Health and Safety Code including equitable and cost effective distribution of allowances to maximize total benefits to California; minimizing leakage, and cost effectiveness;

The staff's proposed regulatory text meets the statutory requirements for a market-based mechanism identified in section 38570 of the Health and Safety Code including: consideration of the potential for direct; indirect, and cumulative emission impacts; prevention of increases in emissions of toxic air contaminates or criteria pollutants and maximizing additional environmental and economic benefits for California;

The staff's proposed regulatory text was developed in an open public process, in consultation with affected parties, through public workshops, individual meetings, and other outreach efforts;

The staff's proposed regulatory text is predicated on GHG regulations that are clear, consistent, enforceable, and transparent and helps meet the goals of AB 32; and

The staff's proposed regulatory text would provide for a linked Cap-and-Trade Program between California and Québec, effective January 1, 2014, where allowances and compliance offsets issued by each jurisdiction would be fungible across both Programs.

WHEREAS, the WCI coordination process to have a linked Cap-and-Trade Program between California and any of the WCI Partner jurisdictions as described in the ISOR does not set a precedent for other mechanisms for California to accept compliance instruments from other types of programs;

WHEREAS, the California Environmental Quality Act (CEQA) requires that a public agency not approve a project as proposed if there are feasible alternatives or feasible mitigation measures available which would substantially lessen the significant environmental impacts of such a project; in the event that specific economic, social, or other conditions make infeasible the alternatives or mitigation measures, the project may be approved if it is determined that any remaining unavoidable significant impacts are acceptable due to overriding considerations;

WHEREAS, Public Resources Code section 21080.5 allows public agencies with regulatory programs to prepare a plan or other written document in lieu of an environmental impact report or negative declaration once the Secretary of the Resources Agency has certified the regulatory program;

WHEREAS, that portion of ARB's regulatory program that involves the adoption, approval, amendment, or repeal of standards, rules, regulations, or plans has been certified by the Secretary of Resources Agency (CEQA Guidelines, section 15251(d));

WHEREAS, ARB's certified regulatory program provides that prior to taking final action on any proposal for which significant environmental issues have been raised, the decision maker shall approve a written response to each such issue;

WHEREAS, in accordance with ARB's certified regulatory program at title 17, CCR, section 60005 (b), and the policy and substantive requirements of CEQA, ARB staff prepared an assessment of the potential for significant adverse and beneficial environmental impacts associated with the proposed action and a succinct analysis of those impacts in Chapter IV of the ISOR;

WHEREAS, the environmental analysis (EA) in Chapter IV of the ISOR set forth a programmatic level of analysis of broadly defined types of indirect impacts that could occur as a result of the proposed action, including potential alternatives;

WHEREAS the environmental analysis was circulated as part of the ISOR for a 45-day written public comment period from May 14, 2012, until June 27, 2012;

WHEREAS, ARB reviewed written comments on the potential for environmental impacts associated with the proposed action received during the initial 45-day comment period and subsequent 15-day comment periods and prepared written responses to these comments;

WHEREAS, on April 9, 2013, ARB posted a document called the *Response to Comments on the Environmental Analysis Prepared for the 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* (Response to EA Comments);

WHEREAS, at a duly noticed public hearing held on April 19, 2013, staff presented the Response to EA Comments for approval, and the Final Regulation Order for adoption; and

WHEREAS, the Board has reviewed and considered the EA and the Response to EA Comments.

NOW, THEREFORE, BE IT RESOLVED that the Board hereby certifies that the EA was completed in compliance with CEQA under ARB's certified regulatory program, reflects the agency's independent judgment and analysis, and was presented to the Board whose members reviewed, considered and approved the information therein prior to acting on the proposed Final Regulation Order.

BE IT FURTHER RESOLVED that the Board approves the written responses to comments raising significant environmental issues included in the Response to EA Comments.

BE IT FURTHER RESOLVED that in consideration of the EA and Response to EA Comments, and in accordance with the requirements of CEQA and ARB's certified regulatory program, the Board adopts the Findings and Statement of Overriding Consideration as set forth in Attachment C to this Resolution.

BE IT FURTHER RESOLVED that the Board adopts the amendments to the California Greenhouse Gas Emissions and Market-Based Compliance Mechanisms to Allow for the Use of Compliance Instruments Issued by Linked Jurisdictions set forth in Attachment A to this Resolution.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to finalize the Final Statement of Reasons and submit the rulemaking package to the Office of Administrative Law by May 8, 2013.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to report to the Board at least annually on the status of the linked Cap-and-Trade Program.

BE IT FURTHER RESOLVED that at least six months prior to any of the following taking effect in a linked jurisdiction, the Executive Officer will provide a report to the Board that includes an assessment of environmental factors and will provide a recommendation for

Board action if appropriate. The report to the Board will also include an opportunity for public review and input.

Changes to the stringency of the Program, including changes to the cap;

The adoption of a new compliance offset protocol or significant amendments to an existing compliance offset protocol;

Linkage to another Cap-and-Trade Program; and

Any other change to a linked jurisdiction's Program which would significantly affect the stringency, integrity, enforceability or successful functioning of the combined Programs.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to work with Québec to complete pre-linkage activities prior to the effective date of January 1, 2014. These activities should include those steps needed to ensure implementation readiness, which may include, but are not limited to, testing of the auction platform to allow for a joint auction, a practice joint auction between California and Québec, testing of the tracking system to enable transfers across program participants, and a review (and adjustments as needed) of processes, procedures and systems of California's and Québec's programs to ensure consistency and compatibility.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to coordinate with the Government of Québec to ensure both jurisdictions maintain an enforceable linked Cap-and-Trade Program, and that the implementation of the Cap-and-Trade Program in linked jurisdictions is as rigorous as California's implementation of its Cap-and-Trade Program. This coordination should include the reporting and verification of emissions, reports on implementation of offset programs, market surveillance, and updates on investigations and enforcement actions.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to coordinate with the Government of Québec to implement the linked Cap-and-Trade Program in an efficient and transparent manner, and directs the Executive Officer to document the coordination process in a written agreement with the Government of Québec and provide it to the Board and make it available to the public.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to work with linked jurisdictions to ensure that information is shared between the jurisdictions to ensure robust surveillance, oversight and enforcement, and that enforcement is applied in an equivalent manner in all linked jurisdictions.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to update the Board in Fall 2013 on the status of the auction platform and trading system to support linkage and progress toward implementing the linked markets prior to providing a report to the Secretary of Cal/EPA and the Governor's office by November 1, 2013, as directed in the Governor's April 8, 2013, letter to ARB.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to continue working with the non-linked WCI Partner jurisdictions to harmonize the Programs by developing appropriate regulatory amendments necessary to formally link the Programs, and by developing appropriate policy and technical protocols necessary to effectively implement the linked jurisdictions' Programs.

I hereby certify that the above is a true and correct copy of Resolution 13-7, as adopted by the Air Resources Board.

Tracy Jensen

Tracy Jensen, Clerk of the Board

Resolution 13-7

April 19, 2013

Identification of Attachments to the Board Resolution

Attachment A:	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.
Attachment B:	Response to EA Comments are found at: http://www.arb.ca.gov/board/books/2013/041913/start.pdf
Attachment C:	Findings and Statement of Overriding Consideration