State of California
AIR RESOURCES BOARD

AMENDMENTS TO THE CALIFORNIA CAP ON GHG EMISSIONS AND MARKET BASED COMPLIANCE MECHANISMS

Resolution 15-19

June 25, 2015

Agenda Item No.: 15-5-6

WHEREAS, the Health and Safety Code, sections 39600 and 39601 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 (Assembly Bill 32; Chapter 488, Statutes of 2006; Health and Safety Code, section 38500 et seq.) (AB 32) declares that global warming poses a serious threat to the economic well-being, public health, natural resources, and environment of California and provided initial direction on creating a comprehensive multi-year program to reduce California's greenhouse gas (GHG) emissions to 1990 levels by 2020, maintain and continue reductions beyond 2020, and initiate the transformations required to achieve the State's long range climate goals;

WHEREAS, AB 32 added to the Health and Safety Code, section 38501 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 GHGs 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, the Health and Safety Code, section 38501(d) 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, the Health and Safety Code, section 38510 designates ARB as the State agency charged with monitoring and regulating sources of GHG emissions to reduce these emissions;

WHEREAS, the Health and Safety Code, sections 38562(c) and 38570 authorize ARB to adopt regulations that utilize market-based compliance mechanisms;

WHEREAS, the Health and Safety Code, section 38570(c) further directs ARB to adopt regulations governing how market-based compliance mechanisms may be used by regulated entities subject to GHG emissions limits and mandatory emissions reporting requirements to achieve compliance with their GHG emission limits;

WHEREAS, the Health and Safety Code, section 38571 directs ARB to adopt methodologies for the quantification of voluntary GHG emissions reductions and regulations to verify and enforce any voluntary GHG emissions reductions that are authorized by ARB for use to comply with GHG emissions limits established by ARB; the adoption of methodologies is exempt from the rulemaking provisions of the Administrative Procedure Act;

WHEREAS, the Board adopted the Final Regulation Order establishing a GHG Cap-and-Trade Program (Program) for California in 2011; the regulation (Regulation) became effective January 1, 2012, and includes the following elements:

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

Identifies the program scope: starting in 2013, electricity, including imports, and large (emissions >25,000 metric tons carbon dioxide equivalent per year) 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. 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 emission reductions;

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 2-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 Regulation; 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 voluntary participation in this program for entities whose annual GHG emissions are below the threshold triggering mandatory participation;

WHEREAS, the Board approved for adoption amendments to the Regulation in 2012 to make targeted implementation changes that became effective September 1, 2012;

WHEREAS, the Board approved for adoption amendments to the Regulation in 2013 to formally link the California Cap-and-Trade Program with the Province of Québec's Cap-and-Trade Program that became effective October 1, 2013, making California and Québec allowances and offsets available for compliance purposes in both jurisdictions;

WHEREAS, the Board adopted amendments to the Regulation in April 2014 to adopt an additional compliance offset protocol for Mine Methane Capture and make additional implementation changes that became effective July 1, 2014;

WHEREAS, the Board approved for adoption amendments to the Regulation in September, 2014 to make adjustments to allocation and adopt three updated Compliance Offset Protocols that became effective January 1, 2015;

WHEREAS, pursuant to Resolution 10-42, the Board directed the Executive Officer to initiate a public process for the review of additional compliance offset protocols for the purpose of bringing additional protocols to the Board for consideration; and ARB staff has proposed a new Rice Cultivation Projects Compliance Offset Protocol (Rice Protocol) as part of this rulemaking;

WHEREAS, in Resolution 11-32, the Board directed the Executive Officer to monitor protocol development and to propose technical updates to adopted protocols, as needed; and ARB staff has proposed an update to the U.S. Forest Compliance Offset Protocol (U.S. Forest Protocol) as part of this rulemaking;

WHEREAS, in Resolution 14-31, the Board directed the Executive Officer to remove the updates to the common practice values in the Assessment Area Data File that use the latest data from the U.S. Department of Agriculture Forest Service (Forest Service) Forest Inventory and Analysis National Program and Forest Service adjustments for the classification of high and low site class productivity to align with the site class stratification used in the adjusted common practice values for the U.S. Forests Projects Compliance Offset Protocol and directed the Executive Officer to propose updates to the common practice values in the version of the U.S. Forest Projects Compliance

Offset Protocol being presented today; and ARB staff has proposed those updates as part of this rulemaking;

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" (ISOR or Staff Report), which presents the rationale and basis for the proposed regulation amendments, the new Rice Protocol and updated U.S. Forest Protocol, and identified the data, reports, and information relied on;

WHEREAS, staff proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, as set forth in Appendix A to the Staff Report released to the public on October 28, 2014;

WHEREAS, ARB's regulatory program that involves the adoption, approval, amendment, or repeal of standards, rules, regulations, or plans has been certified by the Secretary for Natural Resources under Public Resources Code section 21080.5 of the California Environmental Quality Act (CEQA; California Code of Regulations, title 14, section 15251(d)), and ARB conducts its CEQA review according to this certified program (California Code of Regulations, title 17, sections 60000-60007);

WHEREAS, ARB prepared in 2010 and certified in 2011 a Functional Equivalent Document for the California Cap on GHG Emissions and Market-Based Compliance Mechanisms (2010 FED), which included an analysis of the environmental benefits and impacts of the U.S. Forest Protocol on the contiguous 48 states.

WHEREAS, ARB prepared an Environmental Analysis (EA) included as Chapter III of the ISOR, which includes specific environmental analyses under its certified regulatory program for both the Rice Protocol and the U.S. Forest Protocol (included as Chapter III in Appendices B and C to the ISOR, respectively), and circulated the EA for 45 days from October 31, 2014, through December 15, 2014;

WHEREAS, the environmental analysis for the proposed Rice Protocol and associated regulatory language changes concluded that the compliance responses would result in beneficial impacts to greenhouse gas (GHG) emissions; less than significant impacts to aesthetics, agricultural and forest resources, air quality, biological resources, cultural resources, energy demand, geology, soils and minerals, hazards, hydrology and water quality, land use, noise, employment, population and housing, public services, recreation, transportation and traffic, and utilities/service systems; and no potentially significant adverse impacts to the environment;

WHEREAS, the environmental analysis for the proposed updated U.S. Forest Protocol and associated regulatory language changes supplemented and incorporated by reference the analysis contained in the 2010 FED, and concluded that implementation

of the proposed updated U.S. Forest Protocol would not result in any new types of potentially significant adverse impacts on the physical environment in the contiguous 48 states that were not already addressed in the 2010 FED; however, the proposed updated U.S. Forest Protocol would geographically extend the environmental effects identified in the 2010 FED by expanding project eligibility to areas of Alaska, which would result in the following impacts to areas of Alaska: beneficial impacts to GHG emissions; less than significant impacts to aesthetics, agricultural and forest resources, air quality, cultural resources, energy demand, geology, soils and minerals, hazards, hydrology and water quality, noise, employment, population and housing, public services, recreation, transportation and traffic, and utilities/service systems; and potentially significant adverse impacts to biological resources and land use and planning;

WHEREAS, on December 22, 2014, the Board conducted a public hearing on the proposed amendments to the Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms and the EA prepared for the proposal;

WHEREAS, following the public hearing, the Board adopted Resolution 14-44, directing the Executive Officer to make any appropriate conforming modifications available for public comment, with any additional supporting documents and information, for a period of at least 15 days; the Executive Officer was further directed to consider written comments submitted during the public review period and make any additional appropriate conforming modifications available for public comment for at least 15 days, evaluate all comments received during the public comment periods, including comments on the EA, and prepare written responses to the EA comments as required by ARB's certified regulations at California Code of Regulations, title 17, sections 60000-60007 and Government Code section 11346.9(a); the Executive Officer was also directed to present to the Board, at a subsequently scheduled public hearing, the EA and staff's written responses to any comments on the EA for consideration for approval, and the finalized amendments for consideration for adoption.

WHEREAS, following the Board hearing, the modified regulatory language and supporting documentation were circulated for a 15-day comment period, with the changes to the originally proposed text clearly indicated, according to provisions of California Code of Regulations, title 1, section 44 and Government Code section 11340.85, from May 20, 2015 through June 4, 2015;

WHEREAS, staff reviewed written comments received on the EA and prepared written responses to those comments raising significant environmental issues in a document entitled *Response to Comments on the Environmental Analysis Prepared for Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms* (Reponse to EA Comments);

WHEREAS, on June 15, 2015, staff posted on the rulemaking page the Response to EA Comments;

WHEREAS, prior to the duly noticed public hearing held on June 25, 2015, staff presented the EA and the Response to EA Comments, as set forth in Attachments D and E to this resolution, to the Board for consideration;

WHEREAS, a public hearing and other administrative proceedings have been held according to the provisions of Chapter 3.5 (commencing with section 11340) part 1, division 3, title 2 of the Government Code;

WHEREAS, the Board received comments at the June 25, 2015 hearing indicating a public desire for additional communications between the public and ARB staff regarding clarification and guidance to be provided to stakeholders;

WHEREAS, in consideration of the ISOR, written comments and public testimony, the Board finds that:

The proposed amendments to the Cap-and-Trade Regulation to modify and clarify offset related definitions are necessary for proper implementation of the offset program;

The proposed Rice Cultivation Compliance Offset Protocol meets AB 32 offset criteria and is necessary to further ensure a sufficient supply of offsets and cost-containment benefits;

The proposed update to the U.S. Forest Compliance Offset Protocol meets AB 32 offset criteria, addresses necessary changes based on the most recently available data, and modifies and clarifies the protocol as necessary for enhanced implementation;

The proposed amendments to the Cap-and-Trade Regulation meet the statutory requirements for a market based mechanism identified in section 38570 of the Health and Safety Code;

The proposed amendments to the Cap-and-Trade Regulation were developed in an open public process, in consultation with affected parties, through numerous public workshops, individual meetings, and other outreach efforts, and these efforts are expected to continue;

No reasonable alternatives to the amendments considered to date, or that have otherwise been identified and brought to the attention of ARB, would be more effective at carrying out the purpose for which the regulation is proposed or would be as effective and less burdensome to affected entities that the proposed regulation; and

The proposed amendments are consistent with ARB's environmental justice policies and do not disproportionately impact people of any race, culture, or income.

NOW, THEREFORE, BE IT RESOLVED that the Board hereby certifies that the EA included in Attachment D to this resolution was completed in compliance with ARB's certified regulatory program to meet the requirements of CEQA, reflects the agency's independent judgment and analysis, and was presented to the Board whose members reviewed and considered the information therein before taking action to approve the amendments;

BE IT FURTHER RESOLVED that the Board approves the Response to EA Comments set forth in Attachment E to this resolution;

BE IT FURTHER RESOLVED that in consideration of the EA, the Response to EA Comments, and the entirety of the record, the Board adopts the Findings and Statement of Overriding Considerations set forth in Attachment F to this resolution;

BE IT FURTHER RESOLVED that the Board hereby adopts the amendments to sections 95802, 95973, 95975, 95976, 95981, 95985, and 95990, title 17, California Code of Regulations, as set forth in Attachment A;

BE IT FURTHER RESOLVED that the Board adopts the Rice Protocol, as set forth in Attachment B to this resolution;

BE IT FURTHER RESOLVED that in further consideration of the Rice Protocol, the Board directs the Executive Officer to evaluate the potential addition of rice baling projects, including any potential environmental benefits and impacts, and present any modification of the Protocol to the Board for future consideration;

BE IT FURTHER RESOLVED that the Board adopts the update to the U.S. Forest Protocol, as set forth in Attachment C to this resolution;

BE IT FURTHER RESOLVED that the adopted regulatory text may be further revised with non-substantial or grammatical changes, which will be added to the rulemaking record and indicated as such;

BE IT FURTHER RESOLVED that the Board reiterates its direction to the Executive Officer to update the Board, at least annually, on the status of the Cap-and-Trade Program, including the status of existing compliance offset protocols and potential new compliance offset protocols;

BE IT FURTHER RESOLVED, the Board directs ARB staff to continue to work with stakeholders, including holding workshops, and accepting comment on draft guidance prior to finalizing a guidance document for the approved U.S. Forests Projects Compliance Offset Protocol.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to finalize the Final Statement of Reasons and submit the completed rulemaking package to the Office of Administrative Law, and transmit the Notice of Decision with the Response to EA Comments to the Secretary of the Natural Resources Agency for posting.

NOW, THEREFORE, BE IT RESOLVED that the Board hereby certifies that the EA included in Attachment D to this resolution was completed in compliance with ARB's certified regulatory program to meet the requirements of CEQA, reflects the agency's independent judgment and analysis, and was presented to the Board whose members reviewed and considered the information therein before taking action to approve the amendments;

BE IT FURTHER RESOLVED that the Board approves the Response to EA Comments set forth in Attachment E to this resolution;

BE IT FURTHER RESOLVED that in consideration of the EA, the Response to EA Comments, and the entirety of the record, the Board adopts the Findings and Statement of Overriding Considerations set forth in Attachment F to this resolution;

BE IT FURTHER RESOLVED that the Board hereby adopts the amendments to sections 95802, 95973, 95975, 95976, 95981, 95985, and 95990, title 17, California Code of Regulations, as set forth in Attachment A;

BE IT FURTHER RESOLVED that the Board adopts the Rice Protocol, as set forth in Attachment B to this resolution;

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BE IT FURTHER RESOLVED, the Board directs ARB staff to continue to work with stakeholders, including holding workshops, and accepting comment on draft guidance prior to finalizing a guidance document for the approved U.S. Forests Projects Compliance Offset Protocol.

BE IT FURTHER RESOLVED that the Board directs the Executive Officer to finalize the Final Statement of Reasons and submit the completed rulemaking package to the Office

of Administrative Law, and transmit the Notice of Decision with the Response to EA Comments to the Secretary of the Natural Resources Agency for posting.

I hereby certify that the above is a true and correct copy of Resolution 15-19 as adopted by the Air Resources Board.

Tracy Jensen

Tracy Jensen, Clerk of the Board

Resolution 15-19

June 25, 2015

Identification of Attachments to the Board Resolution

Attachment A: Final Regulation Order Amendments to the California Cap on GHG Emissions and Market-Based Compliance Mechanisms, sections 95802, 95973, 95975, 95976, 95981, 95985, and 95990, California Code of Regulations, title 17.

Attachment B: Compliance Offset Protocol Rice Cultivation Projects.

Attachment C: Compliance Offset Protocol U.S. Forest Projects.

Attachment D: EA Prepared for the Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, as set forth in Chapter III in the ISOR, released October 28, 2014. http://www.arb.ca.gov/regact/2014/capandtradeprf14/capandtradeprf14.htm

Attachment E: Response to Comments on the EA Prepared for the Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, released on June 15, 2015. http://www.arb.ca.gov/regact/2014/capandtradeprf14/capandtradeprf14.htm

Attachment F: Findings and Statement of Overriding Considerations (distributed at the June 25, 2015 ARB Board hearing).