

State of California
AIR RESOURCES BOARD

**Notice of Public Availability of Modified Text
and Availability of Additional Documents**

**Amendments to the California Cap on Greenhouse Gas Emissions and
Market-Based Compliance Mechanisms Regulation**

Public Hearing Date: November 15, 2018
Public Availability Date: November 15, 2018
Deadline for Public Comment: November 30, 2018

At its November 15, 2018, public hearing, the California Air Resources Board (CARB or Board) considered staff's proposed sections 95801 to 96022, title 17, California Code of Regulations (CCR). These sections comprise the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms Regulation, including Compliance Offset Protocols (Cap-and-Trade Regulation or Regulation).

The Board directed the Executive Officer to determine if additional conforming modifications to the Regulation were appropriate and to make any proposed modified regulatory language available for public comment, with any additional supporting documents and information, for a period of at least 15 days in accordance with Government Code section 11346.8. The Board further directed the Executive Officer to consider written comments submitted during the public review period and make any further modifications that are appropriate available for public comment for at least 15 days.

The regulatory documents for this rulemaking are available online at the following CARB website:

<https://www.arb.ca.gov/regact/2018/capandtrade18/capandtrade18.htm>

The text of the modified regulatory language is shown in Attachment A. The originally proposed regulatory language is shown in ~~strikethrough~~ to indicate deletions and underline to indicate additions. New deletions and additions to the proposed language that are made public with this notice are shown in ~~double-strikethrough~~ and double underline format, respectively.

In the Final Statement of Reasons, staff will respond to all comments received on the record during the comment periods. The Administrative Procedure Act requires that staff respond to comments received regarding all noticed changes. Therefore, staff will only address comments received during this 15-day comment period that are responsive to this notice, documents added to the record, or the changes detailed in Attachment A.

Summary of Proposed Modifications

The following summary does not include all modifications to correct typographical or grammatical errors, changes in numbering or formatting, nor does it include all of the non-substantive revisions made to improve clarity.

1. Modifications to Section 95802. Definitions.

The definition of “Energy Imbalance Market (EIM) Outstanding Emissions” is modified to maintain consistency with the definition in the Regulation for the Mandatory Reporting of Greenhouse Gas Emissions (MRR). In the 45-day MRR proposal, EIM Outstanding Emissions would have been calculated through March 31, 2019 using annual data and beginning April 1, 2019 using five-minute interval data. In the 15-day MRR proposal, EIM Outstanding Emissions are calculated using annual data for all time periods. Thus, the proposed changes remove references to calculating EIM Outstanding Emissions by different methods in different time periods.

The definition of Energy Imbalance Market Purchaser” or “EIM Purchaser” is changed from any entity serving California load with EIM purchases to electrical distribution utilities (EDUs) that both receive allowance allocation and serve California load with EIM purchases. This change also specifies the information that will be used to determine whether an EDU is an EIM Purchaser. EDUs that directly or indirectly purchase from EIM at any point in the data year to meet their California load will be included as EIM Purchasers. This change is necessary to ensure that those EDUs that are participating, directly or indirectly, in the California Independent System Operator (CAISO) 5-minute market proportionally share in the responsibility of addressing emissions leakage resulting from EIM.

These changes limit consideration of entities whose participation in the EIM to only include existing covered entities, specifically the EDUs that participate in CAISO and whose customers benefit from the EIM. It is only these entities that will be responsible for addressing EIM leakage in order to ensure the environmental integrity of the Cap-and-Trade Program (Program). This change provides a simpler and more implementable way to quantify and compensate for EIM emissions leakage than the 45-day proposal.

In the 45-day proposal, staff proposed to assess a compliance obligation on EIM Purchasers for each EIM Purchaser’s share of total EIM Outstanding Emissions. Under this 15-day proposal, the environmental integrity of the Program for EIM Outstanding Emissions would be preserved through direct retirement of allowances that are freely allocated to EIM Purchasers, as newly defined. The 45-day proposal would have included in-State generators with negative imbalances as covered entities, in some cases causing entities to be newly covered by the Program. Several stakeholders submitted comments expressing concern about how such entities would understand and manage their potential obligation and about unintended impacts on CAISO’s

markets by changing scheduling and bidding behavior. The new EIM Purchaser definition limits the responsibility for preserving the environmental integrity of the Program for EIM emissions leakage to EDUs that participate in EIM and receive freely allocated allowances.

The definition of “Energy Imbalance Market Purchaser Emissions” is modified to change an MRR citation from “section 95111(h)(2)(A)” to “section 95111(h)(2).” This ensures that the calculation of EIM Purchaser Emissions is based on the annual retail sales for each EIM Purchaser.

The definition of “First Deliverer of Electricity” is modified to remove EIM Purchasers from the types of entities that would be considered a first deliverer of electricity. In section 95811, EIM Purchasers are removed from the list of covered entities under first deliverers of electricity, and the change to the definition of “First Deliverer of Electricity” is needed to maintain consistency with that change.

The definition of “Volumetric” is revised to clarify that this term applies to the direct distribution of proceeds to ratepayers. This change clarifies that use of allocated allowance proceeds for specific activities or projects allowable under the Regulation would not be deemed volumetric. For example, spending allocated allowance proceeds on purchasing renewable electricity from a specific facility or on an infrastructure project to support vehicle electrification would not be deemed volumetric and would therefore be permissible. However, the volumetric return of allocated allowance proceeds directly to customers through rates, including specialized rates for electric vehicle charging, would continue to be deemed volumetric and would therefore continue to be prohibited by the Regulation.

2. Modifications to Section 95811. Covered Entities.

Section 95811 is modified to remove EIM Purchasers from the list of covered entities under first deliverers of electricity. EIM Purchasers were added to the list of covered entities in the initial staff proposal, but this 15-day proposal includes a modified definition of “EIM Purchaser” and no longer assesses a direct compliance obligation on EIM Purchasers for EIM Outstanding Emissions. Because the 15-day proposal does not assess a direct compliance obligation on EIM Purchasers, it is necessary to remove EIM Purchasers from the list of covered entities in this section.

3. Modifications to Section 95812. Inclusion Thresholds for Covered Entities.

Section 95812 is modified to remove the inclusion threshold for EIM Purchaser Emissions. EIM Purchasers were included in the list of covered entities in the initial 45-day staff proposal, but the 15-day proposal no longer assesses a direct compliance obligation for EIM Outstanding Emissions on EIM Purchasers. An inclusion threshold for EIM Purchaser Emissions is not needed in the current proposal because there is no direct compliance obligation assessed for EIM Purchaser Emissions.

4. Modifications to Section 95852. Emission Categories Used to Calculate Compliance Obligations.

Section 95852(b)(1)(D) is modified to remove the assessment of a direct compliance obligation on EIM Purchasers, which was added in the initial 45-day proposal. Assessing a direct compliance obligation for EIM Outstanding Emissions on EIM Purchasers is no longer needed in the current 15-day proposal, because CARB will directly retire allowances that were freely allocated to EDUs that are EIM Purchasers to ensure the environmental integrity of the Program for EIM emissions leakage. This proposal accounts for EIM emissions leakage and shifts the responsibility for addressing the leakage from the State to the entities in the electricity sector whose customers are benefiting from electricity from the EIM. This change provides a simpler and more implementable way to quantify and compensate for EIM emissions leakage than the 45-day proposal. The 45-day proposal would have included in-State generators with negative imbalances as covered entities, in some cases causing entities to be newly covered by the Program. The change places the responsibility to ensure environmental integrity of the Program only on those EDUs that participate in EIM and receive freely allocated allowances.

Text in section 95852(b)(1)(E) that specifies the calculation of EIM Outstanding Emissions in MRR for each data year is moved to section 95852(l). This text is moved to clarify that EIM Outstanding Emissions are not part of a direct compliance obligation for first deliverers of electricity. New text in section 95852(l) cites the calculation of EIM Purchaser Emissions for each EIM Purchaser in MRR to support the retirement of allowances to address EIM emissions leakage and ensure the environmental integrity of the Program. Citations to MRR are updated to maintain consistency with changes to the calculation of EIM Outstanding Emissions and EIM Purchaser Emissions in MRR.

Text from section 95911(h)(2) describing the retirement of future vintage allowances to cover EIM Outstanding Emissions from January 1, 2018 through March 31, 2019 is modified for clarity only and moved to new sections 95852(l)(1)-(2). The regulatory requirements remain unchanged.

New sections 95852(l)(2)-(3) specify the process for the Executive Officer to retire allowances for EIM Outstanding Emissions after March 31, 2019. Beginning April 1, 2019, allowance allocation to EDUs that are EIM Purchasers is designated for direct retirement by CARB for EIM Outstanding Emissions. The Executive Officer is required to retire these allowances by November 1 of each year. These provisions are necessary to support CARB retirement of allocated allowances for the purposes ensuring environmental integrity of the Program to address EIM emissions leakage.

5. Modifications to Section 95854. Quantitative Usage Limit on Designated Compliance Instruments—Including Offset Credits.

Text in the last sentence of new section 95854(e) of the 45-day proposal contained a typographical error. This section has been revised to correctly spell the word “comply.”

6. Modifications to Section 95870. Disposition of Vintage 2013-2020 Allowances.

Table 8-1 in section 95870 is modified to update leakage risk classifications for the two industrial activities that were added to the table in the 45-day proposal. It was indicated in the initial proposal that staff would continue to evaluate the leakage risk for these sectors and potentially propose an update to the leakage risk classification for each sector as part of this rulemaking process.

The industrial sectors “Textile and Fabric Finishing Mills” (NAICS code 313310) and “Other Structural Clay Product Manufacturing” (NAICS code 327123) were added to Table 8-1 in the 45-day proposal to allow for allowance allocation to potential new entrant facilities that operate in these sectors. Staff continued to assess the activities conducted by potential new entrant facilities and proposes to update the initially proposed NAICS sector definitions in Table 8-1 to more accurately reflect the industrial activities performed by these entities. Table 8-1 is modified to change the sector “Textile and Fabric Finishing Mills” (NAICS code 313310) to “Textile Mills” (NAICS 313) and to change the sector “Other Structural Clay Product Manufacturing” (NAICS code 327123) to “Ground or Treated Mineral and Earth Manufacturing” (NAICS code 327992). The specific industrial activities within those sectors are also updated in Table 8-1 to more accurately reflect the activities conducted by potential new entrant facilities.

Staff conducted a leakage risk assessment for these updated industrial sectors using CARB’s standard methodology that has been applied for all industrial sectors listed in Table 8-1.¹

CARB’s standard approach typically evaluates industrial sectors at the 6-digit NAICS code level, but staff proposes to evaluate “Textile Mills” at the 3-digit NAICS code level because data for the relevant 6-digit NAICS code (313310) are too limited for an accurate assessment. The emissions intensity for “Textile Mills” (NAICS code 313) is calculated to be 505 MT CO_{2e} per million dollars of value added, so this sector is classified as low emissions intensity. The trade share of this sector is 45 percent, so it is classified as high trade exposure. The combination of low emissions intensity and high trade exposure places for “Textile Mills” (NAICS code 313) in the medium leakage risk category.

Staff calculated the emissions intensity for “Ground or Treated Mineral and Earth Manufacturing” (NAICS code 327992) to be 677 MT CO_{2e} per million dollars of value added and the trade share to be 18 percent. Thus, this sector is classified as low emissions intensity and medium trade exposure, and “Ground or Treated Mineral and Earth Manufacturing” (NAICS code 327992) is placed in the medium leakage risk category.

¹ California Air Resources Board. 2010 Proposed Regulation to Implement the California Cap-and-Trade Program, Staff Report: Initial Statement of Reasons, Part I, Volume IV, Appendix K: Leakage Analysis. <http://www.arb.ca.gov/regact/2010/capandtrade10/capv4appk.pdf>

Both “Textile Mills” (NAICS code 313) and “Ground or Treated Mineral and Earth Manufacturing” (NAICS code 327992) are entered in Table 8-1 with “Medium” leakage risk classification and assigned appropriate assistance factors through 2040. The industrial sector “Cut and Sew Apparel Manufacturing” (NAICS code 3152) is moved within Table 8-1 so that its NAICS code is in proper numerical order. The footnote to Table 8-1 that was added to explain the meaning for “TBD” is deleted because it is no longer needed.

7. Modifications to Section 95891. Allocation for Transition Assistance and Leakage Minimization.

Section 95891(c)(2)(D) is modified to specify the historic baseline annual greenhouse gas emissions used to evaluate emissions stability for new entrant facilities. This section covers allowance allocation to facilities that have newly entered the Cap-and-Trade Program and conduct activities that are newly added to Table 8-1. Changes in this section ensure that appropriate data are used to assess a new entrant’s emissions stability and that newly covered entities receive accurate true-up allowance allocation to provide for leakage assistance during their transition to being covered by the Cap-and-Trade Program.

The definition of the variable “BE_t,” the baseline annual greenhouse gas emissions for year “t,” is modified to specify for which years baseline emissions for a facility are equal to zero and for which years baseline emissions are calculated by the specified equation. For years prior to having its activity added to Table 8-1, a change is proposed so that for an entity conducting an activity that was recently added to Table 8-1, “BE_t” is calculated by the specified equation instead of being set equal to zero.

This modification ensures that appropriate data are used to assess a new entrant’s emissions stability, which in turn is used to determine if the new entrant receives allocation by the stable energy-based method in section 95891(c)(2)(C), the transitional energy-based method in section 95891(c)(2)(B), or newly eligible energy-based method in section 95891(c)(3). Because true-up allocation is applied differently under these different energy-based allocation methods, this change ensures that newly covered entities receive accurate true-up allowance allocation to provide for leakage assistance during their transition to be covered by the Cap-and-Trade Program.

Section 95891(f) is revised to modify the method of determining the baseline allowance allocation level (the quantity “BaselineAllocation”) used to calculate allowance allocation to waste-to-energy facilities. In the 45-day proposal, “BaselineAllocation” is calculated based on the historic average of annual covered emissions for the 2015-2017 data years less the emissions associated with sold electricity that is generated from non-biogenic fuel. The current 15-day proposal modifies “BaselineAllocation” to be based on the historic average of annual covered emissions for the 2011-2017 data years. This approach provides transition assistance to waste-to-energy facilities as they are no longer exempt from having a compliance obligation in the Cap-and-Trade Program and

is responsive to Board direction provided during the Board Hearing held November 15, 2018.

The time period for allowance allocation to waste-to-energy facilities would remain the same as the 45-day proposal. Waste-to-energy facilities would receive true-up allocation for budget years 2018 and 2019, and then receive allowance allocation through budget year 2024 pursuant to Board Resolution 17-21.

8. Modifications to Section 95892. Allocation to Electrical Distribution Utilities for Protection of Electricity Ratepayers.

Section 95892(a)(3) is added to specify the pool of allowances that are retired to recognize EIM Purchaser Emissions beginning April 1, 2019. This new section specifies that EIM emissions leakage will be addressed through the direct retirement of allowances allocated to EDUs that are EIM Purchasers in the amount of each EDU's EIM Purchaser Emissions. The change places the responsibility to ensure environmental integrity of the Program on those entities that receive freely allocated allowances and participate in the EIM. This change does not impact how allocation to EDUs is calculated or the amounts specified in Table 9-3, 9-3A or 9-4.

EIM Purchasers, as defined in the initial 45-day proposal, expressed concerns through their public comments that they would not be able to effectively plan or manage a compliance obligation resulting from EIM Purchaser Emissions. New section 95892(a)(3) addresses these concerns by removing the need for EIM Purchasers to directly manage the compliance responsibility for EIM emissions leakage. CARB will calculate EIM Purchaser Emissions pursuant to MRR for each EDU and communicate the amount to each EDU after the verification deadline in the Mandatory Reporting Regulation, but prior to the allowance allocation deadline. CARB will directly retire a portion of the allowance allocation to each EIM Purchaser in the amount of its EIM Purchaser Emissions. This is a simple, streamlined approach to addressing EIM emissions leakage.

Section 95892(b)(2)(B) is modified to correct the term "federal power authority" to "federal power marketing administration." Text is added to clarify that a "custom product contract" is included in the applicable contractual agreements between federal power marketing authorities and electrical distribution utilities. These changes only clarify text, and the meaning of the section is not changed.

Section 95892(d)(3) is modified to include spending on educational programs as an allowable use of allocated allowance proceeds. This change accommodates changes to section 95892(d)(4), which now specifies how and under what circumstances allocated allowance proceeds may be used for educational programs for which expected greenhouse gas (GHG) emissions reductions cannot be easily estimated.

Section 95892(d)(3)(C)(1) is modified to explicitly allow the use of allocated allowance proceeds to reduce emissions of hydrofluorocarbons (HFCs), which have large climate impacts similar to sulfur hexafluoride. Because projects or activities that reduce HFC

emissions provide GHG reductions that benefit ratepayers (e.g., through rebate programs to replace refrigerants in commercial refrigeration systems through retrofits or new equipment installations), expenditures on such projects or activities is an allowable use of allocated allowance proceeds.

Section 95892(d)(3)(C)(2) is added to address electrical distribution utility requests to allow using allocated allowance proceeds for wildfire risk reduction and forest carbon sequestration activities. Such activities are added as an allowable use of proceeds only after the adoption by CARB of a standardized method for quantifying GHG emissions reductions from fuel reduction activities pursuant to section 38535 of the Health and Safety Code as added by Senate Bill 901 (Dodd, 2018). In addition, any activities implemented after the adoption by CARB of standardized methods will need to be in conformance with sections 8386 and 8397 of the Public Utilities Code, as applicable. This new text specifies how allowance proceeds may be used for these purposes and supports consistency with statewide efforts to carefully manage and reduce the risk of wildfires and the resulting potential GHG emissions.

Section 95892(d)(4) is modified to clarify and add detail regarding allowable administrative and outreach costs and to allow for the use of limited amounts of allocated allowance proceeds for certain educational programs that have the primary purpose of reducing EDU ratepayers' GHG emissions. Spending on such educational programs would be capped at one percent of the EDU's total expenditures in the data year or \$100,000, whichever is larger.

To date, with the exception of investor-owned EDUs spending on outreach for California Climate Credit programs at their inception, EDUs and natural gas suppliers have generally not spent allocated allowance proceeds on educational programs. However, some utilities have requested that use of proceeds be allowed for educational programs that pursue GHG emission reduction purposes, but for which GHG emission reductions cannot be easily demonstrated. Educational programs may have value for achieving GHG reductions and benefitting ratepayers, but the effectiveness of such programs for these purposes is uncertain and difficult to evaluate. Therefore, staff believes that expenditures of allocated allowance proceeds on educational programs should be limited in favor of projects and activities for which ratepayer benefit and GHG reductions can be more directly demonstrated.

Staff proposed to limit spending of allocated allowance proceeds on educational programs to either one percent of total proceeds spent by an EDU or \$100,000, whichever is larger, to accommodate the wide range of allocated allowance proceeds received by EDUs. Based on an assessment of potential total annual expenditures by utilities, staff believes that these limits will allow for sufficient funds to design and implement an educational program while ensuring that the majority of allowance proceeds are returned to ratepayers or used to reduce GHG emissions in a manner such that the reductions can be demonstrated. An EDU could use allocated allowance proceeds for educational programs in excess of these limits if the EDU is able to demonstrate GHG emission reductions by the program. Educational programs that

fulfill the requirements of section 95892(d)(3)(C), including quantifying expected GHG emission reductions pursuant to section 95892(d)(5), would not be subject to the limits proposed in section 95892(d)(4).

Section 95892(d)(5) is modified to respond to utility comments that this requirement be further clarified. The change clarifies that the requirement is for the utility to estimate the expected GHG reductions from each use of allocated allowance proceeds.

Section 95892(d)(7) is reorganized for clarity. Sections 95892(d)(7)(A)-(D) are added to more clearly list the prohibited uses of allocated allowance value without changing the meaning of the text. Text in section 95892(d)(7)(C) is changed to more clearly state that the purchase of allowances with allocated allowance proceeds is prohibited. Purchasing allowances is a clear cost of complying with the Cap-and-Trade Regulation, and it is therefore a prohibited use of allocated allowance proceeds. In addition, section 95892(d)(7)(C) is modified to add a general prohibition on spending allocated allowances on costs, penalties, or activities mandated by any legal settlement, administrative enforcement action, or court order. These changes support CARB oversight of the uses of allocated allowance proceeds to ensure usage on its main purposes—reduction of GHG emissions and ratepayer benefit.

Section 95892(e)(4)(A) is modified to require reporting of the GHG emissions reduction purpose for allocated allowance proceeds expended on educational programs in order to ensure the educational programs are focused on achieving GHG emissions reductions as required in the revised section 95892(d)(4).

Section 95892(e)(4)(B) is modified to clarify that EDUs should use the elements applicable to the specific projects and activities they conduct in order to estimate the GHG reductions from the use of allocated allowance proceeds.

Section 95892(e)(4)(C) is modified to require itemized reporting of educational program expenses which are now allowed pursuant to section 95892(d)(4).

9. Modifications to Section 95893. Allocation to Natural Gas Suppliers for Protection of Natural Gas Ratepayers.

Section 95893(d)(3) is modified to include spending on educational programs as an allowable use of allocated allowance proceeds. This change accommodates changes to section 95893(d)(4), which now specifies how and under what circumstances allocated allowance proceeds may be used for educational programs for which expected GHG emissions reductions cannot be easily estimated.

Text in section 95893(d)(3)(B) that requires that use of allocated allowance proceeds on projects or activities that reduce emissions of uncombusted natural gas not be mandated by any legal settlement or enforcement action is moved to section 95893(d)(7)(B). The moved text is modified to more generally prohibit use of *any* allocated allowance proceeds to pay for costs, penalties, or activities mandated by any

legal settlement, administrative enforcement action, or court order.

Section 95893(d)(4) is modified to clarify and add detail regarding allowable administrative and outreach costs and to allow using limited amounts of allocated allowance proceeds for certain educational programs that have the primary purpose of reducing natural gas supplier ratepayers' GHG emissions. Spending on such educational programs would be capped at one percent of the supplier's total expenditures in the data year or \$100,000, whichever is larger.

To date, with the exception of investor-owned EDUs spending on outreach for California Climate Credit programs at their inception, EDUs and natural gas suppliers have generally not spent allocated allowance proceeds on educational programs. However, some utilities have requested that use of proceeds be allowed for educational programs that pursue GHG emission reduction purposes, but for which GHG emission reductions cannot be easily demonstrated. Educational programs may have value for achieving GHG reductions and benefitting ratepayers, but the effectiveness of such programs for these purposes is uncertain and difficult to evaluate. Therefore, staff believes that expenditures of allocated allowance proceeds on educational programs should be limited in favor of projects and activities for which ratepayer benefit and GHG reductions can be more directly demonstrated.

Staff proposed to limit spending of allocated allowance proceeds on educational programs to either one percent of total proceeds spent by a supplier or \$100,000, whichever is larger, to accommodate the wide range of allocated allowance proceeds received by natural gas suppliers. Based on an assessment of potential total annual expenditures by utilities, staff believes that these limits will allow for sufficient funds to design and implement an educational program while ensuring that the majority of allowance proceeds are returned to ratepayers or used to reduce GHG emissions in a manner such that the reductions can be demonstrated. A natural gas supplier could use allocated allowance proceeds for educational programs in excess of these limits if the supplier is able to demonstrate GHG emission reductions by the program. Educational programs that fulfill the requirements of section 95893(d)(3)(B), including quantifying expected GHG emission reductions pursuant to section 95893(d)(5), would not be subject to the limits proposed in section 95893(d)(4).

Section 95893(d)(5) is modified to respond to utility comments that this requirement be further clarified. The change clarifies that the requirement is for the utility to estimate the expected GHG reductions from each use of allocated allowance proceeds.

Section 95893(d)(7) is reorganized for clarity. Sections 95893(d)(7)(A)-(D) are added to more clearly list the prohibited uses of allocated allowance value without changing the meaning of the text. Text in section 95893(d)(7)(C) is changed to more clearly state that the purchase of allowances with allocated allowance proceeds is prohibited. Purchasing allowances is a clear cost of complying with the Cap-and-Trade Regulation, and it is therefore a prohibited use of allocated allowance proceeds. This clarification ensures that allocated allowance proceeds are not returned volumetrically to ratepayers

through the purchase of allowances. In addition, text in section 95893(d)(7)(C) is modified to add a general prohibition on spending allocated allowances on costs, penalties, or activities mandated by any legal settlement, administrative enforcement action, or court order. These changes support CARB oversight of the uses of allocated allowance proceeds to ensure usage on its main purposes—reduction of GHG emissions and ratepayer benefit.

Section 95893(e)(4)(A) is modified to require reporting of the GHG emissions reduction purpose for allocated allowance proceeds expended on educational programs in order to ensure the educational programs are focused on achieving GHG emissions reductions as required in the revised section 95893(d)(4).

Section 95893(e)(4)(B) is modified to clarify that natural gas suppliers should use the elements applicable to the specific projects and activities they conduct in order to estimate the GHG reductions from the use of allocated allowance proceeds.

Section 95893(e)(4)(C) is modified to require itemized reporting of educational program expenses which are now allowed pursuant to section 95893(d)(4).

10. Modifications to Section 95894. Allocation to Legacy Contract Generators for Transition Assistance

Section 95894(d) is modified to provide transition assistance to legacy contract generators without industrial counterparties for the third compliance period. The transition assistance would be provided as vintage 2020 allowance allocation, including true-up allowance allocation for the 2018 and 2019 budget years.

Transition assistance to legacy contract generators helps address compliance costs for generators with contracts that were in place before AB 32 was passed. Legacy contract generators received transition assistance from 2013 through 2017, and that assistance ended beginning 2018. Under the initial 45-day proposal, legacy contract generators without industrial counterparties would resume receiving transition assistance after the third compliance period, beginning with vintage 2021 allowance allocation and with no true-up allowance allocation for the 2018 and 2019 budget years. CARB's long-term approach for legacy contracts is to encourage renegotiation of legacy contracts so that energy prices include GHG costs. Including transition assistance during the third compliance period (2018-2020) helps to avoid a potentially disruptive change in compliance costs as legacy contract generators work to renegotiate legacy contracts.

Section 95894(e) is deleted to remove the legacy contract natural gas (LCNG) true-up allocation provision that was part of the initial proposal. Staff initially proposed the LCNG true-up allocation to align CARB's implementation of legacy contract allocation with a recent California Public Utilities Commission (CPUC) decision about the pass-through of GHG costs in natural gas rates.

Since allocation of vintage 2015 allowances, CARB's calculation of legacy contract

allowance allocations has assumed, based on a 2015 CPUC decision (Decision 15-10-032), that natural gas prices used in calculating electricity or thermal energy users' payments to some legacy contract generators would include GHG costs that are proportional to the natural gas supplier consignment rate (i.e., the minimum percentage of allocated allowances that natural gas suppliers must consign to auction). That decision was reheard and did not go into effect until 2018 (see CPUC Decision 18-03-017), contrary to CARB's assumption that it would be effective for natural gas pricing during the 2015 to 2017 period. The LCNG true-up allocation was proposed to align with the final outcome of the CPUC decision by trueing-up previous legacy contract allocations to reflect the most recent GHG pricing information.

Stakeholder comments on the 45-day proposal expressed concerns regarding the proposed change and asserted that it would undermine efforts at contract renegotiation. As the stakeholder comments correctly indicate, the legacy contract provisions of the Regulation are intended to provide transition assistance, not full coverage of a legacy contractor generator's annual compliance obligation. CARB has previously expressed concerns that providing full coverage of legacy contract generators' compliance obligations would provide a disincentive to renegotiate contracts.

CARB has always calculated, and will continue to calculate, allowance allocation to legacy contract generators based on the most appropriate information available at the time, in light of previous Board direction to provide transition assistance and incentivize contract renegotiation. Given the likelihood that the initial proposal may have decreased the incentive to renegotiate legacy contracts, CARB now proposes to delete the LCNG true-up allocation provision.

Moreover, the timing of the LCNG true-up allocation proposed in the 45-day language—providing v2020 allowances in 2019 to true-up initial v2015-v2017 allowance allocation—would not be timely for managing the relevant compliance obligations because the triennial compliance surrender deadline for all covered emissions in 2015 through 2017 has already occurred (i.e., on November 1, 2018).

Based on these considerations, staff is removing the proposed LCNG true-up allocation provision. Through this change, staff is continuing to implement the legacy contract allocation provisions in a manner that is consistent with current and past implementation.

CARB is committed to maintaining consistency and alignment with other State agencies (including the CPUC) whenever possible, and staff will continue to evaluate opportunities to harmonize policies where appropriate and under a more certain timeframe.

11. Modifications to Section 95911. Format for Auction of California GHG Allowances.

The text "...or EIM Outstanding Emissions" is deleted from section 95911(h) because

staff believes it is more appropriate to discuss the retirement of allowances to cover EIM Outstanding Emissions in new sections 95852(l)(1)-(2). Text similar to the text related to the retirement of allowances to cover EIM Outstanding Emissions in section 95911(h)(2) is moved to new section 95852(l)(1)-(3) based on the new text in section 95852(l) and to ensure EIM-related provisions are more clearly consolidated together.

12. Modifications to Section 95915. Price Ceiling Sales.

Based on stakeholder feedback, section 95915(d) is modified to specify that a Price Ceiling Sale cannot be conducted until after all allowances have been sold from both tiers of the new price containment reserve tiers. In the 45-day language, it was possible for a Price Ceiling Sale to be held if allowances remained in the second Reserve Tier. In the modified text, both tiers must be depleted before a Price Ceiling Sale may be held. This change is needed to make the Price Ceiling Sale process more closely conform to the requirements of AB 398.

13. Modifications to Section 95977.1. Requirements for Offset Verification Services.

Based on stakeholder feedback, section 95977.1(b)(3)(M) is modified to clarify that three percent means 3.00 percent. This clarification specifies the number of decimal places that must be used in the determination of compliance with this provision. The use of two places after the decimal is consistent with other determinations made in Subarticle 13 of the Regulation, such as the offset material misstatement evaluation in section 95977.1(b)(3)(Q).

14. Modifications to Section 95973. Requirements for Offset Projects Using ARB Compliance Offset Protocols

Section 95973(a)(2)(D) is modified to provide more information on how the verification of a project using the Compliance Offset Protocol U.S. Forest Projects will be conducted subsequent to updating to the latest version of the protocol. Forest projects are unique in that during the initial verification for a crediting period, the baseline for the project life is required to be reviewed, and it is not explicitly required to be reviewed again until a crediting period is renewed, although it is within the discretion of the verifier to review at any time. Updating to a new version of the protocol may require a new baseline, which must be verified. Additionally, there may be changes to the listing requirements, which again are only explicitly required to be verified during the initial verification for a crediting period. In order to ensure conformance to the new version of the protocol, the modification is made to clarify that the listing requirements needs to be fully verified upon updating to a new version of the protocol.

Section 95973(b)(1)(B) is modified to provide more information on the types of information CARB can rely on when determining that a compliance offset project has returned to regulatory compliance. The modified text identifies documentation that includes information on when activities subject to enforcement action have ended,

documentation that the Offset Project Operator, Authorized Project Designee, or forest owner have acknowledged responsibility for the activity, and documentation of the ongoing status of the enforcement proceedings with the relevant local, state, or federal regulatory oversight body. These modifications, which are responsive to multiple stakeholder comments, will also give CARB more flexibility in identifying the time period that must be removed from the reporting period in situations where the relevant local, state, or federal regulatory oversight body is unable to provide a written determination regarding the date when the project returned to regulatory compliance to the satisfaction of CARB.

15. Modifications to Section 95989. Direct Environmental Benefits in the State.

Section 95989(b) is modified, in response to several comments, to clarify the original intent of the provision that the phrase “that is not credited pursuant to the applicable Compliance Offset Protocol” applies to both air pollutants and pollutants that could have an adverse impact on waters of the State.

16. Additional Modifications

In addition to the modifications described above, additional modifications correcting grammar, punctuation and spelling have been made throughout the proposed changes. These changes are nonsubstantive.

These modifications do not change implementation of the Regulation in any way that affects the conclusions of the environmental analysis included in the Staff Report because the modifications consist primarily of definition and provision clarifications that do not alter the compliance responses, so no additional environmental analysis or recirculation of the analysis is required.

Environmental Analysis

These proposed modifications do not change implementation of the regulation in any way that is anticipated to affect the conclusions of the environmental analysis included in the Staff Report because the modifications consist primarily of refinements and clarifications to the initial proposal. At this stage in this rulemaking process, CARB does not expect that any changes in compliance responses resulting from the modifications would result in any of the circumstances requiring recirculation of the analysis as set forth in section 15088.5 of the CEQA Guidelines.

References

There were certain documents referenced in footnotes in the Staff Report that are part of the record for this rulemaking. This notice clarifies that these documents are part of the record. These references are as follows:

Frances C. Moore & Delavane B. Diaz, Temperature impacts on economic growth warrant stringent mitigation policy, *Nature Climate Change* (2015), <https://www.nature.com/articles/nclimate2481#t1>.

Frances C. Moore et al., New science of climate change impacts on agriculture implies higher social cost of carbon, *Nature Communications* (2017), <https://www.nature.com/articles/s41467-017-01792-x#Sec6>.

Institute for Policy Integrity, *The Social Cost of Greenhouse Gases and State Policy, A Frequently Asked Questions Guide* (Oct. 2017), https://policyintegrity.org/files/publications/SCC_State_Guidance.pdf.

Interagency Working Group on Social Cost of Carbon, United States Government, Technical Support Document: Social Cost of Carbon for Regulatory Impact Analysis Under Executive Order 12866 (Feb. 2010), <https://obamawhitehouse.archives.gov/sites/default/files/omb/inforeg/for-agencies/Social-Cost-of-Carbon-for-RIA.pdf>.

Interagency Working Group on Social Cost of Carbon, United States Government, Technical Support Document: Social Cost of Carbon for Regulatory Impact Analysis Under Executive Order 12866 (July 2015), <https://obamawhitehouse.archives.gov/sites/default/files/omb/inforeg/scc-tsd-final-july-2015.pdf>.

Interagency Working Group on Social Cost of Carbon, United States Government, Technical Support Document: Social Cost of Carbon for Regulatory Impact Analysis Under Executive Order 12866 (August 2016), https://obamawhitehouse.archives.gov/sites/default/files/omb/inforeg/scc_tsd_final_clear_8_26_16.pdf.

Intergovernmental Panel on Climate Change, *IPCC Fourth Assessment Report: Climate Change 2007, 3.5.3.3 Cost-benefit analysis, damage cost estimates and social costs of carbon*, https://www.ipcc.ch/publications_and_data/ar4/wg3/en/ch3s3-5-3-3.html.

National Academy of Sciences, *Valuing Climate Damages, Updating Estimation of the Social Cost of Carbon Dioxide* (2017), <https://www.nap.edu/catalog/24651/valuing-climate-damages-updating-estimation-of-the-social-cost-of>.

William D. Nordhaus, Revisiting the Social Cost of Carbon, *PNAS* (Nov. 2016), <http://www.pnas.org/content/pnas/114/7/1518.full.pdf>.

Agency Contacts

Inquiries concerning the substance of the proposed regulation may be directed to Jason Gray, Branch Chief, Climate Change Program Evaluation Branch, at (916) 324-3507 or Mark Sippola, Manager, Program Development Section, at (916) 323-1095.

Public Comments

Written comments will only be accepted on the modifications identified in this Notice. Comments may be submitted by postal mail or by electronic submittal no later than 5:00 pm on the due date 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>

Please note that under the California Public Records Act (Gov. Code § 6250 et seq.), your written and verbal 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.

In order to be considered by the Executive Officer, comments must be directed to CARB in one of the two forms described above and received by CARB by 5:00 p.m., on the deadline date for public comment listed at the beginning of this notice. Only comments relating to the above-described modifications to the text of the regulations shall be considered by the Executive Officer.

If you need this document in an alternate format or another language, please contact the Clerk of the Board at (916) 322-5594 or by facsimile at (916) 322-3928 no later than five (5) business days from the release date of this notice. TTY/TDD/Speech to Speech users may dial 711 for the California Relay Service.

Si necesita este documento en un formato alternativo u otro idioma, por favor llame a la oficina del Secretario del Consejo de Recursos Atmosféricos al (916) 322-5594 o envíe un fax al (916) 322-3928 no menos de cinco (5) días laborales a partir de la fecha del lanzamiento de este aviso. Para el Servicio Telefónico de California para Personas con Problemas Auditivos, ó de teléfonos TDD pueden marcar al 711.

CALIFORNIA AIR RESOURCES BOARD



Richard W. Corey
Executive Officer

Date: November 15, 2018
Attachment

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 CARB's website at www.CARB.ca.gov.