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**Catherine H. Reheis-Boyd**

Executive Vice-President and Chief Operating Officer

August 7, 2009

Dr. Lawrence Goulder, Chairman  
AB 32 Economic and Allocation Advisory Committee  
California Air Resources Board  
1001 I Street  
Sacramento, CA 95814

Subject: **AB 32 Implementation – Economic and Allocation Advisory Committee**

Dear Dr. Goulder:

Governor Schwarzenegger, Cal/EPA Secretary Adams and Air Resources Board (CARB) Chair Nichols have given you and the other members of the Economic and Allocation Advisory Committee (EAAC) the responsibility of providing the State of California with recommendations on the design of a Cap and Trade Program that will achieve our greenhouse gas reductions without impairing robust economic growth. The Western States Petroleum Association (WSPA) applauds your committee's willingness to take on that task.

WSPA is a non-profit trade association representing twenty-eight companies that explore for, produce, refine, transport and market petroleum, petroleum products, natural gas and other energy supplies in California and five other western states. WSPA and its member companies are prepared to help you fully assess the potential impact of policy options on California's energy supply and economy.

Throughout the AB 32 implementation process, WSPA has steadfastly re-iterated that CARB must include in its economic impact analysis an assessment of the impact on the availability of adequate, reliable and affordable energy supply for California. Governor Schwarzenegger states in his letter to each EAAC member: "yours is a most important endeavor." Economic and energy policy experts and WSPA all agree -- adequate, reliable and affordable energy supply is critical for a robust economy.

WSPA understands your charge is to develop design recommendations for a cap and trade program for California that is part of and works with a regional market envisioned by the Western Climate Initiative. However, we believe it is equally important for California's program to link and work with the emerging federal program.

While California's cap and trade program must work with the regional and federal markets, it must also work with international markets. Further, it must work with the other complimentary measures proposed in the Scoping Plan, in particular the Low Carbon Fuel Standard (LCFS) for transportation fuels and the Renewable Portfolio Standard (RPS) for electricity.

WSPA believes your effort will help address key questions/issues raised in the language of AB 32 and in CARB's Adopting Resolution for the Scoping Plan. Your work will also be absolutely vital to an overall cost-effective program. Key questions include:

- 1) What is the overall economic impact on California consumers, particularly small businesses, especially taking into account the price forecasts of energy in the second compliance period when transportation fuels are in the program? Moreover, there was considerable controversy over the findings of CARB's economic analysis of the Scoping Plan, evidenced in part by the reaction of the peer reviewers (see the peer review comments at [http://www.arb.ca.gov/cc/scopingplan/economics-sp/peer-review/peer\\_review\\_comments\\_arb\\_responses.pdf](http://www.arb.ca.gov/cc/scopingplan/economics-sp/peer-review/peer_review_comments_arb_responses.pdf)). EAAC is in the position to weigh in on and reconcile these differences.
- 2) What is the overall economic impact of limiting offsets? How will this limitation affect Gross State Product, the price of allocations, emissions and economic leakage? The Board Resolution adopted with the Scoping Plan specifically calls for an analysis of the economic impact of the limits on offsets in the Scoping Plan. To date, this analysis has not been performed by CARB staff. The EAAC are in a position to carry out this analysis.
- 3) What are the potential impacts of California moving forward with a greenhouse gas (GHG) control program that has limited practical linkage with other state, regional, federal and international programs? What would the impacts be if California's program were linked directly to other markets or indirectly through acceptance of tradeable instruments?
- 4) What transitional issues/concerns should be considered as CARB implements the Scoping Plan from 2010 to 2020, particularly those issues/concerns related to the design of the emissions allocation system (free distribution vs. auctions), offsets, and compliance trajectories for GHG reductions? Would a transitional program similar to other international market designs that allows a less stringent approach during the learning phase, (e.g. 5 years, transitioning to a more stringent approach after learning has occurred) be one method to control market volatility and dampen potential differential economic impacts to California's economy?
- 5) What are the key early warning indicators that California should monitor to ensure that any necessary mid-term corrections can be made before our economy is significantly damaged?

WSPA also believes that your efforts to help address the above questions will result in an appropriate and adequate evaluation of cost-effectiveness that is critical to the successful implementation of AB 32. This is because failure to adopt the most cost-effective policies will have significant consequences for the State. Consider that an increase in average emission reduction costs by just \$5 per ton would impose nearly \$1 billion in unnecessary annual costs on the California economy.

### **Limits on Offsets**

Attached is a copy of WSPA's April 30, 2009 comment letter to CARB on the importance of offsets. Our letter highlights that high quality, geographically broad and unlimited quantities of tradable offsets for AB 32 implementation could save California more than \$20 billion in Gross State Product by 2020. WSPA believes our comments remain valid today. We urge EAAC to review those comments and are prepared to discuss them in detail with you and the EAAC.

## **Impact of Transportation Fuels in Cap and Trade on Energy Prices, the Carbon Market and the Economy**

The Scoping Plan envisions adopting cap and trade regulations that, in the second trading period, would bring transportation fuels under the cap and trade program. WSPA has previously commented that CARB should carry out an analysis to determine the effect of putting fuels in a cap and trade system. At a minimum such an analysis should include consideration of the following:

- What effect would including transportation fuel emissions in a market system have on fuel supply (including potential fuel supply disruptions) and on the fuel supply infrastructure?
- What effect would it have on the cost of fuel to consumers (price and volatility)?
- How would the emissions allowance allocation process mitigate or exacerbate changes in fuel supply adequacy or costs to consumers?
- How would inclusion of transportation sector emissions in a cap and trade program (essentially doubling the size of the market) affect the rest of the market?
- How would the inclusion of transportation emission in a market integrate with, affect the design of, obviate the need for, or duplicate other transportation sector policies?
- What are the design elements necessary to ensure equity in a program where a regulated sector (electric sector supply, price and rate of return by the Public Utilities Commission) and an unregulated sector (fossil fuel sector) produce the products and generate the emissions both of which will be affected by the cap and trade program?
- What are other market based approaches for addressing transportation fuels and what might be their affect on potential fuel supply disruptions and price volatility for consumers?

## **Linkages**

One of the design elements that CARB is considering is linkage with other regional, national and international market programs. WSPA believes that EAAC's effort should include an analysis of the implications of California moving forward with limited practical linkage to other programs as compared to a program with broader linkage, such as to the European Union Emission Trading Scheme or a federal program, and that it should also recommend design elements to ensure environmental effectiveness, cost-effectiveness and equity.

## **Transitional Issues**

The AB32 program will push the limits of technology as well as the ability of covered entities to execute emission reduction projects. WSPA requests that EAAC identify the transitional issues during the implementation period of 2010 to 2020 and recommend program designs to address the transitional issues, particularly relative to GHG emission allocations (free distribution vs. auctions), offset use and compliance trajectories for GHG reductions.

## **Early Indicators**

The cap and trade program will affect a significant portion of California's energy market. We believe it is critical that California monitor key early economic indicators so that any mid-term corrections can be made before significant harm is done to our state's economy. WSPA requests that your report include recommendations on the key early warning indicators of the economy that CARB should monitor as part of the AB 32 program implementation.

As stated above, WSPA is prepared to help as you address the myriad issues related to a well-designed cap and trade program ó in particular, the issues highlighted in this letter that we feel are critical to successful implementation of AB 32.

Thank you for considering our comments. We look forward to continuing working with you and CARB staff to ensure the success of your efforts. If there are any questions, please contact me.

Sincerely,

A handwritten signature in blue ink that reads "Cathy Boyd". The signature is fluid and cursive, with the first name "Cathy" and last name "Boyd" clearly legible.

cc: Linda Adams, California Environmental Protection Agency  
Cindy Tuck, California Environmental Protection Agency  
Dan Pellissier, California Environmental Protection Agency  
California Air Resources Board Members  
David Crane, Governor's Office  
John Moffatt, Governor's Office  
James Goldstene, California Air Resources Board  
Edie Chang, California Air Resources Board  
Lucille Van Ommering, California Air Resources Board  
Joe Sparano, President, Western States Petroleum Association

Enclosure