CALIFORNIA CARBON MARKET COLLABORATIVE
COMMENT LETTER TO CARB
17 AUGUST 2023

Re: California Carbon Market Collaborative Comments on CARB's Informal Workshop on Potential Amendments to the Cap-and-Trade Regulation

The California Carbon Market Collaborative (CCMC) appreciates the opportunity to provide public comment on the California Air Resources Board's (CARB) informal workshop on potential amendments to the Cap-and-Trade (C&T) Program held on 27 July 2023.

The CCMC supports the design and implementation of an ambitious and equitable California C&T Program through 2045 and beyond. The CCMC convenes a wide array of C&T stakeholders to deepen mutual understanding and undertake careful examination of key Program design features. Participants of the CCMC include, among others, Environmental Defense Fund, Liminality Capital LP, and Pacific Gas & Electric.[1]

1. **The CCMC recommends prioritizing building out allowance budgets for 2031 to 2045 and beyond.**

The fundamental question facing California's C&T Program is whether it extends beyond 2030. Uncertainties around the existence of the Program beyond 2030 negatively impact California today by stymying long-term emissions-reducing infrastructure projects. Any further clarity CARB can provide on the future of the C&T Program beyond 2030 will deliver additional and immediate benefits to Californians through stronger and more predictable incentives to invest in emissions-reducing infrastructure projects.

An indication of future allowance budgets between 2031 and 2045 would also paint a more complete and accurate picture of the expected role for the C&T Program in achieving California's 2045 climate target. In turn, indicative post-2030 allowance budgets would provide a robust foundation for making decisions about pre-2030 allowance budgets. The CCMC recommends prioritizing building out allowance budgets for 2031 to 2045 and beyond ahead of any formal rulemaking.

It is worth nothing that if CARB extends the C&T Program through 2045 and beyond, then California would provide the certainty necessary for investors to stack carbon market incentives on top of funding from the federal Inflation Reduction Act. In short, an extended C&T Program in California would supercharge new federal subsidies to accelerate decarbonization efforts within our state.

2. **The CCMC supports the 48% by 2030 scenario and is interested in reviewing any modeling results for the 55% by 2030 scenario.**

As background, the CCMC supports the C&T Program playing an increasing role in California's overall climate policy mix over time because the C&T Program is uniquely positioned among the

[1] The CCMC is convened by Elevate Climate, a company dedicated to strengthening carbon markets through analysis and facilitation. For more information on the CCMC, please email alicia@elevateclimate.com.

state's suite of climate policies to lead the achievement of ambitious climate targets for the following reasons.

- Emissions Certainty: The C&T Program responds in real-time by increasing abatement if other policies fail to hit their expected abatement goals. Underperformance of other policies already occurs and may increase as California's climate targets become more ambitious. In this context, the C&T Program provides much needed reassurance by reducing the uncertainty of emissions reductions across California's climate policy mix and thereby improving the likelihood of achieving climate targets.
- Economic Incentives: Compared to direct regulations, technology standards, or government subsidies, an increasing role for a well-designed C&T Program means that California can reduce more emissions more quickly because the market identifies least-cost emissions reductions and incentives emissions-reducing innovations.
- Environmental Justice: According to data provided by the State of California, $6.7 billion of the $9 billion in cap-and-trade revenue implemented by the Legislature since 2013 has benefited disadvantaged and low-income communities and households.[2] In 2022 alone, revenues from the C&T Program were used to implement nearly 19,500 new projects through $1.3 billion in funding, with $933 million of that funding directly benefiting disadvantaged communities and low-income communities and households.[3] In addition, independent academic analysis[4] indicates that the program has narrowed local air pollution disparities over the 2012 to 2017 timeframe, although this favorable outcome is not necessarily guaranteed over time and communities remain concerned over local air emissions. An ambitious well-designed C&T Program can further enhance equitable outcomes such as direct investments and improved local air emissions.

The CCMC supports the 48 percent by 2030 scenario with the adjustment in the emission inventory because cap levels should be aligned such that covered sources achieve at least their proportional share of abatement relative to uncovered sources called for by the 2022 Scoping Plan. If the C&T Program were to play a lesser role, then California would be put in the position of fighting to achieve the 2022 Scoping Plan goal with one hand tied behind its back.

The CCMC supports CARB's ongoing efforts to conduct economic modeling of the 55% by 2030 scenario. Information on the impact of proposed changes on allowance prices will not only inform preferences on scenario selection but also inspire ideas for alternative policy designs. The more information available ahead of the formal rulemaking the better.

3. The CCMC supports integrating high-quality carbon management into the existing C&T Program.

In light of recent passage of Assembly Bill 1279 and Senate Bill 905, and the significant reliance on carbon management in the 2022 Scoping Plan, it is crucial that high-quality management is properly accounted for and incentivized by the C&T Program. A market-based approach would allow for an efficient allocation between removals and reductions within the constraints imposed by Assembly Bill 1279, leading to more affordable outcomes. There are a number of recent

[2] California Climate Investments: https://www.caclimateinvestments.ca.gov/priority-populations.
[3] California Climate Investments: https://www.caclimateinvestments.ca.gov/.
[4] Hernandez-Cortes, Danae and Kyle C. Meng. 2023. "Do Environmental Markets Cause Environmental Injustice? Evidence from California's Carbon Market". *Journal of Public Economics* 217: 104786.

studies that outline an array of policy options for incorporating high-quality carbon management approaches into cap-and-trade programs, including a recent effort by the International Carbon Action Partnership.[5] The CCMC will convene with stakeholders to discuss which approach may be most suitable to California's context.

4. **The CCMC suggests incorporating further design details into CARB's modeling efforts.**

The benefits and costs of the scenarios under consideration depend not only on overall ambition but on a number of detailed policy design issues. The CCMC suggests modeling the impact of removing allowances from different pools of allowances for each scenario including retiring from the price ceiling and different combinations of auctioned and allocated allowances. Impacts should be described not only in economic terms (i.e., allowance price or overall cost) but also in environmental terms (e.g., does removing allowances from the pool under consideration lead to lower overall emission levels). More detailed modeling results would inform preferences on a number of policy issues including scenario choice, the design of price containment reserves, and consideration of an emissions containment reserve.

5. **The CCMC suggests modeling an alternative scenario for the Standardized Regulatory Impact Assessment.**

The typical process for a Standardized Regulatory Impact Assessment (SRIA) is not well-suited for the C&T Program given that it is an economy-wide market-based policy. Specifically, the "cost" of the C&T Program must be compared to what policy would achieve emissions reductions instead of the C&T Program. In theory and in practice, all other policies would be more expensive in terms of dollars per ton of emission reduced, as evidenced by many analyses and studies. Therefore, arguments for not fully relying on cap-and-trade need to be based on evidence unrelated to costs, such as adverse competitiveness impacts or emissions leakage rates. In this context, it is worth noting that command-and-control policies often create adverse competitiveness impacts and emissions leakage rates, which should be fully noted in any economic analysis undertaken by CARB.

The CCMC recommends modeling an alternative scenario when CARB begins the SRIA process. Given the substantial uncertainty surrounding the performance of regulatory policies, it may be useful to model an alternative scenario or set of scenarios that involves designs capable of adjusting to the *actual* performance of regulatory policies over time.

There are many potential alternative scenarios that may be worthwhile to model. Among these options, the CCMC highlights one example below that facilitates "flexing" between the 48% and 55% scenarios based on market outcomes, while noting that this example could be applied to other emissions scenarios.

An emission containment reserve could be considered such that if allowance prices at quarterly auctions sit at or below a predetermined trigger price, then a specified quantity of supply is withheld. The *maximum* quantity of supply withheld via an emissions containment reserve could be set equal to the difference between the 48% and 55% scenarios under consideration (125

[5] International Climate Action Partnership. 2021. Emissions Trading Systems and Net Zero: Trading Removals. Available here: https://icapcarbonaction.com/en/publications/emissions-trading-systems-and-net-zero-trading-removals.

million allowances = 2,340 allowances for 48% scenario minus 2,215 allowances for the 55% scenario).

- For example, if we assume that every one of the 24 auctions[6] between 2025 and 2031 triggers the emissions containment reserve, then 125 million allowances worth of supply would be withheld.
- As another example, if we assume that only one of these auctions triggers the emissions containment reserve, then ~5 million allowances (125 million allowances divided by 24 auctions) worth of supply would be withheld at a single auction.

Such a scenario is worthwhile to consider because it allows pre-2030 allowance budgets to adjust to the *actual* performance of regulatory policies, rather than setting pre-2030 allowance budgets based on *estimated* future performance of regulatory policies.

The difficulties in estimating the performance of regulatory policies nearly a decade into the future are virtually unsurmountable but the resulting uncertainty is easily addressed with a design approach that dynamically responds to market signals in real time.

Conclusion

The CCMC applauds CARB's leadership in updating California's C&T Program. We look forward to engaging with staff and stakeholders to ensure an ambitious and equitable Program through 2045 and beyond.

Sincerely,

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[6] Six years between 2025 when regulations may be adopted and 2031 when regulations expire multiplied by four auctions per year.