

Stakeholder Input Key to Success in Implementing Climate Change Law

Much has changed since Governor Arnold Schwarzenegger signed AB 32, The Global Warming Solutions Act of 2006. Two years since its passage, the bill has spurred a regulatory program that is more far-reaching than any other and that affects all consumers and businesses in the state. California continues to be watched by other states and nations as the process moves forward.

In December 2008, the California Air Resources Board (ARB) adopted the "Scoping Plan" for implementing AB 32. This plan includes the overall framework for achieving the greenhouse gas (GHG) reduction goals outlined in the bill. It includes strategies and reductions that are expected from various sectors. Without question, it will affect the entire California economy in some capacity.

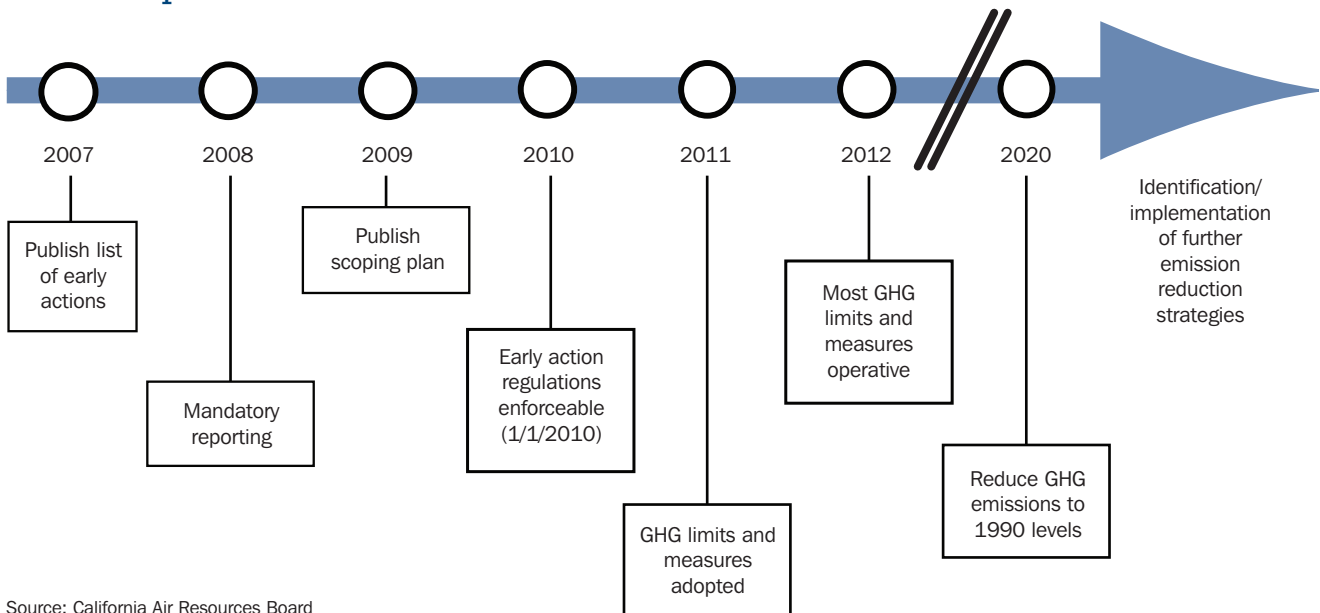
The amount of regulatory uncertainty due to the nature of the Scoping Plan is a rising issue for businesses and industries statewide. With the state's grim economic outlook for the current fiscal year,

the business community is increasingly concerned about the additional costs that are expected from this plan.

The Implementation Timeline

The timeline for implementation is tight, especially considering the broad scope of the plan. Thus far, ARB has focused on implementing the reporting guidelines, creating a framework for the various "discrete early actions," such as the Low Carbon Fuel Standard, and developing the Scoping Plan. Now that the Scoping Plan is complete, ARB will work on implementing the actual strategies through regulatory proceedings. Each strategy will go through its own regulatory process with the expected workshops, stakeholder meetings and analysis. With the 2010 enforcement date for the discrete early actions just around the corner, and 2012 just a few years away, however, it is clear that the regulatory process will be busier and further demanding.

AB 32 Implementation



Source: California Air Resources Board

The Cap

One of the ARB's more important tasks since the implementation process began was to set the cap for the 2020 goal. This GHG cap is based on the state's 1990 GHG emission levels, which amounts to an approximately 30 percent reduction from "business as usual." According to the Scoping Plan, ARB estimates that business-as-usual emissions in 2020 would be 596 million metric tons of CO₂ (MMT_{CO₂E}) if there were no cap. The ARB believes that with the Scoping Plan in place, the state can reduce emissions to 422 MMT_{CO₂E} by 2020. This is a very significant reduction and will require businesses and industry to drastically alter practices in order to reach the 422 MMT cap.

The chart illustrates that there are a total of 146.7 MMT_{CO₂E} in reductions coming from capped sectors. These are the sectors that would be included under a cap-and-trade system. The sectors include transportation, electricity, commercial and residential, and industry. An estimated 27.3 MMT_{CO₂E} would come from those sectors that are not under the

cap-and-trade system, which includes sources such as sustainable forests and landfills.

Heavy Control Measures

Although the Scoping Plan includes a cap-and-trade system as an element to reach the 2020 cap, a number of the sectors under the market would be subject to specific strategies the ARB has prescribed in the Scoping Plan. Just to name a few: the Low Carbon Fuel Standard (LCFS), a 33 percent Renewable Portfolio Standard (RPS), and industry measures such as energy efficiency and co-benefit audits are listed as key strategies to achieving the reductions.

The table lists all the recommended measures the ARB is looking to implement in the coming years. As seen on the list, transportation measures such as the Pavley vehicle standards (named for the author of the legislation requiring the standards) account for a significant amount of the reductions. The ARB also is relying on the LCFS to garner additional reductions in the fuels sector.

Businesses are concerned about a

number of the measures outlined in the table. Many of the measures are very difficult to pursue, given various obstacles. As explained in the energy article in this *Guide*, for example, a 33 percent RPS target has been set through the Governor's executive order, but many issues tied to transmission planning and the cost of renewables still exist. In addition, the ARB has attributed 5 MMT_{CO₂} to regional transportation-related targets while much debate and many questions exist about what methodology and what threshold actually should be used for land use development and transportation planning in the state.

The ARB also has included imposing new building standards for both residential and commercial buildings. The plan supports the establishment of an environmental performance rating system and suggests the state "adopt mechanisms to encourage and require retrofits for buildings that do not meet minimum standards of performance."

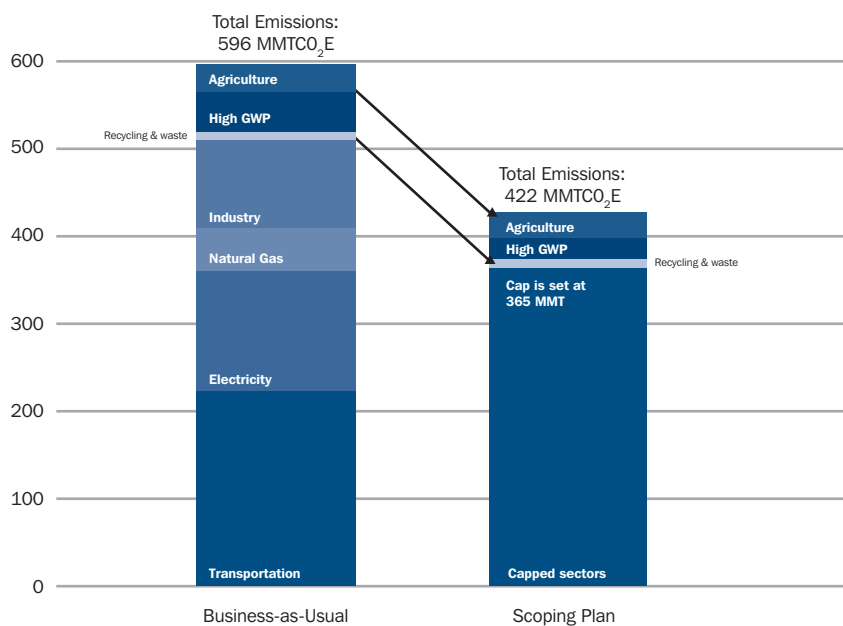
Developers are concerned about the additional cost that would result from more command-and-control standards placed on buildings. New building requirements could add tens of thousands of dollars to home prices, making new homes less affordable and marketable in the existing economy, as described further in this *Guide*.

Business stakeholders are hoping that ARB minimizes the use of control measures that would limit industry's ability to meet their targets through the market. Industry is concerned that more control measures will make it extremely difficult to minimize costs and that the market will be limited in scope due to the major reductions required through these measures.

CEQA and AB 32

Further complicating AB 32 implementation is the question of how land use projects should be evaluated for their climate change impacts pursuant to the California Environmental Quality Act (CEQA). Under CEQA, a land use project must undergo an extensive environmental review process, which in the past did not generally include consideration of GHG emissions. Because of the state's concerted efforts to regulate GHG emissions in California, however, that trend is changing and the political reality is that CEQA documents will most likely require

Greenhouse Gas Emissions in 2020 and Recommended Reduction Measures



Source: *Climate Change Proposed Scoping Plan*, California Air Resources Board (October

Recommended Greenhouse Gas Reduction Measures

Recommended Reduction Measures	Reductions Counted Towards 2020 Target (MMTCO ₂ E)
ESTIMATED REDUCTIONS RESULTING FROM THE COMBINATION OF CAP-AND-TRADE PROGRAM AND COMPLEMENTARY MEASURES	
	146.7
California Light-Duty Vehicle Greenhouse Gas Standards <ul style="list-style-type: none"> Implement Pavley standards Develop Pavley II light-duty vehicle standards 	31.7
Energy Efficiency <ul style="list-style-type: none"> Building/appliance efficiency, new programs, etc. Increase CHP generation by 30,000 GWh Solar Water Heating (AB 1470 goal) 	26.3
Renewables Portfolio Standard (33% by 2020)	21.3
Low Carbon Fuel Standard	15
Regional Transportation-Related GHG Targets ¹⁶	5
Vehicle Efficiency Measures	4.5
Goods Movement <ul style="list-style-type: none"> Ship Electrification at Ports System-Wide Efficiency Improvements 	3.7
Million Solar Roofs	2.1
Medium/Heavy Duty Vehicles <ul style="list-style-type: none"> Heavy-Duty Vehicle Greenhouse Gas Emission Reduction (Aerodynamic Efficiency) Medium- and Heavy-Duty Vehicle Hybridization 	1.4
High Speed Rail	1.0
Industrial Measures (for sources covered under cap-and-trade program) <ul style="list-style-type: none"> Refinery Measures Energy Efficiency & Co-Benefits Audits 	0.3
Additional Reductions Necessary to Achieve the Cap	34.4
ESTIMATED REDUCTIONS FROM UNCAPPED SOURCES/SECTORS	
	27.3
High Global Warming Potential Gas Measures	20.2
Sustainable Forests	5.0
Industrial Measures (for sources not covered under cap and trade program) <ul style="list-style-type: none"> Oil and Gas Extraction and Transmission 	1.1
Recycling and Waste (landfill methane capture)	1.0
TOTAL REDUCTIONS COUNTED TOWARDS 2020 TARGET	
	174
Other Recommended Measures	Estimated 2020 Reductions (MMTCO ₂ E)
State Government Operations	1-2
Local Government Operations	TBD
Green Buildings	26
Recycling and Waste (other measures)	9
Water Sector Measures	4.8
Methane Capture at Large Dairies	1.0

¹⁶ This number represents an estimate of what may be achieved from local land use changes. It is not the SB 375 regional target. ARB will establish regional targets for each Metropolitan Planning Organization (MPO) region following the input of the Regional Targets Advisory Committee and a public consultation process with MPOs and other stakeholders per SB 375.

Source: *Climate Change Proposed Scoping Plan*, California Air Resources Board (October 2008.)

a level of climate change analysis in the near future.

Legal Challenges

In 2007, as legal challenges mounted against projects lacking climate change evaluation, several trial courts addressed the CEQA issue. Three trial courts denied plaintiffs' requests to force climate change consideration on specific projects, while other cases settled out of court. Most notable was Attorney General Jerry Brown's lawsuit against San Bernardino County

filed in April 2007 (*People v. County of San Bernardino*), which claimed that the county should be forced to consider the climate change impacts of its General Plan. San Bernardino officials settled with Brown in August of that year by agreeing to identify the sources of GHG emissions in the county and draw up plans for reducing their overall emissions.

Significantly, Brown's settlement sent a clear signal to stakeholders that suing projects on this basis could produce

results and effectively force defendants to either make mitigating concessions or risk having the project tied up in the court system indefinitely.

Who's in Charge?

AB 32 clearly spells out that ARB is the sole agency charged with regulating GHG emissions in California. In fact, supporters of AB 32 insisted that ARB be given total authority to regulate GHG emissions due to the agency's expertise. Under AB 32's timeline, ARB has been given until 2012 to develop and implement regulations that will account for, cap and reduce California's GHG to 1990 levels by 2020. Part of this process will be determining the appropriate role for CEQA in addressing climate change.

To help in this process, SB 97 was passed in 2007 during the budget impasse, requiring the Governor's Office of Planning and Research (OPR) to develop guidelines for the State Resources Agency that address how climate change impacts should be mitigated under CEQA. The Resources Agency is required to adopt OPR's recommended guidelines by January 2010. Before this date, OPR has been able to provide only informal guidance to CEQA lead agencies on how to plan for addressing climate change in the future.

While these guidelines are being developed, ARB will be simultaneously developing official rules on how sources of GHG emissions will be regulated in order to reduce the state's carbon footprint. Because of these parallel efforts, it is important that the adoption of OPR's guidelines be coordinated with ARB's final land use-specific regulations so that the many uncertainties surrounding climate change analysis and mitigation under CEQA are removed.

Impacts

Failure to remove these uncertainties could be devastating for California's economy. Historically, CEQA has been the basis for an abundance of lawsuits that have stalled land use projects by tying them up in the court system indefinitely. This problem will certainly be intensified if projects continue to be sued for not following GHG rules and regulations that do not yet exist. Not only is this illogical, but it directly subverts the authority AB 32 granted to ARB to be the lone agency charged with regulating GHGs in California. Until official regulations are adopted and in effect, it is imperative that land

use projects are not held liable or put on hold indefinitely for failing to address their potential climate change impacts.

Determinations of Significance

One of the keys to ensuring that future CEQA regulations requiring climate change analysis are successful will be appropriately determining what levels of GHG emissions would qualify as significant, thus requiring mitigation from a project. The global nature of GHG emissions suggests that a statewide threshold of significance for GHG emissions is a superior approach to creating project-specific thresholds.

Accordingly, in determining whether a proposed project's GHG emissions may have a significant impact on climate change, CEQA lead agencies should consider whether, among other factors, the project complies with emissions standards promulgated by ARB under AB 32, the air districts, or by other state agencies or commissions applicable to new and existing GHG emissions sources.

If a project does meet applicable standards promulgated by ARB, the air district or other state agencies/commissions, then it should be determined that the project does not have a significant impact on climate change. Such an approach will provide much-needed certainty to project proponents and will encourage consistency and uniformity in the CEQA analysis of GHG emissions throughout the state.

Alternatively, project-specific thresholds could create the counterproductive effect of driving highly desirable projects outside of California, with the further unintended effect of causing global GHG emissions to rise as the distance between energy supply and consumption increases.

Cap-and-Trade

A key aspect to developing a market structure will be to ensure that it remains cost-effective and makes real reductions in greenhouse gas emissions. There is no doubt that a cap-and-trade system has the ability to garner significant reductions in CO₂ if designed appropriately. A cap-and-trade system is a market-based tool that industries can utilize to reduce their GHG emissions. Under such a system, industries are regulated under a strong cap, but would have the ability and time to reduce emissions, both on- and off-site. The structure would run as a marketplace where carbon is the commodity.

California has become a model for the rest of the nation. It is under the microscope as neighboring nations are watching how ARB is designing the framework for the GHG program. The framework contained in the Scoping Plan includes a cap-and-trade system as one of the many tools to get to 2020 goals and beyond.

Currently, California is working with six other states as part of the Western Climate Initiative (WCI) to design a cap-and-trade system for the region (see map on next page). According to the Scoping Plan, California's cap-and-trade market would link to the regional WCI system to allow for regional trading. It is clear that if California does not pursue a cap-and-trade route, there is not much hope for the WCI effort to succeed.

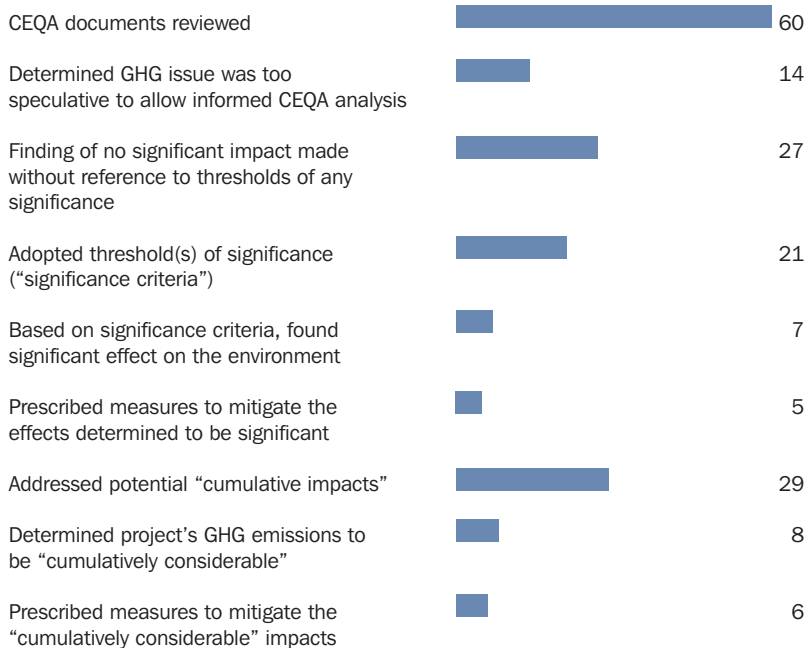
Furthermore, California is unique in that it has a hard cap. The other participating states are not bound by a cap in statute. There is ongoing concern that California businesses will be disadvantaged, given that neighboring states do not have such a hard cap for their businesses.

Allowance Allocation

A key design element to the cap-and-trade market is how the allowances (ability to emit) are distributed. If the allowances are distributed via an auction, industries will have to bear additional cost, whereas if the allowances are freely allocated, industry would have more flexibility to invest in on-site improvements and energy-efficient equipment that can further reduce emissions. Auctioning allowances to the capped sectors will act as a tax on regulated industry because each entity would have to pay for each ton emitted, depending on the auction percentage.

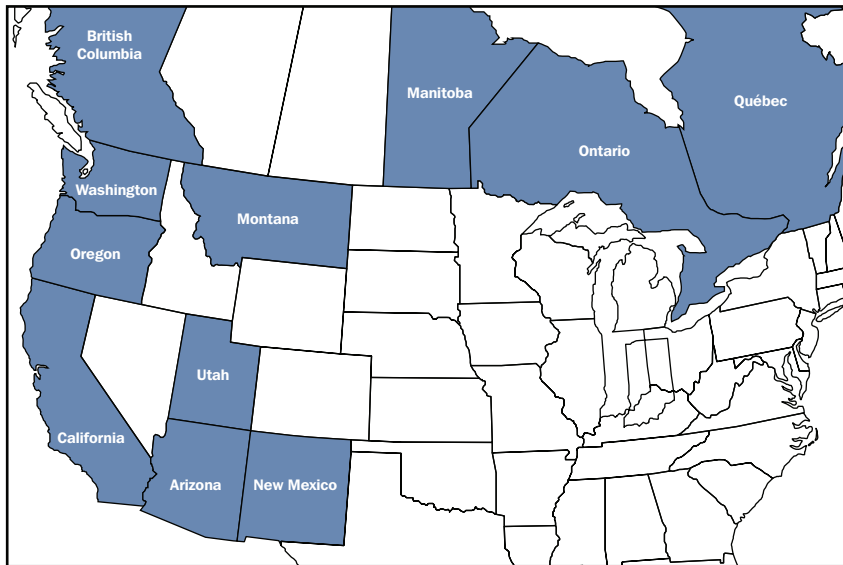
According to the Scoping Plan, ARB believes that "a transition to a full auction is a worthwhile goal for distributing allowances." The WCI process also is proposing to use an auction method to allocate allowances, starting with 10 percent for the first three years and then increasing the auction percentage to 25 percent in 2020. The business community, however, is very concerned that jumping into an auction system will amount to

California Litigation Greenhouse Gas/California Environmental Quality Act Analysis



Source: James T. Burroughs and Heather S. Riley, "Fitting Climate Change Into CEQA," *California Litigation*, State Bar of California, 2008.

Western Climate Initiative Partners



a multibillion-dollar tax on industry that will only make current economic conditions worse.

Offsets

One of the more controversial issues discussed in the Scoping Plan is the use of offsets to reach GHG emission reductions in the state and beyond. Offsets allow regulated industries to develop projects either off-site or in other regions to reduce emissions. Due to the global nature of climate change, offsets can play a large role in mitigating GHGs emissions in regions that are less-efficient than California.

The Scoping Plan discusses the need for offsets and recognizes that there should not be regional boundaries for the use of offsets if they are real and verifiable. According to the plan: "High quality offset projects located outside California can help lower compliance costs in California while reducing GHG emissions in areas that would otherwise lack the resources needed to do so." Of particular interest would be regions such as Mexico, where there is much opportunity to reduce emissions right at the state's border. Many offset projects are being developed in China and India, where there is an increase in energy use and emissions.

The plan does, however, speak to restricting the amount of emissions an

entity can offset in a compliance period. ARB will develop a limit on offsets to achieve a certain amount of reductions on-site. According to the WCI program design, no more than 49 percent of each partner jurisdiction's total emission reductions comes from offsets or other trading systems. It is uncertain whether ARB will defer to the WCI limits or develop a different quantitative limit. Regardless, regulated entities are facing considerable costs because only a portion of the reductions will be made through market structures.

Program Funding

The Scoping Plan proposes a number of new funding mechanisms that would help pay for the regulatory program and reduction strategies. For example, ARB recommends placing a public goods charge for water collected on water bills to pay for water efficiency improvements, water recycling and other such actions. The ARB estimates such a fee could generate up to \$500 million annually. In addition, ARB has calculated that it will need \$55 million annually just to fund the administration, implementation and enforcement of the emission reduction measures. To fill this gap, ARB will create a fee regulation to present to its board in early 2009. ARB is looking to start collecting these fees from regulated entities

in the 2009-10 fiscal year.

As mentioned earlier in this article, ARB is looking to "auction" allowances to those entities participating in the cap-and-trade market. The revenues collected from this auction could be used for a number of activities.

The Scoping Plan outlines the following:

- Funding energy efficiency and renewable resource development.
- Achieving environmental co-benefits (criteria and toxic pollutant mitigation).
- Incentives to local governments.
- Consumer rebates.
- Direct refunds to consumers.
- Climate change adaptation programs.
- Subsidies.
- Research, development and demonstration funding.
- Worker transition assistance.
- Administration of GHG program.
- Direct emission reductions.

The above is a snapshot of what ARB is looking to fund through potential auction revenue. The regulated community is concerned about the fees and costs associated with the implementation of AB 32. When added up, the multiple proposed costs will be heavy for California consumers and businesses. It is certain that ARB will have to work hard to find a way to fund its program while keeping economic concerns in mind.

Emerging Action on National Front

Shortly after being elected, President Barack Obama stated that his presidency "will mark a new chapter in America's leadership on climate change that will strengthen our security and create millions of new jobs in the process. That will start with a federal cap-and-trade system. We will establish strong annual targets that set us on a course to reduce emissions to their 1990 levels by 2020 and reduce them an additional 80 percent by 2050."

These remarks at the Governors' Global Climate Summit in November 2008 help describe what is to be expected in the coming years. With a new federal administration and Congress, climate change issues have taken on a new precedence. Furthermore, with Republican leaders such as U.S. Senator John McCain highly supportive of climate legislation, the country is moving even closer to developing a nationwide cap. Although California has gotten a signifi-

cant head start in this process, it is vital for the state to align itself with the future national program to prevent duplication and to minimize regulatory uncertainty. If designed unilaterally, California's program could cost more for the state's consumers and businesses.

CalChamber Position

The California Chamber of Commerce will work to minimize the compliance costs by actively pushing for measures that effectively reduce carbon while allowing for continued economic growth. All regulations created by ARB should be implemented with stakeholder input. It is impossible to create a successful program and achieve real, quantifiable reductions without understanding the various industries targeted by the regula-

tions. Furthermore, regulations should be developed in a way that allows for business growth in California.

The CalChamber believes that for the state to be a true leader on this issue, it needs to share its proven energy efficiency knowledge while harnessing the innovation and creativity of its citizens to pioneer new, low-carbon technologies. In fact, policy approaches that recognize and encourage California's leadership and innovation in the environmental arena can be more effective than taxes or fees. Successful technologies developed in California and implemented throughout the world could provide a win-win situation for California businesses by both helping to reduce greenhouse gas emissions here and in other nations, and providing jobs in the state.



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