

South Bay Cities Council of Governments

November 20, 2014

TO: SBCCOG Board of Directors

FROM: Steve Lantz, Transportation Director

SUBJECT: California Cap and Trade Program Overview

Adherence to Strategic Plan:

Goal A: Environment, Transportation, and Economic Development. Facilitate, implement and/or educate members and others about environmental, transportation, and economic development programs that benefit the South Bay.

BACKGROUND

What is Cap-and-Trade?

Cap-and-Trade is a government regulatory strategy that creates a price and a market mechanism for reducing Greenhouse Gas (GHG) carbon emissions, which are considered contributors to global warming. Cap-and-trade sets a firm limit on GHG emissions while minimizing the compliance costs for owners of major GHG emission sources to achieve the GHG emission reduction goals. This reduction is accomplished by establishing a market for selling or trading permitted emissions. Governments impose a limit (cap) on the amount of CO² that may be released by industry and then issue a finite number of permits for allowable emissions. The trade side of the equation occurs when those permits are then auctioned or given away by governments and then sold in a secondary market. Businesses are also free to sell excess permits that they don't need, allowing market forces to distribute and price these allowances. Revenues from the public auctions of the permits are used to fund governmental GHG emission reduction strategies that offset the permitted emissions.

The California Cap-and-Trade Program

The California Air Resources Board (ARB) established a cap-and-trade regulatory program in early 2012 pursuant to AB 32, the California Global Warming Solutions Act of 2006. The AB 32 Scoping Plan identified a cap-and-trade program as one of the strategies California is employing to reduce the greenhouse gas (GHG) emissions to 1990 levels by the year 2020, and ultimately achieve an 80% reduction from 1990 levels by 2050. The ARB rules and regulations to implement the program were effective beginning January 1, 2013. Relevant regulations appear at sections 95800 to 96023 of title 17, California Code of Regulations.

The California cap on statewide GHG emissions from major sources, which is measured in metric tons of carbon dioxide equivalent (MTCO₂e), will decline over time, achieving GHG emission reductions throughout the program's duration. The largest businesses in the state—defined as those that emit more than 25,000 tons of carbon dioxide a year—have to get permits from the state government for those emissions. Businesses under nearly every industry are covered, including refineries, food processors, manufacturers, and utilities.

The state gives out the majority of these permits free, and has developed an auction system to distribute the rest.

State regulators capped allowed emissions for the industries covered in 2014 at 160 million metric tons. The plan calls for the California GHG emissions cap to decline approximately 3 percent each year. However, in 2015, that goal will jump to 395 million metric tons, when it is expanded to include gasoline wholesalers to capture emissions from the gasoline refining process. The program will cap emissions at 334 million metric tons by 2020 to help satisfy a mandate by the state legislature that emissions in the state that year equal 1990 levels.

Since November 2012, there have been eight quarterly auctions in California. Two pools of allowances were sold at each auction: one controlled by the utilities, which receive all of their allowances free, and another controlled directly by the state. Per ARB guidance, investor-owned utilities are required to sell all of their allowances and then buy back what they need to cover their own emissions. The allowances in the state-controlled pool are sold directly to businesses that need them. About 90% of the state-issued permits are still given away. The state has sold \$2.27 billion of CO2 allowances—\$1.4 billion from the utility-controlled pool and the balance from the state pool.

The utilities have to spend their proceeds on things like alternative or renewable fuels, or by giving relief to customers.

Cap-and-Trade Auction Revenue Funding Opportunities

The state's share of revenue from the auctions is allocated to the state's Greenhouse Gas Reduction Fund. The funds are then allocated to specified state agencies for implementation of their GHG reduction programs through the annual state budget process.

SB 535 (Chapter 830 of the 2012 Statutes) requires the California Environmental Protection Agency to identify disadvantaged communities for investment opportunities. The law also requires the Department of Finance to allocate 25% of the available moneys in the Greenhouse Gas Reduction Fund to projects that provide benefits to disadvantaged communities, as specified, and to allocate a minimum of 10% of the available revenues in the Greenhouse Gas Reduction Fund to projects located within disadvantaged communities.

A total of \$832 million in auction funding has been allocated across 12 project categories to state agencies through the FY 2014-15 state budget. Most of the categories are one-time allocations with out-year allocations subject to annual budget appropriations. There are exceptions, high speed rail has an ongoing allocation of 25% and sustainable communities and clean transportation programs will be allocated 35% of ongoing revenues.

The FY 2014-15 appropriations by category are:

<u>Investment Category</u>	<u>Administrative Department</u>	<u>2014-15 \$</u>
California High Speed Rail	High Speed Rail Commission	\$250 mil.
Sustainable commun. / affordable housing	Strategic Growth Council	\$130 mil

Low carbon transit operations	State Transit Assistance	\$25 mil.
Transit & Intercity Rail Capital	Caltrans	\$25 mil.
Low Carbon Vehicles / Rebates	Air Resources Board	\$200 mil.
Energy efficiency upgrades / weatherization	Community Services & Dev.	\$75 mil.
Water diversion	Cal Recycle	\$25 mil.
Wetlands and watershed restoration	Fish and Wildlife	\$25 mil.
Public Bldg. Energy efficiency retrofits	Energy Commission	\$20 mil.
Fire prevention / urban forestry projects	Forestry & Fire Prev.	\$42 mil.
Agricultural energy & operational efficiency	Food & Agriculture	\$15 mil.
	Total	\$832 mil.

Details on the specific funding opportunities are expected to be released over the next few months by the departments that are administering the 12 programs.

Information on the quarterly cap and trade auction programs and agencies responsible for allocating auction proceeds is available here:

<http://www.arb.ca.gov/cc/capandtrade/auctionproceeds/budgetappropriations.htm>

SB 535 text is available here: http://www.leginfo.ca.gov/pub/11-12/bill/sen/sb_0501-0550/sb_535_bill_20120930_chaptered.html

The FY 2014-15 state budget section on Cap and Trade Expenditures is available here:

<http://www.ebudget.ca.gov/2014-15/pdf/Enacted/BudgetSummary/CapandTradeExpenditurePlan.pdf>

More background information on the California Cap-and-Trade program is available on the ARB website at: <http://www.arb.ca.gov/cc/capandtrade/capandtrade.htm>.

RECOMMENDATION

Receive and file.

Reviewed and approved by Kim Fuentes