

Environmental Law

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California Air Resources Board Finalizes Cap and Trade Regulation

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It was another all-day hearing filled with testimony about the effects of climate change and about the repercussions of the California Air Resources Board's ("CARB" or "Board") proposed cap and trade regulation. It was a scene that has played out many times over the past three years.

Stakeholders were making one last argument in front of the Board before another vote on the initial version of the regulation. At the end of the day, the Board produced a unanimous vote in support of California's fledgling market-based approach to reducing greenhouse gases. What it wasn't, was an ordinary meeting. This vote was different. This vote was the *final* vote needed for program approval. It was the concluding vote in what had become a multi year regulatory development process aimed at establishing the nation's first economy wide carbon cap and trade program.

There was testimony on both sides of several key remaining issues, and in a display of robust public policy the Board actively questioned staff and stakeholders on various topics. But their 8-0 vote cemented the state once again as an environmental progressive willing to forge ahead where others have not.

It is hard to understate the importance of this vote. Once this regulation becomes effective in January 2012, it will change the economics of California's energy and transportation sectors, probably forever. Depending on which side of the debate you're on, this is either a breakthrough, or a breakdown, of public policy.

More than 80 speakers provided testimony and many urged the Board to change the proposed rule to minimize costs or adjust one of a myriad of implementing provisions, including costs, allocations, reporting requirements, definitions, and offset buyer liability requirements. There was a sense of finality that hung over the room prior to the historic vote.

Because the statutory clock had basically run out on CARB (due to a one-year limit on the public process, the final staff report being due October 28, 2011), the Board was in an unusual position, and was only authorized to approve or deny the environmental review packet associated with the proposed regulation. No changes to the regulation itself could be made. Any amendments to the regulation would have to occur in a separate, future rulemaking, as any such requests by the Board could only be put in the context of future review and analysis to be included in the adopting resolution.

The Board made plenty of requests of staff for future amendments. The draft adopting resolution was 13 pages long before the day started.

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After debate, discussion, a recess of the hearing and final statements from staff, additional clauses were included. They related to distribution of allowance value related to water supply, continued work with the CPUC, CEC, and Cal-ISO on "point of regulation" issues for imported power and carbon cost pass-through, evaluating the life cycle emissions of waste-to-energy operations, and expanding the work being done to understand the needs of the state universities to evaluate the use of auction revenue for compliance.

In reality, those are the weedy details that make the program run. In the bigger picture, the fact that a major economy is implementing a cap and trade program was the headline news.

The program will start in 2012 with compliance obligations starting in 2013. The first public auction of allowances (cap and trade compliance instruments) will be on August 15, 2012. This auction, along with preliminary third-party trading, will set the initial price tag of the program.

To ensure that the program had sufficient oversight in the coming years, the Board asked for quarterly updates on the program from CARB staff. The resolution also outlines a series of amendments or tweaks to the program that will be brought back to the Board starting in mid summer of 2012. Each one of these potential changes to the regulation will need to go through a complete rulemaking process, including environmental review and updated economic analysis. It can be reasonably anticipated that CARB will only open up that small portion of the cap and trade regulation in need of changes, with the bulk of the program not available for amendment or public comment. It is this fact more than anything that makes the recent final vote that much more important.

This regulation is the last major piece to the greenhouse gas reduction puzzle laid out in the 2008 Scoping Plan as required by AB 32. The other major regulatory pieces include the Renewable Electricity Standard, California's Clean Car Standards, and the Low Carbon Fuel Standard. AB 32 requires the state to reduce carbon dioxide emissions to 1990 levels by 2020. Together they make a complex web of regulations that can't be ignored.

The professionals at Manatt are fully engaged in this issue and those issues surrounding California's efforts to reduce greenhouse gases. For additional information on how this ruling or the pending Cap and Trade regulatory requirements will affect you, or for assistance participating in CARB's continued rulemaking process, contact [Jon Costantino](#) at 916-552-2365 in the [Energy, Environment & Natural Resources](#) practice group at [Manatt, Phelps & Phillips, LLP](#). Jon Costantino is also the Executive Director of the Association of Carbon Market Participants.

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