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California Releases Proposed Cap and Trade Regulation

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On October 28th, the [California Air Resources Board \(CARB or Board\)](#) published their proposal for the country's first economy-wide [Cap and Trade regulatory program](#). The long-awaited 3,500-page package includes the [proposed regulation \(182 pages\)](#), various appendices, and a focused environmental and economic analysis. But most importantly, it provides stakeholders with the answers to the big-ticket policy questions that have surrounded the proposed program for over a year.

Also released for public comment are the proposed changes needed to update California's existing Mandatory Reporting Regulation so it meshes with the Cap and Trade program. The dual 45-day public [comment](#) periods for the regulations start on November 1st and continue until the Board hears both items on December 16th and/or 17th.

It is safe to say that the Cap and Trade regulation was the most anticipated environmental document of the year. This multibillion-dollar program is the centerpiece of California's climate change mitigation program. Its release date had been postponed several times, but it needed to be released last week to ensure meeting the end-of-the-year deadline established by AB 32. The timing of the release came just four days before California's November 2nd election when voters will have the rare opportunity to impact such a large state policy by delaying the entire climate change program by passing [Proposition 23](#). Though Proposition 23 is behind in polling, if it were to pass, CARB still intends to take these regulations to their Board in December knowing that they would not be able to implement them right away.

The Cap and Trade program design followed the [Proposed Draft Regulation](#) issued last November in its basic structure. Beginning in 2012, large industrial sources will be subject to obtaining carbon allowances to cover their greenhouse gas emissions. The program will expand to include natural gas and transportation fuels in 2015. The biggest outstanding policy questions surrounded the allocation methodology (how carbon credits will be distributed and if they would be sold or given away) and the limits to which carbon offsets could be generated and used. Acknowledging the climate of both the state and national economies, the Board opted to freely distribute the vast majority of allowances in the beginning of the program. This soft-start approach was designed to include a variety of other cost-containment mechanisms as well and is seen as way to help ensure that the program actually gets adopted in the face of extreme political opposition, including Proposition 23.

California is proposing to link this program with other jurisdictions participating in the [Western Climate Initiative \(WCI\)](#). Currently, those jurisdictions planning on moving forward with a program in 2012 include New Mexico and four Canadian provinces. But any additional linkage to established programs and their pools of existing credits is not being

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allowed at this time and will require an additional rulemaking effort to modify the program. Only four offset protocols will have the initial blessing of the Board: U.S. Forests, Urban Forests, Dairy Digester and Ozone Depleting Substances. Also, the amount of allowable offsets has been increased from four to eight percent to account for CARB's introduction of a strategic allowance reserve (credits held back to soften potential credit price spikes).

The [staff report](#) openly acknowledges that this is a complex issue and that the CARB staff is still seeking comments to help finalize the regulation before the final Board vote in December. The bottom line is that this is a very complicated issue with huge implications for California's economy. For further information regarding the proposed Cap and Trade regulations, or for assistance participating in CARB's rulemaking process, please contact [Jon Costantino](#) or any attorney in the [Energy, Environment & Natural Resources](#) practice group at [Manatt, Phelps and Phillips, LLP](#).

As an additional note, Manatt Partners [Chris Cole](#) and [Craig Moyer](#) along with industry leaders will team up on November 9, 2010, to present "[Green Marketing: Understanding the New Legal Landscape](#)," a webinar hosted by BNA. For information on this event, please click on the above link.

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