Defending the Price Containment Reserve: Benefits and Options

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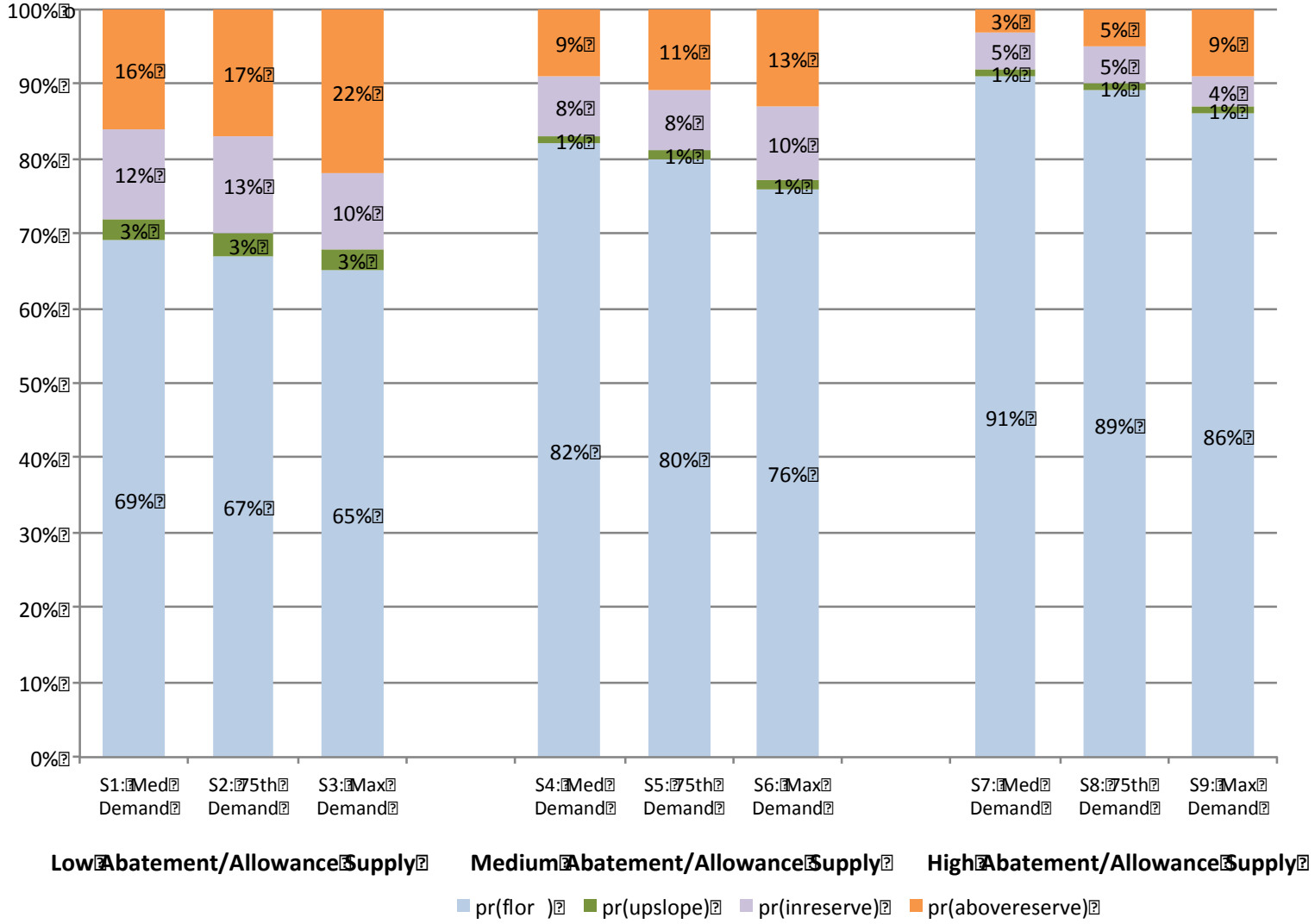
Benefits of Defending Containment Reserve

- Limits the possible price and economic impacts from volatility in supply or demand
  - Especially if abatement supply is very inelastic
- Avoids possible market disruption if shortage occurs near end of market period (2020)
- Eliminates price increase that incorporates low probability of skyrocketing price
- Eliminates incentive to push price above current reserve levels through market manipulation

Allowance Price Probabilities by Scenario



Cost Containment and Allocation

- Allocations through output-based updating dilute the impacts of allowance prices
  - Reduce the responsiveness to allowance prices.
  - Can be acceptable side-effect for trade-exposed industries with options for reducing CO2 intensity.
  - Makes no sense for emissions related to end-use fuel consumption (e.g. gas).
- Diluting incentives provided by allowance prices is not true cost-containment.
  - Can be counter-productive by making high allowance prices more likely and raising the economic costs of abatement.

Principles for Price-Containment

- Should be ex-ante transparent
  - A deterrent only works if market knows it exists
- Should be credible
  - A hard quantity cap is not credible if the prices that result are unsustainable
- Should be timely
  - Measures need to kick in immediately to avert disruption
- Should consider broad environmental benefits instead of narrow ones
  - Environmental integrity of global pollutant involves more than just capped CA (or WCI) emissions

ARB Options

- We believe there is a non-trivial possibility current reserve could be exhausted
  - Would not support the do nothing option
- Delay or cancellation of compliance obligations would be disruptive and harmful to the program
  - Significant equity impacts on differing participants.
- EMAC strongly prefers an option that substantially increases availability of allowances – sufficient to credible contain the maximum price (or allows a fixed payment in lieu of permits).
  - Could borrow from post 2020 period.
  - Proceeds could be applied to offsets, or other sources of GHG emissions.
  - Can provide a greater overall GHG reduction under those circumstances.

Thank you