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Vice President

May 2, 2019

Mr. James Duffy
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California Air Resources Board
1001 I Street
Sacramento, California 95814

via e-mail at LCFSworkshop@arb.ca.gov

Re: WSPA Comments on the April 5, 2019 CARB LCFS Workshop

Dear Jim,

The Western States Petroleum Association (WSPA) appreciates the opportunity to provide the following comments in response to the California Air Resources Board (CARB) staff presentation during the April 5, 2019 Low Carbon Fuel Standard (LCFS) Workshop. WSPA is a non-profit trade association that represents companies that explore for, produce, refine, transport and market petroleum, petroleum products, natural gas and other energy supplies in California and four other western states.

As noted in the CARB staff presentation, the CARB Governing Board in Board Resolution 18-34 provided the following directive:

> "[*T*]*he Board directs the Executive officer to monitor the cost containment provision of the Low Carbon Fuel Standard, including the Credit Clearance Market, and to propose technical adjustments through future rulemaking if needed to further strengthen the cost containment features of the program."*

WSPA appreciates that CARB staff has taken the first step in responding to this important directive through the workshop which focused on Credit Clearance Market (CCM) principles and concepts. This is a significant priority for WSPA and its members and we look forward to engaging with CARB and other stakeholders on finding a practical, effective solution. Specifically, WSPA supports concepts that provide a mechanism to supply credits to balance all deficits in the CCM on an annual basis without having entities carry over deficits with a penalty.

The current CCM provides a guaranteed outlet for credit sellers who are unable to find buyers but does not limit the potential cost of the program itself. Theoretically, a cost containment mechanism balances free market principles with achievable targets in a way that provides certainty that the market remains liquid.

Further, the CARB concepts do not include WSPA's earlier recommendations regarding:

- Eliminating the "name and shame" component.
- Eliminating the interest component in the event of a deficit carryover.
- Providing an affirmative defense for buyers should credits purchased in the CCM be declared invalid at a later date.
- Establishing a formal, independent process for assessing the outlook of the program.

This proposal further extends the "name and shame" aspect of the regulations (including unacceptable release of confidential business information) by requiring that an entity entering the CCM in two consecutive years to develop a public report detailing the entities plan to meet its obligation in the future and does not fully eliminate the interest penalty. We believe each of these issues adversely impacts the LCFS program's functionality and distorts the intended goal of the CARB concepts to provide credit availability. Each of these issues must be addressed as CARB staff continues its efforts to strengthen the cost containment provisions of the regulation.

Credit Clearance Market - Principles

As the current Credit Clearance Market (CCM) language in the LCFS Regulations does not address significant shortages in LCFS credit availability in the market or through the CCM, CARB staff presented in their workshop presentation four principles:

- Strengthen cost containment features of the program.
- Enable parties subject to CCM to fully retire all outstanding deficits annually.
- Limit credit price volatility in the regular LCFS credit market.
- Maintain the current stringency of the LCFS program in terms of estimated GHG reductions between 2020 and 2030.

WSPA can support the first three of these four principles. However the fourth principle, without flexibility in either timing or reduction targets (or both), can actually undermine the first three principles. WSPA believes a more effective fourth principle may be:

- Balance the current stringency of the LCFS program in terms of estimated GHG reductions between 2020 and 2030 to support the other three principles.

Credit Clearance Market - Concepts

Potential Price Cap in Daily Market

CARB staff's concept of a hard transaction price cap at $200/tonnes, indexed for inflation, may not be verifiable and/or enforceable. During the workshop, Leigh Noda of Stillwater Associates[1] submitted the following questions related to this concern:

- How will that be enforced when the credit and fuel price is in the same transaction?
- Can't a fuel seller put a premium in the fuel and just report the max price?

In response to these questions at the workshop, CARB staff appeared to acknowledge that the wide-ranging nature of potential transactions does not lend to the ability to identify LCFS credits within a transaction. Further, the concept appears to conflict with the market-based design of the LCFS. Effective cost containment and achievable targets must go hand in hand. A price cap is only helpful if credits are available. Clearly, it is better to have realistic carbon intensity

[1] E-mail correspondence from Dr. Leigh Noda to April 5′ 2019 CARB LCFS Workshop coordinator at sierrarm@calepa.ca.gov.

(CI) targets and let the market freely determine how to achieve these targets (as discussed later in this letter).

Advance Credits

The Advance Credit concept represents a new and significant policy change for CARB. If implemented, this would be the first instance in any CARB regulatory scheme where "borrowing" credits from the future would be allowed. In addition, §95487(a)(2)(B) of the LCFS regulations currently prohibits credit borrowing. A policy change of this magnitude demands very serious consideration and discussion.

The Advance Credit concept involves credits to be provided by CARB to electric utilities from 2020 to 2025, and to be repaid through a reduced number of future credits provided to utilities for non-metered residential electric vehicle charging occurring in 2026 to 2030. WSPA has concerns about this concept. Taking credits from the future will help contain costs in the near-term but may still not be adequate to keep the market liquid. This approach will also further challenge compliance in later years (as credits being made available earlier means there will be fewer credits available in the future years). Finally, the concept does not address a systemic (structural) LCFS credit shortfall that may still be in place by 2025 and beyond. To cap any approach at 10 MM credits leaves a potential for a substantial credit availability gap (as shortfalls could approach 10 MM credits ***per year***) with no means to close the gap without further future intervention. The critical design element for a workable CCM is that it ensures that any credit gap is filled. Unfortunately by limiting the number of credits that design criteria is not met. We encourage CARB not to artificially limit the number of credits. In addition, we note that if CARB does not limit the number of credits available in the CCM, there should be no need to attempt to cap the price of credits in the daily market.

WSPA believes that CARB should consider a durable solution that maintains fuel neutrality in the program. If Advance Credits are provided for non-residential EV charging, the program should be extended to other types of fuels. The Advance Credit application process would involve demonstrating concrete plans for credit generation during the repayment period and assurance of financial stability on the part of the credit generator. In addition, buyers of advance credits would need to be fully indemnified against any failure by a credit generator to repay the credits. A good faith purchaser of such credits should not be held liable should the predicted credit generation not occur.

The CARB concept also emphasizes the need for greater transparency in the calculation and issuance of non-metered residential charging credits. WSPA has expressed concerns for years over the methodology used by CARB to estimate the level of residential charging. If CARB is now considering issuing credits against future residential charging, a full public review is even more necessary.

<u>Recommended Path Forward</u>

WSPA strongly supports CARB's consideration of an approach to address systemic (structural) issues with the LCFS program that result in significant credit shortfalls. In a sense, borrowing credits from future years is effectively resetting the CI compliance schedule. If this were to become necessary, we believe it would be more practical and provide more certainty for the regulated community to initiate a systematic method, including measureable triggers, to adjust

CI targets (benchmarks) to provide the market with an increase in liquidity when it needs it most. Systematically adjusting the compliance CI benchmarks would both contain costs and provide the market clear price signals to weigh decisions on how to best manage compliance costs.

If CARB staff is, however, only interested in making credits available to regulated parties who experience a compliance shortfall through a mechanism such as the Advance Credit concept, WSPA would prefer a methodology for the State to issue credits directly to those parties. The proceeds could be directed to disadvantaged communities as desired, providing they were dedicated to GHG reduction projects.

WSPA appreciates the opportunity to provide feedback on this important issue. WSPA looks forward to working with CARB staff and other stakeholders to explore CCM concepts. If you have any immediate questions, please contact me at (805) 701-9142 or via email at tom@wspa.org.

Sincerely,