Despite business opposition, California's cap-and-trade auction starts Wednesday

By Dale Kasler, Staff Writer
The Sacramento Bee, November 13, 2012

Despite fierce opposition from much of the business community, California's grand experiment in taming global warming begins in earnest Wednesday.

State officials are set to auction tens of millions of dollars' worth of carbon-emission allowances to scores of oil refiners, cement manufacturers and other large industrial polluters.

The computerized auction marks the beginning of California's "cap-and-trade" market. The market is the centerpiece of Assembly Bill 32, the state's 2006 law aimed at reducing greenhouse gases, and Wednesday's kickoff is being closely watched.

"A lot of eyes are on us," said Harold Pestana, a senior manager at Pacific Gas and Electric Co., one of the companies affected by the state law.

Cap and trade will force affected companies to scale back their carbon pollution – or purchase allowances to get into compliance.

State officials and environmentalists say the market-based approach gives companies flexibility in how they reduce emissions.

Many affected businesses call it a cleverly disguised tax that will cost them upwards of $1 billion in the first year. The expense will balloon in 2015, when refineries will have to buy more credits to cover greenhouse gases spewed by cars and trucks.

"It's going to be a huge burden," said Shelly Sullivan of the AB 32 Implementation Group, a business coalition. "That turns into a multibillion-dollar energy tax on the state's economy."

Her group, which includes the California Chamber of Commerce and the California Manufacturers & Technology Association, has petitioned Gov. Jerry Brown to abort the auction.

But the auction is expected to proceed.

"Everything is still on schedule; we're moving forward," said spokesman Stanley Young of the California Air Resources Board, the agency running the auction.

Carbon trading isn't new. Polluters in the European Union have been subject to a greenhouse gas market since 2005, and a similar program covers power plants in the northeastern United States and eastern Canada.

But until Wednesday, when carbon trading comes to California, it's never been tried on a large scale in America.

More than 62 million allowances – each representing the right to emit a ton of carbon – will be offered for sale in a three-hour window starting at 10 a.m. The minimum bid price is $10 a ton.

The auction will be a low-key affair. It will be run electronically, with a half-dozen staffers monitoring the bidding behind closed doors at agency headquarters in Sacramento.

"This happens in a sealed room with no windows," said David Clegern, another agency spokesman.

The agency says potential buyers aren't allowed to publicly discuss their purchasing plans, out of fear that disclosure could skew the market. Results of the auction, including pricing and volume, won't be revealed until Monday.

Some analysts believe many potential bidders will sit out Wednesday's auction. Another auction is set for February, and there will be regular auctions each year. Besides, companies needing carbon credits will be able to buy them on the open market and don't have to go through the state.

Uncertainty could dampen bidding in the first auction as well. Jon Costantino, head of the Association of Carbon Market Participants, said bidders might be dissuaded by rumors circulating that an industry group could file a last-second lawsuit to block the auction.

Analysts say the uncertainty has caused prices to drop on private futures markets where California carbon credits have been traded for months. The per-ton price, which had been around $20 over the summer, has fallen to around $12, according to Bloomberg business news.

Low prices could undermine the state's goal of curtailing emissions. If carbon is cheap, there's less incentive for industries to reduce their pollution. That's why the Air Resources Board has set a $10 minimum on bidding in the state's auction.

While businesses complain about costs, environmentalists say a strong carbon price will pay dividends for the economy: It will give polluters an incentive to invest in green technologies to clean up their smokestacks.

The market will work like this: California has set an overall ceiling on the amount of carbon that can be emitted. The cap will decline by 2 percent to 3 percent a year. By 2020, emissions are supposed to fall to 1990 levels.

The affected companies include more than 400 of California's industrial heavyweights. They will get 90 percent of their emission allowances free in the first two years, but the percentage of freebies will decline in future years.

Business groups say California could achieve its goals of curtailing carbon without holding an auction. The state, they say, could simply give away all of the emissions allowances for free, and then enforce the cap. As companies move toward compliance, they will buy and sell the allowances among themselves and a price will emerge for carbon.

But state officials reject that argument. The Air Resources Board says an auction is needed to jump-start the market and make sure a competitive price for carbon is established.

California was hoping the market would cover multiple Western states. But only the Canadian province of Quebec is linking its carbon with California's, starting next year.

As a result, businesses in California say this go-it-alone approach leaves them at a cost disadvantage against companies in other states.

"Our California operation is certainly exposed to out-of-state competition that does not have to comply," said Bruce Ray of Johns Manville, which runs a fiberglass insulation plant in Willows.

Bill Klesse, the chief executive of Valero Energy Corp., owner of two California refineries, ripped the upcoming auction during a recent conference call with investors. "They're coming up with regulations that are totally not workable," he said.

The big utilities are being treated differently than most participants. The state has crafted a complicated scheme designed to buffer their customers from major rate shock. How well the buffer works isn't yet known, however.

"We can't really say what the cost impact to our customers is going to be," said Lynsey Paulo, spokeswoman for PG&E, which supports the auction plan. "We know there's going to be one."

Cap and trade should be pain-free for customers of the Sacramento Municipal Utility District. SMUD said it has enough hydroelectricity and renewable energy that it won't need to buy any carbon allowances for at least several years, meaning there will be no cost to customers.

State to officially launch greenhouse gas system

In the Stockton Record, Modesto Bee and other papers, Monday, Nov. 12, 2012

SAN FRANCISCO (AP) — California's largest greenhouse gas emitters will begin buying permits in a landmark "cap-and-trade" system designed to control emissions of heat-trapping gases and to spur investment in clean technologies.

The program is the most wide-ranging of its kind in the nation and a key part of California's 2006 climate-change law that dictates standards for cleaner-burning fuels, more efficient automobiles, and increased use of renewable energy.

Under the plan, the California Air Resources Board will auction off pollution permits on Wednesday called "allowances" to more than 350 businesses, including electric companies, food processors and refineries.

In essence, the auction will put a price on carbon emissions.

The program also places a cap on emissions spewed by individual polluters. Businesses are required to either cut emissions to the cap levels or buy allowances from other companies for each metric ton of carbon discharged over the cap each year.

Businesses can satisfy up to 8 percent of emissions reductions through the purchase of carbon credits from forestry and other certified projects.

"It is entirely in line with the notion ... that competitive economics in the 21st century is built upon clean and more efficient ways of generating energy, making products and doing business," Mary Nichols, the air board's chairman, wrote in an email.

However, some of the businesses regulated under the plan say the extra costs will result in higher electricity rates and job losses in an economy already struggling to recover. A coalition of business groups has petitioned Gov. Jerry Brown to delay the program — a request he has refused.

"The auction will take place," said Evan Westrup, a spokesman for the governor. "We will be monitoring the program very closely and the Air Resources Board will make modifications as appropriate."

For the first two years of the program, large industrial emitters will receive 90 percent of their allowances for free in a soft start meant to give companies time to reduce emissions through new technologies or other means. The cap, or number of allowances, will decline over time in an effort to drastically reduce greenhouse gas emissions by 2050.

The board has estimated that businesses will pay a total of $964 million for allowances in fiscal year 2012-2013. About 23 million allowances will be sold for 2013 emissions, and 39.5 million allowances are being pre-sold Wednesday for 2015 emissions.

The state is still unclear about how the money will be used, but California law dictates it go into a greenhouse gas reduction account, and any programs that use the funds be consistent with the goals of AB32, the climate change law.

Some groups have proposed using part of the money to help businesses regulated under the cap to buy and install energy efficient technology to help save money.

While no one believes California's cap-and-trade program alone will remedy climate change, the system is designed to show it can be done in the world's ninth-largest economy and provide a blueprint for other governments, the board said.

Officials believe the re-election of President Barack Obama, who in his acceptance speech voiced support for battling climate change, will embolden states to follow California's lead.

"With the election, we expect states that had dropped their own climate efforts to take a new look at what they can do, and some of these ideas will be adapted or adopted elsewhere," Nichols said.

Business groups say California's regulations and high taxes are already a threat to their bottom lines, and adding more costs in a bad economy is perilous to growth.

Utilities say ratepayers should expect increases.

The Modesto Irrigation District — which provides its customers with a mix of energy from traditional coal-and-natural gas-fired power plants and renewable sources — said customers will see bills increase in 2013 due to cap and trade.

"We will have on our billing a surcharge that will address cap and trade, and show ratepayers exactly how much more they will pay," said Greg Salyer, resource planning and development manager at the district.

Salyer said the district will not know exactly how much higher rates will go until after Wednesday's auction, which will set prices for each ton of carbon emissions.

Ratepayers will see a bit of relief early on because some of the auction proceeds have been earmarked for return to utility customers. The California Public Utilities Commission will ultimately decide how those rebates are handled next year.

In the end, proponents of California's ambitious new program say the increases in costs will be offset by gains in the state's clean technology sector, and by air quality improvements and other benefits of emission reductions.

That said, even supporters acknowledge that changes in the price of energy are likely to occur.

"We don't want to dismiss the idea that there will be changes to the energy price structure because of a program like this," said Timothy O'Connor of Environmental Defense Fund. "But that's not a reason to throw it out."

California's model climate policies will maintain momentum in Obama 2nd term

Maria Gallucci, InsideClimate News
In The Sacramento Bee, Sunday, Nov. 11, 2012

For decades, California has been the engine of growth behind America's sputtering clean energy economy - adopting groundbreaking clean air and climate policies as federal efforts lagged behind.

The hope was that California's initiatives would become the template for a national law to slow global warming.

That hasn't happened yet - and it isn't likely to over the next four years. In his second term, President Barack Obama faces the same divided Congress that rejected carbon-reduction targets and a price on carbon dioxide emissions, two cornerstones of California climate policy.

But an Obama White House provides California a key federal partner that wants to regulate global warming emissions from power plants and cars and won't interfere. Steady support from the top might encourage other states to copy or join California's pioneering initiatives, according to policy experts and advocates, which only helps the Golden State.

"I can imagine a set of states deciding to take on something like California's program several years into an Obama administration, having warmed up to the idea of greenhouse gas regulation and having seen it work in practice," said Cara Horowitz, executive director of UCLA Law School's Emmett Center on Climate Change and the Environment.

California's clean economy is driven by at least four sweeping policies: an economywide cap-and-trade program that puts a price on carbon pollution; a low-carbon fuel standard that limits the sale of carbon-intensive fuels; a 33 percent renewable electricity standard; and rigorous clean-car mandates for automakers.

Some of those are brand-new, and many state and federal officials will be watching closely to see if the policies reduce heat-trapping gases while creating new business opportunities, rather than causing electricity price spikes and job losses, as critics contend.

Here's a rundown of the policies, and a look at how the second Obama administration could help them along.

Cap and trade: Removing the stigma

After six years in the making, California is set to launch the first auction of its cap-and-trade program on Nov. 14.

The program is the hallmark of California's global warming law, AB 32, which requires the state to cut greenhouse gas emissions by 30 percent by 2020 and 80 percent by 2050.

Regulators will set a ceiling on CO2 emissions from utilities, oil extractors and fossil fuel-burning factories and require them to pay for their pollution by buying carbon allowances in quarterly auctions.

In year one alone, the program is expected to generate between $660 million and $3 billion in auction proceeds. By 2020, cap and trade could send $8 billion into state coffers annually.

California's program is the nation's second cap-and-trade system and the first to target carbon polluters across the economy. The Regional Greenhouse Gas Initiative limits emissions from power plants in nine participating Eastern states. In both cases the states established the program without federal involvement and approval.

Obama supported federal cap-and-trade legislation in his first term, and rumors are swirling that he might push for a national carbon tax to help cut the deficit. Far more certain is that his Environmental Protection Agency will finalize greenhouse gas limits for existing power plants and oil refineries.

Any action from Obama on greenhouse gases could help chip away at the stigma of regulating carbon, said Horowitz of UCLA's climate change center. "States may learn that regulating greenhouse gas is actually not as scary as they thought it was." Already, some states are awakening to its economic benefits.

California tried to create a regional cap-and-trade pact with six other states called the Western Climate Initiative, but political will faded after Congress failed to pass federal climate legislation, the economy soured and skepticism about global warming became a tenet of GOP politics. A similar effort among Midwestern states was also abandoned.

For now, California is expected to link its scheme to Quebec's carbon market in 2013.

Matthew Kahn, an economist and professor of environmental economics at UCLA, said the more states that adopt cap and the trade, the better for California. "There would be less backlash ... if there's the perception that the rest of the country is catching up and that we're a trendsetter" and not a "green guinea pig."

Kahn explained that California's carbon polluters will each have to spend millions of dollars a year to buy pollution allowances, increasing business costs and raising the risk that jobs could "leak" to other states. If other states enact cap and trade, it would create a level playing field, he said. It would also increase the size of the pool for buying and selling allowances, which stabilizes prices of permits.

The ideal scenario, Kahn said, would be for California to link or fold its cap-and-trade program into a national carbon-trading scheme. While federal climate policy remains a remote reality, Kahn expressed slight optimism that if California's experiment proves good for the environment and the economy, moderate Republican lawmakers would get behind national carbon legislation.

Low-carbon fuel standard: Will Obama weigh in?

Another critical piece of California's global warming law is a rule to slash carbon emissions in transportation fuels. The Obama administration isn't directly involved with the measure, but the standards are stuck in legal limbo and the White House could opt to weigh in.

The low-carbon fuel standard - the first of its kind in the world - went into effect in the spring. Under the rule, oil importers, refiners and fuel blenders must cut the "carbon intensity" of their fuel mix by one-quarter of a percent this year and by 10 percent by 2020. The rule would discourage the use of oil sands crude and other high-carbon fuels and encourage greater adoption of electric cars and other clean vehicles.

Transportation accounts for 40 percent of California's global warming emissions and about a third of U.S. emissions.

In December, a federal judge ruled the policy was unconstitutional because it regulates economic activity outside California's borders, siding with oil companies, Midwestern ethanol producers and other opponents. Advocates appealed the decision.

The rule's fate now rests with a three-judge panel in the 9th Circuit Court of Appeals, which is expected to issue its final decision in 2013. The Obama administration could, in theory, attempt to sway the 9th Circuit judges by filing a friend-of-the-court brief expressing support for the program.

Obama has previously backed a national low-carbon fuel standard. On the 2008 campaign trail, he pledged to establish a program to cut the carbon-intensity in fuels by 10 percent by 2020. But he has also supported corn ethanol producers, who say the standard discriminates against them because it counts the greenhouse gases their ethanol-carting trucks emit en route to California. The president could anger them by championing the fuel rule.

"If I were betting, I'd imagine the Obama administration would stay out of this altogether," said Ann Carlson, faculty director of UCLA Law School's climate change center.

Still, the president could indirectly support the goals of the low-carbon fuel standard by continuing federal mandates and incentives for cleaner-burning fuels, experts agreed.

Obama could, for instance, extend a 4-year-old production tax credit for cellulosic ethanol, which could increase the supply of a particularly low-carbon ethanol for California's fuel suppliers. Cellulosic ethanol is made from non-food crops like wood chips, switchgrass and plants - not from corn, which is a higher-carbon ethanol.

The $1.01-per-gallon credit is set to expire Dec. 31, 2012, and while there's still no cellulosic ethanol being produced in the United States at a commercial scale, three plants with nearly 80 million gallons in combined capacity are expected to become operational next year.

Renewable portfolio standard: Doing fine on its own

Last year, California approved a tougher Renewable Portfolio Standard (RPS) requiring utilities to get 33 percent of their electricity from renewable sources by 2020. As of July, each of the three major investor-owned utilities said they were nearly two-thirds of the way toward meeting that goal.

Even so, "it it will be easier to achieve" under Obama than it would have been under Mitt Romney, said Michael Gerrard, who directs Columbia Law School's Center for Climate Change Law.

The reason is that Obama is more likely to push to extend federal loans, grants and tax credits for wind and solar energy installations and other clean technologies, which Mitt Romney indicated he might cut.

California's first RPS was passed in 2002. The policy has helped turn the state into the backbone of the U.S. clean economy. The state accounts for more than half of the country's solar projects and about 10 percent of all wind farms.

Nearly 170,000 California residents have jobs in the broadly defined green economy, according to a recent study. Last year California took in $3.7 billion in venture capital investments in clean technologies - more than half of all such investments in North America.

Gerrard said a national clean electricity standard that spurs a nationwide boom in installations would help California's utilities, because they're allowed to meet part of their RPS requirements by purchasing credits from owners of projects in other states.

Obama has supported a plan to require 80 percent of the nation's electricity generation to come from lower-carbon sources, including natural gas and nuclear energy, by 2035.

Zero-emissions vehicle mandate: A sigh of relief

For California's new mandate for ultra-clean cars, Obama's victory removes any doubt the program will move forward.

The rule, approved in January, requires 15 percent of all cars sold in California to be zero-emissions vehicles (ZEV). Compliance begins with model year 2018; full compliance is expected by 2025. State regulators unanimously passed the mandate after four years of bargaining with the auto industry and environmental groups.

The mandate could result in more than 1 million all-electric, plug-in hybrid electric and hydrogen vehicles on California's roads in the next decade, about 20 times the amount of such cars on U.S. roads today. It's the latest move in California's half-century-long effort to cut air pollution and carbon emissions from cars and trucks.

California has sole authority under the Clean Air Act to regulate new car emissions, so long as the state's standards are as stringent as federal standards and the EPA grants it a waiver. It earned that designation largely because of its pioneering efforts in the late 1950's to limit smog emissions, long before the federal government got on board.

Currently, California is waiting for a waiver from the EPA to move ahead with the ZEV program. Ann Notthoff, the California director of the NRDC Action Fund, the advocacy arm of the Natural Resources Defense Council, said EPA is expected to grant the waiver this year.

Notthoff said if Romney had won the presidency, and a decision on the waiver was delayed, it could have potentially put the program at risk.

The EPA's approval will open the door for other states to adopt the ZEV rule. Ten states and Washington, D.C., have already pledged to do so for the 2018-2025 model years. They are: Connecticut, Maine, Maryland, Massachusetts, New Jersey, New Mexico, New York, Oregon, Rhode Island and Vermont.

That could double the impact of California's program and spur sales of more than 3.3 million electric and hydrogen cars across the country, according to estimates.

Overall, Notthoff and other environmental advocates are breathing a sigh of relief. "It's going to be easier to move forward" under Obama, Notthoff said.

The onus is now on California to show other states the environmental and economic benefits of adopting its policies, said Horowitz of UCLA. "I don't think that depends very much on who is in the White House."

(InsideClimate News is a nonprofit, non-partisan news organization that covers clean energy, carbon energy, nuclear energy and environmental science. More information is available at http://insideclimatenews.org/.)