



Chris Lang

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How California's cap and trade market undermines environmental justice

Last week, Senator Bob Wieckowski (D-Fremont) and Senate President pro Tempore Kevin de León (D-Los Angeles) gave a [press conference](#) about a new bill, SB 775, aimed at changing California's cap-and-trade scheme. The proposed bill would start a new cap-and-trade scheme in 2021 that would include no offsets, no free pollution allowances, and a per-capita dividend.

Vox journalist David Roberts has written [a very useful overview of SB 775](#). It's safe to say that Roberts likes SB 775:

I gotta say, if this thing passes, it will be close to a miracle. To my eye, it elegantly balances technical and political considerations in a system that is simple, reliable, and sturdy.

EDF, on the other hand, doesn't like it. EDF's Erica Morehouse [argues](#) for keeping California's cap-and-trade scheme:

Rather than scrapping the current system and starting over with an unproven approach, the state should build on success, keeping what is working well while strengthening the program by doing more to address local air pollution and environmental justice.

Meanwhile, a [press release](#) from four environmental justice groups supports SB 775:

The California Environmental Justice Alliance, Asian Pacific Environmental Network, Center on Race, Poverty & the Environment, and Leadership Counsel for Justice and Accountability are pleased to see such a bold vision for a more equitable, effective carbon pricing program in California released today through SB 775. We thank Senator Wieckowski and Senate pro Tem de León for their leadership.

California was one of the first states in the USA to pass legislation that includes a legal definition of environmental justice. In California, environmental justice is defined as follows:

“environmental justice” means the fair treatment of people of all races, cultures, and incomes with respect to the development, adoption, implementation, and enforcement of environmental laws, regulations, and policies. ([Government Code Section 65040.12](#))

In a recent paper, Patrick Bigger, a Senior Research Associate at Lancaster University, looks at environmental justice and at how fairness is regulated in California’s current cap-and-trade carbon market. It is published as a chapter in a book edited by Stephanie Paladino and Shirley J. Fiske: “[The Carbon Fix](#)”.

California’s Global Warming Solutions Act

California [launched](#) its cap and trade scheme in January 2013. It’s part of AB 32, the California Global Warming Solutions Act of 2006, and it runs until 2020. AB 32 is just 13-pages long, but as Bigger points out, the market-based governance mechanisms are complex:

While the basic principles of carbon market design are fairly straightforward, the nuances in rule-making are multitudinous, the negotiations over those nuances protracted, and the number and types of

interlocutors trying to influence all of the moving parts of the system are vast.

Bigger's analysis is based on 14 months of fieldwork in Sacramento, California. He points out that California's carbon market may have started with the intention of making "polluters pay". It's based on the economic idea that putting a substantial price on carbon would drive down emissions of greenhouse gases and other pollutants. But the reality is that "pay to pollute" is the operating principle of California's carbon market. Bigger writes that,

Environmental justice organizations have long feared such an outcome, believing that emissions will not be avoided and that polluters can eschew responsibilities to impacted communities through accounting tactics and the outsourcing of reductions with offsets.

Bigger found that the concerns of environmental justice organisations "were sidelined through the regulatory decision to conduct a specific kind of carbon pricing".

AB 32 requires California's Air Resources Board to convene an Environmental Justice Advisory Committee. Earlier this year, the Environmental Justice Advisory Committee put out a [declaration](#) specifically opposing carbon offsets:

the Environmental Justice Advisory Committee stands with communities around the world in opposition to carbon trading and offset use and the continued over reliance on fossil fuels

The fact is that offsets allow pollution to continue in California, not just of greenhouse gases but of other pollution. Many of the [most polluted cities in the USA](#) are in California. And landfills, oil refineries, rail yards and other polluting facilities are [concentrated](#) in low-income communities and communities of colour.

Not all claims to fairness are equally influential, Bigger writes. Industrial lobbyists succeeded in reducing arguments about fairness to cost reductions for industry. California gave away many more allowances than were needed to ensure a high price for carbon.

Bigger looks at three key decisions that were influenced by claims about fairness, outlined briefly below.

Over-allocation of pollution permits

The Air Resources Board allocates pollution permits to regulated industries, after emissions levels have been determined and a cap set. Bigger found that this was the most divisive and important decision in the design of the market.

Industry groups argued that pollution permits should be handed out for free. Environmental justice groups and academics argued that pollution permits should be auctioned.

Industry argued that if companies had to pay to pollute in California, they would relocate to avoid extra costs. This relocation is called “leakage”. In 2012, the AB32 Implementation Group, an industry group urged the Air Resources Board to,

immediately amend the regulation so that all industries will be allocated 100% of allowances thereby eliminating the auction. This is reasonable given that there is no strategy to address leakage and job loss created by an auction.

ARB developed what Bigger calls “convoluted formulas to determine how much pressure from imports each industry was under”. ARB then handed out free permits based on the risk of companies in California being undercut by companies operating in jurisdictions without climate change legislation.

In the first compliance period (up to the end of 2014), the majority of regulated industries received about 90% free permits. Continued industry lobbying led to increases in trade-exposed industries, from breweries to natural gas suppliers. Bigger writes that,

This reduced the number of allowances auctioned by more than a quarter in 2015, and eliminated the need for auction participation from some industries through 2020, the entire design life of the market. Under current regulations, ARB is projected to give away over 700 million

[tonnes of] CO2 worth of allowances over the life of the market just to utilities, which is roughly the equivalent of the climate pollution generated by Germany in 1 year.

Resource shuffling

Resource shuffling occurs when a company that imports power from outside California changes its suppliers to low carbon sources. A California utility could, for example, buy hydropower from Ontario instead of coal-fired power from Arizona. The coal power would, however, be sold elsewhere, resulting in no net emissions reductions. About 30% of California's energy is imported.

In the initial regulation, resource shuffling was banned. Power generators and importers lobbied against this ban. As a result, ARB adopted a series of "safe harbor" provisions. A [2013 paper](#) by Danny Cullenward and David Weiskopf of the Stanford Law School found that these provisions could result in leakage of up 197% of emissions reductions mandated by AB32.

Offsets and more offsets

Offsets can be used to meet 8% of a regulated company's emissions target. While this may not sound like much, Bigger explains that,

What this means over time – as the cap is lowered – is that roughly half of the mandated aggregate emissions reductions could come from sources outside of the cap, because the overall cap is scheduled to decline by about 16 percent over the course of the program. This raises concerns about polluting industries simply buying their way out of making serious pollution reductions, and the attendant health impacts of the co-pollutants in industrial processes.

The 8% offset figure is double the limit that the Air Resources Board initially proposed in 2009. The decision to increase the limit on offsets followed lobbying by groups like the [California Chamber of Commerce](#).

While industry and BINGOs like EDF are in favour of offsets, environmental justice groups oppose offsets. In their [press release](#) about SB 775, environmental justice groups explain that,

The current cap and trade system has significant environmental justice flaws that our members, our alliance and leading researchers have highlighted for many years. Pollution from large greenhouse gas emitting facilities disproportionately impacts people of color. More than half of the greenhouse gas sources covered under cap and trade, including 15 of 20 refineries in the state, are located in or within one-half mile of a disadvantaged community. These facilities do not just release carbon dioxide; their emissions are strongly correlated with a range of pollutants that harm health and quality of life. Current features of cap and trade, like offsets and an oversupply of allowances, allow facilities to comply with legal requirements without actually reducing the pollution coming out of their smokestacks.

The inclusion of [REDD offsets in California's cap-and-trade scheme](#) has been discussed for several years. Inclusion of REDD offsets would allow polluting companies, in particular fossil fuel corporations, to greenwash their operations and would delay much needed emissions reductions in California.

Bigger argues that companies appropriated the language of fairness to argue against California's regulations that were designed to constrain their polluting operations. He concludes his paper with a plea for direct regulation:

It seems that transformative carbon reduction impacts will more likely be achieved via direct regulation, such as renewable energy standards and other policies that are described as merely 'complementary' to the carbon market.

Full disclosure: This post is part of a series of posts and interviews about [California's cap-and-trade scheme](#), with funding from Friends of the Earth US. [Click here](#) for all of REDD-Monitor's funding sources.