



## **Clean and Prosperous California Comment Letter to California Air Resources Board 04 May 2026**

Clean and Prosperous (CAP) California emphasizes the importance of timely implementation of the proposed amendments at the upcoming May Board hearing, which is critical to the credibility of the California Air Resources Board (CARB) after extensive delays to the ongoing rulemaking over the last two and a half years (Section 1).<sup>1</sup>

The proposed expansion of the Manufacturing Decarbonization Incentive (MDI) may discretionarily allocate Build Up California Allowances (BUCAs) to certain facilities undertaking decarbonization activities and vulnerable to emissions leakage. The possible reintroduction of 118.3 million allowances through the MDI undermines emissions accounting that is central to CARB's cap setting (Section 2). For this reason, if CARB moves forward the MDI as drafted, reductions in future caps equal to the quantity of BUCAs would maintain the integrity of CARB's emissions accounting (Section 2). In recognition that such changes would trigger a second 15-day and thereby preclude timely implementation, these changes could be made during a follow-on rulemaking guided by Board direction.

The allocation of BUCAs by CARB can be constrained by targeting marginal reductions through a variety of strategies discussed in Section 3 including (a) allocating BUCAs proportional to reductions, and (b) targeting activities that are additional, conservativeness, and permanent. Similarly, these suggestions could be taken up during a follow-on rulemaking guided by Board direction.

### **1) Timely implementation of the proposed amendments at the May Board hearing is critical to protect CARB's credibility**

The cap-and-invest rulemaking is the longest duration and most delayed update to California's program since its inception. Correspondingly, allowance demand has dropped whenever CARB further delays and/or weakens ambition, thereby causing allowance prices to drop from a high of nearly ~41 USD to current prices at or below the floor of ~27 USD.<sup>2</sup>

These drops reflect a variety of factors with the driving factor being CARB's credibility at delivering a timely rulemaking update, including cuts to allowance supply. For this reason, it is critical for the proposed rulemaking to be adopted at the May Board hearing.

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<sup>1</sup> CAP California. 2025a. "[Money Left on the Table: Restoring Cap-and-Trade Auction Revenues Through Legislative Reauthorization](#)".

<sup>2</sup> CAP California. 2025a. "[Money Left on the Table: Restoring Cap-and-Trade Auction Revenues Through Legislative Reauthorization](#)".

If the May Board hearing is missed, a careful analysis suggests that CARB probably delays implementation of proposed updates into 2027, with potential negative implications for rollout of the California Climate Credit (CCC) and market linkages with Washington and Quebec.<sup>3</sup>

## **2) Reducing future caps commensurate with the quantity of allocated BUCAs would ensure the integrity of CARB's emissions inventory**

The possible reintroduction of 118.3 million allowances through MDI undermines emissions accounting that is central to CARB's cap setting. Per CARB's ISOR Staff Report, "Removing 118 million allowances from 2027-2030 allowance budgets is needed to account for updates to CARB's GHG Emission Inventory." (Staff Report, p. 30, Jan. 20, 2026).

The GHG Emission Inventory informs cap setting by establishing the share of total statewide emissions that fall within the scope of the cap-and-invest program, which is then applied to statewide statutory targets to derive allowance budgets. As CARB explained in its October 2025<sup>4</sup> informal workshop, "Updates made in the 2022 GHG Inventory identified a downward adjustment that would have impacted allowance budgets adopted in the 2016 Cap-and-Invest Rulemaking," which set the 2020-2030 annual budgets. CARB estimated this downward adjustment equals roughly 118.3 million allowances. By CARB's own estimates, the 118.3 million allowances that are being removed from pre-2031 budgets should never have been introduced in the first place. Therefore, once removed, this quantity of allowances should not be reintroduced as currently contemplated by the proposed amendments.

Based on our understanding, any significant changes to the MDI would trigger a second 15-day commenting period, almost certainly delaying the May Board hearing and probably precluding implementation in 2026. For this reason, if the MDI moves forward as implemented, then CARB would be required to reduce future caps commensurate with the quantity of allocated BUCAs. This would be easiest implemented at the level of compliance periods, such that the quantity of allowances of allocated BUCAs in one compliance period is counterbalanced by an equal reduction in caps for the next compliance period. Our analysis suggests that MDI would allocate 27 million allowances annually at maximum.<sup>5</sup>

## **3) The quantity of allocated BUCAs should be targeted at marginal reductions**

The allocation of BUCAs by CARB can be constrained by targeting marginal reductions through a variety of strategies discussed in Section 3 including: (a) targeting activities that

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<sup>3</sup> Elevate Climate. 2026. "Policy Note on Rulemaking Timing". See Attachment A.

<sup>4</sup> [Cap-and-Invest Workshop October 2025](#)

<sup>5</sup> CAP California. 2026. "MDI Bounding Exercise". See Attachment B.

are additional, conservative, and permanent; (b) allocating BUCAs proportional to expected or actual reductions; and, (c) penalizing entities that do not deliver timely reductions.

**a) Targeting activities that are additional, conservative, and permanent**

In theory, the MDI could be designed to have no net impact on cap levels, but that outcome would require “additionality” and “conservativeness” as described below:

- **Additionality of reductions:** The reductions caused by the BUCAs must exceed what the carbon price or other climate policies would have achieved. This is similar to the concept of “additionality” in the carbon offsets literature and “marginality” in the economics literature.
- **Conservativeness of BUCAs:** CARB issues one BUCA for one reduction caused by the MDI (sometimes referred to as a “one-to-one” requirement). This is similar to the concept of “conservativeness” in the carbon offsets literature.

As proposed, the MDI requires neither additional or conservativeness. Therefore, the quantitative impact of MDI on cap levels depends on whether CARB discretionarily adheres to these principles and, if not, which principles above are relaxed.

- If CARB does not target additional reductions, then all BUCA allocations would increase the cap. While additional reductions contribute to achieving the cap, “non-additional” reductions that are awarded BUCAs do not, and instead effectively increase the cap. In the extreme, if MDI is fully subscribed and used for “non-additional” reductions, then the MDI would effectively increase the cap by 118.3 million tons.
- If CARB does not issue a “conservative” quantity of BUCAs, then the impact on the cap depends on the degree to which CARB “overawards” BUCAs. For example, if CARB awards three BUCAs for one ton of additional emissions reduction, then the cap would effectively increase by two tons. In this example, if MDI is fully subscribed, then the MDI would effectively increase the cap by 78.87 million tons (118.3 million BUCAs - 39.43 million reductions).<sup>6</sup>

A core constraint in the design of the MDI is that MDI-eligible facilities are already covered by the cap-and-invest program and therefore subject to the carbon price, which in itself is designed to incentivize emissions reductions. Therefore, any emissions reduction that is truly additional should, by definition, be more expensive than today’s carbon price—otherwise it would have already occurred.

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<sup>6</sup> Note: if BUCAs lead to additional decarbonization activities for capital investments, then reductions can occur over many years and even beyond years applicated for MDI.

This creates a design tension. CARB could (i) strictly impose additionality and one-to-one conservativeness requirements, in which case MDI uptake is likely to be constrained to a narrow set of projects that cost more than the carbon price but less than two times the carbon price<sup>7</sup>, or (ii) relax additionality and conservativeness requirements, which is likely to result in systematic over-allocation of BUCAs relative to emissions reductions and an increase in the effective cap.

In the context of the MDI, the Executive Officer could clarify CARB's intent to use additionality and conservativeness as criteria for applying facilities by issuing guidance for applying facilities. On that basis, the Executive Officer can accept applications that are additional and conservative, while rejecting those that are not.

#### **b) Allocating BUCAs proportional to reductions rather than expenditures**

Allowing for tailoring of the modified cap adjustment factor: CARB's rulemaking documentation creates ambiguity as to whether MDI facilities receive a fixed CAF of 0.8 or a CAF of "up to 0.8." If the CAF is fixed at 0.8, as suggested in the 15-Day Notice, facilities are likely to be over-awarded relative to their reductions. By contrast, if facilities must apply for a CAF "up to 0.8," as reflected in the proposed amendments, CARB can reject applications that request excessive BUCAs relative to planned reductions. CARB should consider clarifying this ambiguity ahead of MDI implementation, for instance, by correcting the 15-Day Notice or through a Board Resolution.

Provide additional guidance prioritizing cost effectiveness: to minimize the incidence of overallocation, CARB should treat the MDI as a competitive procurement process that rewards the fewest BUCAs for the most reductions. In that context, the Executive Officer should issue guidance ahead of each compliance period that outlines criteria that will be used in assessing whether to approve or deny a facility's proposed modified cap adjustment factor.

Furthermore, CAP California suggests that cost effectiveness be the primary criterion against which the modified CAFs are deliberated. As currently drafted, there is no clear criteria that distinguishes between facilities that plan to reduce more emissions for the same modified CAF. For example, two facilities could request a modified CAF of 0.6, while one could reduce one ton of emissions and the other one hundred, yet there is no preference within the proposed language that would prioritize the more cost-effective application or provide grounds to deny the less cost-effective application.

CAP California suggests that the Executive Officer should (1) publish guidance ahead of each compliance period for MDI applications that (2) prioritizes cost-effectiveness as a

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<sup>7</sup> An entity that is awarded one BUCA per reduction would be willing to provide reductions up to two times the carbon price because reducing that emissions (1) avoids the need to retire an allowance for one ton of emissions and (2) can monetize a BUCA at the price of an allowance.



criteria and (3) empowers itself to deny applications if an excessive quantity of BUCAs is awarded per reduction.

Clawbacks based on reductions rather than expenditures: As drafted, the regulations require an MDI facility must return allowances to CARB based on the proportion of unspent monetary value of BUCAs. This provides a layer of accountability but an imperfect one because facilities that spend money on eligible activities but never reduce emissions (e.g., breaking ground on a CCUS project that never materializes), or reduce fewer emissions than expected, would not be penalized.