

May 4, 2026

Chair Lauren Sanchez

California Air Resources Board

1001 I Street

Sacramento, CA 95812

Dear Chair Sanchez, Board Members and Staff,

As a financial economist with decades of experience in risk management and climate policy, I write to express my serious concerns regarding the 15-day package of proposed revisions to the Cap-and-Invest (C&I) program.

While the program is a vital tool for California's climate goals, the April 2026 amendments significantly weaken its ambition. At a minimum, **CARB should remove and retire 118.3 million allowances from the 2027-2030 annual budgets without reintroducing these allowances** into the Build Up California Reserve.

Fiscal and Environmental Risks of the MDI

The primary objective of the C&I program is to reduce emissions. The January 2026 proposal to remove 118.3 million allowances was not a result of increased ambition, but rather a necessary adjustment to account for updates to CARB's GHG Emission Inventory.¹ The April 2026 proposed amendments effectively reverse necessary technical adjustments by reintroducing up to 118.3 million allowances into the market via the Manufacturing Decarbonization Incentive (MDI) and Build Up California Reserve. This shift from removal to redistribution creates critical risks:

- **Weakened and Distorted Price Signals:** Reintroducing up to 118.3 million allowances represents a significant expansion of supply that distorts price signals. California allowances cleared at \$27.94 during the February 2026 auction—less than half the price of EU, UK, and Washington markets. Allocations to the MDI risk pushing secondary market prices below the auction reserve price.
- **Revenue Loss:** Analysis from UC Santa Barbara's Environmental Markets Lab suggests that if fully utilized, the MDI could lower auction revenue by \$4 billion over the next four years. This would result in a \$2.3 billion reduction for the Greenhouse Gas Reduction Fund (GGRF) and \$1.7 billion for the California Climate Credit.²

Capital Misallocation

Long-term climate investments depend on stable expectations of future prices. Accommodative measures like these to the MDI provide excessive allowances to emitters, increase the overall cap and distort the price of emissions. The mispricing of emissions naturally leads to the misallocation

¹ https://ww2.arb.ca.gov/sites/default/files/barcu/regact/2026/cap_invest/nc_isor.pdf

² https://emlab.ucsb.edu/sites/default/files/documents/2026_capinvest_manufacturing_decarbonization_incentive.pdf

of capital, discouraging the investment in decarbonization technology that a steadily increasing price on emissions is designed to induce.

CARB should prioritize a consistent policy signal. Adopting the MDI as currently outlined will likely result in sustained low prices, reduced state revenue, and a failure to reach the marginal cost of abatement necessary for behavioral change.

Sincerely,

Bob Litterman