



DRA

*Division of Ratepayer Advocates
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Ms. Mary Nichols
Chairman
California Air Resources Board
1001 I Street
Sacramento, CA 95814-2828

Re: Division of Ratepayer Advocates' Comments on the Air Resources Board Proposed Regulation to Implement the California Cap-and-Trade Program

Dear Ms. Nichols:

The Division of Ratepayer Advocates (DRA) appreciates this opportunity to submit comments to the Air Resources Board (ARB) regarding the Proposed Regulation to Implement the California Cap-and-Trade Program (Proposed Regulation). DRA is an independent division of the California Public Utilities Commission (CPUC) created by Section 309.5 of the Public Utilities Code. DRA's mission is to obtain the lowest possible consumer rates for utility services consistent with safe and reliable service.

DRA appreciates the significant progress ARB has made in developing California's cap-and-trade program with the extensive public process and input from stakeholders it has received through 2009 and 2010. While efforts to cap greenhouse gases (GHGs) at the national and international levels have been hindered by uncertainty, California has made clear through Assembly Bill (AB) 32 and its Scoping Plan that it will implement a strategy to achieve the GHG reduction limit established in the law. Although it will require a broader national and international effort to achieve the GHG reductions that are forecasted as necessary to combat the threat of climate change, California can use this opportunity to position its economy and businesses to benefit from future national and international efforts to reduce emissions of GHGs and make early, cost-effective preparations for a GHG-constrained future. DRA recognizes that a cap-and-trade program with the necessary cost containment and transitional components could afford covered entities flexibility to seek out and implement cost-effective options to reduce emissions below the overall statewide limit (cap level), and in addition to the specified measures in the California Scoping Plan and otherwise required by law or regulation.

The following is a summary of DRA's recommendations on the Proposed Regulation, to help ensure that the transition into the cap-and-trade program is smooth, and that businesses and consumers are not adversely impacted by California's leadership role of reducing GHGs:

1. DRA supports ARB's proposal to allocate allowances to the electric distribution utilities for the benefit of their customers.
2. DRA recommends free allocation of allowances to natural gas distribution utilities, beginning in 2015 when they are covered under the cap-and-trade program, analogous to how investor-owned utilities are treated in the electricity sector.
3. DRA recommends that 100 percent of allowance value freely allocated to electric distribution utilities should be directly returned to ratepayers in the form of rebates and ARB should clearly state this intention in the Proposed Regulation.
4. DRA supports the use of offsets as a cost containment measure. If the supply of offsets in the California program is constraining the ability of compliance entities to meet their offset limit of eight percent, then ARB should have an active process to review additional offset protocols to include in the program.
5. DRA recommends that ARB establish a market oversight committee, with experience in market monitoring activities, which has the authority to suspend the program or recommend that the Governor suspend the program if the program is not achieving the objectives as defined by AB 32 or if the costs of compliance are unexpectedly high.
6. DRA requests that the adjustments to the cap level are clarified further to support the revised 2020 allowance budget of 334.2 million metric tons of carbon dioxide equivalent (MMT CO₂e).

The following provides a more in-depth discussion of DRA's recommendations:

DRA Supports Free Allocation of Allowances to Electric Distribution Utilities

DRA supports ARB's proposal to allocate allowances to the electric distribution utilities for the benefit of their customers. Free allocation of allowances to the electricity sector is essential for the California cap-and-trade program. This should provide the utilities with more time to reduce their emissions in a cost-effective manner, limit unnecessary short-term costs, and enable the utilities to transition to a low-carbon economy at the right pace. While it is clear that California can be a model for regional, national and international cap-and-trade programs, California consumers should not pay for the greater part of these efforts.

DRA Recommends Free Allocation of Allowances to Natural Gas Distribution Utilities

DRA recommends free allocation of allowances to natural gas distribution utilities, beginning in 2015 when they are covered under the cap-and-trade program, analogous to how investor-owned utilities are treated in the electricity sector. Similar to electricity customers, it is important to protect natural gas customers from significant rate impacts.

DRA Recommends that the Allowance Value From Electric Distribution Utilities Should be Returned to Ratepayers in the Form of Rebates

DRA supports the requirement that electric distribution utilities must auction the allowances directly allocated to them, and use the proceeds from the auctions to the benefit of ratepayers. DRA recognizes that the CPUC and local governing boards (for publicly-owned utilities) will have oversight over the proceeds from the sale of allowances, and if there is no clear guidance provided by ARB, there will likely be a proceeding at the CPUC to determine the final amount of investor-owned utility (IOU) proceeds dedicated to rebate programs or to other GHG-reduction programs that will “benefit ratepayers.” DRA is concerned that the Proposed Regulation is too vague to ensure that the allowance proceeds are used to directly benefit ratepayers. Without more specific language, DRA believes that there is a risk of the allowance proceeds being spent on programs or investments that may not translate to the direct cost savings that are necessary to balance the impacts of AB 32 programs on electricity rates.

DRA recommends 100 percent of allowance value freely allocated to electric distribution utilities should be directly returned to ratepayers in the form of rebates. Rebates (as opposed to rate reductions) will ensure that the carbon price will still be reflected in retail rates and incentivize increased conservation and energy-efficiency activities. If the Proposed Regulation does not adopt this recommendation, DRA requests that ARB provide clear guidance in the Proposed Regulation as to where the allowance proceeds should be directed. This should be supported by analysis that shows how and to what extent the specified programs will mitigate the bill impacts of AB 32 programs on their distribution customers.

DRA Supports the Use of Offsets as a Cost Containment Measure and ARB Should Ensure Offset Supply Throughout the Program

Cost containment is a key policy objective within GHG cap-and-trade compliance programs, and DRA supports the use of offsets as a cost containment measure. DRA supports the increased offset limit of eight percent of an individual entity’s compliance obligation. DRA believes this will provide covered entities with compliance flexibility while also ensuring that some emissions reductions occur from sources outside of capped sectors. While the majority of emissions reductions need to come from sectors that are regulated by the program, this offset limit could help provide the appropriate balance between emissions reductions required by covered entities and containing costs from reaching harmful levels.

DRA is aware of the market concern that there will not be enough offsets available to meet the demand of the increased offset limit. If the supply of offsets in the California program is constraining the ability of compliance entities to meet their offset limit, then ARB should have an active process to review additional offset protocols to include in the program. DRA supports ARB’s criteria for offset quality requirements: real, additional, quantifiable, permanent,

verifiable, and enforceable. DRA is also encouraged by the framework that is established for sector-based offset credits from developing countries, and believes that offset credits from reducing emissions from deforestation and forest degradation (REDD) are important to meet California's demand for offsets. DRA recommends that ARB continues its leading role in developing sector-based offset crediting mechanisms, and work towards approving REDD credits for meeting compliance obligations in the California program.

DRA Recommends that ARB Establish a Market Oversight Committee

Effective market oversight is a necessary component of GHG cap-and-trade compliance programs. The California cap-and-trade market is likely to be a complex system and its costs to consumers need to be regularly monitored and evaluated. The Proposed Regulation notes that "unanticipated effects and results could occur over the life of the program" and that "ARB will monitor the program to ensure that it is achieving emissions reductions and other AB 32 objectives and is not resulting in unanticipated outcomes." Further, "ARB will regularly (at a minimum, once every three-year compliance period) evaluate whether the objectives identified by the statute are being achieved."¹

DRA supports this program monitoring, however also believes that ARB should establish a market oversight committee that meets regularly to assess whether the market is functioning as expected. The committee should be comprised of market experts with experience in market monitoring activities and could include members from ARB, the CPUC, the CEC, and CAISO. DRA recommends that this committee be given the authority to suspend the program or recommend that the Governor suspend the program if allowance prices remain unacceptably high, if the program is not achieving the objectives as defined by AB 32, or if the program results in unforeseen and harmful impacts to consumers.

DRA Requests Clarification of the Revised 2020 Cap Level

The AB 32 goal of reducing statewide emissions to 1990 levels by 2020 establishes a hard target for the 2020 economy-wide emissions level (427 MMT CO₂e). ARB's Scoping Plan initially estimated the 2020 cap for sources covered by the cap-and-trade program at 365 MMT CO₂e. The Proposed Regulation revises the 2020 cap level for sources covered by the program to 334.2 MMT CO₂e. This presumably means that the expected emissions from sectors and sources outside of the cap-and-trade program have increased, as the overall economy-wide emissions level in 2020 should remain constant at 427 MMT CO₂e. However, ARB has indicated that the revised estimate is based on better facility level data for emissions from sources covered by the cap-and-trade program. DRA requests that the difference in cap calculations should be further explained in Appendix E: Setting the Program Emissions Cap, as the credibility of the 2020 cap

¹ CARB, Proposed Regulation to Implement the California Cap-and-Trade Program, p 57, October 28, 2010.

calculation is critical to the cap-and-trade program, and it is important that both capped and uncapped sources share the responsibility of emissions reductions in California.

Thank you for this opportunity to comment on the Proposed Regulation to Implement the California Cap-and-Trade Program and we look forward to providing ARB staff with more comments on program aspects that are still being developed. For any questions regarding these comments, please contact Jordan Parrillo at Jordan.Parrillo@cpuc.ca.gov or (415) 703-1562.

Best Regards,

 /s/
Dave Ashuckian
Deputy Director
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