



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Office of the General Manager

October 22, 2013

Richard R. Corey
Executive Officer
Air Resources Board
1001 I Street
Sacramento, CA 95814

Re: Air Resources Board's Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms (Proposed Amendments)

Dear Mr. Corey:

The Metropolitan Water District of Southern California (Metropolitan) has reviewed the Air Resources Board's (ARB) Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms (Proposed Amendments), which ARB released on September 4, 2013, and provides the following comments on this document.

Background

As the nation's largest provider of drinking water, Metropolitan distributes water from the Colorado River and Northern California to 26 member agencies (cities and water districts), and supplies more than one-half of the water used by nearly 19 million people in the 5200 square-mile coastal plain of Southern California. Metropolitan's mission is to provide its member agencies with adequate and reliable supplies of high quality water to meet present and future needs in an environmentally and economically responsible way. In order to bring Colorado River water to Southern California, Metropolitan directly imports wholesale electricity for the sole purpose of operating the electrical pumps on the Colorado River Aqueduct (CRA). Metropolitan also obtains a significant portion of its water from the State Water Project (SWP) and pays more than 70% of the energy costs that the SWP incurs.

Metropolitan has a significant financial and regulatory stake in the cap-and-trade regulations and, consequently, has actively participated in the formulation of those rules from the beginning of the ARB process. Since Metropolitan does not buy power in-state, it incurs cap-and-trade-related costs through the purchase of allowances to cover the emissions associated with its imported non-hydroelectric energy. Since the SWP does not presently import energy, most of the cap-and-trade-related costs that it incurs are the indirect costs associated with higher energy prices, and with the operation of the natural gas-fueled Lodi Energy Center.

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In spite of the ARB resolutions instructing ARB staff to work with the water sector to mitigate AB 32 compliance costs and the numerous discussions between ARB staff and water sector representatives, the parties have been unable to agree upon specific regulatory language or an allocation methodology that adequately mitigates cost impacts on the ratepayers of wholesale water providers. While the latest amendments to the cap-and-trade regulations provide some cost mitigation to Metropolitan in the form of a small allocation of free allowances, the methodology for this allocation in the amended regulations is fundamentally flawed. In addition, the amended regulations provide no cost mitigation for the SWP.

Comments

Metropolitan appreciates the efforts made by ARB staff to address cost impacts on publicly-owned wholesale water utilities and their ratepayers. However, additional modifications to the existing regulations will be required in order to provide adequate and equitable cost mitigation. Metropolitan provides the specific recommendations included below. These recommendations stem from the over-arching need to provide comparable treatment to the customers of both Metropolitan and the SWP that ARB has provided to the customers of the Electric Distribution Utilities (EDUs). Metropolitan recognizes that ARB has chosen to deal with the wholesale water utilities through a separate process and is not requesting that ARB revisit the EDU allowance allocation process. Metropolitan is, however, requesting that ARB not impose burdens on the water utilities that it imposed on the EDUs without also bestowing comparable benefits.

1. Definition of “Public Wholesale Water Agency”

As Metropolitan has consistently argued in its formal and informal comments to ARB, cost mitigation should clearly be provided to both Metropolitan and the SWP. As ARB implicitly recognized when it permitted the POU's to either monetize their free allowances or use them to meet their compliance obligation, both direct and indirect costs will be borne by a utility's ratepayers. Public agencies, including the POU's, Metropolitan, and the SWP, must pass all of their costs along to their ratepayers in the form of rate increases, irrespective of how the costs are incurred. Thus, with respect to price mitigation, the costs of increased energy prices are indistinguishable from the costs of purchasing allowances to meet a compliance obligation.

Furthermore, when ARB allocated free allowances to EDUs, it did so for the benefit of the EDUs' ratepayers, stating that allowance value could be used for “rebates, customer bill relief, or to pay for GHG-reducing measures such as energy efficiency, renewable electricity generation, or other similar programs.”¹ This rationale for the use of free allowances clearly contemplates that free allowances may be used by the EDUs to mitigate any cost impacts on ratepayers (direct

¹ Proposed Regulation to Implement the California Cap-and-Trade Program, Staff Report: Initial Statement of Reasons (“ISOR, 2010 Regulations”) at II-28. (Posted on Oct. 28, 2010: <http://www.arb.ca.gov/regact/2010/capandtrade10/capisor.pdf>)

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or indirect). There is no equitable basis for utilizing a different standard for wholesale water agencies.

Recommendation: Revise Section 95802(a)(287) to include Department of Water Resources in the definition as follows:

“Public Wholesale Water Agency” means a covered entity that is owned and operated as a special district, as defined in Statutes of 1960, Ch. 209 (California Water Code appendix § 109), and a state agency acting pursuant to California Water Code sections 120 and 12931 et seq., that uses electricity to convey wholesale water supplies.

2. Distribution of Allowances to Public Wholesale Water Agencies

Consistent with the comments in section 1 above, it is inequitable to limit a Public Wholesale Water Agency’s use of allowances to direct compliance costs. Such a limitation is inconsistent with the rationale upon which ARB relied when permitting POUs to either monetize free allowances to mitigate ratepayer impacts or use them to meet their compliance obligations:

Most POUs own and operate their own generation and do not compete with independent generators in the way IOUs do. Because of this, allowances directly allocated to POUs may either be consigned for sale at the general quarterly auctions or used directly to meet their compliance obligations. If a POU decides to auction some of its allowances at the general auction, the same auction rules apply to the POUs as those described above for the IOUs.¹

ARB should therefore modify its Proposed Amendments to give Public Wholesale Water Utilities the same flexibility that it has given EDUs in utilizing free allowances for the ultimate benefit of their ratepayers.

Recommendation: Revise Section 95870(d)(2) as follows:

Allocation to Public Wholesale Water Agencies. The Executive Officer will place an annual individual allocation in the limited use holding account of a public wholesale water agency on or before October 15, or the first business day thereafter, of each calendar year from 2014-2019 for allocations from 2015-2020 annual allowance budgets. The Public Wholesale Water Agencies shall advise the Executive Officer of the amount of allowances needed to be moved from the limited use holding account to the compliance account, so the Executive Officer can conduct these transfers. The Public Wholesale Water Agency may monetize at auction, allowances that remain in the limited use holding account, after their compliance obligations have been met. The Public Wholesale Water Agencies shall use the moneys obtained from the allowances solely for projects that reduce greenhouse gas emissions. The Public Wholesale Water Agencies shall

¹ ISOR, 2010 Regulations at II-32.

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provide an annual report to the Executive Officer on their use of these moneys.

3. Specific Allocation of Allowances to Metropolitan

Because its need to purchase imported energy, and thereby obtain allowances, varies based on operational needs, Metropolitan provided historical data to ARB, including annual averages, in order to facilitate the calculation of its allowance allocation. However, in calculating the allocation reflected in Table 9-5 of Section 95895, ARB relied on factors other than Metropolitan's actual compliance costs.

ARB purports to allocate allowances to Metropolitan "in a manner similar to the allocation to EDUs" based on "the compliance burden on ratepayers,"¹ but, in actuality, it would impose upon Metropolitan the burdens it placed on EDUs without conferring any of the benefits. In calculating the free allowances to be distributed to the EDUs, ARB considered the compliance costs associated with California's Renewable Portfolio Standard (RPS) as one basis for *providing* an allocation. ARB then reduced the EDUs' allowance allocation in the out years based on the theory that the initial investment in renewable resources would reduce the future need for allowances.

Since it does not serve retail electric customers, Metropolitan does not have an RPS requirement. While it would therefore be inappropriate to provide Metropolitan with assistance in meeting a RPS requirement, it is also inequitable to use an RPS requirement to reduce Metropolitan's allowance allocation going forward. Furthermore, the EDUs' declining allocation is based at least in part on the declining cap. Applying the declining cap and factoring in a reduced need for allowances due to renewable energy procurement unfairly reduces Metropolitan's allowance allocation well below its anticipated compliance costs.

The table below contains a calculation of allowances that should be allocated to Metropolitan, consistent with the principles articulated herein. To the extent possible, Metropolitan has used the input categories that ARB utilized to calculate its proposed allocation.

¹ Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, Staff Report, Initial Statement of Reasons at 22. (Posted on Sept. 4, 2013: <http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isor.pdf>.)

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Metropolitan Water District - Colorado River Aqueduct Cap and Trade Cost Burden Mitigation								
Year	2013	2014	2015	2016	2017	2018	2019	2020
MWD CRA Energy Use Total (MWh) - Average 2008-2012	1,795,257	1,795,257	1,795,257	1,795,257	1,795,257	1,795,257	1,795,257	1,795,257
MWD Large Hydroelectric Hoover and Parker Dams (MWh) - Average 2008-2012	1,301,308	1,301,308	1,301,308	1,301,308	1,301,308	1,247,085	1,247,085	1,247,085
MWD Unspecified within CA (MWh) - Average 2008-2012	168,937	168,937	168,937	168,937	168,937	168,937	168,937	168,937
Average Net Unspecified Energy to be Imported into California (MWh)	325,012	325,012	325,012	325,012	325,012	379,235	379,235	379,235
Natural Gas and Market Energy Emission Factor (MT/MWh)	0.4354	0.4354	0.4354	0.4354	0.4354	0.4354	0.4354	0.4354
Greenhouse Gas Associated with Unspecified, Imported Energy (MT)	141,510	141,510	141,510	141,510	141,510	165,119	165,119	165,119
Cap Decline Factor	0.981	0.963	0.944	0.925	0.907	0.888	0.869	0.851
Emissions for Cost Burden Mitigation (MT)	138,822	136,274	133,586	130,897	128,350	146,626	143,488	140,516
Energy Efficiency Credit	3,908	3,908	3,908	3,908	3,908	3,908	3,908	3,908
Annual Allowance Value	142,730	140,182	137,494	134,805	132,258	150,534	147,396	144,424
Allowance Allocation to MWD			420,406	134,805	132,258	150,534	147,396	144,424

Recommendation: Replace the allocation in Table 9-5 of Section 95895 with the last line from the table above.¹

Metropolitan appreciates this opportunity to comment on the proposed amendments to the cap-and-trade regulations and is available to discuss its recommendations in greater detail.

Sincerely,



Jeffrey Kightlinger
 General Manager

¹ Metropolitan endorses the allocation methodology for the SWP provided in the comments of the California Department of Water Resources and the State Water Contractors.