

COMMENTS OF SOUTHERN CALIFORNIA EDISON COMPANY TO THE
CALIFORNIA AIR RESOURCES BOARD ON LINKING CALIFORNIA'S CAP-AND-
TRADE PROGRAM TO OTHER GREENHOUSE GAS TRADING PROGRAMS

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Dated: **August 21, 2009**

I.

INTRODUCTION

Southern California Edison Company (“SCE”) appreciates the opportunity to comment on potential linkages between a California greenhouse gas (“GHG”) cap-and-trade program and other cap-and-trade programs. SCE agrees with the California Air Resources Board (“CARB”) staff in its July 27, 2009 workshop on “Linking California’s Cap-and-Trade Program to Other Greenhouse Gas Programs” that linkage will provide significant benefits for both regulated entities as well as customers within California. SCE therefore supports CARB’s efforts to develop a framework for linkages and encourages CARB to implement all possible linkages that further the goals of Assembly Bill (“AB”) 32.

SCE recommends that CARB consider the following issues when developing protocols for linking with outside cap-and-trade programs.

II.

A CAP-AND-TRADE LINKAGE FRAMEWORK SHOULD MAINTAIN

CALIFORNIA’S ENVIRONMENTAL INTEGRITY

CARB should ensure that any future linking of cap-and-trade programs will not compromise the integrity of the GHG emissions reductions undertaken by entities within California. Any programs linked to by CARB must have a robust program administration, including provisions for monitoring, reporting, verification, and enforcement. Further, programs under consideration for linking must have regulations and cap levels with GHG emissions reductions at least as stringent as that of California.

A. Outside Programs Must Have Provisions for Monitoring, Reporting, Verification, and Enforcement.

Provisions for emissions monitoring, reporting, enforcement, and compliance are the backbone of a cap-and-trade program. CARB must ensure that any linked program has reporting

standards and requirements analogous to California's: one ton of carbon in Program A must be the same as one ton of carbon in Program B. The outside program must have systems in place to ensure that GHG emissions can be adequately and reliably monitored and verified. In addition, the agency administering the outside program must have strong mechanisms available to enforce compliance with the cap-and-trade program.

B. Outside Programs Must Have Rigorous Reduction Targets.

Any outside program linked to by California must have reduction targets that are at least as stringent as those in California. In assessing program stringency, CARB should focus on the long-term emissions target (the 2020 cap level or the 2050 cap level if available). A program's long-term target is the most critical indicator of its stringency and should be given greater weight than short-term targets.

C. CARB Should Consider the Effect of Indirect Linkages When Linking to Outside Programs.

CARB should recognize and closely evaluate the impact of indirect linkages on environmental integrity. An indirect linkage, where two programs are effectively linked because each has linked to a third program, may result in California accepting allowances created under less rigorous standards. Other cap-and-trade programs may have flexibility provisions for allowances such as safety valves, banking, multi-year compliance periods, and offsets, which have not been vetted under the strict review required in California and may be considered too weak. As CARB staff has recognized, when California links to an outside cap-and-trade program, the outside program's flexibility provisions will flow through to California's program. Flexibility provisions in a third cap-and-trade program linked to by the outside program will also flow through to California. Thus, CARB should recognize that linking to one outside program means that California will effectively accept not only that program's weakest provisions, but also the weakest provisions of any other cap-and-trade programs linked to it.

The potential for indirect linkage is crucial in considering the type of offsets accepted by other programs. California cannot realistically accept only a subset of offsets from an emissions reduction crediting system. For example, CARB might determine that some clean development mechanism (“CDM”) credits are desirable while others are not. However, accepting any CDM credits from another cap-and-trade program is tantamount to accepting all of them. If CARB accepts only “good” credits, a third program that accepts all CDM credits could simply sell some “good” credits to entities in California and replace them with “bad” CDM credits. Consequently, the environmental result is identical to a scenario in which CARB itself accepted all CDM credits. Similarly, if the European Union Emission Trading System (“EU ETS”) accepts *any* credits from the CDM, and California links with the EU ETS, then CARB has also essentially accepted *any* CDM credit as suitable for compliance in California.

III.

COST CONTAINMENT PROVISIONS ARE CRUCIAL WHEN LINKING TO OUTSIDE CAP-AND-TRADE PROGRAMS

CARB should consider cost-containment a necessary component for any program under consideration for linkage. However, CARB should ensure that other programs’ cost containment provisions do not compromise environmental integrity.

In particular, CARB should carefully examine the offset protocols of any programs under consideration. At a minimum, the outside program’s offset policies must ensure credits issued represent offsets that are real, permanent, verifiable, and additional. Ideally, additionality should be tested through the use of a positive list that identifies pre-approved eligible project types. If a case-by-case test of additionality is used, CARB should evaluate financial barriers as well as common practices.

IV.

DIFFERENCES IN PROGRAM SCOPE AND ALLOWANCE ALLOCATION ARE IRRELEVANT WHEN CONSIDERING LINKAGE TO OUTSIDE CAP-AND-TRADE PROGRAMS

The inherent flexibility of market-oriented policies such as cap-and-trade programs allows linkage with programs that may differ in certain respects from California's cap-and-trade program. To the extent that programmatic variations do not compromise the environmental integrity of California's program or pose technical problems with implementing a linkage, these variations should not be seen as an obstacle to linkages.

Differences in the scope and number of covered sectors in outside cap-and-trade programs should not prevent California from linking with such programs. Because some sectors are more difficult to regulate than others, one would expect to see variations in covered sectors in other programs, particularly when considered across multiple timeframes. For example, in California and in the Western Climate Initiative, two key sectors may not be added to the cap-and-trade program until the second compliance period. It is unrealistic for California to expect another program to have an identical set of covered sectors at all points in time. In any case, such a requirement would be unnecessary and inefficient, as differences in scope would not present technical problems in linking California to an outside program.

Similarly, differences in allowance allocation schemes will not affect market interactions when two cap-and-trade programs are linked. Consequently, allowance allocation should not be considered in any linkage determinations.

V.

CARB SHOULD AVOID UNNECESSARY QUANTITATIVE LIMITS ON ALLOWANCES

Limits on the number of allowances that may be transferred from one jurisdiction to another will only limit the number of opportunities for cost-effective reductions. SCE

recommends avoiding quantitative limits on the volume of allowances traded across jurisdictions.

VI.

CAREFUL EXAMINATION OF OTHER CAP-AND-TRADE PROGRAMS BEFORE LINKAGE IS ESSENTIAL TO MAINTAINING REGULATORY STABILITY

CARB should seek to avoid actions that cause undesirable volatility in the allowance market, such as repeated linking and delinking with other cap-and-trade programs. When forming a linkage with a program from another jurisdiction, it is always possible that the outside program might change, making a linkage no longer desirable. CARB should include provisions in its cap-and-trade program that allows for delinking in cases where an outside program undergoes significant changes. Specific conditions that would precipitate delinking should be clearly established prior to linking.

Dramatic changes such as delinking could precipitate large price swings (in particular, price spikes) that would be undesirable from the perspective of all parties. Delinking should be seen as a strategy of last resort. Before linking with an outside program, CARB should be reasonably confident that the program is stable and is unlikely to necessitate later delinking.

VII.

CARB SHOULD LINK CALIFORNIA'S CAP-AND-TRADE MARKET TO THE LOW-CARBON FUEL STANDARD CREDITS MARKET

SCE supports a linkage to the market created through the Low-Carbon Fuel Standard ("LCFS"). The transition in the transportation sector from liquid fossil fuels to electricity has the potential to become a cost-effective source for GHG reductions. Electrification of transportation has the potential to reduce the emissions from the liquid fuel transportation sector by millions of metric tons by 2040. While SCE stands ready to help reduce transportation emissions, electrification could cause emissions in the electricity sector to rise. As a result, electricity customers would be burdened with a cross-sector shift in regulatory obligation. Although the

electric sector can provide part of the solution to the transportation emissions challenge, electricity customers should not be unfairly burdened with this shift in regulatory expense. LCFS credits are essential to help mitigate these displaced costs. CARB should take advantage of this opportunity to reduce California's overall cost in achieving its AB 32 goals.

By linking LCFS credits into California's AB 32 cap-and-trade program, CARB can help to establish a viable trading market for LCFS credits. Currently, there is concern within the industry that the liquid fuels sector will not participate in the LCFS market. LCFS-regulated parties in the liquid transportation fuels sector could have significant monopsony power over the LCFS credit market. Allowing the trading of LCFS credits in the AB 32 cap-and-trade market would alleviate this concern and protect electricity customers from the burden of a cross-sector shift in regulatory expense.

CARB staff identified a few concerns related to linking with the LCFS market during its July 27th workshop. Mechanisms are available to address their issues regarding double-counting and additionality. Given that CARB will be administering both the LCFS market and the AB 32 market, CARB can ensure that the registry systems protect against the possibility of double-counting. In addition, because the LCFS market will have stringent emissions requirements and will require reductions below Business-as-Usual emissions in the transportation sector, LCFS credits will represent real and additional GHG reductions in the electric sector. Allowing the use of LCFS credits in the AB 32 cap-and-trade market will thus facilitate further reductions in total emissions.

VIII.

CONCLUSION

SCE appreciates the time and effort from CARB staff in bringing California closer to its GHG reduction goals and urges CARB to adopt regulations in accordance with the principles discussed herein.

Respectfully submitted,

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