CALIFORNIA AIR RESOURCES BOARD

May 2019

Guidance on Electrical Distribution Utilities and Natural Gas Suppliers Use and Reporting of Allocated Allowance Proceeds

(*Cap-and-Trade Regulation sections 95892 and 95893)*

Note: This document is provided to describe regulatory requirements in a user-friendly format. It does not have the force of law, does not establish new requirements, and in no way supplants, replaces, or amends any of the legal requirements of the Cap-and Trade Regulation (Regulation). Any omission or truncation of regulatory requirements in this guidance does not relieve entities of their legal obligation to fully comply with all requirements of the Regulation.

INTRODUCTION

This document provides guidance for electrical distribution utilities (EDUs) and natural gas suppliers (NG suppliers) on sections 95892 and 95893 of the Cap-and-Trade Regulation (Regulation).[1] Sections 95892(a) and 95893(a) of the Regulation state that, "[a]llowance value, including any allocated allowance auction proceeds, obtained by an [EDU or NG supplier] must be used for the primary benefit of retail [electricity or natural gas] ratepayers of each [EDU or NG supplier], consistent with the goals of AB 32 and must not be used for the primary benefit of entities or persons other than such ratepayers."

This document provides responses to frequently asked questions regarding the amended Regulation that is effective April 1, 2019. Amendments to the Regulation clarify, enhance, and streamline provisions on the permissible use of allowance value allocated to EDUs and NG suppliers for the purpose of benefitting their ratepayers consistent with the goals of AB 32.

The amended Regulation requires that expenditure of EDU allocated allowance proceeds (allowance proceeds) must fall into one of four general categories that benefit ratepayers and are consistent with the goals of AB 32: renewable energy, energy efficiency, and fuel switching, other GHG reducing activities, and non-volumetric return of proceeds to ratepayers. Similarly, NG suppliers must use allowance proceeds for energy efficiency or other GHG reducing activities, or for non-volumetric return of proceeds to ratepayers.

Among the allowed uses of allowance proceeds, the amended Regulation provides a potential path for the use of allowance proceeds for wildfire risk reduction and allows limited use of allowance proceeds on certain educational programs. Other amendments clarify allowance value use for reasonable administrative and outreach costs and specify particular activities that are prohibited uses of allowance value, including compliance activities, lobbying, and benefitting employees or shareholders. The amendments require the reporting of estimated GHG reductions for uses of allowance proceeds other than non-volumetric returns and certain educational programs and reorganize reporting requirements to clarify how expenditures must be reported and what time periods they cover.

[1] https://www.arb.ca.gov/cc/capandtrade/capandtrade/ct_reg_unofficial.pdf

Frequently Asked Questions

Question 1: *How do the requirements for the use of allocated allowance value in sections 95892(d) and 95893(d) of the amended Regulation apply to EDU and NG supplier allocated allowance proceeds already received prior to the effective date of the amended Regulation (April 1, 2019) but not yet spent?*

Answer: The adopted amendments apply to all uses of allowance proceeds after the effective date, including all uses of allowance proceeds received prior to the effective date that remain unspent by the effective date (i.e., allowance proceeds that have not been either disbursed or specifically obligated pursuant to a contract for a specified use where the contract is executed prior to the effective date of the amendments).

Allowance proceeds spent *prior* to the effective date of the amendments and proceeds that were specifically obligated pursuant to a contract for a specified use where the contract was executed prior to April 1, 2019 are subject to the use requirements of section 95892 or 95893 of the Cap-and-Trade Regulation effective October 1, 2017.

Question 2: *How do the requirements on the reporting of allocated allowance value in sections 95892(e) and 95893(e) of the amended Regulation apply to EDU and NG supplier allocated allowance value use that has not yet been reported to CARB?*

Answer: Uses of allocated allowance value that have not yet been reported to CARB are subject to the amended Regulation, effective April 1, 2019 with regard to the reporting requirements of section 95892(e) or 95893(e). Revised Use of Allocated Allowance Value Reporting Forms with detailed instructions and new GHG Benefits Estimation Tools are available at the EDU and NG supplier Use of Allocated Allowance Value webpage to facilitate reporting on the use of allowance value in the 2018 data year.

Question 3: *In earlier years of the Cap-and-Trade Program, I reported only on the use of proceeds received from the sale of allowances with a specific vintage year, and sometimes the reporting period spanned 18 months. Should I still report use of allowance proceeds in this way?*

Answer: No. Based on amendments effective October 1, 2017, all use of allowance value reporting is now on a calendar year basis. Reporting should only cover expenditures and unspent proceeds in the applicable data year. By June 30, 2019, EDUs and NG suppliers must report on all proceeds spent during data year 2018, regardless of the allowance vintage year of allowances sold to generate the proceeds.

For investor-owned utilities, use of value reporting should conform to the expenditures of allowance proceeds reported to, and approved by, the California Public Utilities Commission.

Question 4: *My use of allowance proceeds is not addressed by the GHG Benefits Estimation Tool provided by CARB, and I am not sure how to estimate its benefits. What should I do?*

Answer: CARB staff is available to assist with estimating GHG emissions reductions for all allowable uses of allowance proceeds in conformance with the requirements of the amended Regulation. CARB provided a GHG Benefits Estimation Tool to support EDU and NG supplier compliance with the reporting requirements in the Regulation. The tool contains calculators to estimate GHG emissions reductions for the most common uses of allowance proceeds that are reported to CARB. Using this tool is optional, and CARB staff is available to assist EDUs and NG suppliers with using the GHG Benefits Estimation Tool if needed.

For allowable uses of allowance proceeds not included in the GHG Benefits Estimation Tool, CARB staff is available to assist in discussing approaches to estimate GHG reductions from those uses that are consistent with the requirements of the Regulation. Please contact staff as soon as possible so that we may assist you in a timely manner.

Consistent with the requirements of sections 95892(d)(5) and 95892(e)(4)(B) for EDUs and sections 95893(d)(5) and 95893(e)(4)(B) for NG suppliers, the GHG Benefits Estimation Tool uses the following framework:

- The benefits are estimated for the entire expected project lifetime.
- GHG benefits are estimated by comparing the anticipated emissions attributable to the use of allowance proceeds to the anticipated emissions in the absence of the use of allowance proceeds. This estimate applies the emissions factors in the "Emission Factors" tab of the GHG Benefits Estimation Tool, which are consistent with the requirements of the Regulation.
- The GHG benefits of allowance proceeds use are prorated to the percentage of total lifetime project costs that are covered by allowance proceeds, including allowance proceeds used for administration and outreach of the project.

  For example, if the total lifetime projected cost of a project were $10,000 and $5,000 of allowance proceeds were spent on the project during the data year, then 50 percent of the total estimated GHG benefits of the project would be attributable to the use of proceeds on that project in that data year.

Question 5: *Our utility is using allowance proceeds for a single project that will be funded with allocated allowance proceeds from multiple years. How should I estimate the GHG benefits for a single year?*

Answer: First, estimate both the total GHG benefits and total project costs over the expected project lifetime. Then calculate the allowance proceeds spent in the data year, including administrative and outreach expenditures, as a percentage of the total project costs over the expected lifetime. Multiply the total GHG benefits over the expected lifetime by the percentage project costs funded with allowance proceeds in the data year to estimate the GHG benefits attributable to the use of proceeds during the data year.

For example, if the total cost of a project over its lifetime is expected to be $10,000 dollars and $5,000 of allowance proceeds were spent on the project during the first data year, then 50 percent of the total estimated GHG benefits of the project would be attributable to the use of allowance proceeds in the first data year. If in the second data year, $2,000 dollars of allowance proceeds are spent on the project, then 20 percent of the total GHG benefits should be reported for the second data year.

This calculation method is built into the GHG Benefit Estimation tools.

Question 6: *How do I report itemized administrative and outreach costs?*

Answer: EDUs and NGS may report itemized administrative and outreach costs using Use of Allocated Allowance Value Forms for data year 2018. These forms are available on the EDU and NG supplier Use of Allocated Allowance Value webpage. These forms contain specific instructions on how to report administrative and outreach costs. For expenditures during 2019 and later, pursuant to section 95892(d)(4) or 95893(d)(4), spending on administrative and outreach costs must be limited to necessary costs to administer the projects and activities undertaken using allowance proceeds and outreach that directly supports the implementation of allowable projects or activities under the Regulation.

For non-volumetric return of proceeds to ratepayers, acceptable administrative and outreach costs may include changes to billing systems and bills inserts necessary to provide and explain the returns to ratepayers. For expenditures on GHG reducing activities, acceptable administrative and outreach costs may include utility personnel costs to oversee the GHG reducing activity and to conduct outreach necessary to recruit program participants. Any use of allowance proceeds on administrative and outreach costs must be itemized in a manner that enables CARB to assess its relationship to the implementation of the reported project or activity.

CARB expects that GHG reducing activities, such as energy efficiency programs and development of renewable energy projects, will generally require small amounts of administration and outreach costs and that the administrative and outreach costs necessary for the non-volumetric return of proceeds will be a very small percentage of the proceeds returned. CARB will assess the necessity of these administration and whether outreach expenditures directly support allowable uses of proceeds based on reported and public data on comparable uses and any applicable legislative requirements.

The administrative and outreach costs reported to CARB by investor-owned utilities should conform to the administrative and outreach costs reported to and approved by the California Public Utilities Commission.

Question 7: *When can EDUs use allowance proceeds for wildfire risk reduction?*

Answer: Using allocated allowance proceeds to fund wildfire risk reduction activities differs from most allowed use types insofar as its intended impact on GHG emissions is to reduce the risk of wildfires, and thereby reduce the risk of increased GHG emissions from wildfires.

Wildfires are a significant source of GHG emissions in California and reducing wildfire risk may constitute reducing *expected* emissions. Any use of allowance proceeds for these purposes must be aligned with statewide efforts to appropriately manage wildfire risks in a manner that benefits and protects ratepayers and the climate. Use of allowance proceeds for wildfire risk reduction must also demonstrate expected GHG emission reductions, consistent with the requirements of the amended Regulation.

EDUs may use allowance proceeds to fund wildfire mitigation and forest carbon sequestration activities contingent on both the development of a standardized system for quantifying GHG emissions reductions pursuant to Health and Safety Code section 38535(a) and the approval of a utility's wildfire mitigation plan as required by statute.

CARB is currently working with CAL FIRE to develop a standardized methodology for quantifying GHG reductions from fuel reduction activities that is consistent with Health and Safety Code section 38535(a). CARB plans to issue guidance once that effort has been completed to indicate when and how allowance proceeds may be used for wildfire risk reduction.

Question 8: *Can I use allocated allowance proceeds for research and development?*

Answer: All uses of allowance proceeds must conform to the requirements of the Regulation. To the extent that research, development, and demonstration projects have quantifiable GHG emissions reductions, such activities may be permissible uses of allowance proceeds pursuant to the sections 95892(d)(3)(C) and 95893(d)(3)(B) of the Regulation ("Other GHG Emission Reduction Activities"). Allocated allowances are provided to the EDUs and NG supplier to benefit ratepayers and reduce GHG emissions, and any expenditures of allowance proceeds must meet these requirements. Generally, research and development efforts with uncertain outcomes do not meet these requirements.

Question 9: *How can I use allowance proceeds for educational programs?*

Answer: Effective April 1, 2019, EDUs and NG suppliers may use up to $100,000 or one percent of the total allocated allowance auction proceeds expended by the utility in that data year, whichever is larger, for educational programs that cannot demonstrate expected GHG emissions reductions benefits. These educational programs must have the primary purpose of reducing the GHG emissions of the EDU's or NG supplier's ratepayers.

For example, if a utility spends $20 million dollars of allowance proceeds in the data year, they may spend up to one percent of that amount ($200,000) in that data year on educational programs that cannot demonstrate GHG emissions reduction benefits. If a utility spends $400,000 of allowance proceeds in a data year, then it may spend up to $100,000 dollars on educational programs that cannot demonstrate GHG emissions reduction benefits.

Educational programs for which GHG emission reduction benefits can be demonstrated pursuant to the reporting requirements of the Regulation may also be allowable under the “Other GHG Reduction Activities” category (95892(d)(3)(C) or 95893(d)(3)(B)), which does not have a spending cap. In addition, allowance proceeds may be used to fund outreach activities that directly support the implementation of the projects or activities funded pursuant to sections 95892(d)(3)(A)-(D) or 95893(d)(3)(A)-(C).

EDUs and NG suppliers can first report these uses for the 2019 data year in June of 2020.

Question 10: *Does the amended Regulation require that the use of allowance proceeds result in GHG emissions reductions beyond what is required by law? For example, to use allowance proceeds for renewable energy procurement, does the procurement need to be in excess of the Renewable Portfolio Standard (RPS) requirements?*

Answer: No, the Regulation does not contain an additionality requirement for uses of allowance proceeds. Uses of allocated proceeds must conform to the requirements of section 95892 or 95893 of the Regulation, which specify allowable uses. Expenditures on renewables must be for renewable energy projects or renewable electricity that is either directly delivered to California in conformance with RPS portfolio content categories 1 or zero, as specified by Public Utilities Code Section 399.16, or from or for a ratepayer-owned renewable generator or a renewable generator in the EDU’s service territory. Renewable electricity purchased with allowance proceeds must meet these requirements, but it does not need to be in excess of the RPS requirements. EDUs may use the GHG Benefits Estimation Tools available on the [EDU and NG supplier Use of Allocated Allowance Value] webpage to estimate GHG emissions reductions for renewable energy purchases.

Question 11: *Can a publicly owned utility (POU) deposit its allocated allowances for compliance with the Cap-and-Trade Program? Can a utility use allowance proceeds to purchase allowances to satisfy compliance obligations? What about compliance obligations associated with electricity sold into CAISO markets?*

Answer: POUs may have allocated allowances deposited directly into compliance accounts to fulfill their own or related compliance obligations as allowed by section 95892(b)(2). However, section 95892(d)(7)(B) of the Regulation effective April 1, 2019 explicitly prohibits using *allowance proceeds* to purchase allowances in order to satisfy compliance obligations.

Pursuant to section 95892(d)(7)(A) of the Regulation, allocated allowances may not be used to fulfill a compliance obligation associated with electricity sold into the California Independent System Operator (CAISO) markets. In order to assess compliance with section 95892(d)(7)(A) for allocated allowances deposited directly into compliance accounts, POUs and electrical cooperatives (COOPs) are required, pursuant to section 95111(a)(12) of the Mandatory Reporting Regulation (MRR), to report the annual amount of electricity sold into CAISO markets (MWh) for which they have a compliance obligation under the Cap-and-Trade Regulation. Utilities must satisfy compliance obligations associated with this reported electricity sold into CAISO markets using compliance instruments other than allocated allowances. CARB assesses compliance with this prohibition on using allocated allowances for compliance obligations associated electricity sold into CAISO markets at the end of each multi-year compliance period.

If a POU or COOP purchased allowances with allocated allowance proceeds prior to April 1, 2019—(an activity that is explicitly prohibited after April 1, 2019)—then the POU or COOP must ensure they are in compliance with the provision that prohibits using these allowances to satisfy any compliance obligation associated with any sales into CAISO markets. CARB may request that POUs and COOPs provide information demonstrating compliance with section 95892(d)(7)(A) for allowances purchased with allowance proceeds pursuant to Health & Safety Code section 38580 and Government Code sections 11180 and 11181.