



MEMORANDUM

TO: California Air Resources Board

FROM: Modesto Irrigation District
Redding Electric Utility
Turlock Irrigation District

SUBJECT: Cap-Setting Comments

DATE: June 2, 2009

Introduction

Modesto Irrigation District (“MID”), Redding Electric Utility (“REU”), and Turlock Irrigation District (“TID”), collectively the “Utilities,” appreciate the opportunity to comment on the issues raised during the cap-setting workshop held on the April 28, 2009.

The cap-and-trade program design must encompass not only setting an appropriate cap trajectory to meet the State goal of reducing Statewide emissions to 427 MMTCO₂E by 2020, but must also include a method for distributing allowances, incorporating flexible compliance measures (such as offsets, early action credits, banking and borrowing), identifying who will participate in the market, establishing enforcement and market oversight mechanisms, and guiding the distribution and use of revenues derived from the market. Such program design details must equitably balance conflicting policy and economic interests of the various economic sectors as well as impacted entities and cost-bearing citizens.

The Utilities

MID, REU and TID are local publicly owned electric utilities. MID and TID are irrigation districts located in the Central Valley and REU is a municipal electric utility within the City of Redding. MID serves over 110,000 electric customers with a peak load around 650 Megawatts (MW). TID serves about 100,000 electric customers with a peak load of approximately 600 MW. REU serves 42,000 customers with a peak load of 247 MW. The Utilities maintain similar resource mixes, including hydroelectric, eligible renewables and fossil fuel sources. They also share similar challenges, including weather patterns, demographics and economics.

The Utilities have consistently supported the goals of AB 32 and participated in CARB's effort to create a successful implementation program. The Utilities continue to urge CARB to move forward in a manner that protects the reliability of the electric grid and maintains the Utilities' efforts to provide reliable and affordable power to their customers.

Cap-Setting Process

The Utilities agree with CARB that the design of the cap level and trajectory should be simple and easy to understand. It is important that the structure of California's cap be equivalent to other entities participating in the Western Climate Initiative (WCI) to reduce the opportunity for gaming, market manipulation, or disproportionate impacts throughout the WCI region.

Capped Sources

The Utilities do not address entities to be included within the cap as the Scoping Plan sets forth the sectors to be covered. However, as new methods for monitoring and measuring emissions are developed, CARB should revisit its determination on which sectors should be included within the cap. If additional sectors are identified for inclusion, adjustments would need to be made to the cap and the trajectory. CARB must also acknowledge that if a long-term viable Offset program is developed for a specific sector, that sector will have the ability to measure its emissions and may eventually need to be included under the cap.

Cap Level & Cap Trajectory

Multi-year compliance periods will be required in order to provide capped entities with the ability to adjust their long-term planning criteria and to manage uncontrollable variables such as weather, the economy and population growth patterns. A three-year compliance period was recommended by the WCI, requiring compliance measures at the end of 2014, 2017 and 2020. Annual cap targets could be set as guidance for capped entities; however, allowances would only be required to be surrendered at the end of the compliance period.

The cap would initially be set at the beginning of the first compliance period in 2012 and would transition to 365 MMTCO_{2e} in 2020, based on the 427 MMTCO_{2e} limit adopted by CARB on December 6, 2007. A trajectory must be established to transition from the 2012 level to the 2020 goal.

Several options have been identified for establishing the initial cap level in 2012. These options can be developed by referencing the forecasted level of emissions based on CARB's business as usual case or the actual measured emissions reported prior to 2012.

The Utilities recommend setting the cap at the average number of actual emissions recorded for 2009 through 2011 based on the verified emissions reports submitted pursuant to CARB's mandatory reporting regulations. By including current emissions levels for setting the cap, early emission reductions will not be recognized, however, they would be rewarded through the use of

early action credits.¹ Thus, the combined approach of setting the cap using an average of current years' emissions and issuing credits for qualified early actions will meet the goals of establishing an accurate starting place for the allowance market and encouraging early emission reductions. A multi-year averaging approach to setting the initial cap would also help smooth out any abnormalities that could result from variations in weather or water availability.

If early action credits are not incorporated into the cap-and-trade system, CARB should assess using business as usual projections for setting the 2012 cap. Although excess allowances may result in the early years using this approach, such impact would be ameliorated over the multi-year compliance period.

In any case, when calculating the initial cap for 2012 for purposes of determining the downward trajectory to the 2020 goal, it is important that all sectors that are included within the 2020 goal be included in the 2012 figures. Thus, every sector that has been given a compliance obligation under the 365 MMTCO₂E goal in 2020 should be factored into the starting level in 2012. If additional sectors are included under the cap after 2012, both the cap at the time of the new entry and the 2020 goal will have to be adjusted accordingly regardless of the trajectory pattern selected by CARB to account for this new entry. It is critical that the introduction of new sectors under the cap after 2012 does not steepen the reduction trajectory for capped sectors with compliance obligations starting in 2012.

Reduction goals for each compliance period can be established by a straight line or multi-tiered trajectory. In a multi-tiered trajectory options include setting a higher cap in the early years with lesser reductions to 2020 or a lower cap in the early years with an accelerated reduction as we near 2020. Under further analysis, the Utilities have concluded that a straight-line trajectory from 2012 to 2020 would result in a multi-tiered trajectory as well. As mentioned above, at a minimum all of the 2012 emissions from the sectors that are designated to be capped in 2020 must be included to set the initial trajectory.

The Utilities urge CARB to adopt a trajectory, or provide for off-ramps, which increases compliance flexibility in the earlier years of the cap-and-trade program to account for delays in resource and transmission development. Regardless of the trajectory path, allowances must be included in the design of the cap level and trajectory at any point in time that a new sector is added to the scope of the cap-and-trade program or to respond to changes in sector emissions caused by electrification or other shifts in responsibility among capped sectors.

The Utilities believe that California's GHG reduction program should be coordinated and adjusted to harmonize with the WCI and/or a federal GHG reduction program so that there is a single system that does not impose multiple layers of compliance complicated by jurisdictional overreach.

¹ The Utilities proposal on "Voluntary Early Action Design" dated March 31, 2009 can be found on the CARB website at <http://www.arb.ca.gov/cc/capandtrade/meetings/031009/mar10pcmidreutid.pdf>.

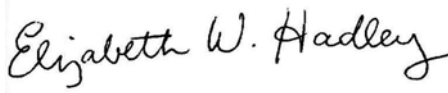
Conclusion

The Utilities appreciate the opportunity to comment on the cap trajectory and welcome the opportunity to discuss this with CARB to develop these concepts further.

Respectfully submitted,



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