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June 19, 2009

**VIA E-MAIL TO  
CCWORKSHOPS@ARB.CA.GOV**

Dr. Kevin Kennedy  
Assistant Executive Officer  
California Air Resources Board  
1001 I Street  
Sacramento, CA 95814

**Re: Pacific Gas and Electric Company's Comments on the California Air Resource Board Staff's Proposed Criteria for Reviewing and Approving Offset Projects and Protocols**

Dear Assistant Executive Officer Kennedy:

Pacific Gas and Electric Company ("PG&E") welcomes the opportunity to provide these preliminary comments in response to the California Air Resources Board (ARB) staff's May 21, 2009 workshop on Criteria for Reviewing and Approving Offset Projects and Protocols. We appreciate ARB's efforts to begin the process for defining eligible categories of offsets and applaud staff's preliminary approach on the matter. In particular, staff's preliminary approach on independent third party verification, monitoring and reporting, and issuance will help establish a rigorous offset market.

Even with those preliminary efforts, PG&E is concerned that an adequate supply of offsets may not be available at the start of a cap and trade program. In order to meet the State's greenhouse gas (GHG) emission reduction goal and do so economically, it is imperative that an offset program is quickly implemented by leveraging existing efforts to adopt or develop high quality protocols that are uniform across regional initiatives or national programs.

**A. Offsets Projects Need To Be Available At The Same Time As Allowances Are Allocated.**

A functional offset program at the start of a cap and trade program will provide complying entities the required information to make investment decisions. In order for there to be sufficient supply of projects to meet the demand from complying entities, project developers need time to get to market and regulatory certainty to make the necessary financial investment.

Through PG&E's experience under its voluntary ClimateSmart™ program, we have found that a significant amount of time is required to initiate a project, have the project independently

verified, and have the verification accepted and offset credits issued. As an example, PG&E recently announced a contract for a livestock methane capture project with California Bioenergy near Bakersfield. California Bioenergy estimates that it will take approximately one year to complete the steps necessary to construct the project. This includes the scoping, surveying, designing, and engineering of the project as well as obtaining the required air,<sup>1/</sup> water, and building permits. Only after the project is complete, can it generate offsets. Verification of the offsets will take place one full year after the project has begun to generate offsets, which California Bioenergy estimates to be in late 2011.

Given long lead times for the development of offset projects, it is imperative that protocols are adopted early in 2010 so that offset projects are available by January 1, 2012, in conjunction with allowance allocation, at the start of the program. Having the offset program in place at the same time as allowance allocation allows flexibility for complying entities to make appropriate investments in a cap and trade system.

**B. Adopt The Best Pre-Existing Protocols And Expedite Development Of New Protocols.**

The current regulatory uncertainty associated with compliance offsets is delaying development of projects. PG&E recommends that the ARB review protocols already established in the offset market, such as the Climate Action Reserve (Reserve), rather than replicating this work. We also encourage ARB to start the development of new offset protocols.

From inception to implementation, protocol development is a lengthy process, taking between 1.5 and 6 years. For example, it took the Reserve 1.5 years from the time work was initiated on the Landfill Project Reporting Protocol to the time of issuance of offsets from a project. That was under the best circumstances. In the case of forestry, it took the Reserve approximately 6 years for the development of the first forest projects. With respect to livestock methane management, the Reserve issued offsets this year from three projects in Idaho, taking approximately three years from the time work was initiated on the protocol. Finally, while the urban forest protocol has been developed, no GHG emission reductions have been issued to date.<sup>2/</sup>

In order to allow the necessary lead time to develop protocols, we suggest that ARB adopt the best of the pre-existing protocols, which have already addressed and resolved questions regarding making offsets real, permanent, additional, verifiable and enforceable. Furthermore, we also encourage ARB to expedite the development of new offset protocols so that additional protocols are available at the start of the cap and trade program.

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<sup>1/</sup> California Bioenergy is working closely with the local air district to permit their project without impacting local air quality.

<sup>2/</sup> Climate Action Reserve database. Downloaded June 16, 2009.

### **C. Maintain Function Of The Market.**

To maintain a fluid market, offset protocols should be uniform across state, regional, or national schemes. We suggest ARB work with regional initiatives as well as the federal government to ensure that the offsets available to meet AB 32 requirements are fully fungible. Given that offset investments are long-term contracts, it is critical for us, as well as project developers, to have certainty that the value of a project is realized over the full life of the project.

### **D. Specific Comments On The Criteria Discussed On May 21<sup>st</sup> Workshop.**

#### Protocol Adoption

PG&E supports the use of offsets that meet rigorous quality standards. Rigorous standards ensure projects are real, permanent, additional, verifiable and enforceable. PG&E supports standards-based protocols, including regulatory and sector-based common practice criteria, which are developed through a transparent and public protocol development process. If a project protocol is not available, PG&E supports the use of project specific tests of regulatory additionality and common practice in order to ensure high quality offsets.

In addition to rigorous standards, PG&E encourages the state to establish broad geographic eligibility of offsets to ensure that: (1) an adequate supply of quality offsets is available; and (2) that California's cap and trade system, including offsets is harmonized with emerging regional and national cap-and-trade markets. Currently, California offset projects make up about 1 percent of the annual GHG emission reductions globally and about 12 percent of the Reserve GHG emission reductions in the United States.<sup>3/</sup> Of the 50 projects listed on the Reserve as of June 16, 2009, only 12 are in California. The majority of the Reserve's Livestock Methane projects (11) and all 27 of the Landfill Methane projects are located outside of California. This underscores the importance of no geographic limits to offsets to ensure sufficient supply.

It is imperative that a sufficient supply of high quality offsets is available to help keep costs to customers manageable, especially in the first compliance period of the program when volatility in the incipient market may be high and prices unpredictable. Of equal importance is linkage with other systems throughout the nation to create a fungible cap-and-trade system that benefits Californians.

Overly complicated and restrictive offset rules in California could limit the development of the market and inhibit emission reduction opportunities that would not have otherwise occurred. If developers find California rules too confusing or inconsistent with regional offset rules or other

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<sup>3/</sup> Ecosystem Marketplace and New Carbon Finance estimates that Reserve reductions account approximately 10 percent of global reductions in "Fortifying the Foundation", State of the Voluntary Carbon Markets 2009 report, released on May 20, 2009. As of June 16, 2009, PointCarbon data shows that California reductions account for 12 percent of Reserve reductions. Therefore, PG&E estimates that California reductions account for 1 percent of the global market (10% x 12% = 1%).

widely recognized protocols, they may not develop projects for the California market that could comply with California protocols. A segmentation of the market rules will mean that developers will have a hard time taking advantage of lessons learned from previous projects or grouping projects for economies of scale, driving up offset costs.

#### Validation

PG&E agrees with ARB staff's conclusion that due to the use of standardized methodologies to quantify emission reductions, validation should not be required.

#### Registration

PG&E supports registration as it allows for an initial screening of projects. However, so as not to hinder the development of eligible projects, the Registration period should have a limited timeframe for approval.

#### Monitoring and Reporting

Monitoring and Reporting requirements necessary to ensure high quality projects should be embedded in the protocols. The verification process itself will then ensure that projects are following the requirements. California should not create separate monitoring or reporting requirements outside of those in the protocols. Rules that are complicated or cumbersome will stifle the creation of projects that can serve the California offset market.

#### Verification

PG&E supports ARB staff's initial assessment that verification must include clear and transparent quantification methods, monitoring, reporting, and documentation requirements. We agree that third-party verification is essential for a rigorous offset program. Different projects require different types of verification. We encourage ARB to accept the Reserve's established verification protocols for use in verifying projects under the Reserves current protocols. For new project protocols, we encourage the ARB to follow the example of the Reserve and develop verification protocols for each project protocol.

#### Certification

PG&E asserts that certification is an unnecessary step given rigorous, standardized, third-party verification requirements. Once emission reductions are independently verified, ARB should review the verification report, approved or reject the report, and, if approved, issue offsets.

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Issuance

PG&E has no comment at this time on the ARB staff thinking about Issuance.

Enforcement

PG&E believes that enforceability can be established through the development of protocols and the independent verification of projects. Using the model developed by the Reserve, project developers would submit their projects along with a verification report from an independent verifier to a central organization such as the Reserve. The ARB would then review the projects and the verification report, accept them if they meet the state's criteria and issue the offsets. If an offset project fails subsequent to ARB approval, those credits should be invalidated and the complying entity that used them for compliance would be required to surrender allowances or purchase other offsets.

Thank you for the opportunity to opportunity to provide these preliminary comments in response to the California Air Resources Board (ARB) Staff's May 21, 2009 workshop on Criteria for Reviewing and Approving Offset Projects and Protocols. Please do not hesitate to contact me at (415) 973-6617 if you have any questions regarding these comments.

Very truly yours,

/s/

John W. Busterud

JWB:kp

cc: via e-mail  
Ms. Lucille Van Ommering  
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