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SoCalGas

A Sempra Energy utility

September 19, 2016

Rajinder Sahota
Chief, Climate Change Program Evaluation Branch
California Air Resources Board
1001 I Street – P.O. Box 2815
Sacramento, CA 95812

Re: SoCalGas Comments on Proposed 2016 Amendments to the Cap-and-Trade Regulations

Dear Ms. Sahota:

On behalf of the Southern California Gas Company (SoCalGas), the following comments are respectfully submitted in response to the California Air Resources Board's (ARB) Proposed Amendments to the Cap-and-Trade Regulations (Proposed Amendments), released on August 2, 2016. Our comments address five issues: 1) Post-2020 annual emissions budgets, 2) allowance consignment requirements, 3) allowance price containment reserve, 4) allowance allocation, and 5) renewable natural gas.

I. POST-2020 ANNUAL EMISSION BUDGETS

- **Support the Proposed Straight-line Emission Budgets from Original 2020 Cap to 2030** – SoCalGas supports ARB's post-2020 emission cap levels as presented in the Proposed Amendments to the Cap-and-Trade Regulations; a linear decline between the established 2020 cap and the calculated 2030 cap level. Maintaining the established 2020 cap level is consistent with the stated goals of AB 32, and the 2008 California Climate Change Scoping Plan: reducing greenhouse gas emissions to 1990 levels by 2020. We agree with the decision to reject the 2020 to 2021 "step-down" that was previously considered, but ultimately not included in the Proposed Amendments. We believe this is the correct decision because it would have resulted in a reduction in allowances that could have led to unintended and unknown ratepayer impacts.

- **Support the Continuation of Linear Emissions Cap from 2031-2050** – The continuation of a linear cap on emissions to 2050 provides a long-term signal to stakeholders. Staff also proposes an equation that would be used to calculate the 2031-2050 annual allowance budgets. These proactive actions support long-term planning and generally contribute to the stability of the emissions market.

II. ALLOWANCE CONSIGNMENT REQUIREMENTS

- **Support Current Consignment Level Increases of 5% per year** – The most recent Initial Statement of Reasons (ISOR) that accompanies the 2016 Proposed Amendments indicates that staff is "evaluating an acceleration of the natural gas supplier consignment requirement" for post-2020 program years. SoCalGas urges ARB to maintain the current 5% annual increase in required allowance consignment levels for natural gas suppliers.

  Alternative consignment levels have already been evaluated. Less than three years ago, California's natural gas utilities and other stakeholders worked together with ARB staff to determine the appropriate consignment rate of allowance allocations under the Cap-and-Trade Regulation. This effort included extensive policy discussions resulting in ARB's decision of starting with a minimum 25% consignment in 2015 and gradually increasing the minimum by 5% per year to 50% in 2020 with the goal of 100% consignment by 2030 (see page 16 of the September 4, 2013 Initial Statement of Reasons-Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms[1] and page 66 of the May 2014 Final Statement of Reasons-Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms[2]). A change in course creates unacceptable uncertainty for the regulated business community. Businesses depend on firm decisions especially those that are agreed upon to extend over time; regulators should take these decisions seriously and alter them only when merited by substantial new evidence and public debate.

  Further, any acceleration of consignment requirements overlooks the documented reasoning for a more gradual transition to a full price signal and is simply unsupported by any new information presented by staff. The original consignment level is an approach that remains sound today. The following points outline reasons why a continuation of 5% annual consignment increase is the most judicious approach:

  1. ARB staff raised the concern of inequity between "covered" and "non-covered" electric generation customers as a reason for accelerating full consignment in the 2016 Proposed Amended ISOR Report (2016 ISOR). The 2016 ISOR states that "non-covered customers of natural gas suppliers are facing a carbon cost that is a fraction of the cost faced by covered entities, creating inequities among covered

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[1] http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isor.pdf

[2] http://www.arb.ca.gov/regact/2013/capandtrade13/ctfsor.pdf

and non-covered entities." This argument is based on a false premise that all non-covered electric generating customers are in direct competition with the covered electric generating customers, and therefore, benefit from a competitive advantage resulting from lower cost fuel. In fact, only a small fraction of non-covered electric generating customers sell into the power market or enter into power agreements with utilities. An acceleration of consignment levels and a hastened cost pass-through will adversely impact ALL non-residential customers, including small businesses, non-profits and other vulnerable customer segments. Staff's hope to level the playing field between covered and non-covered customers will, in actuality, harm all non-residential customers in the effort to target a very small minority of electric generating customers. We feel this is an unbalanced approach. Exacerbating this impact is the fact that natural-gas rate structures typically assign a lower tariff to its largest consumers and vice versa, effectively nullifying any subsidy perceived between non-covered and covered electric generating customers.

2. The idea that full-price pass through more closely aligns the natural gas utilities with the electric distribution utilities' allocations fails to recognize the fundamental difference in the assessment of compliance obligations between natural gas utilities and electric distribution utilities. The compliance obligation is allocated directly to the gas utility based on retail sales, compared to point-of-generation or import in the electric sector. While the State's natural gas suppliers are working to increase the number and volume of natural gas alternatives, supply is still too low to replace conventional natural gas at any significant scale. This necessitates a longer transition period to full rate impact for consumers.

3. The 2016 ISOR claimed that an accelerated consignment will "further the policy desire to limit the amount of fugitive methane emissions," but no evidence is provided to support this assertion. Fugitive emissions from natural gas utilities are emitted along the transmission and distribution systems and at storage facilities. These emission sources are both upstream from end-users and either outside the scope of the Cap-and-Trade Program or occur at facilities that are already directly covered by the Cap-and-Trade Program. Therefore, any perceived cost signal resulting from accelerated consignment would have a negligible impact on reducing emissions as rationalized in the 2016 ISOR. As previously stated in comments to ARB, SoCalGas is supportive of the Short-Lived Climate Pollutant (SLCP) Reduction Strategy's goals and objectives to reduce powerful climate forcing emission sources and putting organic waste to beneficial use as energy feedstocks and soil amendments. We remain supportive of working collaboratively with stakeholders and focusing on efforts that make real impacts on SLCP reductions. An accelerated consignment is not an effective measure to reduce SLCPs and will have an adverse economic impact on our vulnerable small business customers and other core customer segments.

4. Changes to current consignment requirements introduce regulatory uncertainty around procurement activities for all market participants by suggesting that ARB staff may suddenly modify allocation frameworks. The agreed levels of consignment for natural gas suppliers were designed to provide a balanced transition to a full carbon price-signal, mitigate market risk, and manage costs for California's natural gas customers. Altering the rate of consignment, particularly some of the more aggressive options proposed, fails to recognize the time needed to implement carbon reduction activities by both utilities and consumers.

SoCalGas believes it is imperative for ARB to consider cost impacts from the Cap-and-Trade regulation in light of <u>all</u> future customer bill impacts for both natural gas and electricity, and to take into account the totality of bill increases that natural gas customers will be facing, especially low income households and small businesses. This is particularly important given that customers cannot currently distinguish between price increases due to California's greenhouse gas programs and other costs such as those imposed by other regulatory changes.

III. ALLOWANCE PRICE CONTAINMENT RESERVE

- **Recommend Maintaining Three Price Tiers** – SoCalGas is concerned that collapsing the existing three reserve-price tiers to one will increase the chances of extreme price spikes and price volatility in the linked California and Quebec Cap-and-Trade carbon market. The risk for this market behavior is heightened when combined with the proposal to remove surplus unsold allowances from the Auction Holding Account (AHA) and transferring them to the Auction Price Containment Reserve (APCR), starting in 2018. The result could be very costly to compliance entities and damaging to utility ratepayers. The Carbon Market Compliance Association completed an analysis that found as many as 250 million unsold allowances could be transferred from the AHA to the APCR by 2020.

- We are in agreement that transferring unsold allowances to the APCR is a positive change when considered as a stand-alone measure, but could be de-stabilizing to the market when considered with a single-tier framework. SoCalGas also sees the virtue in modifying the pricing mechanism to establish a fixed price difference in real dollars between the Auction Reserve Price and Reserve Sale Price. But, we recommend having at least three tiers of reserves at a certain percentage over the price floor which would allow the market to more smoothly transition to higher prices and would also allow reserve prices to keep pace with inflation while not widening the gap over time as was noted as a concern by ARB.

IV. DIRECT ALLOWANCE ALLOCATION

- **Support a Continuation of Current Cap Adjustments Factors for Allowance Allocation** – While a change to the current allowance allocation adjustment factors was not proposed in the Proposed Amendments, SoCalGas strongly supports a continuation of current methods under the existing Cap-and-Trade Regulation. As intended, the direct allocations have successfully protected against rate impacts to utility ratepayers. A gradual step-down in emission caps coupled with the gradual increase (five percent per year) in consignment requirements is a prudent approach to safely introduce a price signal while ensuring consignment revenue for distribution of Climate Credits to natural gas utility ratepayers.

V. RENEWABLE NATURAL GAS

- **Support Development of the Renewable Natural Gas Market** – In contrast to the electricity sector, renewable natural gas (RNG) is in its early stages of development with limited access to feedstock sources. We urge ARB against artificially raising natural gas costs (such as through accelerated consignment or reduced direct allocation), at the expense of the consumer, in an attempt to encourage more RNG production and distribution. Rather than increasing carbon costs we feel a better return on investment will result from focusing on more policy incentives, capital cost assistance, and streamlining permitting and pipeline interconnection barriers. We support the objectives stated in the 2016 ISOR of transitioning to a more sustainable natural gas sector, and believe targeted policies and incentives that help the RNG industry develop are more productive than broad-brush increases in the cost of natural gas.

Again, SoCalGas thanks you for this opportunity to comment on the Proposed Amendments to the Cap-and-Trade Regulations, and we look forward to additional dialogue as the amendments move forward. Please contact me if you have any questions or concerns about these comments.

Sincerely,

Tim Carmichael

Tim Carmichael
Agency Relations Manager – Energy and Environmental Affairs
SoCalGas