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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 the April 2018 Cap-and-Trade Regulation Workshop

Dear Ms. Sahota:

On behalf of the Southern California Gas Company (SoCalGas), we respectfully submit the following comments in response to the topics discussed at the California Air Resources Board's (ARB) April 26, 2018 Amendments to Cap-and-Trade Regulation Workshop (Workshop). We appreciate the opportunity to provide feedback on potential changes to the regulation as directed by AB 398 and in response to Board Resolution 17-21. SoCalGas submitted written comments with the Gas Utility Group in response to the March 2018 Workshop on Cap-and-Trade Regulation Amendments. As many of the same issues remain, we offer brief comments on the following issues: 1) post-2020 allowance allocation to natural gas utilities, 2) price ceiling, 3) post-2020 reserve tiers, 4) offset limitations and 5) the use of allowance proceeds.

1. POST-2020 ALLOWANCE ALLOCATION TO NATURAL GAS UTILITIES

Allowance allocation for natural gas utilities continues to be an important issue for SoCalGas. Maintaining the current rate of decline for the post-2020 Cap Adjustment Factors (CAFs) is critical to the protection of utility customers.

The proposed post-2020 CAF levels will create a significant rate impact for SoCalGas customers and at the same time reduce the value of climate credits that are planned to be returned to them. For example, we estimate that by 2025 the residential rates will see a 29% increase, or an additional 22 cents-per-therm under the proposed post-2020 CAFs. While the annual climate credit would be *reduced* by approximately $11. Small businesses would see a rate increase of 66% and average monthly bills increasing $64.[1] This is especially financially damaging because the California Public Utilities Commissions (PUC or Commissions) ruled that only residential customers are eligible to receive the California Climate Credit.[2] As such, commercial and industrial customers are relying solely on the CAFs to offer transition assistance and blunt the anticipated steep rise in energy costs.

Furthermore, SoCalGas feels that natural gas utilities face unique challenges that are separate from other industrial sectors. Natural gas use in commercial and industrial applications has largely reached its potential in energy efficiency and has limited opportunities for additional end-use improvement. These consumers are then faced with higher prices without any feasible ways to reduce their demand.[3,4]

Finally, the incremental costs to our customers from the more onerous CAFs is counter-productive to efforts made by SoCalGas and other natural gas utilities, to decarbonize their pipelines through investment and development of the renewable gas market. Unlike the electric sector, which gets recognized for their additional cost burden from the Renewable Portfolio Standard and other mandates, natural gas sector gets no such adjustments. Reducing the allowance allocation further for the natural gas sector only exacerbates such inequities.

In alignment with the BR 17-21 directive, we urge CARB to re-establish the previous allowance allocations for natural gas utilities that has been applied for 2015-2020. This change is critical to protect the most vulnerable utility customers from economic hardship and to gradually introduce cap-and-trade costs as the State strives to meet its ambitious greenhouse gas reduction goals.

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[1]Average residential bill assumed natural gas consumption of 34 therms per month. Average core commercial and industrial bill assumes monthly consumption of 300 therms per month. Allowance prices were derived by taking the average of 4 base case allowance price forecasts from the CEC, CalCarbon, ICIS and Alpha Inception. Forecasted rate impacts are compared against most recent rates for each customer class, effective as of January 1, 2018. The Climate Credit reduction was derived by comparing estimated consignment value with current CAF rate of decline versus the proposed CAF rate of decline and using the aforementioned allowance prices for both scenarios.

[2] Gas GHG OIR final decision D.18-03-017.

[3] California Climate Change Center, *Price Impact on the Demand for Water and Energy in California Residences*, (CEC-500-2009-032-F) (2009).

[4] Bernstein, M.A., Griffin, J., *Regional Differences in the Price-Elasticity of Demand for Energy*, National Renewable Energy Laboratory, (Subcontract Report NREL/SR-620-39512) (2006).

2. PRICE CEILING

SoCalGas appreciates the difficulty with determining an appropriate ceiling price while balancing the various and sometimes divergent objectives of setting this policy. We urge ARB to use the criteria laid out in the AB 398 legislation to guide them, as required by law:

- To avoid adverse impacts on resident households, businesses, and the state's economy.
- To consider the 2020 tier prices of the APCR.
- To consider the social cost of carbon.
- To consider the auction reserve price.
- To minimize economic and environmental leakage.
- The cost per metric ton of greenhouse gas emissions reduction to achieve the statewide emissions targets established in Sections 38550 and 38566.

We recommend that ARB stay focused on the above considerations of the statute and not drift into other objectives and considerations such as internal corporate carbon pricing and other concepts. Furthermore, SoCalGas feels that it is important to use a relevant and defensible price ceiling to protect from threatening the long-term viability and support for the Cap-and-Trade Program within the Western Climate Initiative (WCI) and other jurisdictions with which it might link in the future.

SoCalGas makes the following additional suggestions:

- Staff needs to consider and define what constitutes "adverse impacts on residential households, businesses and the state's economy" as is worded in AB 398. This will allow for stakeholders to propose values that align with the intended purpose of the Price Ceiling.

- Some independent experts have found that in cap-and-trade markets with a finite compliance period and with hard floor and ceiling prices, the equilibrium price will most likely be at the floor or ceiling.[5] This phenomenon should be carefully considered when evaluating potential ceiling prices.

- Staff proposed to move any other remaining Allowance Price Containment Reserve Price (APCR) allowances, after the anticipated 40,611,000, into the Price Ceiling. SoCalGas believes that these allowances would be better utilized in the Post-2020 Reserve Tiers (Reserve Tiers). This strategy will decrease the

[5] "Expecting the Unexpected: Emissions Uncertainty and Environmental Market Design", Severin Borenstein, James Bushnell, Frank A. Wolak, and Matthew Zaragoza-Watkins, Energy Institute at Haas Working Paper 274, August 2016.

chances of market prices reaching the ceiling at all – which we believe is a better outcome and aligns with the intent of AB 398.

We urge Staff to investigate these issues in detail, and we look forward to further dialogue from all stakeholders on the topic.

3. POST-2020 RESERVE TIERS

As acknowledged in Staff's summary of stakeholder input, many take the position that the Reserve Tiers would be more effective if spaced evenly between the floor price and ceiling price, rather than being clustered together near the ceiling. SoCalGas also holds this position. If the Reserve Tiers are placed too close together or too close to the ceiling price we fear they would be ineffective and fail to act as a brake on short-term price spikes as intended by the authors of AB 398.

The Reserve Tier prices presented in the March 2018 Cap-and-Trade Amendments Workshop were too high and seemed to have been derived incorrectly. It appears that Staff used the current program's APCR prices to guide the *lowest* Reserve Tier price. This is contradictory to the direction of AB 398, which requires the *price ceiling* to consider the APCR, not the Reserve Tiers. Doing so skews the pricing structure upward in a way we believe was not intended by the authors of AB 398 and would place the Reserve Tiers too close to any viable Price Ceiling.

In addition to the prices selected for the Reserve Tiers, ARB must allocate allowances to each tier. SoCalGas believes that in order for the Reserve Tiers to be effective they must have sufficient volume. In the Workshop, Staff requested feedback on where the APCR allowances and unsold allowances should be placed. One possible way to help achieve adequate volumes in the Reserve Tiers is to transfer APCR allowances and unsold allowances into the Reserve Tiers. Therefore, SoCalGas recommends that the 52.4 MMT that ARB planned to add to the post-2020 APCR be placed in the post-2020 Reserve Tiers and not the Price Ceiling. Allocating these allowances in the Reserve Tiers would increase the effectiveness of the Reserve Tiers in mitigating rising allowance prices and reduce the risk of hitting the Price Ceiling.

4. OFFSET LIMITATIONS

As with the vast majority of stakeholders who commented on the March Cap-and-Trade Workshop, we support using precise statutory language in the amended regulation for defining Direct Environmental Benefits (DEBs). All projects located in California should automatically meet DEBs standards and out-of-state offset projects can meet the standards by demonstrating they provide environmental benefit to California. Limitations beyond the letter of the law could stifle the offset market when it already faces additional post-2020 restrictions to California-based offsets and the reduced offset usage limits.

Additionally, on this topic, we urge ARB to move quickly in forming the new Compliance Offsets Compliance Protocol Task Force so that more offset protocols that benefit California can be developed and made available to compliance entities.

5. ELIGIBLE USES OF ALLOWANCE PROCEEDS FOR NATURAL GAS UTILITIES

Staff proposed specific language in the March Workshop's Preliminary Discussion Draft that restricts electric and natural gas utilities from using allocated allowance proceeds for activities other than as described. In particular, the additional language proposed in Sec. 95893(d)(3) restricts the use of allowance proceeds to the programs set forth in Sec. 95892(d)(3)(A)-(D) of the electric utility section without providing for natural gas specific measures such as renewable natural gas or near-zero emission vehicles. SoCalGas feels that this language is overly prescriptive and only considers uses applicable to the electric sector. SoCalGas recommends broadening the language to include allowable uses of the funds for any-and-all greenhouse gas reducing strategies and programs, inclusive of procurement of renewable gas and funding renewable gas infrastructure.

SoCalGas appreciates this opportunity to comment on the areas discussed at the Workshop, and we look forward to additional dialogue to ensure utility customers are not only gradually introduced to the rate impacts of the cap-and-trade program, but are protected to the extent possible against volatility in the carbon markets. 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