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Ms. Rajinder Sahota
Assistant Division Chief
Industrial Strategies Division
California Air Resources Board
1001 I Street
Sacramento, California 95812

Re: Pacific Gas and Electric Company’s Comments in Response to the Air Resources Board’s October 12, 2017 Workshop on Next Steps for Amendments to the Cap-and-Trade Regulation

Dear Ms. Sahota:

Pacific Gas and Electric Company (PG&E) appreciates this opportunity to comment in response to the Air Resources Board’s (ARB) October 12, 2017 workshop regarding next steps for updating the Cap-and-Trade Regulation pursuant to Assembly Bill 398 and ARB Board Resolution 17-21. For ease of reading, these comments will refer to the “AB 398 amendments.”

PG&E strongly supports California’s greenhouse gas (GHG) emission reduction goals. PG&E was the first utility to formally support AB 32, and is an active participant in California’s suite of GHG reduction programs, including the Cap-and-Trade Program, the Low Carbon Fuel Standard, and the Renewables Portfolio Standard, among others. In 2016, PG&E’s electric portfolio was nearly 70% carbon free.¹

California’s Cap-and-Trade Program plays a critical role in California’s policy portfolio, serving as a flexible, cost-effective reduction measure that encourages investment in low carbon technologies and provides an environmental backstop to other programs. ARB has documented that the total GHG emissions from covered sources for the Program’s first two-year compliance

¹ [“PG&E Renewable Energy Deliveries Grow; GHG-Free Portfolio Is Nearly 70 Percent.”](#) PG&E News Release. March 16, 2017.

period were significantly lower than the ARB-determined GHG emissions cap,² and California is on track to meet the 2020 target of reducing GHG emissions to 1990 levels.³

AB 398 and BR 17-21 offer an opportunity to further refine this successful and world-leading emissions reduction program to ensure that Cap-and-Trade continues to be an effective and flexible policy tool and an excellent example to other jurisdictions looking to tackle the issue of climate change.

To this end, PG&E presents input that should inform the AB 398 amendment process on the following specific issue areas:

- I. Managing Perceived “Overallocation”
- II. Establishing and Implementing a Price Ceiling
- III. Defending the Environmental Integrity of the Price Ceiling
- IV. Establishing Price Containment Points
- V. Interpreting Offset Credit Limits
- VI. Addressing Banking and Holding Limits
- VII. Supporting Transportation Electrification
- VIII. Revisiting Natural Gas Allocation

I. Managing Perceived “Overallocation”

AB 398 directs ARB to evaluate and address concerns related to overallocation “as appropriate.” Some parties claim that there is an overallocation of allowances in the 2021 to 2030 timeframe, caused by banked pre-2021 allowances being available for post-2020 compliance. Stakeholders often point to the difference between the tons of allowances available before 2021 and the (lower) amount of actual emissions. In short, more allowances will be available by 2021 than will be “needed” for compliance by that time, and holding over the difference could lead to emissions above the cap after 2021.

However, because the Cap-and-Trade Program has been extended through 2030, the Program is not overallocated through 2030 due to the State’s ambitious emission reduction goals. Any analysis of the overallocation issue needs to consider the full scope of the Program, including its full 18 year length (2013-30) and its linkage with Quebec and Ontario. Available analysis (described below) generally projects that allowance demand will exceed supply, including

² Total emissions for 2013-2014 were 291.2 Million Metric Tons (MMT) of carbon dioxide equivalent (CO₂e). The Emissions limit for the same period was 322.5 MMT CO₂e. See the full 2013-2014 compliance report at <https://www.arb.ca.gov/cc/capandtrade/2013-2014compliance/2013-2014compliance.pdf>

³ ARB’s Scoping Plan homepage: <https://www.arb.ca.gov/cc/scopingplan/scopingplan.htm> (See Section “What is the Status of AB 32 implementation”)

banked allowances, before 2030, which indicates that the Program is not overallocated. When demand exceeds supply, prices will increase, perhaps sharply. Permanent removal of allowances from the market restricts supply, bringing forward the date that allowance prices will increase. While cumulative in-state emissions will be lower, compliance costs will be higher. With higher costs, economic and emissions leakage may result, as well as greater negative impacts to household income.

PG&E suggests that ARB examine the analyses on this topic from the University of California Energy Institute (UCEI), Bloomberg New Energy Finance, and ICIS for clear evidence that the Cap-and-Trade Program is not overallocated.⁴

Another important point is that the appearance of overallocation is not a design flaw that needs to be corrected, but an indication of successful GHG policy. The difference between pre-2021 allowance budgets and actual emissions is in part due to California's other GHG programs, which are reducing emissions. These programs also impose costs on California consumers, which should not be compounded by arbitrarily removing allowances from the Cap-and-Trade Program.

Additionally, ARB's program design already dynamically addresses any potential overallocation through its auction reserve price. With this mechanism, allowances are withheld from the regular auctions temporarily (and are permanently moved to the APCR after 24 months) when demand for allowances is low. This mechanism is sufficient to maintain allowance prices above prices that are "too low."

II. Establishing a Price Ceiling

AB 398 directs ARB to establish a price ceiling in accordance with a set of guiding criteria. PG&E strongly supports establishing a price ceiling because it provides certainty that helps compliance entities make prudent, long-term investments in emissions-reducing technologies. Additionally, a price ceiling ensures that allowance prices cannot exceed acceptable levels, above which there is risk of a pause or an end to the Program that would compromise California's emissions reduction efforts.

PG&E is currently examining potential ceiling price levels that would be politically acceptable, provide a meaningful price signal, and help reach statewide GHG targets. One prudent starting place could be in the range of the existing Allowance Price Containment Reserve. Another might be more in line with current estimates of the social cost of carbon.

⁴ UCEI Working Paper 281 (Borenstein, Bushnell) is available publicly. PG&E is happy to work with ARB, BNEF, and ICIS to try and facilitate ARB access to these private analyses consistent with the terms and conditions of BNEF and ICIS.

PG&E looks forward to continued dialogue with staff on appropriate price ceiling levels as the AB 398 amendment process advances.

III. Defending the Environmental Integrity of the Price Ceiling

The Cap-and-Trade Program serves as the environmental bulwark of the state's GHG reduction portfolio, ensuring that even if other measures fail to achieve expected emissions reductions, the state will still not exceed the overall emissions caps. AB 398 directs ARB to maintain environmental integrity by using the proceeds from the sale of price ceiling allowances to procure at least equivalent metric ton reductions outside of the Program.

The sale of allowances at the price ceiling indicates the additional emissions reductions from capped sectors are costly; as such, ARB should have discretion to procure a broad range of instruments and reductions from projects that meet the statutory criteria (additional, verifiable, quantifiable, etc).

Three significant design issues that merit further discussion in this proceeding are how and where ARB would look to achieve the necessary emissions reductions outside of the Program, clarifying which entities may buy at the price ceiling, and determining ARB's interpretation of the "if needed for compliance" condition.

PG&E looks forward to working with ARB through the AB 398 amendment process to design an effective price ceiling that, if triggered, mitigates program costs to California consumers while maintaining the environmental integrity of the Program.

IV. Establishing Price Containment Points

AB 398 directs ARB to establish two price containment points at levels below the price ceiling. PG&E supports the establishment of these "speed bumps" as an opportunity for cost containment on allowances prices that, analysis shows, could rise very quickly post-2020.

The price containment points better serve their purpose if spaced evenly between the floor and ceiling price, rather than clustered together near the ceiling. This would provide an earlier initial opportunity to balance out demand and ameliorate the potential for large price swings, helping maintain Program affordability.

V. Interpreting Offset Usage Limits

AB 398 directs ARB to establish limits for the use of offset credits for compliance. Between 2021 and 2025 the limit is four percent; between 2026 and 2030 the limit is six percent. In either case, no more than half of the total usage limit may be sourced from projects that do not provide "direct environmental benefits in the state."

PG&E has been, and remains, a strong proponent of offsets as real, additional, quantifiable, and verifiable GHG emission reductions. Not only do they provide a benefit to the atmosphere from uncapped sectors like agriculture and forestry, but in some cases these emission reductions can be achieved at lower cost than other GHG emission reductions, reducing the overall cost of the Cap-and-Trade Program and thereby its economic impact on California consumers.

ARB should take a fair and open-minded approach to interpreting the definition of the “direct environmental benefits in the state.” Projects that are not geographically located within the state but that provide clear reduction or avoidance of any pollutant that could have an adverse impact on the air or waters of the state should not be arbitrarily labeled as failing to providing a direct environmental benefit for the purposes of the AB 398 offset limits. Offset projects in neighboring states, for example, likely benefit California air quality and watersheds, which do not strictly stop at state lines.

It is also critically important that ARB clearly indicate, in advance of the fourth compliance period, which projects provide in-state benefits and which do not, as this is necessary for both project developers to supply reductions and for compliance entities to effectively plan for compliance.

Finally, PG&E notes that ARB’s delineation of offset limits as applied to emissions year is helpful and appropriate.⁵ For example, it is accurate that the offset limit for the 2020 emissions year is eight percent of a compliance entities total obligation.

VI. Addressing Banking and Holding Limits

AB 398 directs ARB to establish allowance banking rules that discourage speculation, avoid financial windfalls, and consider the impact on complying entities and volatility in the market.

Current banking rules, which allow use of pre-2021 compliance instruments, including offset credits procured under existing protocols post-2021, should be maintained to support market continuity, to allow compliance entities to adequately plan for their compliance obligations, maintain investment in high quality offset projects, and to avoid potential price volatility and market disruption.

ARB should consider whether changes to the holding limit are necessary now that the Program extends beyond 2020. The extension of the Program creates the opportunity to evaluate whether or not the existing holding limit supports the additional program period.

⁵ [Staff Presentation: “Cap-and-Trade Regulation Workshop.” October 12, 2017. Air Resources Board. Slide 25.](#)

VII. Supporting Transportation Electrification

A key element for reaching the State's 2030 GHG reduction goals is the decarbonization of the transportation sector, facilitated by use of alternative fuel vehicles. PG&E looks forward to working with staff to evaluate methods to quantify transportation-related load growth and accordingly augment electrical distribution utility allocation to ensure that Californians are incented to further adopt and rely on alternative fuels for their transportation needs, and guarantee that the costs of this transition are distributed equitably.

VIII. Natural Gas Allocation

BR 17-21 directs ARB to work with natural gas utilities to ensure adequate customer protection as the state pursues strategies to decarbonize the natural gas system. Natural gas remains an important alternative fuel in both the electric and transportation sectors as the state continues to decarbonize, and PG&E looks forward to working with staff on this issue as part of the AB 398 amendment process.

Conclusion

PG&E continues to support Cap-and-Trade as a program that will help the state meet its aggressive environmental goals while maintaining a healthy economy. We look forward to working with ARB staff to further refine the Regulation in line with AB 398 and BR 17-21.

Sincerely,

/s/

Nathan Bengtsson
Senior Representative
Pacific Gas and Electric Company