Pacific Gas and Electric Company

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April 28, 2017

Mr. Richard Corey
Executive Officer
California Air Resources Board
1001 I Street
Sacramento, California 95812

Re: Pacific Gas and Electric Company's Comments on the Air Resources Board's April 2017 15-Day Amendment Text for the Cap-and-Trade Regulation

Dear Mr. Corey,

Pacific Gas and Electric Company (PG&E) appreciates this opportunity to comment on the Air Resources Board's (ARB's) second 15-Day Amendment package for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms (Cap-and-Trade) Regulation, released April 13, 2017 (April changes or April 15-day package).

PG&E supports ARB's continued efforts to develop and improve the Cap-and-Trade Regulation in pursuit of the Senate Bill 32 (SB 32) greenhouse gas (GHG) reduction target of 40 percent below 1990 levels by 2030. By making prudent adjustments to Cap-and-Trade, ARB can help ensure that California meets its aggressive GHG emissions reductions goals beyond 2020 while maintaining a vibrant economy.

Before addressing the April changes, PG&E notes support for ARB's Assembly Bill 197 (AB 197) analysis and agrees with ARB's conclusions. In particular, we agree that ARB has considered the social cost of GHG emissions by estimating the avoided damages from the policy using the U.S. Government's Interagency Working Group of the Social Cost of Greenhouse Gases Social Cost of Carbon. We also agree that the proposed Cap-and-Trade Program design, including gradually declining caps on GHG emissions and a quantitative usage limit on offsets, will result in direct emissions reductions at covered entities including large stationary sources.

PG&E has previously commented extensively on the proposed amendments to the Cap-and-Trade Regulation.[1][2][3] The following comments address topics specific to the April 15-day package, namely:

I. **Electric Allowance Allocation** – PG&E supports ARB's proposed modifications to Section 95892 regarding allowance allocation to electric distribution utilities (EDUs) for protection of electricity ratepayers.

II. **Gas Allowance Allocation –** PG&E appreciates ARB's proposal to maintain the current consignment scheme for natural gas suppliers (NGS), but recommends ARB continue to explore options to modify the cap adjustment factor for NGS to protect customers while opportunities to decarbonize the natural gas system continue to mature.

III. **Market Design Considerations** – PG&E discusses a number of changes related to the limited exemption from the holding limit, Allowance Price Containment Reserve (APCR), offsets.

IV. **California Independent System Operator (CAISO) Energy Imbalance Market (EIM) Considerations -** PG&E supports the changes to Section 95852 reinstating the resource shuffling exemption.

I. SECTION 95892. ELECTRIC ALLOWANCE ALLOCATION

PG&E supports ARB's proposed modifications to Section 95892 regarding allowance allocation to EDUs for protection of electricity ratepayers. In particular, PG&E supports the removal of the cap adjustment factor from the post-2020 EDU allocation calculations in recognition of the significant GHG reductions expected from EDUs that are already factored into ARB's allocation calculations. In addition, PG&E supports ARB's proposed change to the Renewables Portfolio Standard (RPS) calculation in the EDU allocation spreadsheet to recognize that bucket 2 RPS resources may not be zero-emission resources from a climate policy cost burden perspective. Also, PG&E supports ARB's proposed recognition of Diablo Canyon's 2024 and 2025 license expiration dates in the EDU allocation calculations through prorating assumed nuclear generation in 2025. As modified, the proposed allowance allocations effectively mitigate expected climate policy compliance costs to electricity customers. PG&E looks forward to continuing to work with ARB in a future rulemaking

[1] Pacific Gas and Electric Company. "Re: Pacific Gas and Electric Company's Comments on the Air Resources Board's Proposed Amendments to the Cap-and-Trade Regulation." Sept. 19, 2016. https://www.arb.ca.gov/lists/com-attach/51-capandtrade16-VSVQMVQKU2VVDFQ3.pdf
[2] Pacific Gas and Electric Company. "Re: Pacific Gas and Electric Company's Comments on the Air Resources Board's Proposed Modifications to the 2016 Cap-and-Trade Amendments." Nov. 4, 2016. https://www.arb.ca.gov/lists/com-attach/57-ct-amendments-ws-VyddPFMNUmRWDwRn.pdf
[3] Pacific Gas and Electric Company, "Re: Pacific Gas and Electric Company's Comments on the Air Resources Board's Proposed Amendments to the Cap-and-Trade Regulation 15-Day Amendment Text." January 20, 2017. https://www.arb.ca.gov/lists/com-attach/165-capandtrade16-AHACY1M3VloAZQRr.pdf

to establish an additional allowance allocation mechanism to address increased load from electrification.

II. SECTION 95983. GAS ALLOWANCE ALLOCATION

PG&E supports allocating free allowances to protect ratepayers from rising GHG costs and to offer transition assistance that gradually introduces a price signal across all portions of California's economy in the coming years. To this end, PG&E appreciates ARB's April changes to maintain the current rate of consignment for natural gas suppliers at a five percent annual increase reaching 100% in 2030.

However, the proposed amendments will effectively double the cap adjustment factor (CAF) for the natural gas sector from approximately two to four percent per year. PG&E maintains that a lower post-2020 CAF for the sector is appropriate for a number of reasons.

For one, natural gas suppliers currently have limited near-term opportunities to lower compliance costs through the procurement of renewable or low carbon natural gas (RNG). PG&E supports the goal of transitioning the natural gas sector to a more sustainable future through increased deliveries of RNG, and providing natural gas customers a lower cap adjustment factor will allow natural gas suppliers time to ramp up development and procurement opportunities in the nascent RNG market. While the state's natural gas suppliers are working to increase deliveries of RNG and the dairy pilot projects required by Senate Bill 1383 will help spur project development, supply is still too uncertain to replace conventional natural gas at any significant scale. In contrast to the broad availability of renewable electricity, the potential supply of RNG is still limited, and is relatively expensive as a GHG abatement opportunity. The cost of developing the RNG market will be reflected in retail gas rates, and a steep increase in the cap adjustment factor will exacerbate those rate increases.

Additionally, ARB's reasoning for increasing the CAF to four percent per year relies on the hypothesis that customers facing direct carbon prices will be incented to reduce consumption or utilize alternatives to natural gas. PG&E believes that increasing rates and net costs is not an effective lever to increase conservation or energy efficiency. Historically, natural gas demand from residential, small commercial and small industrial customers has not been highly responsive to retail price signals. Direct incentives for promoting efficiency or conservation may work more effectively.

For these reasons, PG&E recommends ARB continue the dialogue with natural gas suppliers to provide a post-2020 allocation that strikes the appropriate balance between incenting GHG reduction and protecting natural gas customers.

III. MARKET DESIGN CONSIDERATIONS

A. Section 95920. Limited Exemption from the Holding Limit

The April 2017 changes to Section 95920 regarding the limited exemption from the holding limit (limited exemption) represent a significant departure from the previous calculation method. Under the current regulation, calculation of the limited exemption is rooted in emissions from base years at the start of the Cap-and-Trade Program. Many entities in the electric sector have significantly reduced their emissions since those base years, in line with California's GHG reduction policies like the RPS. The new methodology which relies on emissions from more recent years will likely result in a decreased limited exemption for some entities that have made progress toward reducing their emissions.

PG&E has consistently advocated that covered entities with large obligations should be provided additional flexibility to engage in legitimate hedging activities and/or plan for post-2020 compliance. ARB's modifications to Section 95920 frustrate this goal. ARB should provide an opportunity for compliance entities that may need to rebalance their portfolios given the more restrictive limited exemption calculation to receive an exemption from the newer, lower limit. Compliance entities developed portfolio management strategies consistent with the current regulation and should not be subject to holding limits violations due to new regulatory changes. Accordingly, PG&E recommends that ARB provide covered entities an exemption from the new effectively lower holding limit so that covered entities may reallocate existing portfolios in line with the proposed changes.

B. Section 95913. Sale of Allowances from the Allowance Price Containment Reserve

PG&E supports ARB's proposed modification regarding the calculation of the 2021 APCR value; we agree that calculating the fixed dollar amount in 2020 rather than establishing its dollar value in this rulemaking provides certainty in the cost of APCR allowances.

However, establishing the fixed dollar amount based on the 3rd tier of the 2020 APCR results in too high a fixed increment and too high a post-2020 APCR price to provide sustainable cost containment. This issue is increasingly important as the rate of cap decline doubles post-2020 to achieve deeper reductions. In order to provide more meaningful cost-containment in the post-2020 program, PG&E encourages ARB to consider a lower fixed dollar amount above the floor price; specifically, we encourage ARB to adopt a fixed dollar amount tied to the 1st tier of the APCR instead of the 3rd tier APCR.

In addition to providing more effective cost-containment, a smaller step between the auction floor price and the APCR price reduces the incentive to manipulate the market to raise prices.

C. Section 95895. Invalidation of Offset Credits

PG&E supports the change in Section 95895 regarding the replacement of Forest Buffer Account offset credits. We concur that, instead of a default 50% buffer account credit replacement in the event of invalidation, the calculation of credits in the buffer account that need to be replaced be done on a project by project basis, based on the total percentage of buffer account credits that have been retired to compensate for reversals up to the date of the invalidation.

IV. SECTION 95852. RESOURCE SHUFFLING/EIM CONSIDERATIONS

PG&E supports ARB's change to Section 95852(b)(1)(B) to clarify that CAISO EIM transactions do not constitute resource shuffling. We agree that the interim measure proposed in the ARB's December 2016 15-day notice package and the permanent measures being discussed in the CAISO Regional GHG Initiative will address ARB concerns about assigning GHG obligations for "leakage" emissions. PG&E expects that the ARB and CAISO will achieve their objective of accurately accounting for these EIM emissions. PG&E fully supports clarifying that the results of the CAISO dispatch model do not constitute resource shuffling. This change helps avoid a potential dampening of EIM participation.

V. CONCLUSION

In 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. PG&E hopes that the ARB will seriously consider the suggestions made herein, and looks forward to continuing to collaborate on the Program through 2030.

Sincerely,

/s/

Nathan Bengtsson
Senior Representative
Pacific Gas and Electric Company

Cc:
Edie Chang
Steve Cliff
Rajinder Sahota
Mary Jane Coombs
Jason Gray
Michael Gibbs