THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Executive Office

ELECTRONIC SUBMITTAL

April 3, 2014

Clerk of the Board
Air Resources Board
1001 I Street
Sacramento, CA 95814

Re: Air Resources Board's Notice of Public Availability of Modified Text and Availability of Additional Documents and Information (15-Day Notice) on Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms

The Metropolitan Water District of Southern California (Metropolitan) has reviewed the March 21, 2014, Proposed 15-Day Modifications (Proposed Modifications) to the September 4, 2013, Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms and provides the following comments on modifications to Section 95895.

Background

Starting with the release of the Cap-and-Trade Preliminary Draft Regulation in November 2009, Metropolitan has actively participated in the California Air Resources Board's (CARB) rule-making process for the sole purpose of protecting Metropolitan's customers from the adverse financial impacts of the Cap-and-Trade program. Metropolitan has submitted numerous written comments and has provided oral testimony to CARB. At multiple meetings, CARB members have noted that the water sector has been overlooked in the drafting of the Cap-and-Trade Regulation. They have directed staff in several resolutions to continue working with the water sector to adequately address its legitimate and unique issues, and to resolve its inequitable treatment under the Cap-and-Trade Regulation. However, despite numerous meetings and an extensive exchange of information, CARB staff has not successfully resolved the concerns of the Public Wholesale Water Agencies. Metropolitan appreciates the effort that CARB staff has put into formulating an allocation of allowances for Metropolitan, and the slight increase in the proposed allocation in this most recent revision. However, the Proposed Modifications must be further revised in order to, once and for all, provide a fair and equitable allocation of allowances to Metropolitan that will provide satisfactory mitigation for the cost burdens unquestionably imposed by the Cap-and-Trade regulations.

Metropolitan is responsible for acquiring the wholesale energy needed to operate its pumps on the Colorado River Aqueduct (CRA). For the entirety of its 80+ year existence, Metropolitan has relied heavily on non-Greenhouse Gas (GHG) emitting hydroelectric energy for its CRA load. Today, Metropolitan meets over 70% of the average CRA electrical pumping load with federal hydroelectric energy from the Hoover and Parker Dam Power Plants. In some years with lower CRA pumping loads, federal hydroelectric energy satisfies the entire CRA demand. Unlike the energy requirements of a retail serving electric utility (or Electric Distribution Utility (EDU)), the annual CRA pumping load can vary significantly from one year to the next, in large part, due to the changing availability of water from the State Water Project (SWP). During years of normal to high SWP allocations, Metropolitan pumps less water on the CRA, while during minimal SWP allocation years, Metropolitan needs to greatly increase the pumping of Colorado River water. During years of heavy CRA pumping, Metropolitan will obtain and import into California, supplemental energy to meet the increased CRA electric load. This will result in an obligation under Cap-and-Trade regulations to acquire and surrender allowances.

This year, 2014, illustrates the strong relationship between the availability of water from the SWP and the energy requirements of the CRA. Due to the severity of the current drought, Metropolitan will receive a zero allocation of water from the SWP in 2014. This lack of water from the SWP will require Metropolitan to operate the CRA at peak capacity and load from March through the end of the year to meet the water demands of southern California. If the drought continues into 2015, the CRA will continue to operate at peak capacity and Metropolitan will continue to acquire supplemental energy.

Comments on Allowance Allocation Methodology

As stated in previous comments and during meetings with CARB members and staff, Metropolitan is not an EDU and as such does not fall under the Renewable Portfolio Standard (RPS) requirement. To incorporate the EDU RPS requirement in the methodology to determine an allocation of allowances for Metropolitan is not appropriate. The characteristics of the electrical energy requirements of Public Wholesale Water Agencies are unique and different from those of EDUs. As such, the determination of allowances for Public Wholesale Water Agencies should take that into account.

CARB has inappropriately applied the standard EDU RPS requirement percentages (increasing from 21% in 2013 to 33% in 2020) to Metropolitan, and, in particular, applied them against Metropolitan's total CRA electrical load. This results in an allocation of allowances that not only fails to provide sufficient mitigation of Metropolitan's cost burden, but also, perversely, penalizes Metropolitan for having acquired such a large amount of GHG emissions-free resources. This is apparent from the results of CARB's calculations in Table 9-5 of the Proposed Modifications. In years 2019 and 2020 Metropolitan's allowance allocation would have been zero (or actually negative) except for the use of an Energy Efficiency Credit of 3,908 allowances. These values are the result of applying an increasing RPS percentage, up to 33%, to the entire CRA load when, on average, 70% of the load is already met with hydroelectric power and in some years the entire load is satisfied with hydroelectric power. The implication of such results is that Metropolitan must acquire renewable energy resources that will typically be surplus to its needs, requiring it to dispose of the surplus renewable energy or energy from its hydroelectric resources. This is not a reasonable or desirable outcome and shows the inappropriateness of using the standard EDU RPS requirement in the methodology to determine an allocation of allowances for the Public Wholesale Water Agencies.

In essence, the methodology in the Proposed Modifications fails to adequately address Metropolitan's cost burdens because it emulates the allowance allocation methodology used for the EDUs only with respect to the ***reduction*** of allowance allocations. Since the EDUs are required to meet the RPS requirements, a reduction in allowances commensurate with meeting these standards is logical and fair. Such a reduction is consistent with mitigating actual Cap-and-Trade customer costs since the costs of RPS compliance to the EDUs' customers are independent from the costs of Cap-and-Trade compliance.

Now CARB has decided to provide free allowances to the Public Wholesale Water Agencies to offset some of their direct costs of purchasing allowances. However, CARB's methodology to determine the amount of allowances uses the same process of reducing the allowances by incorporating the EDU's RPS requirement. By reducing the Public Wholesale Water Agencies' allowance allocation based on a requirement applicable only to EDUs, the Proposed Modifications do not mitigate the water agencies actual direct compliance costs in the same manner that the original Cap-and-Trade regulations mitigate the EDUs' actual costs to customers. This lack of cost mitigation will be especially onerous given the additional drought related costs Metropolitan is currently experiencing.

<u>Recommended Allocation Approach</u>

Metropolitan does recognize CARB's desire to incentivize the acquisition of renewable energy. If CARB determines that it must apply standard RPS percentages to Metropolitan's allowance allocation, a more appropriate and equitable method would be to apply the RPS percentages on the average amount of supplemental energy Metropolitan uses on the CRA. This approach is consistent with the comments of CARB Member De La Torre at the October 25, 2013, CARB meeting:

> "And to me, it's pretty clear that hydro by definition is not polluting. So that should not be included in whatever formula, whatever mechanism that we use….I think the hydro component should be subtracted from whatever it is that we're asking them to do to mitigate….whatever metric you want to choose that's a reasonable number for how much hydro they've gotten over the last several years on a going forward basis they should not have to offset that or mitigate that." Tr. at 178-79.

This recommended approach uses the same process as CARB's original calculations and bases the increasing annual amount of renewable energy on the average supplemental energy Metropolitan uses, as CARB Member de la Torre suggests, instead of the total CRA demand. Using this approach, the following table provides the annual allocation of allowances for Metropolitan that should be used in lieu of Table 9-5 in the Proposed Modifications:

Table 9-5: Allocation to Each Public Wholesale Water Agency

Annual Allocation

	2015	2016	2017	2018	2019	2020
Metropolitan Water District	496,268	153,110	148,256	154,387	147,019	139,993

In response to Metropolitan's comments and the direction provided by CARB members at the October 25, 2013 meeting and in Resolution 13-44, CARB staff has attempted to address Metropolitan's concerns by marginally increasing the allowance allocation in the Proposed Modifications for year 2015 from 136,491 to 182,499. The increase is appreciated; but it is inadequate in addressing Metropolitan's cost burden. The recommended methodology proposed above will, however, satisfy the goals of both CARB and Metropolitan, by both incentivizing the acquisition of renewable energy and mitigating Metropolitan's cost burden for Cap-and-Trade compliance. This will be accomplished by applying the same general methodology CARB has used for other entities while making appropriate modifications for Metropolitan's unique characteristics, so it is a fair and reasonable approach for CARB to adopt. Metropolitan believes that regulations and legislation which provide for accommodations for unique and special circumstances, particularly regarding public agencies with large amounts of hydroelectric resources, have been developed in the past and should be applied in this situation.

Thank you for your consideration of Metropolitan's comments on the Proposed Modifications.

Sincerely,

Jeffrey Kightlinger
General Manager