



Joint Gas Utility Comments

Regarding Proposed Amendments to §95893—Allocation to Natural Gas Suppliers for Protection of Natural Gas Ratepayers

October 24-25, 2013 Air Resources Board Meeting Item

I. Introduction

These comments are submitted jointly on behalf of investor owned natural gas local distribution utilities (IOUs) Southern California Gas Company (SoCalGas), Pacific Gas and Electric Company (PG&E), San Diego Gas & Electric, Southwest Gas Corporation, and publicly owned natural gas local distribution utilities (POUs) serving the Cities of Palo Alto, Long Beach, and Vernon (referred to collectively as the “natural gas utilities” or “Utilities”). The comments address the California Air Resources Board (ARB) proposed amendments to Article 5, Section 95893, “Allocation to Natural Gas Suppliers for Protection of Natural Gas Ratepayers,” to be considered by the Air Resources Board at the scheduled board meeting on October 25, 2013.

The Utilities appreciate both the opportunity to file comments on the proposed amendments, as well as the transparent and constructive process managed by ARB leadership and staff. The Utilities support the addition of Section 95893 which relates to the allocation of allowances to natural gas suppliers on behalf of their customers. The proposal provides a fair allocation to natural gas suppliers, on behalf of their customers, with a balanced approach to the consignment of allocated allowances. In addition, the Utilities support the proposal to use 2011 as the baseline year for the initial allocation of allowances. We appreciate ARB staff’s effort to address our concerns through its recommended change to the baseline year. The utilities also strongly support the Air Resources Board’s efforts to develop new offset protocols to increase offset supply and provide cost containment benefits.

In the discussion below, the Utilities provide comment on specific aspects of Section 95893 of the proposed regulation for your consideration.

II. Discussion

Section 95890(f): Eligibility Requirements for Natural Gas Suppliers – Potential for Withholding Allowances.

The proposed Section 95890(f) appears to permit ARB to withhold allowances from natural gas suppliers that fail to comply with the MRR regulations and would thereby potentially impose a “double” penalty on natural gas suppliers and their customers over and above the significant daily penalties already authorized under section 95107 of the MRR. Such allowance withholding also discriminates against entities that receive direct

allocations by punishing these entities and not parties that have purchased allowances or are subject only to the reporting obligation and associated penalties.

The proposed Section 95890(f) could also potentially allow ARB to withhold significant quantities of allowances without any showing of wrongdoing by the natural gas supplier and would not limit the amount of allowances withheld to the alleged under-reporting. ARB should not be permitted to withhold allowances in excess of those attributable to the non-compliant report.

To resolve these issues, the Utilities propose the following changes to section 95890(f):

Section 95890(f) A natural gas supplier that is a covered entity shall be eligible for direct allocation of California GHG allowances if it has complied with the requirements of the MRR by obtaining ~~and has obtained a~~ positive or qualified positive emissions data verification statements for its individual GHG MRR report in accordance with section 95103(f) and section 95103(l) for the prior year pursuant to the MRR. If a natural gas supplier submits an inaccurate data verification statement for its individual GHG MRR report, ARB may withhold direct allocation of allowances up to an amount equal to the unverified tons within the Assigned Emission Level for the non-compliant report until such time as the natural gas supplier has obtained a positive or qualified positive emissions data verification statement regarding the non-compliant report.

Finally, if the withholding provision is intended to operate as a forfeiture of allowances, we request that ARB clarify how allowances withheld under section 95890(f) would be recirculated back into the marketplace to avoid a sudden increase in the cost of compliance instruments that could be caused by the forfeiture of a large quantity of allowances.

§95893(d) (3)—Limitations on the Use of Auction Proceeds and Allowance Value

This new section proposes that any revenue return to ratepayers must be accomplished in a non-volumetric manner. The CPUC has exclusive jurisdiction over investor-owned utility ratemaking under Article XII of the California Constitution. Likewise, the governing boards of publicly owned utilities have jurisdiction over POU retail rate design. The natural gas utilities suggest that 95893(d)(3) be modified to parallel the electric utility language in 95892(d)(1) and 95892(d)(2) to avoid jurisdictional conflicts with other state and local agencies and request the following changes to section 95893(d) (3):

Auction proceeds and allowance value obtained by a natural gas supplier shall be used exclusively for the benefit of retail ratepayers of each natural gas supplier, consistent with the goals of AB 32, and may not be used for the benefit of entities or persons other than such ratepayers. ~~Any revenue returned to ratepayers must be done in a non-volumetric manner.~~

A. Appendix A: Proposed Compliance Offset Protocol for Mine Methane Capture Projects

The Utilities support the adoption of additional protocols to provide an adequate supply of offset credits to the Cap-and-Trade market. The use of high-quality offset credits is an effective cost-containment tool and an essential component of a successful Cap-and-Trade program; however without adequate supply, the cost-containment benefit of offset credits will not be fully realized.

Offset credit supply is expected to play an even larger role in cost-containment, with the forthcoming linkage of California and Quebec's cap-and-trade programs. One of the Utilities, PG&E, conducted an analysis and found that compliance costs are forecasted to be higher if offset credit supply in California and Quebec is lower. At the same time, several analyses, including PG&E's, indicate that a supply of offset credits equivalent to the 8%

Quantitative Usage Limit will not be available in Compliance Periods 2 and 3 unless additional protocols are adopted. Therefore, the Utilities urge ARB to approve the proposed Mine Methane Capture (MMC) and forthcoming Rice Cultivation protocols, which will pave the way for additional offset credit supply.

Approval of the Mine Methane Capture (MMC) protocol is important because it can facilitate the generation of a significant supply of offset credits. While estimates vary, MMC projects have the potential to reduce tens of millions of tons of CO₂e from mines whose methane would otherwise be released to the atmosphere. With regard to leakage, ARB, CAR, and EPA analyses^[1] note that revenues from coal mining are sufficient to incentivize mine drainage, that mine ventilation is already required by U.S. regulation, and that methane recovery and destruction does not typically take place when it is not economic to do so. U.S. MMC projects can generate emission reductions without leakage and also meet ARB's criteria of being real, additional, quantifiable, permanent, verifiable, and enforceable.

While the Rice Cultivation protocol is not expected to support the generation of a significant volume of offset credits, its continued development and ultimate approval are important to the adoption of additional agricultural protocols by ARB. Agriculture is a major industry in California and reducing GHG emissions from this sector is important in helping the state meet its longer-term GHG reduction goals.

Additionally, the Utilities fully support staff in their efforts to review protocols, and look forward to opportunities for collaboration. For example, the ozone-depleting substances (ODS) destruction protocol was originally developed in 2009. Since then, baseline scenarios have changed for both refrigerants and foam blowing agents, which should be reflected in a revised protocol. The livestock protocol should also be revised to take into account more recent data. Revisions to these protocols in particular are important to ensure technical accuracy, program integrity, and the maximization of supply from existing protocols.

III. Conclusion

Thank you for the opportunity to comment on the proposed rule regarding allowance allocation to natural gas suppliers and the general provisions for direction allocation. The Utilities appreciate ARB's collaborative and transparent approach. Generally, the Utilities support the proposed new rules, with the exceptions noted above.

Overall, the draft rules provide for a balanced allocation formula to the natural gas suppliers, on behalf of their customers. Through the proposed allocation formula contained in section 95893, there will be a framework to develop a phased, balanced price signal. This will both help manage AB 32 customer costs as well as contribute to achieving the statewide greenhouse gas reductions goals. Furthermore, the proposed changes described above will help clarify the regulations and mitigate undue costs for natural gas customers. We look forward to working with ARB toward the continued success of California's Cap-and-Trade program.

[1] See ARB 8/19/2013 Workshop Presentation on Discussion of Potential New Compliance Offset Protocols:
http://www.arb.ca.gov/cc/capandtrade/meetings/081913/offset_workshop_presentation.pdf

See CAR Coal Mine Methane Project Protocol FAQs:

<http://www.climateactionreserve.org/how/protocols/coal-mine-methane/faq/>

See EPA Coalbed Methane Outreach Program FAQs:

<http://www.epa.gov/cmop/faq.html#eight>