November 4, 2016

Ms. Rajinder Sahota
Climate Change Program Planning and Management Branch
California Air Resources Board
1001 I Street
Sacramento, California 95812

Re: Gas Utility Group (GUG) Comments on the California's Air Resources Board's (ARB) Cap-and-Trade Regulation Amendments Workshop on October 21, 2016

Dear Ms. Sahota:

These comments are respectfully submitted jointly on behalf of investor owned, natural-gas distribution utilities (IOUs): Pacific Gas and Electric Company (PG&E), Southern California Gas Company (SoCalGas), San Diego Gas & Electric (SDG&E), Southwest Gas Corporation (Southwest Gas), and publicly-owned natural gas distribution utilities (POUs): serving the Cities of Long Beach and Vernon. All of the above utilities are referred to collectively as the "GUG" or "Utilities". The Utilities appreciate this opportunity to comment on the Air Resources Board's (ARB's) Cap-and-Trade Regulation Amendments Workshop (Workshop) that was held on October 21, 2016.

The GUG wants to differentiate natural gas from electricity and make the case for the separate treatment of natural gas in ARB's Cap-and-Trade Regulation Amendments. Natural gas is a primary fuel, whereas electricity is a versatile, high quality power source. Natural gas is directly delivered to customers and used predominantly to combust and produce heat. Electricity is used for a variety of purposes: lighting, electronics, controls, process equipment, refrigeration, heating and air conditioning, etc. There are numerous opportunities for decarbonizing the electricity that powers these multiple end uses, while natural gas decarbonization opportunities are quite limited at this time.

Separate treatment of natural gas in ARB's Cap-and-Trade Regulation Amendments would help bring consistency to the regulatory treatment of natural gas customers in California. While Staff's presentation at the Workshop proposed sending strong price signals to customers by raising the cost of natural gas for use in clean burning heating devices, the ARB is also working with local and regional air districts to provide monetary incentives to replace wood-burning heating devices with natural gas models. For example, the San Joaquin Valley Air Pollution Control District's 'Burn Cleaner' program has spent millions of dollars in the last decade to replace wood-burning devices due to their large contribution to fine particulate pollution. We believe it is counter-productive to the goals of reducing pollution emissions and improving air quality if customers shift to heating models that will be more expensive to operate due to natural gas price increases, especially if natural gas prices reach a level of unaffordability that prompts residents to revert to wood burning.

The natural gas sector needs more time for the development of renewable and more efficient alternatives. Therefore, the GUG makes the following recommendations to continue a gradual phase-in of compliance costs for natural gas customers.

The GUG Opposes an Accelerated Allowance Consignment Schedule

The existing Cap-and-Trade Regulation sets forth a minimum consignment of natural gas suppliers' allocation of allowances that began at 25% in 2015 and increases by 5% per year, so that full consignment will be achieved by 2030.

At the Workshop, Staff proposed the much more aggressive schedule of 100% consignment beginning in 2021. Currently, allowances that are not consigned to auction may be retired to meet a natural gas supplier's compliance obligation, which minimizes the impact of Cap-and-Trade costs on customer rates. This approach helps transition the cost of greenhouse gas reduction into natural gas rates to avoid rate shock. Moving to full consignment so precipitously would represent a dramatic departure from current regulations and would create significant cost impacts to natural gas customers.

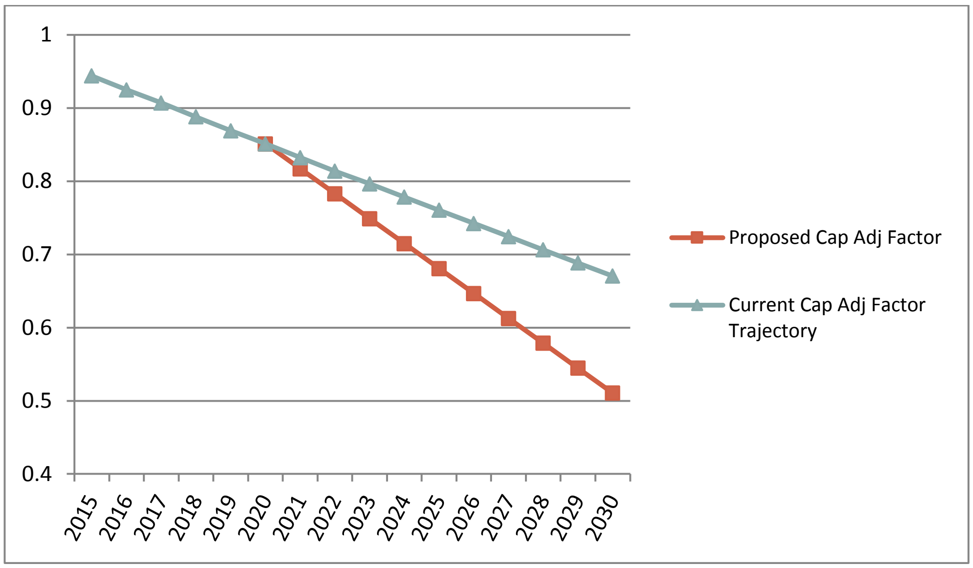
The GUG worked closely with ARB in 2013 and 2014 to develop the current consignment percentages. ARB's proposal to accelerate the rate of consignment overlooks the documented reasoning for a more gradual transition to a full price signal and in the absence of any new information, does not justify a shift away from the gradual transition that was agreed to by the stakeholders when natural gas was originally came under the cap-and-trade program.

The GUG urges ARB to continue with the consignment rate that was previously agreed upon as the most effective way to continue to reduce greenhouse gas emissions while steadily increasing costs for California businesses and customers.

The GUG Supports Maintaining the Current Cap Adjustment Factor (CAF) for 2021-2030

The GUG believes that it is appropriate for ARB to apply the same cap adjustment factor for 2021-2030 that has been applied for 2015-2020. This lower CAF for natural gas customers is appropriate to maintain because they do not have the same broad suite of efficiency options as electric customers have. Opportunities to reduce natural gas usage are considerably fewer and unlike the electric sector where there is a range of zero-greenhouse gas sources available for electric distribution utilities, natural gas suppliers currently have scant opportunity to procure renewable natural gas (RNG).

The proposed CAFs, as presented on slide 47 of the Staff presentation at the Workshop, would nearly double the annual rate of decline from current CAFs for "Standard" sectors (1.86% to 3.4%). As illustrated in the figure below, the direct allocation allowance gap widens with each year. By 2030, Standard sectors would receive only 50% under the proposed changes compared to 67% of direct allocation allowances that would occur under existing regulations.



Reductions in directly allocated allowances will increase the cost pass-through to customers while simultaneously decreasing the amount of allowances available for consignment, which are used to mitigate costs for impacted customers through the issuance of climate credits. The proposed CAFs are also estimated to generate lower climate credit value right when compliance costs are at their highest, which would only serve to undermine public support for the program.

Maintaining the current regulation avoids this mismatch in credits and costs that will result in rate impacts to utility customers. The GUG urges ARB to maintain a gradual step-down in emission caps coupled with the gradual increase (five percent per year) in consignment requirements to produce a more prudent approach to carefully introduce a price signal while ensuring consignment revenue for distribution of Climate Credits to natural gas utility ratepayers.

The GUG Opposes Changes to the Allowance Price Containment Reserve (APCR)

Staff's proposal to move allowances that remain unsold for 24 months into the APCR is premature. There are many factors, including secondary market surplus and recently undersubscribed auctions, that could cause the temporarily soft markets, but that does not justify a deliberate shifting of allowances into the APCR to create an artificial scarcity which will increase prices.

This condition would be exacerbated by the proposal to collapse the three reserve-price tiers into one. The remaining one tier will increase the chances of extreme price spikes and price volatility in the linked California and Quebec Cap-and-Trade carbon market.

The GUG urges ARB not to adopt the plan to move allowances that are unsold for 24 months to the APCR or the proposal to consolidate the three reserve-price tiers into one. These two changes together would be very costly for compliance entities and damaging to utility customers. Indeed, the only beneficiary of such interferences in the marketplace is the state of California which will be getting more for the allowances it sells, at the expense of California residents and businesses who will have to pay more for their natural gas and electricity needs.

The GUG Opposes Lowering the Offset Usage Limit Post-2020

ARB's proposal to lower the offset credit usage limit reduces an important cost-containment mechanism that protects California's customers and businesses, and supports AB 32 objective's to cost-effectively reduce greenhouse gases.

The GUG not only opposes lowering the offset credit usage limit but believes that ARB should strengthen the current, early-stage offset market by expanding the role of offsets in California's Cap-and-Trade Program. ARB should pursue all actions that contribute to a robust offset market, including increasing usage limits, improving and expanding offset protocols, and other actions that instill confidence in the offset market in which California participates.

The GUG members looks forward to continued dialogue with ARB as the amendment process moves forward. Thank you again for the opportunity to comment on the amendments to the Cap-and-Trade Regulations presented at ARB's Workshop.

Sincerely,

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