

October 17, 2014Richard Corey
Executive Officer
California Air Resources Board
1001 I Street
Sacramento, CA 95812-2828**Re: Pacific Gas and Electric Company Comments on the Clean Harbors Initial Determination**

Dear Mr. Corey:

Pacific Gas and Electric Company (PG&E) appreciates the opportunity to comment on the Air Resources Board's (ARB) preliminary determination in the investigation of Clean Harbors' compliance with the requirements of California's Cap-and-Trade Regulation and Ozone Depleting Substance (ODS) Protocol.

I. INTRODUCTION

PG&E appreciates the ARB's efforts to ensure that each offset credit used in the Cap-and-Trade Program meets strict criteria, and results from safe and environmentally-sound projects. As a covered entity under the Cap-and-Trade Program and an early proponent of the use of offset credits, PG&E has the following concerns regarding the investigation process and preliminary determination, as described below. Moreover, PG&E encourages ARB to finalize its investigation swiftly and leverage its findings to improve the investigation process going forward.

II. INVESTIGATION PROCESS

While the number of invalidated offsets is relatively small, PG&E is concerned that the investigation process has been disruptive to commercial processes in the offset credit market because of both the length of the investigation and the lack of a clear investigation process.

During the investigation, approximately 4.4 million compliance offset credits were removed from their Compliance Instrument Tracking System Service (CITSS) accounts, with little communication regarding when they might be determined invalid or returned to their accounts. The length of the investigation—it has been over four months since ARB's initial announcement on May 29 that it was conducting an investigation—and lack of transparency resulted in market uncertainty, disruptions to commercial processes, and could decrease the willingness of counterparties to transact, which may then reduce the counterparty pool and the total credits offered.

Further, ARB's discretion in interpreting its regulatory language to extend the length of the investigation process, without timely communication of this interpretation to market participants, undermines the certainty needed for markets to function effectively. Going forward, PG&E recommends that ARB amend the Cap-and-Trade regulation to clarify the sequence and timing of steps in an invalidation determination.

III. IMPACT OF THE PRELIMINARY DETERMINATION

A robust supply of offsets can reduce overall costs in the Cap-and-Trade Program. PG&E is concerned that ARB's preliminary determination—which invalidated offsets for an alleged violation unrelated to the actual destruction of ODS—could increase offset costs by complicating buyers' due diligence and offset assessment processes, as described below.

Currently, each offset credit undergoes a thorough review process. Offset credits are verified by a third-party ARB-approved verifier, reviewed by an Offset Project Registry for listing, and reviewed again by ARB for issuance, all before being screened by buyers and made subject to their due diligence processes. From a buyer perspective, it is crucial to be able to rely on the above processes to determine that they hold valid offsets.

However, the preliminary determination appears to undermine that certainty by expanding the grounds for invalidation beyond the veracity of offset project reductions. By invalidating the offsets for an alleged violation unrelated to the actual destruction of ODS, ARB would appear to open the door to a multitude of potential invalidations that would be unknowable to even the most diligent buyers.

To counter this risk, buyers will likely need to employ additional safeguards, leading to a decline in offset value. This could further result in higher costs for offset buyers, less income for offset marketers and developers, or both and thereby lower offset supply. This in turn could raise compliance costs with the Cap-and-Trade Program.

Moreover, forecasts indicate that offset supply will be insufficient in the second and third compliance periods. As such, PG&E recommends that ARB act to reassure the market by revisiting the value of the Program's invalidation provisions. Specifically, ARB should consider alternate approaches to buyer liability, such as a buffer account.

IV. CONCLUSION

PG&E appreciates ARB's efforts to ensure that each offset credit used in the Cap-and-Trade Program meets strict criteria and results from safe and environmentally-sound projects. However, PG&E remains concerned about the potential negative effects of the investigation on the offset market. ARB should finalize its investigation swiftly and leverage its findings to improve regulatory clarity.

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Sincerely,

A handwritten signature in black ink, appearing to read 'Mark C. Krausse', with a long, sweeping horizontal line extending to the right.

Mark C. Krausse
Senior Director, State Agency Relations

Cc: Brienne Aguila, via email
David Mallory, via email
Patrick Gaffney, via email
Jimmy Steele, via email