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Submitted electronically

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Rajinder Sahota
California Air Resources Board
1001 I Street
Sacramento, CA 95184

Re: **Comments of the Northern California Power Agency on March 29 Workshop on Setting Post-2020 Emission Cap and Allowance Allocation**

Dear Ms. Sahota:

The Northern California Power Agency[1] (NCPA) provides these comments in response to the March 29 California Air Resources Board (CARB) Workshop on proposed amendments to the Cap-and-Trade Program Regulation related to setting the post-2020 emissions cap and allowance allocation.

Determining the final post-2020 cap for the Cap-and-Trade Program and establishing the manner in which allowances will be allocated to affected covered entities are critically important issues. The following comments and recommendations are based on the information currently available and NCPA's understanding of Staff's objectives. NCPA appreciates the opportunity to provide these comments and looks forward to continuing to work with CARB staff and other stakeholders on final resolution of these issues.

Post-2020 Cap Setting

Staff proposes to maintain the economy-wide cap post-2020, and puts forth two options for setting the 2030 goal. Option 1 would entail a linear decline between the current 2020 and expected 2030 cap level. Option 2 sets a linear decline from the estimated 2020 covered GHG emissions and the estimated 2030 cap. While CARB has not yet determined the final goal, which is dependent upon the separate and ongoing analysis being undertaken as part of the Scoping Plan Update, of the two options presented, Option 1 represents the best alternative moving forward. The final 2030 cap will apply program-wide, regardless of the option selected. However, Option 2 would subject the markets and compliance entities to significant uncertainty since the starting point would be based on a currently unknown estimate of 2020 emissions. Based on CARB's estimated projections for the 2030 cap,

1 NCPA is a not-for-profit Joint Powers Agency, whose members include the cities of Alameda, Biggs, Gridley, Healdsburg, Lodi, Lompoc, Palo Alto, Redding, Roseville, Santa Clara, and Ukiah, as well as the Bay Area Rapid Transit District, Port of Oakland, and the Truckee Donner Public Utility District, and whose Associate Member is the Plumas-Sierra Rural Electric Cooperative. NCPA owns, operates, and maintains a fleet of power plants that is among the cleanest in the nation, providing reliable and affordable electricity to more than 600,000 Californians.

Option 1 represents a 4.4% annual decline rate, which is a significant increase over the current 2-3% annual rate of decline. This decline will continue to present a challenge for California's compliance entities. However, even with the greater reductions, Option 1, which represents a consistent transition from the current program to the post-2020 program, would provide compliance entities – and the markets – with the most seamless and certain path toward continued reductions. Of the two options Staff presented during the Workshop, Option 1 is preferable.

Allowance Allocation

The post-2020 allowance allocation proposal set forth in the March 29 Workshop Presentation is based largely on continuation of existing policies. This includes continuing to "implement current industrial allocation policy" (Workshop Presentation, p. 14) and to "continue EDU allocation through 2030 based on compliance obligation associated with supplied electricity." For EDU-allocation to individual EDUs, Staff's proposal is use the 2020 allocation, "with an adjustment for utility-specific industrial emissions as the starting point, but account for planned changes in electricity sources (e.g., planned coal divestiture, availability of nuclear resources)." (Workshop Presentation, p. 23)

NCPA supports Staff's proposal to continue with the existing allowance allocation policies adopted by the Board in 2011,[2] and in particular, the allocation of allowances directly to EDUs for the benefit of their ratepayers. The key principles upon which the preliminary EDU allowance allocation was based included covering the distribution utilities' compliance cost burden and recognition of early investments. (2011 FSOR, p. 575) In doing so, the Board recognized that EDUs were uniquely situated such that expenditure of allowance value by the EDU would most directly benefit California's electricity customers that would ultimately pay for the increased electricity costs associated with covering compliance obligations for GHG emissions. The "purpose of allowance allocation to the electric utilities is not for price mitigation, but to provide ratepayer relief while maintaining the price signal." (2011 FSOR, p. 2175) The original rationale for allocating allowances directly to EDUs in 2011 is still valid today, and even more important in the post-2020 program as greater emission reduction targets are mandated. Allocation of allowances to EDUs for the benefit of their ratepayers has been demonstrated to be the best means by which to ensure that the value of the allowance continues to directly benefit electricity customers.

Staff has proposed that this allocation continue to be based on the EDU's cost burden, with adjustments to the 2020 allocations to address known changes in electricity procurement. These changes are anticipated to include such things as increased renewable energy procurement, divestiture of coal resources and switching to state-of-the-art natural gas-fired generation, and the changing availability of nuclear power. In order to properly establish the methodology for calculating the projected cost burden, CARB should convene a working group to discuss the specific utility documents and filings that can be used to calculate the EDU-level allocation. NCPA and its member utilities look forward to working with CARB staff, other affected EDUs, and stakeholders on the methodology for determining the appropriate number of allowances to allocate to EDUs.

Adjustment for Emissions Associated with Electricity Sold to Industrial Covered Entities:

While the Workshop Presentation sets forth an allocation scheme for the industrial and electricity sector that is consistent with past policies, the proposal also includes a fundamental change. Staff

2 California's Cap-and-Trade Program, *Final Statement of Reasons,* October 2011 (2011 FSOR).

has proposed a revision to the allocation structure that would subtract allowances for industrial sector electricity purchases from the baseline number of allowances allocated to EDUs, and allocate allowances directly to covered industrial customers to cover their electricity purchases. If properly and accurately calculated, this revised approach would not have a net impact on allocation of allowances to EDUs based on their cost burden. Ensuring that industrial sector entity-specific electric purchases align with the EDU-specific allocations, however, will necessarily involve a complex methodology.

NCPA understands that this proposal is an attempt to address potential differences in the manner in which allowance value is distributed to energy-intensive, trade-exposed (EITE) entities located in different service territories. However, to the extent that this change would only apply to EITE entities that are also covered entities, even this proposal will not result in absolute uniformity across all EITE entities. Nor is such uniformity necessary. All EDUs are required to use the value of their allocated allowances for the benefit of electric customers. That mandate includes industrial customers – both those that are covered entities and those that are not. Indeed, allocation directly to covered industrial customers could result in those customers receiving both freely allocated allowances to cover their emissions, as well as the benefit of reduced utility costs resulting from the EDU's use of the value of their freely allocated allowances. In contrast, this scenario reduces the beneficial impact to the EDU's remaining electric customers. The proposal to revise the allocation methodology associated with electricity sold to industrial sector covered entities diminishes the ability of the EDU to ensure that the value of its allowances directly benefits the electric customers on whose behalf the allowances were allocated.

To properly account for the proposed adjustment, the allowances must be accurately allocated based on the emissions associated with the electricity sold. Based on the Workshop Presentation and discussion, it appears that the methodology that will be used for determining the number of allowances to credit to industrial customers differs from the projections that are contemplated for determining the allowance adjustments for EDUs. As such, there is a chance that the reduction in electricity sector allocations will not align with the industrial sector electricity purchases for which EDUs will not receive allowances.

As CARB found in 2011, "Allocation to electricity utilities was chosen as the preferred method to return the allowance value to those affected by this program. Because most industrial facilities and Californians use electricity, returning allowance value via electricity utilities is the best alternative to reduce the cost burden of this program. We modified the regulation to include 95892 that demands electric utilities use allocation value to benefit ratepayers, which includes both industry and Californians." (2011 FSOR, p. 567) NCPA believes that maintaining the current allocation design is best for the state. If there is to be a fundamental shift from this policy, NCPA is interested in working with CARB to better understand the rationale and manner in which this significant change in the allocation methodology would work. More information and a better understanding of the manner in which the adjustment – both for crediting industrial customers and deducting industrial sector emissions from the EDUs – is necessary in order to provide more meaningful comments on the manner in which this proposal would be administered.

Demonstration of Transportation Electrification:

Staff proposes that allowances be allocated to EDUs to recognize the impacts of electrification through "evidence-based allocation." (Workshop Presentation p. 24) As such, Staff explained that an EDU must make a demonstration of the impacts of electrification on its GHG emissions, after which allowances would be allocated. NCPA understands that rather than creating an electrification baseline, CARB is looking at an after-the-fact assessment of electrification and an allocation of the corresponding allowances in a future year. Staff is seeking stakeholder feedback on the way in which to "quantify and verify increased load due to electrification." (Workshop Presentation p. 24)

NCPA appreciates the recognition of the need to address the impacts on the electricity sector from increased electrification of transportation and Staff's recognition that these allowances would be in addition to the post-2020 EDU sector allocation. (Workshop Presentation p. 23) Transitioning the transportation sector to greater use of electric vehicles could result in significant reductions in the State's GHG emissions, especially as the transition expands well beyond electric vehicles to the State's shipping ports and major transportation hubs. In the Legislature's clear direction to encourage greater transportation electrification, there was also acknowledgment of the corresponding impact of this transition on electric retail sellers and POUs from such electrification.[3] Allocation of allowances to EDUs will be a critical tool in helping to ensure that increased electrification of transportation will not be accomplished to the detriment of electric utility ratepayers. Consequently, establishing the correct metric for this demonstration will be both critically important and challenging. In determining the appropriate demonstration, CARB must ensure an accurate accounting and avoid imposing new and burdensome reporting or tracking requirements, which could result in significant additional costs for EDUs, and especially smaller POUs. It is also important that the pool from which these allowances will be drawn is appropriately designated in order to ensure that there is no cost- or compliance-shifting, and that sufficient allowances are available in each compliance period (or year, depending on the frequency of the demonstration) to cover the associated emissions. NCPA also urges CARB to fully consider the manner in which the existing policies and provisions regarding the Low Carbon Fuel Standard (LCFS) will interact with this demonstration. Likewise, changes that will be a direct result of both CARB's and the California Public Utilities Commission's implementation of H&S § 44258.5(b) will also have a bearing on the impact of transportation electrification and potentially the demonstration CARB is contemplating.

<u>Consignment of Allowances to Auction:</u>

Staff proposes to retain all of the existing provisions regarding the manner in which IOUs and POUs consign allowances to auction. (Workshop Presentation p. 24) This includes what the Workshop Presentation has termed "optional consignment" for POUs. Stakeholders must understand that this alternative consignment option does not in any way alter the fact that POU electric ratepayers receive the full value of the allowances allocated to the POU. NCPA agrees with CARB's proposal to continue the current structure that allows POUs to place freely allocated allowances into either the auction or directly into their compliance accounts. EDUs have different business models and many POUs are largely vertically integrated. CARB's original findings recognized these differences and provided POUs with the ability to allocate allowances directly to their compliance accounts or designate them for auction. (2011 FSOR, pp. 578-580) Strict

3 Health & Safety Code § 44258.5(b) provides: The state board shall identify and adopt appropriate policies, rules, or regulations to remove regulatory disincentives preventing retail sellers and local publicly owned electric utilities from facilitating the achievement of greenhouse gas emission reductions in other sectors through increased investments in transportation electrification. Policies to be considered shall include, but are not limited to, an allocation of greenhouse gas emissions allowances to retail sellers and local publicly owned electric utilities, or other regulatory mechanisms, to account for increased greenhouse gas emissions in the electric sector from transportation electrification.

provisions regarding the use of allowance value – both from allowances sold into the auction and those placed directly into a POU's compliance account – ensure that POU customers receive the full benefit of value of those allowances. The use of that allowance value is thoroughly explained and documented in a report filed with CARB each year, further ensuring the validity and integrity of the program. There is no reason to alter the existing program or amend the provisions of 95892(b)(2).

Other Program Impacts

The March 29 Workshop was but one in a series of workshops designed to address the scope of proposed amendments to the existing Cap-and-Trade Program and Mandatory Reporting Program Regulations. Discussing the proposed amendments by topic facilitates more in-depth deliberation on the various issue areas. At the same time, it is important that CARB Staff and stakeholders not lose track of the inter-related nature of the various discussions. Compliance costs, modeling and forecasts, cost containment provisions and measures, and potential amendments to compliance periods all directly impact discussions relevant to cap-setting and allowance allocation. The manner in which the allowances currently set-aside in the allowance price containment reserve are utilized – either redistributed into the program or otherwise designated for future cost containment - will also directly impact compliance entities. Likewise, any amendments to the underlying structure and treatment of electric generation facilities subject to the EPA's Clean Power Plan will also have ramifications on the overall program. NCPA appreciates the more detailed discussions that come out of the issue-specific workshops, but once these specific issues have been more thoroughly developed, these matters need to be assessed holistically as part of comprehensive workshops prior to moving onto formal regulatory revisions.

Conclusion

NCPA appreciates the opportunity to provide these comments and looks forward to working closely with Staff and other stakeholders as the State works through these important issues. If you have any questions regarding these comments, please do not hesitate to contact the undersigned or Scott Tomashefsky at 916-781-4291 or scott.tomashefsky@ncpa.com.

Respectfully submitted,

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