M-S-R Public Power Agency

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September 19, 2016

Submitted electronically

Mary Nichols, Chair
California Air Resources Board
1001 I Street
Sacramento, CA 95812

Re: **Comments on Proposed Amendments to Cap-and-Trade Program**

Dear Ms. Nichols:

The M-S-R Public Power Agency (M-S-R)[1] appreciates the opportunity to provide these comments to the California Air Resources Board (CARB) regarding the *Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanism Regulation*.[2]

Introduction

Created in 1980, the M-S-R Public Power Agency is a public agency formed by the Modesto Irrigation District, the City of Santa Clara, and the City of Redding. M-S-R is authorized to acquire, construct, maintain, and operate facilities for the generation and transmission of electric power and to enter into contractual agreements for the benefit of any of its members. Currently, M-S-R and its members have contractual arrangements for over 625 megawatts of California Energy Commission (CEC) RPS-certified renewable energy. Each of M-S-R's member agencies are covered entities under the Cap-and-Trade Program Regulation (Regulation), and are directly impacted by the requirements set forth therein. As electrical distribution utilities (EDUs), M-S-R's members are also subject to additional programs and mandates administered by other state agencies as part of the California's greenhouse gas (GHG) emission reduction strategy, including the Renewable Portfolio Standard (RPS) program.

1 Created in 1980, the M-S-R Public Power Agency is a public agency formed by the Modesto Irrigation District, the City of Santa Clara, and the City of Redding.

2 Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanism; Staff Report: Initial Statement of Reasons, dated August 2, 2016 (Staff Report).

These comments, and those of the Joint-Utility Group in which M-S-R has joined, are provided in the interest of ensuring that amendments to the Cap-and-Trade Program, and indeed, the continued operation of this important market-based measure, enhance, rather than inhibit, the ability of compliance entities such as M-R-S to reduce their GHG emissions in the most cost-effective and technologically feasible manner possible.[3]

M-S-R joins in the comments submitted by the California Joint-Utility Group and urges the Board to ensure that the changes discussed therein are part of the ongoing Rulemaking and reflected in further revisions and 15-day Changes to the Regulation. M-S-R does not reiterate all of the points raised in the Joint-Utility Group comments, but rather focuses these comments on the following distinct issues:

First, M-S-R asks that the Board acknowledge the full impact on California utilities of meeting the state's climate change and clean energy objectives; this cost burden is not limited to costs associated solely with meeting the Cap-and-Trade program compliance obligation. In fact, investments in clean energy resources and GHG-reducing programs and measures can result in higher costs for California's residential and business electricity customers than GHG allowances. As such, it is important that the electrical distribution utilities be allocated sufficient allowances to cover these cost burdens and pass along the value of those allowances to directly benefit their electricity ratepayers. As more fully addressed below, this includes recognition of the importance and impacts of the RPS Program and the impacts resulting from increases in electricity sales associated with electrification of other sectors of the economy, including the transportation sector.

Second, M-S-R urges the Board to recognize that the Cap-and-Trade Program has implications for other important programs that are part of the State's energy policies, particularly the RPS Program. The RPS Adjustment should be retained as part of the Cap-and-Trade Program, and should be implemented in a way that ensures that compliance entities under the Cap-and Trade Program are not forced to retire allowances for electricity imports associated with contracts for renewable, zero-GHG, RPS-eligible resources.

Third, consistent with the mandates of Health & Safety Code section 44258.5(b), CARB must consider the impacts of increased GHG emissions in the electricity sector that result from transportation electrification. As part of that assessment, CARB should consider allocating allowances to electrical distribution utilities to address those increased emissions.

Fourth, M-S-R asks that the Board only allow California's program to be linked with other programs if that linkage ensures that there is a sufficient supply of compliance instruments for California compliance entities. Linkages with other emissions-based programs that do not afford California compliance entities access to additional compliance instruments while allowing California compliance instruments to be retired for other than the Program should be avoided.

3 The cities of Redding and Santa Clara are also members of the Northern California Power Agency (NCPA) and support the comments submitted to CARB by NCPA, as well.

COMMENTS

1. Cost Burden and Post-2020 EDU Allowance Allocation

The Cap-and-Trade Program, while a critically important tool in meeting California's GHG reduction and clean-energy goals, is not the only mandate on electric utilities associated with meeting those statewide policy objectives. Indeed, as but one of the many measures addressed in the Scoping Plan, the Cap-and-Trade Program is intended to complement other programs and measures addressed therein. Allocation of allowances to the EDUs is an important element of the Cap-and-Trade Program. As CARB has noted, the "purpose of allowance allocation to the electric utilities is not for price mitigation, but to provide ratepayer relief while maintaining the price signal."[4] The need for ratepayer relief extends to cost associated with meeting the state's far-reaching climate objectives. The Staff Report and 45-day proposed amendments do not include a specific proposal for the post-2020 EDU allocation, but discusses a proposal for establishing the allocation "based in part on the methodology used for 2013-2020 EDU allocations." (Staff Report, pp. 41-43)

M-S-R appreciates the recognition that EDUs should continue to receive allowances and in collaboration with other stakeholders, is working with CARB staff on the appropriate methodology. Part of that evolving process includes determining the EDUs' cost burden. When assessing the cost burden on electrical distribution utilities of meeting clean energy goals, CARB must look at the totality of the measures EDUs are required to implement to reduce statewide emissions, and not consider the Cap-and-Trade program in a vacuum. Rather, the cost burden should be considered in the context of the Scoping Plan itself. This is critically important because EDU costs associated with these other programs have a direct impact on their compliance obligation under the Program. Reduced compliance costs associated with the Cap-and-Trade Program do not necessarily translate to a reduced cost burden for EDUs; California's electric utilities must meet renewable energy, energy efficiency, and energy storage mandates, for example, all of which should reduce GHG emissions but not necessarily at lower costs than Cap-and-Trade Program allowances. Furthermore, the electric sector alone will be responsible for ensuring California's compliance with the Environmental Protection Agency's (EPA) Clean Power Plan (CPP) should it become law, adding another level of compliance responsibilities on the sector.

For these reasons, M-S-R urges the Board to direct staff to continue to work with stakeholders on the important issue of determining the appropriate methodology for allocating allowances to the EDUs. M-S-R asks that the Board further direct staff to address cost burden consistent with the principles for defining cost burden set forth in the comments of the Joint Utility Group in furtherance of developing that methodology.

2. RPS Adjustment

The 2008 Scoping Plan included the RPS program as a recommended complementary

4 California's Cap-and-Trade Program, Final Statement of Reasons, October 2011 (2011 FSOR), p. 2175.

measure, recognizing it is a means by which to "achieve cost-effective emissions reductions while accelerating the necessary transition to the low-carbon economy required to meet the 2050 target."[5] In recognition of these complementary roles, the RPS Adjustment should be retained as part of the Cap-and-Trade Program. Since it was first included in the Regulation, the RPS Adjustment has served the important function of ensuring that the Cap-and-Trade Program does not work *against* the objectives of the RPS Program by recognizing the significant investments utilities have made in renewable resources, not all of which are located in California. As the utilities have repeatedly noted – in both formal and informal comments to CARB and to Staff – the RPS Adjustment serves an important function in both ensuring that the value of out-of-state renewable energy resources are fully realized by the California electricity customers whose utilities made the investments while also recognizing the overlapping policy objectives of two important but separate programs aimed at meeting California's climate change goals. M-S-R opposes Staff's proposal to eliminate the RPS Adjustment after 2020.

Eliminating the RPS Adjustment has Significant Adverse Cost Implications for Compliance Entities: The importance of the RPS Adjustment should not be marginalized by simply because utilizing the provision is "optional"; it is a critically important measure for avoiding paying additional and unwarranted costs for clean energy imports, as well as ensuring that the GHG emissions profile of the EDUs that have invested in those resources accurately reflects those investments. M-S-R's members have existing resource commitments for RPS-eligible resources located outside of the state that are "firmed and shaped" before serving California load. Those resources account for as much as 35% of the City of Santa Clara's RPS compliance obligation and as much as 85% of Redding Electric Utility's (REU) total renewable portfolio. For REU along, the value of the RPS Adjustment post-2020 is estimated at over $600,000 based on conservative price estimates. For the members of M-S-R that have significant investments in these out-of-state renewable contracts, the RPS Adjustment is not deemed an option.

Furthermore, while M-S-R appreciates staff's explicit acknowledgement of the interaction between the Program and renewable energy imports, Staff's proposal to address these impacts through the allocation of allowances directly to EDUs to cover the emissions associated with these imports does not alleviate the cost impact, as these transactions were never intended to be treated as ones that involved a compliance obligation.

The Joint Proposal Addresses the Stated Concerns: M-S-R understands and shares CARB staff's concern that the integrity of the Cap-and-Trade Program be preserved and that the state's emissions be accurately counted. However, eliminating the RPS Adjustment is not necessary to address those concerns. Indeed, eliminating the RPS Adjustment would result in greater compliance costs for covered entities and provide an inaccurate picture of California's true emissions associated with imported electricity. Rather than do away with this important cost-containment measure that helps to protect California ratepayer's long-term investments in

5 Climate Change Scoping Plan, December 2008, pp. 19, see also p. 44.

renewable energy resources, the regulatory language should be amended to provide for greater clarity. Amendments to the Cap-and-Trade Program and the Mandatory Reporting Regulation (MRR) will address both CARB staff and stakeholders' concerns without the need to eliminate the RPS Adjustment. Misunderstandings associated with utilization of the RPS Adjustment are the result of differing interpretations of language found in the Cap-and-Trade Regulation and the MRR. On January 15, 2016, a coalition of California utilities presented CARB with proposed amendments that would address the stated concerns.[6] Modifications to the regulatory language in both regulations to ensure consistency and clarity should go far to ameliorate the current issues regarding RPS Adjustment claims and ensure that only the entity with title to the environmental attributes (renewable energy credits or RECs) would be qualified to claim the import as specified power and utilize the RPS Adjustment, therefore, removing the potential risk of double counting that claim. Implementing these changes will also make certain that the total emissions attributed to compliance entities like EDUs with contracts for zero-emission renewable energy are accurate. Under the current structure, even when entities like M-S-R settle their transactions contractually, the final emissions factor attributed to the utility does not reflect the zero emissions from the renewable resource, thus providing an inaccurate picture of their emissions profile. The proposed changes address concerns about double counting and program integrity, which can be entirely eliminated by acknowledging REC ownership for purposes of claiming the adjustment.

Total Emissions for Affected EDUs are Overstated without the RPS Adjustment: The RPS Adjustment correctly adjusts the Cap-and-Trade compliance obligations so that imports of clean, zero-GHG resources used for RPS program compliance are not assigned a compliance obligation under the Cap-and-Trade Program. This does alter or otherwise impact the emissions reported under the MRR. As such, while use of the RPS Adjustment does not affect the accuracy of CARB's GHG inventory report, elimination of the RPS Adjustment does overstate GHG emissions that are assigned a compliance obligation for entities that must now treat their RPS-eligible resource as one with a GHG emission. Therefore, the total GHG emissions attributed to compliance entities with claims to the renewable attributes that were unable to claim the RPS Adjustment reflect a GHG intensity that is greater than their actual emissions, thus skewing both the GHG profile of the compliance entity and needlessly increasing their compliance obligation under the Program.

Allocation of Allowances Based on a Set Percentage of the RPS Program Purchases of Portfolio Content Category 2 Resources is an Ineffective and Insufficient Replacement for the RPS Adjustment: As part of staff's proposal to eliminate the RPS Adjustment beginning in 2021, staff contemplates allocating allowances to the EDUs "that accounts for RPS-eligible electricity that is purchased together with RECs but cannot be directly delivered to California." (Staff Report, p. 53) The specific details regarding the manner in which this allocation would be calculated are still outstanding and will likely not be fully developed until 15-day language.

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6 The California Utilities' January 15 Letter is appended to the California Joint-Utility Group comments on the Proposed Amendments, dated September 19, 2016.

However, as currently contemplated, allowances intended to replace the RPS Adjustment would be based on a quantity of Portfolio Content Category (PCC) 2 allowances defined in Public Utilities Code (PUC) section 399.16(b)(2) and (c). This proposal suffers from several significant infirmities. First, not all utilities have the same amount of PCC 2 resources; to the extent that allocation of allowances is to be determined based on the EDU's cost burden, the amount of PCC 2 resources at issue must be factored in. Second, a one-time allocation would not take into account future PCC 2 contracts or changes to existing agreements. The ever increasing RPS mandate, coupled with what will be escalating Cap-and-Trade compliance costs under a declining cap, make it imperative that EDUs retain the maximum flexibility in their renewable resource procurement plans going forward. Third, the proposal does not address RPS Program resources deemed PCC 0 by the CEC, as defined in PUC section 399.16(d). M-S-R members have significant investments in renewable resources that meet the PCC 0 statutory requirements, but would be wholly unacknowledged under the current proposal. As noted above, the financial implication of eliminating the RPS Adjustment associated with these resources is considerable; the proposed allowance allocation alternative does not address them all. Fourth, the quantity of allowances allocate would be subject to the declining cap, while procurement associated with these RPS-eligible resources would not. Finally, as noted above, while allocating allowances would at least help to offset the increased compliance costs that would result from the change in policy regarding the treatment of these RPS-eligible resources, it would not address the misrepresentation of the EDU's actual GHG emissions. That is because it would still require a GHG compliance obligation for imports of zero-GHG emission resources. For all of these reasons, staff's proposed alternative fails to adequately address the gap that would ensue should the RPS Adjustment be eliminated.

3. Transportation Electrification

Without a doubt, electrification of other sectors will have a beneficial impact on total statewide GHG emissions and play an important part in meeting the state's climate objectives. At the same time, increased electrification of California's homes, businesses, and modes of transportation will result in increased GHG emissions in the electric sector. The legislature clearly acknowledged this link in Senate Bill 350 when it added section 44258.5 to the Health & Safety Code. H&S section 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.

Despite this charge, the proposed amendments do not address this issue at all. The Staff Report notes only that "Staff is continuing to evaluate how increased electrification for the transportation sector for the post-2020 period should be accounted for in the allocation methodology for EDUs." (Staff Report, p. 43) M-S-R agrees that it is important to ensure that there is an accurate method to calculate the impacts, but does not believe that it is appropriate to exclude transportation electrification impacts from the allowance allocation discussion at this time. The 15-day language should include Proposed Amendments that address the manner in which increased emissions for EDUs from transportation electrification will be specifically recognized in the Cap-and-Trade Program.

4. One-Way Linkages

California's Cap-and-Trade Program should only be linked with other programs if that linkage ensures that there is a sufficient supply of compliance instruments for California compliance entities. Linkages with other emissions-based programs that do not afford California compliance entities access to additional compliance instruments while allowing California compliance instruments to be retired for other than the Cap-and-Trade program should be avoided. M-S-R encourages CARB to seek linkages with other jurisdictions that can be mutually beneficial, but is concerned about one-way linkages that could compromise the ability of California compliance entities to meet their compliance obligations under the declining cap that will be imposed. The Legislature provided clear direction to CARB regarding the criteria that must be met before it would be appropriate to link programs, and each of those provisions should continue to be followed when assessing the viability of potential trading partners with which to link California's Program. M-S-R is also concerned about the ability to reconcile one-way linkages with partners within and outside of the jurisdiction of the EPA's CPP should the CPP become law. The state should pursue arrangements that will allow additional trading among sister states under the CPP program. Especially at the nascent stages of exploring the feasibility of utilizing the Cap-and-Trade program for compliance with the CPP, M-S-R believes that the provisions for linkages already included in section 95943 of the Regulation should be retained.

CONCLUSION

For the reasons set forth herein, and in the comments of the California Joint-Utility Group, M-S-R asks that the Board direct staff to continue to work with stakeholders to draft further revisions to the Proposed Amendments that address the concerns raised and consistent with the recommendations provided.

Respectfully submitted,

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M-S-R Public Power Agency