



December 9, 2016

Richard Corey
Executive Officer
California Air Resources Board
1001 I Street
Sacramento, CA 95812-2828

RE: California Joint Utility Group Comments on Proposed Electric Distribution Utility Allowance Allocation

Dear Mr. Corey,

Introduction

The California Joint Utility Group (“JUG”)¹ respectfully submits this letter, on behalf of customer interests, to the California Air Resources Board (“ARB”) regarding staff’s methods for post-2020 allowance allocation to electric distribution utilities (EDUs) as presented at the workshop on October 21, 2016. The JUG appreciates staff’s availability for continued dialogue on the proposed changes to the Cap-and-Trade Program post-2020, and views the proposals in this letter as a step in that iterative process.

The JUG proposal suggests improvements, on behalf of customer interests, to four main areas of the current ARB staff EDU allowance allocation structure. The aim of these recommendations is to minimize potential cost impacts to ratepayers that could result from insufficient allowance allocation. Adopting the changes proposed in this letter will help ensure that the cost of the State’s climate policies will not unduly impact California households, and will further enable EDUs to continue investing in cleaner electricity resources, providing critical support to help the State meet its ambitious climate goals.

The key areas of concern are:

1. **Ensuring Consistency through Technical Improvements** – Consistency across programs is critical for market stability. In support of this, the JUG suggests the Renewables Portfolio Standard (RPS) component of the allowance allocation computation should be applied to retail sales and not load including losses, consistent with the way compliance is calculated for the RPS Program. Additionally, ARB should base their allocation calculation on demand forecasts that do not include additional achievable energy efficiency (AAEE). Finally, emission factors for greenhouse gases should be updated in line with the latest International Panel on Climate Change (IPCC) recommendations.

¹ Southern California Edison, Pacific Gas & Electric Company, San Diego Gas and Electric, Southern California Gas Company, Los Angeles Department of Water and Power, Sacramento Municipal Utility District, Southern California Public Power Authority, Northern California Power Agency, Pacificorp, Turlock Irrigation District, Modesto Irrigation District.

2. **Rapid Rate of Allocation Decline** – The current proposal entails a precipitous 9-12 percent or so annual reduction in allocations between 2021 and 2030 due to reliance on both a cap adjustment factor (CAF) *and* a ramp up to a 50 percent RPS. This is approximately double the overall adjustment in the Cap over the period. The JUG recommends that the standard CAF be reevaluated for the electricity sector and the movement to a 50 percent RPS be removed from the allocation methodology.
3. **Mitigating the Allocation “Program Transition Cliff” in 2021** – The proposed EDU allocation methodology results in a reduction in allocation between 2020 and 2021 that is greater than 50 percent for many EDUs. The JUG believes this is inconsistent with the allocation principles of covering the customer cost burden, and a desire to avoid abrupt increases in utility rates due to carbon pricing.
4. **Electrification of Transportation and other End Uses**– Utility customers should not shoulder additional compliance costs due to the implementation of electrification measures, which will necessarily increase electric generation but achieve net emission reductions from a societal perspective. Without a clear mechanism that awards credit for electrification initiatives, ARB would effectively impose additional costs to the EDUs for reductions achieved through electrification and remove the incentive for EDUs to invest in electric vehicle infrastructure. JUG recommends that ARB continue work to develop allowance allocation rules and other regulatory mechanisms that encourage vehicle electrification by EDUs in keeping with the spirit of SB350.

Without these changes, the JUG is concerned that the proposed allowance allocations will not serve the ARB’s intent of mitigating the approximate cost burden levied upon utility customers. Because customer rates are impacted not only by Cap-and-Trade but also by complementary measures such as the 50 percent RPS, doubling of energy efficiency and energy storage mandates, the JUG contends that sufficient allowance allocation on behalf of our customers is critical to managing the broader cost burden of the state’s climate programs. While the JUG recognizes that the Electric Sector is in a unique position to be able to contribute substantial reductions, California ratepayers should not have to bear significant cost burdens associated with the investments required to become California’s low carbon sector leader.

Detailed Recommendations and Rationale

Ensuring Data Accuracy and Program Consistency through Technical Improvements – The JUG suggests three key changes to bring the allocation methodology in line with the RPS Program and remove inclusion of AAEE, as these savings are uncertain and have historically proven to differ significantly from actual achieved energy efficiency. Ensuring data accuracy and program consistency is necessary for effective EDU investment decisions, planning, and program management.

First, when considering how much renewable generation supports load, ARB should apply the annual RPS percentage in a resource portfolio to retail sales, not total load with losses. This is consistent with the RPS Program itself, which clearly considers a percentage of retail sales, not load with losses, when determining compliance.

Second, ARB should base allocations on demand forecasts that do not include any AAEE. Forecast AAEE amounts are highly uncertain, and historical experience shows actual savings are commonly significantly lower than forecast savings. Additionally, expected AAEE data is not available for all utilities, potentially leading to the inequitable treatment of EDUs. The JUG also notes that removing

AAEE is consistent with the current EDU allocation methodology, which does not decline allocations at all with respect to energy efficiency estimates.²

Including AAEE in the allocation methodology would effectively reduce allocations to EDUs for continued investment in energy efficiency, the first resource in the State's loading order, reducing the incentive for EDUs to pursue these investments. Finally, including AAEE in the EDU allocation methodology is equivalent in concept to updating the benchmarks for utilities every year, something ARB staff is not proposing for other allocated sectors such as industrial customers.

The JUG also notes that the allocation methodology should rely on the most up-to-date emissions factors as consistent with the recently updated IPCC global warming potentials. Using the new emission factors for allocation will match what will be used for compliance obligations.

Rapid Rate of Allocation Decline – Both Method 1 and Method 2 proposed by staff include a very sharp annual decline in allowances to EDUs, on the order of 9-12 percent per year, 100 percent or more higher than the decline would be if allocations just followed the cap. This occurs due to reliance on *both* the cap adjustment factor (CAF) and the linear ramp of RPS attainment from 2021-2030 up to 50 percent. The JUG recommends that ARB reevaluate the CAF for the electricity sector and remove the linear ramp up to 50 percent RPS in the allocation.

An allocation methodology and cap decline factor unique to the electricity sector is proposed in order to recognize the additional compliance burden placed on EDUs as a result of increased electrification in the transportation sector. In addition, further reducing EDU allocation because of our required investment in renewable resources is inappropriate given the expected customer cost burden from these resources and the associated infrastructure necessary to reliably deliver renewable electricity to our customers.

Additionally, the assumption that each EDU's compliance burden will be reduced by the ramp up to 50% RPS by 2030 is inappropriate when determining allowance allocations, due to the inconsistent accounting of RPS eligible electricity between the RPS Program and the Cap-and-Trade program. First, not all RPS eligible electricity will directly reduce an EDU's carbon obligation under the Cap-and-Trade program. The RPS program allows up to 10 percent of the RPS target to be satisfied using unbundled renewable energy credits (RECs), which represent renewable electricity produced but not delivered to California, so this procurement will not reduce the EDU's carbon obligation under the Cap-and-Trade program. Second, it is unclear at present to what degree the RPS Adjustment can be claimed by the EDUs to reduce their compliance obligation for the 15%-25% of the RPS that can be met with Portfolio Content Category 2 resources and many grandfathered resources. Third, RPS eligible electricity that is directly delivered to a California Balancing Authority area may not reduce an EDU's carbon obligation if the electricity is not delivered all the way to the EDU's service territory. Finally, some significant amount of RPS-driven overgeneration is very likely in this 2020 – 2030 time period and, when this occurs, there will be little or no GHG emissions reductions. Given these facts, the increase in RPS procurement from 33% to 50% is unlikely to reduce an EDU's carbon obligation under the Cap-and-Trade program by the full amount suggested by going from 33% to 50%. Therefore, the JUG proposes to hold the RPS percentage flat at 33% for purposes of determining the EDU's allowance allocation.

² In the current methodology, the overall electric sector allocation is set in the Cap-and-Trade Regulations, and is simply the starting number of 97.7 million metric tons times the declining cap factor through 2020. Committed energy efficiency, but not additional achievable, is considered when dividing this total up amongst utilities, but inclusion in this manner does not reduce overall EDU allocations over time.

Mitigating the Starting Allocation “Program Transition Cliff” in 2021 – The proposed allocation methodology results in a significant decrease in allocation between 2020 and 2021 – greater than 50 percent for many EDUs. This deep and abrupt reduction in allocation is inconsistent with ARB’s stated policies of customer protection and avoidance of abrupt increases in customer costs related to carbon pricing and related complementary measures. The JUG is considering a number of solutions to remedy this issue with the current cost-burden methodology, and expects to bring a consensus solution forward at the next opportunity to meet with ARB to discuss allowance allocation.

Electrification of Transportation and other End Uses – In order to meet the State’s emission reduction goals in 2030 and 2050, electrification needs to be cost effective and remain a low cost alternative fuel for transportation and other end uses. In addition, electrification of the transportation and other sectors of California will yield substantial net reductions in criteria pollutants that will be needed for attaining ambient air quality standards for ozone and particulate matter under the federal Clean Air Act. This is clearly identified in the text of SB350, and the JUG believe more needs to be done to ensure that utilities and other interested parties are encouraged to pursue electrification opportunities where they are appropriate.

Under the proposed ARB allocation methodology, there likely will be insufficient coverage of emission cost burden, leading to significant electricity rate increases, particularly in a tightening market where allowance prices approach or reach APCR levels. This runs the risk of having a preemptive chilling effect on the needed electrification initiatives of public and private sector entities. Without a clear signal that EDU emissions from electrification will be appropriately covered by allowances or a similar policy, the JUG believes it will be much more difficult for California to achieve its 2030 emission reduction target. It is important that ARB develop an effective regulatory framework for encouraging the electrification of the transportation and other sectors of the California economy. Key components of this framework will include recognition that most forms of electrification will not naturally be accompanied by sub-metering programs, and requiring such sub-meters acts as a barrier to implementation. The JUG recommends that ARB keep the “big picture” perspective in mind as it develops the post-2020 allowance allocation rules for the electricity sector in regards to carbon-reducing electrification activities.

Conclusion

Member companies of the Joint Utility Group appreciate the continued dialogue with ARB staff and management on these important issues. JUG members urge ARB staff to include the proposed changes to the EDU allowance allocation methodology. Thank you for your time and for your careful consideration of these issues.

CC:

Steve Cliff
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