SEEC Webinar Presentation
Cap & Trade: Overview and CPUC Procedural Activity

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Assembly Bill 32 – The California Global Warming Solutions Act of 2006

- Establishes a goal of reducing statewide emissions of greenhouse gases to 1990 levels by 2020 and 80 percent below 1990 levels by 2050.
- Air Resources Board issued a scoping plan in December 2008 that identified key measures to achieve emission reductions.
  - Cap and Trade
  - Complementary Measures
    - California Light Duty Vehicle GHG Standards
    - Energy Efficiency
    - Renewables Portfolio Standard
    - Low Carbon Fuel Standard
    - California Solar Initiative
    - Efficiency Improvement to and the Electrification of Goods Movement
    - Medium and Heavy Duty Vehicle Efficiency Improvements and Hybridization
  - Complementary measures account for approximately 80 percent of total emissions reductions required to achieve 2020 target
    - Cap & Trade is a "back-stop" – to the extent additional reductions beyond what is realized through the complementary programs are necessary in order to achieve the 2020 target, the market will determine the solution.

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Overview of the Cap and Trade Program

- Establishes annual emissions cap across sectors with compliance beginning in 2013
- Initially cap covers large stationary sources
  - Cap is "source-based" meaning that, in most cases, the regulated entity is the entity actually producing carbon emissions.
  - A substantial share of the emissions allowances will be directly allocated to covered sectors and/or entities.
    - Electric Distribution Utilities will receive a direct allocation based on their expected emissions, with additional allowances provided to recognize early action on renewables and energy efficiency.
    - Entities determined by the ARB to be "Trade Exposed and Emissions Intensive" will receive a direct allowance allocation based on a "product benchmark" reflecting 90% of the average embedded emissions in the goods they produce.
- In 2015 the framework expands to include transportation fuels and gas suppliers

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Cost Burden of Cap & Trade

- Who ultimately bears the costs under cap & trade depends on the ability of entities to avoid carbon cost exposure and/or the ability to pass any carbon costs upstream (to suppliers) or downstream (to customers)
  - Commercial entities may be able to reduce carbon cost exposure through process changes, investments in energy efficiency, etc.
  - They may also be able to pass costs through to customers in the form of higher prices/fees.
    - Note that this does mean that these commercial entities may lose some business, as higher prices leads to reduced demand, however, this rebalancing of demand reflects a more socially optimal outcome as it includes the price on carbon.
  - However, some entities cannot raise prices owing to being "trade exposed".
    - If these entities try and raise prices, consumer demand will simply to suppliers of these goods and services that are not subject to a carbon price. Total (global) emissions will be unchanged or will increase as production shifts to facilities located outside of the cap and trade framework. This is known as "emissions leakage".
  - The buck stops with households.
    - Ultimately, substantial share of the costs incurred under cap & trade will be incurred by households with those increases resulting in substitution and/or reduced consumption.

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Cost Mitigation Under Cap & Trade

- As an approach to emissions mitigation, cap & trade enables the market to find least cost reductions
  - Entities that are able to reduce their emissions at a price less than the cost of emissions allowances will reduce their emissions until the marginal abatement cost is equal to the allowance price.
  - Entities for which the cost of emissions reductions exceeds the allowance price will procure allowances to cover their emissions.
- Offsets
  - ARB regulation allows up to 8 percent of an entity's annual compliance obligation to be met with offsets; these are projects that reduce emissions in areas/sectors not already covered by the cap.
- Banking
  - Entities may back a given years allowances/offsets and apply them to future years.
- Cost Containment Reserve
  - ARB has set aside a portion of the allowances into a containment reserve which will be sold to regulated entities if prices reach a certain threshold.
- Direct allocation of emission allowances
  - Emissions intensive trade exposed entities receive a direct allowance allocation based on the level of their trade exposure on a per product basis.
  - Electric Distribution Utilities receive an direct allocation of allowances but are required to consign these allowances to auction, with the proceeds being used for the benefit of ratepayers to compensate them for the costs of AB 32.
- Air Pollution Control Fund
  - The auction of allowances not directly allocated to the Electric Distribution Utilities will be auctioned and the proceeds of these auctions will be accrued in the Air Pollution Control Fund, with the use to be determined. These monies will be used for purposes designated in the Health and Safety Code upon appropriation by the Legislature.

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The CPUC's Greenhouse Gas Order Instituting Rulemaking

- In March, the CPUC opened Rulemaking 11-03-012 to address a number of issues related to the ongoing implementation of the cap & trade program
  - Track I is addressing the use of the revenues generated from the sale of emission allowances allocated to the IOUs; current schedule calls for a decision in June 2012.
  - Track II will address the use of any revenues generated from the sale of Low Carbon Fuel Standard Credits; current schedule call for a decision in October 2012.
  - Track III will address gas utility procurement authority as it relates to GHG compliance products and use of revenues (to the degree applicable).

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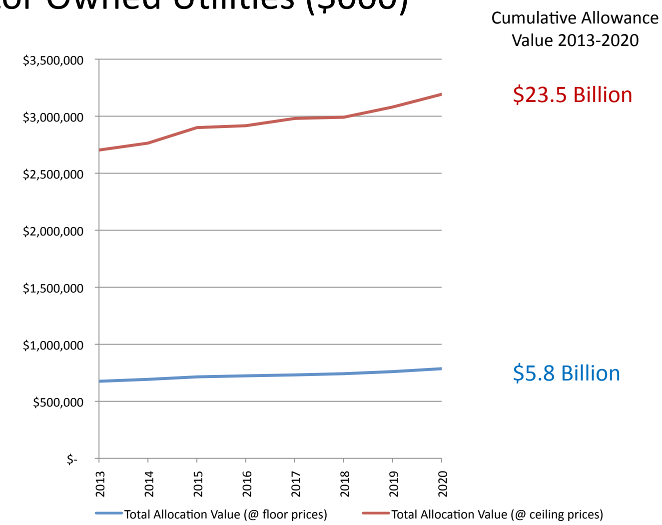
Estimated Value of Allowances Allocated to the Investor Owned Utilities ($000)



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Policy Outcomes/Considerations on Use of Allowance Value

- Preserve the Carbon Price Signal
- Prevent Economic Leakage
- Equitably Distribute Revenue Value Recognizing Atmosphere as a Public Asset
- Reduce/Mitigate Adverse Impacts on Low Income Households
- Correct for Market Failures That Lead to Underinvestment in GHG Mitigation Activities and Technologies
- Competitively Neutral Across Load Serving Entities
- Administratively Simple/Easy to Understand

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Stakeholders Participation in the Proceeding

- 47 Active Parties, representing utility, generator, environmental, low-income, consumer, community choice aggregator, energy service provider, industrial interests, and local government interests
- Parties have submitted initial proposals on the use of allowance revenues
- Key Issues:
  - Addressing indirect emissions costs exposure for EITE entities
  - Basic allocational approach to distributing revenues – cost-based or lump sum
  - Additional uses of revenues
    - Support additional investments in renewables, energy efficiency, research and development
    - Community benefit funds; capacity building to address climate change impacts
  - Maintaining appropriate incentives for combined heat and power

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Additional Opportunities for Stakeholder Involvement on Issues Related to Cap & Trade Allowance Revenues

- Air Pollution Control Fund

- SB 535 – Community Benefits Fund
  - Introduced by Senator De Leon
  - Would create the "California Healthy Air Revitalization Trust" in the State Treasury
  - Trust would be funded with a minimum of 10% of the allowance auction revenues that accrue to the Air Pollution Control fund
  - Monies would be used to fund programs in the state's most disadvantaged and impacted communities to address health and environmental impacts associated with climate change.

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