June 21, 2024
LEG 2024-0096

Rajinder Sahota
Deputy Executive Officer
California Air Resources Board
1001 I Street
Sacramento, California 95814

RE: Sacramento Municipal Utility District's Comments on Potential Amendments to Cap-and-Trade Program

Dear Ms. Sahota:

The Sacramento Municipal Utility District (SMUD)[1] appreciates the opportunity to comment on the California Air Resources Board's (CARB) May 31, 2024, workshop on potential changes to the Cap-and-Trade program. SMUD is a not-for-profit, publicly-owned utility (POU) with a locally-elected Board of Directors. SMUD's customers, community, and partners are at the heart of all it does. Maintaining low rates, encouraging electrification, and reducing greenhouse gases (GHG) in the Sacramento region while providing safe and reliable power are central to SMUD's work and the pursuit of its aggressive climate goals.

The current ratepayer protections built into the Cap-and-Trade program, in the form of electric distribution utility (EDU) allowance allocations, directly support these important efforts. SMUD's customers have additionally benefited from the current regulatory flexibility that allows SMUD, as a local POU, to customize and optimize use of its allowances for maximum community benefit. The EDU allocation, coupled with this flexibility, directly mitigates Cap-and-Trade cost impacts that would otherwise be borne by SMUD's customers. This, in turn, helps SMUD maintain the affordable rates needed to encourage electrification, supports investments in GHG-reducing projects and programs, and facilitates the transition to a greener, reliable grid.

As CARB considers potential amendments to the Cap-and-Trade program, it is imperative that the program retain these essential ratepayer protections—namely, the EDU allocation and the POU flexibility to use allowance allocation for compliance or consignment.

In the following pages, SMUD is pleased to address questions presented by CARB staff at the May 31, 2024, workshop.

[1] SMUD is a signatory to the Joint Utilities Group (JUG) letter dated June 21, 2024, and also supports the comments of the California Municipal Utilities Association. SMUD additionally offers more detailed feedback in response to select questions posed at the May 31, 2024, workshop.

Question: Is the current EDU and NGS allocation sufficiently aligned to promote state electrification goals?

SMUD believes that maintaining the current EDU allocation, as set forth in Table 9-4 of the Cap-and-Trade regulations, is necessary to protect ratepayers and support state electrification goals. Achieving electrification goals and realizing their associated benefits requires sufficiently low electricity rates to encourage fuel switching and clean electricity generation. The current EDU allocation is set at a level that reflects EDUs' reasonably anticipated cost burden for the 2021-2030 period. This allocation, alongside POUs' limited but critical flexibility to optimize value for customers, mitigates the rate impacts that would otherwise be associated with Cap-and-Trade while simultaneously encouraging POUs to invest in GHG-reducing projects and programs.

A reduction in the EDU allocation would likely result in Cap-and-Trade compliance costs impacting rates and making it more challenging to promote state electrification goals. Today, there are myriad factors placing upward pressure on electric utility rates, the impact of which may potentially discourage electrification. Cap and Trade has not been, and should not become, one of them.

The EDU allocation provides significant benefits to POU customers, including a downward pressure on rates.

To date, the EDU allocation has provided substantial value to SMUD's customers. Since 2013, over $680,000,000 of Cap-and-Trade allowance value has directly benefited SMUD's customers and local community by offsetting the cost of program compliance and supporting investments in clean energy, electrification, and a suite of other GHG-reducing projects and programs while also contributing to SMUD's ability to offer some of the lowest rates in the state. In fact, SMUD estimates that the value of its 2025-2030 EDU allocation is equivalent to an annual rate offset of roughly 8-13% for increased renewable energy purchases or avoided Cap-and-Trade compliance costs. A loss or reduction of that allocation could require equivalent ratepayer contributions to support those investments, making it harder to maintain affordable rates and accelerate clean energy progress.

This support for ratepayers is critical as SMUD progresses with its 2030 Zero Carbon Plan—an ambitious path toward eliminating carbon dioxide emissions from SMUD's power supply by 2030, with reliability and affordability in place as guardrails. Importantly, with its Zero Carbon Plan, SMUD has committed to keeping rate increases at or below inflation. SMUD anticipates that the Cap-and-Trade allowance allocation will play a key role in helping SMUD decarbonize in the coming years while maintaining the affordable rates that are needed to encourage electrification.

The flexibility to optimize use of POU EDU allocations allows POUs to maximize value to their customers and local communities.

Under the existing Cap-and-Trade regulation, POUs like SMUD are able to determine whether to retire allowances for compliance and/or consign allowances to auction. This regulatory framework ensures that SMUD and other public, locally-governed utilities can optimize their allowance allocation to best serve their customers. In line with this framework, on an annual basis, SMUD evaluates the specific needs of its community and customers and right-sizes its strategy accordingly.

For example, between 2020-2024, SMUD elected to use a portion of its EDU allocation directly toward compliance, thereby enabling SMUD to avoid, each year, the equivalent of an estimated 3-4% rate increase. Over this same period, SMUD invested a portion of its allowance value in climate-friendly, GHG-reducing projects, including renewable energy purchases, without passing on the costs of these investments to ratepayers. Together, this strategy helped SMUD maintain lower rates, which encourages customers to electrify their homes and vehicles, contributing to further emissions reductions in SMUD's service area. While SMUD's use of Cap-and-Trade allowances has varied over time, depending on its local community's specific priorities, the value derived from these allowances has always directly supported SMUD's customers.

The current EDU allocation should largely be maintained to continue incentivizing decarbonization investments based on reasonable assumptions of Cap-and-Trade compliance costs.

SMUD understands that CARB is considering revisions to the EDU allowance allocation with the intent of more closely aligning with individual EDUs' potential Cap-and-Trade compliance costs. These revisions may include updating the forecasted electricity supply and demand assumptions and the Renewables Portfolio Standard (RPS) requirements that underpin the EDU allocation calculations. However, as described in the JUG's comments, a key purpose of establishing a 10-year allocation was to create regulatory certainty and incentivize decarbonization investments while protecting electricity ratepayers from program costs.[2] A mid-stream change to the underlying supply and demand data, and thus the EDU allocation, undermines those benefits. Accordingly, SMUD recommends against such a change.

That said, SMUD agrees that it is reasonable for CARB to update the RPS requirements used to calculate the EDU allocation in conformance with recent changes in state law; namely, increased RPS procurement requirements would generally translate to a reduced Cap-and-Trade compliance obligation and therefore a reduced need for allowances. However, as noted in the JUG letter, the current EDU allocation calculation fails to fully account for the different ways that utilities may satisfy the RPS requirements set forth in Public Utilities Code section 399.11 et seq. Specifically, as EDUs increase

[2] See, for example p. 39 of the *Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms, Final Statement of Reasons*, dated August 2017; p. 34. at p. 39

the quantity of RPS-eligible electricity they procure, they must also satisfy the portfolio balance requirement (PBR). The PBR requires at least 75% of RPS-eligible electricity consists of bundled renewable energy purchases that are directly delivered to California (also known as Portfolio Content Category 1, or PCC 1, resources). Those do not incur Cap-and-Trade compliance obligations. Importantly, however, the remaining procurement (25%) of RPS-eligible electricity may come from a combination of PCC 2 and PCC 3 resources, which are not required to be directly delivered to California (or, in the case of PCC 3, to be bundled) and may incur Cap-and-Trade compliance obligations. This is important, as CARB's EDU allocation calculation assumes that only up to 10% of RPS-eligible procurement may incur Cap-and-Trade compliance obligations when, in fact, that should be 25% of RPS-eligible procurement.

As described in the JUG letter, reflecting the full extent of allowable RPS procurement within the EDU allocation is becoming increasingly important as RPS targets escalate, and EDUs face mounting procurement challenges. Therefore, SMUD urges CARB to update the RPS assumptions used to calculate EDU allocations both to reflect the higher procurement targets established by Senate Bill (SB) 100 *and* the maximum of 25% of RPS procurement that can be met by renewable resources that may incur Cap-and-Trade compliance obligations. Absent these tandem changes, the EDU allocation may not sufficiently reflect the costs attributable to the Cap-and-Trade program, eroding the crucial ratepayer protections that otherwise would promote the state's electrification goals.

Question: Should there be any additional limitations on the types of GHG reduction projects that can be funded with EDU or NGS allocated allowance value?

No, CARB should not establish any additional limitations on the types of GHG reduction projects than can be funded with EDU allocated allowance value. CARB should additionally preserve the ability for POUs like SMUD to determine whether to retire allowances for compliance and/or consign allowances to auction. As described above, this regulatory framework is efficient and cost-effective, and it ensures that POU customers reap the maximum benefits of Cap-and-Trade allowance value. Without flexibility to optimize benefits to ratepayers, the EDU allocation would be less effective in providing the downward pressure on rates that is needed to encourage customers to electrify their homes, vehicles, and businesses.

Conclusion

Thank you for the opportunity to provide feedback on potential changes to the Cap-and-Trade program. SMUD looks forward to working with CARB and stakeholders to develop proposed regulatory changes that align the Cap-and-Trade program with the state's climate goals while continuing to include affordability protections for POU electricity customers.

/s/

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cc: Corporate Files