December 15, 2023

Rajinder Sahota
Deputy Executive Officer for Climate and Research
California Air Resources Board
1001 I Street – P.O. Box 2815
Sacramento, CA 95812

Subject: SoCalGas Comments on the November 16, 2023, California Workshop on Potential Amendments to the Cap-and-Trade Regulation

Dear Deputy Executive Officer Sahota:

SoCalGas appreciates the opportunity to provide comments on the California Air Resources Board's (CARB) November 16, 2023 Workshop on Potential Amendments to the Cap-and-Trade Program. We appreciate CARB's effort to model the impact of allowance reductions and other changes to the Program to forecast the impact on prices at the end of this decade. It is crucial to balance the increasing stringency of Cap-and-Trade regulation with policies that manage volatility in the marketplace. California is most likely to achieve its 2045 carbon neutrality goals through a long-term planning process that supports affordable and resilient decarbonization.

SoCalGas's comments highlight the following: 1) Sharp increases in allowance prices modeled in the workshop will result in increased energy costs for utility ratepayers; 2) Current exemptions from holding limits are wholly appropriate for utilities and should remain unchanged; 3) Allowance banking is a key strategy for long-term planning and cost containment; 4) Investment in clean fuels provides the best long-term opportunity for ratepayers to experience affordable and resilient decarbonization that complements electrification.

I. Sharp increases in allowance prices modeled in the workshop will result in increased energy costs for utility ratepayers.

SoCalGas and other utilities have repeatedly raised concerns regarding potential ratepayer expenses resulting from compliance with proposed changes to Cap-and-Trade. We recognize this theme is redundant, but it is enormously significant. Rate and bill increases do not unfold in a vacuum as other programs and potential reductions in natural gas demand throughput may exert additional pressure on natural gas rates with cumulative cost impacts. Pass-through costs associated with SoCalGas's allowance procurement are unavoidable because energy generated for ratepayers comprises the overwhelming majority of the CO2e emissions SoCalGas is responsible for under Cap-and-Trade.

Over 90% of the gas for which SoCalGas uses allowances to comply with Cap-and-Trade is supplied to homeowners, small businesses, renters, and other customers across California.[1] Ratepayer costs could prove to be extremely challenging by 2030, when utilities must consign all allowances to the auction market and will need to purchase allowances from the market to cover emissions. The November 16 workshop projects allowances to be approximately three times as expensive as they are today. Ultimately the increased cost will fall on ratepayers.

All stakeholders involved must manage affordability issues to preserve public support for California's aggressive decarbonization policies. Polls indicate that most Californians are justly proud that our state is taking a lead in fighting climate change but also wary of paying higher energy costs. A fascinating study released in July 2023 by the Public Policy Institute of California found that strong majorities of Californians are concerned about the impact of climate change and supportive of Governor Gavin Newsom and the state legislature in their handling of environmental issues. Yet despite these convictions only 43% of Californians said they are willing to pay more for electricity from renewable sources.[2] Therefore, it is important to consider measures to address affordability in the context of achieving California's 2045 goals.

II. Current exemptions from holding limits are wholly appropriate for utilities and should remain unchanged.

At the workshop, CARB raised the issue of consolidated holding limits for allowances and exemptions from those limits for covered entities in direct corporate associations. One of the categories that may be implicated is corporate affiliates that share a parent company. SoCalGas, San Diego Gas & Electric (SDG&E), and Sempra Gas & Power Marketing (SGPM) are affiliates that share a parent company: Sempra. They are also separate cap-and-trade covered entities. Affiliate transaction rules imposed by CPUC and FERC prohibit these companies from sharing certain resources and information, including, but not limited to, the joint or coordinated procurement of allowances and offsets. As set forth in 17 CCR Section 95833(c)(1), any "registered entity subject to affiliate compliance rules promulgated by state or federal agencies shall not be required to disclose information or <u>take other action that violates those rules</u>." (Emphasis added.) These affiliates are exempt from group holding limits normally imposed on entities in a corporate association. While we appreciate CARB's concern for potential market manipulations, SoCalGas, SDG&E, and SGPM are prohibited from sharing *any* sensitive non-public market information.[3] If consolidated holding limits were imposed on these companies, they would violate the affiliate transaction rules.

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[1] 2022 California Gas Report, pp. 167-18. See https://www.socalgas.com/sites/default/files/Joint_Utility_Biennial_Comprehensive_California_Gas_Report_2022.pdf

[2] https://www.ppic.org/publication/ppic-statewide-survey-californians-and-the-environment-july-2023/

[3] The affiliate transaction rules collectively refer to the following: CPUC Decisions D.06-12-029 and D.98-03-073, and FERC Orders 697, 707, and 717.

Implementing holding limits on non-compliance entities involved in the purchase of allowances may be more appropriate. Companies, such as hedge funds, could otherwise buy and stockpile allowances. As the overall allowances released into the market decrease, these entities could acquire an excessive portion of the allowance market, leading to a potentially undesirable scenario for pricing.

III. Allowance banking is a key strategy for long-term planning and cost containment.

At the workshop, CARB noted the benefits of banking, but also invited stakeholders for input on potential alterations to rules of banking allowances. SoCalGas agrees with CARB that the banking policy has successfully added flexibility, incentivized early action, and reduced compliance costs of the Cap-and-Trade Program. Banking thus provides covered institutions flexibility in the planning and implementation of emission reduction strategies.

The modeling presented during the workshop indicated significant increases in forecasted allowance prices around 2030. This coincides with the deadline for utilities to consign all allowances to the auction market. Banked allowances acquired in earlier years at lower prices have already reduced the allowance pool, encouraging early emission reductions. In the future, these banked allowances will assist utilities in managing volatility in their incurred Cap-and-Trade compliance costs. If CARB determines that adjustments to banking practices could enhance the Cap-and-Trade system, we recommend limited changes that preserve crucial cost containment and climate early reduction benefits to alleviate potential impact on ratepayers.

IV. Investment in clean fuels provides the best long-term opportunity for ratepayers to experience affordable and resilient decarbonization that complements electrification.

Ratepayer affordability for decarbonization policies over the long term is a crucial concern. As alluded to in our response to the June 27 workshop, SoCalGas is building out a clean fuels network consisting of "drop in" fuels that decarbonize the existing natural gas pipelines, construction of dedicated hydrogen infrastructure for industrial and/or hard-to-abate uses, and pipeline carbon transportation to support carbon capture and sequestration (CCS). These clean fuels and abatement strategies complement electrification of California's economy by providing integration and backup for renewable energy and resilient transportation of energy underground (much of it in existing infrastructure).[4] Several items from the recent workshop are relevant to the construction of this clean fuels network.

First, SoCalGas asks CARB to consider the tradeoff for emissions reductions between a more stringent allowance policy for utilities in the medium term and the investment funding that policy will divert from investment in the clean fuels network. SoCalGas' Clean Fuels Report projects that thermal generation and clean molecules are the lowest-cost approach for integrating and backing up a high-renewables system.[5] Without a clean fuels network, a significantly larger buildout of transmission, renewables and storage is needed. Alternative forms of long duration storage would

[4] Massachusetts Institute of Technology, Lincoln Laboratory, "Interdependence of the Electricity Generation System and the Natural Gas System and Implications for Energy Security," pg. 6, 15 May 2013.
[5] See p. 41. https://www.socalgas.com/sites/default/files/2021-10/Roles_Clean_Fuels_Full_Report.pdf

need to be scaled up from a nascent level and would need to reach low price targets to avoid a high-cost burden.

Second, we reiterate a request from a previous letter that natural gas utilities be afforded greater flexibility to invest allowance consignment proceeds in decarbonized energy. Under current policy, electric utilities are permitted greater opportunity to invest in renewable energy resources (or the integration of renewable energy resources) that can be used in their respective service territories.[6] While this distinction may have made sense fifteen years ago, advancements in clean fuels technology combined with a greater awareness of the needed scale of decarbonized energy at midcentury render it obsolete. Revenue from consigned allowances could be used, among other things, for the procurement of biomethane, support for transitioning biomethane fuels currently incentivized through the Low Carbon Fuel Standard (LCFS) to non-transportation and stationary end uses (especially in the hard to abate sectors), CCS buildout, and clean renewable hydrogen projects.

Third, we note that CARB is not yet able to account for CCS in allowance modeling because the regulatory framework is still in development. We suggest that CARB consider ways to account for or encourage CCS abatement as outlined in SB 905.

Fourth, we urge CARB to commit to expanding the Cap-and-Trade system until 2045. Long-term planning inherent to the construction of the clean fuels network and allowance budgeting needs long-term policy support where timelines align with California's 2045 climate goals.

Conclusion

SoCalGas appreciates the opportunity to provide comments and participate as a stakeholder regarding amendments to the Cap-and-Trade Program. SoCalGas is committed to a decarbonized energy system that is affordable for all Californians. We look forward to continued engagement in CARB's regulatory process.

Respectfully,

/s/ Kevin Barker

Kevin Barker
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[6] Cap and Trade Regulation, pp. 200-205 and 217-220. There are a few exceptions such as pyrolysis gasification projects under SB 1440.