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**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking to Address Utility Cost and
Revenue Issues Associated with Greenhouse Gas
Emissions.

R. 11-03-012
(Filed March 24, 2011)

**REPLY COMMENTS OF THE NATURAL RESOURCES DEFENSE COUNCIL
(NRDC), SIERRA CLUB CALIFORNIA, THE GREENLINING INSTITUTE
(GREENLINING), UNION OF CONCERNED SCIENTISTS (UCS), LOCAL
GOVERNMENT SUSTAINABLE ENERGY COALITION (LGSEC), NATIONAL
CONSUMER LAW CENTER (NCLC), CLIMATE PROTECTION CAMPAIGN (CPC),
CALIFORNIA HOUSING PARTNERSHIP CORPORATION (CHPC), AND
COMMUNITY ENVIRONMENTAL COUNCIL REGARDING PARTIES' PROPOSALS
TO ALLOCATE GREENHOUSE GAS ALLOWANCE REVENUES**

February 14, 2012

Alex Jackson
Natural Resources Defense Council
111 Sutter Street, 20th Floor
San Francisco, CA 94104
415-875-6100
ajackson@nrdc.org

Andy Katz
Sierra Club California
801 K Street Suite 2700
Sacramento, CA 95814
510-848-5001
andykatz@sonic.net

Ryan Young
The Greenlining Institute
1918 University Avenue, 2nd Floor
Berkeley, CA 94704
510-926-4018
ryany@greenlining.org

Jasmin Ansar
Union of Concerned Scientists
2397 Shattuck Avenue, Suite 203
Berkeley, CA 94704
510-809-1570
jansar@ucsusa.org

Jennifer K. Berg
Jody S. London
Local Government Sustainable Energy
Coalition
P.O. Box 3629
Oakland, CA 94609
(510) 839-0688 x 213
Jennifer.berg@ngem.com
jody_london_consulting@earthlink.net

Olivia Wein
National Consumer Law Center
1001 Connecticut Avenue, NW, Suite 510
Washington, DC 20036-5528
202-452-6252
owein@nclc.org

Barry Vesser
Climate Protection Campaign
P.O. Box 3785
Santa Rosa, CA. 95402
(707) 525-1665
bvesser@climateprotection.org

Ross Nakasone
California Housing Partnership Corporation
369 Pine Street, Suite 300
San Francisco, CA 94104
415-433-6804 x310
RNakasone@chpc.net

Tam Hunt
Community Environmental Council
26 W. Anapamu St., 2nd Floor
Santa Barbara CA 93101
(805) 214-6150
tam@communityrenewables.biz

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1 Introduction

Pursuant to Rules 1.1 and 1.10 of the California Public Utilities Commission's (Commission) Rules of Practice and Procedure, the Natural Resources Defense Council (NRDC), Sierra Club California (Sierra Club), Greenlining Institute, Union of Concerned Scientists (UCS), Local Government Sustainable Energy Coalition (LGSEC), National Consumer Law Center (NCLC), Climate Protection Campaign (CPC), California Housing Partnership Corporation (CHPC), and the Community Environmental Council (SBCEC) (collectively "Joint Parties") respectfully submit these reply comments based on the "Assigned Commissioner and Administrative Law Judges' Joint Scoping Memo and Ruling" (Scoping Memo) dated September 1, 2011, the "Joint Administrative Law Judges' Ruling Adopting Modified Schedule" dated November 16, 2011, and the "Administrative Law Judges' Ruling Extending Deadline" dated December 28, 2011, to allocate revenues generated from the sale of emission allowances by the three investor-owned electric utilities (Utilities) subject to the jurisdiction of the Commission.

We reiterate our request that the Commission assess parties' comments and allocation proposals to the extent they adhere to the entirety of ARB's guidance and intent in developing the cap-and-trade rule, and the collective set of objectives identified in this proceeding. The burden of persuasion should rest on parties to justify why the Commission must resign itself to reverse course from its standing policy position that allowance revenues should finance investments in energy efficiency and renewable energy and not "dampen the price signal resulting from the cap-and-trade program."¹

2 Parties

NRDC is a non-profit membership organization with nearly 100,000 members in California and has a longstanding interest in minimizing the societal costs of the reliable energy services that Californians demand.

Sierra Club is a national, California-based non-profit membership organization with 150,000 members in California, with an interest in increasing energy efficiency and renewable energy to reduce greenhouse gas emissions.

The Greenlining Institute is a national policy, organizing, and leadership institute working for racial and economic justice. The organization's mission is to empower communities of color and other disadvantaged groups through multi-ethnic economic and leadership development, civil rights, and anti-redlining activities.

The Union of Concerned Scientists (UCS) is a national, non-profit, membership organization with over 14,000 members in California and is devoted to building a healthier environment and a safer world through the use of rigorous scientific analysis, innovative thinking and committed citizen advocacy.

The Local Government Sustainable Energy Coalition (LGSEC) is the only statewide organization that formally represents the interests of local governments before California's energy and environmental regulatory agencies. Members are leaders among local governments in energy efficiency, renewable energy, climate action planning, sustainability and related issues.²

¹ See D.08-10-037 at 227-228 and OP 15.

² The LGSEC is a statewide membership organization of cities, counties, associations and councils of government, special districts, and non-profit organizations that support government entities. Each of these organizations may

The National Consumer Law Center (NCLC) was established in 1969 with the mission of advocating on behalf of low-income consumers in the economic marketplace. In addition to focusing on many other consumer issues, NCLC has long worked on a range of energy and utility issues, with the goal of ensuring that low-income households have access to essential utility services and to energy efficiency programs. NCLC actively participated in the public policy discussions around the Waxman-Markey bill and other climate change legislation that came before Congress, particularly on the issue of how to allocate sufficient revenues to low-income customers to address bill impacts and to mitigating the effects of climate change.

The Climate Protection Campaign (CPC) is a California-based non-profit organization which focuses on public policy that will significantly reduce greenhouse gas emissions through increasing energy efficiency, developing renewable energy and other means.

The California Housing Partnership Corporation (CHPC) is a statewide organization dedicated to assisting nonprofit and government housing agencies to create, acquire, green, and preserve housing affordable for lower-income households, while providing leadership on housing preservation policy and funding. CHPC is also the convener of the Green Rental home Energy Efficiency Network (GREEN), a coalition of over 35 organizations committed to increasing access to energy efficiency resources for very low income residents of multifamily rental properties in California and ensuring that publicly assisted properties serving the state's lowest income households receive an equitable distribution of these resources.

The Community Environmental Council is a member-supported environmental non-profit organization formed in Santa Barbara in 1970 and is the leading environmental organization in the Central Coast region of California. In 2004, the Council shifted its primary focus to energy and transportation issues and is spearheading a regional effort to wean Central Coast communities from fossil fuels, on a net basis, during the next two decades. The Council is almost unique in combining on the ground work on a number of energy and climate change-related issues with concurrent work on state and federal policy issues. The Council's state policy work is directly informed by experience with what has worked, or is likely to work, at the local level. More information on the Council and its energy programs may be found at www.cecsb.org.

have different views on elements of these comments, which were approved by the LGSEC's Board. A list of our members can be found at www.lgsec.org.

3 Discussion

We respond to comments offered by the Joint Utilities, Agricultural Parties,³ PacifiCorp, the Division of Ratepayer Advocates (DRA), the California Energy Efficiency Industry Council (Efficiency Council), The Utility Reform Network (TURN), the Direct Access Customer Coalition (DACC), the California Construction Industry Labor Management Trust (Trust), the Independent Energy Producers Association (IEP), and the City and County of San Francisco (CCSF).

3.1 Investing Allowance Revenues in Additional Energy Efficiency and Carbon Mitigation Programs is Appropriate to Consider in this Proceeding

Several parties in their opening comments suggest that investing any portion of allowance revenues in additional clean energy programs is unnecessary or duplicative given existing Commission mandates.⁴ Yet these parties fail to reconcile their position with the clear direction from ARB, expert panels, and this Commission that proposals for allocating allowance revenues should be evaluated to the extent they invest in additional carbon mitigation activities such as energy efficiency and distributed generation.⁵ To comply with AB 32 and achieve California's long-term climate objectives at least cost, the Commission should follow through on the expert recommendations of the ETAAC and EAAC to invest a portion of allowance revenues to address systemic market barriers to implementing low-cost carbon mitigation strategies in the electric sector that pricing alone will not unlock.⁶

³ Comprised of the California Farm Bureau Federation, the Agricultural Council of California, the California League of Food Processors, and the Agricultural Energy Consumers Association.

⁴ See, e.g., Opening Comments of the Joint Utilities at 5-10; Opening Comments of PacifiCorp at 12.

⁵ See ARB Board Resolution 10-42 at 13, (December 16, 2010), available at:

<http://www.arb.ca.gov/regact/2010/capandtrade10/res1042.pdf>; CPUC, D.08-10-037 at OP 15; Economic and Allocation Advisory Committee (EAAC), "Allocating Emissions Allowances Under a California Cap-and-Trade Program: Recommendations to the California Air Resources Board and California Environmental Protection Agency," at 67, 70 (March 2010), available at:

http://www.climatechange.ca.gov/eaac/documents/eaac_reports/2010-03-22_EAAC_Allocation_Report_Final.pdf; "Recommendation of the Economic and Technology Advancement and Advisory Committee (ETAAC): Final Report," (February 14, 2008), available at: <http://www.arb.ca.gov/cc/etaac/ETAACFinalReport2-11-08.pdf>.

⁶ EAAC Report at 67, 70; ETAAC Report.

3.1.1 Our Proposal is Designed to Achieve Additional Reductions Under a Carbon Mitigation Framework that the Commission’s Current Programs are Not Equipped to Capture

The Utilities argue that the Commission has established proceedings in place to consider funding decisions for existing clean energy programs (such as customer energy efficiency) and that proposals to expand programmatic offerings in those areas should therefore be taken up in those proceedings to “ensure customers are not required to pay multiple times or excessively for the same programs.”⁷ Rather than assess our investment proposal on the merits, which is designed specifically to address how allowance revenues can unlock *additional* savings opportunities that the Utilities’ current programs are not capturing, the Utilities focus instead on characterizing our proposal as simply a “backdoor” attempt to fund a “litany” of “special interest purposes.”⁸

Contrary to the Utilities’ implication, or the examples the Utilities spotlight from other parties’ proposals, we do not propose the Commission use allowance revenues as a “fallback” for perceived shortcomings in current programs. With respect to energy efficiency, for example, the Utilities’ current energy efficiency portfolios are designed under a resource procurement framework – i.e., the current funding levels and cost-effectiveness parameters are structured in comparison to the avoided cost of acquiring the marginal supply side alternative.⁹ To maintain an apples-to-apples comparison between efficiency and supply side resources (consistent with the loading order), the Commission should retain this framework for funding efficiency programs through the Utilities’ procurement budgets.

But as we outline in our proposal, we propose the Commission allocate *allowance revenues* under a fundamentally different approach (consistent with AB 32), which would shift the emphasis to programs designed to achieve energy savings over a longer payback period (i.e., greater than the 20-year procurement time horizon), and assess cost-effectiveness from the perspective of the least-cost reduction strategies to achieve the goals of AB 32 and California’s long-term climate objectives.¹⁰ In other words, the current energy efficiency proceeding is not designed or equipped to fund the projects and programs we propose the Commission target with

⁷ Opening Comments of the Joint Utilities at 3

⁸ Id. at 5-6. The Utilities make their case by drawing from proposals offered by other parties, but make no mention of our proposed investment framework.

⁹ See Revised Proposal of the Joint Parties at 37-40.

¹⁰ Id.

allowance revenues (which draw heavily from the ETAAC and EAAC’s recommendations to target market barriers holding back carbon mitigation solutions).¹¹ Accordingly, the Commission must act *in this proceeding* to assess whether allowance revenues provide an opportunity to achieve additional reduction opportunities beyond the Commission’s current suite of programs.

3.1.2 The Commission Can Move Forward With an Investment Framework Without Making Specific Funding Decisions in this Proceeding

Other parties, such as TURN, argue that this proceeding is not the appropriate forum to consider expanding programmatic offerings, as none of the proposals are sufficiently developed to be adopted at this time.¹² TURN also cautions the Commission against “rushing” into approving new public goods programs in this proceeding.¹³ As we note in our revised proposal, however, we are not proposing that the Commission attempt to finalize the details of an investment program at this stage in the proceeding. Rather, the Commission must first determine the appropriate amount and mechanism by which to allocate revenues towards uses other than direct bill relief. Following that decision, the Commission should initiate a follow-up phase to assess opportunities and develop an overall allocation framework that leverages and coordinates with existing proceedings (including R.11-10-003, R.09-11-014, and A.11-05-017 et al.). Specific programs eligible for funding from allowance revenues would be subject to the same level of review as any other program funded through the current proceedings. Funding decisions for specific programs would thus not be spread over various proceedings under our proposal, and key stakeholders in those proceedings would have ample notice and opportunity to be involved in the decision-making process.¹⁴

3.1.3 Investing Allowance Revenues in Additional Carbon Mitigation Activities Advances a Core Objective of this Proceeding

PacifiCorp characterizes our proposal to expand current energy efficiency programs under a carbon mitigation framework as a “wholesale departure from long-standing ratemaking,

¹¹ Both the ETAAC and EAAC recommended investing a substantial share of allowance value as a means to overcome market barriers holding back energy efficiency and clean technology solutions that will reduce long-term costs. See note 4, *supra*.

¹² See Opening Comments of TURN at 2.

¹³ *Id.* at 4.

¹⁴ See Opening Comments of the Joint Utilities at 6.

resource planning, and general policy principles.”¹⁵ As with the Utilities, however, PacifiCorp ignores entirely one of the core objectives identified by the Commission in this proceeding – to use auction revenues to correct for market failures that lead to ongoing underinvestment in carbon mitigation activities and technologies.¹⁶ It is worth emphasizing that the Scoping Ruling clarifies that this objective “refers to the degree to which the proposed *use of auction revenues* [not existing funding sources] addresses market failures that are likely to continue to inhibit or prevent investment in carbon mitigation activities and technologies, irrespective of emissions pricing” (emphasis added).¹⁷

3.1.4 Our Proposal Balances the Commission’s Objectives in this Proceeding to Advance the Short-Term and Long-Term Interests of Retail Customers

The Utilities assert that “it is significant that the customer advocacy” groups support the return of “substantially all of the allowance revenues directly to customers,”¹⁸ as opposed to proposals – like our own – that draw attention to the benefits to customers from investment. We remind the Commission, however, that the Joint Parties include longstanding consumer advocates such as the National Consumer Law Center and Greenlining Institute, and that the Joint Proposal calls for roughly 70% of allowance revenues be returned directly to customers (tracking closely the EAAC’s recommended division between investment and direct bill relief).¹⁹ What our proposed allocation represents is rather the product of a careful balancing of the objectives the Commission put forth to guide parties’ proposals in this proceeding, which reflects the diverse set of interests represented in our coalition and recognizes the need to both mitigate short-term costs and invest in future bill reductions through improved efficiency.

Indeed, an array of parties – including labor, industry, and consumer advocates – all call attention to the need to invest allowance revenues to advance clean energy solutions and mitigate long-term customer costs.²⁰ The California Construction Industry Labor Management Trust, for example, “stress[es] the importance of investing in energy efficiency and distributed generation

¹⁵ Opening Comments of PacifiCorp at 12.

¹⁶ “Assigned Commissioner and Administrative Law Judges’ Joint Scoping Memo and Ruling,” at 9 (Sept. 1, 2011), available at: <http://docs.cpuc.ca.gov/efile/rulc/142511.pdf>.

¹⁷ Id. (Appendix A).

¹⁸ Opening Comments of the Joint Utilities at 10.

¹⁹ Based on forecast allowance prices. Sierra Club and LGSEC also propose a greater share of allowance revenues above the floor price be set aside for investment.

²⁰ See, e.g., Opening Comments of CCSF at 3, Opening Comments of the Efficiency Council at 2-3, Opening Comments of DRA at 11, Opening Comments of the Trust at 2; and Opening Comments of GPI at 7.

activities that will help support California’s communities, businesses, and local governments to upgrade their buildings and facilities in order to mitigate their carbon footprint.”²¹ Similarly, the Efficiency Council documents the range of benefits achievable through expanding investments in energy efficiency.²² Chief among them, the Council draws attention to the cost savings to utility customers that improvements in energy efficiency will bring about in a carbon-constrained economy.²³

The potential for significant long-term customer savings likewise underlies DRA’s proposal to invest allowance revenues in energy efficiency.²⁴ DRA recommends the Commission invest in energy efficiency financing to achieve long-term emission and bill reductions, and supports “allocating a portion of the GHG revenue towards investments that will decrease long term compliance costs, rather than the Utilities’ proposal which would only mitigate higher electricity costs in the short-term without investing in long-term GHG reduction measures.”²⁵

3.1.5 ARB Did Not Intend to Foreclose Investment Opportunities by Requiring Allowance Revenues Be Used for the Exclusive Benefit of Retail Customers

The Utilities further argue the Commission should not invest allowance revenues in additional clean energy programs because the Commission could not be sure that revenues allocated for investment would be used exclusively for the benefit of IOU customers, as required by ARB.²⁶ We agree that the Commission should only invest in programs with a clear connection to customers’ electricity use and which fall within its legal purview.²⁷ We also agree the Commission should only make programs directly available to the Utilities’ bundled customers or DA/CCA customers on whose behalf the Utilities will receive allowances.

But the Utilities’ depiction of the required nexus to retail customers would in effect foreclose the possibility of investing *any* portion of allowance revenues, as it would not be possible to rule out spillover effects to other sectors or customers of other load-serving entities.

²¹ Opening Comments of the Trust at 2.

²² Opening Comments of the Efficiency Council at 2-3.

²³ Id. As we note in our opening comments, the Council likewise highlights the positive experience in the RGGI states to date in following just such an approach.

²⁴ Opening Comments of DRA at 11.

²⁵ Id.

²⁶ Opening Comments of the Joint Utilities at 9 (citing to Section 95892(a) in the cap-and-trade rule).

²⁷ See Revised Proposal of the Joint Parties at 33-35.

That interpretation runs contrary to ARB’s explicit guidance elsewhere in developing the cap-and-trade rule, which directs the Commission to evaluate investing allowance revenues in additional clean energy programs.²⁸ The more likely interpretation of the required nexus to retail customers, and one which comports with ARB’s intent expressed elsewhere in developing the cap-and-trade rule, is that ARB wanted to be explicit about the reason it allocated allowances freely to the Utilities (who hold a compliance obligation only to the extent they own or operate electric generation): due to their retail relationship with customers they are uniquely situated to use allowance revenue on their customers’ behalf and must do so accordingly. But the Commission has final say on how allowance revenues can best be used to meet the needs of their customers.²⁹

3.1.6 Our Investment Proposal is Not Dependent on “Excess Revenues”

Finally, we clarify for the record that our investment proposal is not dependent on revenues that the Utilities will receive in excess of what ARB forecasts will be required to fully offset incremental generation costs from the cap-and-trade program on retail customers.³⁰ As we addressed in our opening comments, we recognize alongside the Utilities that ARB signaled its intention that allowance revenues could be used to offset AB 32 costs beyond the cap-and-trade program.³¹ Unlike the Agricultural Parties, however, our proposed allocation between investment and direct customer return is not dependant on residual “excess revenues”.³² Rather, we propose the Commission use the floor price in the cap-and-trade as the benchmark to determine the appropriate amount of revenue to allocate to each purpose.³³

²⁸ See, e.g., ARB Resolution 10-42 at 13. Moreover, this concern has not forestalled progress on the Commission’s existing clean energy programs, which undoubtedly have some spillover effects that benefit recipients other than IOU customers.

²⁹ As the Utilities themselves successfully argued before ARB in removing more explicit guidance on returning allowance revenues in the cap-and-trade rule.

³⁰ See Opening Comments of the Joint Utilities at 10-12.

³¹ See Opening Comments of the Joint Parties at 16. We also note ARB offered other guidance directly relevant to this proceeding that the Utilities conveniently dismiss or ignore entirely.

³² See Revised Proposal of the Joint Parties at 18-19.

³³ Sierra Club California proposes the Commission allocate additional allowance value for investment based on the market price.

3.1.7 Setting Aside a Portion of Allowance Revenues for Investment Will Not Cause a Delay in Returning Remaining Revenues to Customers

The Agricultural Parties suggest that due to the uncertainty in total allowances revenues that will be available each year, proposing to invest a portion of allowance revenues will necessarily “translate into years of delay” before customers receive revenues allocated for direct customer bill relief.³⁴ As noted above, our proposal avoids this concern by allocating revenues for investment based on the pre-established floor price in the cap-and-trade rule. The Commission would thus know in advance the total revenues available for investment, as the market clearing price would simply determine the specific rebate amounts available to each eligible customer. We are similarly not proposing the Commission hold off on returning revenues directly to customers while it takes the time to set up and administer an investment program. We recommend instead the Commission initiate a follow-up phase to this proceeding to determine the appropriate uses, criteria, and process to invest allowance revenues.

3.2 The Commission Can Provide Bill Relief to Customers Without Skewing Incentives for Efficiency and Conservation

3.2.1 The Utilities and Agricultural Parties Discount the Bill Reduction Benefits of Improved Efficiency

The Utilities and Agricultural Parties suggest that we do not propose providing any bill relief for non-EITE commercial and industrial customers.³⁵ They are correct insofar as we do not propose to provide direct rebates to these customers, but a cornerstone of our proposal involves targeting investment opportunities in the commercial and industrial sector to bring about bill reductions through reductions in consumption (particularly for customer segments that will be more constrained in their ability to pass through costs to consumers).³⁶ As California’s long experience with energy efficiency bears witness, reducing consumption through improved efficiency lowers customer bills far more effectively than maintaining low rates (despite paying more per kWh than the national average, for instance, Californians’ average monthly electric bills are more than a 25% lower than the rest of the U.S., and more than 40% lower than average

³⁴ Opening Comments of the Agricultural Parties at 5-6.

³⁵ Opening Comments of the Joint Utilities at 13; Opening Comments of the Agricultural Parties at 10-11.

³⁶ Revised Proposal of the Joint Parties at 23, 35.

bills in Texas and Florida).³⁷ The experience of the RGGI states documents the same trend: while electricity prices rise in the near term to cover carbon allowance costs, electricity customers enjoy a net benefit overall through improved efficiency financed with allowance revenues.³⁸

We do not discount the possibility that other non-EITE commercial and industrial customers will face similar constraints in passing costs through to consumers. We are amenable to the Commission exploring approaches to provide additional relief to these customers as appropriate. The only proposal on the table (volumetric return), however, comes at the expense of other critical objectives in this proceeding, undercuts incentives for efficiency and conservation, and ignores ARB's explicit direction.³⁹ We do not consider that a legitimate alternative.

3.2.2 ARB's Policy Direction and the Commission's Objectives in this Proceeding Support Returning a Share of Allowance Revenues to All Customers

The Utilities argue CARE and Tier 1 and Tier 2 customers should not receive allowance revenues as they will not face direct costs in the form of rate increases from the cap-and-trade program, and any indirect costs they face are not the Commission's responsibility (as they will not arise from the electricity sector and are too speculative in any event).⁴⁰ We first note we are not suggesting that non-CARE, 'Tier 1' and 'Tier 2' customers are in fact low income customers (since customers' usage moves between tiers depending on seasonal and other factors, we do not use the terminology 'Tier 1' or 'Tier 2' customers at all).⁴¹ We also reiterate that we are mindful of the differential cost impacts that the prevailing rate restrictions will result in for residential customers, and propose rebate amounts vary by household to account for legitimate variation in electricity usage that may push certain households into the upper tiers despite meaningful

³⁷ See EIA (average rates and bills data current as of November 2011), available at: <http://www.eia.doe.gov/cneaf/electricity/esr/table5.html>.

³⁸ Analysis Group, "the Economic Impacts of the Regional Greenhouse Gas Initiative on Ten Northeast and Mid-Atlantic States: Review of the Use of RGGI Auction Proceeds from the First Three-Year Compliance Period," p. 4-5 (Nov. 2011), available at: http://www.analysisgroup.com/uploadedFiles/Publishing/Articles/Economic_Impact_RGGI_Report.pdf

³⁹ ARB, "California's Cap-and-Trade Program: Final Statement of Reasons," at 2307 (Oct. 2011), available at: <http://www.arb.ca.gov/regact/2010/capandtrade10/fsor.pdf> (observing "volumetric return of allowance value eliminates incentives for greenhouse gas reduction strategies such as conservation of electricity, efficient combined heat and power, and distributed electrical generation").

⁴⁰ Opening Comments of the Joint Utilities at 14.

⁴¹ Id.

efficiency and conservation efforts.⁴² We do not propose this as a “concession,” but as a means to give effect to ARB’s recommendation to maintain accurate and transparent price signals while providing bill relief through separate payments.⁴³ We also contend providing a demonstrable benefit to retail customers in the form of an off-bill payment will facilitate greater public support for the program than keeping customers largely in the dark through rate credits (a view shared by DRA).⁴⁴

We remain open to suggestions on how to mitigate differential impacts and work through other practical challenges associated with providing separate payments. Working with the Utilities, we are confident the Commission can build from our proposal to provide direct bill relief to residential customers in a manner consistent with ARB’s design recommendations and the objectives set out in this proceeding – which includes addressing the disproportionate impacts low income customers will face from carbon pricing and climate change.⁴⁵

3.2.3 The Relative Inelasticity of Short-Term Residential Electricity Demand Does Not Discredit the Long-Term Value of Maintaining Transparent Price Signals and Providing Customer Relief Through Other Means

The Utilities argue that due to the relative inelasticity of residential electricity demand, maintaining the carbon price in retail rates will have little to no effect on customer efficiency and

⁴² See Revised Proposal of the Joint Parties at 27-28.

⁴³ See note 39, supra at 2307 (noting “[we] continue to believe that rebates to residential customers should be made as separate payments, and not simply deducted from consumer bills.”).

⁴⁴ Opening Comments of DRA at 5 (noting “DRA believes that the demonstrable benefit of an annual payment as direct bill relief will garner more public support than if there is no tangible and transparent benefit, yet still significant rate increases because of AB 32 programs other than cap-and-trade”). TURN also supports returning allowance revenues outside of rates, noting the Utilities’ approach would “unnecessarily mask the fact that AB 32 revenues are being credited back to customers.” Opening Comments of TURN at 5 (proposing to return revenues on-bill as a separate line item).

⁴⁵ See D.08-10-037, OP 15 (noting “we recommend that ARB require all auction revenues from allowances allocated to the electricity sector be used to finance investments in energy efficiency and renewable energy or for bill relief, *especially for low income customers*”) (emphasis added); Scoping Memo, Appendix A at A7 (asking parties to explain the degree to which the anticipated costs to low income households resulting from cap-and-trade and climate change are recognized and addressed, given the state’s and the Commission’s longstanding commitment to protect vulnerable communities from adverse outcomes); ARB, Board Resolution 10-42 (directing the Executive Officer to work with the Commission...to ensure allowance value directed to the Utilities is used for the benefit of residential, commercial, and industrial ratepayers that might otherwise face *indirect* costs from the implementation of this regulation, with particular consideration of the potential for impacts from this program on low-income customers) (emphasis added).

conservation efforts over the course of the program, and is not a cost-effective means of achieving emission reductions.⁴⁶ The Commission should not accept either assertion.

A low elasticity of electricity demand suggests that efficiency and conservation efforts in direct response to price increases will be modest in the short-run. The cap-and-trade program is designed to encourage changes in consumer behavior over a much longer period,⁴⁷ however, and elevate the visibility of energy efficiency opportunities long-recognized as being undervalued and overlooked by consumers due to a range of systemic market barriers.⁴⁸ Over time, consumers are more likely to modify their consumption behavior if presented with the appropriate combination of price signals and attractive and accessible options to overcome barriers to improved efficiency. In contrast, offsetting costs in direct proportion to consumption (as the Utilities propose) will prevent any impact on customer bills from carbon pricing despite untapped conservation or efficiency opportunities, and eliminates the opportunity to communicate to customers the link between their usage and emissions.⁴⁹

Second, the Utilities' argument that preserving the carbon price is a costly method of reducing emissions – due to the inelasticity of residential electricity demand – is flawed and incomplete since it ignores the counterpart to proposals that recommend maintain transparent pricing: to compensate customers through other means (e.g., separate transfers or rebates). It is true that the price increase, by itself, will result in a loss of consumer surplus (the difference between what consumers are willing to pay versus what the market requires that they pay). Yet, as we propose – following the recommendation of the EAAC⁵⁰ and ARB⁵¹ – the Commission can more than offset the 'loss' in consumer surplus by returning allowance revenues in the form of

⁴⁶ See Initial Proposal of the Joint Utilities (Appendix A & B).

⁴⁷ And as DRA draws attention to, the price elasticity of demand can be significantly greater in the long-run. See, e.g., M.A. Bernsetein and J. Griffin, "Regional Differences in the Price Elasticity Demand for Electricity," RAND Corporation Subcontract Report, National Renewable Energy Laboratory, February 2006, Figures 4.5, 4.6, pp 29-32. ; Massimo Filippini, "Short and long-run time-of-use price elasticities in Swiss residential electricity demand," CEPE Working Paper No. 76, Center for Energy Policy and Economics – Swiss Federal Institutes of Technology, July 2010, p16 (estimating long-run residential price elasticity to vary between -1.60 and -2.26 during peak demand periods and between -1.27 and -1.65 during off-peak periods).

⁴⁸ See, e.g., ETAAC report and EAAC report, supra note 4; Harcourt et al., "Energy Efficiency Financing in California," (July 2011).

⁴⁹ The latter concern is echoed by the IEP, who note that the Utilities' approach "undermines the Commission's ability to inform the customer of the link between the source of the revenues and their use, and it further weakens consumers' understanding and appreciation of how the C&T program relates to the transformation from a fossil-based electric generation sector to a low- or no-carbon future." See Opening Comments of the IEP at 4; see also Opening Comments of the Efficiency Council at 9.

⁵⁰ See note 4 supra.

⁵¹ See note 39, supra.

rebates⁵² and investing in efficiency and other programs to reduce consumption.⁵³ Designed effectively, as RGGI has shown, this approach maintains price signals to encourage modifications in consumption patterns over the long-run, while providing direct bill relief and investing in efficiency programs to mitigate future customer costs.⁵⁴

3.2.4 ARB's Policy Direction in Developing the Cap-and-Trade Rule Unequivocally Directs the Commission to Maintain a Retail Price Signal through the Return of Allowance Revenues

The DACC asserts that we have not established that using allowance revenues to subsidize electricity rates for non-EITE commercial and industrial customers is at odds with ARB's design principles in developing the cap-and-trade program.⁵⁵ As we have documented, ARB allocated allowances to the Utilities contingent on the "explicit understanding that value would not be used to skew carbon pricing or reduce incentives for greenhouse gas reductions."⁵⁶ The DACC proposes to return allowance revenues to commercial and industrial customers volumetrically in rates, however, which ARB explicitly disavowed because it "eliminates incentives for greenhouse gas reduction strategies" such as conservation and more efficient use of electricity.⁵⁷ Accordingly, the record developed in support of the cap-and-trade program readily supports a finding that ARB did not intend the Commission to use allowance revenues to "skew carbon pricing" in the commercial and industrial sector by subsidizing distribution rates.

⁵² To the extent feasible, we propose that rebates be provided to customers before price increases so these funds can help finance efficiency measures to mitigate the impact of higher prices.

⁵³ Assuming, as seems reasonable, a pricing and lump-sum transfer policy moves the price of carbon closer to its true marginal external cost. Indeed, designed effectively, the policy can achieve a net social gain (measured as the reduction in deadweight loss achieved by lowering pollution levels).

⁵⁴ See note 38, supra.

⁵⁵ Opening Comments of the DACC at 4.

⁵⁶ See note 39, supra at 2307. DRA similarly notes that "ARB has made it clear that the intent of the cap-and-trade regulation is to embed a carbon price in retail electricity rates as well as wholesale electricity rates, in order to create the proper incentives for conservation by end users of electricity as well as for efficient dispatch in the wholesale market." Opening Comments of DRA at 2.

⁵⁷ See note 39, supra at 2307. That view was also reinforced in the final ARB Board resolution accompanying final adoption of the cap-and-trade program, where the Board found that should allowance revenues be returned directly to utility customers, they be returned in a manner "consistent with State efforts to promote energy efficiency and energy conservation." ARB, Board Resolution 11-32 (October 20, 2011), available at.

<http://www.arb.ca.gov/regact/2010/capandtrade10/res11-32.pdf>

4 Conclusion

We appreciate the opportunity to offer these reply comments and look forward to participating in the remainder of this proceeding.

Dated: February 14, 2012

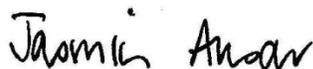
Respectfully submitted,



Alex Jackson
Natural Resources Defense Council
111 Sutter St. 20th Floor
Tel: (415) 875-6100
Fax: (415) 875-6161
ajackson@nrdc.org



Andy Katz
Sierra Club California
801 K Street Suite 2700
Sacramento, CA 95814
510-848-5001
andykatz@sonic.net



Jasmin Ansar
Union of Concerned Scientists
2397 Shattuck Avenue, Suite 203
Berkeley, CA 94704
510-809-1570
jansar@ucsusa.org



National Consumer Law Center
1001 Connecticut Avenue, NW, Suite 510

Washington, DC 20036-5528
202-452-6252
owein@nclc.org



Barry Vesser
Climate Protection Campaign
P.O. Box 3785
Santa Rosa, CA. 95402
(707) 525-1665
bvesser@climateprotection.org



Ryan Briscoe Young
The Greenlining Institute
1918 University Avenue, 2nd Floor
Berkeley CA, 94704
510-926-2018
ryany@greenlining.org



Jennifer K. Berg
Local Government Sustainable Energy
Coalition
P.O. Box No. 3629
Oakland, CA 94609

(510) 839-0688 x 213
jennberg@comcast.net



Ross Nakasone
California Housing Partnership Corporation
369 Pine Street, Suite 300
San Francisco, CA 94104
Tel: 415-433-6804 x310
Fax: 415-433-6805
RNakasone@chpc.net



Tam Hunt
Community Environmental Council
26 W. Anapamu St., 2nd Floor
Santa Barbara CA 93101
(805) 214-6150
tam@communityrenewables.biz