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

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies	R.06-04-009
AB 32 Implementation	07-OIIP-01

REPLY COMMENTS OF THE ENERGY PRODUCERS AND USERS COALITION AND THE COGENERATION ASSOCIATION OF CALIFORNIA ON ALLOWANCE ALLOCATION ISSUES

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BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA
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Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies	R.06-04-009
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REPLY COMMENTS OF THE ENERGY PRODUCERS AND USERS COALITION AND THE COGENERATION ASSOCIATION OF CALIFORNIA ON ALLOWANCE ALLOCATION ISSUES

The Energy Producers and Users Coalition[1] (EPUC) and the Cogeneration Association of California[2] (CAC) (jointly, EPUC/CAC) submit the following reply comments on the allocation of greenhouse gas (GHG) emissions allowances under a cap and trade program, pursuant to the October 15, 2007 Administrative Law Judge's Ruling.

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1 EPUC is an ad hoc group representing the electric end use and customer generation interests of the following companies: Aera Energy LLC, BP West Coast Products LLC, Chevron U.S.A. Inc., ConocoPhillips Company, ExxonMobil Power and Gas Services Inc., Shell Oil Products US, THUMS Long Beach Company, Occidental Elk Hills, Inc., and Valero Refining Company – California

2 CAC represents the power generation, power marketing and cogeneration operation interests of the following entities: Coalinga Cogeneration Company, Mid-Set Cogeneration Company, Kern River Cogeneration Company, Sycamore Cogeneration Company, Sargent Canyon Cogeneration Company, Salinas River Cogeneration Company, Midway Sunset Cogeneration Company and Watson Cogeneration Company.

I. OVERVIEW AND SUMMARY OF RECOMMENDATIONS

The opening comments filed by EPUC/CAC on allowance allocation issues address most of the issues raised by other parties in their comments. These reply comments are therefore limited to addressing the following points raised by Southern California Edison Company (SCE), Pacific Gas and Electric Company (PG&E), The Utility Reform Network (TURN) and the Division of Ratepayer Advocates (DRA):

- SCE's proposal to allocate allowances based on economic harm should be rejected; the mechanics of the proposal are unclear, and the proposal relies on questionable assumptions, conflicts with AB 32 objectives, and is vulnerable to challenge under the Dormant Commerce Clause (DCC);

- TURN's statement that an auction implicitly provides credit for early action efforts is not true for combined heat and power (CHP) investments, making separate emission counting protocols necessary for these resources if an auction were employed;

- PG&E's allocation proposal should be rejected on the basis that it is unnecessarily complex, could affect the operation of multi-sector trading market, undermines the Commission's efforts to further competition, compromises the effectiveness of demand response programs, and makes the GHG regulations vulnerable to challenge under the DCC; and

- DRA's proposal to regulate only in-state sources should be rejected on the basis that it will not satisfy AB 32's directives and will disadvantage in-state resources in competition with imports.

We discuss each of these issues below.

II. SCE'S ECONOMIC HARM THEORY RELIES ON QUESTIONABLE ASSUMPTIONS AND RAISES PRACTICAL QUESTIONS

SCE recommends that allowances be allocated to entities that will suffer economic harm as a result of GHG regulation. According to SCE, entities that will suffer economic harm are limited to generators that have higher emissions than the "marginal generating unit" and to load-serving entities that procure power from these sources. This proposal raises a number of important concerns:

(1) SCE fails to provide detail sufficient to clarify the likely mechanics of its proposal;

(2) SCE assumes that the market clearing price will immediately and fairly compensate the marginal generating unit for GHG compliance costs; and

(3) SCE's proposal, without further refinement, would injure certain generators regardless of their relative emissions levels, including generators with existing bilateral contracts and generators that are price-takers, relying on administratively determined prices that do not allow recovery of all GHG compliance costs.

Due to these factors, reliance on economic harm to allocate allowances is not as simple as SCE contends.

Debate remains regarding whether the market clearing price will allow recovery of all GHG compliance costs even for a marginal generating unit. As discussed in EPUC/CAC's opening comments, there is insufficient information and no national experience that can be used to forecast GHG compliance costs.[3] In addition, the extent to which a firm will be able to pass on these costs will depend upon a wide variety of conditions, as NERA points out.[4] Consequently, it may not be reasonable for California to assume that the market clearing price will adequately compensate even a marginal generating unit for the full costs of GHG regulations.

Even if the market fully reflected compliance costs for the marginal generator, SCE's assumptions are too simplistic to accurately reflect the full scope of entities which will suffer economic harm. As noted in EPUC/CAC's

[3] *See, e.g.*, EPUC/CAC Opening Comments at 11.
[4] *Id.*

opening comments, contracts executed before the final implementation of AB 32 are not likely to specifically or adequately address responsibility for carbon-related costs.[5] As a result, existing bilateral contracts are not likely to allow a generator to recover GHG compliance costs. Likewise, those generators that are price-takers of administratively determined prices (such as CHP Qualifying Facilities (QFs)) have no current means of recovering their GHG compliance costs. The imposition of these compliance costs can drastically impact project margins. As explained in EPUC/CAC's opening comments, even a conservative carbon adder of \$8/MTCO_2 would reduce project margins by 142.9% for QFs relying on short run avoided cost and 58.4% for QFs relying on long-run avoided cost.[6] In short, identifying entities suffering economic harm will not be as clear-cut as SCE claims.

The questionable nature of the above two assumptions exemplifies the complex and confusing nature of SCE's proposal. SCE's opening comments also provide little detail about the mechanics of the allocation process. As a result, it remains unclear exactly how allowances would be allocated. It is also noteworthy that identifying a single emissions rate for the marginal generating unit – a data point that would be required under SCE's proposal -- is likely to be a very contentious process.

In short, the SCE proposal should be rejected on the basis that it rests on dubious assumptions and leaves important practical questions unanswered.

5 EPUC/CAC Opening Comments at 24-27.

6 Comments of the Energy Producers and Users Coalition and the Cogeneration Association of California on Allowance Allocation Issues (EPUC/CAC Comments), at 25-26.

III. ADOPTION OF SCE ALLOCATION PROPOSAL WILL MAKE GHG REGULATION VULNERABLE TO CHALLENGE UNDER DORMANT COMMERCE CLAUSE

SCE's proposal is susceptible to challenge under the Dormant Commerce Clause (DCC). As explained in EPUC/CAC's opening comments to the MAC Report, the negative aspect of the DCC, "*limits the power of the States to erect barriers against interstate trade.*" [7]

SCE's proposal would create barriers to interstate commerce. Under SCE's proposal, allowances provided to in-state entities suffering economic harm would be available to out-of-state entities only if they are in long-term contracts to supply power to California.[8] However, the allowances would be available to in-state entities whether or not they hold long-term contracts to supply the California market. This approach imposes facially discriminatory treatment on foreign firms, to their economic disadvantage, burdening interstate commerce.

SCE notes that those out-of-state entities who are not in long-term contracts to supply power to the California market can make sales to some other non-GHG regulated region.[9] To begin with, SCE is explicitly encouraging the contract shuffling California is attempting to prevent. Moreover, an out-of-state seller could reasonably argue that SCE's method creates economic barriers to imports. Allowances would not be available to an out-of-state seller who is not in a long-term contract but would be available to a similarly situated in-state producer. As explained in EPUC/CAC's opening comments, regulations that only

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7 *Oregon Waste Systems, Inc. v. Dept. of Environmental Quality of the State of Oregon, et al.*, 511 U.S. 93, 98 (1994).

8 SCE Opening Comments, at 7.

9 *Id.*

marginally further health and safety but create substantial barriers to commerce will be invalidated.[10] Adoption of SCE's allocation proposal therefore will make the adopted regulations vulnerable to a DCC challenge.[11]

IV. TURN'S STATEMENT THAT AUCTION IMPLICITLY RECOGNIZES EARLY ACTION EFFORTS IS NOT VALID FOR CHP RESOURCES

TURN recommends the use of an auction to capture the value of early action efforts.[12] It assumes that all emission-reducing efforts result in a reduction in on-site emissions. As explained in EPUC/CAC opening comments, this is not true of CHP investments.[13]

TURN's thinking could be applied to a load-based scenario under an auction approach. Those LSEs which have reduced their portfolio emissions over time would be forced to purchase fewer allowances per kWh of load served, with a lower overall carbon cost to their ratepayers. This thinking also could be applied in the case of a source based scenario. Those generators using technologies with higher efficiencies would be required to purchase fewer allowances per kWh generated than those with older technology.

TURN's thinking cannot, however, be applied to CHP installation. When an industrial site invests in a high efficiency CHP plant, total emissions from the production of electrical and thermal energy used by the industrial consumer are

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10 *Kassel v. Consolidated Freightways Corp of Delaware*, 450 U.S. 662, 670 (1981).

11 EPUC/CAC Opening Comments, at 37..

12 Under a first seller regulatory approach, TURN advocates the use of an auction to allocate allowances, in part, on the basis that "*it avoids administrative determination of credits for early adopters, by rewarding early adoption through the market mechanism (i.e. requires purchasing fewer credits, such that early adoption is its own reward and is encouraged from the moment an auctioning system is announced.*" See TURN Opening Comments, at 10-11.

13 EPUC/CAC Comments, at 15-16, 18-24.

decreased. In particular, as explained below, the emissions attributable to CHP are significantly less than the emissions released as a result of separate central power generation and industrial boiler installations. *While global emissions decrease, however, emissions at the industrial site, are higher, thereby increasing a CHP customer's GHG allowance requirements.*

An auction system, therefore, can penalize a CHP facility by requiring it to purchase more allowances than it would have needed had it not invested in CHP. In other words, the industrial firm has taken an early action to reduce both its indirect and direct emissions, but sees no direct GHG reduction on site – only increased carbon costs. For these reasons, if an auction were employed, adjustments for CHP would be required as detailed in EPUC/CAC's opening comments.

V. PG&E ALLOCATION SYSTEM SHOULD BE REJECTED

PG&E proposes that allowances be allocated to LSEs for free, and LSEs would then auction allowances to the remaining market participants.[14] PG&E's allocation proposal should be rejected on the basis that it (i) is unnecessarily complex, (ii) hinders multi-sector trading, (iii) undermines the state's efforts to further competition, (iv) compromises the effectiveness of demand response programs, and (v) makes the regulation vulnerable to challenge under the DCC. These factors weigh in favor of rejecting PG&E's allocation proposal.

PG&E's proposal unnecessarily complicates the allowance distribution mechanism. PG&E proposes that allowances be allocated to LSEs who would

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14 PG&E Opening Comments, at 4-5.

then auction allowances to generators responsible for compliance.[15] This two-step allocation process adds complexity to the process with little, if any, benefit. The only difference between PG&E's proposal and a direct auction to regulated firms is that the entity in charge of receiving and disbursing auction revenues will be the LSE, rather than another independent organization or state entity. While this may achieve a beneficial end if it allows retention of revenues for GHG reduction projects in the sector, it is not the only way to achieve this objective. The same goal could be achieved through a centralized, multi-sector auction with a material allocation to electricity sector programs.

PG&E's proposal also compromises the goal of a multi-sector market-based cap and trade program. The goal of a market-based cap and trade program should be multi-sector trading. This objective would be best served by a single, multi-sector auction that is transparent and fair. PG&E's proposal would require a separate auction for the electricity sector with potentially different rules and different market values. Splitting up the auction process in this manner would affect the development of an efficient multi-sector trading market.

PG&E's proposal likewise will hamper the state's efforts to further competition. As a preliminary matter, it will give one segment of the market – LSEs -- control over all sector allowances for free. Some of the LSEs which will receive allowances have their own investment in generation, creating a risk that auction revenues may be used inappropriately to further an LSE's own generation development. At a minimum, this approach requires heightened oversight of utility expenditures and ratemaking to prevent this result. For this

15 PG&E Opening Comments, at 4-5.

reason, putting LSEs in charge of auctioning allowances that must be purchased by the LSE and its competitors provides LSEs an undue competitive advantage over other generation sources. As such, it will hinder the state's efforts to facilitate competition.

PG&E's proposal, directed to mitigating ratepayer costs by returning auction revenues directly through consumer rates, will compromise efforts to encourage demand response. As TURN noted in its opening comments, it is anticipated that the investor-owned utilities will spend approximately $4 billion to put an advanced metering infrastructure in place to further the use of demand response programs.[16] In contrast, PG&E's allocation proposal will mitigate ratepayer costs, dampen price signals and lower ratepayer response. To give proper effect to ratepayers' investments in demand response programs, therefore, PG&E's proposal cannot be adopted.

Finally, PG&E's proposal will expose the adopted GHG regulation to a greater risk of challenge under the DCC. As explained in the EPUC/CAC opening comments, the key in a challenge under the DCC is the existence of discrimination.[17] Discrimination is defined as differential treatment which benefits in-state *economic* interests and burdens out-of-state interests.[18] As noted in the opening comments, the stated objective of promoting health and safety must be carried out in reality.[19] Regulations that only marginally further health and safety

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16 TURN Opening Comments, at 20.
17 EPUC/CAC Opening Comments, at 35.
18 *Oregon Waste Systems, Inc. v. Department of Environmental Quality of Oregon*, 511 U.S. 93, 99 (1994).
19 EPUC/CAC Opening Comments, at 37.

but create substantial barriers to commerce will be invalidated.[20] Since the objective of PG&E's proposal is to mitigate in-state ratepayer impact, an out-of-state marketer or generator could reasonably argue that such a regulation is meant to extract payment from out-of-state sellers for the purpose of lowering cost impacts on in-state residents. Unlike statutes that are focused on health and safety issues, no legal presumptions are available to ensure that economically-motivated regulation can withstand DCC attack. For this reason, PG&E's proposal would be more susceptible to challenge than a regulation that invests auction proceeds in other GHG-reducing efforts.

VI. DRA'S PROPOSAL TO IMPOSE GHG REGULATIONS SOLELY ON IN-STATE SOURCES WILL DISADVANTAGE IN-STATE RESOURCES

DRA proposes a regulatory approach which imposes GHG regulations solely on in-state resources. DRA's comments note concern that the use of default emission factors for imports, facilitates gaming and leakage.[21]

DRA's proposal may avoid issues related to the regulation of imports but it should be rejected on the following grounds:

(i) A regulatory approach which fails to address the regulation of imports may fail to adequately achieve the objectives of AB 32; and

(ii) Where GHG regulations apply only to in-state resources, the cost of in-state generation will be higher than the cost of generating out-of-state using the same technologies; this difference will disadvantage in-state resources in competing with imports.

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20 *Kassel v. Consolidated Freightways Corp of Delaware*, 450 U.S. 662, 670 (1981).

21 DRA Opening Comments, at 3.

VII. CONCLUSION

For all of the foregoing reasons, and for the reasons stated in EPUC/CAC's opening comments, the Commissions' recommendation to CARB for the electricity sector should be based on an administrative allocation of allowances. Allowance allocation to CHP facilities should be based on the double-benchmarking approach employed in the EU-ETS. If, however, the recommendation includes some portion of auction, impacts must be expressly mitigated for existing contracts, administratively determined price-takers and CHP facilities as delineated in EPUC/CAC's opening comments.

November 14, 2007

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Karen Terranova hereby certify that I have on this date caused the attached **Reply Comments of the Energy Producers and Users Coalition and the Cogeneration Association of California on Allowance Allocation Issues** in R06-04-009 to be served to all known parties by either United States mail or electronic mail, to each party named in the official attached service list obtained from the Commission's website, attached hereto, and pursuant to the Commission's Rules of Practice and Procedure.

Dated November 14, 2007 at San Francisco, California.

Karen Terranova

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Attachments: #890234 v1 - Revised Reply Comments.pdf

Docket Clerk: Attached is R. 06-04-009 and Docket No. 07-OIIP-01 SMUD's Reply Comments on Allowance Allocation Issues for docketing in this matter. Hard copy will follow via U.S. mail. If you have any questions or have problems opening this document, please contact me at the number indicated below.

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BEFORE THE PUBLIC UTILITIES COMMISSION
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Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	))))))	Rulemaking 06-04-009 (Filed April 13, 2006)

ENERGY RESOURCES CONSERVATION
AND DEVELOPMENT COMMISSION
OF THE STATE OF CALIFORNIA

In the Matter of AB 32 Implementation: Greenhouse Gases.	))))))	Docket 07-OIIP-01

SACRAMENTO MUNICIPAL UTILITY DISTRICT'S REPLY COMMENTS ON THE ALLOWANCE ALLOCATION ISSUES

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SACRAMENTO MUNICIPAL UTILITY DISTRICT'S REPLY COMMENTS ON THE ALLOWANCE ALLOCATION ISSUES

Based upon the direction provided by Administrative Law Judge TerKeurst, the Sacramento Municipal Utility District (SMUD) herein provides comments on two issues discussed in the joint California Energy Commission (CEC) and California Public Utilities Commission (CPUC) workshop held on November 5, 2007 ("Joint Workshop").

1) The similarities and differences between the allocation methods proposed by SMUD and the Los Angeles Department of Water and Power (LADWP); and

2) The auction structure design in light of the overall California greenhouse gas reduction scheme.

COMPARISON OF SMUD'S AND LADWP'S ALLOWANCE ALLOCATION PROPOSALS

SMUD's proposal was and is a compromise allocation method providing benefits to both high carbon utilities and those with early voluntary reductions. The following table and discussion respond to remarks made at the Joint Workshop that the proposals by LADWP and SMUD are largely the same regarding allocation of allowances. Workshop Transcript at 180. Although there are many similarities, there are also differences. We offer our comments to clarify the differences but not to detract from the similarities. This discussion begins with a side by side comparison of the proposals in a table and follows with a discussion of the differences. SMUD has attempted to accurately portray LADWP's proposal as best SMUD understands LADWP's allocation plan.

COMPARISON OF SMUD AND LADWP ALLOCATION PROPOSALS			
Factor	**SMUD's Proposal**	**LADWP's Proposal**	**Similarities & Differences**
2012 Allocation	• Historic/grandfather based on 2004 to 2006 • Administrative allocation	• Historic/grandfather based on most recent multi-year available data (pp.2, 19)*	• Administrative allocation beginning

COMPARISON OF SMUD AND LADWP ALLOCATION PROPOSALS			
Factor	**SMUD's Proposal**	**LADWP's Proposal**	**Similarities & Differences**
		• Administrative Allocation (pp.2, 6)	with historic/ grandfather
Reductions over compliance period	• Smooth transition from historic to benchmark by 2020 • SMUD defines benchmark as an output based allocation scheme (% of retail sales in the state)	• Acceptable hybrid starts with historic and ends with benchmark as the 2020 goal, if – slower reduction in early years for high carbon entities (p.13)	**• SMUD's proposal uses an output based bench-mark for allocations in 2020**
Compliance Cap	• Cap over compliance period between 2012 and 2020 should reflect ability to reduce carbon	• Declining annual cap (p.2)	**• The cap should reflect ability to reduce carbon**
New entrants or growth	• Adjust allocation each year to address new entrants or growth	• Create a new entrant reserve (p. 20)	**• By resetting the allocations each year load changes can be addressed**
Period for full transition to benchmark	• 2012 to 2020, full transition to output based benchmark by 2020		**• Transition to output based bench-mark needs to be complete by 2020**
Auction	• Recommend against auction because regulation will drive reductions • If auction is used, begin very small and grow with adequate oversight • Participants limited to those who need allowances • Auctions add unnecessary costs	• Oppose auction (p.7) •Auctions add unnecessary costs (p.7)	• Auctions will not drive the biggest reductions. • Auctions add costs and are not supported

* All citations are to the Opening Comments of the LADWP on the Administrative Law Judges' Ruling Requesting Comments on Allowance Allocation Issues ("LADWP's Comments"), R: 06-04-009 and Docket No. 07-OIIP-01, Dated October 31, 2007.

Similarities between SMUD's and LADWP's proposals

Both SMUD and LADWP recommend against using an auction for the regulated electric utility industry. Both see the auction for the electric utility industry as an additional, unnecessary cost adder. Both recommend starting in 2012 with an administrative allocation of allowances based upon a historic/grandfathered scheme. Both provide allowances for growth and new entrants albeit by different means. LADWP proposes a reserve and SMUD proposes an annual update of the allocations. Both proposal move to a form of benchmark by 2020. But, each has a different definition of the "benchmark" to be used to set the allowance allocation in 2020.

2020 allowance calculation should use an updated output based benchmark

SMUD does not have a clear understanding of LADWP's definition of "benchmark" as used in their "acceptable hybrid" approach. The Administrative Law Judge's Ruling Requesting Comments and Noticing Workshop on Allowance Allocation issues ("ALJ Ruling") provided a definition of "benchmarking" from the Market Advisory Committee.

> "An allowance or allocation method to which allowances are distributed by setting a level of permitted emissions per unit of input or output" (e.g. fuel used or sales to customer (pounds (lbs)/megawatt-hour or lbs/million Brutish thermal units (MMBtu) (MAC Report, p.90.)

ALJ Ruling at 7. This definition specifically refers to using either fuel use or sales to customer as a basis for calculating the benchmark. LADWP's Comments state in numerous places that any use of a sales based allocation scheme is unacceptable. LADWP's Comments, pp. 14, 16. Therefore, SMUD is unclear about what LADWP means when they refer to "benchmark". SMUD representatives asked representatives of LADWP at the Joint Workshop to clarify what they thought the "benchmark" as they used the term would be in 2020.

> Ms. Luckhardt: . . .You were saying that everyone should reach a common benchmark. Did you have a rough calculation of what you thought that could be – that would be?

Ms. Johnson Kowal: I do not.

> Recorded transcript of the Joint Workshop of the California Energy Commission and California Public Utilities Commission, November 5, 2007, ("Workshop Transcript") pp. 20-21.

Therefore, SMUD is concerned about adopting or agreeing to a proposed solution where a critical component, how the benchmark will be calculated is unclear.

In order for a true "compromise solution" to work, it must acknowledge both the future expenses faced by high carbon utilities and the investments already made and included in the rates of low carbon utilities. SMUD advocates an allocation of allowances no later than 2020 based entirely upon the percent of electrical energy served in California, retail sales, with updating and adjustments for energy efficiency. In an attempt to clarify the differences SMUD refers to their benchmark as an "output based benchmark". A calculation based upon electric energy served/electric sales is necessary to recognize the early voluntary reductions made by entities like SMUD. Furthermore, moving to an output based benchmark no later than 2020 will also reward reductions in carbon by all entities between now and 2020.

Therefore, although the two methods are similar, the calculation in 2020 of the benchmark is different. SMUD believes by 2020 the entire allowance allocation needs to be based upon an updated benchmark calculated from electric energy served/energy sales or a similar metric that recognizes and encourages early carbon reductions.

The transition to output based benchmark must be a smooth line from 2012 to 2020

The changeover from historic/grandfathered allocation in 2012 to benchmark in 2020 must be a smooth line to treat all entities fairly. To maintain historic/grandfathered allowance allocation throughout the transition period simply rewards high emissions as a means of maintaining high allowances. All entities have been aware of the need to reduce carbon emissions at least since the Secretary of State chaptered Assembly Bill 32 in September of 2006. Official California Legislative Information, Assembly Bill 32 (2005-2006 Legislative Session), Complete Bill History. In essence, all entities have been on notice and will have had five years to begin to transition to a reduced carbon future prior to 2012. Therefore, the transition to benchmark should not be weighted to favor high carbon entities throughout the compliance period but should instead move smoothly from the historic/grandfathered system to the benchmark system no later than 2020.

Furthermore, by creating a smooth transition, entities that begin reducing their carbon in the initial years are rewarded for their progress throughout the period between 2012 and 2020. Using historic/grandfather throughout the 2012 to 2020 period would provide an incentive to delay carbon reductions. SMUD believes progress toward reducing the carbon in the electricity supplied to Californians should be rewarded by the allocation scheme.

Transition to output based benchmark needs to be complete by 2020

The change over to benchmark by 2020 is especially important given the questions about the carbon reduction strategies for California beyond 2020. Future legislation will most likely dictate the next steps in greenhouse gas reductions for California beyond 2020. The current program needs to be complete by 2020 and ready to take on the next challenge without ongoing transitional issues.

The allocation scheme should be updated each year

Both LADWP and SMUD provide a method for accommodating growth and new entrants. SMUD advocates for an update of the allocation scheme for allowances each year. By updating, new entrants, load growth or load shift between entities can be taken into account. LADWP proposes setting up a reserve to handle these issues. LADWP's Comments at p.20. Under SMUD's proposal, the allocation of allowances would change each year in the transition from historic/grandfathered to benchmark. Therefore, changes or increases in load would be addressed each year and a reserve would not be required.

The declining annual cap has not been fully addressed in these questions

LADWP presents some information about a declining annual cap. SMUD agrees the cap must decline from 2012 to reach the 1990 goal in 2020. How the cap is distributed, calculated and whether it declines in steps or along a curve has not been fully addressed in these questions. SMUD would defer determinations of caps to a future response, but would advocate for a cap that considers the relative ability of each entity to reduce emissions.

AUCTION DESIGN SHOULD CONSIDER THE BROADER GREENHOUSE GAS REDUCTION PROGRAM

SMUD does not support auction of allowances for the regulated utility industry. Should an auction be used, SMUD urges the CEC and CPUC to design an auction in light of the requirements for the entire state of California. Meeting the greenhouse gas 2020 goal for California will take participation from all sectors. The electricity sector is only one part of the solution. Furthermore, since solutions for other industries may be to electrify current operations, just as LADWP is working to electrify ports, any auction scheme needs to take these load shifts and potential reduction opportunities into account. LADWP's Comments at p. 3. Thus, SMUD urges the CPUC and CEC to coordinate any auction design carefully with the California Air Resources Board so consideration of all industries that need to reduce emissions can be adequately taken into account.

CONCLUSION

SMUD has presented an allowance allocation proposal that in many ways is similar to the proposal presented by LADWP. But, there are important differences between the proposals including the definition of "benchmark". SMUD offers these comments to foster a better understanding of the differences but this discussion of differences should not detract from the considerable similarities.

Dated: November 14, 2007

Respectfully submitted,

/s/

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the attached:

SACRAMENTO MUNICIPAL UTILITY DISTRICT'S REPLY COMMENTS ON THE ALLOWANCE ALLOCATION ISSUES

on all known parties to R. 06-04-009 and CEC Docket No. 07-OIIP-01 by transmitting an e-mail message with the document attached to each party named in the official service list. I served a copy of the document on those without e-mail addresses by mailing the document by first-class mail addressed as follows:

See attached service list

Executed this 14th day of November 2007, at Sacramento, California.

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