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07-011P-1	
DATE	JAN 0 8 2008
RECD.	JAN 0 8 2008

**DOCKET 07-011P-01
CALIFORNIA ENERGY COMMISSION
REPLY COMMENTS OF
PACIFIC GAS AND ELECTRIC COMPANY (U 39 E) ON
TYPE AND POINT OF REGULATION OF
GREENHOUSE GAS EMISSIONS IN THE NATURAL
GAS SECTOR UNDER AB 32**

CHRISTOPHER J. WARNER

Pacific Gas and Electric Company
77 Beale Street
San Francisco, CA 94105
Telephone: (415) 973-6695
Facsimile: (415) 972-5220
E-Mail: CJW5@pge.com

Dated: January 8, 2008

Attorneys for
PACIFIC GAS AND ELECTRIC COMPANY

**DOCKET 07-OIIP-01
CALIFORNIA ENERGY COMMISSION
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I. INTRODUCTION

Pursuant to the ruling of the Administrative Law Judges dated November 28, 2007 (ALJs' Ruling), Pacific Gas and Electric Company (PG&E) provides its reply comments on type and point of regulation of greenhouse gas emissions in the natural gas sector under AB 32. PG&E's comments are in the form of a general response to comments by other parties.

II. PARTIES WHO ADVOCATE THAT LOCAL DISTRIBUTION COMPANIES BE THE POINT OF REGULATION OR THAT A CAP AND TRADE APPROACH BE USED ARE FAILING TO ACKNOWLEDGE THAT A CAP AND TRADE APPROACH SIMPLY MAY NOT BE PRACTICABLE IN THE NATURAL GAS SECTOR

In our opening comments, PG&E posed several fundamental questions which we believe need to be answered before determining the point of regulation for GHG emissions in the natural gas sector. These questions included, *inter alia*: What are the amount and timing of emissions reduction opportunities in the natural gas sector that would be available at a lower cost as related to other sectors, especially for the millions of GHG point sources among residential and commercial "core" gas users who represent the most significant source of emissions not already regulated under emissions limits applicable to large industrial users? To what degree can these opportunities be captured

through programmatic measures made available to these millions of gas users, such as building and appliance standards, as opposed to through specific emissions limits on those users or on upstream entities such as local distribution companies (LDCs) or interstate pipelines? After taking into account the reductions available through programmatic measures, how much of any remaining potential might be captured by bringing that sector into a cap and trade program, especially in light of the transaction costs inherent in applying the cap and trade approach to literally millions of GHG point sources? And in light of these transaction costs, will there be significant market liquidity benefits from bringing these millions of users into a cap and trade market?^{1/}

For the most part, the parties in their opening comments acknowledged these fundamental questions, and attempted to reconcile their general support for market-based mechanisms, such as cap-and-trade, with the practical difficulties of implementing a cap and trade system for GHG emissions associated with millions of small gas consumers in the residential and commercial sectors.^{2/} However, some parties failed to recognize these realities in their comments, and instead generally endorsed a cap and trade approach in the gas sector as an end in itself, without further analysis of whether it actually would work or would result in the liquidity and economic efficiencies expected of cap and trade.^{3/}

PG&E appreciates that many of the parties advocating cap and trade for the gas sector, or advocating that LDCs should be the point of regulation, are genuine in their

^{1/} PG&E Opening Comments, pp. 2- 5, December 17, 2007.

^{2/} SDG&E/SoCal Gas, pp. 3- 4, 6 ; NRDC-UCS, pp. 3- 5, 7- 9.

^{3/} Indicated Producers, pp. 2- 5; SCE, pp. 2- 3; SMUD, pp.2- 3.

support for expanding the benefits of cap and trade as broadly as possible. PG&E aspires to the same ideal and supports the same goals. However, these parties are wrong in supporting cap and trade or LDCs as the point of regulation without evaluating the practical difficulties of implementing such a system in the residential and commercial sector.

For small retail natural gas customers, the emissions reduction opportunities are directly tied to natural gas efficiency improvements at the burner tip, and these improvements are more limited than in the electric sector or for large industrial gas uses. It is likely that the bulk of these savings can be achieved through a well-integrated set of programmatic measures directed at small customer natural gas consumption, which would include state appliance and building efficiency codes and standards, complementary utility customer energy efficiency programs, and possibly a point of sale energy efficiency program. Because of the unique characteristics of household and commercial building uses of natural gas, programmatic measures such as these are likely to be far more efficient and economic than regulating the upstream delivery or transportation of gas in an attempt to indirectly influence downstream emissions at the burner tip.

Likewise, although a cap-and-trade system often provides the greatest economic incentive to seek the most cost-effective reductions, with limited GHG-free fuel alternatives to natural gas and conservation and efficiency as the only other viable option for reducing emissions, the additional liquidity provided by broadening the market to include the natural gas sector is likely to be limited. The Governor's Market Advisory Committee also recognized the potential practical and administrative difficulties of

applying a cap and trade approach in some sectors, such as the natural gas sector, and therefore recommended that policymakers consider excluding such sectors from the initial phases of cap and trade under AB 32.^{4/}

III. CONCLUSION

PG&E recommends that the CPUC and Energy Commission adopt a type and point of regulation for the natural gas sector consistent with these comments. PG&E does not currently recommend including the small commercial and residential segment of the natural gas sector in a California-only cap and trade mechanism. Nor should LDCs be the point of regulation for emissions reductions in the natural gas sector. Instead, the CPUC and Energy Commission should consider a programmatic approach to GHG emissions in the natural gas sector, including enhanced building codes, appliance standards, enhanced financing of appliance replacement and building upgrades in the residential and commercial sectors, and point of sale efficiency standards.

Respectfully Submitted,

CHRISTOPHER J. WARNER

By: _____/s/_____

CHRISTOPHER J. WARNER

Pacific Gas and Electric Company

77 Beale Street

San Francisco, CA 94105

Telephone: (415) 973-6695

Facsimile: (415) 972-5220

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^{4/} "Recommendations for Designing a Greenhouse Gas Cap-and-Trade System for California,"