BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

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: Order Instituting) Informational Proceeding on a) Greenhouse Gas Emissions Cap)	Docket 07-OIIP-01

COMMENTS OF THE MODESTO IRRIGATION DISTRICT ON FINAL OPINION ON GREENHOUSE GAS REGULATORY STRATEGIES

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In accordance with Rules of Practice and Procedure of the Public Utilities Commission ("CPUC") of the State of California, the Modesto Irrigation District ("Modesto ID") hereby files these Comments ("Comments") on the proposed "Final Opinion on Greenhouse Gas Regulatory Strategies" issued September 12, 2008 (the "Proposed Decision" or "PD"). Modesto ID also files these Comments with the California Energy Commission ("CEC") in Docket 07-OIIP-01. In these Comments, the CPUC and CEC will collectively be called the "Joint Agencies."

Modesto ID supports the goals set forth in Assembly Bill ("AB") 32 and is committed to undertaking feasible, cost effective measures to achieve its fair share of greenhouse gas ("GHG") emission reductions. Modesto ID continues to advocate an achievable, programmatic approach to GHG emission reductions that allows entities the flexibility to use all available tools, including energy efficiency and renewable procurements, to meet established emission reduction goals in a manner that best serves the interests of its consumers. Modesto ID also continues to caution against finalizing the design of California's program before a regional or national program has been defined, to ensure not only that the programs are coordinated but also that entities are not burdened with multiple layers of compliance obligation. For the protection of California's ratepayers and all economic sectors, California's GHG reduction program must minimize impacts to electric ratepayers and ensure continued reliability of electric services.

I. BACKGROUND.

Modesto ID is an irrigation district, organized and operated under the laws of the State of California, which undertakes both electric and water operations. It is a vertically integrated publicly owned utility providing electric services to over 114,000 customers in California's Central Valley. With regard to its electric operations, Modesto ID owns and operates facilities for the generation, transmission, distribution, purchase and sale of electric power and energy at wholesale and retail. Modesto ID is a fully integrated, fully resourced, credit worthy utility. In 2007 Modesto ID served a peak summer load of almost 675 MW and had retail sales of over 2,572 GW-hours.

Modesto ID serves this load through a mixture of owned and purchased resources, including wind, large and small hydro, natural gas and coal generation. In addition to ownership interests in significant hydroelectric generation at Don Pedro Reservoir, Modesto ID owns several natural gas generation facilities. Modesto ID purchases power from a variety of resources and suppliers, including renewable resources firmed by the supplier. These purchases are delivered within Modesto ID's service territory, and outside of its service territory at various points both within and out of state. Modesto ID is also a member of a joint powers authority, the M-S-R Public Power Agency ("M-S-R"), which purchases power from wind energy projects in the Pacific Northwest and owns a share of the thermal San Juan Project in New Mexico. M-S-R annually produces about 1,750 GW-hours of energy of which about 35% (605 GW-hours) would be classified as eligible renewable. Modesto ID's published Power Content Label, incorporating the state's average resource mix for all unspecified purchased power, identifies the following resource mix: 15% eligible renewables and 17% large hydroelectric, 31% coal, 36% natural gas and 1% nuclear.

II. CALIFORNIA'S GHG REDUCTION PROGRAM MUST BE FULLY DESIGNED BEFORE ANY IMPLEMENTATION.

GHG emissions are a global issue and solutions will have to be approached on a global level. As the PD recognizes, a California only approach will result in increased costs for the electricity sector without achieving increased GHG reductions. (PD, p. 49.) Modesto ID supports the recommendation to coordinate with the Western Climate Initiative ("WCI") but believes that a single, national approach would be more effective. The PD appropriately recognizes that "future success in reducing GHG emissions will involve increasing coordination at the regional and national levels." (PD, p. 144.) However, multiple regional organizations are attempting to address GHG reductions, each in its own way, each believing that it could influence a national program. In the event that a national program is ultimately developed that does not conform to one or more aspect of the program implemented in California or the WCI, entities operating under the California system would be disadvantaged by having to repeat or duplicate their compliance activities. If California's program continues to exist within the federal system, but is more restrictive, entities will also face competitive disadvantages.

Furthermore, it is not clear "who is on first." Numerous program elements remain undefined with critical details and mechanisms deferred to another entity or additional investigation. For example, the PD recommends coordination with the WCI that has yet to issue its proposed program design. A "coordinated" California program cannot be implemented until the WCI program parameters are adopted. Nor can the appropriate positioning of the California program to "move toward a nationally and ultimately internationally integrated program" (PD, p. 109.) be determined before direction for a federal system is adopted. Modesto ID is concerned that in the rush to adopt and implement a GHG emission reduction program for California before such a program is fully defined and before broader programs necessary to the success of the California program are established, California's electricity sector will be severely disadvantaged.

III. THE MODELING RELIED ON BY THE PD IS FLAWED.

The economic modeling relied upon by the CPUC in making its recommendations in the PD is significantly flawed. As the PD notes, "[t]he GHG calculator does not estimate the impacts of GHG policy choices on energy producers or entities other than the seven groupings of retail providers (and their customers) identified in the model." (PD, p. 28.) These seven groupings include the five largest electric utilities in California and an averaging of all other utilities by geographic location – Northern California utilities and Southern California utilities. Unfortunately, Modesto ID, like others included in one grouping or the other, is averaged in with other entities that do not share its critical characteristics (such as load size and type, and resource mix). Thus, Modesto ID is unable to determine how the various policy scenarios would trend for or impact on Modesto ID. Moreover, because current data is not incorporated into the model, it is not possible to determine how the various policy scenarios would impact any utility based on current statewide data.

The model also assumes achievement of goals that may not be met, fails to consider costs of achieving the goals relied upon, is unable to model certain recommendations or how the recommendations will impact individual entities, and relies on limited and outdated data sources. For example, the GHG calculator is said to estimate the impacts of GHG reduction policies on total retail provider and consumer costs, and concludes that while total utility costs will increase in all modeled resource scenarios, average utility bills would decline with accelerated energy efficiency and renewable mandates because "total utility costs would be reduced due to high level of cost-effective energy efficiency and distributed resources, which offset the higher costs of renewable generation." (PD, p. 40-41.) Yet these results do not factor in the full costs of achieving the recommended energy efficiency as "currently no data or analysis exists to estimate the costs of achieving that level of energy efficiency." (PD, p. 43.) Furthermore, there are no assurances that such levels of efficiencies are even obtainable. As discussed below (see, Section 4.B.1), current experience indicates the opposite. Similarly as the PD notes, "there continues to be a great deal of uncertainty regarding the assumptions underlying a 33% renewable mandate." (PD, p. 91) Again, as discussed below (see, Section 4.B.2), substantial barriers exist and must be removed before such a goal can be achieved. There is "significant uncertainty associated with modeling the costs of achieving 33% renewables and the speed with which necessary system improvements can be achieved." (PD, p. 92.) In addition, the PD admits that "price-induced demand effects will change the estimated cost effectiveness of carbon reduction measures." (PD, p. 62.) Although average price elasticity assumptions were tested, "the effects of price elasticity at higher prices are not clearly understood and the differential impacts on energy-intensive elements of the economy have not been addressed." (PD, p. 63.)

True impacts to rates and ratepayers must be accurately determined before any particular program element is implemented.

IV. A FLEXIBLE, PROGRAMMATIC APPROACH WILL BEST ACHIEVE ALL THE GOALS OF AB 32.

Every utility has a unique resource mix and serves a unique load profile. A utility load profile will be affected by such things as load type, weather and water flow, breadth of service area, and population growth. For example, being located in the Central Valley, Modesto ID serves a largely agricultural business and commuter based load, experiences load peaks in the hottest part of the summer months, and is dependent of snow melt coming out of the Sierras for a significant portion of its non-emitting hydroelectric resources. Thus, the ability of each utility to achieve emission reductions from various mechanisms may be equally diverse. Emission reduction goals must be established for the electricity sector and regulated entities within the electricity sector must have the flexibility to use a mix of tools to meet these goals. Such goals must be set to avoid counter-productive mandates and penalties that use up funds that could better be directed toward achieving emission reduction goals.

As noted above, Modesto ID believes that a programmatic approach that sets a GHG reduction goal and allows regulated entities the flexibility to achieve that goal is the preferable approach to achieving the reductions required by AB 32. Modesto ID does not support specific mandates or a mandatory cap and trade program.

A. INHERENT RATE IMPACTS

The PD attempts to balance the need to mitigate rate impacts while avoiding the creation of windfall profits. It acknowledges that "[u]nless great care is taken, carbon regulations inadvertently could have disparate customer impacts due to the different generation mixes." (PD, p. 134.)

> Overall the electricity sector costs and rate impacts due to achieving 2020 GHG caps through more energy efficiency measures, greater use of renewable energy, and increased reliance on CHP are potentially significant but appear acceptable against the backdrop of the economic and environmental costs of doing nothing to address the need to reduce GHG emissions. Total utility costs are expected to increase...due to load growth and expected real increases in capital and fossil fuel costs.
>
> (PD, p. 10.)

The PD concludes that average customer bills could be lowered with the increase in energy efficiency and renewable procurements even though average retail rates would increase because there would be less load over which utilities could spread fixed costs. At the same time acknowledges that "[t]he actual impact of the rate increases would be felt differently by different types of customers." (PD, p. 11.) Customers with less discretionary usage, or that are unable to afford efficiency measures, or that otherwise have less ability to take advantage of energy efficiency opportunities could be significantly impacted. In analyzing the impact of various programs, policies and approaches to achieving AB 32 objectives, the PD must be careful not to rely on benefits that may not actually result from the reduction of GHG emissions. What happens if the costs of achieving energy efficiency load reductions outweigh the rate savings from such load reductions? What happens if green industry does not develop as rapidly in California as some expect? These questions must be examined before program recommendations are adopted.

B. MANDATES

If increased mandates are to be recommended, such mandates must rely on available technologies and set achievable goals based on thorough assessments of historical achievements and known barriers. The proposals presented in the PD are too dependent on the occurrence of events and the removal of barriers that are uncertain. The parameters, measures and enforcement of each recommended mandate must be fully defined and analyzed before any recommendation is presented to ARB.

The PD urges ARB to impose mandates on publicly owned utilities ("POUs") setting energy efficiency and renewable procurement requirements equal to those set by the CPUC for investor owned utilities. In making these recommendations the PD does not discuss the jurisdictional restraints that may exist. Even if ARB or the CEC does have the legal authority to regulate POUs, with or without additional legislation, separate proceedings in which the POUs actively participate must be undertaken to independently evaluate and establish the parameters of such mandates. CPUC programs cannot be adopted and imposed on non-jurisdictional POUs without such independent review.

1. Energy Efficiency

The PD recommends "nearly a doubling of efficiency goals" to mandate that utilities – both investor and publicly owned – capture all cost effective energy efficiency. (PD, p. 10.)

> With intensified efforts in building and appliance standards and utility programs, and with new strategies and technologies, the State can capture all cost-effective energy efficiency.
>
> (PD, p. 5.)

The cost of achieving such objectives has not been evaluated. Neither has the likelihood of overcoming the barriers to such objectives that have been identified. Nor has any review of new technologies and their potential for implementation been conducted. The CPUC has adopted its Energy Efficiency Strategic Plan calling for new codes and bold measures; however, the "market transformation" required to meet the objectives of that Plan is equally uncertain.

2. Renewable Portfolio Standards

The PD's recommendation for a minimum increase in renewable portfolio standards to 33 percent likewise depends on the occurrence of uncertain events – significant investments in new transmission infrastructure, augmentation of key utility programs, and the removal of contracting, permitting and grid integration barriers. (PD, pp. 90-1.) Again the development and implementation of new technologies is required.

In addition critical program measures and definitions have yet to be developed, making these recommendations premature as well. For example, the breadth of efficiency savings a utility can take credit for has not been determined, the definition and role of renewable energy credits is being determined in other proceedings that again may not be directly applicable on a sector wide basis.

C. CAP AND TRADE

Modesto ID has stated in previous filings that it does not support a cap and trade system, does not believe AB 32 requires a cap and trade system, and is not persuaded that a mandated market system is necessary to achieve GHG emission reductions. Without further definition of the detailed mechanisms of such a system its ability to act as a "backstop" or an "insurance policy" is slim to none.

If and when a cap and trade system is undertaken in California for GHG reductions, it should be phased in gradually and ensure that substantial protections against market manipulation – intentional and incidental – are securely in place before its start. It is critical that allowances and allowance values do not result in shifting costs among sectors or ratepayers. Impacts to the electricity sector resulting from electrification of other sectors must be neutralized so that the sector responsible for the emissions generated bears the resulting emission costs, whether such costs arise from additional reductions to be achieved to offset the new load, additional efficiencies or renewables to be procured, or the direct costs of additional allowances needed by the electricity provider. (See, PD, p. 127.)

All the elements and measures required for a successful program must be fully developed before any program is initiated; the target must be clearly drawn and placed before the first shot is fired. Unfortunately, the PD recommendations contain a number of issues requiring further development, including how output would be measured, how fuel differentiations would be weighted, how transitions from emission to output measures will occur, how offsets will be judged, what baseline periods will be used, and how the program would be integrated with the WCI program or more importantly with future federal or international programs.

1. ALLOWANCES

The PD recommends a dual system of allowance distribution. First the total number of allowances for California will be determined. Such determination is effected in coordination with the WCI. Then those allowances are divided among capped sectors based on their respective portion of historical emissions. The portion of allowances allotted to the electricity sector would then be divided among sector entities. For the first five years of the market operation a portion of electricity sector allowances would be auctioned and the remainder freely allocated; thereafter the entire allotment would be subject to auction. The portion allocated would be given to regulated deliverers with emitting resources based on a fuel differentiated output methodology. The portion auctioned would be given to retail providers who would be required to sell them at an auction administered by ARB or its designee. All proceeds from the auction would go directly to and be used by the retail provider for AB 32 purposes. Initially the distribution to retail providers would be based on historical emissions during a baseline period transitioning "by 2020" to an output basis.

Modesto ID does not support auctions and previously filed comments regarding its concerns with distributing allowances through auction. Modesto ID believes the proposed transition slope to 100 percent auction is too steep. Entities with ownership obligations and debt, or with long term commitments, may need more time to fully address these existing commitments depending on legal constraints, the economy, the availability of low or zero emission replacement resources, and other factors. Five years is not sufficient time to adjust such portfolios. This trajectory should be smoothed out. In such an event, the PD recommends that the allocation methodology for non-auctioned allowances transition from the fuel differentiated output basis to a pure output basis. It does not elaborate on how or within what time frame this transition would occur.

The recommended allocation methods both between the electricity and other sectors and among entities within the electricity sector depend on "baseline" determinations. However, the PD defers identification of the baseline to a later date. It is impossible to determine the validity or impact of the allocation methodology without establishment of a baseline. A multi-year baseline is crucial to address variables unique to the electricity sector. Modesto ID believes a four year average using the years 2005 through 2008 would be a fair representation of the electric sector at the time AB 32 was adopted and best represents typical hydroelectric fluctuations in California, including two years of low (2008 and 2007) and two years of high (2006 and 2005) hydro production. This average meets the objectives stated in the PD.

The operation of the centralized market proposed by the PD must also be designed and evaluated before any market system can be initiated. If initiated, protections must be put in place while the market system develops to ensure against instability and price fluctuations.

The PD does properly recommend that all auction proceeds go directly to the retail providers for specified uses, protecting the funds from diversion to more general state uses and allowing each utility to determine its own best use of auction proceeds to minimize the impact of GHG reduction activities and to protect their ratepayers. For POUs this authority is properly placed with the local governing boards. These elected and appointed governing boards provide oversight to POU activities similar to the CPUC's oversight of the IOUs.

2. FLEXIBLE COMPLIANCE MECHANISMS

Flexible compliance mechanisms will be necessary to the success of any AB 32 implementation program. Such mechanisms should be as broadly designed as possible to maintain the environmental integrity of the program. Modesto ID concurs with the PD's recommendations for multi-year compliance periods and unlimited banking. Modesto ID also agrees that use of "limited" offsets without geographic boundaries should be permitted. However, the PD does not define the limits it is recommending and notes that further modeling is needed in order to set the appropriate levels of allowable offsets. (PD, p. 270.) Allowable offsets should be defined before this recommendation can be fully evaluated.

V. CONCLUSION.

Modesto ID appreciates the opportunity to review its concerns regarding the PD and urges the CPUC to clarify the issues identified herein. The CPUC must provide program design recommendations to achieve compliance with AB 32 in the most cost effective manner and avoid unnecessary or disproportionate impact to electric sector ratepayers and entities.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I, Linda Fischer, certify under penalty of perjury under the laws of the State of California that the following is true and correct:

On October 2, 2008, I served the attached:

COMMENTS OF THE MODESTO IRRIGATION DISTRICT ON FINAL OPINION ON GREENHOUSE GAS REGULATORY STRATEGIES

on the service list for R.06-04-009 by serving a copy of each party by electronic mail, or by mailing a properly addressed copy by first-class mail with postage prepaid to each party unable to accept service by electronic mail.

Electronic copies and hard copies by first-class mail with postage prepaid were also sent to Administrative Law Judges Charlotte F. TerKeurst (cft@cpuc.ca.gov) and Jonathan Lakritz (jol@cpuc.ca.gov) , and to Commissioner Peevey's advisor Nancy Ryan (ner@cpuc.ca.gov).

A copy was sent by first-class mail with postage prepaid to the California Energy Commission, Docket Office, MS-4, Re: Docket No. 07-OIIP-01, 1516 Ninth Street, Sacramento, CA 95814-5512. A copy was also served by email to the CEC docket office.

A copy of the service list is attached hereto.

Executed on October 2, 2008, at Modesto, California.

Linda Fischer

Linda Fischer

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