Cap-and-Trade Program Summary of 2015-2020 Natural Gas Supplier Use of Allocated Allowance Value

Purpose

This report summarizes how natural gas suppliers (NG suppliers) used the value of allowances allocated to them by the California Air Resources Board (CARB) under the Cap-and-Trade Program (Program) during the period 2015-2020. The value of these allocated allowances is referred to as "allocated allowance value" or, if the allowances have been consigned to auction and sold, "allocated allowance auction proceeds" or "auction proceeds."[1]

Background

Under the Cap-and-Trade Regulation (title 17, California Code of Regulations, sections 95801 *et seq.*) (Regulation)[2], NG suppliers face a compliance obligation for each ton of greenhouse gas (GHG) emissions released from the combustion of the natural gas supplied to their customers, less any natural gas delivered to facilities that are covered by the Program. In order to protect utility ratepayers from this Program cost burden while maintaining the Program incentive to reduce natural gas use, CARB allocates free allowances to NG suppliers. Pursuant to the Regulation, these allowances must be used for the benefit of natural gas ratepayers, consistent with the goals of the California Global Warming Solutions Act of 2006 (Assembly Bill 32, Nuñez, Chapter 488, Statutes of 2006, AB 32). NG suppliers were first covered by the Program in 2015, and the first NG supplier allocations were from the 2015 allowance budget year (i.e., vintage 2015 allowances).

For 2020, allowances allocated to NG suppliers were approximately 12 percent of the total Program allowance budget. Per section 95893(a) of the Regulation, the number of allowances annually allocated to each NG supplier is based on the NG supplier's

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[1] Proceeds resulting from the auction of allowances allocated to NG suppliers are distinct from the auction proceeds received by the State from the auction of State-owned allowances, which are deposited into the Greenhouse Gas Reduction Fund (GGRF) pursuant to section 16428.8 of the California Government Code. For more information on GGRF expenditures, see: *California Climate Investments webpage.*

[2] *Cap-and-Trade Regulation (unofficial copy)*.

2011 total sales of natural gas, less any natural gas sold to facilities that are covered by the Program, and declines each year in proportion to the decline of the overall Program cap.

CARB allocates allowances to two types of NG suppliers—investor-owned utilities (IOUs) and publicly owned utilities (POUs)—that together provide all natural gas supplied in California. IOUs are the largest NG suppliers in the State and are subject to oversight by the California Public Utilities Commission (CPUC), which also directs how the IOUs use their allocated allowance auction proceeds. POUs are much smaller than IOUs and are owned and operated by city governments, which determine how to use their allocated allowance value. Both IOUs and POUs must spend their auction proceeds in accordance with the requirements in the Regulation.

The Regulation requires all NG suppliers to consign a minimum percentage of their allocated allowances from each vintage year to the four quarterly Program auctions held during that calendar year. The minimum consignment requirement was 25 percent for vintage 2015 allocated allowances and increases by five percent each year, as specified in Tables 9-5 and 9-6 of the Regulation. The minimum consignment requirement was 50 percent for vintage 2020 allocated allowances and will reach 100 percent for vintage 2030 allocated allowances. As required by section 95893(d)(3) of the Regulation, NG suppliers must either use the resulting auction proceeds for programs to reduce GHG emissions or return the proceeds to ratepayers as non-volumetric credits. For IOUs, the percentage of allowances consigned to auction is approximately equal to the percentage of Program costs that IOUs pass through to their customers in rates. Allowances that IOUs do not consign to auction are used directly for Program compliance, reducing their Program costs, and thus reducing the costs passed through to customers.

CARB Reporting Requirements and This Summary Report

The Regulation requires each NG supplier to report to CARB by June 30 of each year on its use of allocated allowance value during the prior calendar year. The NG supplier must describe how allocated allowance value was used during the calendar year and how those uses were consistent with the requirements of the Regulation.

The "IOU Use of 2015-2020 Allocated Allowance Value" section of this report summarizes the individual IOU use of allocated allowance value reports submitted to CARB. Through 2020, about 61 percent of the allowances allocated to IOUs have been deposited directly for compliance. The remaining allowances allocated to IOUs were consigned to auction, and most of the auction proceeds have been returned to residential ratepayers in the form of annual on-bill California Climate Credits.

The "POU Use of 2015-2020 Allocated Allowance Value" section of this document summarizes the individual POU use of allowance value reports submitted to CARB. Through 2020, just over half of the allowances allocated to POUs have been deposited directly for compliance. The remaining allowances allocated to POUs were consigned to auction, and most of the auction proceeds were unspent as of January 1, 2021.

IOU Use of 2015-2020 Allocated Allowance Value

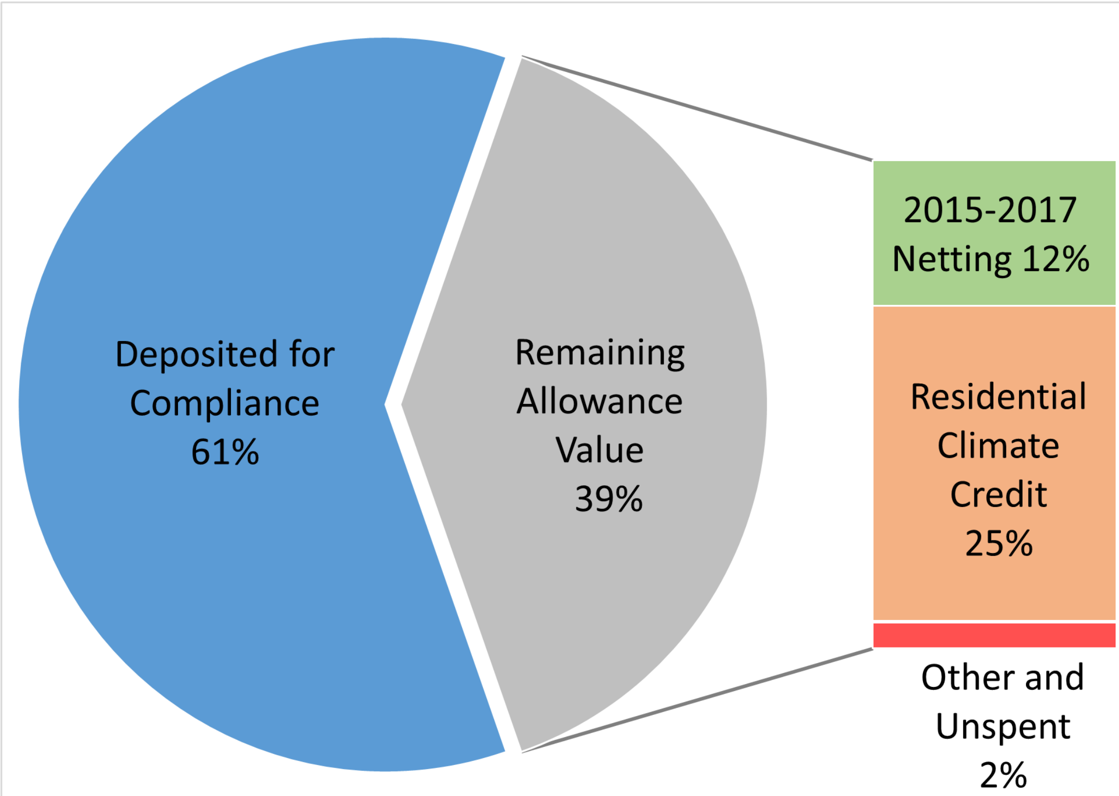
There are four investor-owned natural gas suppliers (investor-owned NG supplier, or IOU) in California with a compliance obligation under the Program: Southern California Gas Company, Pacific Gas and Electric Company, San Diego Gas and Electric Company, and Southwest Gas Corporation. Together, the four IOUs account for almost all retail natural gas sales in California, and they receive about 98 percent of the allowances allocated to NG suppliers. The total value of vintage 2020 allowances that CARB allocated to IOUs was approximately 686 million dollars.

IOU use of allocated allowance auction proceeds is largely directed by CPUC. Per CPUC Decision 18-03-017,[3] auction proceeds from vintage 2015 through 2017 allocated allowances, less a small amount used for administration and outreach expenses, were netted against Program compliance costs for those years. Starting in 2018, this CPUC decision directed all IOU auction proceeds to be used to provide annual credits to residential ratepayers. These credits are reduced in 2020 through 2023 so that a portion of proceeds can be used for building decarbonization programs, as required by Senate Bill (SB) 1477 (Stern, Chapter 378, Statutes of 2018).

Figure 1 shows the cumulative use of allocated allowance value by all IOUs during the period 2015-2020. The information presented in Figure 1 is based on the IOU annual reports to CARB. Each category of allowance value use shown in Figure 1 is described later in this report. CARB has compiled Figure 1 data, annual allocated allowance auction proceeds, and specific reported uses of allocated allowance value in a publicly available *spreadsheet*.

[3] Decision Modifying Decision 15-10-032, D.18-03-017 (March 2018). *CPUC Decision 18-030-017.*

Figure 1. IOU Use of 2015-2020 Allocated Allowance Value ($3.79 billion).[4]



Through 2020, investor-owned NG suppliers have received approximately 3.75 billion dollars in allocated allowance value over the history of the Program. As of January 1, 2021, the total allocated allowance value that either (1) has been spent on eligible activities, (2) has been reserved for spending on specific programs in future years, or (3) is not yet spent or reserved for specific future spending is approximately 3.79 billion dollars. Figure 1 shows that of the total vintage 2015-2020 allowance value that has been received or reserved, 61 percent was used directly for Program compliance and 12 percent was netted against 2015-2017 Program costs. After a small amount was used to cover outreach and administrative costs, 25 percent was returned to residential households as annual California Climate Credits. Two percent remained unspent due to (1) use of forecasts when calculating per-household California Climate Credits,[5] and (2) funds reserved for building decarbonization programs.

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[4] "Other" includes administrative and outreach costs, which account for 0.12% of total allocated allowance value. The amount of allocated allowance value presented in this figure includes interest accrued on unspent auction proceeds.

[5] The amount of unspent auction proceeds due to the use of forecasts is included in the amount of auction proceeds available in subsequent years.

Allowances Deposited for Program Compliance

Per CPUC direction in Decision 15-10-032,[6] all investor-owned NG suppliers deposit into their compliance accounts the maximum number of allocated allowances that is allowed by the Regulation (section 95893(b), Table 9-5). Each NG supplier surrenders these allowances to CARB to partially fulfill its compliance obligation under the Program, thereby reducing its Program compliance costs, which are recovered from ratepayers. The percentage of allowances allocated to IOUs that were deposited for compliance was 75 percent in 2015, 70 percent in 2016, 65 percent in 2017, 60 percent in 2018, 55 percent in 2019, and 50 percent in 2020.

2015-2017 Auction Proceeds Netted Against 2015-2017 Program Compliance Costs

In 2018, CPUC Decision 18-03-017 directed each IOU to net the auction proceeds it had received from the sale of vintage 2015-2017 allocated allowances against the costs it incurred in purchasing allowances to meet Program compliance obligations for covered emissions during 2015-2017. After this netting, the remaining balance of auction proceeds for each IOU was applied to its 2018 Residential California Climate Credits.

Residential California Climate Credit

CPUC Decision 18-03-017 directed most IOU auction proceeds from 2018 and following years to be used for annual credits to residential ratepayers. These credits are referred to as California Climate Credits to mirror the semi-annual credits electric IOU ratepayers have received since 2014. For each IOU, all auction proceeds not used for the other purposes listed below (i.e., administration, outreach, and building decarbonization programs) are divided equally among that IOU's residential customers and returned to each residential customer as an on-bill annual California Climate Credit. These annual credits first appeared on customer bills in either October 2018 or April 2019 and subsequently have been distributed each April. The CPUC webpage provides more details on California Climate Credits distributed by the IOUs.[7]

Administration and Outreach

Administrative and outreach costs include necessary costs to administer the California Climate Credits and other allowed uses of auction proceeds and to inform ratepayers

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[6] Decision Adopting Procedures Necessary for Natural Gas Corporations to Comply with the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms (Cap-and-Trade Program), D.15-10-032 (October 2015). *CPUC Decision 15-10-032*.

[7] See the Residential Natural Gas California Climate Credit section on the *CPUC California Climate Credit webpage*.

about these uses. Less than 0.4 percent of total IOU auction proceeds expenditures have been for administrative and outreach costs during 2015-2020.

Building Decarbonization

SB 1477 directs a portion of IOU auction proceeds to fund two building decarbonization programs: the Building Initiative for Low-Emissions Development (BUILD) Program and the Technology and Equipment for Clean Heating (TECH) Initiative. BUILD will focus on increasing electrification in new buildings, and TECH aims to electrify space and water heating, especially in existing buildings. The programs are defined by SB 1477 and directed by CPUC Decision 20-03-027.[8] SB 1477 requires that for each budget year starting July 1, 2019 and ending June 30, 2023, $50 million of combined IOU auction proceeds be set aside to fund BUILD and TECH. Each IOU contributes its share of auction proceeds to these programs in proportion to its share of total IOU allocated allowances. $50 million represents about 15 percent of annual IOU auction proceeds.[9] Through the end of the 2020 calendar year, the IOUs have collectively reserved $75 million for spending on BUILD and TECH.[10]

POU Use of 2015-2020 Allocated Allowance Value

There are three publicly owned natural gas suppliers in California: City of Long Beach, City of Palo Alto, and City of Vernon. POUs supply a small fraction of the total natural gas consumed in the State, and they receive about two percent of the allowances allocated to all NG suppliers. The total value of vintage 2020 allowances that CARB allocated to POUs was approximately 11 million dollars.

Allowances allocated to POUs can be either deposited for compliance or sold at auction, however a minimum percentage must be consigned to auction each year as specified in Tables 9-5 and 9-6 of the Regulation. The Regulation requires that the use of these allowances must benefit ratepayers and be consistent with the goals of AB 32. POUs are not subject to CPUC jurisdiction or the requirements of SB 1477.

Figure 2 shows the cumulative use of allocated allowance value by all POUs during the period 2015-2020. The information presented in Figure 2 is based on the individual POU annual reports to CARB. CARB has compiled Figure 2 data, annual allocated allowance auction proceeds, and specific reported uses of allocated allowance value in a publicly available *spreadsheet*.

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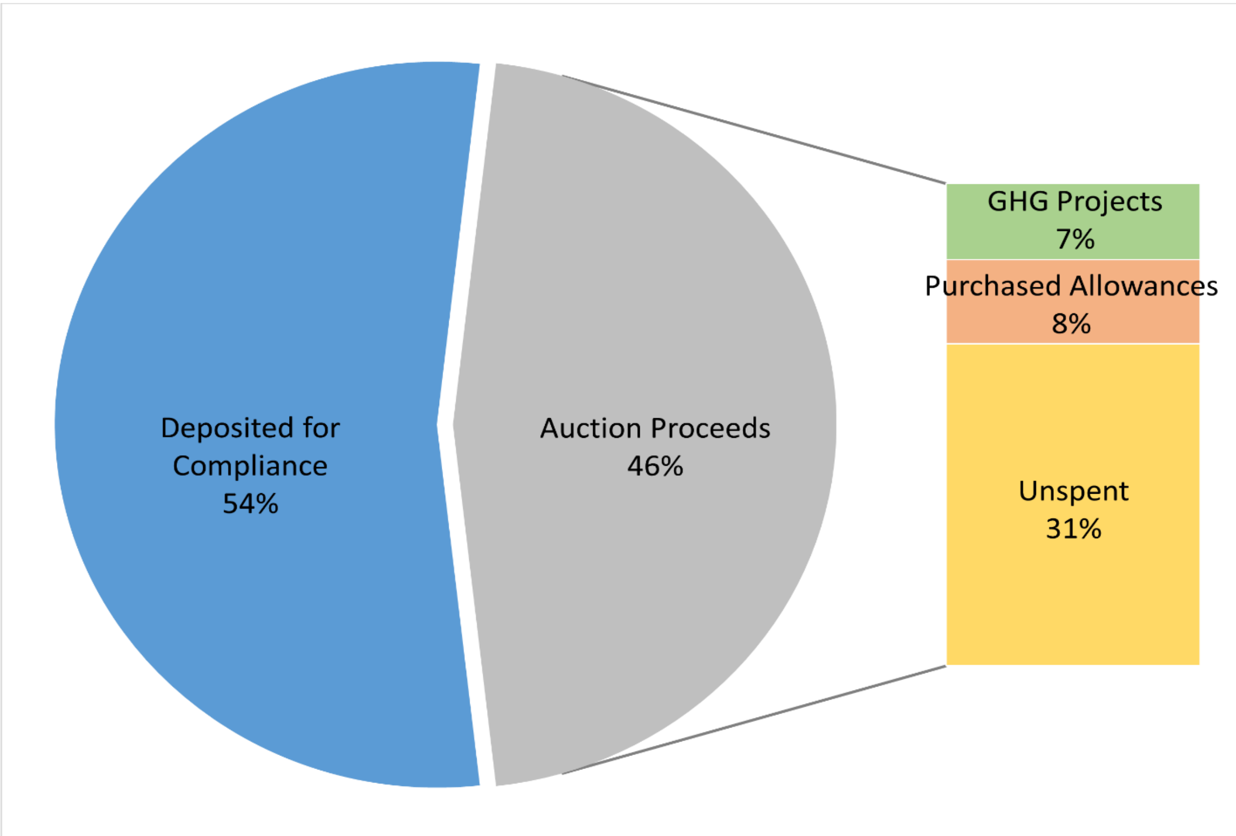
[8] Decision Establishing Building Decarbonization Pilot Programs, (D.) 20-03-027 (March 2020). *CPUC Decision 20-03-027*.

[9] Based on 2020 proceeds assuming all IOU allocated allowances that are consigned to auction sell at the auction floor price.

[10] $37,404 of the $75 million reserved for the BUILD and TECH programs were spent in 2020 on early-stage administrative costs.

Figure 2. POU Use of 2015-2020 Allocated Allowance Value ($0.060 billion).[11]



POUs have received approximately 60 million dollars in allocated allowance value over the history of the Program. Figure 2 shows that of the vintage 2015-2020 allowance value allocated to publicly owned NG suppliers, 54 percent was used directly for Program compliance, eight percent was used to purchase allowances in 2016 (which is not currently an allowable use of auction proceeds), seven percent was used for energy efficiency and electrification activities, and 31 percent remains unspent as of January 1, 2021. Energy efficiency and electrification activities have included installing LED streetlights, building energy efficiency retrofits, solar energy projects, battery storage, industrial efficiency activities, residential energy efficiency outreach, and installing electric vehicle charging stations. If a POU does not spend proceeds on eligible activities before the rolling 10-year deadline set in section 95893(d)(8) of the Regulation, it must return the proceeds to ratepayers in a non-volumetric manner.

[11] Administrative and outreach costs are included within other activities rather than shown separately because they were not required to be reported separately to CARB until reporting for the 2018 data year.