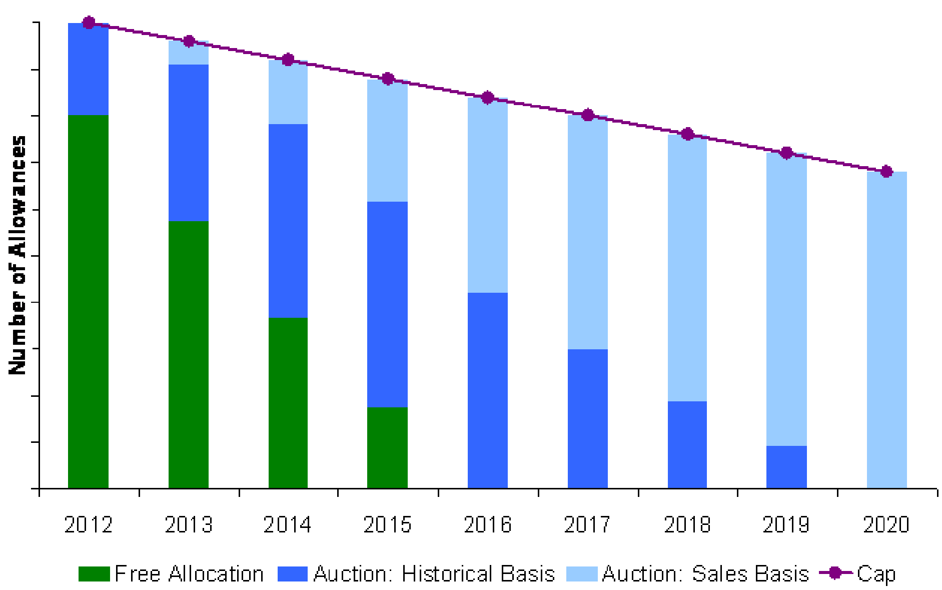
CPUC/CEC Recommendations on Allowance Allocation in the Electricity Sector

In 2008 the CPUC and the CEC unanimously adopted a joint decision providing recommendations to CARB on implementation of AB32 for the electric sector. The Joint Decision's recommendations on allowance allocation in the electricity sector consists of three basic elements: 1) some allocation to electricity deliverers on a fuel differentiated, updating output basis from 2012 through 2015, 2) allocation to retail sellers of electricity transitioning from an historical emission basis to an updating sales basis over time, and 3) mandatory auctioning of the allowances allocated to retail sellers with revenues returned to the retail sellers to be used in ways benefitting ratepayers consistent with AB 32. The chart below illustrates the transitions from deliverer allocation to retail seller allocation. Of the five criteria listed in the Joint Decision, two were particularly important in determining the final recommendation: minimizing cost to consumers and treating market participants equitably and fairly.[1]

The Commissions supported an initial allocation to deliverers primarily to provide ARB and market participants some time to ensure that the auction process functions smoothly and market abuses are avoided. The fuel-differentiated, output basis for allocation was chosen to both minimize windfall profits accruing to independent generators and to minimize transfers of wealth from customers of retail sellers with relatively GHG-intensive portfolios to customers of retail sellers with low-GHG portfolios.

Allocation to retail sellers based initially on historical emissions was selected in the interest of fairness to high-GHG retail sellers. The Commissions recognized that retail sellers with high-GHG portfolios will need some time to build or procure electricity from other sources in order to reduce their dependence on their high-GHG resources. Eventual transition to a sales-based allocation was chosen to provide strong long-term incentives to invest in low GHG resources and was also described as consistent with moving toward the "polluter pays" principle.

The Joint Decision states that auction revenue must be used for purposes related to AB 32. The Commissions listed financial support for energy efficiency programs, above-market renewable energy, research, and lump-sum bill relief (to preserve the marginal price signal) for customers as examples of acceptable uses for auction revenue.



1 The other criteria cited by the Commissions were supporting a well-functioning market, minimizing administrative complexity, and aligning incentives with the goals of AB 32.