California Compliance Offsets – A Buyer’s Perspective

Obadiah Bartholomy
Sacramento Municipal Utility District

September 20, 2012
Climate Action Reserve Webinar

Powering forward. Together.
Outline

• SMUD as a Covered Entity Overview
• SMUD View on Offsets
• SMUD RFO
• Compliance Offsets Outlook
SMUD Compliance

Entity Overview

• Publicly Owned Utility, covering approximately County of Sacramento, Local Governing Board publicly elected

• 4 primary natural gas combined cycle (3 cogeneration) facilities plus imports
  – Total ~2.7 Million tonnes CO2 compliance obligation, primary variable is hydro

• Allowance allocations exceed retail obligations, not allowed to be used for wholesale sales obligations
  – SMUD short on wholesale sales compliance instruments
SMUD View on Offsets

- See value in promoting high quality offsets for California, US, Internationally for policy purposes
- Began voluntary carbon offset program for customers to complement our green pricing program Greenergy in 2007
  - Utilizes CAR offset projects, including offsets from dairy developed by SMUD
- Want to make use of good offsets projects to minimize compliance costs for Cap and Trade
- Must minimize our risk in procuring these as compliance instruments
  - SMUD generally cannot take open positions or speculate
  - Concern over new market, price uncertainty, stability/volatility
  - Concern over regulatory and legal challenges
SMUD Offsets RFO

• Seeking up to 200,000 tonnes per year for 2013 and 2014
• Released at end of July 2012
• Proposals due end of August 2012
• Significant response (no bid deposits or credit guarantee)
• Shortlist forthcoming (delayed from 9/13 expected date)
• Risk Abatement:
  – Offerers required to cover conversion
  – requested to double-verify
  – some provided fully guaranteed products
  – SMUD will be seeking guarantees against legal injunction, regulatory invalidation from sellers
Compliance Offsets Outlook (1/2)

• Expect to see offsets as a viable compliance instrument with a lower cost than allowances
• Significant uncertainty around price of allowances not helpful for decision-making internally
• Price ‘floor’ stability in new regulatory market challenging to accept
• Credit attributes of counterparties and regulatory stability of individual offset protocols as well as offset mechanism will be challenges in moving toward deals
Compliance Offsets Outlook (2/2)

- Uncertainty in new offset protocol acceptance by ARB is challenging from a procurement timing perspective
  - Supply and demand dynamics will be changing significantly over the next 6 months

- Optimal procurement mechanisms and location in supply chain for volumes SMUD is seeking is still to be determined for us
Conclusions

• SMUD eager to see robust offset market to help contain carbon prices
• Some risks apparent but contractual mechanisms available to mitigate most
• Uncertainties around value (allowance mkt fundamentals), conversion and reversal risks/costs, and regulatory/legal dynamics are key barriers to full market
  – Latter issue will remain well after 1st two
• If we don’t move forward, it will make it more difficult for offsets to realize their promise
Thank You!

Obadiah Bartholomy
Obadiah.Bartholomy@smud.org
916-732-6835