

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

