

May 11, 2012

**Comments of the Independent Energy Producers Association
On CARB's Cap-and-Trade Electricity Workshop
Convened May 4, 2012**

The Independent Energy Producers Association (IEP) is pleased to comment on CARB's Cap-and-Trade Electricity Workshop, convened May 4, 2012. IEP represents over 26,000 MWs of installed, non-utility, independently owned generation resources in California. Accordingly IEP's involvement in the cap and trade rulemaking has been primarily focused on designing a program that (1) maintains a competitive level playing field within the electric sector and (2) treats similarly situated entities equal. IEP's specific comments on the unresolved issues that were raised during the CARB electricity workshop continue to speak to these principles.

Specific Comments on the Cap and Trade Electricity Workshop:

The Proposed "Hierarchy" for Determining the First Deliverer Should Distinguish Between the Scheduling Coordinator and the Facility Operator. During the discussion on first deliverers of electricity, CARB proposed some minor modifications to the definition of electricity importer to clarify the hierarchy of the obligation, which looks to the NERC E-Tag first and then to the scheduling coordinator *or* the facility operator in cases where E-Tag data is not available.¹ However, the facility operator and the scheduling coordinator are not always one in the same. The purpose of defining a hierarchy is to define who owns the power so that an obligation can be assigned. In most cases the owner of the power will be the scheduling coordinator; however, when a broker is involved and ownership of power does not transfer, the obligated entity will be the generator. Accordingly, CARB should identify the hierarchy between the scheduling coordinator and the facility operator as well. At the workshop, CARB staff indicated that the hierarchy would likely impose the obligation on the PSE identified on the NERC E-Tag first, the scheduling coordinator second, and the facility operator third. IEP agrees with this approach and encourages CARB to add this clarification to the proposed modifications.

CAISO's Role Under a Cap and Trade Program Needs to be Clarified. During the workshop the CAISO suggested that if in the past it has been identified as the PSE on a NERC E-Tag (i.e. the entity responsible for importing power to California), and the PSE continues to be a responsible entity under the CARB cap and trade regulations, the CAISO would no longer be identified as the PSE going forward. Essentially, the CAISO indicated that they will not be subject to a GHG emissions obligation. IEP is interested to know how the CAISO will engage in transactions going forward. Who will be named on the E-Tag as the First Deliverer? If the CAISO plans to avoid a compliance obligation, how and when will their rules/tariff change? It is critical for CARB to answer these questions in advance of the first auction, before obligated entities begin to purchase allowances for their compliance obligation. Obligated entities need to truly understand how the CAISO process will change as it relates/integrates with the cap and trade program. So far, there has been no clear guidance on how transactions that the CAISO

¹ CARB Presentation, slide 11.

currently participates in will change going forward. If CARB does not get this important piece of the regulation right, litigation against the cap and trade program seems inevitable. Answers to these questions need to occur sooner rather than later.

CARB Should Design a Guidance Document that will Provide Clarity on What Constitutes Resource Shuffling. Attributing a default emissions factor to unspecified power equal to the highest emitting resource in a particular area/zone will create an incentive for importers to specify their resources and thereby reduce the probability that resource shuffling will occur. Unfortunately, CARB did not adopt this approach in the design of its cap and trade program. Instead, CARB is requiring companies to complete an attestation stating that they have not engaged in resource shuffling, without providing much guidance on what does/does not qualify as resource shuffling. To the extent that CARB can provide clarity on what would qualify as resource shuffling, through a guidance document or some sort of pre-approval process for energy transactions, that would be helpful. Resource shuffling must be discouraged in order to avoid leakage and other anticompetitive impacts that would be detrimental to the overall goals of the cap and trade program. However, without clarification, regulated entities will not know when otherwise legitimate market transactions would be perceived as avoiding an emissions obligation, and thus constitute resource shuffling.

Electrical Distribution Utilities Should Not be Able to Use Allowances/Allowance Value for Sales into the CAISO Market; CARB Has Taken the Correct Approach. CARB staff is proposing to maintain Section 95892(d)(5) of the regulation, which prohibits the use of the value of any allowance freely allocated to an electrical distribution utility from being used to meet a compliance obligation for electricity sold into the CAISO market. IEP agrees with this approach.

As IEP understands it, the small POUs are seeking special treatment with regards to use of allowances and allowance value for electricity sold into the CAISO market. They are claiming financial risk exposure when managing emissions and obtaining compliance instruments, as well as an administrative burden that they might not have otherwise incurred. In response to their claims that they are too small to participate in the allowance market, IEP would like to point out that it is their size that gives them flexibility. As a small entity, they will not have to participate in every auction to meet their compliance obligation, nor will they have to retire all of their allowances at once.

POUs have been given free allowances to be used exclusively for the benefit of retail ratepayers, consistent with the goals of AB 32. As a practical matter, if they are selling into the CAISO markets they should not be getting free allowances because they are in essence behaving like a market participant, not a vertically integrated utility. This argument aside, allowing these small POUs to use allowances or allowance value for their sales into the CAISO market raises significant concerns.

First, if given this special treatment, POUs will have yet another carve-out that is not available to other similarly situated entities. In fact, many small generators, some IEP members, face the same financial risk and administrative burden that is being claimed by the POUs. As noted by CARB, the purpose and criteria for prohibiting use of allowance value for sales into the CAISO market, is to treat all first deliverers equally, whether they are in-state generators or importers of electricity.² If POUs are excused from buying allowances to match the power that

² CARB Presentation Materials, slide 14.

they sell into the CAISO market, they will have a competitive advantage against those that have to bid electricity into the CAISO market with an associated GHG cost (i.e. independent power producers). As a result, all else being equal, POUs will always clear the CAISO market because their power will always be cheaper. Giving the POUs this special treatment will essentially remove the balance between in-state and out-of-state resources, as well as the treatment of independent power producers versus electric distribution utilities.

Second, if the POUs are allowed to use free allowances/allowance value to manage their sales into the CAISO market, they will have an incentive to maximize the value associated with their free allowances, which could lead to resource shuffling. Since POUs act as generators and load serving entities, POUs have an opportunity to leverage their allowances to seek the lowest cost option to serve their load. In order to avoid these potential detrimental effects, CARB has appropriately excluded allowances/allowance value from being used to match sales into the CAISO market.

The QE Adjustment Should Maintain the Simultaneous/Near Simultaneous Condition to Avoid Resource Shuffling. The Qualified Export (QE) adjustment should be designed such that it does not impede simultaneous or near simultaneous “wheel through” transactions; however, it must be stringent enough so that it does not foster resource shuffling. Resource shuffling, whether it occurs inside or outside of the state, is a bad outcome for the cap and trade program. While IEP supports the concept of the QE adjustment and agrees that a QE adjustment should be retained, it is apparent that the market effects of the QE adjustment will need to be monitored over time, including the effect that the QE adjustment has on resource shuffling. As IEP understands it, the QE adjustment may be made for exported and imported electricity during the same hour by the same PSE. IEP does not support expanding this concept to include transactions that occur outside of the hour. Accordingly, CARB needs to maintain the simultaneous/near simultaneous requirement (i.e. within the hour) as suggested in the current regulation.

In Conclusion, IEP thanks CARB for the opportunity to comment on the May 4, 2012 Cap and Trade Program Electricity workshop. IEP appreciates CARB’s attention to these unresolved issues.

Respectfully Submitted,



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