

June 27, 2012

**Comments of the Independent Energy Producers Association
On CARB's Amendments to the California Cap on Greenhouse Gas Emissions And
Market-Based Compliance Mechanisms**

The Independent Energy Producers Association ("IEP") submits these comments on the California Air Resources Board ("CARB") Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms and the Amendments to Allow for the Use of Compliance Instruments Issued by Linked Jurisdictions. IEP represents over 26,000 MWs of installed, non-utility, independently owned generation resources in California. IEP's involvement in the cap and trade rulemaking has been 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 proposed amendments are identified below.

I. Pre-Existing Contracts Without a Reasonable Means of Cost Recovery Should be Treated Comparably Across Linked Jurisdictions. IEP remains concerned that neither the proposed amendments to the cap and trade program nor the proposed amendments on linkage address the treatment of existing contracts that do not have a reasonable means of recovering the cost of GHG allowances required for their continued operation. For a small subset of IPPs operating under existing contracts, currently no viable mechanisms exist within their existing contract structures to recover the cost of the GHG allowances they must obtain to comply with the Cap and Trade (C&T) program.

The Quebec Regulation, on the other hand, provides a free allocation to electric power generation sold under a fixed-price contract executed before January 1, 2008, that has not been renewed or extended after that date.¹ Unlike the Quebec Regulations, the amendments to the California cap and trade program and the amendments to facilitate linkage provide no consideration of this issue whatsoever. This lack of specific consideration in the cap and trade regulation regarding generators caught in these specific circumstances raises serious equity and consistency concerns not only in the context of the California cap and trade program, but also in the context of linking in form and function to the Quebec program.

CARB Staff has indicated its preference for resolution of this issue through contract renegotiation between contract counterparties; however, the counterparties to the IPPs have no incentive to renegotiate these contracts. In fact, the buyer in the context of these pre-existing energy contracts may have a clear incentive to not renegotiate these energy transactions as the counterparty/buyer will garner windfall profits from the sale of the electricity in a market where the Market Clearing Price ("MCP") contains a GHG value.

¹ See Quebec Regulation, App. C, Pt. 1, Table A.

Quebec has addressed the competitive concerns related to assigning GHG costs to generators that have no means of passing those costs through in a satisfactory manner by allocating free allowances to these entities. In the effort of making the Quebec and California programs as compatible as possible, CARB should actively engage in a solution for generators that do not have a means to pass through the GHG costs associated with their fixed price contracts.

IEP Recommendation: CARB should commit now, in a Resolution, to resolve the treatment of existing contracts without a reasonable means of GHG cost recovery by the end of 2012.

II. Auction Purchase Limits

A. The Auction Purchase Limit Discriminates Against Independent Generators. The proposed amendments to the cap and trade program set an auction purchase limit for current vintage allowances at 15 percent of the allowances offered for auction for all Covered Entities, except electrical distribution utilities.² For electrical distribution utilities, CARB is proposing an auction purchase limit equal to 40 percent of the allowances offered for auction.³ While IEP appreciates CARB's proposal to include a purchase limit for electrical distribution utilities, as opposed to imposing no limit at all as was considered in prior proposals; CARB is creating a discriminatory outcome between Independent Power Producers ("IPP") and Utility-Owned-Generation ("UOG") by establishing a purchase limit for electrical distribution utilities that is nearly three times the purchase limit for IPPs.

This proposal has a number of anti-competitive features. First, CARB is affording electrical distribution utilities significant flexibility in managing their compliance obligations through a significantly larger purchase limit, which is not available to other covered entities. Second, this policy could enable electrical distribution utilities, acting on behalf of their UOG, to obtain more allowances than they need for their own compliance obligation, only to sell those allowances back to their IPP competitors when prices are high. Furthermore, CARB is proposing this policy in spite of the fact that independent power producers generally have greater risk for cost recovery than electrical distribution utilities. Electric distribution utilities have a guaranteed rate of return and ensured cost recovery for GHG related costs from ratepayers. IPPs must recover these costs from the competitive market.

B. The Auction Purchase Limit Should Be Scaled to Need. The purchase limit must be established such that all covered entities face comparable opportunities/risks buying out of the auction those allowances necessary to meet their compliance obligations. Accordingly, CARB should set a purchase limit that recognizes different covered entities vary in the magnitude of their compliance obligations, and if purchase limits do not reflect this reality they will have disproportionate impacts on covered entities.

For example, while the 15% purchase limit may have little, if any, impact on relatively small emitters of GHG, such a proposal for relatively larger emitters or those with corporate associations may create constraints on their ability to choose which auctions to enter, when to purchase allowances from the auction, etc. In recognition of the dissimilar effect that the purchase limit will have on different covered entities, the Purchase Limit should generally remain at 15% of the allowances offered for auction; however, for large covered entities or a

² Section 95911(d)(4)(a); Section 95911(d)(4)(b); Section 95914(d)(3)(a)

³ Section 95911(d)(4)(a); Section 95911(d)(4)(b); Section 95914(d)(3)(a)

group of covered entities with a corporate association, CARB should set the Purchase Limit for these entities such that recognizes the different magnitudes of compliance obligations. IEP believes that this adjustment may only apply to a very small subset of covered entities or a group of covered entities with a corporate association. This amendment should be made to the regulation prior to the first auction in 2012.

IEP Recommendation: The auction purchase limit should be set at a level that makes the impact of the limit comparatively proportional for covered entities based on the size of their compliance obligation; and, it should make no distinction as between ownership type (e.g. UOG vs. IPP).

III. Section 95921(f)(1) is Problematic for Transactions that Occur Between Electric Distribution Utilities and their Counterparties. Section 95921(f)(1) now states that “an entity cannot acquire allowances and hold them in its own holding account on behalf of another entity.”⁴ This language prohibits transactions where an electric distribution utility acquires allowances on behalf of a generator pursuant to a contract between the two entities. For example, an electrical distribution utility may be in charge of the dispatch of a generator’s unit and subsequently responsible for obtaining the respective allowances to satisfy that generator’s compliance obligation; however, this language would prohibit that kind of contractual agreement. There must be some room for Electric Distribution Utilities to obtain allowances on behalf of their counterparties pursuant to the stipulations of their contracts.

IEP Recommendation: CARB should strike Section 95921(f)(1) as currently drafted. Alternatively, we support a structure that enables electric distribution utilities to meet their contractual obligations (and/or cover a compliance obligation if a pre-existing contract) and obtain allowances for the compliance purposes of an electric generator (e.g. their counterparty).

Respectfully Submitted,



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⁴ Section 95921 (f)(1)