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July 9, 2013

Dr. Steven Cliff
Chief, Climate Change Program Evaluation Branch
California Air Resources Board
1001 I Street
Sacramento, CA 95812

Re: M-S-R Comments on June 25 Cap-and-Trade Workshop

Dear Steve:

M-S-R Public Power Agency¹ (M-S-R) provides these comments to the California Air Resources Board (CARB) regarding the June 25, 2013 Cap-and-Trade Workshop addressing compliance matters, information disclosure, and cost containment provisions in the Cap-and-Trade Regulations (Regulations). In these comments, M-S-R explains why CARB should add a subcategory of allowances in the compliance account that can distinguish between purchased and freely allocated allowances before the instruments are withdrawn for retirement, as well as why CARB should not release individual compliance account balance information. M-S-R also urges CARB not to shorten any of the current reporting and/or verification timelines.

Retirement of Compliance Instruments

CARB should revise the proposal for withdrawal of compliance instruments for retirement to distinguish between allowances purchased by an electrical distribution utility versus those that are freely allocated. During the June 25 Workshop, staff set forth a proposal that would specify the order in which allowances are withdrawn by the Executive Officer from

¹ Created in 1980, the M-S-R Public Power Agency is a public agency formed by the Modesto Irrigation District, the City of Santa Clara, and the City of Redding. M-S-R is authorized to acquire, construct, maintain, and operate facilities for the generation and transmission of electric power and to enter into contractual agreements for the benefit of any of its members.

an entity's compliance account for retirement. Allowances would be withdrawn each year in order to meet both the annual surrender obligation, as well as the triennial compliance obligation at the end of each compliance period. Staff has proposed that for both the annual and triennial surrender, allowances would be withdrawn from the compliance account beginning with offsets, followed by any allowances purchased from the Allowance Price Containment Reserve Account (APCR), followed by other allowances. The remaining allowances (exclusive of "true-up allowances") would be withdrawn by vintage, beginning with the earliest vintage. M-S-R agrees that offsets and allowances purchased from the APCR should be withdrawn first. For the third tier of allowances that are withdrawn, however, CARB must distinguish between freely allocated allowances and those that are purchased through the auction or market. The need to make this distinction is based on the fact that electrical distribution utilities that receive freely allocated allowances are restricted in how they can spend the proceeds (or imputed value) of those allowances. These restrictions include a prohibition on the "use of such allowances to meet compliance obligations for electricity sold into the California Independent System Operator markets." (Section 95892(d)(5)) Under the Regulations, POUs may elect to place their freely allocated allowances directly into their compliance accounts, which designation must be made by September 1 of each year prior to receiving the annual allocation. (Section 95892(b)(2)) This creates the potential for POUs to have freely allocated allowances in their compliance account that may be older than purchased allowances, but yet should not be retired because such retirement may result in a violation of the use restrictions placed on free allowances. Because the allowance designation is made in advance and because covered entities may not remove allowances from their compliance accounts once that designation has been made, there are circumstances under which a POU may have compliance obligations associated with sales into the CAISO for which they may not use the freely allocated allowances already in their compliance account. In such instances, the freely allocated allowances should remain in the compliance account, and CARB should withdraw the purchased allowances in the corresponding amount.

In order to address this situation, M-S-R recommends that allowances to be withdrawn from the compliance account for retirement purposes be distinguished between freely allocated allowances and purchased allowances.

Publication of Entity-Specific Compliance Account Balances

CARB should not allow the disclosure of non-aggregated compliance account data during the intervening years of a compliance period. Staff's proposal to release entity-specific compliance account balances each quarter would jeopardize the ability of M-S-R's members and other compliance entities to effectively strategize for the acquisition of necessary allowances, and would increase the costs associated with complying with the Regulations. During the Workshop, Staff set forth a proposal for the public disclosure of information relevant to the Cap-and-Trade Program including allocation data, CITSS registrants, retired instruments, and offset project data. Also included in this list was the proposal to disclose compliance account balances on the last business day of each quarter. During the Workshop presentation, Staff noted that all options were still being considered, including alternatives to individual account balance disclosure. Staff opined that it was necessary for the markets to know compliance account balances in order to function properly and send the correct signals regarding long positions. In balancing the potential exposure to compliance entities against the potential benefits of preventing market manipulation, CARB must consider not only what the public knows, but its own role in tracking compliance transactions as well as that of the market monitor. M-S-R concurs with the chorus of stakeholders that opposed the release of this information on an entity-specific level, noting that release of this information in aggregate properly addresses all of the concerns raised by Staff. The release of this of this information in the aggregate would allow market participants and monitors alike to gauge whether the market is short or long, while preserving confidential strategies covered entities employ to meet their compliance obligations. Dissemination of entity-specific data will not provide the market with any greater clarity, but could severely disadvantage the compliance entity by providing savvy and sophisticated market participants with insights into allowance acquisition strategies.

Furthermore, disclosure of individual account balances would violate the provisions of Section 95921(e), which specifically direct the Executive Officer to "protect confidential information to the extent permitted by law." It is within this framework that the Regulations call for the disclosure of compliance account balances. All information regarding account balances and trading conduct – both in the auction and secondary markets – is subject to ongoing review and analysis by CARB and the market monitor. Accordingly, any anomalies relevant to

individual conduct will be scrutinized and reviewed and the transparency needed to ensure a robust and viable market is achieved by the disclosure of aggregate account balance information.

Conclusion

M-S-R appreciates the opportunity to provide these comments, and the ongoing efforts of CARB Staff to work with stakeholders to ensure the viability and success of not only the Cap-and-Trade Program, but of the very businesses and industries subject to the Regulation. To that end, M-S-R strongly encourages CARB to add a subcategory of allowances in the compliance account that can distinguish between purchased and freely allocated allowances before the instruments are withdrawn for retirement. M-S-R also urges CARB not to release compliance account balance information for individual accounts, but rather release the information only in the aggregate, as not to harm or disadvantage compliance entities. Finally, M-S-R agrees with the comments raised by other stakeholders opposing any changes to the reporting and/or verification timelines that would constrain or reduce the amount of time that a covered entity has to complete its necessary reporting and verification processes.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'M. Hopper', with a stylized flourish at the end.

Martin Hopper
General Manager
M-S-R Public Power Agency