BP America, Inc.

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Via Email
Dr. Steve Cliff
California Air Resources Board
1001 I Street, P.O. Box 2815
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Subject: CARB Cap and Trade Proposed Regulatory Amendments

Dear Steve:

BP America, Inc. submits these comments on the Proposed Changes to the California Greenhouse Gas Cap and Trade Regulations as detailed in the Discussion Draft dated July, 2013.

Compliance Timelines
Though actual regulatory changes do not appear to exist in either the proposed regulatory amendments to the Cap and Trade Regulation or the Mandatory Reporting Regulation, staff is proposing to move up the deadline for MRR verification by two weeks – from September 1 to August 15. BP strongly objects to moving up this deadline because the proper timeframe needs to be allowed to ensure a rigorous verification process is maintained and that reported data is properly corrected if any errors are discovered during the verification process. The current verification window ensures that there is adequate time and resources available to support the verification process. Regulated entities with complex process or accounting records may need to address multiple iterations of data requests to verifiers, and may also need to correct and resubmit reports based on the verification process. The current verification window between April and September also occurs during a very busy reporting period for both Environmental and Accounting professionals. Meeting the September 1 deadline is already challenging.

We request that the September 1 date for verification remain as is. If certain sectors believe they need more time between verification and participation in a future auction, the regulation should move up the verification timeline for that sector only – and not for all regulated entities.

Clarity on documentation on short-term transactions needed
The Regulation has not added language to clarify documentation requirements for short-term power transactions. During discussions at the July 23 webinar, staff indicated a preference for something comparable to a Western Systems Power Pool (WSPP) Master Agreement for sale of electricity to explicitly state when parties to that agreement intend to allow for the short-term transactions of specified electricity via oral confirmation alone. This is not standard industry practice, nor is it being contemplated in the approach currently being developed by the WSPP. The Regulation should indicate what documentation (such as summaries, transcripts of oral confirmations, IMs) would be considered sufficient for reporting such short-term transactions.

Registration & Account Requirements
BP understands and appreciates the objectives of transparency and public disclosure in regulatory proceedings and the need to safe guard against the potential for collusion and sub-optimal market behavior in meeting environmental goals through market mechanisms. However, we believe there are several examples within the regulation of the "cure being worse than disease" as discussed in the following sections.

§95830 Registration with ARB
BP is concerned that the disclosure requirement to provide names and contract information for "all persons employed by the entity that will either have access to any information regarding compliance instruments, transactions or holding, or be involved in decisions regarding transactions or holding of compliance instruments" is overly broad, onerous, unworkable, and unnecessary. As currently drafted this requirement would create significant administrative burden - especially for large corporations where literally hundreds of people could have knowledge of, access to, or input to information or decisions regarding these issues. BP therefore recommends that the Regulation narrow the proposed language to identify employees who have delegated authority to commit the company to purchases and sales of compliance instruments.

§95833 Disclosure of Corporate Associations
BP understands the need for CARB to be aware of and track corporate associations for those participating in the state's CARB's cap-and-trade program. However, under the proposed changes to the rule, the requirement that a company list all of its associations, regardless of whether those corporate associations have ever participated in the cap-and-trade program is onerous and unnecessary to the proper functioning of the program.

BP, as one of the largest and most diverse corporations in the world, has hundreds of such associations across the globe that could fall under the overly broad reach of the proposed regulation. The vast majority of these corporate associations – whether they are a wind farm in Texas, a refinery in Ohio or Australia, or a pipeline in Azerbaijan - are not even remotely related to or impacted by BP's transactions in CARB's cap and trade program.

BP routinely buys and sells business lines in response to changes in the prospects of particular products or markets around the world. If such changes would trigger a change in registration, both for CITSS and the auction of allowances, BP would be faced with continually burdensome paperwork to register each change for what appears to be little or no benefit to California consumers or the health of the carbon market. The larger potential

impact, however, would be felt because of the proposed changes in subsection 95912(d)(5): "an entity with any changes to the auction application information list in subsection 95912(d)(4) 30 days prior to an auction, or an entity whose auction application information will change 15 days after an auction, will be denied participation in the auction." Due to the proposed ongoing obligation for BP to update its corporate associations coupled with the denial of participation in upcoming auctions if in fact such a change will occur during the stated time frames, BP could face a situation where a good faith effort to comply with the regulations makes it ineligible to participate in the market.

If there is evidence that a company may have been engaged in collusion or market manipulation, then the CFTC, as part of an investigation, could request that the company submit information on all of its corporate associations and the links among them to investigate the issue.

BP recommends that the proposed language "regardless of whether the second entity is subject to the requirements of this article" be removed *and* that the Regulation clarify that notification is required only for corporate associations that have a compliance obligation or that are planning to hold or trade compliance instruments.

Compliance Requirements for Covered

(§95856) EntitySurrender of Compliance Instruments
BP opposes the proposed regulatory provisions specifying a particular order of retirement of compliance instruments and is particularly troubled by the potential for CARB to confiscate carbon offsets surrendered above the 8% quantitative limit. BP believes that the covered entity, not CARB, should decide which compliance instruments should be surrendered.

A covered entity may have a variety of commercial reasons to retire certain types and particular vintages of compliance instruments in a given year or compliance period. Such flexibility will reduce the cost of the program to industry and consumers.

BP recommends that introducing this flexibility for individual account holders to designate compliance instruments for retirement, by type and vintage, can be facilitated by providing each regulated entity a retirement account. Covered entities can then transfer the desired compliance instruments into the retirement account and if a covered entity does not do so by a required date, CARB can retire compliance instruments according to the priority identified in the Proposed Regulatory Amendments.

Trading & Banking

§ 95921 Conduct of Trade
We assume that CARB's intention in asking for the proposed data is to ensure that the market is functioning and healthy. However, if this in fact the intent, then BP believes sufficient reliable information providing secondary market details will be available from ICE and other exchanges without creating the duplicative and unnecessary administrative burden that would be imposed by this proposed change to the Regulation. Requiring

additional data will increase administration costs to market participants with no real benefit to market functionality or operations.

In some instances the data requested may not be readily accessible due to the nature of both OTC multi-commodity and credit deals as well as OTC structured emissions deals where the stand-alone emissions price may not be transparent or able to be unwound. BP is concerned that an inability to 'unwind' and provide price information for a transaction could be considered a transfer request deficiency with potential to prevent transfer of instruments and reduce the liquidity of the market.

BP recommends that the Regulation not adopt proposed changes that require submission of additional data associated with transaction agreements and rely instead on existing sources of price information to monitor the health of the market.

§95923 Disclosure of Cap and Trade Contractors

BP is concerned that the amendments relating to the disclosure of consultants, advisors and cap and trade contractors as currently proposed is overly broad and may potentially extend to the likes of subscription market intelligence services that BP does not believe is CARB's intent. BP recommends CARB narrow its Criteria for Determining cap and trade Contractors, to entities that under ss(a)(1)(b) 'Advises or consults with the entity *on individual market strategy* regarding compliance with the cap and trade Program, and receives information from another registered cap and trade participant'(emphasis added).

Cost Containment

We reiterate our previous submitted concerns on cost containment. We believe the current proposed regulatory amendments on cost containment do not go far enough in that they do not bring additional compliance instruments into the market. The proposed method for cost containment may be able to address limited, temporary price spikes, but will not address the more concerning and damaging structural or persistent high allowance costs in the cap and trade program. Moreover, to the extent the proposal for cost containment *can* address short term price spikes, it does so in a way that creates greater scarcity of allowances in future compliance years – increasing the potential for future price spikes.

In general, we believe strongly that the right cost containment measures can and should avoid having problems occur in the first place – rather than simply attempting to address a problem once it has occurred. There is no reason or need to allow allowances prices to spike to the highest Allowance Price Containment Reserve (APCR) level before additional cost containment measures take effect. The APCR was designed as a price cap. Cost *containment* design measures are very different than a price cap – and these two very different design elements should not be conflated.

Cost containment measures that suggest re-filling the APCR are fundamentally flawed because they allow prices to run up before any additional cost control measures are put in place. It is very likely that if the program gets to the point where the APCR is exhausted – or nearly exhausted – turmoil in the allowance and energy markets and a consumer backlash will result in swift action by the Governor or the Legislature with CARB losing control of the solution. Moreover, affected businesses dislocated by both the direct and indirect costs of high allowance and energy costs may be forced to make decisions to

reduce, curtail or relocate production before prices reach the level of the highest APCR tier. So while potential action taken by the Governor or the Legislature in reaction to allowance price spikes may be warranted given the potential impacts on the economy from a swift and/or sustained run up in allowances prices, this sort of abrupt action can also have many negative consequences, can't undo decisions that have already been made by businesses – and can be avoided with proper planning and design.

To avoid these abrupt actions, to avoid CARB losing control of the solution, to stay within the requirements of both AB32 and the Board Resolution, and to increase the potential that problems are avoided in the first place rather than fixed after they happen – there are numerous, relatively simple design measures that CARB can put in place. We believe it is possible to design additional cost containment into the system by working with the current design of the system – without the need to add on additional, complex and controversial design elements. These fixes include:

- Increase the offset quantitative limit and allow use of international offsets
- Increase liquidity in offset markets by establishing a registry that links CCO serial numbers to an invalidation guarantee
- Allow covered entities that do not use their entire eight percent offset limit to redistribute that unused portion into the market or to other covered entities. This concept has been discussed in several forums between market participants and staff. BP would be happy to share with staff our specific thinking on this topic.
- Remove or greatly increase holding limits for regulated parties
- Allow use of allowance vintages from within the year in which the compliance obligation is due – not in which it is calculated

BP's comments of July 9, 2013 further detail our recommendations on cost containment and the elements listed above.

Allowance Allocation

The Proposed Amendments which allocate additional allowances to trade exposed industry, we believe, is a positive development that reduces the burden on consumers and regulated industry, maintains the environmental integrity of the program, and increases the political and economic sustainability of the program.

With regard to the proposal to fully allocate free allowances to natural gas suppliers, we are concerned that this proposal creates additional market distortions on top of those already in place due to the allocation and use of revenue for the electric utility sector.

We are sympathetic to the need to protect ratepayers, consumers and industry from the costs of the program. While a price signal is a necessary part of a market based program, all reasonable opportunities to reduce impacts on consumers and industry, where the environmental integrity of the program can be maintained, should be pursued. However, a primary objective of a market-based, GHG-reduction program, such as a cap and trade program, should be to establish a broad, consistent price for carbon across the widest segment of the economy as is practicable. A broad, consistent carbon price will result in

the fairest, most effective and most efficient reduction of GHGs and will best distribute the economic burden and increasing opportunities for low-cost abatement measures.

A cap and trade system that distinguishes emissions from different sectors for differential treatment does not result in market consistency, does not equitably distribute economic burden and opportunity, and is a serious violation of the intent of a cap and trade program. This is the case when it comes to the Regulation's treatment first of the electricity sector and now natural gas suppliers – with the planned the use of auction revenue to mitigate the price impact of carbon costs in these sectors – and in these sectors only.

A clear example of the market distortion created by this inequity is a consumer faced with the choice of purchasing a device, appliance or vehicle based on the fuel used. All other factors being equal (including the carbon intensity of the chosen fuel), with the inequities created by the current and proposed regulations, the choice of fuel to operate the device, appliance or vehicle will be influenced by the fact that the use of electricity and natural gas comes with a monthly rebate check (or other mechanism to mitigate the cost), while the use of gasoline, diesel or other fuels does not. So Mrs. Smith who fuels her vehicle with gasoline pays for the full GHG emissions from that fuel while Mrs. Jones who charges her electric vehicle (potentially powered by coal) or fuels it with natural gas does not. This is a clear and unacceptable market distortion and a divergence from the intent of a cap and trade system.

While we are aware that other programs within AB32 are meant to incentivize certain fuels, providing incentives for individual fuels should not occur within a market based program such as cap and trade. This picking of winners and losers distorts the effect of decisions that actually should influence energy choices and consumption. Emissions and consumers must be treated equally, under a market based program, in order to provide the proper incentive for reductions and for energy consumption choices. In order for the cap and trade program to be successful and equitable, the criteria for allocation must be consistent amongst sectors – and the use of auction revenue should not result in arbitrary, differential price signals amongst energy types.

Please don't hesitate to contact me should you have questions regarding this correspondence.

Sincerely,

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Sr. Director, Governmenta & Public Affairs
BP America, Inc.

cc (via email): Edie Chang
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