

August 2, 2013

**Comments of the Independent Energy Producers Association on
CARB's Discussion Draft on 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's *Discussion Draft on the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms* ("Discussion Draft") released July 2013. IEP's comments also address the workshop convened Thursday, July 18, 2013. The comments focus initially on CARB staff's proposal for "Legacy Contracts," followed by comments on other proposed changes to the cap and trade regulation.

- I. Legacy Contracts.** Board Resolution 12-33 requires CARB staff to provide "transition assistance to covered entities that have a compliance obligation cost that cannot be reasonably recovered due to a legacy contract."¹ In response, CARB staff has proposed an allocation to legacy contract generators for years 2013 and 2014, using 2012 emissions data and 2015 vintage allowances.²
 - a. Transition Assistance for Legacy Contracts Must Extend for the Duration of the Existing Contract.** In both the workshop on July 18th and in the *Notice of Public Availability of the Cap-and-Trade Discussion Draft and Workshop* ("Summary of Proposed Modifications") CARB staff indicated that "transition assistance, limited to the 2013 and 2014 emissions for the portion of a generator's output subject to legacy contract, appropriately recognizes those that have remaining legacy contracts concerns while maintaining a strong incentive to continue renegotiation."³ IEP strongly disagrees.

Legacy Contracts are defined as:

"a written contract or tolling agreement governing the sale of electricity and/or qualified thermal energy from an electric generating facility or cogeneration facility at a price, determined by either a fixed price or price formula, *that does not allow for recovery of the costs associated with compliance of this regulation...*"

(Discussion Draft, page 28, emphasis added)⁴

¹ California Air Resources Board Resolution 12-33.

² Workshop Presentation on Proposed Changes to the California Greenhouse Gas Cap-and-Trade Regulations, slide 69.

³ *Notice of Public Availability of the Cap-and-Trade Discussion Draft and Workshop*, page 17.

⁴ *Discussion Draft on the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms*, Section 95802(a).

Unlike obligated entities that have a reasonable means for passing through the costs of their GHG compliance obligation, generators operating under Legacy Contracts, by definition, do not have a reasonable means of cost recovery for their AB 32 compliance obligation for the entire duration of their existing contract. Under these circumstances the Board's directive to provide transition assistance could not reasonably be inferred to mean "for only a short period of the existing contract" or else the Board would have stated so in Resolution 12-33. Transition assistance for legacy contract generators should be required for the duration of the existing contract as a matter of fairness and equity.

The staff proposal to provide transition assistance to legacy contract generators only for 2013 and 2014 significantly truncates the transition assistance that is actually needed by these Legacy Contract generators and does not fully address the compliance costs that cannot be reasonably recovered due to a Legacy Contract. *IEP recommends, consistent with Resolution 12-33, that CARB provide transition assistance to Legacy Contracts for the duration of their existing contracts.*

- b. Little Incentive Remains for Renegotiation.** CARB staff indicates that transition assistance, limited to 2013 and 2014 maintains a strong incentive to continue renegotiation.⁵ However, IEP is not convinced that the staff's proposal creates any new incentive for renegotiation among contract counterparties.

Where the counterparty is 1) a marketer; 2) an industrial entity that does not receive a free allocation; or 3) an IOU, no incentive exists to renegotiate. The only circumstance where there *may* be some incentive to renegotiate is in situations where the contract counterparty is an industrial entity receiving a free allocation. As IEP understands it, only in this instance does CARB propose to subtract allowances from those allowances freely allocated to counterparties of legacy contract generators. Even in this case, there is not a huge incentive for contract renegotiation.

- c. CARB Cannot Wait to Address Legacy Contracts that Extend Beyond 2014.** While CARB continues to press for re-negotiation for these limited number of deals, IEP is not convinced, as described above, that there is a real incentive to renegotiate. In the meantime, these Legacy Contract holders are facing the real world implications of having unrecoverable costs associated with their generation assets which lead to downgraded credit ratings, inability to finance debt, etc.

In addition, CARB is currently proposing to allocate 2015 vintage allowances to legacy contract generators for transition assistance for 2013 and 2014 mainly because there are no more 2013 or 2014 vintage allowances left to allocate. If CARB waits too long to address legacy contracts that extend beyond 2014, no more current vintage allowances for those years will be available to allocate. As a result, it is important for CARB to make decisions now regarding how allowances will be divvied up for Legacy Contract generators in the out years.

⁵ Notice of Public Availability of the Cap-and-Trade Discussion Draft and Workshop, page 17.

- d. **CARB Should Provide Transition Assistance for the duration of the Existing Legacy Contract Irrespective of Counterparty.** IEP appreciates CARB's acknowledgement that a common solution should be provided to all legacy contract generators regardless of the counterparty.⁶ IEP supports CARB taking full responsibility for all legacy contract generators, including legacy contracts with IOU counterparties.
- e. **Emissions Associated with Legacy Contracts are De Minimis from a Program-Wide Perspective, Yet Likely Create a Significant Cost Burden on Individual Generators.** The allowances that CARB would need to cover all Legacy Contracts for the duration of their existing contracts is de minimis, particularly in comparison to all the other freely allocated allowances throughout the duration of the cap and trade program. As these contracts expire, allocation to Legacy Contracts necessarily will decline. Furthermore, as the cap declines the coverage to legacy contract generators will also decline.

The facts reveal that the emissions associated with legacy contract generators are de minimis in terms of the overall cap and trade program. As a matter of fairness and equity, it is appropriate for CARB to provide Legacy Contract generators with allowances to cover their compliance obligation for the duration of their existing contract.

- f. **2015 Vintage Allowances Allocated to Legacy Contract Holders for 2013 and 2014 Should be Eligible for Use Prior to 2015.** During the workshop, CARB indicated its intent to allow 2015 vintage allowances, allocated to legacy contract holders for 2013 and 2014 emissions, to be used for compliance prior to 2015. IEP supports this approach. Unfortunately, language signifying this intent was not included in the Discussion Draft. CARB's proposal to allocate allowances to these generators, which cannot be used until 2015, defeats the purpose of providing these generators with an allocation. *Importantly, CARB should ensure that these 2015 allowances granted for 2013 and 2014 emissions are available to be used by the affected generators in time for the first annual surrender obligation (November 2014).*
- g. **2013 Emissions Data Should Determine the Allowance Allocation Granted to Legacy Contract Generators for the 2013 and 2014 Transitional Period.** CARB is proposing to use 2012 emissions data to calculate the allocation that will be granted to legacy contract generators for the 2013 and 2014 transitional period. Given that the actual allocation will not occur until October 15, 2014, CARB should use 2013 emissions data, which will be reported and verified prior to the 2014 allocation date to determine the amount of the allocation.

Using 2013 emissions data will more accurately represent the emissions for 2013 and 2014 because the information will be closer in time to the actual allocation in 2014. This is consistent with how CARB is proposing to determine the allocation for natural gas suppliers, which will use 2013 data for determining their allocation

⁶ Notice of Public Availability of the Cap-and-Trade Discussion Draft and Workshop, page 17.

granted in 2014.⁷ Accordingly, IEP recommends using 2013 emissions data for determining the allocation for 2013 and 2014 transitional assistance to legacy contract generators.

II. Other Comments Associated with the Proposed Changes to the Cap and Trade Regulation.

- a. **Potential Changes to the Mandatory Reporting Program May Hinder Obligated Entities' Ability to Provide the Most Accurate Data.** During the July 18th Cap and Trade Workshop, CARB staff discussed the proposal to move the emissions verification deadline up in time from September 3rd (current requirement) to August 15th (proposed change). In prior workshops CARB indicated that the proposal to move the emissions verification deadlines forward created an opportunity for more people to know their final emissions obligation so that they could participate in the Allowance Price Containment Reserve (APCR) to obtain any residual allowances they may need before the compliance obligation is due in November. In prior workshops CARB insisted that they did not want to move the APCR to a later date, which was CARB's reasoning for moving up the emissions verification deadlines.

CARB is now proposing to move the emissions verification deadlines forward in time and the APCR back in time.⁸ Given that the CARB has moved the APCR sale to a later date, it is unclear why the emissions verification deadline must be moved forward. By moving the APCR back, the emissions verification deadline could stay the same (i.e. current requirement of September 3rd) while still allowing more people to participate in the later reserve sale.

Given CARB's intent to receive the most accurate reporting data from obligated entities, moving the emissions verification dates up, even if only by a few weeks, may hinder obligated entities' ability to provide the most accurate data. According to a CARB news release dated July 12, 2013, "Nine companies have been fined for failure to supply complete information by the appropriate deadlines for either the reporting or verification stages."⁹ The article reports that the fines assessed totaled approximately \$295,000, with the largest penalty imposed at \$120,000. Moving the verification deadlines forward will only create an additional burden on obligated entities.

Given that each of these penalties were related to either the "reporting or verification stages" IEP is concerned that moving the verification deadlines up, as proposed in the workshop materials may hinder an obligated entities ability to provide the most accurate data. In order for CARB to obtain the most accurate information from obligated entities, IEP recommends **against** moving the reporting verification deadlines up and suggests that the CARB maintain the status quo in terms of

⁷ *Discussion Draft on California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms*, Sections 95870(i); 95893(a)

⁸ Workshop Presentation on Proposed Changes to the California Greenhouse Gas Cap-and-Trade Regulations, slide 44, 45

⁹ CARB News Release #13-39: *Air Resources Board fines nine companies under greenhouse gas reporting rule*, July 12, 2013.

verification deadlines. Further, as the reserve sale has been moved to a later date, the original intent for moving the verification deadlines forward no longer exists.

b. Obligated Entities Should Have the Ability to Designate Which Compliance Instruments are Ultimately Retired Once Placed into the Compliance Account.

CARB is proposing to retire compliance instruments in the following order: offsets, allowances (earlier vintages first), future vintage allowances up to the true up allowance amount, and then allowances purchased from the Allowance Price Containment Reserve.¹⁰ As a practical matter, each of these instruments are essentially equal in terms of meeting a compliance obligation under the cap and trade program; thus the only reason for CARB to put an order on how allowances are retired is in the case that there are more allowances in a compliance account than are actually needed to meet a compliance obligation.

Rather than specifying an arbitrary order for how compliance instruments ought to be retired, the discretion for determining which compliance instruments are ultimately retired should be up to the obligated entity. For example, if an entity places more compliance instruments in its compliance account than are actually needed for a compliance obligation, CARB should retire only the allowances that are actually needed to meet the compliance obligation. To the extent that more allowances in a compliance account exist than are needed to comply, those remaining instruments should remain in the entities compliance account for future use. If an entity wants to voluntarily submit additional allowances in excess of its compliance obligation that should be a separate designation. Given that each of the allowances has a unique serial/identification number, this functionality should not be too difficult to implement.

Accordingly, IEP supports the concept as discussed at the workshop of allowing an obligated entity to designate which compliance instruments in the compliance account are ultimately retired by CARB. This recommendation supplants the need for an ordering of compliance instruments.

c. Allocations to Natural Gas Suppliers Should Be Appropriately Tracked and Monitored.

Natural gas suppliers may also own, operate, and develop electric generation assets in competition with independent power producers (IPPs). Accordingly, any freely allocated allowances to these utilities on behalf of their natural gas interests, must be tracked, monitored, and accounted for by an appropriate regulatory agency such as the CPUC. CARB must be mindful that these allowances (or their intrinsic value) could be reattributed in a manner that inappropriately creates competitive advantage, an outcome that to date CARB has steadfastly opposed.

Going forward, the regulatory agencies should not delegate to the utilities the responsibility for managing how those allowances or their value are distributed. Rather, CARB should require proper oversight, and ensure that these allowances are fully tracked and monitored in terms of their use while subject to appropriate regulatory oversight.

¹⁰ Workshop Presentation on Proposed Changes to the California Greenhouse Gas Cap-and-Trade Regulations, slide 38

IEP appreciates the opportunity to comment on CARB's *Discussion Draft on the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms*. IEP looks forward to working with CARB staff as these issues unfold.

Respectfully Submitted,



Steven Kelly
Policy Director
Independent Energy Producers Association
1215 K Street, Suite 900
Sacramento, CA 95814
(916) 448-9499
steven@iepa.com



Amber Riesenhuber
Policy Analyst
Independent Energy Producers Association
1215 K Street, Suite 900
Sacramento, CA 95814
(916) 448-9499
amber@iepa.com