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August 2, 2013

Chief
Climate Change Program Evaluation Branch
California Air Resources Board
1001 "I" Street
Sacramento, California 95812

Dear Sir /Madam:

Subject: Los Angeles Department of Water and Power (LADWP) Comments
California Air Resources Board (CARB) Greenhouse Gas
Cap-and-Trade Regulation

The LADWP appreciates the opportunity to submit the following comments on CARB's proposed changes to the California Greenhouse Gas Cap-and-Trade Regulations released on July 15, 2013 and presented at its public workshop on July 18, 2013.

1. §95802(137) Definition of Imported Electricity

The proposed amendments add the following sentence to the definition of "imported electricity":

Imported Electricity does not include electricity imported into California by an Independent System Operator to meet NERC Reliability Standard EOP-002.

It appears that "Independent System Operator" refers to the California Independent System Operator (CAISO). The purpose of EOP-002 is to ensure Reliability Coordinators and Balancing Authorities are prepared for capacity and energy emergencies. Although the CAISO is a large balancing authority in the state, there are other balancing authorities such as Los Angeles Department of Water and Power (also known as LADWP) which are also subject to EOP-002. In addition, "balancing authority" is already defined in the cap-and-trade regulation whereas "Independent System Operator" is not. Thus, LADWP recommends that the

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definition be revised to apply consistently to all California balancing authorities as shown in underline/strikeout format:

Imported Electricity does not include electricity imported into California by an ~~Independent System Operator~~ balancing authority to meet NERC Reliability Standard EOP-002.

2. §95802(XX) Definition of Futures

CARB is proposing a new definition for "futures" as follows:

"Futures" means an agreement to purchase or sell a commodity for delivery in the future at a price that is determined at the initiation of the contract and that obligates each party to fulfill the contracts at a specified price.

The definition of "future" appears to be partly drawn from the Commodity Futures Trading Commission's (CFTC) definition of "Futures Contract:"

*Futures Contract: An agreement to purchase or sell a commodity for delivery in the future: 1) at a price that is determined at the initiation of the contract; 2) that obligates each party to the contract to fulfill the contract at the specified price; 3) that is used to assume or shift price risk; and 4) that may be satisfied by **delivery or offset** [emphasis added].*

Delivery is not defined in CARB's regulation but CFTC defines Delivery as:

Delivery: The tender and receipt of the actual commodity, the cash value of the commodity, or of a delivery instrument covering the commodity (e.g. warehouse receipts or shipping certificates), used to settle a futures contract.

CFTC defines offset as:

Offset: Liquidating a purchase of futures contracts through the sale of an equal number of contracts of the same delivery month, or liquidating a short sale of futures through the purchase of an equal number of contracts of the same delivery month.

CARB did not include parts (3) and (4) from the CFTC definition and there is no explanation of this new definition in CARB's *Summary of Modifications* document.

CARB seems to be entering into an area that may be wholly or partially governed by CFTC rulemaking and/or the Securities and Exchange Commission related to a number of federal laws, including, for example, the Commodity Exchange Act, 7 U.S.C. §1, et seq., and the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (2010) commonly referred to as the "Dodd-Frank Act." This may be especially true as CARB considers coordinating its cap-and-trade regulation with provinces in Canada, such as the Canadian Province of Quebec.

Furthermore, “[futures contracts or their functional equivalents have been traded for millennia.” *Bloomberg L.P. v. CFTC*, 2013 U.S. Dist. LEXIS 80275 (D.D.C. June 7, 2013). Moreover, defining what is not a “futures contract” may be just as important as defining what is a “futures contract.” For example, the appellate court in the *Bloomberg L.P.* case contrasted a “swap” from a “futures contract.” *Id.* Also, for example, the regulation 17 CFR §1.3(bbbb) defines what a futures contract is not based on certain foreign sovereign debt.

Therefore, CARB may want to either rely on federal definitions of “futures contracts,” similar to its definition of “derivatives clearing organization” in 17 CCR 95814(a)(1)(C), or reconsider the need to redefine terms that have had some history of development over federal law (statutes and regulations) and case law. (see, e.g. 17 CFR §1.3 (e)(“commodity”), (t)(“open contracts”), and (kk)(“strike price”); *United States v. Radley*, 632 F.3d 177, 184 (5th Cir. Tex. 2011); *Bloomberg L.P. v. CFTC*, 2013 U.S. Dist. LEXIS 80275 (D.D.C. June 7, 2013).

3. § 95814(a)(3) and § 95830(c)(1)(I) Registration with CARB

The proposed amendments include a new section (§95814(a)(3)) applicable to an individual employed by an entity subject to requirements of the Mandatory Reporting Rule, or cap-and-trade regulation, or by an organization providing consulting services related to these regulations that chooses to register as a Voluntarily Associated Entity (VAE) in CARB’s trading system. Such individual would be required to provide a notarized letter from the individual’s employer stating that the employer is aware of the employee’s plans to apply as a VAE and that the employer has conflict of interest policies to prevent the employee from using information for personal gain in the cap-and-trade program.

The proposed amendments also contain the following new requirement applicable to entities registering with CARB (§95830(c)(1)(I)):

Names and contact information for all persons employed by the entity that will either have access to any information regarding compliance instruments, transactions, or holdings; or be involved in decisions regarding transactions or holding of compliance instruments; or both. An entity already registered in the tracking system must provide the notarized letter from their employer no later than January 31, 2015.

LADWP believes that CARB’s concern that individuals with access to potential market-related data would use that information for personal gain is addressed in proposed §95814(a)(3). The proposed requirements of §95830(c)(I), if broadly applied, would burden covered entities with the task of providing names and contact information for all employees that will have access to compliance instrument information. Larger companies make decisions related to compliance with the cap-and-trade regulation on several levels: staff, work group, and executive levels which involves a significant number of employees. Requiring the individual be responsible for providing the notarized letter per §95814(a)(3) would be sufficient; thus, LADWP requests that the following language in §95830(c)(1)(I) be added at

the beginning of the provision to narrow the application of the provision to those entities having employees registering as VAEs: “Pursuant to § 95814(a)(3), Names and contact information...”

4. § 95852(b)(2) Resource Shuffling

LADWP appreciates CARB's efforts in working with electric utility entities to develop CARB's Resource Shuffling guidelines. LADWP further supports the inclusion of the guidelines into the rule which provides more certainty with respect to compliance with the regulation.

5. § 95852(b)(3)(D) and 95852(b)(4) REC Retirement for Specified Source Imports and RPS Adjustment

LADWP appreciates CARB's efforts working with electric utility entities in clarifying the timing of the REC retirement to claim the RPS adjustment as well as specifying that REC serial numbers would be reported for specified source imports. The clarification with respect to REC retirement will enable entities such as LADWP to claim an RPS adjustment without being required to prematurely retire its RECs under the California Energy Commission's Renewable Portfolio Standard Program.

6. § 95856(h) Compliance Instrument Retirement Order

CARB's proposed language with respect to its retirement of an entity's offset credits in its compliance accounts (triennial compliance) states that the oldest offset credits would be retired first and “offset credits retired in excess of the quantitative usage limit will not count toward the triennial compliance obligation”. This language means that CARB would permanently retire offsets from an entity's compliance account which exceed the 8 percent quantitative usage limit as all offsets in an entity's compliance account would be retired first. LADWP believes that this action is punitive, discourages the use of offsets for compliance, and unnecessarily increases the complexity of complying with the regulation. Entities placing offsets above their 8 percent limit into their compliance account to ensure compliance with the rule should not be penalized by losing those offsets. LADWP recommends that entities be able to use those offsets towards compliance in the next compliance period.

Under §95892(d)(5), electrical distribution utilities (EDUs) are prohibited from using the value of their allocated allowances to meet compliance obligations that do not benefit its retail ratepayers consistent with the goals of AB 32, including the use of such allowances for electricity sold into the CAISO markets. CARB proposes to surrender compliance instruments from entity compliance accounts in the following manner: offsets (oldest vintage first), allowances purchased from the Allowance Price Containment Reserve (Reserve), allowances (oldest vintage first), then true-up allowances. Although an EDU would be in compliance with §95892(d)(5) with respect to its procurement of allowances, this surrender proposal could have the unintended effect of appearing to conflict with §95856(h). In addition, covered entities such as EDUs would not have serial number information to decipher which allowances in their compliance accounts are allocated versus purchased for sales into the CAISO. Thus, EDUs' accounting of allowances may not match

CARB's. For example, a publicly-owned utility (POU) may have correctly estimated the number of purchased allowances (e.g. via regular auction) toward sales into the CAISO markets but have more administratively allocated allowances than needed to cover its native load in its compliance account. It appears that CARB's proposed surrender order would not necessarily reflect the POU's accounting of its purchased vs. allocated allowances as the administratively allocated allowances would be surrendered first. LADWP believes that EDUs should not be penalized if they have properly procured and accounted for their allowances but have differences with CARB's due to its proposed surrender order of allowances.

7. § 95913(f)(5) Sale of Allowances from the Reserve

CARB proposes to conduct a Reserve sale immediately preceding the compliance obligation instrument surrender of November 1, starting with the Reserve sale immediately preceding the compliance obligation instrument surrender deadline on November 1, 2015. CARB also added §95913(f)(1) to specify the source of allowances for the Reserve. That provision refers to §95870(f)(1) which does not exist. It appears that the correct cross reference should be §95870(j)(1).

LADWP supports CARB's proposal with respect to containing costs during temporary demand imbalances. Having more allowances available at the highest price tier of the Reserve will help in discouraging a market participant's willingness to pay more than that price for allowances. However, LADWP believes that this proposal is not sufficient to address Board Resolution 12-51 which is to ensure that allowances prices do not exceed the highest tier price of the Reserve while minimizing the impact of existing allowances and achieving the program's environmental objectives. LADWP recommends that CARB adopt the Joint Utilities Group's cost containment approach which is to implement a portfolio of measures consisting of:

- a) Measures which take effect now and gradually, over time, reduce the likelihood of prices rising above the Reserve in the future;
- b) Measures that, when triggered, would quickly alter compliance instrument demand/supply dynamics and constrain upward pressure on market prices for a period of time; and
- c) Measures that, when triggered, would keep allowance prices at the highest price tier of the Reserve regardless of current demand, while preserving the environmental integrity of the cap-and-trade program.

Please refer to the Joint Utilities proposed cost containment measures document that LADWP attached to its comment letter of July 9, 2013 for additional information.

8. § 95912 Auction Administration and Participant Application

CARB is proposing the following new provision (§ 95912(d)(5)):

An entity with any changes to the auction application information listed 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.

The regulation also states the following (§95912(e)(2):

An entity approved for auction participation must inform the Auction Administrator at least 30 days prior to an auction when reporting a change to the information disclosed, otherwise the entity may not participate in that auction.

These two provisions do not appear consistent with each other as §95912(d)(5) states that any changes in an entity's auction application will result in denial of the entity's ability to participate in the auction (whether the change in status is positive or negative) whereas §95912(e)(2) implies that CARB will make a decision whether to allow the entity to participate. In addition, 15 days after an auction, the entity will have already participated in the auction as far as submittal of bids and may not be able to predict if its auction application information will change. Therefore, LADWP requests CARB clarify §95912(d)(5) such that it is consistent with §95912(e)(2) and further define what constitutes a "change" in the status of an ongoing investigation.

9. Conclusion

LADWP appreciates this opportunity to comment and looks forward to working with CARB staff on these important issues. If you have any questions or require additional information, please contact me at (213) 367-0403 or Ms. Jodean Giese at (213) 367-0409.

Sincerely,



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Director of Environment and Efficiency

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