

June 17, 2013

**Comments of the Independent Energy Producers Association
Regarding
CARB's Workshop on Suppliers of Natural Gas Convened June 3, 2013.**

The Independent Energy Producers Association (IEP) appreciates the opportunity to comment on CARB's Workshop on Suppliers of Natural Gas, convened June 3, 2013. IEP represents over 26,000MW of installed generation serving California. While not directly impacted by the Cap and Trade ("C&T") rules and regulations affecting natural gas suppliers, electric generators are indirectly impacted, particularly those electric generators that rely on natural gas as their fuel. IEP's interest is to ensure that all sectors facing a compliance obligation under the cap and trade program are held to similar standards and levels of fairness, and that the regulations imposed on natural gas fuel suppliers are equitable and fair to downstream users such as electric generators.

Currently, beginning with the second compliance period of the C&T program (January 1, 2015), suppliers of natural gas will be "responsible for gas delivered to in-state end users other than covered entities."¹ Pursuant to the existing C&T regulation(s), natural gas suppliers do not receive free allowances once they become "covered entities." As a result, natural gas suppliers will be required to purchase their allowances in the market along with other covered entities.

The purpose of CARB's workshop on June 3, 2013 was to gain feedback from stakeholders on whether CARB should retain the current approach in the regulation (i.e. no free allocation to natural gas suppliers) or, alternatively, whether and how CARB should provide some free allocation of carbon allowances to suppliers of natural gas. IEP's comments address these issues below.

I. CARB's Treatment of Natural Gas Suppliers Under the C&T Program Should be Fair, Equitable, and Non-Discriminatory.

Whether CARB decides to provide some sort of free allocation to natural gas suppliers or, alternatively, retain the approach in the current regulation which calls for no allocation, CARB's allocation methodology must be consistent such that all natural gas suppliers are treated equally. While CARB identifies the Investor-Owned Utilities (i.e. Pacific Gas and Electric, San Diego Gas and Electric, and Southern California Gas Company) as the natural gas suppliers with the compliance obligation in most cases, the principle by which the CARB allocates allowances to the natural gas deliverers should provide fair and consistent treatment to all natural gas suppliers delivering to California end-use customers, including intrastate pipeline owners and publicly-owned gas utilities. This is a critical detail on which the utility proposal is unclear.

Treating one or a group of natural gas suppliers under different standards will tilt the competitive playing field among suppliers of natural gas, which would be inappropriate. In

¹ CARB Presentation on Suppliers of Natural Gas: Background and Options, slide 6.

addition, a secondary affect will be to tilt the competitive playing field among the end-users of natural gas, including obligated entities such as electric generators fueled by natural gas. For example, if free allowances are given to the IOUs, but not other natural gas suppliers, natural gas prices would reflect carbon costs for some customers and not others. This could negatively affect the electric sector to the extent that it creates an inequitable playing field for those receiving natural gas from IOUs vs. those receiving natural gas from other entities.

In order to ensure consistency in terms of how the natural gas suppliers are treated, as well as ensuring that other sectors are not harmed by the entrance of natural gas in 2015, IEP recommends that any allocation provided to natural gas suppliers be done in a fair, equitable, and non-discriminatory manner.

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

During the CARB workshop, the Investor Owned Utilities proposed full administrative allocation for the emissions associated with their natural gas supply. In addition, they indicated their preference for being able to use their allowances for direct compliance without having to go through the CPUC to determine how the allowances/allowance value should be distributed. The IOUs argue that this treatment is akin to how the Publicly Owned Utilities have been treated in the electric sector.

IEP does not support this proposal. While the IOUs are the natural gas suppliers in this context, they also own, operate, and develop electric generation assets in competition with independent power producers (IPPs). To the extent that any allowances are freely allocated to these utilities on behalf of their natural gas interest, these freely allocated allowances 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.

As a result, to the extent that the utilities are granted any allowances under this proposal, for either their electric operations or their gas operations, 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.

III. At the Election of a Generator Operating Under a Legacy Contract Without a Means for GHG Cost Recovery, CARB Could Shift the C&T Compliance Obligation Upstream for the Generators That Elect This Option.

Recently, in parallel to the workshop on the natural gas sector, CARB convened a similar process for addressing and hopefully resolving a number of issues directly related to the electric sector, including the treatment of so-called Legacy Contracts. While IEP has separately submitted comments on these electric sector issues, particularly Legacy Contracts, we see a nexus between the treatment of some of the electric issues and the treatment of the natural gas sector. Thus, while incorporating herein by reference our prior comments related to the electric sector, dated May 21, 2013, we make the following observations and suggestions.

As noted in its prior comments to CARB regarding Legacy Contracts, IEP believes the most efficient, fair and non-discriminatory solutions for Legacy Contract holders is to directly allocate for free 100% of their compliance obligation for the duration of their existing contract. For the reasons stated previously, this methodology should be applied to all Legacy Contracts without a reasonable means of cost recovery for carbon allowances, including CPUC jurisdictional contracts.

While preferring the approach of 100% free allocation for the duration of the existing contract, IEP does believe that the proposal discussed at the CARB Workshop on the Proposed Adjustments to the Treatment of Legacy Contracts (May 1, 2013) to shift the GHG compliance obligation from the electric generators to the natural gas suppliers, i.e. move the point of compliance “upstream” in the fuel supply, has merit for those Legacy Contract operations in which natural gas is their fuel. We note, however, that this may not solve for all Legacy Contracts, particularly any Legacy Contract operations for which natural gas is not the fuel. On the other hand, under the proposal, the GHG compliance obligation would fall on the natural gas supplier which presumably could be passed through to the customer(s) as a component of the generator’s fuel cost (e.g. in a tolling arrangement).

While this proposal may not solve for all Legacy Contract holders, for those legacy contracts where the fuel supply is natural gas and the generators are able to pass-on to their buyer their fuel costs, this seems like a reasonable option. However, because this option may not work for every legacy contract holder that remains, the decision to shift the compliance obligation upstream should be decided at the election of each individual Legacy Contract holder that wishes to employ this option.

IEP thanks the CARB for this opportunity to comment on the June 3, 2013 Workshop on Natural Gas Suppliers.

Respectfully Submitted,



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