



April 24, 2009

Ms. Jeannie Blakeslee
Ms. Edie Chang
Office of Climate Change
California Air Resources Board
1001 I Street
Sacramento, CA 95814

**Re: Comments of the Indicated Producers on CARB AB 32 Revised
Administrative Fee Draft Regulations**

Dear Ms. Blakeslee:

The Indicated Producers (IP)¹ is an *ad hoc* coalition representing the interests of in-state and other domestic natural gas producers, natural gas marketers, and large industrial end-users engaged in oil and gas production and refining. The proposed AB 32 administrative fee will impact IP members in their capacity as producers, marketers and end-users.

The revised regulations reflect significant improvements to mitigate potential for double regulation and to ease the administration of this fee. One change, however, will open the door to new problems. The revised AB 32 administrative fee regulations move the point of regulation for natural gas end users not receiving supplies delivered by a public utility to the interstate pipeline. In the original draft regulations, the point of regulation lay with the end user receiving supplies directly from an interstate pipeline. While this change may appear to promote administrative ease, it can:

- Result in differential impact on marketers depending on the customers they serve;
- Prevent the pass-through of costs to end-users, as CARB intended, under existing long-term contracts that cannot be modified to address the issue;
- Prevent pass-through of costs to end-users in future contracts, where the price index used does not typically reflect in-state costs; and
- Create jurisdictional problems because it seeks to assess a fee directly on a FERC jurisdictional entity.

¹ The Indicated Producers is an *ad hoc* coalition which includes, for the purposes of these comments, Aera Energy LLC, BP Energy Company, BP America Inc. (including Atlantic Richfield Company), ConocoPhillips Company, Chevron U.S.A. Inc., Midway Sunset Cogeneration Company (an affiliate of Aera Energy) and Occidental Energy Marketing Inc.

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As explained below, charging the fee directly to this group of end use customers is not as burdensome as CARB may suspect. Accordingly, moving the fee back to these select end use customers, as CARB contemplated in its initial draft regulations, is a simple way to avoid the problems identified above with minimal administrative burden.

In addition to this change, CARB should clarify that public utilities will be paying the administrative fee on behalf of the end use customers they serve. This would better reflect CARB's intent to have the sources of emissions bear the fee.

Imposing an Administrative Fee on End Use Customers Directly Receiving Gas from an Interstate Pipeline Will Not Significantly Increase Administrative Burden

There are only a select few end use customers that connect directly to an interstate pipeline. In fact, only 20-30 customers fall into this category. CARB could obtain a list of these customers from the interstate pipeline and receive monthly data on end-use volumes for billing purposes. All other end use customers receive gas through deliveries made on intrastate pipelines, where pass-through can be affected through in-state transportation surcharges.

While CARB may have changed the original regulation language to ease its administrative burden, as discussed below, there are material drawbacks to moving this point of regulation upstream. When these problems are balanced against the administrative burden of billing 20-30 end use customers directly, the balance weighs in favor of billing the end-use customers over the interstate pipeline.

Application of the Administrative Fee to Interstate Pipelines Can Result in Differential Impact on Marketers Depending on Customers Served

If CARB imposes the administrative fee on interstate pipelines, it can lead to a differential impact on marketers. Under the regulations, where a marketer of out-of-state gas sells gas to a utility or utility end-use customer, the utility would pay the fee and pass it through directly to its end-use customers in transportation fees. In contrast, if a marketer sells gas to an end use customer directly connected to an interstate pipeline (direct connect end use customer), the interstate pipeline would be responsible for the fee. The interstate pipeline would pass this cost through to the party transporting gas on its system. In most instances, the interstate pipeline would pass the cost through to the marketer who holds the transportation contract, *not* the end-use customer. If a marketer is then unable to pass through the incremental costs associated with the administrative fee, it would be differentially impacted when compared with marketers delivering to utility customers.

Pass-through of the administrative fee by a marketer under these circumstances is complicated and not assured. First, the marketer could be in an existing long-term contract that does not reflect these new costs. Typically these contracts are based solely on a market index price that does not include in-state charges. If the market index price does not reflect the full value of the administrative fee borne by the marketer, the marketer will not be able to pass the full cost through to the end user. Second, it is not clear that future contracts can be structured in a manner that provides full recovery of these costs. In short, pass-through would not be assured and would require an undue disruption in contracts between marketers and their customers.

Application of the Fee on Direct Connect End Use Customers Will Avoid Jurisdictional Legal Issues

It is unclear whether imposition of the administrative fee on interstate pipelines is within CARB's jurisdiction given that interstate pipelines fall within FERC jurisdiction. Not only would CARB first have to establish its own ability to assess the fee on the interstate pipeline, it would also have to ensure that the assertion of this authority does not detract from FERC jurisdiction. It is possible that these legal hurdles can be overcome, but the problem could be completely avoided if CARB reverts to imposing the administrative fee directly on those direct connect end use customers.

Draft Regulations Should Clarify that Public Utilities Will Pay the Administrative Fee On Behalf of End Use Customers

Consistent with California Health & Safety Code § 38597, CARB has repeatedly noted its interest in having the sources of greenhouse gas bear the administrative fee.² To reflect this directive, the regulations should clarify that public utility gas corporations operating in California will pay the administrative fee on behalf of end use customers. In the draft regulations, it is not evident that the end use customers, served by the public utility gas corporations, are the actual sources of emissions.

Recommendations

While CARB has made some changes to the administrative fee regulations in the hopes of lessening the administrative burden, the imposition of the administrative

² California Health & Safety Code § 38597 states that “ *The state board may adopt by regulation, after a public workshop, a schedule of fees to be paid by the sources of greenhouse gas emissions regulated pursuant to this division, consistent with Section 57001. The revenues collected pursuant to this section, shall be deposited into the Air Pollution Control Fund and are available upon appropriation, by the Legislature, for purposes of carrying out this division.*”

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fee directly on interstate pipelines will create new problems that must be avoided. As noted above, there are only 20-30 end use customers that directly connect to an interstate pipeline. Rather than open the door to the problems identified above, CARB should impose the fee directly on these customers. The interstate pipelines can continue to play a role in this process by identifying these customers and then providing data on gas deliveries to these customers. Accordingly, IP recommends that the following change be made to the revised regulations:

95201. Applicability

(a) This article applies to the following entities. The terms used below are defined in Section 95202.

(1) Natural Gas Utilities, Users, and Pipeline Owners and Operators.

(A) All public utility gas corporations ...

(B) ~~Any~~ ~~owners or operators of interstate and intrastate pipelines~~ owner/operator or entity purchasing or consuming natural gas in California that has been transported directly by any interstate pipeline, and not otherwise included in subpart (A), ~~that distribute natural gas directly to end users~~. Fees shall be paid for each therm of natural gas directly distributed to end users by interstate or intrastate pipelines.

To clarify that public utility gas corporations will be obligated to pay the administrative fee on behalf of end use customers, IP recommends the following change:

95201. Applicability

(b) This article applies to the following entities. The terms used below are defined in Section 95202.

(2) Natural Gas Utilities, Users, and Pipeline Owners and Operators.

(C) All public utility gas corporations operating in California. Fees shall be paid on behalf of end use customers for each therm of natural gas delivered to any end user.

IP looks forward to discussing these issues further.

Very truly yours,



Evelyn Kahl