Comments of the Western Power Trading Forum

To the California Air Resources Board

On Electricity Issues under the Cap and Trade Program

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Clare Breidenich

WPTF GHG Committee Director

Email: cbreidenich@aciem.us

The Western Power Trading Forum[1] (WPTF) appreciates the opportunity to provide comments to the California Air Resources Board (CARB) on issues related to the treatment of electricity under the cap and trade program. These comments address the following issues raised at the May 4th workshop:

- Electricity imports to the California Independent System Operator (CAISO) at interties outside the state
- Prohibition on Publicly-owned utilities' use of allowances for power sold into the CAISO markets
- Resource-shuffling
- Reporting of the appropriate emission rate to avoid resource-shuffling
- Qualified Export Provisions
- Renewable Portfolio Standard (RPS) Adjustment Provisions

Imports to CAISO at external interties

WPTF anticipates that as of January 1, 2013 that power prices in the CAISO markets will normally include a carbon premium due to the new costs imposed on in-state generation as a result of the cap and trade programs. Any entities that sell power into these markets will receive a higher price for their power relative to what they would have receive prior to cap and trade implementation, while entities that purchase power from these markets will pay a higher price. In order to ensure equivalent treatment of all electricity deliverers (in-state and out-of state), WPTF believes that all entities that bid and schedule power into the CAISO should be held responsible for the carbon associated with these imports. This approach will ensure that the entity that receives payment for power delivery into California – and the carbon premium imbedded in the power price – will also have the carbon obligation for the associated emissions. It also aligns the carbon obligation with the entity best able to control imported emissions and ensures equal treatment of all importers.

An alternative approach whereby the CAISO would be required to determine the emissions associated with electricity delivered to external interties, acquire and retire allowances to cover these emissions, and to somehow pass these costs to load would be substantially more complicated to implement, may result in load paying for carbon twice, and could create a loophole where imports to California via CAISO external interties would receive a premium for carbon, but no associated carbon obligation. This would be unfair to end use customers and other importers, and create an incentive for imports through those points. For these reasons, WPTF opposes an outcome that would require the CAISO being held responsible for carbon for imports at external ties.

None-the-less, WPTF recognizes that other stakeholders have raised valid concerns regarding CARB's legal authority to hold entities responsible for carbon emissions associated with deliveries to the CAISO at

[1] WPTF is a diverse organization comprising power marketers, generators, investment banks, public utilities and energy service providers, whose common interest is the development of competitive electricity markets in the West. WPTF has over 60 members participating in power markets within California, western states, as well as other markets across the United States.

interties outside the state boundary and the legitimacy of an approach that assigns carbon obligation based on scheduling (i.e. NERC tags) rather than title transfer. The fact that these concerns appear to be legitimate creates uncertainty for all market participants about potential legal challenges to the program and resultant changes to the regulation after implementation has started.

For theses reason, WPTF strongly urges CARB to continue to work with the CAISO and the California Department of Justice and the Federal Energy Regulatory Commission to develop the most legally sound approach, consistent with the CAISO tariff, to ensure that the assignment of the carbon obligation on imports is appropriately designed for power delivered into the CAISO markets.

Prohibition on Publicly-owned utilities' use of allowances for power sold into the CAISO markets

The cap and trade regulation appropriately requires that investor-owned utilities consign their directly allocated allowances to auction and prohibits the use of directly allocated allowances to cover their own GHG compliance obligation. Publicly Owned Utilities, however, may use allocated allowances to cover their own emission obligations with the exception of emissions associated with power that is sold into the CAISO markets.

WPTF strongly supports retention of the prohibition on the POU use of directly allocated allowances to cover emissions of power sold into the CAISO. Elimination of this prohibition would give POUs a competitive advantage over other suppliers in the CAISO markets because the POU would incur no carbon cost for their power sales, while other entities would.

Resource-shuffling

The current definition of 'resource-shuffling' in the cap and trade regulation is so broad that it provides no clarity or regulatory certainty to electricity entities regarding which transactions would be considered legitimate specified or non-specified imports and which would be considered resource-shuffling. The resultant lack of clarity could cause two entities acting rationally to interpret resource shuffling in vastly different ways, and will increase the risks associated with what would other be efficient and cost-effective wholesale electricity market transactions, raising compliance costs.

It is clear from discussions at the May 4 workshop, that electricity market participants need more clarity on what constitutes resource shuffling and how it will be identified. WPTF recommends that CARB provide this clarity by 1) modifying the definition of resource shuffling in the regulation, 2) developing guidance documentation for use by electric entities and verifiers around 'bright-line' scenarios that clearly would or would not be considered resource-shuffling and 3) establish a formal process by which an individual entity can get an upfront determination by CARB of the appropriate emission factor to be used for specific import situations. We elaborate each of these elements below.

In the July 15, 2011 proposed 15-day modifications, CARB included a more detailed definition of resource shuffling. This definition, while imperfect, was clearer in that it focused on the specific scenarios that are of most concern to CARB. WPTF therefore proposes the following definition of resource-shuffling, which is based on but modifies the July version:

"*Resource Shuffling" means any plan, scheme, or artifice to lower an entity's compliance obligation for the delivery of electricity to the California grid, for which:*

> *(A) An emission factor below the default emission factor is reported pursuant to the MRR for electricity, excluding surplus, that that has been historically owned by or committed under a contract of five years or longer to a load-serving entity outside of California; or*
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> *(B) The default emission factor or a lower emissions factor is reported pursuant to MRR, for electricity that replaces electricity from a generation source with an emissions factor higher than the default emission factor that was previously owned by or under contract of five years or longer, to a California load-serving entity; except when the replaced electricity no longer serves California load as a result of actions taken to comply with the Emission Performance Standards adopted by the California Energy Commission and the California Public Utilities Commission pursuant to Senate Bill 1368 (Perata, Chapter 598, Statutes of 2006), or equivalent legislation within another jurisdiction within the WECC.*

At the March 4th workshop, staff outlined several scenarios, such as 'cherry-picking' and 'facility-swapping' that, in their view, would clearly be considered resource-shuffling. WPTF believes that our proposed definition would cover these scenarios, but that further guidance is necessary to enable electricity deliverers and verifiers indentify them . WPTF therefore recommends that CARB staff develop guidance documentation around these, and any other clear-cut scenarios that may be identified. Guidance documentation should, to the extent possible, address cases that would clearly be considered resource-shuffling and cases that would not. CARB could expand upon and elaborate the guidance documentation over time as staff entities become more experienced with electricity import scenarios.

CARB has indicated a concern that the development of guidance documentation could lead entities to erroneously believe that similar, but not identical, situations fall under one of the bright-line scenarios. While we recognize this concern, we see it as a drafting challenge rather than an insurmountable problem, and that the benefits of providing this sort of guidance to market participants outweighs those risks. CARB should be able to make it clear in the guidance documentation that determinations of resource-shuffling are dependent on specific situations and that variations in individual circumstance may alter a determination. CARB should elaborate the other factors that would need to be taken into consideration in the guidance documentation.

WPTF anticipates that even with a better definition of resource shuffling and the availability of guidance documentation on bright-line scenarios, there will be electric power entities with unusual or unforeseen situations that are not clearly addressed. In this event, it would be extremely useful for CARB to provide a mechanism by which an entity can get a formal, up-front determination on its particular situation and proposed approach to reporting under the MRR. This up-front determination process should result in a formal record for the entity concerned, but need not be subject to public disclosure.

Finally, WPTF encourages CARB to provide greater transparency on how emission factors for resources that have not previously been specified will be calculated. While the MRR provides general information on how CARB will calculate emission factors, for many generation types (e.g. cogeneration, biomass) the data sources to be used (i.e. U.S. Environmental Protection Agency versus Energy Information Agency) and emissions included in the calculation are not clear. CARB should therefore develop and publish examples, using existing specified resources, of how emission factors are calculated.

Reporting of the appropriate emission rate to avoid resource-shuffling

At the workshop on May 4th, CARB staff indicated that that an entity should use a higher emission rate (i.e. default) for specified electricity imports in order to avoid resource-shuffling. Similar statements are made in the Final Statement of Reasons for both the cap and trade regulation and the reporting regulation.

WPTF has read both regulations closely and cannot find any provision in either regulation that requires this. Rather, the Mandatory Reporting Rule clearly states in section 95111 (4) that "The electric power entity **must report all direct delivery of electricity as from a specified source** for facilities or units in which they are a generation providing entity (GPE) or have a written power contract to procure electricity."

Use of an emission rate other than the specified emission rate in these cases would appear to be a direct violation of the mandatory reporting regulation. If CARB intends that an entity use a different emission rate than the specified rate for specified imports in particular circumstances, then it is incumbent upon CARB to explicitly provide for this in regulation.

Qualified Exports

At the May 4th workshop, CARB identified several possible modifications to the provisions related to Qualified Exports (QE), including the elimination of these provisions. WPTF strongly supports retention of the QE provisions, along with modifications of the rules for calculating the QE adjustment.

As WPTF has explained previously, the CAISO uses two different types of schedules for handling wheeling of power through California. The first, called a wheel-through results in a single NERC tag, while the second, a simultaneous import/export, results in two separate NERC e-tags. The only difference between the two-types of schedules is simply that in a wheel-through, the participant has required a concurrent dispatch of its import and export bids, whereas in the simultaneous import/export, the participant will accept either the import or the export or both.

Both types of wheel-through schedules have an identical impact on the electrical flows and generation dispatch both within and outside of the CAISO grid. The CAISO does not actually allocate physical or contractual transmission inside the CAISO between the two points. Rather, the CAISO effectively treats the import side and the export side of the wheel-through as if they are distinct physical deliveries into and out of the state respectively. The CAISO adds the concurrent imports/exports of a wheel-through schedule type to its own internal generation resource bids, load demand bids and other import/export and wheel-through bids to derive a least cost overall portfolio solution for the CAISO.

If CARB were to eliminate the QE provisions, then power that is wheeled-through the state on a single NERC tag would be exempt from the regulation, whereas power that is wheeled through on two separate tags would not, despite the fact that both types of schedules have an identical impact on the electricity grid and are treated identically by the CAISO. This inconsistent treatment would create an economic incentive for increasing use of wheel-through schedule types in the CAISO, instead of the more flexible simultaneous import/export schedules, which will lead to economic inefficiencies in the CAISO without reducing GHG emissions. For this reason, WPTF support retention of the QE adjustment provisions.

The current QE adjustment provisions require that the emission rate assigned to QE be equal to the emission rate of the cleanest import or export in that hour. WPTF considers that this requirement is unnecessary, overly restrictive and would similarly create an economic incentive to increase the use of wheel-throughs in the CAISO. We support modifying the regulation to assign emission rates to qualified exports in ascending order from the lowest, non-zero emission rate of imports in that hour.

RPS Adjustment Provisions

WPTF has previously raised the concern that the rules for the RPS adjustment require that the Renewable Energy Credits (RECs) associated with the renewable energy generation be retired for compliance with the RPS within the same calendar year. This requirement is inconsistent with the RPS rules that allow RECs to have a "shelf life" of 36 months, and be used in a different RPS compliance period then the one in which they were generated. Section §95852(b)(3)(D) of the cap and trade regulation would effectively prevent an entity from using the RPS adjustment if the associated RECs are held for RPS compliance in a later year. The mismatch between the cap and trade requirements and RPS multi-year compliance requirements must be addressed.

WPTF supports CARB's objective of ensuring that the RPS adjustment is applied for electricity imported and used pursuant to the California RPS, in particular the so-called 'category 2' transactions. However, we believe that CARB's concern about the possibility of a category 2 REC being resold as a category 3 (i.e. unbundled REC) are not valid. The different RPS requirements for category 2 and category 3 RECs provide a strong financial deterrent for resale of category 2 RECs as category 3. First, the RPS requires that that category 2 RECs be sold to a California LSE prior to generation. Because category 2 also requires energy delivery, category 2 procurement will include congestion costs. Further, because of the lower limits of category 3 RECs, category 2 RECs will be of higher value to California LSEs. Thus, it is highly unlikely that an LSE would resell a REC procured as category 2 as category 3.

WPTF also considers that CARB's objective of ensuring that the RPS adjustment is applied only in the case of electricity imported and used for RPS category 2 procurement can be achieved by means other than mandatory REC retirement within the calendar year. Rather than require that the associated RECs have been retired, CARB should instead require that these RECs be generated in the same year for which the RPS adjustment is applied and be held in the WREGIS account of the California LSE that purchased them. This could be easily verified through WREGIS and, if necessary, through the LSE's RPS compliance filings to the CPUC and CEC.