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By Electronic Submission

(http://www.arb.ca.gov/lispub/comm2/bcsubform.php?listname=5-4-electricity-ws&comm_period=1)

Hon. Mary D. Nichols, Chairman
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Re: Comments on Public Meeting to Discuss Compliance Requirements for First Deliverers of Electricity in the Cap-and-Trade Program (May 4, 2012)

Dear Madame Chairman:

Calpine Corporation ("Calpine") appreciates the opportunity to provide these written comments on the California Air Resources Board ("CARB" or the "Board") Public Meeting to Discuss Compliance Requirements for First Deliverers of Electricity in the Cap-and-Trade Program, which was held on May 4, 2012 (hereinafter, "Electricity Workshop")¹.

As the largest independent power producer both in California and the United States, Calpine is a long-time supporter of Cap-and-Trade and looks forward to working with CARB Staff to assure a successful launch of CARB's Cap-and-Trade Program Regulation (Cal. Code Reg., tit. 17, §§ 95800 *et seq.*) ("Regulation").

I. Summary

Calpine is concerned that CARB's proposal to maintain the existing definition of, and prohibition on, "resource shuffling" will pose significant restraints on transactions involving imported power. It is by no means clear what constitutes "resource shuffling". As a consequence, wholesale power transactions involving no intent to defraud CARB could be severely hampered, if not altogether impeded, due to the vague and undefined nature of this concept. Moreover, the chilling effect this could have on traders' willingness to even enter into such transactions could raise serious concerns regarding the program's legality. For this reason, it is critical that CARB continue to work with stakeholders to provide additional clarity on the contours of proscribed resource shuffling prior to the commencement of the first compliance period.

¹ Presentation, "Cap-and-Trade Program Electricity Workshop", CARB, May 4, 2012 (hereinafter, "Presentation"), available at: http://www.arb.ca.gov/lispub/comm2/bcsubform.php?listname=5-4-electricity-ws&comm_period=1.

II. CARB Should Continue To Work With Affected Stakeholders To Remove The Restraints That The Existing Definition Of Resource Shuffling May Impose On Sales Of Imported Power

A. Background on Resource Shuffling. Resource shuffling is defined as “any plan, scheme, or artifice to achieve credit based on emissions reductions that have not occurred, involving delivery of electricity to the California grid.” Cal. Code Reg. tit. 17 § 95802(a)(251). Resource shuffling is prohibited and a violation of the Regulation. *Id.*, § 95852(b)(2). The Regulation requires all first deliverers of electricity to submit annual attestations, wherein an individual represents, under penalty of perjury, that the company for which he or she is acting as agent, “has not engaged in the activity of resource shuffling to reduce compliance obligation for emissions, based on emission reductions that have not occurred as reported under [the Mandatory Reporting Rule (“MRR”).]” *Id.*, § 95852(b)(2)(A).

CARB initially proposed a more specific definition of “resource shuffling”, when it first introduced the concept in the July 25, 2011 15-day modifications. *See* proposed Cal. Code Reg. tit. 17 § 95802(a)(245) (July 2011), at A-40.² This definition would have identified two specific types of activity as “resource shuffling”:

- (1) Deliveries from a source that has not historically served California load for which an emission factor lower than the default emission factor was reported pursuant to the MRR (*i.e.*, as a specified source), while, “during the same interval(s), electricity with higher emissions was delivered to serve load located outside California and in a jurisdiction that is not linked with California’s Cap-and-Trade Program”; or
- (2) Deliveries for which the default emission factor or a lower factor was reported “for electricity that replaces electricity with an emissions factor higher than the default emission factor that previously served load in California”, except in the case of electricity that no longer services California due to the Emission Performance Standards adopted pursuant to Senate Bill 1368 (Perata, Chapter 598, Statutes of 2006) (“SB 1368”). *Id.*

Only if a delivery of imported power fell within one of these two criteria would it constitute “resource shuffling”.

Both of these criteria would have been unworkable in application. In the former case, it would have simply been impossible for a first deliverer of low-emitting power from a specified source to know whether higher-emitting power was being delivered outside of California at the same time as it delivered power that had not previously served California load. In the latter case, it would have likewise been impossible for a first deliverer to know whether power purchased and then sold from the wholesale pool was replacing power that no longer served California load or, if it did, whether that was somehow attributable to the impacts of SB 1368. In either case,

² Available at: <http://www.arb.ca.gov/regact/2010/capandtrade10/candtmmodreg.pdf>.

whether a specific delivery fell within the definition of resource shuffling would have depended on the actions of unrelated third-parties, over which the first deliverer had no control and of which it likely would have no knowledge.

CARB responded by eliminating these specific criteria, saying it was also deleting references in the definition to the term “fraud”, “as well as other language that could impede typical electricity market activity, which was not staff’s intent.” Final Statement of Reasons, 57; *see id.*, 1493 (reporting that CARB deleted the two criteria above from the definition, in response to commenters’ concerns). CARB emphasized in its responses to comments that the definition’s focus on “any plan, scheme or artifice” was designed to assure that unintentional conduct was not the focus of the prohibition. *Id.*, 1494-95. Thus, according to CARB, a first deliverer need not worry about “the unknown and essentially unknowable” emissions consequences of certain power market transactions. *Id.*, 1494.

Affected stakeholders, such as Calpine, had hoped that CARB would replace the hastily thought out criteria that were first proposed with the definition of resource shuffling with more specific and detailed guidance on what constituted permissible, as opposed to unlawful, market behavior.

B. CARB’s Proposal to Make No Changes. At the Electricity Workshop, CARB announced that, although it had taken the Board’s instructions into consideration,³ it was recommending no changes to the definition of resource shuffling. Presentation, 23. Rather, CARB staff “will provide *limited* guidance regarding what is not resource shuffling” and “will work with stakeholders to help inform stakeholders whether specific actions constitute resource shuffling”. *Id.* (emphasis added). CARB also provided examples that, in CARB’s view, clearly constitute “resource shuffling”, including “Cherry Picking”, “Facility Swapping” and “Laundering”. *Id.*, 24. It also provided examples that do not constitute resource shuffling, including “[c]hanges in delivery of electricity pursuant to state or federal laws and regulations” and “[d]eliveries of emergency power”. *Id.* Both of these concepts are abundantly unclear.⁴

C. Problems with CARB’s “We’ll Know It When We See It” Approach. CARB previously responded to our concerns regarding the definition of “resource shuffling” by expressing its hope that, “with additional discussion and consideration of these provisions, commenters will gain a better understanding.” Final Statement of Reasons, 1497. However, the great deal of discomfort expressed by stakeholders during the Electricity Workshop last Friday indicates that, to-date, no

³ In Resolution 11-32, the Board directed CARB to consider amendments to the “[d]efinition of Resource Shuffling to: (a) provide appropriate incentives for accelerated divestiture of high-emitting resources by recognizing that these divestitures can further the goals of AB 32; and (b) ensure changes in reported emissions from imported electricity that serves California do not result merely in a shift of emissions within the Western Electricity Coordinating Council region, but reduces overall emissions”. Resolution 11-32, 11.

⁴ Indeed, would an import from a gas-fired peaking unit out-of-state due to peak demand that might possibly have been satisfied previously by baseload power generated from coal assets in-state or elsewhere constitute “emergency power”?

greater understanding has been gained. Rather, all that is clear is that CARB continues to take a "we'll know it when we see it" approach to resource shuffling (*see id.*, expressing CARB's view that it may be difficult to identify resource shuffling until it is actually observed in practice). As a consequence, significant questions remain among affected stakeholders about what will constitute legitimate vs. prohibited activity. This risks great uncertainty and raises serious concerns as a matter of public policy.

Calpine believes the discussion at the Electricity Workshop was both productive and overdue. To assure a smooth launch of the Cap-and-Trade Program, it is critical that CARB continue to engage with stakeholders to provide greater clarity regarding the contours of resource shuffling, prior to the beginning of the first compliance period. We are concerned that, without such clarity, the resource shuffling prohibition could dissuade legitimate market behavior driven in part by the price signals CARB intends to send through implementation of the Cap-and-Trade Program.

Further, because the resource shuffling prohibition only affects imported power, we are concerned that the burdens it imposes on sales of power generated outside California would not be found to constitute the least discriminatory alternative to prevent leakage and could be deemed excessive in light of the putative benefits to California.

For these reasons, we strongly encourage CARB to continue working with stakeholders in a series of meetings similar to the Electricity Workshop to discuss what constitutes "resource shuffling" and how parties might obtain comfort prior to the start of the first compliance period to engage in legitimate market activity that might otherwise be deterred due to the vagueness of the current definition. We agree with the comments of the Western Power Trading Forum with respect to guidance CARB might provide to reduce the restraints imposed on legitimate market activity by the definition of "resource shuffling" and look forward to participating in any future discussions of this topic.

Please feel free to contact me with any questions or concerns regarding these comments. Thank you for the opportunity to submit these comments.

Sincerely,



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Director, Government and Legislative Affairs

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