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April 13, 2012

Steven Cliff, Chief
Rajinder Sahota, Manager
Ray Olsson, Lead Staff
California Air Resources Board
1001 I Street
Sacramento, California 95814

Subject: Comments of Wellhead on the March 30, 2012 Discussion Draft for Regulatory Text Changes to Accommodate Linkage with Quebec

Dear Mr. Cliff, Ms. Sahota, and Mr. Olsson:

Wellhead submits these comments to the California Air Resources Board (“CARB”) staff in response to the March 30, 2012 *Discussion Draft for Regulatory Text Changes to Accommodate Linkage with Quebec* (“Discussion Draft”). Wellhead’s comments address the deletion of the Beneficial Holding Relationship provision (Section 95834) and the need for CARB to continue to evaluate and prepare for resolution of the issues faced by a very limited class of generators with pre-AB 32 contracts that have no available mechanism for recovery of AB 32 compliance costs (“Pre-AB 32 Contract Issue”).

The Pre-AB 32 Contract Issue remains an important concern that has not yet been resolved. When Wellhead reviewed the changes to Section 95834 in the Discussion Draft, Wellhead was initially concerned that Staff proposed to remove a potential avenue for addressing the Pre-AB 32 Contract Issue. However, Wellhead appreciates staff’s clarification during the April 9th workshop that staff’s intent was to achieve administrative simplicity by removing an unnecessary requirement to have an allowance transfer relationship approved by CARB. Wellhead appreciates CARB’s statements that transfers of allowances between a load serving entity (“LSE”) and a generator for output and GHG emissions attributable to the generator could still take place in the context of the existing allowance transfer rules.

It is also important to note that the beneficial holding relationship would have exempted allowances purchased pursuant to a beneficial holding relationship from the LSE’s holding limits. Now, it is our understanding that LSEs and other entities purchasing allowances on another regulated entity’s behalf must comply with the holding limit requirements in Section 95914. With the added administrative simplicity intended by the new structure, this is a good outcome provided, as it appears, that an LSE has the flexibility to purchase allowances on behalf of a contract supplier without violating the holdings limits.

Of greatest importance, though, is that the Discussion Draft version of the cap-and-trade regulation would provide an avenue for utilities to address the Pre-AB 32 Contract Issue only *if they adjust and amend the contract*. However, as noted in Wellhead’s previous comments, the utilities currently have no incentive to renegotiate this very limited class of Pre-AB 32 contracts. A generator with a Pre-AB 32 Contract will bear the costs of the cap-and-trade program, and will

be the only generation in the utility's portfolio with carbon costs that the utility and its customers do not see. That condition is clearly contrary to the Statement of Reasons.¹ In the case of tolling arrangements where the utility controls dispatch, the utility will have an incentive to run this limited group of generators more often than would be appropriate with proper consideration of GHG costs, which is also contrary to the intent of the cap-and-trade program. While CARB and the California Public Utilities Commission ("CPUC") have encouraged a negotiated solution, so far, PG&E in filings at the CPUC has dismissed the need to address the issue. Hence, a timely negotiated solution to the Pre-AB 32 Contract Issue will be enormously challenging at this juncture.

While Wellhead still hopes that there will be a negotiated solution, and will continue to engage PG&E towards that end, there is an unmistakable and significant probability that negotiations will not be successful prior to the initial allowance auctions later this year², and in that case, CARB should be prepared to act expeditiously.

Wellhead therefore proposes that CARB include additional amendments to the cap-and-trade regulation to provide the Executive Director with the flexibility to address this issue through administrative adjustments to allowance allocations if the Pre-AB 32 Contract Issue is not resolved prior to the initial allowance auction or free allowance allocation. In summary, Wellhead's proposed revisions would position the Executive Director to adjust a utility's allowance allocation if it determines that a generator with a Pre-AB 32 Contract is bearing costs for which the utility would otherwise receive free allowances attributable to that generation. Wellhead's revisions below are noted in underline:

Section 95892 Allocation to Electrical Distribution Utilities for Protection of Electricity Ratepayers.

- (f) In the event that the Executive Director determines that an electrical distribution utility receives allowances attributable to a long-term contract for the sale of electricity at wholesale, which:
- i. does not provide or refer to GHG costs, for energy dispatched and purchased by the electrical distribution utility, either directly in the long-term contractor through a CPUC authorized pricing basis that includes GHG costs;
 - ii. was full executed before the final approval of AB 32 (September 27, 2006); and
 - iii. has not been amended to address GHG costs with such changes approved by the appropriate regulatory authority on or before September 1, 2012,

then the Executive Director will adjust the allocation of free allowances to that electrical distribution utility to reflect the GHG emissions associated with the utility's purchases under the long-term contract. The Executive Director shall have discretion to freely allocate allowances to the generator for the limited purpose of addressing the generator's

¹CARB was clear in the October 2011 Final Statement of Reasons that the regulations are not intended to confer free allowances when no associated GHG costs are incurred. CARB states that: "... it is not our intent to provide allowances to entities for carbon costs that they do not, in some manner, incur."

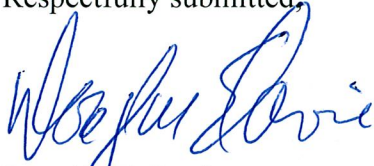
<http://www.arb.ca.gov/regact/2010/capandtrade10/fsor.pdf>

²This is in part because regulatory approval of the changes can take three to six months.

costs of cap-and-trade compliance; provided, that such allowances may not be sold or traded, they may only be used for compliance with these regulations by the recipient. The Executive Director shall have the discretion to adjust future allocations under this provision based on the generator's actual verified emissions for a particular compliance period.

Wellhead appreciates the opportunity to provide these comments and would be pleased to answer any questions you have.

Respectfully submitted,

A handwritten signature in blue ink, appearing to read "Douglas E. Davie".

Douglas E. Davie
Vice President

cc: Douglas K. Kerner