

January 11, 2016

VIA WEBSITE ([COMMENT SUBMITTAL](#))

California Air Resources Board Staff
California Air Resources Board
1001 "I" Street
Sacramento, CA 95814

Re: Comments of Day Carter Murphy LLP Re: Public Workshop on California Plan for Compliance with the Clean Power Plan and Potential 2016 Amendments to the Cap-and-Trade Program

Dear ARB Staff:

We applaud California Air Resources Board Staff's ("ARB Staff") efforts to create a compliance program that works for California and the electric generating units (EGUs) subject to the Environmental Protection Agency's (EPA) Clean Power Plan (CPP). In furtherance of creating a workable CPP program, Day Carter Murphy LLP with contributions from Andre Templeman of Alpha Inception provide the following comments on how best to create this program. Since the electric grid is interconnected throughout the west and electrons do not observe state boundaries, ARB's program should focus on creating a trade ready program that can link with other states or programs like the Regional Greenhouse Gas Initiative (RGGI), while still adhering to SB-1018 by requiring programs that link to have a bilateral agreement in place with California. In addition, this program must maintain California's environmental goals and should retain to the maximum extent feasible state level flexibility to modify the existing cap-and-trade program. We believe the CPP program should include all of the following parts:

- Be trade ready (this may require setting up an EGU only cap-and-trade market),
- Include 111(d) covered EGUs and new EGUs (to maintain consistent treatment across the EGU sector),
- Remove the need to obtain allowances for imported energy produced in linked states (these EGUs will be required to obtain allowances under the CPP linked program), and
- Minimize federal enforceability and its resultant lengthy approval process of modifications to California's cap-and-trade program to allow program flexibility at the state level.

Be Trade Ready

First, California should use a mass based program to be consistent with the Scoping Plan and the existing cap-and-trade program. Next, ARB should consider creating an EGU only allowance designation or market to be able to link to other EGU only markets and states while ring fencing the remainder of California's economy wide greenhouse gas reduction programs from any possible Federal oversight. In order to maintain flexibility and jurisdiction ARB should set the EGU allowance limits at a level to meet the CPP requirements and could still maintain the option of setting lower caps for the sector under the EGU Cap and Trade carve out, but would do so not as part of CPP compliance to avoid any additional jurisdictional oversight by the EPA. Setting EGU sector specific limits would also avoid exposing the broader cap-and-trade market to EPA backstop measures, oversight or required approval for programmatic changes, all of which can take many years in some cases.

The transition to designated electric allowances for the EGU sector ("E Allowances") should occur over time potentially including the first 111(d) compliance period of 2022 through 2024. During the transition period EGUs could use allowances of all types that they may have already purchased or banked. After the transition period EGUs would only be able to use E Allowances, but the broader market could use regular allowances or E Allowances. The purchase and use of E Allowances by a manufacturing facility would not inhibit the EGU program from meeting CPP requirements as it would reduce the number of allowances available for the EGU sector to emit and the EGU sector would still remain under the EGU E Allowance cap set by ARB. If California had a large hydroelectric generation year and a cool summer, the EGU's could have extra E Allowances that would not be needed. The EGUs could sell those E Allowances into the broader cap-and-trade market to another part of the economy that needed the allowances helping mitigate prices for the market in general.

Adding the requirement to EGU Title V permits would be similarly straight forward. As their five year renewals come up, the air districts could add a provision to the Title V permits requiring EGUs to obtain E Allowances equivalent to their emissions for each multiyear compliance period. The provision would make compliance with the CPP program federally enforceable. ARB would be able to verify compliance through the reporting and verification programs. And, ARBs reporting and verification programs would allow both ARB and the EGU to demonstrate compliance to EPA should EPA conduct a Clean Air Act Section 114 Request for Information.

Since EPA's program only applies in the United States, out of country allowances could not be labeled "E". Thus, ARB would need to modify its agreements with out of country liked partners so that allowances from their markets could only be used by the broader market and not by the EGU sector.

Setting up EGU only allowances would also allow ARB to link the EGU market with EGU mass based systems and markets in other states and other markets such as RGGI. ARB would still be required to comply with the requirements of SB 1018 and most likely enter into an agreement

with linked jurisdictions to achieve the enforcement requirements of SB 1018 (Cal. Gov. Code §12894[f]). Nonetheless, reaching agreement should be simpler because it could focus only on the EGU sector and should not require an economy wide greenhouse gas reduction program to link with the EGU only E Allowance market.

Include 111(d) Covered EGUs and New EGUs

One of the hallmarks of California's existing cap-and-trade program is that all sources regardless of existing or new are included in the program. Thus, the concerns about shifting emissions from older facilities to newer facilities are addressed with the statewide cap. This same construct should apply to the EGU sector for compliance with the Clean Power Plan. All facilities regardless of when they are built should all be treated the same way. Equal treatment makes for a level playing field for EGUs and simplifies the overall program. Thus, ARB's CPP program should include both CPP regulated EGUs and new EGUs.

Remove Allowance Requirement for Imports from Linked States

AB 32 requires accounting and emission reductions from all electricity used in California, whether from generation sources within California or from those located out of state. This construct is used to avoid leakage of emissions from in-state generation facilities to out of state generation facilities that are not subject to emission reduction requirements. Under the CPP EGUs in almost all states are regulated by EPA and being asked to reduce carbon emissions. If California can link to another mass based state including making the findings required under SB 1018, the emissions from EGUs in the linked state would be required to obtain E Allowances or equivalent credits for each compliance period just like California EGUs. Those linked state's credits would be acceptable to California based upon the linking decision. Thus, no generation from EGUs located in linked states would need additional "California" allowances when they export power into California.

This change to accept linked state EGU energy without allowances when the energy sinks in California would require ARB to reduce the number of E Allowances available for sale in California. The reduction in the number of E Allowances would need to reflect that those allowances would now be issued or accounted for by the linked state.

Minimize Federal Enforceability

As ARB well knows changing a program approved by EPA takes years to accomplish. A rough estimate is five years to make a change. Thus, we encourage ARB to put just enough in the CPP program to satisfy EPA and not seek to over comply with the CPP in terms of targets submitted to the EPA. As noted previously, ARB and California may still opt for lower state caps on the EGU sector than what is submitted to the EPA, but the two need not and probably should not be the same in order to reduce the risk of Federal oversight and enforceability. All of the financial relief valves to ensure minimal impacts on the broader California economy included in the cap-and-trade system and in AB 32 will be maintained for the non-EGU sectors and would not be

options under the Clean Power Plan program. Furthermore, federal enforcement of what has been since its inception a state program will also weigh heavily on the CPP program. EPA has the authority to over file even when the implementing state is satisfied with its or and the EGUs compliance. EPA can and does frequently use its authority to obtain information from regulated entities under Clean Air Act Section 114. Just responding these requests can involve significant cost and employee hours running into the \$100,000s for larger facilities with numerous records. And, even if an EGU satisfies all of ARBs requests and obtains written clearance for their actions from ARB, EPA can take a different view and send a notice of violation to the EGU and prosecute for noncompliance. And often, it is impossible to get preclearance from EPA. Thus, EPA's enforcement authority adds a significant risk to regulated EGUs. Therefore, all parts of the program that can be excluded from the CPP program should be excluded and caps should be set at the minimum required to comply with the CPP. This includes keeping the remainder of the cap-and-trade program – everything other than the E Allowances – out of the CPP program submitted to EPA. In this environment, less is more.

Conclusion

The electric grid is becoming more regional. The energy imbalance market that began with PacifiCorp is now extending into NV Energy's territory with others lining up to join. Furthermore, PacifiCorp and the California Independent System Operator (ISO) are evaluating the benefits and costs of PacifiCorp becoming a participating transmission owner. If the studies show benefits to customers of both entities, the ISO would become a regional transmission organization operating in California, Idaho, Oregon, Utah, Washington and Wyoming. A consistent greenhouse gas reduction program between western states would remove any disparities in requirements for instate or out of state EGUs. California can continue to lead by creating a rigorous EGU program other states can join showing those states that carbon reduction can be achieved at a reasonable cost and incentivizing other states to follow California's leadership in order to link to to the larger market and comply with SB-1018.

We thank ARB Staff for their consideration of our comments and look forward to future discussions of these issues.

Respectfully yours,

DAY CARTER & MURPHY LLP

/s/

Jane E Luckhardt

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