COMMENTS OF SOUTHERN CALIFORNIA EDISON COMPANY TO THE CALIFORNIA AIR RESOURCES BOARD ON THE PROPOSED 2013 REGULATORY CHANGES TO THE CAP-AND-TRADE REGULATION

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I.

INTRODUCTION AND EXECUTIVE SUMMARY

Southern California Edison Company ("SCE") respectfully submits its comments to the California Air Resources Board ("ARB") on its Proposed Amendments to the California Cap-and Trade Regulation[1] ("Proposed Regulation Order").[2] SCE appreciates the continued opportunity to work with ARB staff on improving the cap-and-trade regulation. SCE's comments suggest that the ARB:

- Modify draft regulation language requesting employee contact information;
- Modify the regulation so that acceptance of an entity's auction application is not contingent on an attestation that the entity has not been subject to investigation;
- Modify the Compliance Instrument Tracking System Service ("CITSS") user terms and conditions to protect confidential information from public disclosure and allow for flexibility in compliance deadlines in the event of a failure of the CITSS platform;
- Specify that any electric distribution utility disclosure required by the California Public Utilities Commission ("CPUC") is permitted;
- Modify the rules for disclosure of cap-and-trade consultants and advisors to reduce administrative burdens and reduce the risk of unnecessary disclosures;
- Change requirements for transfer requests to reflect established transactional processes;
- Refrain from releasing individual compliance account balances, which will unfairly expose compliance entities' sensitive position information;

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1 Regulation for the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms ("Cap-and-Trade Regulation"), CAL. CODE REGS. tit. 17, § 95856(f)(1)(2013).

2 California Air Resources Board, Proposed Amendments to the Cap-and-Trade Regulation ("Proposed Regulation Order") (*available at* http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isorappe.pdf).

- Allow covered entities to select which compliance instruments they will use to meet their compliance obligations;
- Continue to address cost containment, as the proposed increases to the Allowance Price Containment Reserve ("APCR") supply is a good first step but is not sufficiently responsive to Board Resolution 12-51;
- Reflect recent clarifications regarding Renewable Energy Credits ("REC") retirement for the Renewables Portfolio Standard ("RPS") adjustment in the regulation;
- Amend Resource Shuffling Safe Harbor #10 for added clarity;
- Note that its Energy Imbalance Market ("EIM")-related regulation might require future alteration; and
- Retain the measures taken to equitably compensate Combined Heat and Power ("CHP") facilities.

II.

THE ARB SHOULD MODIFY DRAFT REGULATION LANGUAGE REQUESTING EMPLOYEE CONTACT INFORMATION

As currently outlined in Section 95830(c)(1)(I) of the Proposed Regulation Order, ARB seeks to collect names and contact information for "all persons employed by the entity that will have either access to any information regarding compliance instruments, transactions, or holdings; or be involved in decisions regarding transactions or holding or compliance instruments; or both."[3] These requirements are unclear and could present an onerous administrative challenge, particularly for large market participants. Many large covered entities may have hundreds of employees with knowledge of compliance instruments and holdings, most of whom have no role in transaction decision-making. The roles and responsibilities of these

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[3] California Air Resources Board, Proposed Amendments to the Cap-and-Trade Regulation, Appendix E, Proposed Regulation Order, CAL. CODE REGS. tit. 17, § 95913(f)(5)(E), at 181.

employees change frequently, so managing and updating this list would be burdensome, requiring an unnecessarily large and sustained administrative effort.

New proposed language in Section 95912(d)(5) would exacerbate the problem.[4] Under this section, if the aforementioned list changes 30 days prior to an auction or 15 days after an auction, the entity's auction participation may be denied.

The ARB's intent in collecting this employee contact information appears to be directed at preventing covered entity employees from registering as Voluntary Associated Entities ("VAEs") with individual tracking accounts, which would create conflicts of interest between market participants. To more effectively prevent such conflicts of interest, the ARB should focus its due diligence on VAEs and consultants hired as market advisors, rather than relying on exhaustive and unwieldy employee data from large compliance entities.

III.

THE ARB SHOULD NOT MAKE ACCEPTANCE OF AN ENTITY'S AUCTION APPLICATION CONTINGENT ON AN ATTESTATION THAT THE ENTITY HAS NOT BEEN SUBJECT TO INVESTIGATION

The auction participant application, which must be completed by all entities wishing to participate in the ARB's quarterly auctions, currently requires the applicant to identify any "previous or pending investigation" for market violations under current regulations.[5] In Section 95912(d)(4)(E) of the Proposed Regulation Order, this prerequisite for completing the auction application has been changed to require the applicant to attest that the participating entity, along with any other entities with which it shares a direct or indirect corporate association, has not been subject to any previous or ongoing investigation.[6] Below, SCE identifies three critical problems with the attestation provision as proposed by the ARB.

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4 Proposed Regulation Order § 95912(d)(6) at 174.
5 Cap-and-Trade Regulation, § 95912(d)(4)(C).
6 Proposed Regulation Order, § 95912(d)(4)(E), at 173.

A. Investigations Do Not Constitute Evidence of Market Manipulation or Wrongdoing.

Like many other large compliance entities in the cap-and-trade program, SCE actively participates in a variety of different markets, including markets for power, natural gas, securities, derivatives, and emissions. It is common practice for regulators in many of these markets to investigate the actions of many market participants in response to any abnormal functioning of the market. Moreover, such regulators do not always inform the market participants that they are being investigated. Such investigations frequently conclude with many, if not all, of the investigated entities cleared of any charges.

Simply knowing about any previous or ongoing investigations opened against a compliance entity without knowing the outcomes of these investigations would not serve any legitimate purpose for the ARB or Auction Administrator. Information on convictions and penalties assessed as a result of market violations would prove much more relevant to the ARB as a tool to prevent market manipulation.

B. A Participating Entity May Not Be Privy to Information Regarding Market Investigations of Other Entities With Which It Shares a Corporate Association.

Many compliance entities that participate in the ARB auctions, including investor-owned utilities such as SCE, operate as wholly-owned subsidiaries of parent companies, which may also own other commercial entities in whole or in part. These other subsidiary companies would fall under the definition of direct or indirect corporate associations as set forth in the cap-and-trade regulation, and thus would be included in the requirement for the compliance entity to attest to the absence of any market investigations in its auction application.

However, due to rules governing affiliate conduct and standard company practices for information disclosure regarding ongoing legal investigations, company representatives completing the auction application on behalf of the compliance entity may not have access to information regarding previous or ongoing investigations for market violations at other companies with which the compliance entity shares a direct or indirect corporate association. It

is not reasonable for the ARB to require that compliance entities make attestations based on potentially sensitive legal information from other corporate entities.

C. It Is Unreasonable for the ARB to Deny an Entity's Auction Application Solely Based on the Disclosure of Previous or Ongoing Market Investigations.

Participation in the ARB auctions is an important mechanism for ensuring compliance with the cap-and-trade regulation, especially for entities with large compliance obligations that are subject to regulatory restrictions regarding their participation in secondary exchange-traded or over-the-counter markets for compliance instruments. Allowance awards from the ARB auctions also constitute a major source of liquidity that flows into secondary markets for compliance instruments as compliance entities hedge or refine their positions. If the ARB excludes entities that disclose a previous or ongoing investigation from participating in the auctions, as is currently proposed, the ARB would severely limit the possible avenues for the excluded entities to satisfy their compliance obligations and substantially reduce available liquidity in the secondary markets. Both of these outcomes would result in increased costs for all compliance entities to meet their compliance obligations under the cap-and-trade regulation, producing costly and undesirable results for compliance entities and the program as a whole.

There is no reason why the presence of an investigation alone, without a conviction or penalty, should affect the investigated entity's ability to participate in the auctions, especially given the strong existing controls that the ARB employs around auction conduct and market monitoring. This unnecessary control measure could exclude major players from participating in the auctions. Rather than resulting in fairer auctions or reducing the risk of manipulation, this measure would instead raise compliance costs for all entities and cripple the functioning of the entire market.

Since investigations do not equate to evidence of market manipulation or other wrongdoing, the exclusion of compliance entities from bidding at auction based solely upon a prior investigation having taken place would not achieve the ARB's goal of reducing market

manipulation. Accordingly, the ARB should change its proposed requirement for applicants to submit the aforementioned attestation as part of their auction applications. The ARB should require applicants only to disclose penalties or punitive actions that they have incurred for violations of market regulations, but not require information regarding ongoing investigations or actions taken against other associated entities. Unless the ARB deems the information materially relevant to bidding behavior in the auctions, the disclosure of this information should not prevent compliance entities from participating in the ARB auctions.

IV.

THE CITSS USER TERMS AND CONDITIONS SHOULD PROTECT CONFIDENTIAL INFORMATION FROM PUBLIC DISCLOSURE, AND SHOULD PLACE LIABILITY WITH WCI, INC. FOR THE PROPER FUNCTIONING OF THE CITSS WEB PLATFORM

As currently proposed in Appendix B of the Proposed Regulation Order, the CITSS User Terms and Conditions contain provisions that are inconsistent with industry standards for website reliability and the confidentiality of user information. SCE agrees that it is important to specify up front the terms and conditions under which participating entities agree to use the CITSS. However, SCE objects to terms that risk the disclosure of confidential information and do not guarantee the reliability of the system; such terms may force participating entities to choose between obeying their risk policies governing the use of Internet platforms or complying with the cap-and-trade regulation, which provides for no alternative compliance mechanism outside of the CITSS.

The proposed language of the CITSS User Terms and Conditions provides inadequate safeguards around confidential information stored on the CITSS web platform by compliance entities and other users of the site. For example, the Terms and Conditions state that the ARB

"may disclose Content to the public to the extent the disclosure is … [not prohibited] by California law,"[7] where Content is defined as "all information, data, text, or other materials that User provides to ARB or Western Climate Initiative ("WCI"), Inc. through use of CITSS."[8] The proposed language thereby gives the ARB the discretion to release holding and compliance account balances held by compliance entities or other participants to the public. The release of this market-sensitive information to the public without a significant lag time (*i.e.* after the end of a compliance period) could encourage manipulation of the allowance market, as the public could gain insight into compliance entities' bid strategies and take advantage of any entity with a short position near the end of a compliance period.

Additionally, the California Public Utility Commission ("CPUC") Matrix of Allowed Confidential Treatment Investor Owned Utility ("IOU") Data protects the IOUs' Net Open Position Information as confidential due to its market-sensitive nature.[9] Position information stored in CITSS is clearly protected by regulations promulgated by another State agency.

In the ARB's current regulatory framework, CITSS is the only available mechanism for meeting compliance obligations. However, under Section 4.1 of the CITSS User Terms and Conditions, compliance entities are prohibited from seeking any legal damages against the ARB or WCI, Inc. arising from the failure of the CITSS platform.[10] This is problematic, as it appears to insulate the ARB and WCI, Inc. from liability if the CITSS platform were to fail and prevent compliance entities from meeting their compliance obligations in a timely manner. Thus, if the ARB levied penalties against a compliance entity for failing to meet a compliance obligation by a mandated deadline, *even if the failure was a direct result of the CITSS platform malfunctioning*, that entity would have no recourse against the operator of the platform. The current industry standard for user agreements involving Internet platforms includes an availability guarantee on

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7 Proposed Regulation Order, Appendix B §1.4, at 339.
8 Proposed Regulation Order, Appendix B §1.3 at 339.
9 D.06-06-066, Appendix 1 IOU Matrix VI. A.
10 Proposed Regulation Order, Appendix B, at 342.

the part of the platform operator of 99% availability, or more. Not only does the ARB fail to make any such guarantee of the availability of the CITSS, it places the burden of economic harm on compliance entities in the event its Internet platform malfunctions. In order to better meet the applicable industry standard, the ARB should revise the liability provisions of the CITSS User Terms and Conditions to specify that WCI, Inc., as the creator and operator of the platform, will guarantee the availability of the CITSS platform to registered users at least 99% of the time, and that the ARB will postpone compliance deadlines in the event of a failure of the CISTS platform at any point during the 72-hour period preceding a compliance deadline.

V.

THE ARB SHOULD SPECIFY THAT ANY ELECTRIC DISTRIBUTION UTILITY DISCLOSURE REQUIRED BY THE CPUC IS PERMITTED

SCE appreciates ARB's attempt to clarify disclosure prohibitions relating to auction information in Section 95914(c)(2)(D) of the Proposed Regulation Order. SCE recommends that ARB further modify this language to explicitly exempt electric distribution utilities' disclosure of such information when required to do so by the CPUC. Specifically, the Commission requires each utility to discuss procurement strategies and activities with its Procurement Review Group ("PRG"), which is comprised of participants who are subject to strict non-disclosure agreements.

Restricting the PRG's access to procurement-related information could jeopardize regulated utilities' cost recovery. Additionally, there should be no requirement for a utility to report each disclosure to the CPUC or its PRG to the ARB. The CPUC and PRG are entitled to all of SCE's procurement-related information, and it would be administratively burdensome to update the ARB prior to every such disclosure. To this end, SCE proposes the following changes to Section 95914(c)(2)(D) (throughout these comments, SCE's proposed changes are **bolded** to distinguish them from the ARB's proposed amendments):

> When the release is by an electric distribution utility of information regarding compliance instrument cost and other disclosures specifically required by the California Public

Utilities Commission **pursuant to any applicable rules, orders, or decisions**. ~~**In the event of a disclosure pursuant to this section, the electricity distribution utility must provide the specific statutory reference or to ARB that requires the disclosure of the information.**~~

VI.

THE ARB SHOULD MODIFY THE RULES FOR DISCLOSURE OF CAP-AND-TRADE CONSULTANTS AND ADVISORS

Section 95923 of the Proposed Regulation Order defines "Cap-and-Trade Consultant or Advisor" and would require entities registered in cap-and-trade program to disclose identifying information about cap-and-trade consultants or advisors, along with a brief description of the work performed.[11] SCE appreciates the sensitivity to rules governing confidentiality, such as the attorney-client privilege, which the proposed regulation language attempts to address in section 95923(a)(2) by limiting disclosure to a description that does not "violate any of the rules under which the Consultant or Advisor may be required to observe."[12] Still, this proposed section opens the door to possible waivers of privilege, is administratively burdensome, and can easily lead many regulated entities to be unintentionally noncompliant. For example, must the regulated entity now monitor every consultant's employee or law firm associate that might be put on a bill -- and constantly update disclosures accordingly? There is no information released in this disclosure that would be useful to the ARB that cannot be obtained through a subpoena. SCE proposes modifying the regulation language to require regulated entities to maintain records of such consultants or advisors and provide these records to the ARB upon their request, within 10 days of the request.

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[11] Proposed Regulation Order § 95923, at 203.
[12] *Id.*

VII.

REQUIREMENTS FOR TRANSFER REQUESTS MUST BE CHANGED TO REFLECT ESTABLISHED TRANSACTIONAL PROCESSES

SCE appreciates the ARB's attempt to clarify the term "settlement date" as it relates to transfer requests for transferring compliance instruments between accounts.[13] However, the ARB should modify Section 95921(a)(3) of the Proposed Regulation Order to match established transactional protocols. Specifically, the term "execution date" typically refers to the date on which the terms of a (bilateral or exchange) contract are agreed to, not the date on which a transfer is scheduled to occur. The proposed language, as written, could cause confusion. For example, SCE may execute a futures trade over the Intercontinental Exchange on October 11, to purchase 10,000 allowances that will be delivered on December 30. Payment to the seller will not be released until after SCE confirms receipt of the 10,000 allowances on December 30. Under Section 95921(a)(3)(D), the transfer request for this transaction would have to be completed by October 14 even though the delivery under the exchange contract is not scheduled to occur until December 30. To clarify the requirements for transfer requests, SCE suggests the following changes to Section 95921(a)(3):

> (3) The parties to a transfer will be in violation and penalties may apply if the above process is **not** completed:
>
> (A) **Within**~~**More than**~~ three days **of**~~**after**~~ the initial submission of the transfer request; ~~**or**~~**and**
>
> (B) **Within**~~**More than**~~ three days **of**~~**after**~~ the **delivery**~~**execution**~~ date or termination date ~~settlement day~~ of the transaction agreement for which the transfer request is submitted; **or if the above process is completed:**
>
> (C) More than three days after the transfer of consideration from the purchaser of the compliance instrument to the seller as provided by the transaction agreement; or

[13] Proposed Regulation Order, § 95921(b)(3)(B), at 197.

(D) More than three days after the **~~execution~~ payment ~~of~~for** the **compliance instrument(s) ~~underlying~~** trade**d** on an exchange or other trading platform **is received by the seller of the compliance instrument**.

In addition, SCE suggests the following change to the definition in Section 95802(130):

"**~~Execution~~Delivery** Date" means **the date specified in a transaction agreement prior to which ~~a provision of a transaction agreement that requires~~** the transfer of compliance instruments **~~on or before a date specified in the agreement~~ must occur.**

VIII.

RELEASING INDIVIDUAL COMPLIANCE ACCOUNT BALANCES WILL UNFAIRLY EXPOSE COMPLIANCE ENTITIES' SENSITIVE POSITION INFORMATION

Consistent with its previous comments,[14] SCE strongly opposes any release of individual CITSS account balances by the ARB. Releasing entity-specific compliance account balances would put covered entities at a competitive disadvantage because other market participants would be able to estimate their net positions, and could manipulate auction bidding behavior and market prices accordingly.

SCE continues to advocate for the release of aggregated compliance account holdings combined with compliance surrender information. To add clarity, SCE recommends that the ARB make the following change to Section 95921(e) of the cap-and-trade regulation:

> The Executive Officer will protect confidential information to the extent permitted by law by ensuring that the accounts administrator: […]

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[14] Comments of Southern California Edison Company to the California Air Resources Board on the January 25, 2013 Information Sharing Workshop, Feb. 5, 2013, at 1-7 (*available at* http://www.arb.ca.gov/lists/jan- 25-info-share-ws/1-2013-02 05_sce_comments_on_arb_information_sharing_workshop.pdf) and Comments of Southern California Edison Company to the California Air Resources Board on its Discussion Draft of Proposed Amendments to the Cap-and-Trade Regulations, Aug. 2, 2013, at 9-10 (*available at* http://www.arb.ca.gov/lists/com-attach/38-cap-trade-draft-ws-BjRXYVRkWDgGLVVl.pdf).

(4) Releases **aggregated** information on the quantity ~~and serial numbers~~ of compliance instruments contained in **all** compliance accounts in a timely manner."

IX.

THE ARB SHOULD ALLOW COVERED ENTITIES TO SELECT WHICH COMPLIANCE INSTRUMENTS THEY WILL USE TO MEET THEIR COMPLIANCE OBLIGATIONS

At the ARB's July 18 Workshop, regulated entities expressed their opposition to the staff-proposed compliance instrument retirement order. To address these concerns, ARB Staff indicated that they would consider allowing covered entities to select which compliance instruments in their compliance accounts to retire prior to a compliance deadline. By allowing entities to self-select the compliance instruments they wish to retire, the ARB-proposed compliance instrument retirement order would only be enforced if a covered entity failed to select enough instruments for retirement to fulfill its compliance obligation. Retirement flexibility would allow compliance entities to better manage their portfolios, reduce the administrative burden for the regulatory agency, and reduce the risk of an unlawful taking of property if the ARB removed compliance instruments from an entity's account without counting those toward the entity's compliance obligation (e.g., if offset credits in excess of the 8% quantitative usage limit were taken during the annual compliance surrender). SCE supports this framework.

Unfortunately, ARB chose not to implement this change in the Proposed Regulation Order. The ARB instead sought to address the concern regarding the taking of offset credits in excess of the 8% limit by removing the provision for the annual retirement of surrendered compliance instruments under Section 95856(g). While this regulatory change may address the earlier-specified concern, it creates another issue: covered entities may now be more stressed by their holding limits. Under the current regulatory framework, the total holdings of a compliance entity would decrease each year (as ARB retired compliance instruments equivalent to 30% of

the entity's prior year emissions). With the proposed elimination of the annual retirement, the entity's account holdings would continue to increase throughout the compliance period (except in the year following a triennial surrender). The relatively greater volume of compliance instruments an entity must hold at any given time means that some entities may be forced to adjust their compliance strategies so as not to exceed their holding limit and limited exemption, resulting in potentially lower market liquidity and trading opportunities.

SCE urges the ARB to adopt SCE's earlier suggestion of allowing compliance entities to self-select compliance instruments for retirement. The ARB should also continue exploring operational changes to the CITSS to allow for this elective transfer of compliance instruments for retirement.

X.

THE PROPOSED INCREASES TO THE APCR SUPPLY IS A GOOD FIRST STEP BUT IS NOT SUFFICIENTLY RESPONSIVE TO BOARD RESOLUTION 12-51

A. SCE Supports the Approach that Staff Has Identified for Borrowing Allowances, But Borrowing Allowances Is Not a Long-Term Cost Containment Mechanism and Does Not Satisfy Board Resolution 12-51.

SCE supports the proposal to facilitate allowance borrowing from future compliance years to fill the third tier of the ACPR for cost containment purposes.[15] Such an approach can act to moderate short-term price fluctuations and help promote a more smoothly functioning allowance market. Utilizing the APCR ensures that only regulated compliance entities will be able to procure borrowed allowances from future compliance years and that borrowed allowances are used directly for compliance. Additionally, borrowing allowances first from the

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[15] Section 95913(f)(5)(E), at 196-97.

most distant vintage year in circulation allows the allowance market the greatest amount of time to address price volatility.

However, as a stand-alone proposal, this borrowing mechanism is insufficient to provide assurance to the market that allowance prices will not rise above the highest price tier of the APCR,[16] and therefore does not satisfy Board Resolution 12-51.[17]

Resolution 12-51 directs staff to develop mechanisms to ensure that allowance prices do not exceed the highest price of the APCR. The approach included in the Proposed Regulation Order provides no such assurance. Borrowing is important to reduce short-term price volatility, but under a stress-case scenario where demand for allowances exceeds supply for a prolonged period of time, the APCR could be exhausted, which could cause prices to exceed the highest APCR tier price.[18] The Proposed Regulation Order states that if the quantity of accepted bids at the highest price tier of the APCR exceeds the available allowances, including any allowances that have been borrowed from future vintage years, the reserve sale administrator will distribute the available allowances among bidders on a pro-rated basis, causing each bidder to receive fewer allowances than its original bid.[19] In this scenario, if compliance entities are not able to procure all of the allowances they need for compliance at the price of the highest tier of the APCR, it is reasonable to assume that prices in the secondary market would move higher than that price level as well.

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16 The APCR is created by taking allowances from the program's allowance budget across all three compliance periods. The allowances in the APCR are made available for sale at a pre-established price once each quarter to covered entities.

17 California Air Resources Board, Resolution 12-51, Oct. 18, 2012, at 2 (*available at* http://www.arb.ca.gov/cc/capandtrade/final-resolution-october-2012.pdf).

18 For example, if strong economic growth results in reported emissions significantly above expectations for several consecutive years, the volume of allowances in the available future vintage years that are eligible for borrowing under Staff's proposal may be insufficient to keep allowance prices below the level of the highest APCR tier.

19 Proposed Regulation Order, § 95913(h)(5), at 184.

B. A Robust Portfolio of Cost Containment Measures Will Serve to Reduce Price Volatility and Provide True Cost Containment, Satisfying Board Resolution 12-51.

SCE supports the cost containment proposal offered by the Joint Utilities Group.[20] That proposal established three categories of cost containment measures: (1) measures to take effect immediately; (2) measures that would be triggered when the market moves closer to the highest APCR price; and (3) an approach to address compliance instrument availability when the APCR is exhausted. SCE's recommendations for each of these three categories of cost containment measures are described in more detail below.

1. Measures That Would Take Effect Now

SCE recommends that the ARB adopt certain measures that would take effect now. These measures would – over time – reduce the likelihood of prices rising above the APCR in the future by: (1) reducing demand for compliance instruments; (2) increasing the supply of compliance instruments; and (3) ensuring that compliance instruments are accessible in the marketplace. Specifically, SCE suggests that the ARB:

a) Approve more offset protocols to increase the supply of offsets.

b) Exempt offsets from projects within California from the 8% offset limit.

c) Allow each covered entity to carry over any unused portion of its 8% offset limit to use for future compliance.

d) Address constraints imposed by the current holding limit.

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[20] Joint Utility Group presentation at the June 25 ARB Cost Containment Workshop (*available at* http://www.arb.ca.gov/cc/capandtrade/meetings/062513/industry-present.pdf).

e) Hold an additional auction after the end of each compliance period. The ARB should redistribute allowances between auctions to allow for one additional auction per compliance period, and/or acquire more allowances for auction. This auction should be held between September 1 of the year following the end of a compliance period, when verification statements for prior-year emissions are due,[21] and November 1, when compliance entities are required to demonstrate compliance.[22]

2. Measures That Would Be Triggered When the Market Approaches the Highest APCR Price

SCE recommends that the ARB adopt certain measures that, when triggered, would quickly alter compliance instrument demand/supply dynamics and constrain upward pressure on market prices for a period of time. Borrowing of allowances is included in this category. One example of a trigger is a percentage level of depletion of the APCR. Specifically, SCE suggests that the ARB adopt the following proposals:

a) **Unused Offset Proposal**: Currently, a compliance entity is limited in its use of offsets to 8% of its compliance obligation per compliance period. Under the Unused Offset Proposal, when the trigger is reached, the ARB would calculate the program-wide shortfall of unused offsets from earlier compliance periods, and allow compliance entities to apply the difference to later compliance periods. This in effect will increase the quantitative usage limit for entities in a single compliance period, thus reducing upward price pressure on allowances in the short term, while maintaining the quantitative usage limit over the entire term of the program.

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[21] Amendments to the Regulation for the Mandatory Reporting of Greenhouse Gas Emissions, CAL. CODE REGS. tit. 17, § 95103(f), at 64-5.

[22] Cap-and-Trade Regulation, § 95856(f)(1).

b) **Compliance Account Proposal:** When the trigger is reached, the ARB could allow covered entities to transfer surplus allowances from their compliance accounts to their limited use holding accounts. This would allow entities that have built up a bank of excess allowances to re-inject those allowances in the market, which will improve market liquidity.

c) **Limited Borrowing Proposal:** When the trigger is reached, the ARB could allow covered entities to surrender current-year vintage allowances and next-year vintage allowances to meet their compliance obligations for the previous year (not applicable post-2020).[23]

d) **Offset Geographic Scope Proposal:** When the trigger is reached, the ARB could increase the number of compliance-grade offsets by expanding the geographic scope of the approved offset protocols to North America.

e) **Offset Project Start Date Proposal:** When the trigger is reached, the ARB could increase the number of compliance-grade offsets by changing the Offset Project Commencement date established in Sections 95973(a)(2)(B) and (c) of the cap-and-trade regulation to an earlier date.

3. Measures That Would Keep Prices at the Third Tier of the APCR When the APCR Is Exhausted

SCE recommends that the ARB adopt certain measures that, when triggered, would keep allowance prices at the third tier of the APCR regardless of current demand, while still preserving the environmental integrity of the cap-and-trade program over time. Upon depletion of the highest tier of the APCR, the Executive Officer should make available (through the APCR

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[23] Currently, the compliance obligation surrender date is always one year after the last vintage year of allowable allowances.

sale mechanism) additional allowances, in excess of the cap, necessary to satisfy the demand of compliance or opt-in compliance entities at the price set for the highest tier of the APCR in the relevant year. The Executive Officer could then use the funds raised by the sale of these additional allowances to ensure greenhouse gas ("GHG") reductions equal to or larger than the number of additional allowances sold. For example, the Executive Officer could:

a) Commission a third party to obtain and retire high-quality offsets not otherwise eligible to satisfy the compliance obligations of compliance entities;

b) Commission a third party to purchase and retire allowances from emissions trading programs outside of California and linked jurisdictions;

c) Commission a third party to invest funds in emission reduction projects outside the capped sectors; or

d) Mandate emission reductions in sectors not covered by the California cap-and-trade regulation.

XI.

RECENT CLARIFICATIONS REGARDING REC RETIREMENT FOR RPS ADJUSTMENT SHOULD BE REFLECTED IN THE REGULATION

At the ARB's July 18th Workshop, SCE again raised the issue of REC retirement for the RPS adjustment because the proposed regulation language remained unclear. SCE was pleased that the ARB clarified that the regulations allow the RPS adjustment for out-of-state renewable energy that is not imported into California, as long as the corresponding RECs are deposited in the Western Renewable Energy Generation Information System ("WREGIS") "retirement sub-account" in the year they were generated, even though the actual retirement of such RECs for RPS compliance purposes may occur later (within the RPS compliance window set by the California Energy Commission). This is an important clarification because the ARB's language

previously suggested that in order to claim the RPS adjustment, the retirement for compliance with the RPS program must also occur during the same year in which the RECs were created. SCE greatly appreciates this clarity and urges the ARB to make changes in its final regulations reflecting the clarification provided by Staff. Specifically, SCE suggests the following change to Section 95852(b)(4)(B) of the cap-and-trade regulation:

> The RECs associated with the electricity claimed for the RPS adjustment must be placed in the retirement subaccount of the entity party to the contract in 95852(b)(4)(A), in the accounting system established by the CEC pursuant to PUC 399.13 ~~**and designated as retired for the purpose of compliance with the California RPS program** used to comply with the California RPS requirements~~ during the same year ~~in~~ for which the RPS adjustment is claimed (and during the year in which those RECs were created). **The RECs must be designated as retired for the purpose of compliance with the California RPS program on a schedule consistent with the rules governing that program.**

XII.

THE ARB SHOULD AMEND RESOURCE SHUFFLING SAFE HARBOR #10 FOR ADDED CLARITY

SCE thanks the ARB for incorporating resource shuffling safe harbors into the Proposed Regulation Order.[24] SCE believes that these safe harbors provide appropriate clarity to the industry in determining whether substitutions of electricity deliveries from a lower emission resource for electricity deliveries from a higher emission resource would constitute resource shuffling. However, the ARB should further modify Safe Harbor #10 to explicitly clarify that selling utility-owned power from a high-GHG resource that was first bid into the California Independent Systems Operator ("CAISO") markets to serve that utility's own load, but that was

[24] Proposed Regulation Order, § 95852(b)(2)(A), at 84-6.

not scheduled through CAISO due to least-cost dispatch, would not be considered resource shuffling. SCE requests the following changes to Safe Harbor #10:

> 10. Short-term transactions and contracts for delivery of electricity with terms of no more than 12 months, or resulting from an economic bid or self-schedule that clears the CAISO day-ahead or real-time market, for either specified or unspecified power, based on economic decisions including implicit and explicit GHG costs and congestion costs, unless such activity is linked to the selling off of power from, or assigning of a contract for, electricity subject to the EPS rules from a power plant that does not meet the EPS with which a California Electricity Distribution Utility has a contract, or in which a California Electricity Distribution Utility has an ownership share, that is not covered under paragraphs 11, 12 or 13 below. **Selling off of power from, or assigning of a contract for, electricity subject to the EPS rules from a power plant that does not meet the EPS with which a California Electricity Distribution Utility has a contract, or in which a California Electricity Distribution Utility has an ownership share, would not constitute resource shuffling if such power was first bid into the CAISO day-ahead or real-time markets at the unit cost including GHG but did not clear the market and was subsequently sold outside of California**.[25]

XIII.

THE ARB SHOULD BE AWARE THAT ITS ENERGY IMBALANCE MARKET ("EIM") RELATED REGULATION MIGHT REQUIRE FUTURE ALTERATION.

SCE appreciates that the EIM-related amendments included in the Proposed Regulation Order are broad enough to accommodate some potential modifications to the CAISO's proposed EIM design.[26] However, there are still many EIM-related issues and processes that could

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[25] Proposed Regulation Order, § 95852(b)(2)(A), at 85-6.

[26] In particular, the ARB did not use overly specific terms, such as "export allocation," which it had considered including in its regulation. *See* ARB, "Mandatory Reporting Workshop: Potential Updates to the California Regulation for the Mandatory Reporting of Greenhouse Gas Emissions," June 26, 2013, at 11 (*available at* http://www.arb.ca.gov/cc/reporting/ghg-rep/revision-2013/mrr-june-workshop2013-1p.pdf).

considerably alter the EIM design before the Federal Energy Regulatory Commission ("FERC") approves a final EIM design.[27] The ARB should be aware that its EIM-related language might require future alteration depending on the outcome of the EIM Proposal approval process.

XIV.

SCE SUPPORTS THE MEASURES TAKEN TO EQUITABLY COMPENSATE CHP FACILITIES

The Proposed Regulation Order includes a number of new sections that address special treatment for certain CHP facilities, specifically "Legacy Contract Generators," "University Covered Entities," and other facilities afforded limited exemptions. "Legacy Contract Generators" are defined as CHP parties with an unamended contract signed prior to 2006 with a counterparty other than an IOU.[28] SCE supports this distinction, as it accurately acknowledges the amendments offered to all IOU-contracted CHP parties in 2012 pursuant to the CHP Settlement.[29] Due to these "Legacy Amendments," any IOU-contract CHP facility was given the opportunity to amend its existing contract to include payment for GHG. It would be inappropriate to allow a facility who was offered but did not accept one of these options – presumably to retain the higher payment structure under their Legacy Agreement – to "double dip" from the ARB and receive additional payment for its GHG obligations. SCE also supports the ARB's new allocation of allowances to University Covered Entities, which will help these facilities transition to the new GHG-inclusive marketplace.[30] Finally, the limited exemption[31]

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27 The CAISO still has to take the EIM proposal to its Board in November and to the FERC after the CAISO's stakeholder process is complete in Q1 2014. For the issues the CAISO may have to work through before approval, see the stakeholders' concerns in their comments on the Third Revised Straw Proposal available at http://www.caiso.com/Documents/Energy%20imbalance%20market%20-%20papers%20and%20proposals%7CStakeholder%20comments.

28 Proposed Regulation Order, § 95802, at 28-9 ("Legacy Contract" and "Legacy Contract Generator").

29 Information on the CHP Settlement, adopted by D.10-12-035, and the associated Legacy Amendments, can be found *at* http://docs.cpuc.ca.gov/WORD_PDF/FINAL_DECISION/128624.PDF.

30 *See* Proposed Regulation Order, § 95870(f), at 107; *see also* § 95891(e), at 141.

31 *See* Proposed Regulation Order, § 95851(c), at 82; *see also* § 95852(j), at 91; and § 95870(g), at 107.

offered to "but for" CHP facilities (*i.e.*, those facilities whose CHP operations push the site over the emissions compliance threshold of 25,000 metric tons CO_2e) represents a correction of incentives for CHP and an equitable balance of environmental integrity of the cap-and-trade program and equal treatment for industrial facilities with and without CHP.

XV.

CONCLUSION

SCE appreciates the opportunity to comment on the latest set of proposed amendments in the Proposed Regulation Order. SCE urges the ARB to make changes to the regulation in accordance with the suggestions contained herein.

Respectfully submitted,

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