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Dr. Steve Cliff
California Air Resources Board
1001 I Street, P.O. Box 2815
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Re: SGEN Comments on Proposed Amendments to the California Cap-and-Trade Program Regulations

These comments are submitted on behalf of Sempra Generation, LLC ("SGEN") concerning the proposed amendments to the California Cap-and-Trade Program Regulations ("Regulations") published by the California Air Resources Board ("ARB") on March 21, 2014. In keeping with staff instruction provided in the "Notice of Public Availability," SGEN has provided comments only on "noticed changes" in this 15-day version of the Regulations. We have not repeated comments submitted on the 45-day proposed changes in areas that remain unchanged from that version with the express understanding that ARB staff will fully address our earlier comments dated February 14, 2014, in the Final Statement of Reasons.

First Point of Receipt

At section 95802(a)(147), ARB has amended the definition of "First Point of Receipt." As proposed, the definition is not consistent with the definition in the Mandatory Reporting Regulation ("MRR") section 95102(a)(176) and should be amended for consistency.

Overbroad Disclosure of Employees and Contractors

At Regulations section 95830(c)(1)(I), ARB has further amended the requirement that entities provide information on employees or contractors that are involved with an entity's Greenhouse Gas Cap-and-Trade Program ("Program") compliance. While SGEN understands that ARB needs a record of the individuals responsible for an entity's conduct, as well as those that have delegated authority to enter into transactions on behalf of the entity, the language as amended continues to be overly broad and could be interpreted to require entities to provide information on employees with minor, non-substantive administrative roles in the Program.

The language of section 95830(c)(1)(I), which refers to "…all persons employed by the entity with knowledge of the entity's market position (current and/or expected holding of compliance

instruments and current and/or expected covered emissions)...." could be read to include employees that perform solely administrative functions focused, for example, on processing settlement data. These duties are performed by employees not involved in any substantive decisions related to the Program, although they would be exposed to "knowledge" of an entity's "holding of compliance instruments." Indeed, sometimes these types of jobs are performed by contract, temporary, or rotational employees. Presumably, ARB is really concerned with the identity of those individuals developing an entity's compliance instrument procurement strategy, those communicating with other market participants to buy or sell compliance instruments, those establishing an entity's auction bidding strategy, those participating in the quarterly auctions, or those involved in other substantive decision-making for a company registered in the Program.

Thus, SGEN suggests that section 95830(c)(1)(I) be revised to state as follows, in order to focus on employees with substantive decision-making authority for an entity's Program participation:[1]

> Names and contact information for all persons employed by the entity involved in decision-making regarding compliance instrument procurement, the transfer of compliance instruments, or the entity's holdings of compliance instruments in the Cap-and-Trade Program or any External GHG ETS linked pursuant to subarticle 12.

Inconsistent Timing Requirements

The modifications made to several sections of the Regulations to address the requirement to update information previously provided to ARB appears to have created an inconsistency between the timing requirements in sections 95830(c)(1)(I), 95830(f)(1) and 95833(e)(3).

Pursuant to proposed section 95830(c)(1)(H), an entity registering for an account in the tracking system must provide certain information to ARB including, among other things: "Identification of all other entities with whom the entity has a corporate association, direct corporate association, or indirect corporate association pursuant to section 95833 . . ."

Proposed section 95830(f)(1) states:

> Registered entities must update their registration information as required by any change to the provisions of 95830(c) within 30 days of the changes becoming effective. When there is a change to the information registrants have submitted pursuant to 95830(c), registrants must update the registration information within 30 calendar days of the change. Updates of information provided pursuant to section 95830(c)(1)(l) may be updated each calendar quarter instead of within 30 calendar days of the change.

[1] Because the comment draft text published by ARB contains many strike out/underlined changes already, the suggested revisions in this letter are shown in clean text format for ease of review.

Further, at sections 95833(e)(3) and (4), the language has been modified to specify that:

> (3) At least quarterly, for any changes to the information disclosed on corporate, direct and indirect corporate associations, pursuant to section 95830(f)(1); and
> (4) No later than the auction registration deadline established in section 95912 when reporting a change to the information disclosed if the changes relate to another entity registered in the Cap-and-Trade Program, otherwise the entity may not participate in that auction.

The proposed revisions are confusing, and could lead to misunderstanding among Program participants. In addition, the revisions are overly burdensome given the complex nature of some Program participant's corporate structure. Therefore, these provisions should be amended to clearly state the following:

Section 95830(f)(1):

> Registered entities must update their registration information, as required by any change to the provisions of 95830(c), or if a change has occurred to the information provided pursuant to 95830(c), no later than the auction registration deadline established in section 95912. An entity may not participate in the auction if it fails to report this information in a timely manner.

Section 95833(e)(3):

> At least quarterly, for any changes to the information disclosed on corporate, direct, and indirect corporate associations pursuant to 95830(f)(1).

Section 95833(e)(4) should be removed from the Regulations.

<u>Control of an Account</u>

The proposed language at section 95833(f)(7), if read literally, could severely limit and will unreasonably complicate the management and advisory services that companies have traditionally provided to participants in existing markets. Proposed section 95833(f)(7) states in part:

> If some or all of the primary and alternate account representatives who are employees of a registered entity have primary responsibility for developing and executing procurement, transfer, and surrender of compliance instruments of another registered entity or other registered entities within the tracking system, the entities will be considered to have a direct corporate association and the requirements of section 95833(f) apply.

In its Initial Statement of Reasons issued on September 4, 2013, staff explained that section 95833(f)(7) was added to "require covered entities who share staff for management of their

tracking system accounts to be treated like direct corporate associations with a sharing of the purchase or holding limits," since this may lead to "…the potential to coordinate on market related decisions…"

While the Cap-and-Trade Program and carbon market are fairly new, the type of energy management and broker services that this proposed language appears to constrain are services that are not uncommon or prohibited in commodity markets generally. Indeed, companies routinely offer and provide services to other market participants which often include management of market positions, providing recommendations on market position valuation, analysis, and strategy, as well as establishing and maintaining various accounts on behalf of a client so the agent can procure and manage Congestion Revenue Rights, bid-in and schedule a client's generation assets in the day-ahead and real-time markets, and buy and sell gas or power. Companies that provide these services implement robust policies, procedures and compliance programs to ensure compliance with, and ensure employees are well educated on, the same conduct that appears to be at the crux of ARB's concern: compliance with antitrust laws, avoidance of conduct that unreasonably restrains competition, conflict of interest, and the obligation to keep any information obtained as part of an advisor-client relationship confidential. The duties performed by one market participant on behalf of another market participant under these arrangements are allowable by market monitors, who are authorized to observe participants' behavior in the market, to ensure that an open and competitive market is maintained and to prevent no one participant from being able to take unfair advantage of the market rules or procedures, to unduly concentrate market power, or to inhibit competition.

If approved, however, the proposed language at section 95833(f)(7) noted above would impose on both entities the requirement to treat each other as if they had a 'direct corporate association' with all of the obligations under the Regulations that this relationship entails, despite the fact that the two entities have only an agent-client relationship and are not, in fact, legally related in any generally accepted corporate entity sense. This is entirely inappropriate and unworkable, as is the requirement to treat two entirely unrelated legal entities as related for the purposes of sharing purchase and holding limits. Section 95833(f)(7) should be removed from the proposed amendments.

Compliance Instrument Retirement

Section 95856(h)(1) has been modified to address the annual surrender obligation and provide an order in which instruments are to be retired. Subsection 95856(h)(1)(A) specifies that offset credits will be retired first, up to eight percent of the emissions with a compliance obligation pursuant to 95855. While SGEN believes that the application of the Quantitative Usage Limit ("Limit") is appropriate when ARB retires instruments from an entity's compliance account, the application of the Limit to the Annual Surrender, and Triennial Surrender as indicated at section 95856(h)(2), could lead to confusion.

Other relevant sections of the Regulations support the use of the 8% offset limit only in the context of the Triennial Compliance Obligation. For example, Section 95854(b) specifies that each covered entity may surrender, "to fulfill its compliance obligation for *a compliance period*,

offsets to not exceed 8% of the total instruments surrendered, also known as the 'Quantitative Usage Limit'." Under the current definition of 'Compliance Period,' at section 95802(a)(56), this is the three-year period for which the compliance obligation is calculated. Further, section 95856(f)(2) is specific in addressing that "the total number of compliance instruments submitted to fulfill the *triennial compliance obligation* is subject to the quantitative use limit…" Therefore, any suggestion that the 8% offset usage limit should apply to the annual surrender of compliance instruments would disrupt the existing surrender regime under which participants have been operating since the Program began. Indeed, if read literally, the proposed amendment could be read to allow an entity to retire offset credits to fulfill up to 8% of an annual obligation, and another 8% of a triennial obligation.

Accordingly, any changes to 95856(h)(1) and (2) must be consistent with retention of the 8% offset limit only at the Triennial Compliance Obligation surrender stage and should be clarified.

Auction Participation Attestation

At section 95912(d)(4)(E), ARB has proposed amendments to the attestation an entity is required to complete if it intends to participate in an auction. The attestation, as proposed, requires an entity to disclose the existence and current status of any ongoing investigation, or an investigation that has occurred within the last ten years, with respect to any alleged violation of any rule, regulation, or law associated with any commodity, securities, environmental or financial market with respect to the entity participating in the auction, and all other entities with whom the entity has a corporate association, direct corporate association, or indirect corporate association, that participate in a carbon, fuel, or electricity market.

While we understand why ARB may be interested in open investigations of the entity participating in an auction, it is unclear why ARB would require such information for investigations opened (and presumably resolved) within the past 10 years, or investigations of all other entities with whom the registered entity has a corporate association, direct corporate association, or indirect corporate association.

As SGEN has explained in prior comments, many of the participants in the Program (including SGEN) are subsidiaries of large corporations with corporate structures that involve dozens or even hundreds of other affiliates and subsidiaries which operate largely independently from one another, but which are required by the Regulations to be identified as corporate associations even though these other affiliates have nothing to do with the Program. Many or most of these corporate associations may not have readily available access to information regarding the others with whom the only relationship they share is that of having the same indirect ultimate corporate parent. In some cases, affiliated companies are barred from having or obtaining the type of information ARB contemplates requiring by section 95912(d)(4)(E) due to information sharing prohibitions under the California Public Utilities Commission Affiliate Rules and Federal Energy Regulatory Commission Standards of Conduct. Additionally, many or most of the corporate entities in question are not registered in the Program, subject to the Regulations, within the jurisdiction of ARB, or located within California or even in the United States. The proposed language of 95912(d)(4)(E) is drastically overbroad and over-reaching, and will be at a minimum

onerous to comply with for such entities and, at worst, impossible to comply with. Entities will be continuously at risk of not being able to participate in auctions, or risk misreporting or providing ARB inaccurate details under this attestation, which could be considered a violation of 95921(f)(2)(E), (F), or (D), or the affiliate compliance rules promulgated by state or federal agencies.

Thus, section 95912(d)(4)(E) should be revised to state as follows:

> An attestation of the entity participating in the auction, disclosing the existence and status of any ongoing investigation of that entity with respect to any alleged violation of any rule, regulation, or law associated with any commodity, securities, environmental, or financial market.

Changes to Auction Application Information

The proposed amendments modify section 95912(d)(5) providing that auction participation may be denied if an entity "has any changes to the auction application information listed in subsection 95912(d)(4) within 30 days prior to an auction." ARB further amended this section to note that changes to indirect or direct associations are not included, unless the corporate associations have entities registered in the tracking system.

The addition of the language reducing the scope of reporting to only entities also registered in the tracking system is an improvement which SGEN supports. However, this requirement remains burdensome to Program participants who are required to take many steps, and perform extensive due diligence, to ensure that it has informed ARB of any changes to its application information prior to the auction. Given the complexities that exist in large corporate structures, it is unreasonable to force entities that participate in the Program to be at constant risk of violation due to failure to report information that they have no ability to know or discover, in particular if the corporate associations in question are entities which are subject to the information sharing prohibitions under the California Public Utilities Commission Affiliate Rules and Federal Energy Regulatory Commission Standards of Conduct. As provided under the Regulations at section 95833(c), "Any registered entity subject to affiliate compliance rules promulgated by state or federal agencies shall not be required to disclose information or take other action that violates those rules."

Therefore, section 95912(d)(5) should be removed from the proposed amendments. If staff continues to recommend the proposed amendment, however, ARB should revise it as follows:

> An entity with any known changes to the auction application information it submitted, listed in subsection 95912(d)(4), must report those changes to ARB no later than the auction registration deadline established in section 95912. An entity may not participate in the auction if it fails to report this information in a timely manner. For the purposes of changes to indirect and direct corporate associations, this section only applies to those corporate associates with entities registered in the tracking system.

Definition of a "Cap-and-Trade Consultant or Advisor"

SGEN agrees that the term "Cap-and-Trade Consultant or Advisor" ("Advisor") should be defined within the Regulations. However, the language in section 95923(a) as proposed inappropriately suggests that the duties listed within section 95979(b)(2) of the Cap-and-Trade Regulation and section 95133(b)(2) of the MRR are to be considered duties that would classify someone as an Advisor. These referenced sections contain lists of duties a consultant may provide to an entity, but the inclusion of these duties in the definition of an Advisor is overly broad and does not provide the clarity needed regarding the functions performed by an Advisor in the context of participation in the Program.

In its 'Initial Statement of Reasons' issued September 4, 2013, staff's rationale for defining the role of an Advisor was to "differentiate between employees of firms and consultants or advisors, and also to clarify that consulting or advisory services are not publication services available to subscribers but specific services for the entity registered in the cap-and-trade program." The proposed amendments to this section remove the reference to "paid for information or advice related to the Cap-and-Trade Program," yet continue to reference the panoply of duties listed within section 95979(b)(2) of the Cap-and-Trade Regulation and section 95133(b)(2) of the MRR, which goes well above and beyond those that should classify one as an Advisor.

Section 95923(a) should be revised to state as follows in order to avoid confusion when reporting the formation or termination of an advisor-client relationship:

> A "Cap-and-Trade Consultant or Advisor" is a person or entity that is not an employee of an entity registered in the Cap-and-Trade Program, but is retained by the entity to provide information or advice specific to the entity's auction bidding strategy, carbon instrument transactions, or assessment of the entity's holdings of carbon instruments.

Retention of a Cap-and-Trade Consultant or Advisor

Section 95914(c)(3)(A) and (B) have been further amended to remove the requirement that any entity that has retained the services of a Cap-and-Trade Consultant or Advisor must inform ARB of the advisor's retention, "and identify the Consultant or Advisor...and provide an attestation by the Primary Account Representative of the entity retaining the advisor…"

SGEN agrees with this modification, but further modification is required. This amendment continues to be duplicative of the requirement that an entity disclose retention of a Consultant or Advisor under section 95923(b) and (c) when registering with ARB, within 30 days of entering into a contract with a Cap-and-Trade Advisor or Consultant, and within 30 days of a change to any previously reported information regarding a Cap-and-Trade Advisor or Consultant. Further, to impose an obligation on a "Consultant or Advisor" who has clients participating in the Cap-and-Trade Program to inform ARB 15 days prior to each carbon auction of the names of its clients and the advisory services being performed, and specify that this information be

Section 95914(c)(3) should be removed from the proposed amendments.

Proposed Requirements for Transfers

SGEN appreciates the efforts ARB intends to undertake to tailor CITSS to account for all possible transfers that could potentially occur in an entity's account, but the proposed amendments to section 95921(a) and (b) are unnecessary, confusing to Program participants, and overly burdensome.

The Regulations, as proposed, remove the requirement at 95921(a)(1)(E) that, "the completed transfer request must be received by the accounts administrator no more than three days following the day of settlement of the transaction agreement for which the transfer request is submitted," and introduces varying requirements at 95921(a)(3) and (4) making "the parties to a transfer" in violation of these sections if transfers are not processed within the specified time periods. Not only will these amendments cause confusion over the "initial submission date" and "expected settlement date," but these amendments imply that if this requirement is not met, it is *the parties* to the transfer that have violated the Regulations, even though the negligence of one party cannot be reasonably controlled by the other party. This would obviously be wholly unfair.

Sections 95921(a)(3) and (4) should be removed from the proposed Regulations and the language at 95921(a)(1)(E) reinstated. Amended section 95921(i)(1)(C) and (D) should be revised further to eliminate the reference to 95921(a)(1)(C), (a)(3), and (a)(4), and should reference only the timing requirement under 95921(a)(1)(E). If ARB agrees to make the changes SGEN recommends here, the proposed definitions of "Expected Settlement Date," "Expected Termination Date," and "Over-the-Counter" should not be added to section 95802(a) at subsections 138, 139, and 260 because they will not be needed.

The proposed amendments to section 95921(b) would require entities to provide potentially proprietary information regarding transactions with an unreasonable level of detail given the very limited timeframe in which all involved parties must review and approve a transfer. This short timeframe puts transferring entities at risk of either missing a transaction completion deadline, or providing ARB inaccurate details of a transaction which could be potentially viewed as false or misleading, and therefore a violation of 95921(f)(2)(E), (F), or (D). It should be noted that many of the trades that represent transfers in and out of CITSS accounts are transactions which are subject to U.S. Commodity Futures Trading Commission reporting requirements, and the details of the transactions (settlement price for example) is readily available via ICE and other exchanges. Given the limited role of ARB in these transactions, it is more appropriate that ARB utilize its current right to request the underlying contracts for the transactions should additional market monitoring information be desired.

The language of section 95921(b)(1) through (7) in the currently effective Regulation should remain effective, and the suggested modifications to 95921(b) and (c)(1) through (5) in this 15-day version should not be approved.

The language of section 95921(b)(1) through (7) in the currently effective Regulation should remain effective, and the suggested modifications to 95921(b) and (c)(1) through (5) in this 15-day version should not be approved.

* * *

Thank you for this opportunity to comment on the proposed amendments.

Sincerely,

Amy G. Nefouse
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cc: Shawn Bailey
Emily Shults
Katy Wilson