Los Angeles Department of Water & Power

ERIC GARCETTI
Mayor

Commission
MEL LEVINE, *President*
WILLIAM W. FUNDERBURK JR., *Vice President*
JILL BANKS BARAD
MICHAEL F. FLEMING
CHRISTINA E. NOONAN
BARBARA E. MOSCHOS, *Secretary*

RONALD O. NICHOLS
General Manager

February 14, 2014

Dr. Steve Cliff, Chief
Climate Change Program Evaluation Branch
California Air Resources Board
1001 "I" Street
Sacramento, CA 95812

Dear Dr. Cliff:

Subject: Los Angeles Department of Water and Power (LADWP) Comments on California Air Resources Board's (CARB) Potential Amendments to the California Cap on Greenhouse Gas Emissions (GHG) and Market-Based Compliance Mechanisms

The LADWP appreciates the opportunity to submit the following comments on CARB's potential amendments to its cap-and-trade regulation released on January 31, 2014.

1. §95802(140) Definition of First Point of Receipt

LADWP supports CARB's proposed changes which clarify the definition of First Point of Receipt as the generation source specified on the North America Electric Reliability Corporation e-tag. The proposed definition would be consistent with the definition of First Point of Receipt in the Mandatory Reporting Rule (MRR) and as CARB states in its Final Statement of Reasons for the MRR, the revised definition would also result in consistent reporting between 2012 and 2013 compliance years.

2. §95830(c)(1)(I) Registration with CARB

The proposed amendments contain the following new requirement applicable to entities registering with CARB (§95830(c)(1)(I)):

> Names and contact information for all persons employed by the entity ~~in a capacity giving them access to information on compliance instrument transactions or holdings, or involving them in decisions on compliance instrument transactions or holdings~~ who have clearance from the entity to approve, initiate, or review transaction agreements, instruments in the Cap-and-Trade Program or any External GHG ETS linked pursuant to subarticle 12.

111 N. Hope Street, Los Angeles, California 90012-2607 *Mailing address:* Box 51111, Los Angeles, CA 90051-5700
Telephone: (213) 367-4211 www.LADWP.com

It is our understanding that CARB is concerned that individuals with access to potential market-related data would use that information for personal gain. LADWP believes that CARB's concern is already addressed in §95814(a)(3). Per §95814(a)(3), an individual registering as a voluntary associated entity be required to provide a notarized letter from the individual's employer stating that the employer has conflict of interest policies and procedures in place which prevent the employee from using information gained in the course of employment for personal gain in the cap-and-trade program. This requirement would be sufficient deterrent such that a registered individual would not want to use knowledge gained through his/her work as an employee of an entity for personal benefit.

The proposed requirement of §95830(c)(1)(I) to include those individuals that review transaction agreements and compliance instrument information is broad and could include a significant number of employees at a large entity such as LADWP. Implementation of the requirement would be time consuming and very difficult to keep the information updated.

LADWP believes that the name and contact information disclosure requirement should include directors and officers who make decisions authorizing participation in auctions and sale and purchase of compliance instruments and Compliance Instrument Tracking System Services registered users. Thus, LADWP recommends removal of the words "initiate, or review" from §95830(c)(1)(I).

3. §95830(f)(1) and (f)(3) Updating Registration Information

LADWP supports the amendment in §95830(f)(1) which would change the time required to submit updated registration information from 10 working days to 30 calendar days. Since §95830(f)(3) is related to §95830(f)(1), for consistency, LADWP recommends that 95830(f)(3) be amended as follows:

> *"...registration may be revoked or suspended if an entity does not update its registration within ~~10~~ 30 days of a change.*

4. § 95831(a)(6) Annual Allocation Holding Account

CARB proposes to create an annual allocation holding account for an entity that receives a direct allocation to prevent an entity from violating its holding limit with future year vintage allowances that are deposited prior to the compliance year (e.g. to prevent CARB's deposit of an entity's 2015 allowance allocation in its account on October 24, 2014 from leading to a violation of the entity's holding limit). LADWP supports this action as it would be unreasonable for an entity to incur a violation of its holding limit for a regulatory agency deposit of future year allowances.

LADWP also recommends that CARB monitor the holding limit issue closely to determine if it should be increased and/or if other mechanisms should be in place (e.g. allowing entities to surrender compliance instruments at any time) to ensure that the holding limit is not a barrier for an entity's compliance with the cap-and-trade regulation.

5. §95852(b)(4)(B) RPS Adjustment

LADWP appreciates CARB's efforts over the past year to work with electric utility entities to modify the timing with respect to an entity claiming the RPS adjustment such that electric utility entities will not be required to prematurely retire their Renewable Energy Credits (RECs) under the California Energy Commission's Renewable Portfolio Standard (CEC RPS) Program. Although CARB's latest amendment adopted by its Board on October 24, 2013 no longer requires an electric utility to prematurely retire its RECs, LADWP believes that the RPS adjustment credit should be claimed based on REC serial numbers reported under the MRR, rather than retirement of the RECs for the following reasons.

1. Basing the RPS adjustment on REC serial numbers versus retirement would not inadvertently interfere with electric utility entities' implementation of the CEC RPS Program;
2. Basing the RPS adjustment on REC serial numbers would not create swings in demand for compliance instruments due to electric utilities' retirement of RECs related to RPS compliance periods. The cap-and-trade compliance periods do not coincide with the RPS compliance periods.
3. If the RPS adjustment credit is tied to retirement of RECs, it could result in significant increases and decreases in the annual compliance obligation for electric utility entities related to the RPS compliance periods. These swings due to claiming the RPS adjustment credit based on retirement of RECs would not provide an accurate picture of the entity's actual annual compliance obligation.
4. Basing the RPS adjustment on REC serial numbers will keep the RPS adjustment aligned with (e.g. in the same year as) reporting of the imported electricity, and be consistent with the 2011 and 2012 GHG emissions data reports where CARB allowed reporters to claim the RPS adjustment based on REC serial numbers reported under §95111(g)(M) of the MRR.
5. Basing the RPS adjustment on REC serial numbers would enable the RPS adjustment credit to be claimed for *all* eligible imported renewable electricity including imported renewable energy for other programs such as voluntary green power programs (RECs generated from voluntary green power programs are not retired in the CEC RPS accounting system), not just the subset of imported renewable energy used for RPS compliance. Thus, all renewable energy from eligible renewable

generating facilities imported to serve California customers will be treated consistently. If the RPS adjustment credit is tied to retirement of RECs for RPS compliance, green power customers would not be eligible for the RPS adjustment and will not be treated as zero GHG emission under the cap-and-trade regulation.

LADWP proposes the following changes to proposed §95852(b)(4)(B):

The RECs associated with the electricity claimed for the RPS adjustment must be reported and verified pursuant to MRR. ~~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 399.25 and designated as retired for the purpose of compliance with the California RPS program within 45 days of the reporting deadline in section 95103(3) of MRR for the year which the RPS adjustment is claimed.~~

If CARB proceeds with their current approach (tying the RPS adjustment credit to retirement of RECs), the restriction on when RECs can be retired (within 45 days of the reporting deadline in §95103(3) of MRR) should be removed. Per CEC RPS Program rules, RECs may be placed into the retirement subaccount *anytime during the year* but must be retired within 36 months of the month the renewable electricity was generated. For example, a REC generated in January 2013 must be retired by January 2016. The proposed amendment "within 45 days of the reporting deadline in §95103(e) of MRR" is too restrictive – it would allow only RECs retired during the April 15 and July 15 window for the RPS adjustment, but would exclude RECs retired outside of that window (July 16 to December 31 and January 1 to April 14). This amendment does not satisfy the intent of the RPS adjustment which was to offset the compliance obligation for renewable energy that is not directly delivered into California, regardless of when the RECs are retired. All eligible RECs should be recognized for the RPS adjustment, regardless of what time of year they are placed into the retirement subaccount.

In addition, LADWP believes that RECs for renewable electricity imported for voluntary green power programs should also receive credit to offset the cap-and-trade compliance obligation as mentioned previously. By limiting the RPS adjustment credit to only RECs that are retired in the CEC's RPS accounting system, it will create a disincentive to having voluntary green power programs in California because paying the cap-and-trade compliance obligation on imported renewable energy would increase costs to the electric utility and its customers.

LADWP proposes the following alternative language for proposed §95852(b)(4)(B):

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 399.25 and designated as retired for the purpose of compliance with the

> *California RPS program at any time until ~~within~~ 45 days following ~~of~~ the electric power entity reporting deadline in § 95103(e) of MRR during the same year for the year for which the RPS adjustment is claimed. If the RECs were created through voluntary renewable programs, the REC serial numbers must be reported and verified pursuant to MRR.*

6. §95852(b)(4)(A)(2) and §95852(b)(4)(C) RPS Adjustment

There are additional issues related to the RPS adjustment provision that LADWP believes should be addressed to 1) fulfill the original intent of the RPS adjustment provision and 2) recognize renewable electricity imported on behalf of green power program customers.

If the RPS adjustment is intended to neutralize the GHG emissions reported for imported Bucket 2 renewable energy (so that it is treated as zero GHG emission energy under the cap-and-trade program), the credit needs to include both the default GHG emission factor (0.428 MT CO2e/MWh) *and* the 2% transmission loss factor so that the difference between the reported GHG emissions for the imported electricity and the RPS Adjustment credit is equal to zero. Currently, the RPS adjustment gives credit only for the default GHG emission factor but does not provide credit for the 2% transmission loss factor that is applied along with the default GHG emission factor when the imported Bucket 2 renewable energy is reported under the MRR. The result is a 2% deficit in the RPS adjustment credit such that the credit does not completely cover the reported GHG emissions for the imported Bucket 2 renewable energy. The consequence of not including credit for the 2% default transmission loss factor in the RPS adjustment is assigning cap-and-trade compliance costs to renewable energy for default GHG emissions that are not real.

To provide full credit for renewable energy, LADWP proposed the following revision to §95852(b)(4)(C)

> *The quantity of emissions included in the RPS adjustment is calculated pursuant to MRR as the product of the default emission factor for unspecified sources, the transmission loss correction factor for unspecified sources, and the reported electricity generated (MWh) that meets the requirements of this section, 95852(b)(4).*

The original intent of the "contract to import electricity on behalf or" provision in §95852(b)(4)(A)(2) was to recognize transmission services agreements where renewable electricity is imported by Entity #1 on behalf of Entity #2 who owns the renewable electricity and the RECs. Transmission services agreements do not transfer ownership of the electricity and RECs to the importer, only have temporary custody of the electricity. The amended language in 95852(b)(4)(A)(2) no longer captures this intent.

In addition, an electric utility may procure and import renewable energy on behalf of its green power customers, who are not "entities subject to the California RPS."

Thus, LADWP proposes the following language for §95852(b)(4)(A)(2):

> *A contract to ~~procure~~ import electricity ~~and the associated RECs~~ on behalf of an entity subject to the California RPS that has ownership or contract rights to the electricity and associated RECs generated by the eligible renewable energy resource, as verified pursuant to MRR or a contract to procure electricity generated by an eligible renewable energy resource and the associated RECs on behalf of California electric utility customers that participate in voluntary green energy programs as verified pursuant to MRR..*

7. §95856(h) Compliance Instrument Retirement Order – Potential Conflict with §95892(d)(5)

Under §95892(d)(5), Electrical Distribution Utilities (EDUs) are prohibited from using the value of their allocated allowances to meet compliance obligations that do not benefit its retail ratepayers consistent with the goals of AB 32, including the use of such allowances for electricity sold into the California Independent System Operator markets. CARB proposes to surrender compliance instruments from entity compliance accounts in the following manner: offsets (oldest vintage first), allowances purchased from the Allowance Price Containment Reserve (Reserve), allowances (oldest vintage first), then true-up allowances. Although an EDU would be in compliance with §95892(d)(5) with respect to its procurement of allowances, this surrender proposal could have the unintended effect of appearing to conflict with §95856(h). Thus, although the EDU's and CARB's compliance account balance would be the same in terms of the number of allowances, the EDUs' accounting of allowances by vintage and date procured may not match CARB's. Please see attached example for additional information.

To remedy this potential conflict, LADWP recommends the following provision be added:

> *§95856(h)(4): Notwithstanding §95856(h)(1) and (2), an electrical distribution utility will not be in violation of §95892(d)(5) when the Executive Office retires compliance instruments, provided that the electrical distribution utility has a quantity of compliance instruments not allocated to it pursuant to §95870(d) in its compliance account that is at least equal to its compliance obligation for any transactions for which the use of allocated allowance value is prohibited under §95892(d)(5).*

This will ensure that EDUs will not be penalized for differences in accounting for allowances but which result in the same compliance instrument amount balance due to manner in which they were surrendered.

LADWP believes that the best solution to this issue would be for CARB to allow entities to select which compliance instruments to retire by establishing an interactive application such as EPA's Acid Rain Program Clean Air Markets Division Business System (CBS). The CBS has been a user-friendly interactive application that allows covered entities to designate which SO2 allowances to retire first but as a default, EPA retires the SO2 allowances in a specified manner if the entities do not make the designation. Although covered entities under CARB's cap-and-trade regulation would not have access to compliance instrument serial numbers, if an application similar to EPA's were created, entities could designate instruments for retirement by vintage, compliance instrument type, and purchase date of compliance instruments.

8. §95856(h) Annual and Triennial Compliance Instrument Requirements/Compliance Instrument Retirement Order

CARB is proposing to retire compliance instruments from an entity's compliance account on an annual and triennial basis. On an annual basis, CARB would retire 30 percent of a covered entity's compliance instruments correlated to its compliance obligation reported from the previous data year that received a positive or qualified positive emissions data verification statement, or were assigned emissions pursuant to §95131 of MRR. While this amendment would alleviate potential violation of an entity's holding limit, LADWP recommends that entities be provided the opportunity to request retirement of a larger percentage of its compliance instruments. See discussion above regarding LADWP's recommendation that a system be developed such that entities can designate which compliance instruments to retire to fulfill its compliance obligation.

CARB requests comment on whether or not there should be an eight (8) percent offset usage limit on the annual surrender event. LADWP is not opposed to such a limit under the condition that CARB only retires offsets in an entity's compliance account equal to its 8 percent limit and if that entity holds more than the 8 percent limit in their compliance account, it does not incur a violation of the 8 percent usage limit. The entity with offset holdings in excess of the 8 percent usage limit should be able to use those offsets for compliance in future years. As LADWP stated previously, the best solution to this issue would be for CARB to allow entities to select which compliance instruments to retire.

9. §95912(d)(4)(E) Auction Attestation

In the September 4, 2013 45-day changes, CARB proposed to establish a new condition for participating in an auction. Specifically, the proposed amendment would have required an entity to attest that that it "has not been subject to any previous or

ongoing investigation with respect to any alleged violation of any rule, regulation, or law associated with any commodity, securities, or financial market, including a change in the status of an ongoing investigation." This amendment would have changed the provision from a disclosure requirement to an attestation requirement. This would have been a significant change in the rules for participating in an auction and this new requirement could unnecessarily bar many entities from participating in the auction. The fact that there was an investigation would be sufficient to disqualify an entity even if that investigation determined the alleged violations totally lacked merit.

The January 2014 proposed language now consists of an attestation "disclosing the existence and 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, or financial market for the entity participating in the auction…"

The requirement is broadly written, does not have a materiality or knowledge qualifier and covers alleged violations. It would be very difficult to nearly impossible for LADWP to obtain the information over the time period specified, especially if the investigation did not result in an actual violation. Also, in §95912(d)(5), any change, even though the change results in a determination of no violation, to an entity's auction application information could result in the entity being denied auction participation. LADWP believes that the proposed revision would unnecessarily disqualify entities from participating in an auction.

Thus, LADWP urges CARB to further limit the scope of the attestation to previous investigations in which a violation was determined. LADWP recommends that §95912(d)(4)(E) be amended to read as follows:

> *An attestation disclosing investigations that have occurred within the last ten years which resulted in violations of any rule, regulation, or law associated with any commodity, securities, or financial market for the entity participating in the auction, and all other entities with whom the entity has a corporate association, direct corporate association, or indirect corporation association pursuant to §958333.*

10. §95912(d)(5) Auction Administration and Participant Application

CARB is proposing the following amendment to its new provision, §95912(d)(5), as noted in double strikeout format:

> *An entity with any changes to the auction application information listed in subsection 95912(d)(4)* ~~*or account application information listed in section 95830*~~ *within 30 days prior to an auction, or an entity whose auction application information or account*

application information listed in § 95830 will change 15 days after an auction, will be denied participation in the auction.

LADWP supports CARB's narrowing of what constitute "changes" to the auction application information such that any changes in an entity's auction or account application does not result in denial of the entity's ability to participate in the auction. However, LADWP believes that inclusion of the requirement that changes to auction application information that will occur 15 days after an auction could result in denial of the entity's participation in the auction would lead to unnecessary administrative burden. Fifteen days after an auction, the entity would have already submitted its bid guarantee, participated in the auction, and in the case of a purchase of allowances, gone through the administrative task of ensuring that the required funds were transferred to CARB in a timely manner. An entity should not be denied participation in an auction due to changes that will occur 15 days after an auction.

LADWP recommends the following changes:

An entity with any changes to the auction application information listed in subsection 95921(d)(4) within 30 days prior to an auction~~, or an entity whose auction application or account application information listed in section 95830 will change 15 days after an auction~~ may be denied participation in the auction.

11. §95923. Disclosure of Cap-and-Trade Consultants and Advisors

The proposed amendments now require disclosure of cap-and-trade consultants and advisors that provide services listed in § 95979(b)(2) of the cap-and-trade regulation or § 95133(b)(2) of the MRR. Although § 95979 is related to conflict of interest requirements for verification bodies and offset verifiers for verification of offset project data reports, the proposed reference to 95979(b)(2) in § 95923 would require an entity to disclose cap-and-trade advisors and consultants that have provided *non-offset verification services over the past five years* and there is a list of *twenty* non-offset verification services that would apply. Per this proposed definition, this could include attorneys and consultants who provide services unrelated to the cap-and-trade program. The provision should only apply to consultants and advisors who are aware of an entity's compliance instrument position or strategy with respect to procurement or sale of compliance instruments.

LADWP recommends that the amendments be clarified as follows:

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 providing the types of services in relation to the registered entity's Cap-and-Trade Program market

position or strategy in § 95979(b)(2) of the Cap-and-Trade Regulation or §95133(b)(2) of the Mandatory Reporting Regulation specifically for the entity registered in the Cap-and-Trade Program.

12. Conclusion

LADWP appreciates this opportunity to comment and looks forward to working with CARB staff on these important issues. If you have any questions or require additional information, please contact me at (213) 367-0403 or Ms. Jodean Giese at (213) 367-0409.

Sincerely,

DCMark for

Mark J. Sedlacek
Director of Environment and Efficiency

JG:lu
Enclosure
c: Dr. Steve Cliff, CARB
Ms. Rajinder Sahota, CARB
Mr. Jakub Zielkeiwicz, CARB
Mr. Sean Donovan, CARB
Dr. Ray Olsson, CARB
Mr. Mark J. Sedlacek
Ms. Jodean M. Giese

California Air Resources Board (ARB) Greenhouse Gas (GHG) Cap-and-Trade Regulation
Proposed § 95856(h) Compliance Instrument Retirement Order
Example of Potential Impact to Publicly-Owned Utilities (POUs)

Background

CARB's current proposal does not allow entities to specify a retirement order of compliance instruments such as allowances and offsets. ARB is proposing to retire an entity's compliance instruments in its compliance account in the following order:

1. Offset credits
2. Allowances purchased from an Allowance Price Containment Reserve sale
3. Allowances per section 95820(a) and 95821(a), earlier vintage allowances retired first
4. Current calendar year's vintage allowances and allowances allocated just before the triennial surrender deadline up to the true-up allowance amount (for industrial sector)

This proposed surrender order, if adopted, will conflict with Section 95892(d)(5) which applies to electrical distribution utilities (EDUs). EDUs are prohibited from using the value of their directly-allocated allowances to meet compliance obligations that do not benefit its retail ratepayers consistent with the goals of AB 32, including the use of such allowances for electricity sold into the CAISO markets. Emissions associated with these energy sales must be covered by compliance instruments purchased at auction or the secondary market. This provision especially impacts POUs who may have specified that most, or all, of its allocated allowances be put into its compliance account.

The following is an example that shows the conflict between the two provisions.

POU Entity 2013 allocation = 5 MMT
POU Specified Distribution of allocation = 5 MMT to compliance account (specified to ARB on Sept. 1, 2012)
POU 2014 allocation = 4.8 MMT
POU specified distribution of allocation = 4.5 MMT to compliance account (specified to ARB on Sept. 1, 2013); .3 MMT to auction

2013 Compliance Year Activity

POU emissions = 4.5 MMT (4.0 MMT allocated toward AB 32 goals, .5 MMT allocated to sales to CAISO). POU purchased .5 MMT to cover sales to CAISO.

2014 Compliance Year Activity

POU emissions = 4.5 MMT (4.0 MMT allocated toward AB 32 goals, .5 MMT allocated to sales to CAISO)

ARB implementation of the surrender order proposal:
For 2013 and 2014 "triennial" surrender:
Amounts needed for surrender:
2013: 4.5 MMT
2014: 4.5 MMT

How POUs Should Surrender Allowances Per §95892(d)(5) (Allowance Values in MMT)				
	2013		2014	
	Directly-Allocated Allowances	Purchased Allowances	Directly-Allocated Allowances	Purchased Allowances
Direct Allocation	5.0		5.0	
Allowance Purchases		0.5		0.5
Surrender for Native Load Emissions	-4.0	0.0	-4.0	0.0
Surrender for Wholesale Emissions	0.0	-0.5	0.0	-0.5
Allowances Remaining	1.0	0.0	1.0	0.0

CARB's Triennial Surrender Proposal (Allowance Values in MMT)				
	2013		2014	
	Directly-Allocated Allowances	Purchased Allowances	Directly-Allocated Allowances	Purchased Allowances
Direct Allocation	5.0		5.0	
Allowance Purchases		0.5		0.5
Surrender for Total Emissions (Native Load + Wholesale)	-4.5	0.0	-4.5	0.0
Allowances Remaining	0.5	0.5	0.5	0.5

Although ARB and the POU compliance balances are the same in this instance, ARB surrenders the allocated allowances to cover the emissions associated with the CAISO sales. LADWP desires confirmation that ARB recognizes this difference in accounting of allowances and will not penalize the POU before it finalizes its compliance instrument surrender proposal.