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Via Electronic Submission:
http://www.arb.ca.gov/lispub/comm2/bcsubform.php?listname=2013investmentpln-ws&comm_period=1

March 8, 2013

Hon. Mary D. Nichols, Chairman
California Air Resources Board
1001 "I" Street
Sacramento, CA 95814

Subject: PE-Berkeley, Inc.'s Comments Regarding the Public Workshop on the Development of the Cap-and-Trade Auction Proceeds Investment Plan and the Cap-and-Trade Auction Proceeds Investment Plan Draft Concept Paper

Dear Madame Chairman:

PE-Berkeley, Inc. (hereinafter, "PEB"), a 22.47 megawatt ("MW") cogeneration power plant located in Berkeley, California, and Olympus Power, LLC, the asset manager of PEB, appreciate the opportunity to provide these comments regarding the California Air Resources Board's ("CARB" or the "Board") February 25, 2013 public workshop regarding the development of the Cap-and-Trade Auction Proceeds Investment Plan ("Auction Workshop") and the Cap-and-Trade Auction Proceeds Investment Plan Draft Concept Paper ("Draft Concept Paper").[1] The Auction Workshop and Draft Concept Paper represent important steps in CARB's implementation of the Cap-and-Trade Regulation ("Regulation") pursuant to the Global Warming Solutions Act of 2006 ("AB 32").

I. Introduction

The Auction Workshop highlighted the challenges that CARB faces as it drafts the Auction Proceeds Investment Plan. CARB must not only balance the competing interests of multiple stakeholders for the allocation of scarce auction proceeds, but the Board must also adhere to the statutory directives of AB 1532,[2] SB 535,[3] and AB 32. Indeed, as the

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[1] *Available at*: http://www.arb.ca.gov/cc/capandtrade/auctionproceeds/workshops/concept_paper.pdf.

[2] AB 1532, the Greenhouse Gas Reduction Fund Investment Plan and Communities Revitalization Act, circumscribes CARB's use of auction revenues for greenhouse gas ("GHG") mitigation projects and requires multiple agencies, including CARB, to develop an auction revenue investment plan consistent with AB 1532's project eligibility criteria.

Legislative Analyst's Office ("LAO") has indicated, allowance auction revenue must be spent consistent with the purposes of AB 32 to avoid running afoul of the constitutional limitations presented by Proposition 13.[4]

It is undoubtedly a challenge to mitigate GHG emissions, satisfy multiple constituencies, make investments that achieve quick benefits, and stay within the bounds of AB 32. However, PEB submits that investment in combined heat and power ("CHP") resources—including a temporary allocation of auction revenue for existing CHP facilities subject to long-term, fixed-price contracts—satisfies all of these criteria. Accordingly, PEB requests that a portion of CARB's allowance auction revenue be distributed on a case-by-case basis to CHP facilities, such as PEB, subject to fixed-price contracts where there is a risk of backsliding on CARB's air pollution goals if auction revenue is not provided to such facilities. In making such a request, however, PEB does not seek in any way to profit from the receipt of such funds, but to simply be made whole for these unrecoverable costs.

II. Background

PEB supplies thermal energy (i.e., heat in the form of steam) to the University of California-Berkeley ("UC-Berkeley") and electric power to Pacific Gas & Electric Company ("PG&E") under separately memorialized long-term agreements. PEB entered into the contract with UC-Berkeley in 1987, nearly two decades before the California Legislature passed AB 32 and, consequently, well before the State ever contemplated the regulation and abatement of GHG emissions. Therefore, PEB's contract with UC-Berkeley does not provide for the pass-through of GHG costs associated with compliance with the Regulation, despite the fact that UC-Berkeley is the end user of PEB's steam and in the best position to reduce its energy use and resultant GHG emissions.

PEB's contract with UC-Berkeley does not expire until 2017. While the Board directed CARB staff to "develop a methodology that provides transition assistance to covered entities that have a compliance obligation cost that cannot be reasonably recovered due to a legacy contract" and to "return to the Board with proposed regulatory amendments in mid-2013,"[5] it now appears that CARB will not adopt the necessary amendments to the Regulation to address this issue until mid-2014. Given this likely timing, PEB could very well not receive any regulatory relief by the November 1, 2014

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[3] SB 535 requires that the AB 1532 investment plan allocate at least 25% of the CARB auction revenues to provide benefits to disadvantaged communities and at least 10% to fund projects located within disadvantaged communities.

[4] *See* LAO, "The 2012-13 Budget: Cap-and-Trade Auction Revenues", at 4 (Feb. 16, 2012) (stating that "[b]ased on an opinion that we received from Legislative Counsel, the revenues generated from ARB's cap-and-trade auctions would constitute 'mitigation fee' revenues . . . in order for their use to be valid as mitigation fees, revenues from the cap-and-trade auctions must be used only to mitigate GHG emissions or the harms caused by GHG emissions" in order to accord with the limitations of Proposition 13 and associated case law); *see also Sinclair Paint Co. v. State Bd. of Equalization*, 15 Cal. 4th 866 (1997).

[5] CARB, Board Resolution 12-33, at 3 (Sep. 20, 2012).

deadline for PEB to submit its annual compliance obligation to CARB.[6] Thus, until the Regulation is amended to fully address legacy contracts, it is entirely appropriate for CARB to provide transition assistance in the form of allowance auction revenue to CHP facilities such as PEB on a case-by-case basis.

III. CARB Should Provide Interim Relief To CHP Facilities Subject To Legacy Contracts On A Case-By-Case Basis

There are several reasons why providing auction revenue to CHP facilities subject to legacy contracts is lawful and, moreover, good policy.

First, providing auction revenue to CHP facilities on a case-by-case basis is consistent with AB 32. As the Draft Concept Paper states, "[t]he investment of the cap-and-trade auction proceeds provides both the opportunity and the responsibility to spend them well to further the objectives of AB 32."[7] One of the objectives of AB 32 is that CARB must "[e]nsure that activities undertaken pursuant to the [Regulation] complement, and do not interfere with, efforts to achieve and maintain federal and state ambient air quality standards and to reduce toxic air contaminant emissions."[8]

In this case, if it does not receive transitional relief for these unrecoverable costs, PEB may have to permanently shut down. If PEB were to close, UC-Berkeley would, in the short-term, be forced to use its old, inefficient boilers for steam and, potentially, its fleet of diesel-fired emergency generators for electricity, depending on load constraints in the event PEB no longer provides electricity to the Berkeley load pocket.[9] UC-Berkeley's boilers and emergency generators entail much higher rates of GHG, criteria pollutant, and air toxics emissions than PEB.[10] In the long-term, there is no clear local alternative for UC-Berkeley's energy needs, given transmission constraints. Therefore, because the likely alternatives for supplying energy to UC-Berkeley may entail higher emissions than PEB, the

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[6] *See* Tit. 17, Cal. Code Regs. §§ 95855, 95856(a), (d). A covered entity's annual compliance obligation equals 30% of emissions with a compliance obligation reported from the previous data year. A covered entity must surrender its annual compliance obligation by November 1st of the calendar year following the year for which the emissions were reported and the obligation calculated. Accordingly, PEB must surrender allowances equivalent to 30% of its 2013 emissions by November 1, 2014.

[7] Draft Concept Paper, at 1.

[8] Health & Safety Code § 38562(b)(4).

[9] *See* Bay Area Air Quality Management District, Major Facility Review Permit for PEB, Condition 1(c) (Apr. 17, 2012) (stating that, if either "Source 40, Gas Turbine, or Source 41, Duct burner malfunctions and the cogeneration system can not meet the 120,000 lb/hr steam rate, then the existing boilers may fire only to the extent necessary to satisfy the campus steam demands"); *see also* Bay Area Air Quality Management District, Synthetic Minor Application Evaluation Report for UC-Berkeley, at 2, (indicating that UC-Berkeley is permitted to operate three boilers, 36 diesel-fired generators, and seven natural gas-fired generators).

[10] For instance, diesel-fired generators emit air toxics, such as benzene, at relatively high rates. PEB is fired primarily on natural gas, which produces such air toxics emissions at very low rates.

failure of CARB to provide transitional relief to PEB risks backsliding on the clear directive of AB 32 to ensure that GHG regulation does not come at the cost of increasing criteria pollutant and air toxic emissions.

Second, providing auction revenue to CHP facilities subject to legacy contracts fits neatly within the investment principles presented in the Draft Concept Paper. In particular, providing such interim relief to facilities like PEB is aligned with Draft Investment Principle #1 (further AB 32 purposes) and #3 (prioritize funding for the highest GHG emissions sectors, e.g., the electricity sector).[11] PEB believes it is appropriate for CARB to expand Draft Investment Principle #2 to include, not only projects that achieve additional GHG emissions reductions, but projects that avoid GHG emissions backsliding. For instance, if PEB were to close, UC-Berkeley very well may be forced to rely on higher GHG-emitting resources to satisfy its energy needs. CARB should prevent such scenarios from unfolding because they would undermine the GHG emissions reductions achieved elsewhere under the cap-and-trade program.

Finally, providing auction revenue on an interim basis to stranded CHP facilities is consistent with California's larger energy and environmental policy goals. CHP is more efficient than separate electricity generation and heat production, resulting in reductions in fuel use and GHG emissions.[12] As a consequence, CARB's Climate Change Scoping Plan relies on CHP for reducing 6.7 million tons of GHGs (CO_2 equivalent basis) and recommends constructing 4,000 MW of additional CHP.[13] Indeed, it is "the policy of the state to encourage and support the development of cogeneration as an efficient, environmentally beneficial, competitive energy resource."[14] Accordingly, CARB should assist, not strand, existing CHP as being an important part of meeting California's climate, energy, and environmental goals.[15]

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11 Draft Concept Paper, at 15.

12 *See* PEB, Comments Regarding California's Use of Auction Proceeds from Cap-and-Trade Program to Reduce Greenhouse Gas Emissions, at 1-3 (June 22, 2012) (explaining benefits of CHP).

13 CARB, Climate Change Scoping Plan, at 44 (Dec. 2008).

14 Pub. Utilities Code § 372(a).

15 On this point, PEB would note that providing auction revenue to existing CHP subject to legacy contracts accords with the statutory investment criteria outlined in AB 1532. AB 1532 states that, "[m]oneys appropriated from the [GHG reduction] fund may be allocated . . . for the purpose of reducing [GHG] emissions in this state through investments that may include, but are not limited to . . . [f]unding to reduce greenhouse gas emissions through energy efficiency, clean and renewable energy generation, distributed renewable energy generation, transmission and storage, and other related actions, including, but not limited to, at public universities, state and local public buildings, and industrial and manufacturing facilities." Health & Safety Code § 39712(c)(1). PEB fits within these parameters because it is a clean energy generation resource and assisting the facility in this regard will ensure that efficient CHP is not replaced by higher GHG-emitting system electricity and separate heating (e.g., boilers).

IV. Conclusion

CHP is an integral part of reaching AB 32's benchmark of reducing statewide GHG emissions to 1990 levels by 2020. However, CHP facilities subject to legacy contracts face enormous unrecoverable costs due to the Regulation with no corresponding benefit in terms of GHG emissions reductions, due to the end user of the energy not experiencing any change in energy costs. Further, if a stranded CHP facility is closed and replaced by separate system electricity and heat resources (e.g., boilers), GHG emissions could increase. Accordingly, PEB recommends that CARB analyze and provide auction revenue to existing CHP facilities such as PEB, taking into account (i) when the legacy contract was entered into, (ii) when the legacy contract's term expires, (iii) the GHG, criteria pollutant, and air toxics emissions of the facility compared to the likely energy resources that would replace the CHP facility, and (iv) any other co-benefits the existing CHP facility provides. As such, CARB should provide interim relief to PEB, until such time as the Regulation is amended to fully address this issue, because (i) PEB entered into its contract well before the Regulation was contemplated, (ii) the contract expires after PEB's first annual compliance obligation, (iii) PEB's air emissions are lower than the likely alternatives for UC-Berkeley and the Berkeley load pocket, and (iv) PEB provides essential co-benefits, such as black start capability, whereby it can operate independently from the electricity grid to supply electricity and steam during a blackout.

We look forward to our continued efforts with CARB to resolve this important issue in a timely manner.

Respectfully submitted,

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cc: George Haley, Esq., Counsel to P.E. Berkeley, Inc.
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