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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 January 31, 2014.

Overbroad Disclosure of Employees and Contractors

At 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 that are held 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 who have clearance from the entity to approve, initiate, or review transaction agreements, transfer requests, or account balances . . . " could be read to include employees that perform solely administrative contract management functions focused on ensuring agreements are commercially consistent in terms and conditions. These employees do not negotiate contract terms, initiate the underlying commercial arrangement covered by the contract, or possess any insight into a covered entity's carbon position. 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 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]

[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.

> 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.

Control of an Account

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:

> If the PAR or the AAR of a covered entity is responsible for managing the compliance strategy of multiple covered entities and has clearance to approve, approve, initiate, or review transaction agreements or transfer requests in the tracking system accounts of multiple covered entities ~~will have control of the account in the tracking system of another covered entity with which it does not have a direct corporate association~~, the entities will be considered to have a direct corporate association and the requirements in 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 from language introduced in the last comment period to address the annual surrender obligation versus an "evaluation" of an entity's holdings in its Compliance Account, and provides for an order in which instruments are to be retired. Subsection 95856(h)(1)(A) specifies that offset credits will be retired first, without consideration of the quantitative usage limit. Staff further requests input from stakeholders as to whether the 8% offset usage limit should apply to the annual surrender of compliance instruments.

SGEN believes that ARB should use the method originally proposed in the 'Proposed Regulation Order', posted on September 4, 2013, in which ARB would "determine compliance with the annual compliance obligation by evaluating the number and type of compliance instruments in the Compliance Account." Furthermore, in "evaluating" annual compliance, ARB should not apply an 8% offset usage limit on the instruments in an entity's Compliance Account. Such a limit should only apply to the Triennial Compliance Obligation.

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. Accordingly, any changes must be consistent with retention of the 8% offset limit only at the Triennial Compliance Obligation surrender stage.

In addition, currently an entity has only two options for instrument placement: 1) in the Holding Account where the instruments count against the holding limit, and 2) in the Compliance Account where all instruments are subject to retirement and in which the entity does not have the option to choose the order in which its instruments are to be retired. However, entities participating in the Program should be able to manage the retirement of their inventory to allow for internal valuation and accounting considerations, and have the flexibility to specify the instruments that will be retired by ARB or have the instruments retired by the default method if not otherwise specified. Thus, ARB should modify sections 95856(h)(1)(A) and (h)(2)(A) (or

CITSS if possible) and work with Program participants to implement a process that would allow entities to provide written instructions to the Executive Officer a minimum of five (5) days prior to the surrender due date, specifying the vintage and type of instruments that are to be retired and in which order.

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, or financial market with respect to the entity participating in the action and all other entities with whom the entity has a corporate association, direct corporate association, or indirect corporate association.

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 part of large corporations with corporate structures that involve dozens or even hundreds of affiliates and subsidiaries which operate largely independently from one another, but which are required by the Regulations to be identified as corporate associations. However, 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. Additionally, many or most of the corporate entities in question may not be registered in the Program, subject to the Regulations or within the jurisdiction of ARB, 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).

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, or financial market.

"Known" Changes to an Auction Application

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), or account application information listed in 95830 within 30 days prior to an

auction, or an entity whose auction application information listed in section 95830 will change within 15 days after an auction."

A Program participant can take many steps and perform extensive due diligence to ensure that it has informed ARB of any changes to its direct and indirect corporate associations prior to the auction. However, given the complexities that exist in large corporations, as previously noted, it is often impossible for the entity that is registered to participate in an auction to discover the existence of a change in a corporate association that may occur within 15 days after an auction, or if any change is even contemplated. The Regulations should recognize that the existing definition of "corporate association" is not consistent with the real life workings of many large corporate organizations. 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, especially when the information pertains to corporate entities that do not participate in the Program and are outside of ARB jurisdiction.

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 that is aware of any changes to the auction application information listed in subsection 95912(d)(4) within 30 days prior to an auction, or an entity whose auction information listed in section 95830 will change within 15 days after an auction, must report those changes to ARB within 30 business days of being notified of the change(s), or the entity may be denied participation in the auction.

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

SGEN agrees that the term "Cap-and-Trade Consultant or 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 Mandatory Reporting Regulation are to be considered duties that would classify someone as a 'Cap-and-Trade Consultant or 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 'Cap-and-Trade Consultant or Advisor' is overly broad and does not provide the clarity needed regarding the functions performed by a 'Cap-and-Trade Consultant or 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 'Cap-and-Trade Consultant or 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 clarify that 'publication services' do not constitute an advisory role, but the panoply of duties listed go well above and beyond those that should classify one as a 'Cap-and-Trade Consultant or 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.

Requirement to Inform ARB of an Advisor

Section 95914(c)(3) has been further amended to include 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 suggests that ARB expand who at an entity is allowed to provide such attestation, and permit the Alternate Account Representative *or* the Director or Officer who is responsible for the conduct of the entity to submit the attestation, in addition to the Primary Account Representative. Therefore, section 95914(c)(3)(C) should be revised to state as follows:

> Any entity that has retained the services of a Consultant or Advisor must inform ARB of the advisor's retention, and identify the Consultant or Advisor's, employer and contact information, and provide an attestation by the Primary Account Representative, the Alternate Account Representative, or Director or Officer who is responsible for the conduct of the entity of the entity retaining the Consultant or Advisor of the completeness of the disclosure;

Requirement to Inform ARB of a Client

Sections 95914(c)(3)(D) and (E) 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 specifies this information be "physically received by the Executive Officer at least 15 days prior to an auction."

This requirement is overly burdensome to those that provide "Cap-and-Trade Consultant or Advisor" services, and unnecessary because it is duplicative of the information disclosure requirements imposed on entities under sections 95914(c)(3)(C), and 95923(b) and (c). For example, as discussed above, proposed section 95914(c)(3)(C) already specifies that "*Any entity* that has retained the services of an advisor must inform ARB of the advisor's retention," therefore, there should be no gap in notification of an advisor-client relationship to ARB. Sections 95914(c)(3)(D) and (E) 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(b) are unnecessary and overly burdensome. These proposed amendments 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 to 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.

Further amendments have been proposed to section 95921(f)(1)(B) to clarify that an entity cannot acquire allowances and hold them in its own holding account on behalf of another entity, unless the holding is pursuant to an agreement in which both parties agree to provisions specifying a date to deliver a specified quantity of compliance instruments, or specifying a procedure to determine a quantity of compliance instruments for delivery and/or a delivery date. This proposed language is consistent with Staff's assertion that forward contracts are not to be considered a transaction done "on behalf of" another entity, and is necessary to allow for legitimate transactions between Program participants.

While SGEN supports the amendment to 95921(f)(1)(B), we encourage ARB to further evaluate the possible impact of language in the proposed Regulations addressing 'Conduct of Trades' and the 'General Prohibitions on Trading.' With the prohibition on beneficial holding, continuous pressure to eliminate any possibility of an entity acting "on behalf of" another entity without being considered a corporate association, as well as other proposed prohibitions on transactions occurring outside of an auction, ARB risks eliminating lawful and justifiable transactions that currently market participants commonly enter into, which support the Program and creates liquidity in the secondary market. The proposed amendments to section 95921(b) should be removed from consideration at this time to allow for ARB to work with market participants to determine what information would be most useful to ARB, what information is already readily available to ARB, and what information can continue to be obtained through ARB's current information request provisions in the Regulations, instead of implementation of requirements that put an entity at risk of inadvertent non-compliance with the Regulations due to the limited timeframes inherent with these transactions and burdensome and confusing data entry requirements. Additionally, SGEN proposes ARB reconsider amendments to the Regulations in section 95921 generally, which are overbroad and detrimental to the secondary market.

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

Sincerely,

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cc: Shawn Bailey
Emily Shults
Katy Wilson