



**Pacific Gas and
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ARB's Cap-and-Trade Website

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California Air Resources Board
1001 I Street
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Re: Pacific Gas and Electric Company's Comments on the Air Resources Board Draft 15-day Amendments to the Cap-and-Trade Program

Dear Dr. Cliff:

Pacific Gas and Electric Company (PG&E) welcomes the opportunity to submit these comments on the Air Resources Board's (ARB) 15-day draft amendments to the cap-and-trade program.

I. INTRODUCTION

PG&E's comments on the staff proposals are detailed in Section II below. The following summarizes the key issues:

- Changes to Section 95852.2(b)(4) Should Not Become Effective Until January 1, 2015
- ARB Should Not Unreasonably Restrict an Entity's Auction Participation
- Generators That Have Already Bargained For Costs Associated With GHG Regulation Should Not Qualify for Transition Assistance
- Investigation Disclosure Language Should be Modified
- ARB Should Not Include Burdensome Staff Reporting Requirements
- Exemptions Should Be Tied to GHG Reduction Performance
- PG&E Supports The Adoption Of Additional Protocols
- PG&E Recommends Minor Clean-up Language

II. DISCUSSION

A. Section 95852.2. Changes to Section 95852.2(b)(4) Should Not Become Effective Until January 1, 2015

The proposed amendments to Section 95852.2(b)(4) further restrict which emissions are eligible for a compliance obligation exemption under the cap-and-trade program and suggest that vented emissions from underground storage facilities will now count towards the inclusion threshold. To

avoid retroactive rulemaking, PG&E proposes that this change not take effect until January 1, 2015:

95852.2(b)(4) Effective January 1, 2015, vented and fugitive emissions reported under sections ~~95153-2 (e) and (i)~~ of MRR by local distribution companies that report under section 95122 of MRR...

B. Sections 95912 and 95830. ARB Should Not Unreasonably Restrict an Entity's Auction Participation

While PG&E appreciates the changes to Section 95912(d)(5), the language contained in the 15-day discussion draft could still bar an entity from participating in an auction if there are changes to information provided in an entity's auction or account application 30 days before or 15 days after an auction. While this restriction may pose a challenge for any compliance entity, large compliance entities are especially impacted by this provision due to the size and complexity of their business operations. The activities described in the auction or account application cover a range of activities that a company may need to perform in the course of its business and simply cannot remain static, including officer names, capital structure, staff composition, the opening of or changes to an investigation, etc.

While ARB staff acknowledges that Section 95912(d) is intended to facilitate effective settlement of the auctions and support market monitoring the language included in the discussion draft encompasses a far wider array of information additional to what is required to meet ARB's objective. Section 95912(d) should be further tailored to meet ARB's needs without jeopardizing an entity's auction participation for activities associated with its normal business operations or outside of its control. PG&E proposes that Section 95912(d)(5) be revised as follows:

An entity with any changes to the auction application information listed in subsection 95912(d)(4)(A) or (F) 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 section 95830(e)(1)(a) will change within 15 days after an auction, may be denied participation in the auction.

Additionally, Section 95830(f)(3) should be modified to ensure consistency with other deadlines included in the cap-and-trade regulation, including the other registration requirements contained in 95830(f)(1):

~~95830(f)(3) Pursuant to section 95921(g)(3), registration may be revoked, or suspended, or restricted if an entity does not update its registration within 10-30 days of a change pursuant to section 95921(g)(3).~~

As currently drafted, Section 95912(g) would directly conflict with the proposed changes to Section 95914(c)(2)(D), which allows for the disclosure of auction information to regulatory agencies. PG&E suggests a minor edit to harmonize these two provisions. Section 95912(d) also places an unreasonable constraint on "Cap-and-Trade Consultants or Advisors," barring them from communicating any auction-related information for ten years. PG&E also suggests that Section 95912 (g) be revised to limit such communications to two years.

95912(fg) An entity approved for auction participation Individuals and entities registered in the tracking system, entities that have a direct or indirect corporate association with a registered entity pursuant to section 95833, and entities and individuals that have qualified as Cap-and-Trade Consultants or Advisors pursuant to section 95923 in the last ~~two~~ years may not communicate any information on auction participation outlined in section 95914(c) with any entity that is not part of an association disclosed pursuant to section 95914, except as permitted by section 95914 (c)(2) or as requested by the Auction Administrator to remediate an auction application.

C. Sections 95802 and 95894. Generators That Have Already Bargained For Costs Associated With GHG Regulation Should Not Qualify for Transition Assistance

The amended regulation inappropriately provides a free allocation of allowances to generators that: (1) had notice of the potential for future greenhouse gas (GHG) costs; and (2) bargained for the costs associated with cap-and-trade compliance in their contracts. PG&E therefore opposes ARB's proposed "legacy contract" definition to the extent that it would provide a windfall by allocating allowances to generators after the generator has already been and continues to be compensated by PG&E customers. PG&E proposes simple revisions to the definition of "legacy contract" to ensure that generators that were aware of and agreed to assume responsibility for GHG compliance costs bear those costs.

1. Only Contracts Executed Before August 15, 2005, Should be Considered Legacy Contracts

ARB should amend the date before which an executed contract qualifies as a legacy contract from September 2006 to August 15, 2005, because amendments to Assembly Bill (AB) 32 as of August 15, 2005, included broad limits on GHG emissions. The basis for the use of August 15, 2005, is also consistent with California Public Utilities Commission (CPUC) decisions interpreting whether generators foresaw the imposition of a carbon price in the electric sector. In fact, potential governmental action imposing GHG compliance costs on fossil fuel power plants in California was foreseeable *prior to* August 15, 2005.¹

For example, CPUC Decision 12-12-002², dated December 20, 2012, cites August 15, 2005, as the date a firm cap on GHG emissions was introduced by the Legislature. Similarly, CPUC Decision 12-04-046, dated April 4, 2012, states that "contracts negotiated and executed when AB 32 was working its way through the legislature should have taken the potential impacts of AB 32 into consideration. Even those negotiating contracts shortly before then might also have reasonably foreseen that this issue could arise."³

¹ For example, in 2004, the CPUC proposed a GHG Cap-and-Trade Program in an Order Instituting Rulemaking (OIR) and, in its comments on the OIR, the Independent Energy Producers Association mentioned independent generators internalizing the costs of GHG emissions reductions in offers submitted into the utility procurement processes. AB 32 was introduced into the California Legislature in December 2004. In June 2005, GHG emissions reduction targets were established for California by the Executive Order S-3-05.

² D. 12-12-002 is available at <http://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M041/K695/41695122.PDF>

³ D.12-04-046, page 61 available at http://docs.cpuc.ca.gov/PublishedDocs/WORD_PDF/FINAL_DECISION/164799.PDF

IOU counterparties and, presumably other generators, are sophisticated commercial parties with experienced commercial, regulatory, and legal teams aware of the potential for GHG costs prior to the actual date of passage of AB 32. The CPUC agrees with this assessment; and we urge ARB to provide a consistent conclusion. Additionally, the definition of a “legacy contract” should clarify that generators eligible for a legacy Power Purchase Agreement (PPA) and do not pursue this option, are ineligible for transition assistance from ARB because this category of generators have the opportunity to execute a standard contract addressing GHG costs. PG&E therefore recommends the following changes to the definition of a “Legacy Contract” laid out in Section 95802:

(195197)“Legacy Contract” means a written contract or tolling agreement, originally executed prior to ~~September 1, 2006~~ August 15, 2005, governing the sale of electricity and/or Legacy Contract Qualified Thermal Output at a price, determined by either a fixed price or price formula, that does not provide for recovery of the costs associated with compliance with this regulation; the originally executed contract or agreement must have remained in effect and must not have been amended since ~~September 1, 2006~~ execution to change or affect the terms governing the California greenhouse gas emissions responsibility, price or amount of electricity or Legacy Contract Qualified Thermal Output sold, or the expiration date. For purposes of this regulation, legacy contracts exclude contracts that ~~have been amended to include~~ gave rise to are eligible to execute a Legacy PPA Amendment, as defined in the Combined Heat and Power Program Settlement Agreement Term Sheet pursuant to CPUC Decision ~~number D-10-12-035~~, with a privately owned utility as defined in the Public Utilities Code section 216 (referred to as an Investor Owned Utility or IOU). ~~For the purpose of this regulation, Legacy Contracts include contracts that are considered non-standard OF contracts.~~ This definition of a “Legacy Contract” does not apply to opt-in covered entities.

3. The Renegotiation Provision Should Be Reinstated

The removal of provision 95891(f)(4) would provide free allowances to any legacy contract generator even if the contract is renegotiated to include consideration of GHG costs following ARB’s approval of a legacy contract generators’ allowances for a particular budget year. This section should be reinstated to ensure legacy contract generators are not provided a windfall under the cap-and-trade program. In addition, Section 95894(a)(5) could be modified as follows:

If, subsequent to the submittal of the foregoing information and supporting documentation, there is any material change in the information and statements provided to the Executive Officer, the party who submitted such information and statements shall submit a supplemental attestation and supporting materials addressing any such material change to the Executive Officer within 30 days after the change occurs. If the Executive Officer receives information demonstrating that the Legacy Contract was renegotiated to include consideration of greenhouse gas costs, the Executive Officer shall prorate any allocation to include only emissions prior to the date of renegotiation.

4. Transition Assistance Should Not be Extended

Extending legacy contract transition assistance through 2017 further removes any incentive for generators to agree to contract negotiations and prolongs the windfall for generators that have already been and continue to be compensated by PG&E customers. This revision removes any incentive for legacy contract counterparties to engage in negotiations until the end of the second compliance period, conflicting with ARB's and the CPUC's encouragement of the negotiation process. PG&E urges ARB to limit the transition assistance to 2013 and 2014 and therefore recommends the following conforming regulatory changes:

95870 (g) Allowances will be allocated to legacy contract generators for budget years 2013 and through 201447 for transition assistance. The Executive Office will transfer allowance allocations into each eligible generator's limited exemption holding account by October 1524, 2014 for eligible Legacy Contract Emissions pursuant to the methodology set forth in section 95894, and by October 24th of each subsequent year2015 for the 2014 compliance year.

95891(a) Opt-in covered entities are not eligible for transition assistance due to legacy contract emissions. To be eligible to receive a direct allocation of allowances under this section, the primary or alternate account representative of a legacy contract generator shall submit the following in writing via certified mail to the Executive Officer by June 30, 2014 or within 30 days of the effective date of this regulation for allocation in 2014, whichever is later, and by June 30th of 2015each subsequent year when applicable

D. Section 95912. Investigation Disclosure Language Should be Modified

PG&E proposes the following modifications to the ongoing investigation disclosure requirement for auction participation. For a company as large as PG&E, knowledge and materiality qualifiers are essential to PG&E's ability to provide the requested representation in a timely fashion. PG&E would not want to violate the cap-and-trade regulation due to a failure to report a minor administrative violation of a Commodities Futures Trading Commission (CFTC) rule connected to its energy purchases, which would likely be unrelated to PG&E's cap-and-trade activities. In addition, the required attestation should pertain only to those investigations that are currently pending before applicable entities.

95912(d)(4) (E)(C) An attestation disclosing to the best of the participating entity's knowledge the existence and status of any ongoing investigation ~~or an investigation that has occurred within the last ten years~~ by the U.S. Securities and Exchange Commission, Federal Energy Regulatory Commission, or the Commodity Futures Trading Commission with respect to any alleged material violation of any rule, regulation, or law associated with any commodity, securities, or financial market for that 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 pursuant to section 95833. The attestation must be updated to reflect any change in the status of an investigation that has occurred since the most recent auction application attestation was submitted; ~~has not been subject to~~ The identification of of any previous or ongoing pending investigation with respect to any alleged violation of

~~any rule, regulation, or law associated with any commodity, including a change in the status of an ongoing investigation~~ and

E. ARB Should Not Include Burdensome Staff Reporting Requirements

PG&E appreciates the changes to Section 95830(c)(1)(I) introduced in the discussion draft. However, the requirement to report employees who “review transaction agreement[s]” unnecessarily captures a large number of PG&E employees involved in activities unrelated to ARB’s market monitoring efforts, including those involved in administrative responsibilities related to transactions. For example, PG&E would be required to report a large number of staff with access to PG&E’s contracts to fulfill their duties in accounting, settlement, or contract management. Due to the broad scope of individuals covered by Section 95830(c)(1)(I), administration of such a provision would undoubtedly prove burdensome. Further, combined with Proposed Section 95912(d)(5), updates or changes to this information would unreasonably jeopardize an entity’s auction participation. Moreover, it is unclear how such a requirement would contribute to the success of the Cap-and-Trade program or how ARB would analyze, make use of, or benefit from this information. PG&E proposes the following changes to Section 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 and review transaction agreements, transfer requests, or has knowledge of the entity’s - surrender obligation and the entity’s account balances involving compliance instrument account balances s in the Cap-and-Trade Program Tracking System or any External GHG ETS linked pursuant to subarticle 12.~~

F. Sections 95851 and 95852 Exemptions Should Be Tied to GHG Reduction Performance

We thank staff for clarifying that the natural gas utility becomes the point of compliance for emissions from cogeneration and district heating facilities eligible for a limited exemption. As a general principle, we believe that any preferential treatment for Combined Heat and Power (CHP) should be tied to the measured GHG performance of the system in question. In the future, we encourage ARB to use data collected under the Greenhouse Gas Mandatory Reporting Regulation (MRR) to examine operational performance of CHP facilities in relation to separate heat and power production.⁴

⁴ PG&E submitted comments to ARB in September 2012 during the rulemaking process of amendments to the MRR and requested such GHG performance examination of CHP facilities. Please refer to: *PG&E’s Comments on the Proposed Amendments to the Regulation for the Mandatory Reporting of Greenhouse Gas Emissions*, September 10, 2012, Section D & E- page 3-7 http://www.arb.ca.gov/lists/ghg2012/3-091012_mrr_comments_final.pdf

G. PG&E Supports The Adoption Of Additional Protocols

PG&E would like to reiterate its support for the adoption of additional protocols to provide an adequate supply of offset credits to the cap-and-trade market. PG&E also appreciates the incorporation of stakeholder feedback into the offset-related sections of the draft amended regulation and the latest Mine Methane Capture (MMC) protocol discussion draft. The use of high-quality offset credits is an effective cost-containment tool and an essential component of a successful cap-and-trade program. However, as previously stated in PG&E's comments, without adequate supply, the cost-containment benefit of offset credits will not be fully realized. Therefore, PG&E urges ARB to approve the MMC and Rice Cultivation protocols, which will pave the way for additional offset credit supply.

Approval of the Mine Methane Capture (MMC) protocol is important because it can facilitate the generation of a significant supply of offset credits. While estimates vary, MMC projects have the potential to reduce tens of millions of tons of CO₂e from mines whose methane would otherwise be released to the atmosphere. With regard to leakage, ARB, CAR, and EPA analyses⁵ note that revenues from coal mining are sufficient to incentivize mine drainage, that mine ventilation is already required by US regulation, and that methane recovery and destruction does not typically take place when it is not economic to do so. Because US MMC projects can generate emission reductions without leakage and also meet ARB's criteria of being real, additional, quantifiable, permanent, verifiable, and enforceable, PG&E strongly supports the approval of the MMC protocol.

H. PG&E Recommends Minor Clean-up Language to Sections 95802, 95921, 95920, and 95923

PG&E proposes the following clarifications to definitions listed under Section 95802:

(8)(130) "~~Execution Date~~ Agreement Transfer Date" means a provision of a transaction agreement that requires the transfer of compliance instruments on or before a date determined as set forth in by the transaction specified in the agreement.

(244246) "~~Over-the-Counter Agreement~~" means the ~~trading sale~~ of carbon compliance instruments, ~~contracts~~, or other instruments not listed ~~on~~ arranged through any exchange.

(346) "~~Termination Date~~" is a date specified in a transaction agreement on which all requirements related to present or future transfers of compliance instruments are to be completed, excluding contingencies.

⁵ See ARB Staff Report and Proposed Compliance Offset Protocol, Mine Methane Capture Projects:

<http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13isorappa.pdf>

See CAR Coal Mine Methane Project Protocol FAQs:

<http://www.climateactionreserve.org/how/protocols/coal-mine-methane/faq/>

See EPA Coalbed Methane Outreach Program FAQs:

<http://www.epa.gov/cmop/faq.html#eight>

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PG&E recommends a minor change to Section 95920:

(B) Beginning in 2013 on October 1 ~~of each year~~ the limited exemption will be increased by the amount of emissions contained in the most recent emissions data report that has received a positive or qualified positive emissions data verified statement during that year.

PG&E recommends a minor change to Section 95921:

(b)(2)(C) Exchange-based agreements for the sale of compliance instruments through any contract arranged through an exchange or Board of Trade.

PG&E suggests the following modifications to Section 95923:

(c) The entity must disclose the information pursuant to section 95923(b) to the Executive Officer:

(3) Within 30 days of a change to the information disclosed ~~on~~ to Consultants or Advisor

III. CONCLUSION

Thank you for the opportunity to submit these comments. PG&E urges ARB to carefully review these suggestions and make the recommended changes before pursuing further action. We look forward to continuing our work with ARB.

Very truly yours,

/s/

Mark C. Krausse

cc: Rajinder Sahota, via email (rsahota@arb.ca.gov)