



Via electronic submission

February 14, 2014

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

**Comments of the California Cogeneration Council on
CARB's Discussion Draft Regarding California Cap-and-Trade Regulation**

Dear Madame Chairman,

Thank you for the opportunity to comment on the California Air Resources Board's (CARB) January 31, 2014 discussion draft regarding its draft amendments to the California Cap and Trade regulation (the "Regulation"). The California Cogeneration Council (CCC) represents a number of combined heat and power (CHP) facilities with legacy contracts that do not allow for the pass-through of the cost to purchase greenhouse gas (GHG) emission allowances to meet their compliance obligations under the Regulations.

CARB staff has worked with affected stakeholders to address the lingering legacy contract issue, and we appreciate the staff and Board decision to provide relief to legacy contract generators through the end of the second compliance period, i.e. 2017. While this time period satisfies most legacy contract generators a small number have contracts with terms that extend beyond 2017. Negotiation with counterparties has not produced a solution, consequently the CHP generator is facing unrecoverable compliance costs in the third compliance period (2018 through 2020). We ask that CARB continue to seek a resolution to the legacy contract issue for those legacy contract generators.

The CCC has identified a number of issues in the draft amendments and proposes solutions in our comments below.

Specific Comments:

1. Definition of "Legacy Contract Qualified Thermal Output"

In trying to refine the definition of Legacy Contract Qualified Thermal Output (page 33 of the discussion draft), staff has introduced an either (a) or (b) concept which does not make sense from a CHP operational perspective. The definition should cover all thermal output which is included in the terms of the agreement of the legacy contract. This will include the thermal energy produced by the CHP unit and sold to the host, whether it is used for the purposes of

heating or cooling, or in the industrial process of the host facility (counterparty to the legacy contract). This should also include the thermal energy that is not an integral part of the cogeneration unit, but is provided for and sold under the legacy contract. For example, the emissions associated with an auxiliary boiler that may be run to meet the thermal demands of the host either when the cogeneration unit is unavailable, or is unable to meet the host thermal requirements.

Recommendation: Amend the definition to read –

(200) “Legacy Contract Qualified Thermal Output” means thermal energy that is sold to specific end-users, and reported pursuant to MRR section 95112(a)(5)(A). It includes all thermal output from the cogeneration unit that is sold to the legacy contract counterparty and it also includes:

(a) thermal energy used to produce cooling energy (e.g. chilled water) if the facility provides thermal energy to a particular end user outside of the facility boundary that is reported pursuant to MRR 95112(a)(5)(C)(1)(c); and

(b) thermal energy generated by equipment that is not an integral part of the cogeneration unit that is provided or sold to a Legacy Contract Counterparty and meets the eligibility requirements in section 95894.

Legacy Contract Qualified Thermal Output does not include thermal energy that is vented, radiated, wasted, or discharged before it is utilized at industrial processes or operations.

2. Discriminatory Treatment of Legacy Contract Generators

The foundation of the legacy contract issue is that these are commercial agreements between two entities, executed prior to AB 32, that do not contain a provision that would address who is responsible for the compliance costs associated with the GHG emissions produced from the generation of electricity and/or thermal energy. Specifically it is an agreement between a third-party generator (Seller) and a Buyer of that energy. Whether or not the Buyer is an industrial host should not factor into the calculation of the transition assistance that will be provided to the generator. This is not a leakage issue. Consequently there is no rationale for providing different levels of relief to legacy contract generators based upon who is the counterparty and what is the end use of the energy procured under the contract.

In the draft amendments, CARB staff proposes that legacy contract generators with an industrial host be treated differently. Specifically, in calculating the initial allowance allocation to this subset of legacy contracts, CARB staff proposes using 2013 data and providing a subsequent “true-up” to account for any shortfall in allowances not accurately provided for in prior allocations. This same methodology should be applied to all legacy contract generators and the Seller should not be penalized by the regulation based upon who is the Buyer of their energy output.

In the interest of fairness and equity, the same basic principles should apply to **all** legacy contract generators in calculating the amount of relief (in the form of allowances) that should be provided.

- (i) **Use most current data available to calculate GHG emissions allowances.** For all legacy contract generators CARB staff should use 2013 data for the facility's reported GHG emissions or amount of electricity and steam sold pursuant to a legacy contract to ensure the allowance allocations accurately reflect current operating output, and to avoid any inequitable shortfall or over-allocation to generators. 2012 was a recessionary year and review of preliminary data indicates output was lower that year than in 2013. Estimates of expected output in 2014 also exceed 2012 levels. CARB staff proposes using 2013 data for legacy contract generators with counterparties receiving industry assistance and there is no reason not to do the same with all legacy contract holders.
- (ii) **Include a True-Up to ensure relief is based on actual emissions.** This will eliminate the risk of under allocating or over allocating allowances to legacy contract generators. Again, staff is proposing a True-Up for legacy contract generators with industry counterparties and there is no reason why the same principle should not be applied to **all** legacy contract generators. The purpose of the regulation is to encourage increased use of energy efficient facilities, but this provision as currently presented, incents the opposite. Efficient facilities that are called upon to increase their output will have greater onsite emissions, but if there is no True-Up, the facility will receive an under-allocation of allowances leaving it exposed to unrecoverable costs. To ensure emission allowances are provided for all electricity and steam sold pursuant to a legacy contract, CARB staff should include a "true-up" in the equations in Sections 95894(d)(1) and (d)(2) of the draft amendments. Providing this type of true-up is consistent with the allocation calculation methodology in sections 95894(c) of the draft amendments for generators with counterparties receiving industrial allowance allocations.

Conclusion

The legacy contract issue was identified after the first draft cap and trade regulation was published in October 2010. Stakeholders and staff have worked together since that time to address this complicated issue, and the draft amendments published in January 2014 come a long way toward providing a final solution.

To ensure the solution is fair and equitable to all legacy contract generators, the transition assistance calculation methodology should adhere to the same basic principles regardless of the status of the counterparty to the commercial agreement. Specifically, 2013 data should be used when calculating the generators' reported GHG emissions or amount of electricity and thermal energy output pursuant to a legacy contract, and a subsequent true-up should be used to correct for any shortfall in allocations.

Attached to our comments are proposed changes to the draft amendments that implement our specific proposals.

Sincerely,

A handwritten signature in black ink, appearing to read 'BV' followed by a stylized flourish.

Beth Vaughan
Executive Director

cc: Board Members of the California Air Resources Board
Virgil Welch, Special Assistant to the Chairman
Richard Corey, Executive Officer
Rajinder Sahota, Branch Chief, CARB Cap-and-Trade Program

**CARB January 31, 2014 Informal Discussion Draft
Potential Amendments to California Cap-and-Trade Program**

§ 95894. Allocation to Legacy Contract Generators for Transition Assistance

* * * * *

(d) For legacy contracts not covered in 95894(c), the following formulae shall apply:

(1) For stand alone generation facilities:

$$TrueUp_{2015} = (EEm_{lc} * c_{2013}) + (EEm_{lc} * c_{2014}) + (EEm_{lc} * c_{2015})$$

Where:

“TrueUp2015” is the amount of true up allowances allocated from budget year 2015 and allowed to be used for budget years 2013 and 2014 and subsequent years, pursuant to sections 95856(h)(1)(D) and 95876(h)(2)(D), in vintage 2015 allowances based on calendar year ~~2012~~ 2013 Legacy Contract Emissions reported and verified pursuant to MRR;

“EEm_{lc},” is the emissions reported, in MTCO₂e, associated with electricity sold under the legacy contract in ~~2012~~ 2013; and

* * * * *

For years 2016 and 2017, the following equation applies:

$$A_t = (EEm_{lc,t-2} * C_t) + TrueUp_t$$

Where:

$$TrueUp_t = (EEm_{lc,t-2} * C_{t-2}) - A_{t-2, no trueup}$$

Where:

TrueUp_t is the amount of true-up allowances allocated to account for the emissions reported for data year “t”.

"A_{t-2,no trueup}" is the amount of California GHG allowances directly allocated to the Legacy Contract Generator subject to a Legacy Contract from budget year "t-2" not including the true-up for that budget year.

- (2) For legacy contract generators not covered in 95894(c) or 95894(d)(1):

$$TrueUp_{2015} = ((Q_{lc} * B_s + E_{lc} * B_e) * c_{2013}) + ((Q_{lc} * B_s + E_{lc} * B_e) * c_{2014}) + ((Q_{lc} * B_s + E_{lc} * B_e) * c_{2015})$$

Where:

"TrueUp₂₀₁₅" is the amount of true-up allowances allocated from budget year 2015 and allowed to be used for budget years 2013 and 2014 and subsequent years pursuant to sections 95856(h)(1)(D) and 95856(h)(2)(D) in vintage 2015 allowances based on calendar year ~~2012~~ 2013 Legacy Contract Emissions reported and verified pursuant to MRR;

"Q_{lc}" is the Legacy Contract Qualified Thermal Output in MMBtu sold under a legacy contract in data year ~~2012~~2013, as reported to MRR;

"E_{lc}" is the electricity, in MWh, sold under the legacy contract in data year ~~2012~~2013;

* * * * *

For years 2016 and 2017, the following formula applies:

$$A_t = ((Q_{lc} * B_s + E_{lc} * B_e) * C_t) + TrueUp_t$$

Where:

$$TrueUp_t = ((Q_{lc,t-2} * B_s + E_{lc,t-2} * B_e) * C_{t-2}) - A_{t-2,no trueup}$$

"A_t" is the amount of California GHG allowances directly allocated to the Legacy Contract Generator subject to a Legacy Contract from budget year "t". This value shall only be calculated if the entity meets the eligibility requirements, pursuant to section 94894(a) and 95894(b), and is covered under the Cap-and-Trade Program during the second compliance period.

And:

TrueUp_t is the amount of true-up allowances allocated to account for the emissions reported for data year “t”.

“Q_{lc, t-2}” is the Legacy Contract Qualified Thermal Output in MMBtu sold under a legacy contract in data year t-2, as reported under the MRR;

“E_{lc,t-2}” is the electricity, in MWh, sold under the legacy contract in data year t-2.

“B_e” is the emissions efficiency benchmark per unit of electricity sold or provided to off-site end users, 0.431 California GHG Allowances/MWh;

“B_s” is the emissions efficiency benchmark per unit of Legacy Contract Qualified Thermal Output, 0.06244 California GHG Allowances/MMBtu thermal;

“c_t” is the cap decline factor for budget year “t” as specified in table 9-2;

“c_{t-2}” is the is the cap decline factor for the budget year two years prior to year “t” as specified in Table 9-2;

“A_{t-2, no trueup}” is the amount of California GHG allowances directly allocated to the Legacy Contract Generator subject to a Legacy Contract from budget year “t-2” not including the true-up for that budget year;

* * * *

- (e) Data Sources. In determining the appropriate values for section 95894(c) and 95894(d), the Executive Officer may employ all available data reported to ARB under MRR for ~~2012~~ 2013 and all other relevant data, including invoices, demonstrating the amount of electricity and Qualified Thermal Output sold or provided for off-site use that does not include a carbon cost in the budget year for which it is seeking an allocation. If necessary, the Executive Officer will solicit additional data to establish a representative allocation. The operator of the Legacy Contract Generator must provide the additional data upon request by the Executive Officer.