



February 14, 2014

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

**Subject: Comments on CARB's January 31, 2014 Discussion Draft
Amendments to the California Cap and Trade Regulation**

Dear Madam Chairman,

We appreciate the opportunity to provide these comments regarding the California Air Resources Board January 31, 2014 discussion draft amendments to the California Cap and Trade Regulation.

I. Introduction

California Air Resources Board (CARB) staff has worked closely with generators of electricity and steam throughout the development of the Cap-and-Trade regulation, and subsequent amendments, to address concerns regarding long-term fixed-price contracts. Some covered entities have contracts enacted prior to the signing of AB 32 that have no reasonable means to pass GHG compliance costs to the contract counterparty. We appreciate CARB staff's decision in the draft amendments to provide relief to legacy contract generators by providing allocations of allowances.

On October 16, 2013, the ARB published a revised staff proposal to extend transition assistance for legacy contracts through the second compliance period, instead of ending in 2014. In testimony at the ARB Board meeting on October 25, 2013, Crockett Cogeneration pointed out that while this proposal provides sufficient assistance to the majority of legacy contract holders as their legacy contracts either expire before the end of 2017 or closely thereafter, it unfortunately does not provide a complete solution for Crockett Cogeneration, due to the much longer term of the legacy contract.

Crockett Cogeneration is a 240 MW natural gas fired, combined cycle cogeneration facility located at the C&H Sugar refinery in Crockett, California. The facility supplies approximately 1,850,000 megawatt hours of electricity to PG&E and 2,000,000 MMBtu of steam to C&H Sugar annually. Approximately 80% of the steam comes from the CHP facility, and additional steam is provided as needed from auxiliary boilers owned and operated by Crockett Cogeneration.

The cap and trade regulation imposes an unrecoverable cost upon Crockett Cogeneration because its steam sales contract does not explicitly contemplate recovery of the charges for GHG emissions arising from cogenerated steam, and there is currently no other GHG cost recovery mechanism available to the company.

The draft amendments proposed in the January 31, 2014 discussion draft provide two pathways leading to solutions for legacy contracts:

- (1) If the legacy contract holder has an industrial counterparty receiving free allowances, the legacy contract generator will receive free allowances for the term of the contract that will be subtracted from the allocation of allowances that are to be provided to the industrial covered entity. The idea is that this will incent the industrial counterparty to come to the table and renegotiate the legacy contract with the CHP generator. Note that the allowance allocation does not end in 2017.
- (2) In all other cases of a legacy contract, transition assistance (in the form of free allowances) will be given to the legacy contract generator for the first and second compliance periods only.

In (2) above, the term in the September 2013 45-day proposed amendment was to the end of the first compliance period (2014), but in the January 2014 draft amendments it will be to the end of the second compliance period (2017). This satisfies almost all the legacy contract holders because either they fall into pathway (1), or in the case of pathway (2), their legacy contract expires by the end of 2017.

The only legacy contracts with terms beyond 2018 that we could identify are a couple of CHP facilities with industrial hosts that will receive free allowances (pathway (1) above applies) and Crockett Cogeneration. Crockett Cogeneration was one of the last Qualifying Facilities (QF) to come online in 1996 under a 30-year Power Purchase Agreement; consequently the thermal legacy contract with C&H Sugar expires in 2026.

II. Unique Situation of Crockett Cogeneration

Crockett Cogeneration is the only facility on ARB's list of legacy contract generators in the unique situation where the industrial host counterparty meets the criteria to be categorized as high leakage risk (production is highly emissions intensive and competition is strong from out-of-state producers), but it is **NOT** covered by the cap and trade regulation. In this case C&H Sugar refinery is not an industrial covered entity because it does not emit greater than 25,000 MTCO₂e. This is solely because Crockett Cogeneration combusts the natural gas that supplies all the thermal energy used in the production of the sugar, and it provides the steam that C&H uses to run its two steam turbine generators to produce onsite electricity. **"But for"** Crockett Cogeneration, the C&H refinery would need to run additional boilers to meet its total steam needs in an amount that would exceed the 25,000 MT threshold. Consequently, C&H would be an industrial covered entity under the cap and trade regulation and would be eligible for an allocation of free allowances under the cap and trade regulation.

III. Possible Solutions

(i) Include Crockett Cogeneration in pathway (1)

If C&H emitted above the 25,000 MT threshold, it would receive free allowances that could be transferred to Crockett Cogeneration, as per the 45-day proposed amendments (pathway (1) above).

Our recommendation is to make an exception for Crockett Cogeneration, because of its unique situation, and provide transition assistance for the term of its legacy contract essentially adding it to the legacy contracts in pathway (1). The allowance methodology in section 95894 (c) (2) should be used to calculate the amount of GHG allowances (and true-up) to be allocated to Crockett Cogeneration.

(ii) Apply the C&H Sugar NAICS code to Crockett Cogeneration

Table 8-1 of the cap and trade regulation specifies the industrial sectors that are eligible for industry assistance. Food Manufacturing has the NAICS code 311 and the NAICS code for cane sugar refining and associated activities is 311314.

Again, “**but for**” Crockett Cogeneration, the C&H sugar refinery would need to produce its own steam to meet its thermal energy needs in an amount that would exceed the 25,000 MT threshold. Consequently, C&H would be considered an industrial covered entity under the cap and trade regulation and be eligible for industrial assistance.

Therefore, it would be logical to apply the allocation of allowances, which would have otherwise been available to C&H, to Crockett instead. The NAICS code 311314 could be applied to Crockett Cogeneration for solely the portion of emissions associated with the steam production provided to C&H under the legacy contract. The product benchmark calculation in Section 95891 would then be applied to calculate the allocation of industrial assistance.

IV. Conclusion and Recommendations

Since October 2010 when the initial draft of the Cap and Trade regulation was published, Crockett Cogeneration representatives have discussed the legacy contract situation with both CARB staff and C&H Sugar management. C&H Sugar has no incentive to open the steam agreement for renegotiation, and it also has no incentive to opt into the cap and trade program. Consequently, Crockett Cogeneration has no ability to recover or pass through GHG costs. At a carbon price of \$15/MT, the compliance costs for the steam legacy contract alone could be several million dollars per year.

We respectfully request that the ARB consider the unique situation of Crockett Cogeneration and adopt one of the two solutions we have proposed. A final resolution to this last, outstanding legacy contract would mean the legacy contract issue can finally be put to bed and will not need to be re-visited in future amendments to the cap and trade program. We are available to meet with staff and Board members to discuss our proposals and urge CARB to address the unique situation of Crockett Cogeneration.

Respectfully submitted,



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