Comments of the Western Power Trading Forum to the California Air Resources Board on Cap and Trade Regulation Amendments

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The Western Power Trading Forum[1] (WPTF) welcomes the opportunity to provide input to the California Air Resources Board (CARB) on issues raised at the October 21st workshop on Cap and Trade Regulation Amendments. WPTF's comments below address CARB's consideration of options for greenhouse gas emission (GHG) accounting in the Energy Imbalance Market (EIM) and retention of the Renewable Portfolio Standard (RPS) Adjustment.

GHG Accounting in the EIM

In our September 19th comments, WPTF agreed with the staff concern that the way the EIM is currently dispatching and assigning generation to California Independent System Operator (CAISO) load is distorting dispatch and, in some cases, could result in increased emissions in the combined CAISO/EIM footprint. WPTF recommended that CARB work with the CAISO to explore options for modifying the way that the EIM algorithm treats carbon costs in the dispatch and allocation of generation to serve CAISO load. However, we cautioned that changes in the algorithm could result in "GHG accounting that is more in line with the AB32 goals, but may have other consequences that make the solution impractical or politically unacceptable."

To date, CAISO staff have identified three potential approaches to addressing GHG accounting concerns: Intertemporal netting of GHG impacts (option one), incremental above-economic-base deeming" (option two) and a GHG hurdle rate (option three). CARB staff added a fourth option, the "dynamic hurdle rate" at the October 21st workshop. As WPTF follows these discussions, we are becoming increasingly concerned that the negative consequences of proposed options on market efficiency outweigh the potential emission reduction benefits. In particular, WPTF strongly opposes both the CAISO's common GHG hurdle rate approach and CARB's dynamic hurdle rate.

Under the CAISO's variant, a common GHG hurdle rate, determined based on some calculation of residual GHG emissions, would be added to the energy bid of all non-California EIM resources in considering whether to deem such dispatch as delivered to California. This hurdle would be imposed in addition to each resource's specific GHG bid adder, but would be exempted for resources that are contracted to California load-serving entities. Imposition of the hurdle would result in higher costs and increased revenues collected from California load, which would be used by the CAISO to purchase and retire allowances under the cap and trade program.

This proposal would make California resources more economically competitive relative to non-California resources by increasing the costs of non-California resources for supplying California load. This would be distortionary and could be unfair to external resources. Further, is not clear that level of the GHG hurdle would actually change the dispatch of generation in the EIM, nor assignment of generation to California load. For the hurdle rate to impact the displacement of California gas generation, it would need to be higher than the bid difference between non-California zero-emissions resources and that of California thermal generation, which includes carbon costs. More likely, the benefit of this approach would be achieved through retirement of allowances within the cap and trade system – not from any change of emissions within the EIM footprint.

[1] WPTF is a diverse organization comprising power marketers, generators, investment banks, public utilities and energy service providers, whose common interest is the development of competitive electricity markets in the West. WPTF has over 80 members participating in power markets within California and elsewhere across the United States.

CARB's dynamic hurdle rate is equally problematic. This option would also impose a GHG hurdle on all non-California resources based on a 5-minute calculation of system average emission rate for dispatched non-California resources, but would not maintain a distinction between the actual emission rate of individual resources. Rather, the hurdle would effectively assign the same emission rate to all resources, except for RPS-contracted resources. Like the CAISO's option, this hurdle would not result in a compliance obligation for individual resources; costs or compliance obligations would instead presumably be passed through to California load. Staff indicated that this approach could also be applied in a regional power market.

Unlike the CAISO's hurdle approach, CARB's proposal would eliminate incentives and opportunities for emissions leakage/resource shuffling within the EIM. However, it would do so by eliminating the carbon price signal for external resources, except for those contracted under the RPS. CARB and stakeholders have worked for the past several years to promote accuracy in the attribution of emissions to imported power, while providing important incentives for low and zero emission electricity. The program rules for specification of imported electricity reflect this balance. CARB's proposed approach would throw out these rules, and instead effectively treat all EIM generation as unspecified, except that the default emission rate would be calculated in 5 minute increments.

Of the options currently under consideration, the only one that merits further consideration is the 'incremental above-economic-base deeming'. This approach would restrict the eligibility of a resource's output to be deemed delivered to California to incremental generation above a counterfactual economic dispatch optimized for the EIM footprint without transfer to California. To the extent that low-cost, zero-emissions resources are dispatched in the first economic-base run, output of these resources would be attributed to non-California load and thus not available to displace California generation. This would result in gas generation (both California and external) being considered more often for attribution to California, compared to the current EIM algorithm.

On its face, the incremental deeming approach appears to be less distortionary than imposition of a GHG price hurdle, but it would add significant complexity to market operation, as the CAISO has noted. CAISO and CARB would also need to assess whether the approach could accommodate evolving carbon and clean energy regulations in other states and how it could be applied consistently across all the energy markets. WPTF support continued exploration of Option 2.

If it is not possible to implement a solution that works across all electricity markets without undermining the carbon price signal or the efficiency of those markets, then CARB should instead accept that it is not possible to eliminate emissions leakage in the absence of regional carbon policies. Instead, CARB should make a transparent decision to focus on post-2020 solutions, taking into account the strong incentive created by the cap and trade program for import of low and zero emission power across all electricity markets. At the same time, CARB should work to encourage the development and linkage of carbon pricing programs throughout the west to reduce leakage.

RPS Adjustment

WPTF appreciates staff's retention of the RPS Adjustment after 2020 in response to stakeholder comments. However, we are concerned that continued reliance on existing reporting and verification requirements related to the RPS adjustment will perpetuate the difficulties encountered by electric power entities in claiming the RPS adjustment.

To address these problems, WPTF recommends that CARB explicitly acknowledge the relationship between the RPS adjustment and Portfolio Content Category 2 ("PCC2") under RPS program rules. Acknowledgement of this direct relationship would enable CARB to rely upon the RPS program requirements to improve verification. Specifically, we recommend that CARB modify the reporting regulation to accept documentation that e-tags for the import of firming and shaping power have been matched to Renewable Energy Credits (RECs) as part of a PCCC2 transaction for purposes of verifying RPS adjustment claims. Such documentation should be acceptable in lieu of evidence that the RPS power was not directly delivered to California.