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Jon Costantino, Manager
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California Air Resources Board
1001 I Street
Sacramento, CA 95812

Re: **Comments of the Northern California Power Agency on** ***Revised 15-day Language for Proposed AB 32 Cost of Implementation Fee Regulation***

Dear Jon and Jeannie:

The Northern California Power Agency[1] (NCPA) offers these comments on the *15-Day Modifications to the Originally Proposed AB 32 Cost of Implementation Fee Regulation* (15-Day Language), issued by the California Air Resources Board (CARB) on February 26, 2009. The 15-Day Language revises the May 8, 2009 Proposed Regulation (May 2009 Proposed Reg), adopting new Article 3, sections 95200 to 95207, to Title 17 of the California Code of Regulations, termed the "AB 32 Cost of Implementation Fee" (Fee).

I. INTRODUCTION

The 15-Day Language is the result of countless hours of review, two public hearings, and several rounds of comments on the appropriate application of a fee to cover the significant costs associated with *administration* of the various programs and measures contemplated under Assembly Bill (AB 32). NCPA has worked closely with CARB staff and other stakeholders throughout this process and appreciates the clarifications that have been included in the proposed revision to the regulation. With that said, however, NCPA continues to be concerned with the fact that the Proposed Regulation and Initial Statement of Reasons (ISOR)[2] have not been revised

1 NCPA is a joint powers agency whose members include the cities of Alameda, Biggs, Gridley, Healdsburg, Lodi, Lompoc, Palo Alto, Redding, Roseville, Santa Clara, and Ukiah, as well as the Bay Area Rapid Transit District, Port of Oakland, the Truckee Donner Public Utility District, and the Turlock Irrigation District, and whose Associate Members are the Plumas-Sierra Rural Electric Cooperative and the Placer County Water Agency.

2 The *Staff Report: Initial Statement of Reasons for Rulemaking (ISOR) for the Proposed AB 32 Cost of Implementation Fee Regulation*, dated May 8, 2009.

to address the concerns raised by stakeholders regarding (i) improper application of the Fee as assessed on some imported electricity that is not consumed in California (ii) the lack of a total cap on the annual amount of the Fee, (iii) certainty regarding the total fee obligation of affected entities, and (iv) lack of clarity regarding the Fee calculation and enforcement procedures.[3]

The revised 15-Day Language makes several key changes to the May 2009 Proposed Reg, yet fails, in several material provisions, to address or rectify the deficiencies previously identified by stakeholders in written and oral comments made on the record in this proceeding. These shortcomings are significant since the Fee requires entities that are already facing significant costs associated with meeting their own mandated reductions to incur additional costs for administration of statewide programs. Furthermore, the Fee is calculated based on a metric into which stakeholders have no meaningful input into.

II. COMMENTS ON 15-DAY LANGUAGE

A. As Drafted, the Regulation Improperly Imposes Fees on Imported Electricity Not Consumed In California.

Failure to Recognize Net Electricity Imports Adversely Impacts Efficiency of the Electricity Market. The 15-Day Language properly excludes the application of the Fee to power that is wheeled through California and is not used to serve customers in the State (§ 95202(56)(A)). Wheeled power is not properly categorized as imported electricity, and therefore appropriately excluded from calculation of the Fee. Likewise, those transactions that involve power exchanges between imported and exported power should also be excluded from application of the Fee. The 15-Day Language proposes that certain power exchanges – those that occur simultaneously – be excluded from application of the Fee (§ 95202(56)(b)). However, while NCPA supports each of these changes, the proposed revisions do not address all power imports that are not used to serve electricity customers in California.

AB 32 authorized CARB to create a "schedule of fees to be paid by the sources of greenhouse gas [GHG] emissions."[4] Included in the upstream sources upon which the Fee is to be imposed is imported electricity. However, NCPA continues to be concerned with the overly prescriptive definition of imported electricity, and the adverse impact that the current proposed language will have on affected entities. Specifically, it is imperative (and entirely feasible) that the Fee be designed in such a manner as to not financially penalize the efficient and reliable operation of the west-wide electricity infrastructure.

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3 NCPA does not reiterate the positions set forth in the *Comments on the Northern California Power Agency on Proposed AB 32 Cost of Implementation Fee Regulation*, submitted June 24, 2009 (NCPA June 24, 2009 Comments) and the *Comments of the Northern California Power Agency on Staff Proposed changes to the AB 32 Cost of Implementation Fee Regulation*, submitted on September 2, 2009 (NCPA September 2, 2009 Comments), but incorporates those comments herein.

4 Health & Safety Code § 38597 provides, in pertinent part: "*The state board my adopt by regulation, after a public workshop, a schedule of fees to be paid by the sources of greenhouse gas emissions regulated pursuant to this division, consistent with Section 57001 . ..*"

If the Fee is imposed on all electricity imports without recognition of the electricity actually consumed in California, CARB risks jeopardizing the efficient and reliable provision of electricity throughout the State. The purpose of transactions that allow imported electricity to enter the State at one point, change ownership, and be exported back at a different location is to leverage the most effective operation of the entire western electric generation and transmission system, based on transmission constraints, differing peaks, and time of operating various facilities. This provision is especially problematic for entities that use lower-GHG emitting imported power in their portfolios in order to optimize generation and transmission usage. These efficiencies promote cost savings and environmental benefits, as more fully discussed in the June 24, 2009 and September 2, 2009 NCPA comments. If entities know that they are going to be assessed an additional Fee on this electricity, they will be less motivated to act to promote the greatest efficiencies, but rather will need to adjust their transactions to avoid imposition of the Fee. Such an outcome should be avoided, and *can* be avoided by adjusting the proposed Fee to reflect that the charge will only be assessed against the <u>net</u> electricity imports, which actually reflects the electricity *consumed in California*.[5]

Application of the fee should be limited to the amount of actual electricity consumed in California. Assessing the Fee to all electricity produced in California, as well as electricity imported into the State without recognition of electricity exported rather than the net imports adversely burdens the electricity sector by resulting in payment of the Fee on electricity not consumed in California. This outcome is clearly inconsistent with the stated purpose of the Fee in the ISOR and the treatment of other sources of emissions. A simple solution is to allow for the netting of electricity imports and exports that are associated with "energy exchange agreements" or seasonal transactions with a particular region. As more fully explained below, this change is necessary to avoid duplicative and burdensome imposition of the Fee on a single sector. The broad authority set forth in Health and Safety Code § 38597 gives CARB clear authority to craft the regulation in such a manner.

Staff has correctly noted that in order to include a mechanism to net imports in the Proposed Regulation, the provisions must be based on sound public policy and be administratively feasible. NCPA maintains that the netting of imports and exports associated with energy exchange agreements and seasonal/regional transactions are both.

Opponents of this concept have opined that allowing such netting ignores the language in AB 32 that calls for reporting of electricity produced in-state and electricity imports.[6] However, this is simply not true. Determination of the Fee does not change an entity's reporting obligations

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5 The ISOR notes that "electric importers . . . should be able to pass the Fee cost on to the load-serving entities. The load-serving entities can then recover the passed-through Fee cost as a price increase over all of their deliveries. ARB believes that the imposition of the Fee is too small to affect wholesale market dispatch." (ISOR, p. 46) There is no underlying data, however, to support this conclusion. Additionally, a significant portion of the Fee in the early years is based on past amounts, the pass-through of which is impossible.

6 Health & Safety Code § 38530(b)(2).

under AB 32, nor the compliance obligation for emissions reductions as outlined in the statute and the Scoping Plan. Indeed, the Fee is intended to be applied in a manner that is administratively feasible, and the ISOR expressly states that the result is a Fee on approximately 85% of the state's emissions – there is no actual link between a compliance obligation and assessment of the Fee. Additionally, ensuring that the Fee is assessed on the net of imported and exported electricity is also crucial in the development of a multi-jurisdictional cap-and-trade program. If not applied in this manner, electricity consumed in a partner jurisdiction will be assessed a different set of fees and subject to corollary requirements in that jurisdiction. Simply put, the same electricity should not be subject to two sets of fees, especially when the power at issue is not consumed in California.

Furthermore, netting imports and exports is also administratively feasible. These transactions are not uncommon. While power exchanges and seasonal agreements are not single transactions, like wheeled power, they are easily tracked and monitored, and present no additional burdens from a verification standpoint. The imports and exports are all reported, and accordingly, determining the net of these transactions is done in the normal course of business. The mechanism for calculating net energy imports is straightforward and would not entail additional administrative complexities. The reporting of imports and exports under the Mandatory Reporting Tool could be easily tracked with minor modifications to the Tool itself, making verification of the total imported electricity consumed in California easy to determine.

Finally, imposition of the Fee must not adversely impact the overall efficiency of the state and regional electricity grid operations. Any cost conclusions regarding the impact of the Fee on the state's electricity grid operations must be verified. Accordingly, the ISOR should include empirical data that substantiates a finding that "the imposition of the Fee is too small to affect wholesale market dispatch" (ISOR, p. 46) or have the language entirely removed from the document. See NCPA June 24, 2009 Comments, pp. 5-6 and NCPA September 2, 2009 Comments, pp. 2-4.

B. Renewable Gas is Properly Not Subject to the Fee

The 15-day Language properly amends the definition of Natural Gas in § 95020(68) to specifically exclude "biogas." Entities that have biogas in the pipeline would be able to verify those amounts, and any Fees that would otherwise be applicable would be credited against any Fee obligation of the compliance entity. This proposed revision properly recognizes the renewable nature of biogas.

C. The 15-Day Language Creates Continued Ambiguity With Regard to the Total Amount of the Fee Obligation for Affected Entities.

<u>Total Cap on the Fee Still Missing and Ambiguities are Prevalent Regarding the Payment Obligations.</u> While the *February 26, 2010 Notice of Availability* provides a number of additional

records and data to substantiate the costs incurred to date, it does not provide additional data regarding the total amount of the fee in future years, nor assurances regarding potential caps on those amounts, nor is the ISOR properly revised to address concerns regarding this matter. Furthermore, sections § 95203(2) (" . . . the remaining Debt shall be repaid in fiscal year 2013/2014 . . .") and § 95203 (5) ("The annual Total Revenue Requirement is equal to the RR adjusted for the previous fiscal year's excess or shortfall amount . . .") in the "Calculation of Fees" and § 95207(b) (Severability) which allows for collection of past amounts from entities determined by a court to be "ineligible" for fee payment, create even greater uncertainty for compliance entities regarding the total amount of their annual obligation.

As widely noted by a broad range of stakeholders, the entire Fee Regulation is deficient in its failure to include any kind of a cap on the total amount of the Revenue to be collected. It is important to note that the Fee at issue is only designed to cover *the state's* administrative costs for implementing, carrying out, and enforcing a broad range of programs and measures under AB 32. However, affected entities will be faced not only with the cost of the Fee, but AB 32 compliance costs, as well. The costs to the electricity sector, for example, to carry out such measures as expanded energy efficiency programs, increased renewable energy portfolios, and construction of new combined-heat and power facilities, will be quite significant. Consequently, the Fee will amount to an additional financial burden on compliance entities. This financial impact should not be minimized when CARB is looking to the total economic impact on California's electricity customers.

As proposed, the Fee will be set in place to collect *whatever amounts* the state agencies may require in the coming years:

> § 95203(a)(1) provides that "the Required Revenue (RR) shall be the total amount of funds necessary to recover the costs of implementation of AB 32 program expenditures for each fiscal year . . ."

Because of the broad range of "AB 32 programs" that can be covered under the Revenue Requirement, including the proposed cap-and-trade program, the Fee has the potential to be quite large, and likely will increase annually. With CARB only at the nascent stages of implementing the provisions of the Scoping Plan, the total amount of the Fee obligation from year to year is not known. Hence, any reference justifying the structure of the Fee based on the overall amount must be disregarded. See NCPA June 24, 2009 Comments, pp. 3-4.[7]

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7 As noted in the NCPA June 24, 2009 Comments, the failure to include a reasonable cap on the total annual Revenue Requirements is problematic and a fatal flaw to the Fee structure. The Regulation is largely based on the Nonvehicular Source Fee Program (NVSF) that was developed as a result of 1999 legislation (Assembly Bill 1103), which extended indefinitely CARB's authority to collect permit fees from large nonvehicular sources of air pollution. While there are aspects of the NVSF that are similar to the Proposed Regulation (this fee is "intended to help defray the ARB's cost of implementing the nonvehicular provisions of the [California Clean Air Act]"[7]), there is an important difference in that the NVSF is based on a *capped amount*, not subject to annual adjustments. This distinction is crucial. Unlike the NVSF, however, the fee at issue is <u>not</u> subject to a statutorily established cap, nor an open review and approval process. The legislature can change the amount due annually, depending on the budgets submitted by the various state agencies, and indeed, even the State agencies eligible to receive funding under the Fee

Furthermore, as noted above, the additional language in § 95203(2) regarding the debt repayment obligation for 2013/2014 does not even specify the total amount of the debt repayment that will be added to the fee obligation for that fiscal year. Likewise, the fact that the Fee obligation is also subject to adjustment each year (§ 95203(5)), and affected entities essentially serve as guarantors for all uncollected debts from the previous year, makes it extremely difficult, if not impossible, for compliance entities to budget for the amount of their fee obligation, let alone structure their costs to address the pass-through of these costs.[8]

Accordingly, it is imperative that the Proposed Regulation be drafted in a manner that addresses these concerns and places some limit on the total fee obligation entities will be required to pay each year. As noted, this is especially crucial given the fact that those subject to the fee are paying the fee <u>in addition</u> to their AB 32 compliance costs.

D. The Proposed Regulation Properly Uses the Most Recent Data for Calculation of the Fee.

Several stakeholders, including NCPA, expressed concern with previous drafts of the Proposed Regulation regarding the accuracy of the data being used to calculate the Fee. The addition of § 95201(c) addresses this concern. The 15-Day Language properly revised the Proposed Regulation to reflect the fact that the Fee will be calculated based on the most recent emissions data reported to CARB.

E. The 15-Day Language Needs Further Clarification in § 35205 Regarding the Treatment of Sums Not Collected.

The 15-Day Language includes new language in the Payment and Collection section. As proposed, § 95205(a) provides that "ARB will not collect the fee from entities whose total amount due . . . is less than or equal to fifty dollars ($50)." The Proposed Regulation, however, does not provide any further information regarding the treatment of the "uncollected amounts" from § 95205(a) and leaves many unanswered questions. For example, will the amounts accrue in future years, and the total amount be collected from the compliance entity once the amount reaches more than $50? Will the uncollected amount pursuant to this section be deemed a "shortfall" in future years (see § 95203(5)) and added to the obligation of compliance entities paying more than $50 per year in fees? The treatment of the amounts not collected under this section need to be addressed with certainty, as they impact the obligations of the entities at issue, as well as all other compliance entities.

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may change. For the average stakeholder – even sophisticated businesses – the opportunity for meaningful participation in the budget review process of any one agency, let alone at the legislature – is non-existent. Accordingly, those that will be burdened with the requirement to pay the Fee will have no opportunity to provide meaningful input on the amount of the Fee.

8 Likewise, note that § 95207(b) also imposes further "guarantor" obligations on compliance entities.

F. The Provisions for Reporting in the 15-Day Language Should Reflect the Effective Date of the Regulation and the Obligations Under the Existing Mandatory Reporting Regulations.

The 15-Day Language proposes revisions to § 95204(c) that require submission of reported data by March 1, 2010. Since the regulation is not yet effective, the addition of retroactive dates does not add anything to the regulation. Rather, the Regulation should be revised to reflect the deadlines for all future reporting. Additionally, the Regulation should make it clear that the data used for the calculation of the Fee is reported to CARB in once place – namely under the Mandatory Reporting Regulation (commencing with § 95100 of CCR Title 17).

G. The 15-Day Language Does not Clarify Procedures for Enforcement Actions and Imposition of Penalties.

<u>Provisions Should be Added to Address Resolution of Disputes and Clarification of Late Fees</u>. The 15-day Language fails to address the deficiencies indentified with regard to the May 2009 daft of the Proposed Regulation regarding the lack of provisions for timely review of potentially disputed amounts owed. A new section should be included to provide for a procedure for addressing disputed amounts. Likewise, the amount of the late fee referenced in § 95205(d) must be more clearly defined. Affected entities must have clarity regarding what the Board's "additional expenses incurred by the entity's untimely payment" may be. See NCPA June 24, 2009 Comments, pp.8-9.

H. The Proposed Regulation Should Address Future Funding Sources for the Fee.

Although not addressed directly in the Proposed Regulation, the issue of funding the administrative costs associated with AB32 should be reviewed when and if the State adopts a cap-and-trade program. Accordingly, the regulation itself should clarify that the Fee proposed therein will only be an interim funding measure, and that the Fee will be revised to ensure that there is no duplication in collection, and to determine if the Fee should be adjusted, reduced, or eliminated in its entirety with the implementation of the proposed cap-and-trade program. Since it is anticipated that the cap-and-trade program will generate revenue for the State, consideration should be given to utilizing some of those revenues to fund the implementation of AB 32, and eliminate the Fee. (See NCPA June 24, 2009 Comments, p. 9)

I. The Proposed Regulation Should be Updated to Address the Use of Regional Emissions Factors.

In § 95203(b), the Regulation calls for the calculation of the Fee on unspecified resources based on an emissions factor for unspecified sources. The use of default emissions factors could penalize certain entities and not accurately reflect the true carbon content of the imported electricity. Accordingly, the Regulation should provide for the use of a regional emissions factor, and should track the discussions and progress before the Western Climate Initiative regarding the use of regional emissions factors that are designed to address this very concern. (See NCPA June 24, 2009 Comments, p. 6 and NCPA September 2, 2009 Comments, p. 2)

III. CONCLUSION

NCPA appreciates the opportunity to submit these additional comments to CARB and urges the careful review and consideration of the points raised herein. If you have any questions regarding these comments, please do not hesitate to contact the undersigned or Scott Tomashefsky at 916-781-4291 or scott.tomashefsky@ncpa.com.

Sincerely,
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