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OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	Rulemaking R.06-04-009

CEC Docket no. D.07-OIIP-01

COMMENTS OF THE GREEN POWER INSTITUTE ON THE MARKET ADVISORY COMMITTEE REPORT

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Introduction

Pursuant to the July 19, 2007, *Administrative Law Judge's Ruling Requesting Comments and Legal Briefs on Market Advisory Committee Report and Notice of En Banc Hearing*, in R.06-04-009, the **Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies**, the Green Power Institute (GPI) respectfully submits these *Comments of the Green Power Institute on the Market Advisory Committee Report*. Our Comments focus on the issue of implementing the AB 32 program for the electric utility sector as a load-based program, or whether to pursue the Market Advisory Committee's "first seller" approach.

In its landmark Decision in the then-current general procurement proceeding on greenhouse gas incentives, D.06-02-032, the Commission made the threshold determination to pursue a greenhouse gas reduction program within the context of general utility procurement, and further adopted a load-based approach to implementing the program. The recently released report of the Market Advisory Committee recommends a different approach, the first-seller model, which is a variation of a source-based regulatory program. The issue of load-based vs. source-based regulation of electric-sector greenhouse gases was a major issue of contention at the recent (April) series of workshops in this joint PUC / CEC proceeding. The OIR for this proceeding has been amended to reopen the question of load-based vs. source-based, and the ALJ's *Ruling* makes this issue the centerpiece of this set of *Comments* and *Reply Comments*.

The ALJ's *Ruling* asks for a great deal of detailed information on a variety of complex topics, all to be delivered within 2½ weeks of the issuance of the *Ruling*. Given the circumstances, we are able to offer only limited *Comments* on the matters at hand. We assume that the Commission is well aware that a full record on this topic cannot be

amassed in less than a month, and that a good deal of valuable deliberation is likely to follow the En Banc Hearing scheduled for later this month. We offer these *Comments* with the understanding that this is simply an early opportunity for parties to offer preliminary comments, not the final word.

The GPI's overall reaction to the framing of the issues in the ALJ's *Ruling Requesting Comments* is similar to our reaction to the framing of the issues in the recently commented-on *Joint California Public Utilities Commission and California Energy Commission Staff Proposal for an Electricity Retail Provider GHG Reporting Protocol* in this proceeding. In our opinion, the framing of the issues in the *Ruling* is too narrowly focused on California, and fails to anticipate the burgeoning regional context in which future efforts to reduce greenhouse gases will occur. While it is true that the requirements of AB 32 are memorialized in California statute and must be enforced, regardless of whether, or the extent to which our neighbors join in, it is not necessary to focus on this eventuality as a likely outcome. On the contrary, we believe that future planning for AB 32 compliance should be based not only on anticipating, but on actively promoting a cooperative regional approach to all aspects of the program, while taking care of California's particular interests and needs.

Load-Based vs. Source-Based

The GPI's message at the April workshops, and our message here, is that load-based vs. source based regulation may not be the most important question that needs to be settled quickly in order to design an effective program for reducing the greenhouse gas emissions associated with electricity production. In our opinion, the more important threshold issues that need to be addressed are:

- Allocation and distribution of emissions allowance rights
- Tracking and trading rules for emissions liabilities and emissions allowances
- Compliance and enforcement rules

Indeed, the adoption of flexible trading rules for both emissions allowances and emissions liabilities can blur the distinction between a load-based regulatory system and a source-

based system. Any successful greenhouse gas reduction program will have to be able to link emissions allowances to emissions liabilities. Emissions arise with the generator, while allowances are the creation of the regulator, and may be fed into the system in a variety of ways (bureaucratic distribution with or without fees, auctions of various kinds) and places (retail seller, generator, open auction). Ultimately, each unit of emissions will have to be matched with an allowance and retired together permanently from the tracking system. There will have to be consequences for parties who end up with emissions liabilities for which there are no matching allowances.

Emissions liabilities can be linked to their underlying energy and tracked from the generator to the retail seller, or they might be decoupled from the energy, allowing generators and marketers to deal with their energy products and emissions liabilities as separate commodities. Similarly, allowances might be tradable among retail sellers, or they might be tradable among all market participants. In the latter case, for example, a generator might have the option of purchasing some amount of allowances in order to eliminate some or all of the carbon content of the electric product he offers on the market, allowing him to offer a cleaner product to potential customers at a higher cost. By allowing forward trading of emissions allowances, and decoupled trading of emissions liabilities, there is little difference between a load-based system and a source-based system like the first seller approach recommended by the Market Advisory Committee.

The load-based model involves tracking emissions liabilities from the generator to the retail provider, who is obligated to acquire sufficient allowances to retire its amassed liabilities. The source-based model requires generators to obtain sufficient allowances to retire their individual emissions, regardless of where or how the allowances are fed into the market. The load-based model is predicated on retail sellers being able to adjust their supply portfolios as the quantity of available allowances decreases. Programmatic costs are incurred by the retail seller, who procures lower-carbon, but presumably higher-cost resources. By way of contrast, in the source-based model increasing costs for obtaining increasingly rare allowances are incurred by the generators of greenhouse gases, who pass these costs on to their power customers. In many ways the source-based model is similar

to a carbon-tax based system, in which costs are assessed directly to the greenhouse gas emissions associated with energy generation. In this model retail providers find their carbon-intensive resources becoming increasingly expensive, and presumably switch to cleaner resources, which are now the cheaper alternative. Either way, the retail seller's cost of procurement will increase by whatever difference there is between today's costs of fossil-fuel generated electricity, in which carbon intensity is neither valued nor penalized, and the cost of the low-carbon or carbon-free electricity and efficiency that replaces it.

Treatment of Emissions from Electricity Imports

The source-based approach to regulating electric-sector greenhouse gas emissions has one distinct advantage over the load-based approach: It does not require the tracking of emissions liabilities, as they are retired at their point of generation. However, the source-based approach also has a distinct drawback: It does not work very well at all for power that is imported into the regulated jurisdiction. The Market Advisory Committee report addresses this problem by proposing the "first seller" variation of a source-based system. In the first-seller approach imported power is handled by applying the regulation directly to the importer, rather than tracing it to its source, the generator. However, most imports of electricity into California are from unspecified sources, and if regionally-determined fixed emissions factors are applied to such imports a considerable loophole is created, as emissions allowance requirements for this power are no longer directly coupled to their source.

The great Achilles heal of the Market Advisory Committee's first seller approach is imported energy. Some twenty to thirty percent of California's electricity supply is imported from out-of-state, and in the first-seller approach the agent delivering power into the state is responsible for the emissions liabilities associated with that power. It is important to keep in mind that almost all of the coal-fired electricity used in California is generated outside of the state and imported. Thus, the treatment of imported power in the first-seller approach determines how AB-32 will handle coal. If fixed emissions factors apply, carbon laundering would likely become a significant cottage industry. Any

approach to greenhouse regulation under AB-32 will benefit from regional, national, and international application. Source-based regulation, however, is particularly dependent on sufficiently broad application that there is little importing or exporting of power outside of the jurisdictional reach. Indeed, one of the reasons that the Commission adopted the load-based approach in D.06-02-032 is because it was anticipating implementation only within its own jurisdictional boundaries, and in a system with significant amounts of imports and exports, the load-based approach is clearly superior.

Renewable Resources

Decision D.07-01-039 in this proceeding implementing the Emissions Performance Standard for the procurement of new baseload electricity found that renewable energy generation produces no or very low levels of greenhouse gas emissions, or in the case of bioenergy actually reduces greenhouse gas emissions by eliminating higher-emitting alternative waste disposal practices. The material supporting these findings is already part of the record of this proceeding, and should continue to be used here. The two largest existing greenhouse gas reporting systems, RGGI and the European Union, track only greenhouse gases produced by fossil fuel use. Biogenic carbon emissions are not tracked by these systems. The ARB's proposed reporting protocols will track both fossil and biogenic carbon emissions, but the two will be considered as separate categories, and only fossil carbon emissions will be have to acquire allowances in order to be retired.

Within this framework, we propose that renewable energy generators should be considered zero emitters of greenhouse gases for purposes of AB 32 compliance, with the exception that emissions liabilities should be charged for the use of fossil fuels by renewables generators, such as is common practice in the solar-thermal generating industry. For biomass and biogas generators who produce fuel-related greenhouse gas reductions, such offsets should be allowable to the extent that they are demonstrable. Offsets would be equivalent to allowances insofar as they could be used to retire emissions liabilities.

Compatibility Issues

From a technical perspective, all greenhouse gas emissions are the same regardless of their source. In other words, a ton of fossil CO_2 emitted from a power plant has exactly the same climate effect as a ton of fossil CO_2 emitted from a car. In order to create an economically efficient mechanism to reduce overall greenhouse gas emissions, it is essential that emissions liabilities from the electric sector be fully compatible with and tradable with emissions liabilities from all other sectors. AB 32 calls for overall emissions reductions—it does not specify any sector-specific reductions. If the emissions liabilities and allowances used for regulating electric-sector emissions are not fully compatible with those used in other sectors, that would constitute a de facto sector-specific regulation that is contrary to the spirit of AB 32.

Conclusion

The Green Power Institute cautions the Commission against precipitously jumping from the current pathway towards launching a load-based greenhouse gas reduction program for the electric utility sectors, in favor of adopting the Market Advisory Committee's first-seller approach. Until a regional approach to greenhouse gas regulation is assured, the load-based approach offers California the best chance to minimize the risks of program manipulation that are associated with imported power.

Dated August 6, 2007, at Berkeley, California.

Respectfully Submitted,

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PROOF OF SERVICE

I hereby certify that on August 6, 2007, I have served a copy of the COMMENTS OF THE GREEN POWER INSTITUTE ON THE MARKET ADVISORY COMMITTEE REPORT upon all parties listed on the Service List for this proceeding, R-06-04-009. All parties have been served by email or first class mail, in accordance with Commission Rules.

Gregory Morris