The Business Council for Sustainable Energy

April 16, 2008

To: **Western Climate Initiative Allocations Subcommittee**

Regarding: **BCSE Comments on WCI Draft Allocation Design Recommendations**

Submitted Via: **WCI Website**

On behalf of the members of the Business Council for Sustainable Energy (the Council), we appreciate the opportunity to provide comments on the Western Climate Initiative (WCI) draft Allocations Design Recommendations for WCI's greenhouse gas cap-and-trade system. The Council looks forward to working with WCI and, in particular, the Allocations Subcommittee, as you further develop the program design. We remain available to discuss our recommendations in further detail.

Introduction

The Business Council for Sustainable Energy is a broad-based coalition of energy efficiency, natural gas and renewable energy industries that advocates energy and environmental policies that promote markets for clean, efficient and sustainable energy products and services. The Council's coalition includes power developers, equipment manufacturers, independent generators, green power marketers, retailers, and gas and electric utilities, as well as several of the primary trade associations in these sectors. We have several members who are based in the WCI region as well as others that are very active in the region's markets and clean energy activities including Sempra Energy, PG&E, PPM Energy, SMUD, First Environment, Inc., GE Wind, Calpine, 3 Degrees, Enel North America, and Solar Turbines.

The Council and its members have been working consistently with state, federal and international policymakers on market-based measures to reduce greenhouse gas emissions since its inception in the early 1990s. The Council was the first industry coalition to support a binding multilateral regime to address climate change. The coalition supports the establishment of market-based programs for clean energy technology innovation, economic efficiency and enhanced energy security. We view the WCI cap-and-trade program as an important vehicle to reduce greenhouse gas emissions in the western region.

BCSE Position Regarding the Draft Allocation Design Recommendations

The following comments address the Council's positions regarding the WCI Draft Allocation Design Recommendations and build upon comments previously provided by the Council to WCI in November 2007 and February 2008 (see BCSE at http://www.westernclimateinitiative.org/view_comments.cfm).

In general, the Council would like to reaffirm its view that the WCI cap-and-trade program should base allocation methods on performance to provide value to energy efficiency, renewables and cleaner generation. The Council strongly supports an output-based methodology that would distribute allowances based on the amount of electricity generated, not on the amount of fuel used or historic emissions. With this focus on output over emissions, energy efficiency, carbon efficiency and cleaner generation sources – including renewable energy – are directly encouraged. The Council recommends a fuel-neutral, updating, output-based allocation. Output-based policies send a clear signal to the marketplace – lower-carbon emitting energy options receive direct, clear, consistent and bankable value.

In addition to these overarching views, the Council respectfully submits the following comments on specific draft allocation design recommendations:

The Draft Allocations Design Recommendations Should be Amended to Include a Renewable Energy Set Aside

BCSE encourages the WCI to amend the Draft Allocations Design Recommendations to incorporate a set-aside for renewables, energy efficiency and cleaner generation to allow for competition and ensure a level playing field for new

entrants. New entrants in the marketplace should be eligible to receive allowances so they are not put in a position of competitive disadvantage.[1]

BCSE recommends set-aside allowance pools for: 1) small and clean generators; 2) energy efficiency projects; and 3) new entrants, as a means to allocate allowances directly to clean generation and energy efficiency that would otherwise not be included under the primary source allocation. In the context of the Regional Greenhouse Gas Initiative (RGGI) in the northeast states, the Council has encouraged set-aside pools for small, clean generation (under 25MW). The RGGI model rule does, in fact, include a voluntary renewable energy set-aside and several RGGI states have adopted allocation models that direct significant value to renewables, energy efficiency and cleaner generation. For example, Connecticut has created a distinct set-aside pool for combined heat and power to receive five percent of the state's allowances, with a consumer-side distributed resources set-aside of three percent, while renewables will receive approximately 23 percent of auction revenue and energy efficiency will receive approximately 69 percent of auction revenue (with the auction representing 91 percent of CT's allowances). New York will direct 100 percent of its auction revenue toward renewables and energy efficiency.

BCSE is concerned that the Draft Design Recommendations do not mention renewable energy, the voluntary market, or any sector-specific set-aside. BCSE believes there is wide spread support for a renewable energy set aside and strongly encourages the WCI Allocations Subcommittee to incorporate a set aside into the design of the program. The Council further encourages WCI Partners to avoid the use of a hard cap on voluntary renewable energy set-aside pools. Rather the Council recommends that the credits retired through such set-asides be allowed to grow in proportion to the size of the state's/province's voluntary market.[2 & 3]

Distribution of Allowances by Partners

The Council has not taken a position on whether allowances should be distributed centrally, or by individual WCI partners, or by some combination thereof. We support a distribution system that is consistent, transparent, highly efficient, and meets the needs of the individual WCI partners as pertains to their respective generation and emissions profiles, keeping in mind the region's goals to considerably increase the use of renewable generation, energy efficiency and cleaner generation.

Establishment of Cap and Trade Partner Budgets and Partners' Initial Allowance Budgets

The Draft Allocations Design Recommendations establish a regional cap that will decline over time, and each Partner will have an allowance budget within the cap.

BCSE recommends that WCI's allocation budgets be designed to send strong price and low-carbon technology deployment signals to the market. The Council believes the WCI should adopt a fuel-neutral, output-based methodology to distribute allowance value according to the amount of electricity generated by a covered entity, not the amount of fuel used or historic emissions. By basing allocation methods on performance, WCI will provide value to energy efficiency, renewables and cleaner generation, thereby reducing compliance costs, mitigating fuel price increases and achieving the

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[1] For example, the federal set-aside program under the Clean Air Planning Act introduced by Senator Thomas Carper (D-Delaware) was included to avoid the situation where a generator of new, clean and efficient energy would have to purchase allowances from an existing competitor.

[2] As an example, the Council and the Renewable Energy Marketing Association (REMA) recently suggested that New York adopt a sound approach to managing a voluntary renewable energy set-aside account by starting with an initial allocation of allowances based on a percentage of overall allowances (in NY's case, one percent) and subsequently truing-up the account in the following year, based on actual sales. This will ensure that customers in a given state/province who purchase renewable energy through the voluntary market are indeed receiving the environmental benefits they have sought to buy. Further, generation from renewables and combined heat and power via the customer-driven voluntary market benefits state economic interests and all ratepayers, as capital costs for the additional generation are borne by the customer.

[3] For further discussion of a Voluntary Renewable Energy Set-Aside for WCI, please see comments filed to the WCI Allocations Subcommittee by REMA on February 1, 2008.

complementary objective of enhanced energy security. In addition, should WCI pursue an approach that grants allocation to load-serving entities on behalf of their customers, then this approach should also follow an output or sales methodology and be adjusted upward for energy efficiency savings. This allocation methodology will help to distribute allowance value to customers who will likely bear a significant burden through increased energy prices.

Establishment of Cap and Trade Partner Budgets and Distribution of Allowances by Partners

The Draft Recommendations state that:

> Once the allowance budget has been established for each Partner, allowances will be issued by each Partner rather than issued by a regional organization. Through mutual reciprocal recognition by the Partners allowances will be of equivalent use and value through the WCI region, regardless of which Partner issues the allowances. (page 3)

BCSE believes that WCI Partners have the opportunity to create a cap-and-trade program that serves as a model for a future federal program; consistency and market certainty are critical ingredients for a successful program. Therefore, the Allocations Subcommittee should adopt one standard allocation methodology based on a MWh output-based cap and allowance allocation.

Minimum Auction Percentage and Phased Increase of Auctioning

BCSE supports a direct allocation of allowances on a fuel neutral, output basis; however, if the WCI Partners intend to auction of a percentage of their allowance budgets, the Council supports a phase-in period to minimize potential economic impacts on affected sources. BCSE believes that a mixed allowance/auction approach with a phase-in period for the auction would minimize possible dramatic economic impacts that a large-scale auction might have on affected sources in the initial phases of the program. Further, the Council strongly recommends the targeted use of auction revenue to reduce program costs by driving clean energy technology investment and deployment. For example, New York has decided to dedicate 100 percent of auction revenue under its RGGI program to investment in energy efficiency and renewable energy, and the Council strongly supports New York's action as a model for WCI and other states that are considering auctions. Further, this approach is consistent with the Market Advisory Committee's recommendation that California use a portion of the allowance value created under a cap-and-trade program to promote investment in low-greenhouse gas technologies and fuels, including energy efficiency.[4]

Council members believe that any auction revenue should be directed toward expanding renewable energy generation and energy efficiency. This is why criteria for the use of auction revenue under the WCI cap-and-trade program are of great importance. The Council believes that auction revenue should:

1. Reduce the carbon intensity of electric generation
2. Reduce energy demand
3. Provide benefit to the western region's economy
4. Promote private investment through partial funding of investments
5. Enhance complementary energy program benefits
6. Help establish new energy programs
7. Increase the market potential of new technologies

Credits for Early Reductions

As outlined in the Council's November 2007 comments, BCSE strongly recommends that the WCI cap-and-trade program should be designed to promote early action, recognizing early investments in greenhouse gas reductions. Rewarding emission reductions that occur in advance of the enactment of the program has the potential to generate economic and environmental benefits, as well as hasten clean energy technology deployment. The Council encourages WCI to adopt simple and transparent early action program credits to ensure robust participation by interested companies. This could be

[4] *Recommendations for Designing a Greenhouse Gas Cap-and-Trade System for California*, Recommendations of the Market Advisory Committee to the California Air Resources Board, June 30, 2007, p. 60.

accomplished through a specific early-action set-aside within the WCI program. Alternatively, early actors could receive allowance value by a methodology utilized by RGGI that goes over and above the cap. Further, the Council urges the WCI Partners to consider an early action program that may include offsets from other regulatory offset schemes and/or high-quality voluntary schemes.[5]

Banking

The Council supports the WCI provisions to allow banking of allowances without restrictions on the amount of allowances that may be banked or for how long. The Council believes that banking can be a mechanism for providing flexibility into the program and can be an important driver to send signals to the market to make early reductions and investments in energy efficiency and renewable generation.

Conclusion
Thank you for the opportunity to provide on the Western Climate Initiative Draft Allocations Design Recommendations.

If you have any questions or comments please feel free to contact me at (202) 785-0507 or via email at ljacobson@bcse.org.

Sincerely,

Lisa Jacobson
Executive Director

CC: Patrick Cummins, WCI

[5] Early action programs such as those supported by state public utility commissions and other regulatory agencies (i.e., The Climate Trust in Oregon and PG&E's ClimateSmart™ program in California).