February 1, 2008

To: **Western Climate Initiative Allocations Subcommittee**

Regarding: **BCSE Recommendations on WCI Allocation Design Issues**

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) program questions for designing an allocation system 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 move forward with program design. We remain available to discuss our recommendations in further detail and specifically request the opportunity to meet with the Allocations Subcommittee chair in the coming weeks.

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 Recommendations on Allocation Design Issues

The following comments address recommendations on specific program design questions under consideration by the Allocations Subcommittee, building upon comments previously provided by the Council to WCI in November 2007 (see BCSE at http://www.westernclimateinitiative.org/view_comments.cfm):

1. *a) Should allowances be distributed centrally, without apportionment to Partners? or, b) Should allowances be apportioned to, and distributed by Partners individually? or, c) Should some combination of centralized distribution and apportionment be pursued?*

The Council does not take a position on whether allowances should be distributed centrally, or by individual WCI partners, or by some combination thereof. We urge the subcommittee to develop 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.

2. *a) Assuming allowances are distributed by Partners, should distribution methods be standardized? or b) Assuming allowances are distributed by Partners, should distribution methods be left to each jurisdiction to decide? or, c) Should*

some flexibility be allowed within prescribed limits beyond which all Partners must adopt the same distribution system?

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 whether there is a centralized or decentralized allocation, based on a MWh output-based cap and allowance allocation.

3. *a) Assuming there is centralized distribution or at least partial standardization of decentralized distribution, should some of the allowances be distributed directly to covered entities free-of-charge? or, b) Assuming there is centralized distribution or at least partial standardization of decentralized distribution, should some or all of the allowances be auctioned or otherwise sold?*

The Council recommends that WCI's allocation approach be designed to send strong price and low-carbon technology deployment signals to the market. Should WCI decide to allocate allowances for free, it 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 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.

In addition, WCI should consider creating distinct set-aside allowance pools for 1) small and clean generators; 2) energy efficiency projects; and 3) new entrants. This can be accomplished through upfront, direct allowance value; alternatively, WCI could adopt a model with distinct set-aside pools for auction revenue, should WCI pursue an auction. Several states in the Regional Greenhouse Gas Initiative (RGGI) 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 CT'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.

Further, if WCI does not grant renewable energy generators allowance value (as previously suggested under a fuel-neutral, output-based allocation methodology), then WCI should consider creating a distinct set-aside pool for the Voluntary Renewable Energy Market. Several RGGI states, including Connecticut, Massachusetts, and New York, have dedicated one percent of allowances to Voluntary Renewable Energy Market Set-Aside Accounts. The Council further encourages WCI and RGGI states 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.[1 & 2]

c) Should the allowance distribution system have the capacity to change over the life of the program through phasing in particular distribution methods or using different distribution bases?

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[1] 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.

[2] 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.

If WCI pursues an auction, WCI Partners should consider a phase-in period to minimize potential economic impacts on affected sources. Again, the Council strongly recommends the use of a fuel-neutral, output-based allocation methodology if allowances are distributed for free.

d) Should the Partners place restrictions on the use of revenues from auctioned allowances?

Partners should establish clear criteria for the direction of auction revenue to send consistent signals to the market and increase regional use of renewables, energy efficiency and cleaner generation. Should WCI pursue an auction, WCI Partners should strive for transparency and consistency in the use of auction revenue in their respective states/provinces and across the region as a whole. As outlined in the Council's previous comments to WCI in November 2007, the Council believes that the use of auction revenue should adhere to the following criteria:

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

4. *a) The WCI Design Principles state that the program will "provide appropriate recognition and incentives for early emissions reductions." Should the program accomplish this: 1) Through the selection of benchmarking and program start dates? 2) Through special allocations of allowances drawn from within the cap or drawn from outside the cap? 3) Through auctioning of allowances? Or 4) By other means?*

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 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.[3]

Conclusion

Thank you for the opportunity to provide recommendations to the Western Climate Initiative Allocations Subcommittee.

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

[3] Early action programs such as those supported by state public utility commissions and other regulatory agencies (i.e., The Climate Trust in Oregon).