

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

DOCKET 07-OIIP-1	
DATE	NOV 14 2007
RECD.	NOV 14 2007

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

R. 06-04-009

**REPLY COMMENTS OF THE WESTERN POWER TRADING FORUM
ON ALLOWANCE ALLOCATION ISSUES**

Clare Breidenich
224 ½ 24th Avenue East
Seattle, Washington 98112
Telephone: (206) 829-9193
Email: clare@wptf.org
GHG Consultant

Daniel W. Douglass
DOUGLASS & LIDDELL
21700 Oxnard Street, Suite 1030
Woodland Hills, California 91367
Telephone: (818) 961-3002
Facsimile: (818) 961-3004
Email: douglass@energyattorney.com

Attorneys for the
WESTERN POWER TRADING FORUM

November 14, 2007

**BEFORE THE PUBLIC UTILITIES COMMISSION
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.

R. 06-04-009

**REPLY COMMENTS OF THE WESTERN POWER TRADING FORUM
ON ALLOWANCE ALLOCATION ISSUES**

I. Introduction

In accordance with the direction provided in the October 15th, 2007, Administrative Law Judge's Ruling under Rulemaking 06-04-009, the Western Power Trading Forum ("WPTF") respectfully submits the following reply comments regarding distribution of allowances under a greenhouse gas (GHG) emission trading program for the electricity sector.

WPTF notes that many Parties to this proceeding, notably the investor-owned utilities and environmental and public interests organizations, advocate full auction of allowances under a first-seller cap and trade system, with auction revenue to be distributed to load-serving entities. Further, Pacific Gas and Electric and Southern California Edison support allocation of allowances directly to LSEs for subsequent sale to first-sellers. WPTF has substantive concerns with these recommendations:

- An initial 100% auction of allowances under a first seller approach would create unreasonable economic harm for generators and the potential for stranded costs. WPTF advocates administrative allocation as the principle

means of distributing allowances in the early years of the trading system, combined with a gradual phase-in of allowance auctioning

- Allocation of allowances to retail providers under a first-seller approach would be inherently unfair to independent power producers and power markets.

We address these two concerns in our comments below.

II. Auction of 100% of Allowances Initially Under a First-Seller Approach Would Cause Undue Economic Harm to Generators and Could Result in Stranded Costs.

Many parties cite the potential for windfall profits to electric generators under administrative allocation as a principle concern and recommend auction of allowances to eliminate the potential for these profits. The potential for windfall profits to electric generators is overstated and does not justify immediate full auction of allowances.

Under an auction, the ability of a generator to recover its compliance costs depends on its ability to pass 100% of the allowance price for each MWH through in market electricity prices. But market prices are a function of many factors – gas prices, load, expected load, availability of generation, weather, and transmission constraints, to name a few. Because the carbon cost (i.e. allowance price) is just one factor of many affecting market prices, it should not be assumed that generators will be able to completely pass through this cost.

Costs to fossil generators under a GHG cap will be significant and are not likely to be completely compensated by increased revenues. Fossil generators face a real risk of loss of investment value due to GHG regulation, particularly in the early years of a trading system. These lost profits are in effect stranded costs, and should be compensated through initial administrative allocation of allowances.

Many studies have attempted to quantify the profits lost to fossil generators under GHG regulation, and thus the quantity of allowances needed to compensate for the loss of investment value. While these estimates vary depending on assumptions regarding competition, allowance prices and the ability to pass through allowance prices, they are typically in the range of 35 – 50%.¹ When the effect of carbon prices on individual firms is considered, the proportion of allowances that must be freely allocated to compensate adversely affected firms rises to 70 – 100%.² Further, studies that have looked at the quantity of allowances needed if the period of compensation is temporary – as would occur under a transition to auctioning of permits – have concluded that a much higher proportion of allowances must be administratively allocated than if the allocations occurred in perpetuity.

WPTF agrees that a well-designed GHG cap and trade system should change the economics of generator dispatch and investment in favor of cleaner generation. A distribution approach that begins with administrative allocation and gradually transitions to auctioning would reduce the risk of stranded costs because it allows for generators to plan for compliance with GHG caps and accommodate natural capital stock turn-over. Additionally, such an approach would minimize any windfall profits that may occur to fossil generators because generators would be required to purchase allowances in the later years of the trading system.

¹ See for instance, “Allocating Allowances in a Greenhouse Gas Trading System”, National Commission on Energy Policy, 2007 and “Simple Rules for Targeting CO₂ Allowance Allocations to Compensate Firms,” Palmer, Karen, Burtraw, Dallas and Kahn, Danny, 2006.

² For a review of existing studies on the economic impacts of GHG trading systems for the electricity sector, see “Complexities of Allocation Choices in a Greenhouse Gas Emissions Trading Program,” Harrison, David, Jr., Klevnas, Per; Radov, Daniel; and Foss, Andrew prepared for the International Emissions Trading Association. 2007.

For these reason, WPTF advocates administrative allocation of allowances as the principal means of distribution during the initial years of a cap and trade system, with a gradual transition to auctioning over time.

III. Allocation of Allowances to Load-Serving Entities Under a First-Seller Approach would Unfairly Disadvantage Independent Power Producers and Power Marketers.

Under a first-seller trading system, all in-state generators and importers of power will be competing for emission allowances. To the extent that retail electricity providers own in-state generation, or import power, those entities will also be participants in the carbon market. Any distribution method that allocates allowances to retail providers for subsequent auction/sale to other market participants would be patently unfair as it would advantage retail providers over independent power producers and other marketers.

Further, allocation of allowances to retail providers under a first-seller approach would create an unacceptable risk of market power, as a high proportion of the allowances would be held by a small number of large investor-owned and public utilities.

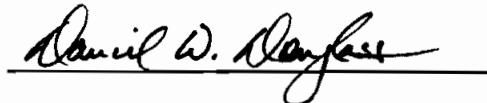
If California decides to dedicate any portion of allowance value to mitigate consumer rate impacts or to promote other GHG reduction goals, then, for the reasons stated above, it would be far preferable to distribute auction revenue to retail providers rather than actual allowances.

WPTF also notes that our concerns explained above regarding early transition to auctioning would also apply to any variant that distributes allowances to retail providers under a first-seller approach.

IV. Conclusion

WPTF appreciates this opportunity to comment and the Commission's consideration of the discussion provided herein.

Respectfully submitted,

A handwritten signature in cursive script, reading "Daniel W. Douglass", is written over a horizontal line.

Daniel W. Douglass
DOUGLASS & LIDDELL
21700 Oxnard Street, Suite 1030
Woodland Hills, California 91367
Telephone: (818) 961-3001
Facsimile: (818) 961-3004
Email: douglass@energyattorney.com

Attorneys for the
WESTERN POWER TRADING FORUM

November 14, 2007

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the **Reply Comments of the Western Power Trading Forum on Allowance Allocation Issues** on all parties of record in R. 06-04-009 by serving an electronic copy on their email addresses of record and by mailing a properly addressed copy by first-class mail with postage prepaid to each party for whom an email address is not available.

Executed on November 14, 2007, at Woodland Hills, California.



Michelle Dangot

SERVICE LIST

R.06-04-009

cadams@covantaenergy.com
steven.schleimer@barclayscapital.com
steven.huhman@morganstanley.com
rick_noger@praxair.com
keith.mccrea@sablax.com
ajkatz@mwe.com
ckrupka@mwe.com
lisa.decker@constellation.com
cswoolums@midamerican.com
kevin.boudreaux@calpine.com
trdill@westernhubs.com
ej_wright@oxy.com
pseby@mckennalong.com
todil@mckennalong.com
steve.koerner@elpaso.com
jenine.schenk@apses.com
jbw@slwplc.com
kelly.barr@srpnet.com
rrtaylor@srpnet.com
smichel@westernresources.org
roger.montgomery@swgas.com
Lorraine.Paskett@ladwp.com
ron.deaton@ladwp.com
snewsom@semprautilities.com
dhuard@manatt.com
curtis.kebler@gs.com
dehling@kling.com
gregory.koiser@constellation.com
npedersen@hanmor.com
mmazur@3phasesRenewables.com
vitaly.lee@aes.com
tiffany.rau@bp.com
klatt@energyattorney.com
rhelgeson@scppa.org
douglass@energyattorney.com
pssed@adelphia.net
akbar.jazayeri@sce.com
annette.gilliam@sce.com
cathy.karlstad@sce.com
Laura.Genao@sce.com
rkmoore@gswater.com
dwood8@cox.net
amsmith@sempra.com
atrial@sempra.com
apak@sempraglobal.com
dhecht@sempratrading.com
daking@sempra.com
svongdeuane@semprasolutions.com
troberts@sempra.com

liddell@energyattorney.com
marcie.milner@shell.com
rwinthrop@pilotpowergroup.com
tdarton@pilotpowergroup.com
lschavrien@semprautilities.com
GloriaB@anzaelectric.org
llund@commerceenergy.com
thunt@cecmail.org
diane_fellman@fpl.com
jeanne.sole@sfgov.org
john.hughes@sce.com
llorenz@semprautilities.com
marcel@turn.org
nsuetake@turn.org
dil@cpuc.ca.gov
fjs@cpuc.ca.gov
achang@nrdc.org
rsa@a-klaw.com
ek@a-klaw.com
kgrenfell@nrdc.org
mpa@a-klaw.com
sls@a-klaw.com
bill.chen@constellation.com
bkc7@pge.com
epoole@adplaw.com
agrimaldi@mckennalong.com
bcragg@goodinmacbride.com
jsqueri@gmssr.com
jarmstrong@goodinmacbride.com
kbowen@winston.com
lcottle@winston.com
sbeatty@cwclaw.com
vprabhakaran@goodinmacbride.com
jkarp@winston.com
jeffgray@dwt.com
cjw5@pge.com
ssmyers@att.net
lars@resource-solutions.org
alho@pge.com
aweller@sel.com
jchamberlin@strategicenergy.com
beth@beth411.com
kerry.hattevik@mirant.com
kowalewskia@calpine.com
wbooth@booth-law.com
hoerner@redefiningprogress.org
janill.richards@doj.ca.gov
cchen@ucsusa.org
gmorris@emf.net

tomb@crossborderenergy.com
kjinnovation@earthlink.net
bmcc@mccarthyaw.com
sberlin@mccarthyaw.com
Mike@alpinenaturalgas.com
joyw@mid.org
UHelman@caiso.com
jjensen@kirkwood.com
mary.lynch@constellation.com
lrdevanna-rf@cleanenergysystems.com
abb@eslawfirm.com
mclaughlin@braunlegal.com
glw@eslawfirm.com
jluckhardt@downeybrand.com
jdh@eslawfirm.com
vwelch@environmentaldefense.org
www@eslawfirm.com
westgas@aol.com
scohn@smud.org
atrowbridge@daycartermurphy.com
dansvec@hdo.net
notice@psrec.coop
deb@a-klaw.com
cynthia.schultz@pacificorp.com
kyle.l.davis@pacificorp.com
ryan.flynn@pacificorp.com
carter@ieta.org
jason.dubchak@niskags.com
bjones@mjbbradley.com
kcolburn@symbioticstrategies.com
rapcowart@aol.com
Kathryn.Wig@nrgenergy.com
sasteriadis@apx.com
george.hopley@barcap.com
ez@pointcarbon.com
burtraw@rff.org
vb@pointcarbon.com
kyle_boudreaux@fpl.com
andrew.bradford@constellation.com
gbarch@knowledgeinenergy.com
ralph.dennis@constellation.com
smindel@knowledgeinenergy.com
brabe@umich.edu
bpotts@foley.com
james.keating@bp.com
Cynthia.A.Fonner@constellation.com
jimross@r-c-s-inc.com
tcarlson@reliant.com
ghinners@reliant.com

zaiontj@bp.com
julie.martin@bp.com
fiji.george@elpaso.com
echiang@elementmarkets.com
fstern@summitblue.com
nenbar@energy-insights.com
nlenssen@energy-insights.com
bbaker@summitblue.com
william.tomlinson@elpaso.com
kjsimonsen@ems-ca.com
Sandra.ely@state.nm.us
bmcquown@reliant.com
dbrooks@nevp.com
anita.hart@swgas.com
randy.sable@swgas.com
bill.schrand@swgas.com
jj.prucnal@swgas.com
sandra.carolina@swgas.com
ckmitchell1@sbcglobal.net
chilen@sppc.com
emello@sppc.com
tdillard@sierrapacific.com
dsoyars@sppc.com
jgreco@caithnessenergy.com
fluchetti@ndep.nv.gov
leilani.johnson@ladwp.com
randy.howard@ladwp.com
Robert.Rozanski@ladwp.com
robert.pettinato@ladwp.com
HYao@SempraUtilities.com
rprince@semprautilities.com
rkeen@manatt.com
nwhang@manatt.com
pjazayeri@stroock.com
derek@climaterestry.org
david@nemtzw.com
harveyederpspc.org@hotmail.com
sendo@ci.pasadena.ca.us
slins@ci.glendale.ca.us
thamilton5@charter.net
bjeider@ci.burbank.ca.us
rmorillo@ci.burbank.ca.us
roger.pelote@williams.com
aimee.barnes@ecosecurities.com
case.admin@sce.com
tim.hemig@nrgenergy.com
bjl@bry.com
aldyn.hoekstra@paceglobal.com
ygross@sempraglobal.com
jlaun@apogee.net
kmkiener@fox.net
scottanders@sandiego.edu
jkloberdanz@semprautilities.com
andrew.mcallister@energycenter.org

jack.burke@energycenter.org
jennifer.porter@energycenter.org
sephra.ninow@energycenter.org
dniehaus@semprautilities.com
jleslie@luce.com
ofoote@hkcf-law.com
ekgrubaugh@iid.com
pepper@cleanpowermarkets.com
gsmith@adamsbroadwell.com
mdjoseph@adamsbroadwell.com
hayley@turn.org
mflorio@turn.org
Dan.adler@calcef.org
mhyams@sfwater.org
tburke@sfwater.org
norman.furuta@navy.mil
amber@ethree.com
annabelle.malins@fco.gov.uk
dwang@nrdc.org
filings@a-klaw.com
nes@a-klaw.com
obystrom@cera.com
sdhilton@stoel.com
scarter@nrdc.org
abonds@thelen.com
cbaskette@enernoc.com
colin.petheram@att.com
jwmctarnaghan@duanemorris.com
kfox@wsgr.com
kkhoja@thelenreid.com
pvallen@thelen.com
spauker@wsgr.com
rreinhard@mofo.com
cem@newsdata.com
hgolub@nixonpeabody.com
jscancarelli@flk.com
jwiedman@goodinmacbride.com
mmattes@nossaman.com
jen@cnt.org
lisa_weinzimer@platts.com
steven@moss.net
sellis@fypower.org
arno@recurrentenergy.com
ELL5@pge.com
gxl2@pge.com
jxa2@pge.com
JDF1@PGE.COM
RHHJ@pge.com
sscb@pge.com
svs6@pge.com
S1L7@pge.com
vjw3@pge.com
karla.dailey@cityofpaloalto.org
farrokh.albuyeh@oati.net

dtibbs@aes4u.com
jhahn@covantaenergy.com
andy.vanhorn@vhcenergy.com
Joe.paul@dynegy.com
info@calseia.org
gblue@enxco.com
sbeserra@sbcglobal.net
monica.schwebs@bingham.com
phanschen@mofo.com
josephhenri@hotmail.com
pthompson@summitblue.com
dietrichlaw2@earthlink.net
Betty.Seto@kema.com
JerryL@abag.ca.gov
jody_london_consulting@earthlink.net
steve@schiller.com
mrw@mrwassoc.com
rschmidt@bartlells.com
adamb@greenlining.org
stevek@kromer.com
clyde.murley@comcast.net
brenda.lemay@horizonwind.com
carla.peterman@gmail.com
elvine@lbl.gov
rhwisner@lbl.gov
C_Marnay@lbl.gov
philm@scdenergy.com
rita@ritanortonconsulting.com
cpechman@powereconomics.com
emahlon@ecoact.org
richards@mid.org
rogerv@mid.org
tomk@mid.org
fwmonier@tid.org
brbarkovich@earthlink.net
johnrredding@earthlink.net
clark.bernier@rlw.com
rmccann@umich.edu
cmkehrlein@ems-ca.com
e-recipient@caiso.com
groenblum@caiso.com
rsmutny-jones@caiso.com
saeed.farrokhpay@ferc.gov
david@branchcomb.com
kenneth.swain@navigantconsulting.com
kdsel@navigantconsulting.com
gpickering@navigantconsulting.com
lpark@navigantconsulting.com
davidreynolds@ncpa.com
scott.tomashefsky@ncpa.com
ewolfe@resero.com
Audra.Hartmann@Dynegy.com
Bob.lucas@calobby.com
curt.barry@iwpnews.com

danskopec@gmail.com
dseperas@calpine.com
dave@ppallc.com
dkk@eslawfirm.com
wynne@braunlegal.com
kgough@calpine.com
kellie.smith@sen.ca.gov
kdw@woodruff-expert-services.com
mwaugh@arb.ca.gov
pbarthol@energy.state.ca.us
pstoner@lgc.org
rachel@ceert.org
bernardo@braunlegal.com
steven@lipmanconsulting.com
steven@iepa.com
wtasat@arb.ca.gov
etiedemann@kmtg.com
ltenhope@energy.state.ca.us
bushinskyj@pewclimate.org
lmh@eslawfirm.com
obartho@smud.org
bbeebe@smud.org
bpurewal@water.ca.gov
dmacmll@water.ca.gov
kmills@cbbf.com
karen@klindh.com
ehadley@reupower.com
Denise_Hill@transalta.com
sas@a-klaw.com
egw@a-klaw.com
akelly@climatetrust.org
alan.comnes@nrgenergy.com

lisa.c.schwartz@state.or.us
cbreidenich@yahoo.com
dws@r-c-s-inc.com
jesus.arredondo@nrgenergy.com
charlie.blair@delta-ee.com
karen.mcdonald@powerex.com
clarence.binninger@doj.ca.gov
david.zonana@doj.ca.gov
agc@cpuc.ca.gov
aeg@cpuc.ca.gov
blm@cpuc.ca.gov
cfl@cpuc.ca.gov
cft@cpuc.ca.gov
tam@cpuc.ca.gov
dsh@cpuc.ca.gov
edm@cpuc.ca.gov
cpe@cpuc.ca.gov
hym@cpuc.ca.gov
hs1@cpuc.ca.gov
jm3@cpuc.ca.gov
jnm@cpuc.ca.gov
jbf@cpuc.ca.gov
jk1@cpuc.ca.gov
jst@cpuc.ca.gov
jtp@cpuc.ca.gov
jol@cpuc.ca.gov
jci@cpuc.ca.gov
jf2@cpuc.ca.gov
krd@cpuc.ca.gov
lrm@cpuc.ca.gov
ltt@cpuc.ca.gov
mjd@cpuc.ca.gov

rmm@cpuc.ca.gov
ram@cpuc.ca.gov
smk@cpuc.ca.gov
sgm@cpuc.ca.gov
svn@cpuc.ca.gov
scr@cpuc.ca.gov
tcx@cpuc.ca.gov
ken.alex@doj.ca.gov
ken.alex@doj.ca.gov
bdicapo@caiso.com
jsanders@caiso.com
jgill@caiso.com
ppettingill@caiso.com
mscheibl@arb.ca.gov
epowers@arb.ca.gov
jdoll@arb.ca.gov
pburmich@arb.ca.gov
bblevins@energy.state.ca.us
dmetz@energy.state.ca.us
deborah.slone@doj.ca.gov
dks@cpuc.ca.gov
kgiffin@energy.state.ca.us
ldecarlo@energy.state.ca.us
mprior@energy.state.ca.us
californiadockets@pacificorp.com
Philip.H.Carver@state.or.us
samuel.r.sadler@state.or.us
pw1@cpuc.ca.gov
psp@cpuc.ca.gov
pzs@cpuc.ca.gov
kyle.silone@ecosecurities.com
ner@cpuc.ca.gov