

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

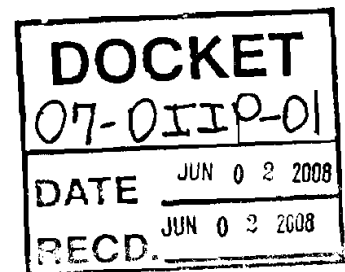
Order Instituting Rulemaking to Implement the Commission's Procurement Incentive Framework and to Examine the Integration of Greenhouse Gas Emissions Standards into Procurement Policies.	Rulemaking 06-04-009 (Filed April 13, 2006)
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BEFORE THE CALIFORNIA ENERGY COMMISSION

AB32 Implementation – Greenhouse Gas Emissions	Docket 07-OIIP-01
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**COMMENTS OF FPL ENERGY PROJECT MANAGEMENT, INC ON THE
COMBINED REQUEST FOR COMMENTS ON THE JOINT COMMISSION
STAFF PAPER ON OPTIONS FOR THE ALLOCATION OF ALLOWANCES,
FLEXIBLE COMPLIANCE MECHANISMS FOR COMPLIANCE WITH
GREENHOUSE GAS REGULATORY ACTIVITIES, THE TREATMENT OF
COMBINED HEAT AND POWER UNDER GREENHOUSE GAS PROGRAM,
AND THE CPUC ECONOMIC IMPACTS MODELING RESULTS**

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June 2, 2008

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FPL Energy Project Management, Inc. (FPLE) submits these opening comments in response to the California Public Utilities and Energy Commission's (Commissions) Rulings¹. FPLE's responses to the specific questions proposed in the referenced ALJ rulings are contained in Attachment A. The Commissions' efforts to advance California's climate change policies stand at a critical crossroads. There must be balance between impacts on the customers of both the investor-owned and municipal utilities and between a California specific approach and the ramifications for a national program. FPLE submits that the Commissions adhere to

¹ These include the April 16, 2008, May 1, 2008, May 6, 2008, and May 13, 2008 Administrative Law Judges' Rulings.

one fundamental principle: Significant greenhouse gas (GHG) reductions will not occur unless the cost of carbon emissions is calculated and realized across all sectors and for all stakeholders.

SUMMARY²

A. Allocations of allowances:

FPLE supports 100% Auction and Re-investment of Auction Revenues

In April 2008, the Commissions Staff issued a paper discussing several policy options for allocating carbon allowances for the electricity sector under a GHG cap and trade program³ (Staff Paper). The Staff Paper assesses three industry-recognized methods of allocating emissions credits as they are typically defined (“pure” forms) and evaluates each according to the established evaluation criteria⁴. In addition, the Staff Paper takes these allocation strategies and redefines each into a staff “preferred” version. The “preferred” options blend the different attributes of the “pure” methods into three new alternative allowance distribution methods. Rather than supporting one method of allowance allocation over another, FPLE will discuss the positive and negative elements within each of the “preferred” allocation methods.

² FPLE has attempted respond to the Commission’s extensive and complex questions by concise and direct responses. FPLE would welcome the opportunity to expand further on any of the positions taken in this response.

³ “Joint California Public Utilities Commission and California Energy Commission Staff Paper on Options for Allocation of GHG Allowances in the Electric Sector”, (JSPAA) R.06-04-009 and D.07-OIIP-01.

⁴ JSPAA, p2, The Commission staff evaluated each method of reducing carbon emissions using criteria stated in staff paper. These criteria include: consumer cost, equity among retail providers, simplicity, and accommodation of new source entrants.

In the absence of an upstream carbon fee program, FPLE supports the auctioning of 100% of the allowances. If the adopted carbon reduction program does not start out at 100% auction, FPLE recommends a transition to 100% auction as soon as feasible. While the current CPUC economic impact modeling shows this as the most costly option to consumers, FPLE submits that “rate shock” can be mitigated through the implementation of the price control mechanisms discussed below. Auctioning all allowances forces generating facilities to pay an appropriate cost for carbon emissions regardless of fuel type or facility configuration. It limits the risk of policy decisions that determine winners and losers through a cap and trade program. Additionally, the auctioning of allowances rewards facilities that implemented early reduction and efficiency measures.

Revenues generated from auctioning allowances can be an important tool in moving California to a lower carbon intensive economy. In order to meet the long term goals of AB32, investments will be needed in carbon reduction technologies, renewable energy projects, energy efficiency programs, and new electric generation technologies. A portion of the revenues from auctioned allowances need to be invested in those programs that will build the framework to achieve long term solutions to climate change. In addition, the Commissions should also dedicate a portion of the auction revenues to the mitigation of the cost impacts a cap and trade program could have on low income consumers. FPLE would however caution the Commissions against using all the auction revenues to cloak the price signal of carbon to consumers. In order for California to reach the 2050 reduction goal, both behavior changes by consumers and operational

changes by emitting sources will be required. Muting the price signal of carbon in the economy would stifle these needed changes.

If the Commissions decide to allocate allowances for free to “first deliverers” in a California GHG cap and trade program, FPLE prefers an output-based allocation (lbs/MWh) without any fuel adjustment factor rather than allocating allowances based on historic emissions or historical heat input. FPLE strongly objects to the assignment of a fuel adjustment factor to an output based allocation as proposed in the Staff Paper. Doing so would defeat the purpose of an output-based approach. The purpose of utilizing an output based allocation methodology is to promote the development of a more efficient generation fleet independent of fuels used. The implementation of a fuel adjustment factor eliminates the incentive to generate power more efficiently. Fuel adjustment factors are economically unfair to customers of natural gas-fired generating companies. These cleaner, typically more efficient gas-fired generators already pay higher fuel prices to produce cleaner generation as compared to coal-fired generation sources. Customers of coal-fired electric generation would continue to reap the benefits of low cost coal and receive additional allowances to offset their pollution under a fuel adjustment factor type allocation methodology.

B. **Flexible Compliance Mechanisms**

FPLE Supports the use of Flexible Compliance and Cost Control Mechanisms

FPLE supports California's adoption of flexible compliance and cost control mechanisms in a cap and trade program for the following reasons:

- absence of viable commercial scale carbon reduction technology for the electric generation sector;
- potential "rate shock" to consumers;
- incentive for the development of carbon reduction and low-emitting generation projects and programs; and
- protection against uncontrollable market forces that could jeopardize the integrity of the program.

1. Flexible compliance mechanisms and cost control mechanisms can protect against rate shock

The Commissions have expressed concern about "rate shock" to consumers. While the inclusion of a price signal for carbon is important to promote behavioral change, extreme economic impacts could undermine the support for the program. FPLE suggests the Commissions recommend the implementation of:

- An increasing price ceiling and floor on the price of auctioned allowances;
- A safety valve mechanism triggered under extreme potentially harmful economic circumstances that would allow the purchase of allowances from future compliance periods;
- Multiple year compliance periods;
- Unlimited use of offsets for compliance; and

- Unlimited banking of allowances.

In order to guard against “rate shock”, the Commissions should recommend the inclusion of a gradually increasing price ceiling on the price of auctioned allowances. It is critical to set the ceiling high enough for the price signal of carbon to promote changes in behavior but low enough to prevent catastrophic economic impacts and political backlash. The Commissions should recommend gradually increasing the upper limit of the carbon price over time, giving consumers and regulated entities an opportunity to adapt to the price of carbon and avoid any harmful economic consequences. Government determination of the price ceiling will limit the potential “rate shock” to consumers while allowing the price of carbon to filter into the economy. In addition, a price ceiling defines the potential worst case cost scenario. This allows investors to more accurately identify potential risk involved with developing new electric generation projects.

2. *Cost control mechanisms will increase investment in carbon reduction and low carbon emitting technologies.*

In addition to a price ceiling, FPLE recommends that the Commissions establish a price floor for auctioned allowances to facilitate investment in carbon reduction projects. A minimum price for carbon allowances will give investors in clean generation technologies and offset projects some level of confidence their product will maintain value in the future carbon market. Establishing a guaranteed value for carbon will limit risk to investors that could otherwise impede the development of carbon reduction projects. This price floor should be increased in parallel with the price ceiling to bracket

the cost of carbon. FPLE supports the utilization of a price floor cost control mechanism as a means to bolster investment in carbon reduction projects and offset projects.

3. *Flexible compliance mechanisms provide necessary protections for emitters with limited compliance options*

a. Safety Valve

Controlling the cost of carbon allowances may not be enough. Inclusion of a safety valve triggered under extreme potentially harmful economic circumstances that would allow purchase allowances from future compliance periods should be an essential element in the cap and trade program. If the cap is too stringent there may not be enough viable emissions reduction options or offsets available to enable emitters to meet their compliance obligations. This shortfall in carbon allowances would drive up the cost of carbon without any assurance that emission sources could meet their compliance obligation.

Since commercial scale emissions control technology is not yet available, some emitters may have no choice but to either stop production or incur non-compliance penalties. A safety valve would allow a temporary expansion of the cap for a given compliance period by allowing for the purchase carbon credits from future compliance periods. If the safety valve is triggered, the cap in future compliance periods would be adjusted so that reductions would stay on a glide path to reach the 2020 carbon reduction goals and, ultimately, the 2050 long term goal. A safety valve must never be used as a crutch that allows emissions sources to arbitrarily shirk compliance obligations. Therefore, the conditions to allow the triggering of this safety valve must be well defined and rigorously monitored. A cost control mechanism incorporating a safety valve would

provide compliance flexibility in the event the emissions cap level is not reasonably attainable. Additionally, a safety valve protects emissions sources against unpredictable and unavoidable shortfalls in the availability of carbon emission allowances and therefore further insulates the California economy from severe economic impacts.

b. Multiple Year Compliance Periods

The use of a multiple year compliance period is another tool that would further protect California's economy against harmful economic impacts. Multiple year compliance periods provide entities a window of time to obtain allowances needed for compliance and the opportunity to seek out least cost reduction options. "First Deliverers" would be able to adjust to changing market conditions or unexpected increases in their compliance obligation. The multiple year compliance periods do not affect the integrity of the cap and allow some needed flexibility for entities with compliance obligations.

c. Offsets

FPLE feels the use of offsets to meet compliance obligations should not be limited by quantity or geographic location as long as they are real and verified. Climate change is a global issue. Carbon reductions in other regions will have the same overall global benefit as local reductions. Limiting offset projects to a region or an entities ability to use offsets could unnecessarily inflate the overall cost of the program. A real reduction in carbon emissions should be allowed no matter where that reduction occurs. Also, CO₂ emissions are different from other pollutants that have more localized effects.

Existing emissions control programs which can not be relaxed are in place to address local ambient air issues, therefore allowing the unlimited use of offsets for compliance should not affect local air quality.

As the emissions cap tightens, meeting compliance obligations will become more and more difficult. With no commercial scale carbon capture and sequestration (CCS) technology currently available, the only reduction options available to the electricity sector are fuel switching and efficiency improvements. Particularly in the early years of the program, offsets may be the only option for many electric generators to significantly lower their GHG compliance obligations. The use of offsets could be critical for California to meet their GHG reduction goals in the electric sector. Also, the restriction on the use of offsets could increase compliance costs. For these reasons, offsets should not be limited geographically or in quantity as long as they are real and verified.

d. Banking of Allowances

FPLE recommends unlimited banking of allowances. Doing so allows entities to hedge against unforeseen increases in emissions caused by the obligation to meet electric load demands and provide incentives for early reductions. If high electric demand happens to coincide with an abnormally dry year, the reduced quantity of electricity generated from hydroelectric plants will cause fossil generating units to increase production to meet load demands. This could cause these fossil generating units to exceed their anticipated carbon emissions potentially leaving them short on allowances. These fossil generating units would then have to purchase more allowances than the

facility managers had planned. Banking of allowances allows fossil generating facilities some protection against unforeseen circumstances that could affect their compliance obligations. The banking of allowances also allows entities to reduce the risk they will face in later years of the program as the cap tightens.

C. Combined Heat and Power

FPLE supports giving credit to CHP facilities under a cap and trade program.

Facilities that operate as a combined heat and power facility should be given credit for their contribution to carbon reductions. FPLE does not have any detailed comments to submit to the Commissions at this time, but would like to reserve the right to respond in the reply comments.

D. E3's Economic Impact Model

1. Model appears to unreasonably mute the carbon price signal

E3's modeling results of the allowance allocation methods appear to focus on muting the price signal to consumers. While FPLE believes the avoidance of "rate shock" is important to maintain public and political support for this program, the muting of the price signal for carbon could be equally damaging to the long term goals of the GHG reduction program. The carbon price signal must be managed; however, the price of carbon is something that must be realized in goods and services in order for consumers to change their behaviors and reduce their carbon footprint. FPLE submits that it would

contravene California's carbon reduction efforts to totally protect electric utility consumers from the price of carbon and assume the cost of carbon reduction will be absorbed elsewhere.

2. *The State GHG reductions appear to be too dependent on the RPS and energy efficiency measures.*

We note that 60% of the GHG reductions anticipated in the E3 modeling results will be achieved by the development of renewable projects and energy efficiency measures. Based on the rate of current renewable energy development in California, there would need to be a significant expansion of both renewable projects and energy efficiency in order for California to meet the goals set in the modeling. These goals are not unobtainable; however, FPLE believes that the Commissions needs to identify significant incentives for these projects either through the use of auction revenues, enhanced power purchase agreements, or an allocation of emission reduction credits.

VIII. Conclusion

The California GHG program currently under development needs to be constructed so it can be linked to a regional or national program easily. In addition, the program must promote the development of the technologies that will result in long term solutions to climate change. For the sake of simplicity, linkability, and promotion of carbon reduction technologies, FPLE urges the Commissions to recommend a 100% auctioning of all allowances. The revenues from auctioned allowances must be used for investment in renewable energy projects, development of energy efficiency programs, investment in the research and development of low or zero emitting energy alternatives,

advancement of carbon capture and sequestration technologies, and the mitigation of economic impacts on low income consumers.

The cost of the program is and should be a major concern of the Commissions. In order to mitigate “rate shock” and to protect the California economy, the Commissions need to implement a variety of cost control and flexible compliance mechanisms which include: price ceiling, safety valve, price floor, multiple year compliance periods, unlimited banking, and unlimited use of offsets. These mechanisms will maintain the integrity of the long term cap while protecting consumers and industry from severe economic impacts. They also gradually introduce the price signal for carbon into the economy in order to promote long term behavioral changes.

Respectfully submitted this 2nd day of June, 2008,

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Attachment A

FPLE’s Response to ALJ Questions proposed in Rulings dated April 16, 2008, May 1, 2008, May 16, 2008 and May 13, 2008, updated May 20, 2008.

The following sections are direct responses to the questions posed in the April 16, 2008, May 1, 2008, May 6, 2008, and May 13, 2008 Administrative Law Judges’ Rulings. The questions were organized in accordance with the May 20, 2008 “Administrative Law Judges’ Ruling Modifying Schedule and Correcting Suggested Outline for Comments and Reply Comments”. FPLE did not respond to all the questions posed but reserves the right to respond during reply comment period.

	<u>Specific Questions in Identified Rulings</u>
I. Summary	N/A
II. General issues	Q3, Q10-Q13 (5/13/08); Q1(a), Q1(b), Q2, and Q3 (5/6/08)
III. Allowance allocation	
A. Detailed proposal	Q1 and Q10 (4/16/08)
B. Response to staff paper on allowance allocation options and other allocation recommendations	Q8-Q13 (4/16/08)
C. Legal issues	Q2-Q7 (4/16/08)
IV. Flexible compliance	
A. Detailed proposal	Q1 (5/6/08)
B. Scope of market and related issues	Q1(a)-Q1(d), Q4, Q5 (5/6/08)
C. Price triggers and other safety valves	Q6-Q7 (5/6/08)
D. Linkage	Q8-Q11 (5/6/08)
E. Compliance periods	Q12-Q13 (5/6/08)
F. Banking and borrowing	Q14-Q16 (5/6/08)
G. Penalties and alternative compliance payments	Q17-Q20 (5/6/08)

	H. Offsets	Q21-Q26 (5/6/08)
	I. Legal issues	Q27-Q31 (5/6/08)
V. Treatment of CHP		
	A. Detailed proposal	Q1 (5/1/08)
	B. Regulation of CHP GHG emissions	Q2-Q15, Q17, Q24 (5/1/08)
	C. CHP as an emission reduction measure	Q16, Q18-Q21, Q23 (5/1/08)
	D. Legal issues	Q22 (5/1/08)
VI. Non-market-based emission reduction measures (other than CHP) and emission caps		
	A. Electricity emission reduction measures	Q1-Q2, Q5 (5/13/08)
	B. Natural gas emission reduction measures	Q1-Q2 (5/13/08)
	C. Annual emission caps for the electricity and natural gas sectors	Q4 (5/13/08)
	D. Legal issues	Q6, Q7 (5/13/08)
VII. Modeling issues		
	A. Methodology	Q8 (5/13/08)
	B. Inputs	Q9 (5/13/08)
	C. Results reported by E3	
	D. Additional modeling and scenarios to support parties' comments	
	Attachment to comments: Copies of scenario documentation tab for any referenced alternative scenarios that use the E3 GHG calculator	

II. General Issues

Q3 (5/13/08). For any non-market-based emission reduction measures for electricity discussed in your opening comments, are there any overlap or compatibility issues with the potential electricity sector participation in a cap-and-trade program? Explain.

FPLE did not mention any non-market based emissions reduction measures in our opening comments, however: we feel it is important for California to maintain their current programs like the Renewable Portfolio Standard (RPS), Energy Efficiency Standards, and the Emissions Performance Standard in order to supplement the cap and trade program and provide further incentive for GHG reductions.

Q10 (5/13/08).What evaluation criteria should be used in assessing each issue area in these comments (allowance allocation, flexible compliance, CHP, and emission reduction measures and policies)? Explain how your recommendations satisfy any evaluation criteria you propose.

The goals of California's GHG reduction program should be structured for long term success while preventing against short term economic hardship. The program should allow the gradual introduction of a price for carbon into the economy facilitated through the implementation of an auction of carbon allowances to emitting sources. The economic impact to consumers should be limited through the implementation of a price ceiling and a safety valve. The integrity of the capped emissions to meet the long term goal should be maintained through adjustments in the glide path of the cap in case the safety valve is triggered. The safety valve proposed by FPLE will provide an opportunity for entities to purchase future vintage allowances to meet their present compliance obligations in order to avoid severe economic consequences while maintaining the integrity of the long term cap. The implementation of a price floor will assure investors that carbon reduction projects will maintain a minimum value in future markets. This will provide incentive for investment in carbon reduction projects in the early years of the program. The unlimited use of offsets will allow sources to seek real and verified carbon reductions from a wider range of least cost opportunities. This will in turn reduce the cost to consumers. The price of carbon driven by a market based program will cause changes in generation and consumption behavior. The auctioning of allowances will prevent policy decisions from determining winners and losers in the market and simplify program implementation. Another advantage of auctioning is it provides revenues needed for investments in: research and development projects for carbon reduction technologies, energy efficiency and renewable energy projects, and mitigation of harmful impacts on low income consumers.

Q11 (5/13/08).Address any interactions among issues that you believe the Commissions should take into account in developing recommendations to ARB.

FPLE has no comment on this question at this time.

Q12 (5/13/08) In establishing policies regarding allowance allocation, flexible compliance, CHP, and emission reduction policies, what should California keep in mind regarding the potential transition to regional and/or national cap-and-trade programs in the future? Are there policies or methods that California should avoid or embrace in order to maximize potential compatibility with other cap-and-trade systems?

California needs to keep their program as simple as possible. The degree of complexity could hinder linkage with other programs like RGGI or the EU ETS. The transition to 100% auction needs to be facilitated as soon as possible to eliminate any obstacles to linking with these other programs.

With respect to a transition to a regional or national program, California must protect against a transfer of wealth from their state to other areas of the country. If the GHG program is structured so large amounts of freely allocated allowances go to historically high emitting sources, as the cap tightens there is a potential for cleaner emitting sources or new sources having to purchase allowances from those higher emitting sources. California's consumers have already made huge investments in switching to cleaner fuels as well as investments in energy efficiency programs. A regional or national program that in effect spreads the cost of GHG reductions to all sources will in essence cause Californians to pay twice for carbon reductions. The danger lies in a free allocation of allowances to high emitting sources for extended periods or otherwise referred to as "grandfathering" of allowances. For this reason, FPLE recommends the California GHG program auction 100% of their allowances.

Q13 (5/13/08).For each issue addressed in your comments, do you have any recommendations about the level of detail and specificity regarding the electricity and natural gas sectors that ARB should include in the scoping plan? Is there enough information in the record in this proceeding to support that level of detail and specificity? What additional information and/or analysis may be needed before ARB finalizes its scoping plan? What determinations regarding the electricity and natural gas sectors should ARB defer for further analysis after the scoping plan is issued? Please be as specific as possible about GHG-related policies for the electricity and natural gas sectors that you recommend be resolved this year, and policies that you believe should be deferred for further analysis after the scoping plan is issued. Address any interactions among issues that you believe the

Commissions should take into account in developing recommendations to ARB.

The Commissions need to evaluate the GHG reductions possible with carbon reduction technologies available. The focus should be the elimination of obstacles to the development of significant quantities of lower emitting electric generation sources and carbon capture and sequestration technologies.

Q1 (5/6/08). Please explain in detail your comprehensive proposal for flexible compliance rules for a cap-and-trade program for California as it pertains to the electricity sector. Address each of the cost containment mechanisms you find relevant including those mentioned in this ruling and any others you would propose.

The Commissions need to consider implementing flexible compliance options that enable real reductions while protecting the economy from severe impacts. FPLE suggests the Commissions utilize flexible compliance mechanisms and cost control mechanisms that include: a price ceiling, a price floor, a safety valve, multiple year compliance periods, unlimited offsets, and unlimited banking of allowances.

a. Discuss how your proposal would affect the environmental integrity of the cap, California's ability to link with other trading systems, and administrative complexity.

When implementing any of these mechanisms it is important to stay focused on the long term goal. Severe economic impacts to consumers and industry could undermine the support for the program. Any adjustment to compliance obligations should not be allowed to affect the long term emissions cap. The auctioning of all the allowances provides the program simplicity needed to enable California to link with other programs.

b. Address how your various recommendations interact with one another and with the overall market and describe what kind of market you envision being created.

FPLE suggests the program gradually introduce the price of carbon into all goods and services. The price ceiling limits the risk of economically damaging price spikes in the allowance prices. As this ceiling is increased over time, the increasing price of carbon is gradually introduced into the economy, allowing customers and industry to adjust to this new price signal. The price floor will prevent the price of allowances from dropping below a certain price. This provides some surety for investors in carbon reduction projects that their investments will have value in future markets. These cost control mechanisms will bracket the increasing price of carbon until it reaches a sustainable value and will allow the economy to adjust to this new cost. As the cost of goods and services increase, customers and industry change their behaviors to avoid the increase. The safety valve is triggered only by extreme events causing either a shortage of allowances or unreasonable spikes in the price of carbon allowances. Future vintage

allowances are then made available for purchase to meet compliance obligations. Since these allowances are purchased from a future compliance period, the long term cap is not affected. If auction revenues are invested in the development of carbon reduction technologies (like CCS), renewable energy, and energy efficiency, these options will be more readily available in future years of the program. This will allow the program to reach GHG reduction goals. Offsets will produce real reductions in GHG emissions and allow for California to maintain grid reliability while reducing the overall cost of the program. Banking allows entities responsible for compliance to plan for future compliance obligations with a restricting cap and protect themselves against unforeseen market fluctuations. All these mechanisms working together will result in a program that shifts behavior while providing opportunity for economic growth.

Q2 (5/6/08). With respect to flexible compliance mechanisms, what should California keep in mind in designing its system when considering the potential transition to regional and/or national cap-and-trade programs in the future? Are there mechanisms that California should avoid or embrace in order to maximize potential compatibility with other cap-and-trade systems?

As mentioned earlier, the complexity of the program could hinder compatibility with other programs. For this reason, we reiterate our support for a 100% auction that would immediately be compatible with RGGI.

Q3 (5/6/08). What evaluation criteria should be used in assessing flexible compliance options?

- Achieve the long term carbon reduction goals;
- Prevent against harmful economic impacts;
- Promote investment in clean generation and carbon reduction technologies;
- Allow the price of carbon into the economy; and
- Maintain the reliability of the electric grid

III. Allowance Allocation

A. Detailed Proposal

Q1 (4/16/08). Please explain in detail your proposal for how GHG emission allowances should be allocated in the electricity sector.

As stated earlier in our comments, FPL prefers that all allowances be auctioned. This eliminates regulatory agencies having to determine winners and losers in the program, instead “first deliverers” pay for what they need for compliance. Since fuels with lower carbon intensity generally cost more, this approach can be viewed as adding the price of carbon to the fuel cost.

Q10 (4/16/08). Describe in detail the method you prefer for returning auction revenues to benefit electricity consumers in California. In addition to your recommendation, comment on the pros and cons of each method listed above, especially regarding the benefit to electricity consumers, impact on GHG emissions, and impact on consumption of electricity by consumers.

It is important not to mute the price of carbon in the economy. Changing the behavior of consumers is an important part of reaching long term carbon reductions goals. Allowing the price of carbon to be introduced into the economy gradually will allow consumers time to adjust to this new price signal and reduce their carbon footprint. The return of all auction proceeds to consumers mutes the price signal that will affect these changes in behavior. The revenues would be better spent on investments in developing lower or zero emitting technologies, infrastructure that will provide lasting solutions to global climate change, and protecting against harmful impacts to low income consumers.

B. Response to staff paper on allowance allocation options and other allocation recommendations

Q8 (4/16/08). The staff paper describes an option that would allocate emission allowances directly to retail providers. If you believe that such an approach warrants consideration, please describe in detail how such an approach would work, and its potential advantages or disadvantages relative to other options described in the staff paper.

FPLE would not support the allocation of allowances directly to retail providers in California because it presents potential competitive fairness issues. New generation in California is built based on a bidding process. Since companies that provide load to consumers also develop their own generation projects, there would be a potential for competitive fairness issues if allowances are allocated to the load serving entities (LSEs). In a market where allowances are being purchased by sources for compliance reasons, the development of new generation projects will have to evaluate the availability and cost of those allowances prior to bidding on a new project. If one of the potential bidders

already has secured the allowances because they have been provided to that bidder for free, this creates competitive fairness issues. Beyond that, just the fact that one bidder is assured the availability of those allowances, free or not, raises competitive fairness issues.

Q9 (4/16/08). Please address the effect that each of the allowance allocation options discussed in the staff paper, or in the articles attached to the staff paper, or in your own or other parties' opening comments, would have on economic efficiency in the economy, and the economic incentives that each option would create for market participants.

They key to all three “preferred” allowance allocation methods is the distribution of the auction revenues. A market based mechanism carbon reduction program should change the behavior of consumers and allow sources to seek out least cost reduction measures. The proposed “preferred” options for the allocation of allowances appear to be attempting to mute the price signal by distributing auction revenues back to consumers. Although this method of revenue distribution may be warranted in the early years of the program in order to prevent “rate shock”, it should not be the only use of the revenues. A more effective way to prevent against “rate shock” would be the use of price control mechanisms. To totally eliminate the carbon price signal sends the message that generation sources will absorb the cost of the reductions. The inability to pass those costs through to the consumer will place an unrealistic burden for carbon reductions on the “first deliverer”. Carbon has a real cost that must be introduced into the cost of goods and services. In order for the long term goals of this GHG program to be realized, changes in behavior must be coupled with advancements in technology. A portion of auction revenues need to be invested into the research and development of carbon reducing technologies, CCS, renewable energy projects, and energy efficiency initiatives. In addition, the Commissions should consider using a portion of the revenues of auctioned allowances to reduce the impact of carbon pricing on low income consumers.

Q11 (4/16/08). If auction revenues are used to augment investments in energy efficiency and renewable power, how much of the auction proceeds should be dedicated to this purpose?

The levels of investment in renewable power and energy efficiency are an important tool in achieving the goals of AB32. Since renewable energy is an existing technology that can reduce GHG emissions, 50% of the auction revenues should go to fully realizing the amount of potential renewable generation in the California supply mix. Research and development of new technologies is another critical part of the solution to global warming; therefore, 25% of the auction revenues should go to the advancement of CCS, energy efficiency, and developing technologies. Finally, it is important to prevent economic harm while also integrating a carbon price signal into goods and services, therefore; 25% of auction revenues should be allocated back to consumers. This will promote behavioral change while preventing “rate shock”.

Q12 (4/16/08). If auction revenues are used to maintain affordable rates, should the revenues be used to lower retail providers' overall revenue requirements, returned to electricity consumers directly through a refund, used to provide targeted rate relief to low-income consumers, or used in some other manner? Describe your preferred option in detail. In addition to your recommendation, comment on the pros and cons of each method identified for maintaining reasonable rates.

If auction revenues are to be used to maintain rates, this mechanism should be phased out at some point to allow the price signal of carbon to enter the economy. If the price of carbon is not allowed to enter the economy, it will be more difficult for the California program to achieve the needed changes in consumer behavior and in essence achieve long term goals of the program. Some of the revenues can be used to protect low income consumers but muting the price signal of carbon for all consumers should not be maintained for a prolonged period of time.

Q13 (4/16/08). If you prefer a combination of methods for returning auction revenues, describe your preferred combination in detail.

FPLE does not support returning all auctions revenues to consumers. If the Commissions decide to implement such a program, the return to customers should be based on retail sales and not historic emissions. The return of revenues based on retail sales will provide additional incentive for LSEs to purchase or produce lower carbon intensive power in order to protect their customers from price increases.

C. Legal Issues

Q2 (4/16/08). Does any of the allowance allocation options discussed in the staff paper, or in the articles attached to the staff paper, or in your opening comments, raise concerns under the Dormant Commerce Clause? If so, please explain why that allocation option(s) may violate the Commerce Clause, including citations to specific relevant legal authorities. Also, explain if and, if so, how the allocation option(s) could be modified to avoid the Commerce Clause problem.

FPLE does not have a comment on this question at this time.

Q3 (4/16/08). Does any of the allowance allocation options discussed in the staff paper, or in the articles attached to the staff paper, or in your opening comments, raise legal concerns about whether they involve the levying of a tax and, therefore, would require approval by a two-thirds vote of the Legislature? If so, please explain why that allocation option(s) is taxation, including citations to specific relevant legal authorities. Also, explain if and, if so, how, the allocation option(s) could be modified to avoid such legal concerns.

As long as auction revenues go toward mitigating the effects of carbon emissions or they go toward preventing or reducing carbon emissions, the program should not trigger the need for 2/3 vote from the Legislature.⁵

Q4 (4/16/08). Does any of the allowance allocation options discussed in the staff paper, or in the articles attached to the staff paper, or in your opening comments, raise any other legal concerns? If so, please explain in full with citations to specific relevant legal authorities. Also, explain if and, if so, how, the allocation option(s) could be modified to avoid such legal concerns.

FPLE does not have any comments on this question at this time.

Q5 (4/16/08). For reply comments: Do any of the allowance allocation options discussed in other parties' opening comments raise concerns under the Dormant Commerce Clause? If so, please explain why that option(s) may violate the Commerce Clause, including citations to specific relevant legal authorities. Also, explain if and, if so, how the allocation option(s) could be modified to avoid the Commerce Clause problem.

FPLE does not have any comments on this question at this time.

Q6 (4/16/08). For reply comments: Do any of the options discussed in other parties' opening comments raise legal concerns about whether they involve the levying of a tax and, therefore, would require approval by a two-thirds vote of the Legislature? If so, please explain why that allocation option(s) is taxation, including citations to specific relevant legal authorities. Also, explain if and, if so, how, the allocation option(s) could be modified to avoid such legal concerns.

FPLE does not have any comments on this question at this time.

Q7 (4/16/08). For reply comments: Do any of the allowance allocation options discussed in other parties' opening comments raise any other legal concerns? If so, please explain in full with citations to specific relevant legal authorities. Also, explain if and, if so, how the allocation option could be modified to avoid such legal concerns.

FPLE does not have any comments on this question at this time.

⁵ "In general, taxes are imposed for revenue purposes, rather than in return for a specific benefit conferred or privilege granted." (*Shapell Industries, Inc. v. Governing Board* (1991) 1 Cal.App.4th 218, 240, "From and after the effective date of this article, any changes in State taxes enacted for the purpose of increasing revenues collected pursuant thereto whether by increased rates or changes in methods of computation must be imposed by an Act passed by not less than two-thirds of all members of the Legislature, except that no new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property may be imposed." *California State Constitution, Article XIII A, Section 3*)

IV. Flexible Compliance

A. Detailed proposal

Q1 (5/6/08). Please explain in detail your comprehensive proposal for flexible compliance rules for a cap-and-trade program for California as it pertains to the electricity sector. Address each of the cost citations to specific relevant legal authorities. Also, explain if and, if so, how the flexible compliance option(s) could be modified to avoid the legal concern(s).

Because carbon reduction technologies are not currently available to electric generation sources on a commercial scale, flexible compliance mechanisms are warranted in the California program. A strict cap of carbon allowances without cost control mechanisms could result in high and/or volatile carbon prices. This would expose the California economy to potentially harmful risks and could discourage the much needed investment in low-carbon emitting alternatives. A sharp carbon price increase would be costly for existing carbon-intensive processes and ultimately consumers. Also, if the price of carbon dropped sharply it would discourage long-term investments in emissions reducing technologies. For these reasons, FPLE urges the Commissions to recommend the use of a price ceiling and price floor when auctioning carbon emissions allowances as well as using a safety valve cost control mechanism that would allow a temporary expansion of the cap against future carbon allowances.

In addition, FPLE supports the use of multi-year compliance periods, unlimited banking of allowances, and the unlimited use of offsets for compliance. The benefits of these mechanisms are discussed in the opening summary of these comments. FPLE is not aware of any legal barriers inherent to these suggested flexible compliance mechanisms.

B. Scope of market and related issues

Q1a (5/6/08) a. Discuss how your proposal would affect the environmental integrity of the cap, California's ability to link with other trading systems, and administrative complexity.

The proposed flexible compliance options discussed should not impact the long term cap at all. Any triggering of a safety valve should also trigger an adjustment to the allowances available in future years of the program. Therefore, the long term cap and goals of the program remain unaffected.

Q1b (5/6/08). Address how your various recommendations interact with one another and with the overall market and describe what kind of market you envision being created.

All FPLE's recommended flexible compliance mechanism and cost control mechanisms interact to protect the integrity of the program while allowing for technology to catch up with need. The three year compliance period will allow for sources to plan and adjust to changing conditions. The safety valve and price ceiling protect against

extreme economic harm while easing the price of carbon into the economy. The price floor will incent investment in carbon reduction projects by establishing a minimum value of carbon in future markets. The use of real and verified offsets will allow emitting sources to seek out the lowest cost reductions while auction revenues are invested into the research and development of commercial scale emissions reduction technologies, renewable energy, and energy efficiency.

Q1c(5/6/08). Describe and specify how unique circumstances in the electricity market may warrant any special consideration in crafting flexible compliance policies for a multi-sector cap-and-trade program.

There are several scenarios where flexible compliance mechanisms like a multi-year compliance periods or a safety valve would be necessary for the electricity sector. For example, extreme weather events could result in abnormally low hydroelectric energy production. This situation combined with a high demand for electricity would place fossil sources in a position where they have to operate more than anticipated. The demand for allowances would rise sharply. If this unanticipated demand for allowances occurs in the later or last year of a compliance period, the allowances needed for compliance may not be available at all or only at unreasonable prices.

Q1d (5/6/08). If your recommendations are based on assumptions about the type and scope of a cap-and-trade market that ARB will adopt, provide a description of the anticipated market including sectors included, expected or required emission reductions from the electricity sector, and the role that flexible compliance mechanisms serve in the market, e.g., purely cost containment, catalyst for long-term investment, and/or protection against market failures.

All of FPLE's recommendations interact to protect the integrity of the program while allowing for technology to catch up with need. The three year compliance period will allow for sources to plan and adjust to changing conditions. The safety valve and price ceiling protect against extreme economic harm while easing the price of carbon into the economy. The price floor will incent investment in carbon reduction projects by establishing a minimum value of carbon in future markets. The use of real and verified offsets will allow emitting sources to seek out the lowest cost reductions while auction revenues are invested into the research and development of commercial scale emissions reduction technologies, renewable energy, and energy efficiency.

Q4 (5/6/08). To what extent should the recommendations to the ARB for flexible compliance in the electricity sector depend on the ultimate scope of the multi-sector cap-and-trade program and other market design issues such as allocation methodology and sector emission reduction obligations? Can the Commissions make meaningful recommendations on flexibility of market operations when the market itself has not yet been designed? Why or why not?

The Commissions can make informed recommendations when they combine the experiences learned from existing emissions markets (Ozone Transport Commission,

Acid Rain Program, EU ETS) and what we can anticipate from a carbon market. They must however strive to keep the program as simple as possible, which is why FPLE recommends the auctioning of all the allowances.

Q5 (5/6/08). Should the market for GHG emission allowances and/or offsets be limited to entities with compliance obligations, or should other entities such as financial institutions, hedge funds, or private citizens be allowed to participate in the buying and selling of allowances and/or offsets? If non-obligated entities are allowed to participate in the market, should the trading rules differ for them? If so, how?

Since the “first deliverers” are responsible for obtaining allowances for their compliance obligations, they should have the first opportunity to obtain auctioned allowances. The participants in an auction should be limited to those entities that are responsible for surrendering those allowances to meeting compliance obligations. If CARB allows other entities to participate in allowance auctions, they will in effect only inflate the cost of compliance. Since every transaction incurs a level of administrative cost, theoretically every time an allowance changes hands, the cost of that allowance will increase. The only reason an entity without a compliance obligation would want to purchase allowances is to profit from the resale of those allowances. Opening the auction to other participants runs the risk of artificially inflating the cost of compliance. The participation of entities without a compliance obligation should be limited to the secondary market that will develop. Furthermore, FPLE recommends that there be a limit to the quantity of allowances that any single entity can purchase through a single auction. This will limit some of the artificial manipulation of the price. FPLE recommends the Commissions and CARB review the auction rules currently being considered by RGGI.

C. Price triggers and other safety valves

Q6 (5/6/08). Should California incorporate price triggers or other safety valves in a cap-and-trade system? Why or why not? Would price triggers or other safety valves affect environmental integrity and/or the ability to link with other systems? Address options including State market intervention to sell or purchase GHG emission allowances to drive allowance prices down or up; a circuit breaker or accelerator which either slows down or speeds up reductions in the emission cap until allowance prices respond; and increasing or decreasing offset limits to increase or decrease liquidity to affect prices. Address how these various strategies would be utilized in conjunction with other flexible compliance mechanisms.

FPLE supports the implementation of a safety valve. If the cap is for some reason too stringent, there may not be enough viable emissions reduction options or offsets available to enable emitters to meet their compliance obligations. This shortfall in carbon allowances would drive up the cost of carbon without any assurance that emission sources still would be able to meet their compliance obligation. Since there are not currently viable commercial scale emissions control technologies available, some emitters may have no other choices but to either stop production or incur huge

administrative penalties. A safety valve would allow a temporary expansion of the cap for a given compliance period by allowing the purchase of carbon allowances from future compliance periods. If the safety valve is triggered, the future glide path of the capped allowances would adjust in order for the program to meet the 2020 carbon reduction goals and ultimately the 2050 carbon intensity target. The Commissions must not lose sight of the fact that the program should be structured to meet the long term goals of carbon reductions. The safety valve must never be used as a crutch that allows “first deliverers” to shirk reasonably obtainable compliance obligations, therefore the terms that would allow the triggering of this safety valve must be well defined and rigorously monitored. A safety valve protects emissions sources against unpredictable and unavoidable shortfalls in the availability of carbon emission allowances.

Cost control mechanisms should be used in a way that does not impede the market function of a cap and trade program while protecting against extreme cost fluctuations that could result in unintended economic harm. In order to accomplish this, the carbon allowances should be auctioned utilizing a gradually increasing price ceiling. It is critical to set the ceiling high enough for the price signal of carbon to promote changes in behavior but low enough to prevent catastrophic economic impacts and political backlash. Since the upper limit of the carbon price would be regulated to gradually increase over time, consumers and regulated entities are afforded an opportunity to adapt to the price of carbon and avoid any harmful economic consequences. The risk of unpredictable price fluctuations would be eliminated and investment decisions could be made with some level of confidence because the potential worst case impacts of a carbon cap and trade program would be known. Also the price ceiling will limit the potential “rate shock” to consumers while allowing the price of carbon to filter into the economy.

FPLE feels the Commissions should recommend the implementation of a price floor to facilitate investment in carbon reduction projects. If a minimum price of carbon allowances is set, it will give investors in clean generation technologies and offset projects some level of confidence their product will have value in the future carbon market. Establishing some guaranteed value for carbon will limit risk to investors that would otherwise impede moving forward with these projects. This price floor should also be increased in parallel with the price ceiling and bracket the cost of carbon. As the market matures the price of carbon will stabilize. FPLE supports the utilization of a price floor cost control mechanism as a means to bolster investment in carbon reduction projects and potential offset projects.

Q7 (5/6/08). Should California create an independent oversight board for the GHG market?⁶ If so, what should its role be? Should it intervene in the market to manage the price of carbon? If such an oversight board were created, how would that affect your recommendations, e.g., would the oversight board obviate the need to include

⁶ In its Final Report adopted February 11, 2008, the Economic and Technology Advancement Advisory Committee recommends that ARB create a California Carbon Trust that could, among other functions, manage the carbon market in California similar to the way that the Federal Reserve Bank manages interest rates by adjusting the supply of emission allowances and credits through sales and purchases. That report is available at <http://www.arb.ca.gov/cc/etaac/etaac.htm>.

additional cost containment mechanisms and price-triggered safety valves in the market design?

FPLE does not have a comment to submit to the Commission on this question at this time.

D. Linkage

Q8 (5/6/08). Should California accept all tradable units,⁷ i.e., GHG emission allowances and offsets, from other carbon trading programs? Such tradable units could include, e.g., Certified Emission Reductions, Clean Development Mechanism (CDM) credits, and/or Joint Implementation credits.

California should accept tradable units from other programs. The ideal situation would be a bilateral agreement that would allow allowances to flow to and from both programs, however, even if a bilateral agreement can not be reached, California should allow real and verified offset projects from other programs to be used for compliance.

Q9 (5/6/08). If so, what effects could such linkage have on allowance prices and other compliance costs of California obligated entities? Under what conditions could linkage increase or decrease compliance costs of California obligated entities? To what extent would linkage subject the California system to market rules of the other systems? What analysis is needed to ensure that other systems have adequate stringency, monitoring, compliance, and enforcement provisions to warrant linkage? What types of verification or registration should be required?

The linking to other programs will decrease the cost of compliance for sources in California: The larger the market, the larger the opportunity to seek out lower cost reductions.

Q10 (5/6/08). If linkage is allowed, should it be unilateral (where California accepts allowances and other credits from other carbon trading programs, but does not allow its own allowances and offsets to California. be used by other carbon trading programs) or bilateral (where California accepts allowances and other credits from other carbon trading programs and allows its allowances and offsets to be used by other carbon trading programs)?

As mentioned earlier, a bilateral agreement should be sought where available. Where bilateral agreements are not available, unilateral agreements could be an acceptable alternative. A greater availability of allowances will lower the cost of compliance for “first deliverers” and California consumers.

⁷ Tradable units refer to (1) GHG emission allowances that permit emission of a ton of carbon equivalent (CO₂E) and (2) offsets that reflect a reduction in GHG emissions of a ton of CO₂E, as addressed in Section 2.8 of this ruling. A credit is a broad term used in this ruling to refer to any tradable unit other than a GHG emission allowance issued by California.

Q11 (5/6/08). If linkage is allowed, should allowances and other credits from other carbon trading programs be treated as offsets, such that any limitations applied to offsets would apply to such credits? If not, how should they be treated?

A tonne of carbon should count for a tonne of carbon regardless of its origin as long as it is real and verified.

E. Compliance periods

Q12 (5/6/08). What length of compliance periods should be used? Should compliance periods remain the same throughout the 2012 to 2020 period? Should compliance periods be the same for all entities and sectors? Should dates be staggered so that not all obligated entities have the same compliance dates?

The suggested three year compliance period similar to the one established for the RGGI program in the northeastern U.S., should be implemented in California. This compliance period term should be consistent through 2020. FPLE feels there is no real need for the Commissions to recommend an initial two year compliance period.

Q13 (5/6/08). Should compliance extensions be granted? If so, under what circumstances?

An extension could be warranted under certain circumstances if an extreme event occurs in the later years of the compliance period that would provoke a high risk of harmful economic impacts to the economy. The Commissions will need to further investigate this potential issue prior to making any recommendations to CARB. FPLE recommends the Commissions review the RGGI policy on the extension of the compliance period. Further, we are aware that some parties have been discussing the possibility of a rolling compliance period that should also be further vetted.

F. Banking and borrowing

Q14 (5/6/08). Should entities with California compliance obligations be allowed to bank any or all tradable units, including allowances, offsets, or credits from other carbon trading programs? Should entities that do not have compliance obligations be able to bank tradable units? If so, for how long and with what other conditions? Should allowances, offsets, or credits from other carbon trading programs banked during the program between 2012 and 2020 be recognized after 2020? If the California system joins a regional, national, or international carbon trading program, how should unused banked allowances, offsets, or credits from other carbon trading programs be treated?

Unlimited banking of allowances should be allowed in the California program. Any entity that banks allowances should have to retire older vintage allowances from their bank first for compliance obligations. Banking will provide an incentive for entities to make reductions earlier in the program. In addition, the banking of allowances

provides companies an opportunity to plan ahead for compliance obligations under a restricting emissions cap.

Q15 (5/6/08). Should limitations be placed on banking aimed at preventing or limiting market participants' ability to "hoard" allowances and offsets or distort market prices?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q16 (5/6/08). Should entities with compliance obligations be allowed to borrow allowances to meet a portion of their obligation? If so, during what compliance periods and for what portion of their obligation? How long should they be given to repay borrowed allowances? Should there be penalties or interest payments? Should there be other conditions on borrowing, such as limitations on the ability to borrow from affiliated entities? Also address the extent to which borrowing might affect environmental integrity and emission reductions.

In general FPLE believes that borrowing emissions allowance against future caps is a risky proposition, but recognizes that it may be necessary to manage the costs of the program. We leave the design of borrowing options to others to determine.

G. Penalties

Q17 (5/6/08). Should there be penalties for entities that fail to meet their compliance obligations? If so, how should the penalties be set? If not, what should be the recourse for non-compliance?

FPLE does not have specific recommendation on where the level of a penalty should be set other than the penalty should strongly discourage an entity from opting for "buying" their way out of a compliance obligation.

Q18 (5/6/08). Instead of penalties, should there be alternative compliance payments? What would be the distinguishing attributes of alternative compliance payments versus penalties? How would the availability of alternative compliance payments affect the environmental integrity of the cap?

Entities that do not meet their compliance obligation should have to purchase their shortfall of allowances immediately and pay a significant penalty by purchasing additional allowances or transferring funds to a program that supports the advancement of low or zero emitting CO2 projects. The integrity of the cap should not be compromised.

Q19 (5/6/08). Would penalties and/or alternative compliance payments allow obligated entities to opt out of the market? Would this add too much uncertainty for other market participants?

The integrity of the long term cap should be maintained, therefore entities should not be able to opt out of their compliance obligation.

Q20 (5/6/08). How should California use the money that would be generated by penalties and/or alternative compliance payments?

FPLE does not have any comment of this issue at this time.

H. Offsets

Q21 (5/6/08). Should California allow offsets for AB 32 compliance purposes?

Offset should be allowed for compliance purposes in the California program.

Q22 (5/6/08). If offsets are permitted, what types of offsets should be allowed? Should California establish geographic limits or preferences on the location of offsets? If so, what should be the nature of those limits or preferences?

The use of offsets should be unlimited as long as those offsets are real and verified. Offsets should not be limited according to a projects location. The ambient air quality standards under the U.S. Clean Air Act address local and regionally transported acute air emissions. Allowing offsets should not affect local air quality standards that are already in place. Climate change is a global issue and a real reduction in carbon emissions should not be limited or discouraged. Limiting offsets to a geographical region potentially increases the cost of achieving carbon reduction.

Q23 (5/6/08). Should voluntary GHG emission reduction projects, i.e., projects that are not developed to comply with governmental mandates, be permitted as offsets if they are within sectors in California that are not within the cap-and-trade program? In particular, should voluntary GHG emission reduction projects within the natural gas sector in California be permitted as offsets, if the natural gas sector is not yet in the cap-and-trade program?

As long as there is a mechanism for verifying that emissions reductions are real and the danger of any double counting is eliminated, voluntary GHG emissions reductions should be incorporated into the California program. FPLE strongly supports the use of Voluntary Emissions Reduction Credits (VERs) and believes they may offer incentives for low or zero emitting technologies.

Q24 (5/6/08). Should there be limits to the quantity of offsets? If so, how should the limits be determined?

As long as offsets are real and verified, there should not be a limit placed on the use of offsets for compliance. Limiting offsets limits the carbon reductions that can be achieved by the program. Allowing unlimited use of offsets will reduce the cost of compliance and the overall cost of the program.

Q25 (5/6/08). How should an offsets program be administered? What should be the project approval and quantification process? What protocols should be used to determine eligibility of proposed offsets? Are existing protocols that have been developed elsewhere acceptable for use in California, or is additional protocol development needed? Should offsets that have been certified by other trading programs be accepted? Should use of CDM or Joint Implementation credits be allowed?

The offset program should be administered through a central entity and employ a set of established and rigorous verification procedures. Protocols established through the California Climate Registry or the World Resource Institute can be useful in evaluating potential offset options.

Q26 (5/6/08). Should California discount credits (i.e. make the credits worth less than a ton of CO₂e) from some offset projects or other trading programs to account for uncertainty in emission reductions achieved? If so, what types of credits would be discounted? How would the appropriate discount be quantified and accounted for?

A real reduction of a tonne of carbon or CO₂e should be credited in full. FPLE does not feel these reductions should be devalued through a discounting process. If offsets are not given full credit, California could deter offset projects that would have resulted in real reductions from ever being developed. Furthermore, the process of devaluing some offset credits will increase the program's complexity and potentially create confusion for participants.

I. Legal issues

Q27 (5/6/08). Under AB 32, is it permissible for GHG emission allowances from non-California carbon trading programs or offsets from GHG emission sources outside of California to be used instead of GHG emission allowances issued in California? Please consider especially the provisions of Health and Safety Code Sections 3805, 38550, and 38562(a) added by AB 32.

FPLE does not have a comment to submit to the Commission on this question at this time.

Q28 (5/6/08). Do any of the flexible compliance options identified in these questions or discussed in the attachments to this ruling or in your opening comments raise concerns under the dormant Commerce Clause? If so, please explain why that flexible compliance option(s) may violate the Commerce Clause, including citations to specific relevant legal authorities. Also, explain if and, if so, how the flexible compliance option(s) could be modified to avoid the Commerce Clause problem. Address, in particular, whether a policy that limits offsets to only emission reduction projects located in California would raise dormant Commerce Clause concerns.

FPLE does not have a comment to submit to the Commission on this question at this time.

Q29 (5/6/08). Do any of the linkage options identified in these questions or discussed in the attachments to this ruling or in your opening comments raise concerns under either the Compact Clause or the Treaty Clause of the United States Constitution? If so, please explain why that linkage option(s) may violate one or both of these Clauses, including citations to specific relevant legal authorities. Also, explain if and,

if so, how the linkage option(s) could be modified to avoid the Compact Clause and/or Treaty Clause problem.

FPLE does not have a comment to submit to the Commission on this question at this time.

Q30 (5/6/08). Do any of the flexible compliance options identified in these questions or discussed in the attachments to this ruling or in your opening comments, raise any other legal concerns? If so, please explain the legal concern(s), including citations to specific relevant legal authorities. Also, explain if and, if so, how the flexible compliance option(s) could be modified to avoid the legal concern(s).

FPLE does not have a comment to submit to the Commission on this question at this time.

Q31 (5/6/08). For reply comments: do any of the flexible compliance options identified by other parties in their comments raise legal concerns? If so, please explain the legal concern(s), including citations to specific relevant legal authorities. Also, explain if and, if so, how the flexible compliance option(s) could be modified to avoid the legal concern(s).

FPLE does not have a comment to submit to the Commission on this question at this time.

V. Treatment of CHP

A. Electricity emissions reduction measures

Q1(5/1/08). Taking into account and synthesizing your answers to other questions in this paper, explain in detail your proposal for how GHG emissions from CHP facilities should be regulated under AB 32.

The treatment of CHP in the California GHG program should be such that any emissions avoided resulting from the development of these projects should be deducted from a facility's compliance obligation. In order to promote the use of CHP, a value for GHG emissions avoided should be calculated by using an established and fully vetted protocol.

B. Regulation of CHP GHG emissions

Q2 (5/1/08) Should GHG emissions from CHP systems be regulated in one sector? If so, which one? How?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q3(5/1/08) For in-state CHP systems, should all of the GHG emissions (i.e., all of the emissions attributed to the electricity generation and to the thermal uses) be regulated as part of the electricity sector? If so, for the electricity that is delivered to the California grid, should the deliverer as defined in D.08-03- 018 be the point of regulation? And, what entity(ies) should be the point(s) of regulation for thermal usage and electricity that is not delivered to the California grid if those uses are included in the electricity sector for GHG regulation purposes?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q4(5/1/08) For out-of-state CHP systems, how should GHG emissions attributed to the electricity delivered to the California grid be regulated? If part of the electricity sector, should the deliverer of the CHP-generated electricity delivered to the California grid be the point regulation? (These questions are based on our view that, for out-of-state CHP systems, only emissions attributed to electricity delivered to California, and not attributed to other electricity or the thermal output, are subject to AB 32.)

FPLE does not have a comment to submit to the Commission on this question at this time.

Q5(5/1/08) Should CHP units be placed in different sectors based on CHP unit capacity size?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q6(5/1/08) Should any of the options for assigning the emissions of a CHP unit to one or more sectors be rejected because it might violate the dormant Commerce Clause?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q7(5/1/08) Should the type of GHG regulation (i.e., cap and trade or direct regulation) be different for a topping-cycle CHP unit versus a bottoming-cycle unit?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q8(5/1/08) Should the sectors used for GHG regulation be different for topping cycle and bottoming cycle CHP units?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q9(5/1/08) Should CHP be part of a cap-and-trade program or not? If so, should the entire unit or certain CHP outputs be part of the cap and trade program?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q10(5/1/08) Should electricity delivered to the California grid by a CHP unit be regulated under the deliverer point of regulation established in D.08-03-018? Why or why not?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q11(5/1/08) Should electricity generated by in-state CHP systems for on-site use be subject to the same regulatory treatment as CHP electricity delivered to the California grid? Why or not?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q12(5/1/08) If CHP is regulated in the electricity sector (either as one combined unit or based only on the total electricity output or based only on the electricity delivered to the California grid), do any of the proposed staff allocation options for electricity need to be modified? How?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q13(5/1/08) If CHP is treated separately from the electricity sector, but is still included as part of a cap-and-trade program, how should allowance allocation to CHP units be handled?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q14(5/1/08) If allowances are allocated administratively to CHP units, should the allocations take into account increased efficiency of CHP? If so, how?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q15(5/1/08) Are there advantages to having all emissions from in-state CHP regulated as part of the electricity sector under cap and trade (and therefore with the need for only a single set of allowances?) How should this be accomplished?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q17(5/1/08) What is the best approach to regulation of CHP emissions to minimize the potential for disincentivizing new installations of CHP and why is that the best approach?

Full credit for avoided emissions attributable to the production of steam for purposes other than electric generation should be deducted for the compliance obligation of that facility.

Q24(5/1/08) Would including all of CHP in cap and trade create a disincentive if natural gas is not regulated under cap and trade?

FPLE does not have a comment to submit to the Commission on this question at this time.

CHP as an emission reduction measure

Q16(5/1/08) Should CHP be considered an emission reduction measure under AB 32? Why or why not?

Yes. The production of steam for industrial processes reduces the need for electricity for those same processes. This should be promoted and given credit as a carbon reduction where warranted.

Q18(5/1/08) Should ARB and/or the Commissions consider policies or programs to encourage installation of CHP for GHG reduction purposes? Why or why not?

Where CHP facilities results in the reduction of GHG emissions, the Commissions should seek opportunities to promote the installation of new facilities.

Q19(5/1/08) Should CHP have an efficiency threshold in order to qualify as an emission reduction measure? If so, why?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q20(5/1/08) Which of the proposed methods best achieves the objectives of an efficiency threshold and why is it the best? Is there a superior method not proposed by staff and why is it superior?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q21(5/1/08) What should the minimum efficiency threshold be (in terms of % savings) to qualify as an emissions reduction measure and why is that the appropriate minimum efficiency threshold?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q23(5/1/08) Should the Commissions pursue policy or programmatic measures to overcome some of the barriers to CHP deployment?

FPLE does not have a comment to submit to the Commission on this question at this time.

C. Legal issues

Q22(5/1/08) Are there other legal and regulatory barriers to CHP implementation in California that should be considered with respect to GHG regulation? If so, please explain in full with citations to specific relevant legal authorities. Also explain if and, if so, how the barriers could be avoided.

FPLE does not have a comment to submit to the Commission on this question at this time.

VI. Non-Market-Based Emissions Reduction Measures (other than CHP) and Emissions Caps

A. Electricity emissions reduction measures

Q1 (5/13/08). What direct programmatic or regulatory emission reduction measures, in addition to current mandates in the areas of energy efficiency and renewables, should be included for the electricity and natural gas sectors in ARB's Assembly Bill (AB) 32 scoping plan?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q2 (5/13/08). Are there additional regulations that ARB should promulgate in the context of implementing AB 32, that would assist or augment existing programs and policies for emission reduction measures in the electricity and natural gas sectors?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q5 (5/13/08). What percentage of emission reductions in the electricity sector should come from programmatic or regulatory measures, and what percentage should be derived from market-based measures or mechanisms? What criteria should be used to determine the portion from each approach? By what approach and in what timeframe should this question be resolved?

FPLE does not have a comment to submit to the Commission on this question at this time.

B. Natural gas emissions reduction measures

Q1 (5/13/08). What direct programmatic or regulatory emission reduction measures, in addition to current mandates in the areas of energy efficiency and renewables, should be included for the electricity and natural gas sectors in ARB's Assembly Bill (AB) 32 scoping plan?

FPLE does not have a comment to submit to the Commission on this question at this time.

Q2 (5/13/08). Are there additional regulations that ARB should promulgate in the context of implementing AB 32, that would assist or augment existing

programs and policies for emission reduction measures in the electricity and natural gas sectors?

FPLE does not have a comment to submit to the Commission on this question at this time.

C. Annual emissions caps for the electric and natural gas sectors Q4 (5/13/08). The scope of this proceeding includes making recommendations to ARB regarding annual GHG emissions caps for the electricity and natural gas sectors. What should those recommendations be? What factors (e.g., potential effectiveness of identified emission reduction measures, rate impacts for electricity and natural gas customers, abatement cost in other sectors, anticipated carbon prices) should the Commissions consider in making GHG emissions cap recommendations? If sufficient information is not currently available to recommend cap levels, what cap-related recommendations should the Commissions make to ARB for inclusion in its scoping plan?

FPLE does not have a comment to submit to the Commission on this question at this time.

D. Legal issues

Q6 (5/13/08) Do any of the non-market-based emission reduction measures discussed in your opening comments raise any legal or regulatory concern(s) or barrier(s)? If so, please explain the legal or regulatory concern(s) or barrier(s), including citations to specific relevant legal authorities. Would additional legislation be necessary to overcome any identified legal barrier(s)? Also, explain if and, if so, how the emission reduction measure(s) could be modified to avoid the legal or regulatory concern(s) or barrier(s).

FPLE does not have a comment to submit to the Commission on this question at this time.

Q7 (5/13/08). For reply comments: do any of the emission reduction measures identified by other parties in their comments raise legal concerns? If so, please explain the legal concern(s), including citations to specific relevant legal authorities. Also, explain if and, if so, how the emission reduction measure(s) could be modified to avoid the legal concern(s).

VII. Modeling Issues

A. Methodology

Q8 (5/13/08) Address the performance and usefulness of the E3 model. Is it sufficiently reliable to be useful as the Commissions develop recommendations to ARB? How could it be improved?

FPLE does not have a comment to submit to the Commission on this question at this time.

B. Inputs

Q9 (5/13/08) Address the validity of the input assumptions in E3's reference case and the other cases for which E3 has presented model results. If you disagree with the input assumptions used by E3, provide your recommended input assumptions.

FPLE does not have a comment to submit to the Commission on this question at this time.

C. Results reported by E3

FPLE does not have a comment to submit to the Commission on this question at this time.

D. Additional modeling and scenarios to support parties' comments

FPLE does not have a comment to submit to the Commission on this question at this time.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing document

**COMMENTS OF FPL ENERGY PROJECT MANAGEMENT, INC. ON THE
COMBINED REQUEST FOR COMMENTS ON THE JOINT COMMISSION
STAFF PAPER ON OPTIONS FOR THE ALLOCATION OF ALLOWANCES,
FLEXIBLE COMPLIANCE MECHANISMS FOR COMPLIANCE WITH
GREENHOUSE GAS REGULATORY ACTIVITIES, THE TREATMENT OF
COMBINED HEAT AND POWER UNDER GREENHOUSE GAS PROGRAM,
AND THE CPUC ECONOMIC IMPACTS MODELING RESULTS**

On all parties of record in the above captioned proceeding by serving an electronic copy on their email address of record, by overnight mail to the Assigned Commissioner Peevey's Advisor Nancy Ryan and Administrative Law Judges, and for those parties without an email address or record, by mailing properly addressed copy by first-class with postage prepared to each party on the Commission's official service list for this proceeding as posted on the California Public Utilities Commission's website for proceeding R.06-04-009.

This Certificate of Service is executed this 2nd day of June, 2008 in Juno Beach, Florida.

/s/ Garson Knapp

Garson Knapp

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