Comments of the Northwest & Intermountain Power Producers Coalition to the Washington Department of Ecology Draft Cap-and Invest Program Rules

July 15, 2022

The Northwest & Intermountain Power Producers Coalition ("**NIPPC**") appreciates the opportunity to submit comments on the Washington Department of Ecology's'("**Ecology**") Draft Cap and Invest Program Rules (Chapter 173-446 WAC) (the "**Draft Cap and Invest Program Rules**"). NIPPC represents competitive power participants in the Pacific Northwest. NIPPC members include owners, operators, and developers of independent power generation and storage, power marketers, and affiliated companies.

NIPPC appreciates the improvements made to the Draft Cap and Invest Program Rules in the most recent iteration.[1] However, additional modifications are necessary to ensure a workable program, particularly with respect to the electric industry. These changes include:

- Further structure and clarifications to ensure that allowances freely allocated to utilities are limited to the utility's retail service and do not create an incentive for leakage.
- Further structure and clarifications to ensure that utilities receiving free allocations of allowances include a cost of carbon in dispatch and capacity planning decisions.
- Clarifications and changes to treatment of electricity traded at the Mid-C market point to ensure Washington's programs do not inadvertently striate the robust and integrated market for electricity on which the state relies.
- Modification to the start date for auctions to allow price discovery prior to the start of the initial compliance period.
- Clarifications on disclosure of holding account balances to clarify publication will be on an aggregated basis.

Each of these issues is addressed below.

[1] NIPPC previously submitted comments on the prior iteration of program rules on January 26, 2022 (the "**January Draft Rules**").

1. **Allocation of allowances to utilities must be based on actual retail load within the state and should not create an incentive for leakage or otherwise disrupt competitive markets.**

NIPPC appreciates that the revised draft program rules specify that Ecology will "use utility specific forecasts that provide retail electric load" for determining the quantity of allowances to be distributed to electric utilities,[2] and now include new provisions addressing allocation of retail load from multijurisdictional electric companies through allocation methodologies approved by the Washington Utilities and Transportation Commission ("**WUTC**").[3] NIPPC recommends that Ecology also ensure that utilities receiving a free allocation of allowances are working diligently to bring the lowest-carbon power to Washington retail customers, and do not take advantage of the free allocation to allocate (or acquire) higher carbon power for use within the state, where they will not bear any carbon costs as a result of free allowances, and then allocate their lower-carbon power to other jurisdictions, or sell it for a premium in wholesale markets. This same concept should apply to any utility (whether or not multijurisdictional) that engages in wholesale or extra-jurisdictional sales which create carbon pricing obligations not related to retail service. Utilities also should be barred from using freely-allocated allowances to meet carbon obligations related to these out of state retail or non-retail transactions.

Potential modifications to ensure the allocation of free allowances is limited to retail load in Washington can be made with a simple addition to proposed Draft Cap and Invest Program Rules WAC 173-446-230(5), as follows:

> (5) Allowances allocated at no cost to electric utilities may be consigned to auction for the benefit of **retail** ratepayers **in Washington**, transferred at no cost to an electric generating facility as described in WAC 173-446-425, deposited for compliance **to be used to meet compliance obligations related to serving retail load in Washington**, or a combination of these uses. While no cost allowances may be held for future use, they may not be traded or transferred other than as authorized to WAC 173-446-425.

2. **The imputed price of carbon should be included in all dispatch and pricing decisions for utilities receiving a free allocation of allowances.**

Utilities allocated free allowances should be required to impute the full cost of carbon in all dispatch decisions, bids into competitive power markets, and procurement and investment decisions. Absent this requirement, utilities may gain an unfair competitive advantage over their

[2] Proposed WAC 173-446-230 Section 1(a)
[3] Proposed WAC 173-446-230 Section 1(b)(i)

generation and marketing competitors who do not receive free allowances. Mitigating the potential for this unfair advantage is essential to maintaining the integrity of competitive regional markets. NIPPC has included as Attachment 1 hereto proposed regulatory language designed to ensure this occurs in a fair and effective manner.

3. **The regulations should adopt a methodology for addressing imported electricity associated with Mid-C ICE transactions as a centralized power market**

As NIPPC noted in its January 26 Comments, any cap and trade rules affecting wholesale electricity transactions must be carefully crafted to maintain a properly functioning regional electric power market. A substantial portion of electricity produced or imported into Washington is traded on the centralized electronic market operated by Intercontinental Exchange, *a/k/a* "**ICE**,"[4] at the Mid-Columbia ("**Mid-C**") market point (or hub) physically located along the Columbia River in central Washington, and those transactions and therefore the liquidity of the Mid-C hub may be compromised based on uncertainty to the extent parties do not know which entity in the chain will bear the carbon cost.

NIPPC appreciates Ecology's efforts to address this issue in the revised Draft Cap and Invest Program Rules, but the issue still remains. Under the revised Draft Cap and Invest Program Rules (and by reference to the Reporting Rules), an electricity importer is defined as "the retail provider, marketer or asset controlling supplier that conducts an electricity transaction through the [Energy Imbalance Market (EIM)] that results in EIM power being delivered to final point of delivery in Washington state." This creates confusion in three ways. First, the definition focuses just on electricity transacted through the EIM, which is a small portion of the overall wholesale energy market. Second, it identifies three different entities as the potential importer – the retail provider, the marketer, and the asset controlling supplier – each of which may be engaged in the same transaction. Third, parties engaged in the transaction may not know whether power is being "delivered to final point of delivery in Washington state" or if that power will ultimately be wheeled to another jurisdiction.

The Climate Commitment Act generally prescribes specific treatment of imported and exported power, and also mandates that Ecology "shall adopt by rule a methodology for addressing imported electricity associated with a centralized electricity market" by October 1,

[4] See, e.g., www.TheIce.com. According to data from U.S. Energy Information Administration, an average of 44 trades occurred at the Mid-C point each day during 2021, with an average trade volume of more than 21,455 MWh per day. See https://www.eia.gov/electricity/wholesale/#history.

2026.[5] NIPPC suggests that this authority may encompass imports associated with Mid-C. NIPPC urges Ecology to further evaluate this rulemaking authority as it relates to Mid-C, invite further public comment on the treatment of Mid-C transactions, and consider whether the problems NIPPC notes here may be most appropriately addressed through regulation or through a potential commercial solution described below.

The problem that must be addressed stems from the fact that buyers and sellers of power at the centralized Mid-C point – each of which may be either a retail provider, marketer or asset controlling supplier – will not know whether such power will be subject to the Washington Cap and Invest Program, nor what entity will be responsible for meeting compliance obligations, until after the transaction, making it impossible to accurately price the electricity. For example, if electricity sold at Mid-C were purchased on ICE by a Washington utility, the seller would be subject to responsibility for the carbon, but if the electricity were purchased by a utility in Oregon, the seller would not be subject to the same costs. To accommodate the potential risk that offers are picked up by Washington utilities, offerors may elect to include potential carbon costs in all offers. But this would also raise prices for buyers located outside the state and could have the unintended consequence of driving transactions away from the Washington market hub at Mid-C to other power markets. This erosion of the Mid-C hub will disrupt the power sector and negatively affect Washington as the host of this hub.

NIPPC recognizes that transactions at Mid-C depend on both a standardized wholesale power agreement (the WSPP agreement), formed on a largely consensus basis through voluntary industry workgroups, and the ability to transact products based on that agreement on the electronic exchange operated by ICE. The industry has already initiated discussions about whether and how to address the issue described here through a modification or addendum to that agreement, but has yet to finalize a solution. If a commercial solution is reached, that may settle this issue. But because Ecology is meanwhile under a statutory deadline to complete rules to implement the Climate Commitment Act, NIPPC recommends that Ecology evaluate this issue in more detail. The solution proposed in the Draft Cap and Invest Program Rules is simply not workable.

NIPPC recommends that Ecology take further public comment on whether and how to use its authority to "adopt by rule a methodology for addressing imported electricity associated

[5] See Climate Commitment Act Section 10(1)(c).

with a centralized electricity market" to specify ways to account for transactions at Mid-C that do not ultimately sink in Washington. NIPPC notes that any such approach must be weighed carefully against the potential for complicating, if not hindering, the possibility of linkage with other jurisdictions.

4. Modification to the start date for auctions to allow for price discovery.

NIPPC urges ecology to hold the initial auction during the fourth quarter of 2022, prior to the start of the first compliance period, to provide price discovery information to participants. Washington's cap and trade program is new, and, until an initial auction is held, parties have no way of knowing whether compliance costs will be close to the 2023 auction floor of $19.70 per metric ton, the auction ceiling of $72.29 per metric ton, or somewhere in between. This level of uncertainty is untenable for many market participants. In the electricity market, this level of uncertainty may cause generators to sell power in other markets with known pricing, potentially destabilizing the power grid in Washington.

One relatively easy solution to avoid this result would be to hold an initial auction in 2022, prior to the start of the initial compliance period. This initial auction would provide at least some level of price discovery that can be used to set transaction pricing for the start of 2023. Whether that initial auction clears at $20, $50, $72, or some other value, market participants will at least gain an understanding of the cost of carbon and can act accordingly.

5. The Regulations must protect the confidentiality of individual holding account information.

NIPPC urges Ecology to further modify proposed WAC 173-446-150(4) to make it clear that the content of holding account information will only be published on an aggregated basis, not just on an anonymized basis. NIPPC appreciates that the revised Draft Cap and Invest Program Rules now reflect that the information will be anonymized, which is an improvement as compared to the January Draft Rules, but submits that the anonymization without aggregation is not sufficient in and of itself. [6]

[6] Proposed WAC 173-446-150(4) reflects the following change from the version published with the January Draft Rules: "Ecology will post **anonymized** information about the contents of each holding account, including but not limited to the number of allowances in the account, on Ecology's Cap-and-Invest public website. **Ecology will also maintain on its** ~~The~~ website ~~also includes~~ a public roster of all covered entities, opt-in entities, and general market participants."

Information about an individual entity's account status should remain highly confidential. Publishing such information could dramatically disrupt the marketplace, and incent anti-competitive, price gouging behavior. For example, if the marketplace is aware that a given counterparty has far fewer (or far more) compliance instruments than needed for an upcoming compliance period, that party may face prices based not on general market costs, but on predatory pricing by competitors.

Anonymization of cap and trade account data is helpful, but does not go far enough. Washington State will have relatively few compliance entities, and there is a wide divergence of actual compliance obligations. Without aggregation of the data, sophisticated market counterparties likely will be able determine with reasonable accuracy the likely entity behind an anonymous compliance account, especially with respect to the larger market participants.

Instead, NIPPC urges Ecology to modify the Draft Cap and Invest Program Rules as follows, making it clear that the number of allowances held in accounts will only be published on an aggregated basis:

> (4) Ecology will post information about ~~the contents of each holding account, including but not limited to the number~~ **the total aggregate number of** allowances **in holding accounts by (**1**) covered entities, (2) opt-in entities and (3) general market participants** ~~in the account ,~~ on Ecology's Cap-and-Invest public website. The website also includes a public roster of all covered entities, opt-in entities, and general market participants.

6. Mandatory Transfer of Allowances to Generators pursuant to WAC 173-446-425.

NIPPC appreciates inclusion of new section WAC 173-446-425 in the Draft Cap and Invest Program Rules, which allows an electric utility to transfer no cost allowances to an electric generating facility or federal power marketing administration under specific circumstances.[7]

[7] **WAC 173-446-425 Transfers of no cost allowances from an electric utility to an electrical generating facility or to a federal power marketing administration.**

(1) An electric utility wishing to transfer no cost allowances to the compliance account of an electrical generating facility or federal power marketing administration may submit a request to ecology asking for the transfer and providing the following information:

(a) The electric utility's holding account number;

(b) The compliance account number of the federal power marketing administration or the electrical generating facility;

(c) The quantity and vintage of no cost allowances to be transferred;

(d) The relationship between the electric utility and the federal power marketing administration or electric generating facility.

(2) Ecology may transfer the allowances only if:

NIPPC believes that the rules should be further modified to make such transfers mandatory in those limited situations where the electric generating facility will retain the compliance obligation.. To the extent that the electric generating facility holds the compliance obligation, granting free allowances to the utility creates unjust enrichment.

7. Conclusion

In offering these recommendations, NIPPC recognizes that the regulations promulgated by Ecology must be consistent with, and follow, the statutory requirements of the CCA and believes all of NIPPC's suggestions follow this criterion. NIPPC also notes that the Act provides Ecology meaningful latitude to tailor implementation of the Cap and Invest Program to ensure success, including a mandate that Ecology bring forth a request for revisions to the legislation where necessary to successfully link with other jurisdictions.[8] To the extent Ecology believes it is restricted from making the proposed clarifications and modifications addressed herein due to conflicts with the Statute, NIPPC urges Ecology to seek appropriate legislative changes.

Sincerely,

Carl Fink
Blue Planet Energy Law and Consulting
Suite 200, 628 SW Chestnut Street
Portland, OR 97219
CMFink@Blueplanetlaw.com
971.266.8940 (o)
503.819.4188 (c)

One of counsel for the Northwest & Intermountain Power Produces Coalition
July 15, 2022

(a) The electric generating facility is operated by the electric utility; or
(b) The electric utility has an agreement to purchase imported electricity or a power purchase agreement, including a custom product contract from the federal power marketing administration or the electric generating facility.
(c) The transfer will not violate the federal power marketing administration's or the electrical generator's holding limit.

[8] *See Climate Commitment Act*, Section 8(6): "The department ***must*** bring forth agency request legislation if the department finds that any provision of this chapter prevents linking Washington's cap-and-invest program with that of any other jurisdiction." Emphasis supplied.

ATTACHMENT 1

NEW SECTION

WAC 173-446-236 Including emissions compliance costs in resource dispatch analyses for electric utility integrated resource planning and clean energy implementation planning, and clean energy action planning.

(1) In its resource plans, each electric utility must include emissions compliance costs in the incremental dispatch cost for each resource, including its owned resources and wholesale power sales and purchases.

(a) Emissions compliance costs must be quantified on a $/MWh basis, calculated by multiplying the dollar value of an allowance, expressed in dollars per MT CO2e, by the actual emissions rate of the facility, expressed in MT CO2e per MWh.

(b) The dollar value of allowances for each year of the planning horizon must be set based on a documented forecast.

(c) For each year of the resource planning analyses, the same dollar value of allowances (in $/MT CO2e) must be included in the incremental dispatch costs for all GHG-emitting facilities in the electric utility's resource portfolio.

(d) The same dollar value of allowances (in $/MT CO2e) must be included in incremental dispatch costs for resources used to sell power in the short-term wholesale market. The utility's resource plan analyses must:

(i) Identify the incremental resource or resources the utility would add to its order of dispatched resources to make the sale;

(ii) Include emissions compliance costs in the incremental dispatch cost or costs of the incremental resource or resources.

(e) The same dollar value of allowances (in $/MT CO2e) must be included in incremental dispatch costs for resources used to purchase power in the short-term wholesale market. The utility's resource plan analyses must:

(i) Identify the incremental resource or resources the utility would remove from its order of dispatched resources to make the purchase;

(ii) Include the emissions compliance cost in the avoided incremental dispatch cost of the resource or resources being displaced;

(iii) If the power purchase is from a GHG-emitting resource or an unspecified source, include the emissions compliance cost in the incremental cost for the purchase.

NEW SECTION

WAC 173-446-237 Including emissions compliance costs in electric utility resource acquisitions.

(1) When analyzing and making resource acquisitions, each electric utility must include emissions compliance costs in the incremental dispatch cost for each resource, including its owned resources and wholesale power sales and purchases.

(a) Emissions compliance costs must be quantified on a $/MWh basis, calculated by multiplying the dollar value of an allowance, expressed in dollars per MT CO2e, by the actual emissions rate of the facility, expressed in MT CO2e per MWh.

(b) The dollar value of allowances for each year of the planning horizon must be set based on a documented forecast.

(c) For each year of the resource acquisition analyses, the same dollar value of allowances (in $/MT CO2e) must be included in the incremental dispatch costs for all GHG-emitting facilities in the electric utility's resource portfolio.

(d) The same dollar value of allowances (in $/MT CO2e) must be included in incremental dispatch costs for resources used to sell power in the short-term wholesale market. The utility's resource acquisition analyses must:

(i) Identify the incremental resource or resources the utility would add to its order of dispatched resources to make the sale;

(ii) Include emissions compliance costs in the incremental dispatch cost or costs of the incremental resource or resources.

(e) The same dollar value of allowances (in $/MT CO2e) must be included in incremental dispatch costs for resources used to purchase power in the short-term wholesale market. The utility's resource plan analyses must:

(i) Identify the incremental resource or resources the utility would remove from its order of dispatched resources to make the purchase;

(ii) Include the emissions compliance cost in the avoided incremental dispatch cost of the resource or resources being displaced;

(iii) If the power purchase is from a GHG-emitting resource or an unspecified source, include the emissions compliance cost in the incremental cost for the purchase.