

7/15/2022

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RE: Chapter 173-446 WAC – Climate Commitment Act Program Rulemaking

Below please find the comments of Grays Harbor Energy, LLC (“GHE”) regarding the Washington Department of Ecology’s (“Ecology”) proposed rule 173-446 of the Washington Administrative Code (“Proposed Rule”) to implement the Climate Commitment Act (“CCA”). Grays Harbor Energy, LLC owns and operates the Grays Harbor Energy Center, a 662 MW natural gas-fired combined cycle electric generating facility in Elma, Washington. GHE is an affiliate of Invenergy, North America’s largest privately held clean energy developer.

GHE appreciates Ecology’s openness and engagement in the rulemaking and respectfully makes recommendations to change or clarify the Proposed Rule in certain respects as described below. GHE looks forward to working with Ecology staff and others to implement the Proposed Rule as a covered entity with one of the, if not the, largest compliance obligations of any covered entity.

Ecology Should Level the Playing Field Among All Electric Generating Facilities Required to Comply with the Proposed Rule

The Proposed Rule requires all electric generating facilities that emitted more than 25,000 MT of CO₂e in 2015-2019 to surrender allowances equal to their emissions starting from Day 1 of the program. However, electric utilities are given no-cost allowances equal to 100% (and more for administrative costs) of their compliance burden related to electric generating facilities they own or contract with according to their own forecasts. To the best of GHE’s knowledge and belief, because of the way that no-cost allowances are allocated, GHE is the ONLY electric generating facility in the state that through an affiliate or counter-party receives ZERO no-cost allowances yet is required by comply 100% from Day 1. This disparate treatment is unfair, inequitable, and actually increases emissions and costs to ratepayers compared to a level playing field. The Proposed Rule is thus counter to the legislature’s intent in enacting the CCA and makes the Proposed Rule vulnerable to challenge on these grounds.

One way to level the playing field between all electric generating facilities required to comply with the Proposed Rule is to extend the allocation of no-cost allowances to all electric generating facilities in the state that are required to comply. This method would resolve disparate and unequal treatment of electric generating facilities based simply on which entities those facilities are owned by or counter-parties with. If Ecology does not so extend the allocation of no-cost allowances, it can at least do so for all emissions associated with power that sinks in the state. Limiting no-cost allowances to those emissions is consistent with how the electric utilities are allocated no-cost allowances, based on the forecast of which generating facilities will be used to serve their retail load in Washington.

If Ecology does not extend the allocation of no-cost allowances, then another way to help mitigate the disparity would be to require all electric utilities to include the value of allowances in their decisions to dispatch electric generating facilities. When considering whether to dispatch a GHG-emitting resource

during its operations, each electric utility should be required to include the emissions compliance cost, quantified on a \$/MWh basis, in the resource's incremental dispatch cost.¹ Without that requirement, electric generating facilities may be dispatched in a manner that is not the most cost-effective or emissions-reducing since the costs of higher-emitting resources will not be required to include the cost of compliance with the CCA. Those higher-emitting resources will be dispatched more often than they would be if their costs were required to include the cost of compliance with the CCA (i.e. the value of allowances, among other things). Requiring utilities to include CCA compliance costs is consistent with the legislature's goals in enacting the CCA of reducing emissions and minimizing the costs of doing so. Moreover, doing so mitigates the harm caused by the disparate treatment of electric generating facilities owned by or under contract with an electric utility versus all other electric generating facilities. This reduces Ecology's vulnerability to legal challenge against the Proposed Rule on those grounds.

The \$/MWh cost should be calculated by multiplying the dollar value of an allowance (in dollars per MT CO₂e) multiplied by the actual emissions rate of the resource (in MT CO₂e per MWh). At the time of each dispatch decision, the same dollar value of allowances (in \$/MT CO₂e) should be included the incremental dispatch costs for all GHG emitting resources in the utility's resource portfolio. Compliance emissions costs (in \$/MWh) will be higher for more emissions-intensive resources.

Emissions compliance costs should also be required to be included in utility decisions to buy or sell power in the wholesale market. For example, if a utility is considering making a sale into the wholesale market, it should be required to: 1) identify the incremental resource(s) that it would add to the top of its stack of dispatched resources in order to make the sale and 2) include emissions compliance costs in the incremental dispatch cost(s) of that resource or resources.

Alternatively, if a utility is considering purchasing in the wholesale market to serve its retail electric customers, it should be required to: 1) identify the incremental resource(s) that it would remove from the top of its stack of dispatched resources in order to make the purchase, 2) include the emissions compliance cost in the avoided incremental dispatch cost of that resource or resources that is being displaced, and 3) if the power purchase is from a GHG-emitting resource, include the emissions compliance cost in the incremental price for the purchase.

Below is GHE's proposal for addition to the Proposed Rule to implement this recommendation:

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.

¹ Indeed, 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. These may exceed CCA compliance costs.

(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.

The Preliminary Regulatory Analyses Inconsistently Evaluates Impact on Independent Power

The Preliminary Regulatory Analyses issued with the proposed rule, as revised, recognizes that the proposed rule may disproportionately affect small businesses (those with 50 or fewer employees). Ecology concludes that it “must include elements in the proposed rule to mitigate this potential disproportion.”² That mitigation should be applied consistently along the spectrum of business size,³ which can be done by assessing output and other impacts with more granularity.

The Regulatory Fairness Act Compliance analysis includes multiple tables illustrating impacts to output, but these impacts are assessed on overly broad industry classifications: “utilities,” “retail,” “wholesale,” “transportation and warehousing,” “construction,” and “manufacturing.”⁴ Meanwhile, the “Regulatory baseline” evaluation of the Preliminary Regulatory Analyses puts forth baseline emissions by electricity sub-sector in Table 20. This table shows that emissions from independent power producers (“IPPs”) averaged 1.1 million MT CO₂e in 2015-2019, or less than 7% of the total electricity sector emissions of 16.4 million MT CO₂e. While Ecology has performed an electricity sub-sector analysis for baseline emissions, a comparative sub-sector analysis is missing when considering the impact of the proposed rule. These impacts include both the effect on output and compliance costs.

Were Ecology’s Preliminary Regulatory Analyses to consistently treat independent power, it would show that, comparing compliance cost burdens to baseline emissions, the independent power sector bears a disproportionate burden of the cost of the CCA program in relation to baseline emissions. Total baseline emissions, per Table 21, are 68.23 million MT CO₂e; independent power accounts for only 1.1 million MT CO₂e of this, or about 1.6%. Given estimated program costs set forth in Table 27, however, and GHE’s estimates of its compliance costs with the proposed rule, independent power’s share of the program cost burden will significantly exceed its share of baseline emissions.⁵ This fact would be more evident were the electricity sub-sector analysis completed in Table 20 applied in other sections of the regulatory analyses.

Ecology’s Expectation of Reduced GHG Emissions due to the Proposed Rule is Unsupported and Unlikely in the Electricity Sector

In the Preliminary Regulatory Analysis, Ecology asserts its expectation that the proposed rule will “result in benefits of reduced GHG emissions.”⁶ In the electricity sector, however, the rule will likely have the

² Preliminary Regulatory Analyses at 21. All references are to the revised document filed June 3, 2022.

³ Businesses impacted by the proposed rule range in size from 1 to an average of 127,498 employees. *Id.*

⁴ Preliminary Regulatory Analyses at 162.

⁵ See also Ecology’s announcement of the public comment period for the proposed rule, “[c]ap-and-invest will reduce greenhouse gases and raise \$500 million per year.” GHE estimates that the proposed rule will cost at least \$40 million per year to comply with, which includes only direct compliance costs and not other costs imposed on GHE by the proposed rule. This represents 8% of the funds Ecology expects to raise.

⁶ At 32.

opposite of its intended effect: as currently structured, the rule encourages the use of utility-owned dispatchable generation over IPP-owned dispatchable generation, even though the only IPP-owned covered entity in Washington State has lower emissions per MWH produced than utility-owned dispatchable generation.⁷

The net effect of broadly defined free allowance allocations to electric utilities—based on the utilities’ own demand forecasts—and no incentives for ensuring that lower-emitting (independently owned) resources are used to serve load—is a likely increase in GHG emissions. Rather than structuring operations to optimize emissions reductions, utilities are incentivized to use their own generation to serve their load, regardless of whether other, lower-emitting resources are available. Moreover, utilities are incentivized to over-estimate load, and the proposed rule includes no true-up provision to mitigate any over-estimation. This is contrary to Ecology’s assertion that the program design “results in an incentive for covered entities to reduce their emissions.”⁸ Indeed, Ecology admits as much when it states that “carbon prices do not induce additional electricity sector abatement because the electricity sector’s modelled reductions match CETA’s ambitious decarbonization targets,” “decarbonization of the electricity sector is driven by CETA regulations,” and “there is limited economic incentive to abate beyond the CETA trajectory” such that more aggressive decarbonization is not even captured in the modeling performed for Ecology.⁹ Simply put, Ecology’s Proposed Rule does not and cannot be expected to lead to significant emissions reductions in the Electricity Sector. Nevertheless, the rule leads to significant harm to GHE, which is among the least-emitting and most cost-efficient generation in the state.

Electric Utilities Should be Required to Transfer No-Cost Allowances When Buying Power to Serve Load

GHE appreciates the addition of section 173-446-425 to the proposed rule, allowing electric utilities to transfer no-cost allowances to electric generating facilities. The current proposed language of this section unnecessarily limits utility actions, however, and should be revised to reflect current utility power acquisition practices. It should also be amended to be proscriptive, requiring electric utilities to transfer no-cost allowances upon purchase of power from a covered entity: electric utilities are granted no-cost allowances in accordance to their need to serve load, and purchased power is used for the purpose of serving load.

GHE advocates for four changes to this section:

1. Amend to *require* transfers of no-cost allowances, rather than merely *allow* for transfers.
2. Require transfers of no-cost allowances to covered entities in transactions facilitated by third-party marketers;
3. Clarify that section 2(b) includes all power transactions, including spot market purchases.

⁷ United States Environmental Protection Agency (EPA). “Power Sector Emissions Data.” Washington, DC: Office of Atmospheric Programs, Clean Air Markets Division. Available from EPA’s Air Markets Program Data web site: <https://campd.epa.gov>.

⁸ *Summary of Market Modeling and Analysis of the Proposed Cap and Invest Program (DRAFT)* at 3, Washington Dept. of Ecology (June 2022) (“Ecology Modeling Report”).

⁹ Ecology Modeling Report at 10, 16 n. 27, 28, and 35.

4. Amend the requirement that a utility must request that Ecology allow the transfer to a requirement to a requirement that a utility notify Ecology of all necessary transfers on a periodic basis.

The first change reflects the CCA's directive that allocation of no-cost allowances to electric utilities be consistent with a forecast of a utility's demand (load).¹⁰ Because utilities would purchase power from covered entities for the purpose of serving load, the no-cost allowances that they are allocated for serving that load should be transferred to the electric generating facility that is serving the utility's load. Otherwise, utilities may have an incentive to bank free allowances while purchasing power from independent power producers who absorb compliance costs under the proposed rule.

Regarding the second change, not all utility power purchases are direct transactions with electric generating facilities. GHE asks that Ecology broaden the language of this section, particularly section 2(b), to clarify that the classification or status of the immediate counterparty to the utility's power purchase transaction does not limit the utility's transfer of no-cost allowances to the ultimate covered entity; or, more specifically, that Ecology may transfer allowances to the generating facility (covered entity) even if the electric utility transacted with a third-party marketer used by the generating facility, rather than directly with the covered-entity electric generating facility.

Regarding the third change, the terms "power purchase agreement" and "customer product contract" are not defined in the proposed rule and there would be no reason to limit allowance transfers to specific transactions. Therefore, GHE suggests either deleting sub-sections 1(d), 2(a), and 2(b), or altering 2(b) to more broadly state that the electric utility has transacted to purchase power, whether directly or through a third-party marketer, from the federal power marketing administration or the electric generating facility.

The fourth change is necessary to implement this section. "Power purchase agreement" is not defined in the proposed rule, and electric utilities may enter into multiple power purchase transactions within a short timeframe. For spot market transactions (i.e., those transactions that occur to serve short-term needs of the utility), requesting permission to transfer allowances prior to each such transaction may be impracticable. At the same time, GHE recognizes Ecology's need to facilitate and monitor transfer activity in a timely manner. GHE thus proposes changing the prior-permission requirement to a regularly scheduled notification requirement. Notification on a monthly basis would not be onerous for electric utilities, and it would provide Ecology with timely information to transfer and track allowances. GHE is also open to notifications over other timeframes, such as annual or for each compliance period.

Incorporating these four amendments, GHE requests that section 173-446-425 be amended as follows:

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) Upon purchasing power from a covered entity other than an electric utility, an electric utility must surrender~~wishing to transfer~~ no cost allowances to the compliance account of ~~the~~an electrical generating facility or federal power marketing administration in an amount equivalent to the amount of emissions associated with the purchased power. At the end of the calendar month in which the transaction occurred, the electric utility must provide~~may submit a request to ecology asking for the transfer and providing the following~~

¹⁰ RCW § 70A.65.120(2)(b).

information to ecology to facilitate the transfer: (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 ~~will~~ may transfer the allowances only if: (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.

Ecology Should Revise its Rule to Coordinate with Other Agencies

Designing, developing, launching and enforcing the CCA cap and invest program is a complex, multifaceted effort. To ensure the program will be robust and achieve the goals of the CCA, efforts to implement it must be deliberate and fully formed.

Ecology's implementation of the rule should not begin without a complete program design and clear compliance requirements. Ecology should not leave significant gaps or vagueness that allows electric utilities with unwarranted discretion to define what constitutes compliance with the cap and invest program. In short, Ecology must not skip steps or cut corners to meet the aggressive CCA timeline.

Along with Ecology, several other state agencies have significant responsibilities for implementing the cap and invest program. To fully achieve the intent of the CCA, it is important to for Ecology to coordinate its cap and invest program rulemaking with the Utilities and Transportation Commission ("Commission") and the Department of Commerce ("Commerce"). The state agencies' work should go on in parallel, but with clear identification of linkages and deliberate coordination of efforts.

Some integration of efforts by the agencies to prepare to implement the cap and invest program is occurring. However, it does not appear to be fully planned. There are gaps and lack of clarity about how the agencies' functions will fit together.

Examples of inter-agency coordination issues that Ecology's proposed rule should address the following topics related to compliance by electric utilities:

1. Ensuring that allocations of no-cost allowances to electric utilities are based on forecasts of resource dispatch costs that include allowance prices.
2. Establishing, by rule, specific requirements for how electric utilities should use their no-cost allowances to benefit their retail electric customers.
3. Requiring after the fact reporting by electric utilities to document how they used their no-cost allowances during each year, including for compliance and to provide other benefits to their retail electric customers.
4. The Proposed Rule should also describe whether, and if so, how, each utility's actual use of no-cost allowances will be trued up with the no-cost allowances that have been allocated to it.

Before adopting the Final Rule, Ecology should work with the Commission and Commerce to coordinate inter-agency work on the electric utility compliance issues listed above. A straightforward way to do this will be to develop compliance requirements in consultation with the Commission and Commerce. The Final Rule will then state the requirements and assign responsibilities to the Commission and the

Department to ensure that electric utilities comply with the requirements. This approach is similar to how the California Air Resources Board developed and implemented its GHG cap-and-trade program rules in coordination with other California state agencies, further supporting linkage between the two jurisdictions as desired by Ecology and allowed by the legislature.

Ecology Correctly Applies Emissions Factors for Generation Projected to Be Served by Natural Gas and for Unspecified Electricity

The Proposed Rule defines emissions factors for generation projected to be fueled with natural gas generation and for unspecified electricity as follows:¹¹

- (1) Total no-cost allowances allocated to electric utilities.
Allowances allocated to electric utilities for a compliance period are based on the cost burden effect of the program. Ecology will use the following methods to determine how cost burden and its effect will be used to allocate allowances to each electric utility for each emissions year.
...
- (c) Ecology will use the following emission factors to determine the emissions associated with the projected generation mix.
 - (i) For generation that is projected to be served by natural gas, the factor will be 0.4354 MT CO₂e/MWh.
...
 - (iv) For any generation from which the fuel type source is unknown or unknowable, and for unspecified market purchases, use the unspecified emission factor using the procedures identified in WAC 173-444-040. WAC 173-446-230.

For allocations of no-cost allowances to electric utilities, GHE agrees with and supports using an emissions factor of 0.4354 MT CO₂e/MWh for generation projected to be served by natural gas. This emissions factor is slightly higher than the typical emissions factor for modern combined-cycle gas-fired generation. It is also lower than typical emissions factors for single-cycle gas-fired generating facilities.

An emissions factor of 0.4354 MT CO₂e/MWh avoids over-allocating no-cost allowances to electric utilities. It also provides direct incentives for electric utilities to use generating resources that have lower emissions factors ahead of generating resources that have higher emissions factors when possible, thereby minimizing their overall GHG emissions in actual operations.

Grays Harbor also agrees with and supports using an emissions factor of 0.437 MT CO₂e for unspecified electricity.

Electricity Generated in Washington and Exported to Another Jurisdiction That Also Regulates GHG Emissions Should Not Be Subject to Compliance Requirements in Both Jurisdictions

Ecology's rules for implementing the CCA should not allow electricity generated in Washington to become subject to GHG emissions compliance requirements in more than one jurisdiction with a GHG emissions reduction program.

¹¹ WAC 173-444-404 identifies the following emissions factor for unspecified electricity: UCO₂e = 0.437 metric tons per MWh.

WAC 173-446-030 defines all entities that generate electricity in Washington and had covered GHG emissions of 25,000 or more metric tons of CO₂e during any year from 2015 through 2019 as first jurisdictional deliverers. This definition applies to electric utilities and non-utilities such as the Grays Harbor Energy Center. Further, WAC 173-446 requires utility and non-utility first jurisdictional deliverers to use emission allowances for covered emissions from electricity generated and used in Washington or exported to another jurisdiction. Meanwhile, the CCA also encourages linking Washington's GHG cap and invest program with GHG emissions reduction programs in other states. Therefore, to avoid duplicating GHG emissions compliance requirements for electricity that is generated in Washington and exported to another jurisdiction, the rules implementing the CCA should clearly identify which jurisdiction's GHG program applies to GHG emissions associated with the exported electricity.

For example, under rules for the California GHG cap and trade program, if an electricity generator is located in a jurisdiction that is linked with California, then the electricity generator's compliance obligations are with jurisdiction where the generator is located. Assuming that Washington's GHG cap and invest program is linked with California's, this approach seems reasonable for electricity generated in Washington and exported to California. The generator would comply with the Washington GHG program and there would not be duplicative compliance obligations for the California program. However, if and until the Washington and California GHG programs are linked, there is a risk of duplicative compliance obligations for electricity generated in Washington and exported to California. Similar concerns arise if other jurisdictions implement GHG programs but have not linked them with the Washington GHG cap and invest program.

GHE encourages Ecology to clarify its rules to address this issue to ensure that electricity generated in Washington and exported to an unlinked jurisdiction is not required to bear duplicative compliance costs in both jurisdictions.

Ecology Should Limit the Scope of its Consultants and Advisors Requirements

The Proposed Rule identifies an exhaustive list of services related to the cap and invest program or the GHG reporting program provided by consultants and advisors to registered entities.

Some of the services listed in WAC 173-446-056 involve assisting a registered entity demonstrate that it is in compliance with the CCA, including gathering data, developing and submitting reports. However, other services are also listed that are unrelated to reporting compliance, including services that are commercially proprietary to a registered entity and/or provided by a non-affiliated entity, including:

- (1)(g) Preparing or producing GHG-related manuals, handbooks, or procedures specifically for a reporting party or an offset project operator, authorized project designee, if applicable, and their technical consultant(s);
- (1)(i) Brokering in, advising on, or assisting in any way in carbon or GHG-related markets;
- (1)(s) Expert services to an emissions reporter or to the offset project operator, authorized project designee, if applicable, and their technical consultant(s) or a legal representative for the purpose of advocating the offset project operator's, authorized project designee's, if applicable, and their technical consultant(s)' interests in litigation or in a regulatory or administrative proceeding or investigation, unless providing factual testimony.

Each registered entity must disclose information about its cap and invest consultants and advisors to ecology, including the type(s) of services provided by each consultant and advisor.

GHE understands the rationale to identify consultants and advisors that assist a registered entity with reporting its compliance with the CCA. However, the requirement to report other broad types of consulting and advisory services is excessive. The CCA does not require registered entities to disclose information about providers of such a broad range of consulting and advisory services. Further, Ecology has not justified the requirement for registered entities to provide information about such a broad range of consulting and advisory services.

Invenergy recommends that WAC 173-446-056 be revised to limit disclosure requirements for consultants and advisors to those that assist registered entities in reporting compliance with the CCA.

Covered Entities Should be Able to Use Renewable Energy Credits as Offsets

The CCA defines an “Offset project” as “a project that reduces or removes GHGs that are not covered emissions under this chapter.” The Proposed Rule goes into more detail and requires that Offset Projects be “an individual activity or operation undertaken to reduce, remove, or avoid greenhouse gas emissions for the purpose of offsetting emissions elsewhere.” Under both definitions, voluntary renewable energy purchases should qualify as offsets valid under the CCA. Nevertheless, Ecology staff seem to take the position that voluntary renewable energy does not reduce emissions. Although it is unclear from presentation materials what this assertion is based upon, in GHE’s experience this is incorrect. If voluntary renewable energy displaces electricity demand that otherwise would have been served by carbon-emitting generation, then voluntary renewable energy certainly does reduce emissions. Indeed, renewable energy credits were a specified compliance instrument under the CCA’s predecessor, the Clean Air Rule. Under that rule, in GHE’s experience, renewable energy certificates were one of the most cost-effective means to comply with carbon reduction obligations. Emissions reductions from renewable energy credits are real, additional (if voluntary), quantifiable, permanent (insofar as that unit of electricity supplied by renewable energy, once consumed, cannot be replaced), verifiable through REC registries, and enforceable.

There does not appear to be any valid reason why renewable energy credits associated with voluntary purchases of renewable energy should not be eligible to be used as offsets to comply with the CCA or Proposed Rule. GHE thus asks Ecology to clarify that renewable energy certificates qualify as offsets under the Proposed Rule. GHE submit the following proposed language for consideration:

WAC 173-446-500

NEW SUBSECTION

(3) For the avoidance of doubt, renewable energy credits for eligible voluntary renewable generation that otherwise meet the requirements of this Section are eligible to obtain offset credits.

Covered Entities Should Receive Allowances or Offsets for Early Action

Whether greenhouse gas reductions occurred in the past or will occur in the future, they have the same effect on reducing the greenhouse effect and all of the associated harms the CCA recognizes. Accordingly, the CCA’s predecessor, the Clean Air Rule, provided credit for early actions taken by greenhouse gas emitting entities to reduce or mitigate their greenhouse gas emissions. Such credit provides emitters with the incentive necessary to continue, and even increase, their pre-existing carbon reduction commitments. In contrast, the Proposed Rule fails to provide credit for early action by

requiring offsets be registered by the arbitrary date of July 2019. This unsupported cutoff has the effect of disincentivizing early action, including especially offsets of greenhouse gas emissions between 2021 and 2023. This effect is contrary to the intent of the CCA to reduce greenhouse gas emissions.

In addition to the precedent of the Clean Air Rule, California’s cap-and-trade program, to which Ecology is pursuing linkage, also recognized the benefit of crediting early action to reduce greenhouse gas emissions. California’s Program for Recognition of Early Action Offset Credits (“Program”) was a program for issuing Air Resource Board (“ARB”) offset credits to early action offset projects. The Program provided a path for early action offset projects using an approved voluntary quantification methodology to convert early action offset credits into ARB offset credits. The Program allowed some greenhouse gas emission reductions and removal enhancements from qualified existing projects to become eligible for use in California’s Cap-and-Trade regime. By recognizing existing projects, it ensured that voluntary reductions received appropriate credit and helped create an initial supply of offset credits for California’s Cap-and-Trade Program, increasing the chance of liquidity for the first California Cap-and-Trade auctions. Ecology should act to not disincentivize emissions reductions, to create a robust pool of initial offsets, and be consistent with the cap-and-trade program that Ecology seeks to link with and recognize the value of early action offset credits. Ecology has not provided any indication that California would not insist on such consistency with its program in order to enter into a linkage agreement. By not adopting such a consistent provision in Washington, Ecology risks implementing a program that fails to reduce the costs of compliance and risks creation of an islanded emissions cap-and-trade program. This is counter to the legislature’s goals of maximizing emissions reductions while minimizing costs.

WAC 173-446-510(1)

...

~~(b) Any offset credits used must have been issued for reporting periods wholly after July 25, 2021, or within two years prior to July 25, 2021;~~

...

~~(d)... (i) The activities that result in GHG emission reductions and GHG removal enhancements are not required by law, regulation, or any other legally binding mandate applicable in jurisdiction in which the offset project is located, and would not otherwise occur in a conservative business-as-usual scenario;~~

Holding Limits Should be a Function of Compliance Obligations

While GHE is not opposed to a holding limit in theory, Ecology’s proposed limit that is mass-based and not at all connected to an entity’s compliance obligation disadvantages entities with larger compliance obligations, such as GHE. The stated purpose of the holding limit is to “protect the integrity of the auctions.” Sec. 12(6). Presumably, this also includes protecting the auctions against speculative, hoarding, and anti-competitive behavior. Whatever the goals of the holding limits, they will be better served and more fairly accomplished with holding limits that are a function of the covered entity’s compliance obligation rather than an arbitrary mass-based standard.

For entities that may not be covered parties under the Proposed Rule but who nevertheless hold allowances in a holding account, Ecology could either keep the mass-based standard in the Proposed Rule or make those entities’ holding limits equivalent to the holding limit for a covered entity with a relatively minimal compliance obligation. This kind of limit should function to reduce speculative behavior, while at the same time recognizing the different amount of allowances entities might hold at any given time based on their current or future anticipated compliance obligations.

To the extent that Ecology retains the holding limit in the Proposed Rule, it should clarify what is meant by “annual cap on emissions.” In any event, the requirement that “a covered entity or an opt-in entity may not buy more than 10 percent of the allowances offered during a single auction” should work to limit speculative allowance purchases even by the entities with the largest compliance obligation. Thus, Ecology can more fairly allow covered entities to cost-effectively and strategically meet their compliance obligations while limiting speculative behavior by tying holding limits to entities’ compliance obligations.

GHE thus recommends the following changes to the Proposed Rule:

WAC 173-446-150

...

(2) Holding limits.

(a) Except as provided in (c) and (d) of this subsection, the maximum total number of allowances of the current or prior vintage that a registered entity may hold in its holding account, its compliance account, or combination of both, is determined by the following:

$$HL_i = 0.1 \times 25,000,000 + 0.025 \times (C_i - 25,000,000)$$

Where:

HL_i = holding limit for year i

C_i = ~~annual cap on emissions~~ **entity’s compliance obligation** for year i

i = current year

(b) Except as provided in (c) and (d) of this subsection, the maximum number of allowances of each vintage subsequent to the current year that a registered entity may hold in its holding account, its compliance account, or a combination of both, is determined by the following:

$$HL_j = 0.1 \times 25,000,000 + 0.025 \times (C_j - 25,000,000)$$

Where:

HL_j = holding limit for year j

C_j = ~~annual cap on emissions~~ **entity’s compliance obligation** for year j

j = year subsequent to the current year

Electric Generating Facilities with Legacy Contracts Should Receive No-Cost Allowances

According to Ecology staff, Ecology seeks to link its CCA Program with the State of California’s Cap-and-Trade Program. The CCA defines linkage as “a bilateral or multilateral decision under a linkage agreement between greenhouse gas market programs to accept compliance instruments issued by a participating jurisdiction to meet the obligations of regulated entities in a partner jurisdiction and to otherwise coordinate activities to facilitate operation of a joint market.” Sec. 1(45). The goals of this linkage provision are, among other things, “to reduce the costs of compliance” and “provide consistent requirements” across jurisdictions. Sec. 24(1)(b). Thus, in order to reduce the cost of compliance and be consistent with California’s cap-and-trade program, Ecology should adopt California’s provision allowing electric generators with legacy contracts to obtain no-cost allowances for a limited period of time. Ecology has not provided any indication that California would not insist on such consistency with its program in order to enter into a linkage agreement. By not adopting such a consistent provision in Washington, Ecology risks implementing a program that fails to reduce the costs of compliance and risks creation of an islanded emissions cap-and-trade program. This is counter to the legislature’s goals of maximizing emissions reductions while minimizing costs.

The CCA and Proposed Rule already recognize such a type of contract that deserves protection against increased costs. See Sec. 14(9). As long as such contracts do not address the costs to comply with the CCA and were in effect as of July 2021, they are protected from increased costs until the end of the first compliance period. WAC 173-446-230(4). Consistent with this provision and with California's program, Ecology should extend similar protections to all electric generating facilities, not just those who have contracts with consumer owned utilities. By recognizing one set of contracts for legacy protection and not others, Ecology is vulnerable to challenges against the rules.

Rather, such as under the California program, the CARB allocated allowances annually to eligible facilities that generated electricity under legacy contracts in order to provide transition assistance for the Cap-and-Trade Program costs not recovered through those contracts. Legacy contract generators were required to submit information to CARB no later than June 1 of the calendar year immediately preceding the year from which the generator was seeking protection.

This "phased-in" compliance obligation for generators under legacy contracts is similar to treatment already provided under the Proposed Rule for waste to energy facilities and landfills. WAC 173-446-030(2), (3). Ecology should extend similar protections to electric generating facilities who were under contracts that did not allocate the costs to comply with the CCA as of July 2021. By not doing so, Ecology is vulnerable to challenges on the basis that the CCA Cap-and-Invest program unfairly prefers and provides benefit to certain covered entities but not others.

GHE therefore submits for consideration the following amendments to the Proposed Rule:

WAC 173-446-230

...

(4) A consumer-owned utility or electric generating facility that is party to a contract that meets the following conditions will be issued allowances under this section for emissions associated with ~~imported~~ the electricity that is subject to that contract, in order to prevent impairment of the value of the contract to either party.

No-Cost Allowances for EITEs Should be Available to all Electricity Providers

Under the Proposed Rule, Ecology is required to allocate no-cost allowances to electric utilities providing electricity to EITEs as follows:

If a facility is identified by ecology as EITE under chapter 173-446A WAC, and if allowances have not been otherwise allocated for the electricity-related emissions for that facility and to the facility under other provisions of this chapter, then ecology will allocate allowances at no cost to the electric utility or power marketing administration that is providing electricity to the EITE facility in an amount equal to the forecasted emissions for electricity consumption for the facility for the compliance period.

Certain EITEs may be eligible to receive electricity from an entity other than just an electric utility or power marketing administration. These might include, but are not limited to, EITEs that have exited the power supply of their utility (such as some entities have done with Puget Sound Energy) and EITEs that are served by on-site electric generating facilities. Accordingly, Ecology should revise WAC 173-446-230(3) as follows:

Change "...allocate allowances at no-cost to the electric utility or power marketing administration that is providing electricity to the EITE facility..." to "...allocate allowances at no-cost to the electric utility, power marketing administration **or other authorized entity** that is supplying electricity to the EITE facility..."

This revision will avoid undue discrimination against Grays Harbor Energy or other non-utility entities that may provide electricity to EITEs.

Ecology Should Clarify for which Administrative Costs Electric Utilities May Receive No-Cost Allowances

The Proposed Rule authorizes Ecology to allocate additional allowances to electric utilities for administrative costs of the program as follows:

An additional number of allowances will be allocated to account for the administrative costs of the program beginning in the second compliance period. The number of allowances allocated for this purpose will be determined by ecology based on a three-year rolling average of program costs derived from audited financial statements from utilities with a cost burden from the program. The mean allowance auction price from this time period will be used to translate average administrative costs into the appropriate number of allowances. WAC 173-446-230 (1)(f).

This part of the Proposed Rule is overly general, and that generality opens up the entire allowance program to abuse and manipulation. In particular, this provision does not define "administrative costs", including what types of costs may be included or how such costs would be reviewed and determined to be allowable. "Program costs" are also undefined. Allowable electric utility uses of the allocated allowances are also not defined. This is especially troubling given that the electric generating facilities not owned or contracted with the electric utilities, that nevertheless compete with utility-owned or contracted generation, do not receive no-cost allowances equal to their compliance obligations, let alone for administrative costs as well. Without further clarity as to how those no-cost allowances for administrative costs may be allocated and used, Ecology is vulnerable to challenges on the grounds that the program is anti-competitive and confers undue preference to certain compliance entities over others.

At a minimum, Ecology should revise WAC 173-446-230(1)(f) as follows:

1. Add a definition of "administrative costs" including scope and types of allowable costs
2. Replace "program costs" with "administrative costs"
3. Prohibit inclusion of costs (e.g., legal, lobbying) that an electric utility has incurred to oppose oversight of its compliance with the cap and invest program requirements
4. Require review and approval of administrative costs by the electric utility's governing board (e.g., by the WUTC for investor-owned utilities and by governing bodies for consumer-owned utilities) that the utility's administrative costs comply with cap and invest program rules before submission to Ecology.
5. Define how electric utilities may use allowances allocated to them for past administrative costs, such as:
 - a. Sale of the allowances to defray ongoing allowable administrative costs

- b. Use of the allowances for compliance
- c. Require allowances allocated to an electric utility for administrative costs be used exclusively for the benefit of the utility's customers

The Cap and Invest Program Must Reflect the Characteristics of the Washington Electric Utility Industry

The CCA and Ecology's proposed rule for the GHG cap and invest program are deliberately patterned after California's GHG cap and trade program. This is explicitly intended to facilitate linkage of the two programs. GHE supports linkage as a promising way to capture efficiencies and other benefits of a larger geographic market approach to reducing GHG emissions.

However, implementing Washington's cap and invest program and linking it with California's cap and trade program should not be done haphazardly. Instead, it requires recognizing and addressing Washington's distinct characteristics, including differences between it and California:

- Electric utility industry structure
- Statutory and regulatory requirements for GHG emissions reductions

Electric Utility Industry Structure

The organizational structures of the electric utility industry in Washington and California are significantly different. Examples include:

- In Washington, most GHG-emitting generation is owned or purchased under contract by investor-owned utilities (IOUs). In California, IOUs own relatively little GHG-emitting generation.
- In Washington, utilities both provide electricity supply and distribution services to their retail electric customers. In California, IOUs distribute electricity provided mostly by non-utility suppliers.
- A centrally dispatched wholesale electricity market.

Statutory and Regulatory Requirements

Statutory and regulatory requirements related to reduction of GHG emissions reduction also differ in Washington and California. Examples include:

- In Washington, no-cost allowances are allocated to utilities that provide electricity supply and distribution services to retail electric customers. In California, no-cost allowances are allocated to electric distribution utilities (EDUs).
- In Washington, the quantity of no-cost allowances allocated to electric utilities is set at 100 percent of their planned needs. In California, the quantity of free allowances allocated to EDUs is based on a declining cap.
- In Washington, utilities are not required to consign their allocations of no-cost allowances for sale in the auction. In California, IOUs are required to consign their entire allocations of no-cost allowances for sale in the auction.

- In Washington, utilities may use their allocations of no-cost allowances for compliance or consign them for sale in the auction. In California, IOUs are required to purchase all of the allowances they need for compliance from the auction.
- In Washington, because utilities are able to use most of their no-cost allowances for compliance, there likely will be relatively small amounts of revenues to be used for the benefit of retail customers. In California, revenues from sale of the utilities' entire allocations of no-cost allowances must be used to benefit retail customers.
- In Washington, because utilities can use their no-cost allowances for compliance, they have reduced incentives to use their no-cost allowances cost-effectively and to minimize GHG emissions. In California, because IOUs are required to purchase all of the allowances they need for compliance, they have direct incentives to use allowances cost-effectively and to minimize GHG emissions.
- In Washington, utilities may be incentivized to use their no-cost allowances for their owned generating facilities ahead of purchasing power from non-utility generating facilities. In California, IOUs have little if any ability or incentive to discriminate against non-utility generating facilities.
- In Washington, retail electricity rates include only the costs of allowances that the utility may need to purchase in excess of its allocation of no-cost allowances. In California, retail electricity rates include the costs of all purchases of allowances needed for compliance.
- In Washington, requirements for utilities to report their use of no-cost allowances is limited. In California, utilities have specific reporting requirements for their use of no-cost allowances.
- In Washington, utilities' ability to use their no-cost allowances for compliance will not ensure that wholesale market prices for electricity incorporate auction clearing prices for allowances. In California, requiring IOUs to purchase all allowances they need for compliance from the auction helps ensure that wholesale market prices for electricity reflect the auction clearing prices.

As described above, there are material differences between Washington and California, including utility industry structure as well as statutory and regulatory requirements. Overlooking these differences in rulemaking and oversight of compliance by electric utilities would reduce the effectiveness of Washington's cap and invest program and diminish the benefits of linking it with California's cap and trade program.

GHE is concerned that the Proposed Rule does not recognize the differences or identify solutions that could help limit negative impacts from them. Ecology should amend the rule in the ways described below and Ecology should also work with the Commission and Commerce to initiate a coordinated process to address implementation of the cap and invest program by the electric utility industry. The process should seek to:

- Ensure Washington electric utilities have clear incentives to use their no-cost allowances cost-effectively, minimize GHG emissions and avoid discriminatory use of allowances.
- Facilitate linkage of Washington's cap and invest program with California's cap and trade program by improving compatibility of both.
- Identify any needed additional regulatory requirements.
- Provide coordinated agency oversight of utility compliance with the cap and invest program and with other regulatory requirements for electric utilities.

Allocations and Actual Use of No-Cost Allowances Must be Reconciled

The Proposed Rule specifies how Ecology will determine the “cost burden effect” for each electric utility for each year. The Proposed Rule identifies several sources that Ecology may use to determine each electric utility’s cost burden effect. Then, another section of the Proposed Rule specifies how n- cost allowances will be allocated to each electric utility based on its projected emissions. WAC 173-446-230(1)(e). While the allocations of no-cost allowances to each electric utility will be based on projections, the utilities’ actual use of no-cost allowances for compliance with the CCA during actual operations in each year are likely to vary from projections. Examples of causes for variances include variations in the utility’s retail electric loads, higher or lower than average hydroelectric conditions, variations from projected prices for fuels and market prices for wholesale power.

Therefore, it is likely that the allocation of no-cost allowances to each utility will either exceed or fall short of the utilities’ actual need for allowances to meet their compliance obligations. If justified, such variations seem reasonable. However, Ecology’s rule does not provide a mechanism for reconciling differences between the allocation of no-cost allowances to an electric utility and the utility’s actual use of allowances. The absence of such a mechanism will make it difficult to determine whether the electric utility has used its no-cost allowances efficiently and, therefore, to minimize GHG emissions.

Conclusion

Thank you for the opportunity to provide feedback on the Proposed Rule. GHE appreciates the efforts of Ecology staff in putting forth the Proposed Rule within a short time.

Respectfully submitted,

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