

Comments of the Western Power Trading
Forum to the Arizona Department of
Environmental Quality on Implementation of
the Clean Power Plan

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The Western Power Trading Forum¹ (WPTF) offers these comments to the Arizona Department of Environmental Quality (AZDEQ) as it considers options for implementation of the U.S. Environmental Protection Agency's Clean Power Plan (CPP.) WPTF is an organization of power marketers, generators, investment banks, public utilities and energy service providers, whose common interest is the development of competitive electricity markets in the Western United States. WPTF has over 80 members participating in power markets within the western states, as well as other markets across the United States and Canada.

The impacts of the CPP on wholesale electricity markets, electrical system operations and grid reliability will be determined as much by the compliance choices made by individual states as by the targets and timelines established in EPA's final rule. Uncoordinated implementation by individual states in the Western Interconnect could distort electricity markets, increase risks to system reliability and increase compliance costs. In contrast, regionally coordinated emissions trading approaches that impose a consistent carbon price signal on generation would align with wholesale electricity markets and security- constrained economic dispatch, and support efficient electrical system operations.

Of the two emission trading options provided in the CPP, WPTF considers that allowance trading under mass targets presents the best opportunity for development of a broad carbon market. WPTF therefore encourages western states to pursue a mass-based allowance trading program under the CPP that covers both existing and new fossil resources and that can easily be linked to programs of other states (i.e. a 'trading-ready' plan). These recommendations are discussed in more detail below.

Harmonized emissions trading systems would align better with electricity markets and systems

Implementation by western states of linked emissions trading programs under the CPP would have significant advantages compared to uncoordinated, individual state implementation plans. These advantages include:

- Lower overall program costs due to the ability to reduce emissions across a wider geographic region.
- Emissions trading is consistent with economic dispatch, since the carbon price is internalized in generator operating costs.
- A harmonized emission trading system implemented by all states within the west would send a uniform carbon price signal to all generators within the region. This would ensure a level playing field for similarly situated resources, and avoid electricity market

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distortions. This is particularly important in light of increasing regionalization and integration of the western grid.

- Imposition of a carbon price via an emissions trading system would incent emission reductions across the entire electrical system without the need for separate implementation program elements targeted at specific areas, such as renewable generation and energy efficiency. The carbon price would alter the relative prices of high and low emission generation (including renewables) and increase the value of energy savings achieved through energy efficiency programs.

Allowance trading presents the best opportunity for a broad carbon market

Of the two emission-trading options provided under the CPP, allowance trading for mass targets and Emission Rate Credit (ERC) trading for rate targets, WPTF believes that allowance trading is more likely to be widely adopted by states, and therefore presents the best opportunity for development of a regional, or even national, carbon market.

ERC trading is not likely to be adopted widely by states due to a number of factors:

- ERC trading is a new concept that is completely untested.
- Issuance of ERCs from renewable energy generation and energy efficiency projects would require states to implement burdensome programs for monitoring and verification of emissions reductions from these activities.
- All emission reduction in the electricity system would not be creditable under an ERC trading system. For instance, emission reductions achieved by closure of facilities would not be creditable.
- The creation of ERC for generation by renewable resources could conflict with existing state renewable programs and Renewable Energy Credit (REC) markets. It is difficult to imagine implementation of an ERC market on top of a REC market.
- An ERC trading system would not provide states with the ability to capture and redirect carbon value to mitigate the economic impact of carbon pricing or to support other policy objectives. Rather, the value of ERCs is transferred solely between creators of ERCs and generators who require ERCs for compliance.

In contrast, allowance trading has several advantages:

- Allowance trading has a successful track record for both conventional air pollutants, as well as greenhouse gas emissions.
- Implementation of an allowance trading program requires monitoring of emissions only, not emission reductions
- Emission reductions across the entire electricity system are captured under an allowance trading system.
- The ability for states to determine how allowances are distributed allows states to alter the incidence of carbon costs, for instance by designating allowance revenue for electricity rate-payer relief, or to pursue other policy objectives.

- The two existing GHG emission trading programs in the United States, the California Cap and Trade system and the Regional Greenhouse Gas Initiative, are allowance trading programs. Additionally, the Federal Implementation Plan adopted by EPA will be likely be allowance trading program due to EPA's long experience with allowance trading.

For these reasons, WPTF believes that adoption of a trading-ready, allowance trading program provides the best opportunity for development of a broad, carbon market. We encourage AZDEQ to pursue such an approach.

New fossil resources should be covered by allowance trading programs

The CPP requires states that adopt allowance trading programs to either include new fossil resources under the program or to demonstrate that the program will prevent emissions leakage to new sources via specific allowance allocations or other means. If new fossil resources are not covered, these units would face lower operating costs than existing sources. This would cause a shift in emissions from existing to new sources. In order to ensure a level playing field for existing and new resources, WPTF recommends that AZDEQ include new fossil resources in the allowance trading system.