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VIA FIRST CLASS AND ELECTRONIC MAIL

Ms. Michele Totten
Connecticut Department of Environmental Protection
Bureau of Air Management
79 Elm Street
Hartford, CT 06106-5127
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RE: R.C.S.A. § 22a-174-31 – Control of Carbon Dioxide Emissions/ Carbon Dioxide Budget Trading Program and R.C.S.A. § 22a-174-31a – Greenhouse Gas Emission Offset Projects

Ms. Totten:

Pursuant to the notice of a public hearing dated December 28, 2007, issued by the Commissioner of Environmental Protection ("DEP") for the rulemaking proceeding to adopt §§ 22a-174-31 and 22a-174-31a of the Regulations of Connecticut State Agencies concerning the abatement of air pollution from electric generating units with a nameplate capacity equal to or greater than twenty-five megawatts, the New England Power Generators Association, Inc. ("NEPGA") hereby respectfully files these comments.[1] NEPGA is the largest trade association representing competitive electric generating companies in New England. NEPGA's member companies represent approximately 25,000 megawatts of generating capacity throughout New England, and over 7,300 megawatts of generating capacity in Connecticut, representing the vast majority of electric generating capacity in Connecticut. NEPGA's mission is to promote sound energy policies which will further economic development, jobs, and balanced environmental policy. NEPGA requests that all further correspondence, communications and other documents relating to this matter be served upon the undersigned as follows:

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[1] The views expressed in these comments do not necessarily represent the positions of each of NEPGA's members. In addition, nothing in these comments should be deemed to waive any rights that NEPGA or any of its members may have to challenge the procedural or substantive legality of the proposed regulation.

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I. Background

The Regional Greenhouse Gas Initiative (RGGI) is a cooperative effort by ten Northeast and Mid-Atlantic States to design a regional emission reduction program covering carbon dioxide emissions from power plants in the region. Beginning in 2009, emissions of CO_2 from power plants in the RGGI states will be capped at current levels, with the cap remaining in place until 2015. The states will begin reducing emissions incrementally over a four year period to achieve a 10 percent reduction by 2019. While the RGGI Model Rule requires the participating state's to allocate a minimum of twenty-five percent of Connecticut's CO_2 Budget Trading Program base budget to a consumer benefit or strategic energy purpose set-aside account, some states have announced intent to auction 100% of their allowances. Therefore, affected generators will need to acquire one CO_2 allowance under the CO_2 Budget Trading Program for every ton of CO_2 emissions from the facility. On October 26, 2007, RGGI released a report containing sixteen recommendations for the implementation of a regional allowance auction which will govern the manner in which generators can acquire CO_2 allowances to comply with RGGI.

Governor Rell signed the RGGI Memorandum of Understanding on December 20, 2005. The Connecticut Legislature, through the passage of Public Act 07-242, § 93, required the Connecticut DEP to adopt regulations to implement RGGI. PA 07-242 mandates that the emission allowance auction proceeds from the 10.7 million CO_2 allowances be invested in energy efficiency and renewable energy. The proposed regulations commented on herein, §§ 22a-174-31 and 22a-174-31a of the Regulations of Connecticut State Agencies, concern the adoption of regulations necessary to implement and comply with the RGGI in Connecticut. The regulations have been reviewed and approved by the Office of Policy and Management, the Governor's Office, and the Attorney General's Office. The resulting revised draft regulations, along with the DEP's response to public comments, will move to the Regulations Review Committee. Once approved, the DEP will begin implementing the regulations to put RGGI in place before the first auction, scheduled for June 2008.

II. Comments of NEPGA

NEPGA supports properly implemented measures to stabilize and then reduce anthropogenic emissions of CO_2 in an economically efficient manner that do not compromise the integrity of the competitive energy markets or the economy in New England. The restructuring of the New England market has been the product of many years of detailed negotiations and discussions among a wide range of market participants: utilities, regulators, customers, generators and other stakeholder groups. Among the benefits of the competitive market system has been substantial new investment in efficient generating plants, much of it in Connecticut.

These units are cleaner and more efficient, so emissions of key pollutants have gone down even as electricity consumption throughout the region has increased.

NEPGA is confident that Connecticut can achieve its economic and environmental objectives by incentivizing private investment in new technology that improve upon environmental efficiencies, while maintaining adequate electrical supply. However, the challenge of maintaining adequate electrical supply is constantly being burdened by regional demand increases, capacity shortfalls and the potential for loss of existing installed capacity from the hasty implementation of poorly developed regulations. Simultaneously, the industry struggles with the ability to develop generating infrastructure and to maintain existing capacity because of the complexities of permitting and stakeholder and political obstructions.

The growth in electrical demand drives the need for a prudent mix of generation, transmission and demand-side resources. Peak demand for electricity in New England is projected to grow nearly two percent per year over the next decade, and Connecticut's growth in demand will grow at a slightly larger rate than the aggregate of the region. [2] This requires adding the equivalent of roughly a 500-MW power plant to the New England system every year. In analyzing ISO-NE's most conservative estimates, the Connecticut Siting Council ("CSC") anticipates that Connecticut will face "a significant generation capacity shortage beyond 2008."[3] In consideration of the foregoing, NEPGA believes the following issues should be fully analyzed and implemented prior to the execution of a CO_2 allowance regulation in order to assure Connecticut consumers a reliable and cost effective electricity supply.

1. <u>The Auction for CO_2 Allowances in Compliance With RGGI Should not Interfere With The New England Energy Markets.</u>

The overall goal of regulations to limit carbon emissions is an important one, but Connecticut cannot ignore the fundamental market operations that are critical to the reliable operation of the bulk power generation system. New England's wholesale electricity market is a well-established, yet evolving marketplace that works effectively to value all products offered into the markets. The marketplace is an open-access trading platform that produces the lowest-cost solution to meeting the demands for reliable electricity. Despite the success of competitive electricity markets in attracting new investments, New England has a declining reserve margin and a corresponding need for energy resources; therefore, it is imperative that Connecticut successfully and accurately develop a plan that seamlessly interacts with the existing electricity markets.

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2 <u>2007 Regional System Plan</u>, ISO New England Inc., October 18, 2007.

3 <u>Review of the Ten Year Forecast of Connecticut Electric Loads and Resources 2007-2016</u>, Connecticut Sitting Council, November 14, 2007, Page 10.

2. <u>The Connecticut DEP Should Coordinate and Participate in the Regional Auction Programs Implemented by the RGGI Organization.</u>

In the absence of mandatory federal controls over greenhouse gas emissions, NEPGA supports Connecticut's participation in the regional auction for CO_2 allowances and would not support promulgating rules that are unique to Connecticut and inconsistent with the regional auction. Therefore, for the purposes of 22a-174-31(f)(4)(A), NEPGA is in favor of Connecticut participating in an auction conducted by the RGGI Staff Working Group, or a contractor chosen by the RGGI Working Group. Furthermore, Connecticut should endeavor as a part of that process to provide adequate consideration to the coordination of the RGGI auction and other CO_2 reduction auctions, specifically the Kyoto Protocol signed by the Canadian government on behalf of the Maritime Provinces.

Of particular interest to NEPGA is maintaining consistent criteria for qualifying offset projects under R.C.S.A. § 22a-174-31a with other regional programs, and the ability to trade allowances within the parameters of those programs. The global efforts being undertaken by numerous jurisdictions will inevitably affect the price and availability of allowances for the individual program participants, and have an undetermined corresponding affect on electric reliability in those areas. A regional auction will increase market liquidity, price transparency and prevent emissions leakage from within the region.[4] Connecticut should take an active role, with broad input from an organized stakeholder process, in developing a regional auction mechanism consistent with the state's energy, economic and environmental policies.

3. <u>The RGGI auction should be a simple and straightforward approach to meeting the goals of the RGGI policy and should contain the following elements:</u>

- **<u>Pricing Mechanisms</u>**: The auction pricing mechanisms should be straightforward and transparent. We recommend utilizing an "English Auction" without the use of a "shot clock" or "shoot out round" with the ultimate price for allowances paid by all purchasers established by the amount of the highest losing bid of the participating sellers. This style of auction is well understood and is compatible with the existing market structure utilized by electric participants in the RGGI region.

- **<u>Noncompliance Provisions</u>** - Generators should not incur multiple fines and penalties for noncompliance as anticipated by 22a-174-31(b)(5)(C). Furthermore, NEPGA disagrees that each ton of CO_2 emitted in excess of the CO_2 budget

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[4] "Emissions leakage" is the concept that there could be a shift of electricity generation from capped sources subject to RGGI to higher-emitting sources not subject to RGGI. *See*, Potential Emissions Leakage and the Regional Greenhouse Gas Initiative (RGGI): Evaluating Market Dynamics, Monitoring Options, and Possible Mitigation Mechanisms (March 14, 2007). *See also*, "CO_2 emission leakage refers to any increase in CO_2 emissions outside of the RGGI cap region <u>which offsets the CO_2 reductions in the RGGI region</u> with the cap imposed. (emphasis added) Evaluation of Impact of Regional Greenhouse Gas Initiative CO2 Cap on the New England Power System, Platts, et. al. at 20.

emissions limitation should constitute a separate violation as provided in 22a-174-31 (b)(3)(B). Such multiple penalties are administratively burdensome for the DEP and overly punitive for generators. The liquidity of the allowance market will remain undetermined until the auctions have gone through numerous iterations. Generators that are not able to comply as a result of market circumstances or inability to obtain allowances should be allowed to comply by alternative market payments consistent with compliance cost of allowances.

- **Review Process** - NEPGA recommends that Connecticut advocate for a comprehensive stakeholder process within the RGGI auction program similar to the stakeholder process utilized in the New England electricity markets. The working relationship between the ISO-NE staff, management, and board, and their willingness to meet with electricity market participants and stakeholders has fostered an atmosphere whereby the respective organizations can communicate their particular expectations for and needs from the electricity market. Involvement by the various stakeholder groups in the development and execution of the allowance auction program ensures a process that is particularly attuned to the needs of the respective stakeholder groups. The result of such an active stakeholder process would be a successful auction implementation and a more dramatic realization of the overall program goals.

4. Connecticut should not Reduce the Allocation of CO2 Allowances below the level of the RGGI MOU.

RGGI has established baseline emission inventories for each state within the region according to that state's historic emissions from the affected budgetary sources.[5] The RGGI Working Group intended to stabilize emissions at the 2005 levels, adjusted for the expected modest increase between the issuance of the Model Rule and the effective date of the program in 2009. RGGI further anticipated a phased approach, with initially modest emissions reductions, to provide market signals and regulatory certainty so that electricity generators could begin planning for, and investing in, lower carbon alternatives.

NEPGA is concerned that the allocation of allowances proposed by 22a-174-31§ (f)(3) and the retirement of allowances proposed by 22a-174-31§ (f)(5) is contrary to RGGI's initial phase in approach and may reallocate the emission baseline to a level that is insufficient to ensure reliable dispatch of all supply side resources. While the RGGI MOU allows Connecticut an initial base annual CO_2 emissions budget of 10,695,036 tons, Table 1 below illustrates how 22a-174-31§ (f)(3) reduces the amount of allowances that is available for electrical generators to 9,732,483 tons, a 9% reduction from the baseline state inventory. Given the absence of compliance options offered by the proposed program, and the unavailability of back-end emission control technologies, many generating units that are essential for electric reliability

[5] The initial regional cap is 188 million short tons of CO_2 per year, which is approximately 4% above annual average regional emissions during the period 2000-2004.

could unavoidably be forced to curtail operations or shut down completely. ISO-NE summarized the effects on the New England electricity market as follows:

> The RGGI cap-and-trade program would create CO_2 emission allowances needed by generators, which would have a market value. This value would be reflected in the generator bid prices, similar to how SO2 and NOx allowances are reflected today. This additional generator cost could shift the dispatch of the generators and their CO2 emissions, and potentially affect electric system operation and reliability in New England.[6] (emphasis added)

Table 1

		Auction Revenue based on Allowance Price/ton		
2009 - 2014	**Allowances (tons)**	$ 3.00	$ 5.00	$ 10.00[7]
CT Auction Account (91%)	9,732,483	$ 29,197,448	$ 48,662,414	$ 97,324,828
CHP Set-Aside Account (5%)	534,752	$ 1,604,255	$ 2,673,759	$ 5,347,518
Consumer Side DR (3%)	320,851	$ 962,553	$ 1,604,255	$ 3,208,511
Voluntary R/E Set-Aside (1%)	106,950	$ 320,851	$ 534,752	$ 1,069,504
Trading Program Base Budget (100%)	10,695,036	$ 32,085,108	$ 53,475,180	$ 106,950,360
Utility Energy Efficiency Accounts		**$ 22,259,044**	**$ 37,098,406**	**$ 74,196,812**

Despite the earnest intentions of this initiative, this is the most aggressive emission reduction auction in regulatory history. RGGI deviates sharply from other "cap and trade" emissions programs implemented by federal and state authorities because all of the allowances are sold to the compliance units; and, in fact, RGGI would not be properly categorized as a true cap and trade program.[8] The obvious distinction drawn between previously administered cap

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6 *See generally*, Evaluation of Impact of Regional Greenhouse Gas Initiative CO_2 Cap on the New England Power System, Platts, et. al.

7 These allowance prices are for reference purposes only, as NEPGA notes that studies have indicated that in order to see any kind of meaningful CO_2 reductions allowances prices would need to be priced at excess of $40/ton. The Inconvenient Math, Credit Suisse, Eggers, Dan, et. al.; Page 7, Exhibit 8. *See also*, "Carbon prices would need to be about $77/ton to meet a target of reducing emissions to 2005 levels 2012," *High Carbon Price for Gas Switch*; Argus Air Daily, Vol. 15, 20, January 30, 2008.

8 The common cap and trade approach first sets an overall cap, or maximum amount of emissions per compliance period, for all sources under the program. The cap is chosen in order to achieve a desired environmental effect. Authorizations to emit in the form of emission allowances are then allocated to affected sources, and the total number of allowances cannot exceed the cap. Individual control requirements are not specified for sources; instead, sources report all emissions and then surrender the equivalent number of allowances at the end of the

and trade programs and RGGI is that under the proposed RGGI program there is no allocation of allowances to affected sources. Additionally, because there is no commercially available emission reduction equipment that is available for significant reductions of CO_2 from electrical generating facilities, by practical exclusion the RGGI program is specifying the purchase of allowances as the only mechanism for regulated sources to manage their carbon emissions. Therefore, NEPGA recommends that Connecticut closely monitor the auction to prevent detrimental price increases or bulk power system disruptions from supply side resources that are unable to comply with the rigorous requirements of the initiative.

5. NEPGA Recommends a Clear and Transparent Expenditure of Auction Proceeds in a Manner that Best Accomplishes the Goals of RGGI.

Like other forecasts of allowance prices, NEPGA has made broad assumptions as to the underlying price of the CO_2 allowances in Table 1; however, there will unavoidably be a substantial aggregate cost to the affected generating units, and a resulting large amount of revenue for targeted programs. There is overwhelming and understandable interest from non-market participants in receiving the revenue generated from the CO_2 allowance auctions. Table 1 above illustrates that 22a-174-31§ (f)(4)(D)(iii) is likely to transfer a approximately $22,259,044 annually (assuming a modest $3/ton allowance price) to Connecticut Light and Power ("CL&P") and United Illuminating ("UI") without even the generalities of a skeletal framework, and without quantitative assurances, for the actual reduction of CO_2 emissions. Prior to the expenditure of any of the auction revenues by CL&P and UI, Connecticut should require that 100% of the allowance revenue be used for the benefit of the Connecticut ratepayers, and that utility shareholders do not enjoy guaranteed profits similar to those that are statutorily provided in their typical business models. The purpose of the RGGI program is "to stabilize and then reduce anthropogenic emissions of CO_2, greenhouse gas, from CO_2 budget sources **in an economically efficient manner,**" and any use of the public funds for the enrichment of the utility shareholders under the auspices of any environmental initiative is contrary to the RGGI rule and offends prudent energy policy.[9]

6. A Federally Administered Joint and Uniform Auction For Allowances Will Eliminate Issues of Leakage, Economic Parity and Provide the Most Effective Reductions in Carbon Emissions.

NEPGA believes that the most effective way to address carbon emission reductions is to develop a national, economy-wide program. To that end, Connecticut ought to provide a sunset provision in the RGGI rules that allows for its elimination and replacement with another rule should a federal program be implemented in the future, as opposed to plurality of compliance

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compliance period. *See*, Tools of the Trade: A Guide to Designing and Operating a Cap and Trade Program for Pollution Control; Environmental Protection Agency; http://www.epa.gov/airmarkets/international/tools.pdf

[9] RGGI Model Rule, §XX-1.1 (emphasis added)

mechanisms threatened by 22a-174-31(b)(8).[10] A regional program, by virtue of the small percentage of global emissions from the limited geographic size, cannot make significant impacts to the overall goal of reducing the amount of global greenhouse gases. Additionally the promulgated regulations should recommend that Connecticut advocate for a provision in any national program that allowances and offsets procured under RGGI will be recognized by the national program at a 1:1 ratio.

NEPGA is supportive of Connecticut's efforts to maximize the environmental efficiencies of, and reduce CO_2 emissions from, stationary sources. However, Connecticut should realize the benefits of a more comprehensive climate change action plan that covers other major sources of greenhouse gases and include direct focus on other economic sectors. NEPGA appreciates the opportunity to comment and requests that the DEP consider its comments as submitted herein. Please contact me if I can provide any further information.

Respectfully submitted,

Christopher P. Sherman
General Counsel

[10] "No provision of the CO2 Budget Trading Program shall be construed as exempting or excluding the owner or operator and, to the extent applicable, the CO2 authorized account representative of a CO_2 budget source from compliance with the provision of any other applicable state or federal law or regulation." R.C.A. 22a-174-31(b)(8), Page 31-13.