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June 5, 2008

VIA ELECTRONIC MAIL: steve.majkut@dem.ri.gov

Mr. Stephen Majkut, Chief
Office of Air Resources
Rhode Island Department of Environmental Management
235 Promenade Street
Providence, RI 02908-5767

Re: **Air Pollution Control Regulation No. 46; CO₂ Budget Trading Program and Air Pollution Control (“Regulation No. 46”) and Air Pollution Control Regulation No. 47; CO₂ Budget Trading Program Allowance Distribution (“Regulation No. 47) (collectively “the Regulations”).**

Dear Mr. Majkut:

Pursuant to the Notice of Public Hearing and Comment Period issued by the Rhode Island Department of Environmental Management, Office of Air Resources (“DEM”) dated May 2, 2008, and in response to the proposed regulations for rules for conducting auctions of CO₂ allowances created under the above referenced Regulations, in compliance with the Regional Greenhouse Gas Initiative (“RGGI”),¹ the New England Power Generators Association, Inc. (“NEPGA”) hereby respectfully files these comments.² NEPGA’s member companies represent approximately 25,000 megawatts of generating capacity throughout the region. 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:

¹ The Rhode Island General Assembly enacted legislation in June 2007 directing DEM to draft rules for Rhode Island’s participation in RGGI and to specify the mechanism for the sale of allowances, *See* RIGL 23-82 (2007).

² 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 administrative, procedural or substantive validity of the proposed regulation.

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Proposed Regulation No. 46 will regulate CO₂ emissions from fossil-fuel-fired electric generating units (CO₂ budget units) with a capacity of at least 25 MW or greater. CO₂ allowances (one allowance is equivalent to a permit to emit one ton of CO₂) will be auctioned or sold by the Department. To demonstrate compliance with the CO₂ Budget Trading Program, CO₂ budget units must provide one CO₂ allowance for each ton of CO₂ emitted during each compliance period. Proposed Regulation No. 46 will have incorporations by reference. Proposed Regulation No. 47 specifies the mechanism to auction or sell CO₂ allowances.

The total capacity of electric generating facilities in Rhode Island is approximately 1,800 MW of privately owned generation, representing approximately 6% of the region's generating capacity. ISO-NE forecasts Rhode Island's overall electricity demand to grow at a rate of 1% annually over the decade, with the state's peak demand, or summertime usage, to grow 1.7% annually over the next decade.³ Generators in Rhode Island sell into highly competitive markets where the prices they sell power at are determined by market forces. While NEPGA supports properly implemented national measures to stabilize and then reduce anthropogenic emissions of CO₂, we are cognizant of how external costs can distort the delivered price of electricity to the ultimate consumer and artificially inflate the price of electricity.

In the absence of a federal program, Rhode Island's regional effort must be implemented in an economically efficient manner that does 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 Rhode Island. These units are cleaner and more efficient, so emissions of key pollutants have gone down even as electricity consumption throughout the region has increased. From 1999 to 2003, as a result of competitive market signals for cleaner energy facilities, the competitive market has delivered 10,000 megawatts of privately financed energy facilities that have decreased regional carbon dioxide emissions by 7.5%, nitrogen oxide emissions by 44%, and sulfur dioxide emissions by 65%.

³ ISO – NE 2007 *Regional System Plan*, ISO-NE 2006 *Annual Markets Report*, and other ISO-NE, Inc. public information.

Generators want to continue to provide Rhode Island with the benefits that consumers have experienced and come to expect over the past several years. NEPGA is confident that this can be accomplished by incenting private investment in new technology to accelerate those benefits to improve the environment, 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. Simultaneously, the industry struggles with the ability to develop new generating infrastructure and to maintain existing capacity because of the complexities of permitting and stakeholder and political obstructions.

In consideration of the foregoing, NEPGA believes the following issues should be fully analyzed and implemented prior to the execution of a CO₂ allowance auction in order to ensure Rhode Island consumers a reliable and cost effective electricity supply.

1. Rhode Island should be Consistent with the Regional Auction Programs Implemented by the RGGI Organization.

NEPGA encourages Rhode Island to fully coordinate every aspect of the state auction with the other CO₂ reduction auctions. Of particular importance is maintaining consistent criteria for each program and the ability to trade allowances within the parameters of those programs. The regional and 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.

Ideally, NEPGA believes that the most effective way to address carbon emission reductions is to develop a national, economy-wide program. A single state or even 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. In contrast, a federal auction will provide greater market liquidity, price transparency and prevent emissions leakage from within the region.⁴ Accordingly, NEPGA urges Rhode Island to enact a sunset provision in the Regulations that allow for their elimination and replacement with another program should such a federal program be implemented in the future. Such a provision would be

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*, “CO₂ emission leakage refers to any increase in CO₂ emissions outside of the RGGI cap region which offsets the CO₂ reductions in the RGGI region 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.

consistent with the RGGI Memorandum of Understanding (MOU) which states as follows:

“when a federal program is proposed, the Signatory States will advocate for a federal program that rewards states that are first movers. If such a federal program is adopted, and it is determined to be comparable to this Program, the Signatory States will transition into the federal program.”

Contrarily, Regulation No. 46, § 3.6 states, *inter alia*, as follows:

No provision of the CO₂ Budget Trading Program... shall be construed as exempting or excluding the owners and operators... from compliance with any other provision of **any** Air Pollution Control Regulation, the Rhode Island State Implementation Plan, a federally enforceable permit, or the Clean Air Act. (*emphasis added*)

Accordingly, NEPGA is concerned that inadequate consideration has been given to the coordination of RGGI and other existing or proposed CO₂ reduction initiatives. Of particular concern are the potential inconsistencies of criteria for qualifying projects under each program and the ability to trade offsets within the parameters of those programs. The global efforts being undertaken by numerous jurisdictions will inevitably affect the price and availability of offsets for the individual program participants, and have an undetermined corresponding affect on electric reliability in those areas. These unknown affects seriously question the prudence of implementing regional programs that engage anything less than all emitting sectors on a national or international basis.

2. The Proceeds of the Emission Auction should be Used to Facilitate the Goals of a CO₂ Reduction.

There is overwhelming and understandable interest from non-market participants in receiving the revenue generated from the one-hundred percent auction. However, without even the generalities of a skeletal framework, no single proposal has been put forth with quantitative assurances for the actual reduction of CO₂ emissions among the competitors for these lucrative proceeds. While promising to be large, numerous questions still remain regarding the availability of revenues to actually achieve the goals of the program.⁵ 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 could unavoidably be forced to curtail operations or shut down completely. In order to maintain electrical reliability and

⁵ The purpose of the RGGI program is “to stabilize and then reduce anthropogenic emissions of CO₂, greenhouse gas, from CO₂ budget sources **in an economically efficient manner.**” RGGI Model Rule, §XX-1.1 (*emphasis added*) *See also*, “the Rhode Island component of the CO₂ Budget Trading Program, ... is designed to stabilize and then reduce anthropogenic emissions of CO₂, a greenhouse gas, from the CO₂ budget sources **in an economically efficient manner.**” Regulation No. 46, §15.1

cost effective electrical supply, Rhode Island should use emission credit proceeds to increase efficiencies at power plants so that actual greenhouse gases are reduced.

3. The Timing and Method of the Auction should be Consistent with the Goals of the Organized Electricity Markets.

Due to the uncertainties of the energy markets, as well as the absence of a functioning RGGI allowance market, generators are currently developing compliance strategies and are unable to properly gauge the likelihood of their success upon implementation. This problem transcends the normal market hedging issues that are experienced by generators pertaining to fuel procurement and the existing markets for environmental allowances, as those trading mechanisms are more developed in both the primary and secondary markets.

The dynamics of New England's competitive electricity market have provided tremendous benefits to the overall region. Of considerable importance to the New England economy is the fact that wholesale electricity prices in New England, adjusted for fuel costs and inflation, have declined by 16.5 percent during the four-year period from 2001- 2004.⁶ However, Rhode Island's retail rates, like those of the other states in New England, are well above national averages and the DEM should remain vigilant about the effects of the Regulations on the markets. ISO-NE summarized the potential effects on the New England electricity market as follows:

The RGGI cap-and-trade program would create CO₂ 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 NO_x 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.⁷ (*emphasis added*)

The liquidity of the allowance market will remain undetermined until the auctions have gone through numerous iterations. Despite the 3-year compliance period, it is conceivable for a generator to be unable to procure sufficient allowances depending upon the dispatch rate of the unit to meet market demands. DEM should consider allowing generators that are not able to comply with the Regulations 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. In this manner the Regulations will be liberally

⁶ ISO New England website, www.iso-ne.com. We have adjusted for inflation ISO New England's fuel adjusted nominal value of 11 percent to yield a real decrease of 16.5 percent.

⁷ *See generally*, Evaluation of Impact of Regional Greenhouse Gas Initiative CO₂ Cap on the New England Power System, Platts, et. al.

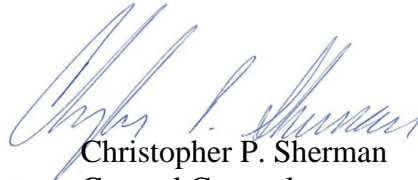
Mr. Majkut
June 5, 2008
Page 6 of 6

construed so as to permit the DEM “to effectuate the purposes of state law, goals and policies.”⁸

Finally, given the infancy of the mandatory carbon control process, NEPGA encourages the DEM to conduct auctions as far in advance to 2009 as possible. In furtherance thereof, NEPGA is supportive of the DEM’s proposal to distribute their 2009, 2010, 2011 and 2012 allowances on or before January 1, 2009, to the Rhode Island Auction/Sale account.

NEPGA appreciates this opportunity to provide written comments and requests that the DEM consider its comments as submitted herein. Please contact me at the information provided above if I can provide any further information.

Respectfully submitted,



Christopher P. Sherman
General Counsel

⁸ See, Regulation No. 46 § 15.3