Independent Power Producers of New York, Inc.

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Preliminary Comments on the RGGI Proposal Dated 8/24/05

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The Independent Power Producers of New York, Inc. (IPPNY) is an Albany-based trade association representing the competitive power supply industry in New York State, including companies involved in the development of electric generating facilities; the generation, sale, and marketing of electric power; and the development of natural gas facilities. IPPNY Members generate almost 75 percent of New York's electricity using a wide variety of generating technologies and fuels including hydro, nuclear, wind, coal, natural gas and biomass. New York State's electric system consists of approximately 100 companies operating over 700 separate units. In New York State, IPPNY Members have invested a total of $5.5 billion in their facilities and over $30 million in their communities. Additionally, IPPNY Members pay $291,431,875 annually in taxes. Our Member Companies directly employ 10,198 workers, with almost half of these represented by unions.

IPPNY submits these preliminary comments on the proposal (dated August 24, 2005) for the Regional Greenhouse Gas Initiative (RGGI), which the Inter-State RGGI Staff Working Group has developed for stakeholder comment and agency head deliberation. IPPNY appreciates the cooperative working relationship that we continue to have with RGGI decision-makers, especially the willingness of New York State environmental and energy agency heads and staff to listen to our concerns and suggestions for ways to improve the structure of the RGGI and the modeling which informs decision-making. Our comments address topics such as the pace of the RGGI and next steps; the need for a comprehensive and timely study of potential program impacts on the reliability of the electric system; the inclusion of a "fail-safe provision" to protect energy consumers and producers; the allowance auction approach and our suggested alternative; the need for unlimited offset projects; limiting the potential cap to one that stabilizes emissions and including credit for previous emission reduction investments; earlier review and sunset of the program; expert review of leakage; modeling issues; and improved energy, environmental and economic entity coordination on the development of the RGGI.

1. IPPNY's Overall Position on the RGGI

IPPNY is participating in good faith in the review of the RGGI's development, to help New York State environmental and energy agency heads and other RGGI decision-makers develop a workable framework for a regional greenhouse gas cap and trade program that can serve as a template for a potential national program and to avoid the anti-competitive impacts that would result from a New York State-only approach or an approach limited to a small subset of the RGGI participating states.

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2. Summary of IPPNY's Comments on the RGGI Proposal

RGGI Next Steps: The RGGI team should not rush to complete the design of the RGGI, and individual state agency heads should not be rushed in deciding whether or not to support the RGGI proposal and to sign-on to the Memorandum of Understanding (MOU). The development of the RGGI should continue to proceed at a pace that allows stakeholders to carefully review and comment upon detailed energy and economic modeling results, a cost-benefit analysis, and the MOU, the details of which have not been provided fully. The economic results presented to date are overly optimistic, and the RGGI team should evaluate potential economic impacts of the highest emissions modeling case, in order to better understand what potential worst case consequences might be. The economy has never before been more impacted by energy costs, and the RGGI should take care not to add to that burden.

Reliability Study: Until the two phases of the reliability study identified as necessary by the NYS Reliability Council are completed and reviewed, the RGGI team cannot know the appropriate structure of key program components. Completion of both phases of the study should precede state agency sign-on to the Draft Model Rule, in order to identify any reliability issues at the regional level and to inform the reliability considerations of each ISO area and each state. Any potential program operation must be monitored continuously to ensure that reliability impacts do not occur, and the RGGI design must avoid creating the need for Reliability-Must-Run (RMR) contracts.

Fail-Safe Provision: The RGGI Draft Model Rule should include a "fail-safe provision," also known as a "safety valve," to stop further implementation of the potential program, in order for a "reality-check" assessment to be completed of the root causes of any difference between reality and the projected modeling results and for any needed adjustments to the program to be made, including relaxing or suspending the cap. The fail-safe provision should be triggered when allowance cost levels exceed twice the estimated allowance cost of the final modeling package case on a year-by-year basis. Additionally, the Draft Model Rule should include provisions that require states to monitor potential implementation prior to 2015 and to modify, slow, or stop the program, if there is any indication that the program is having, or potentially could have, negative impacts on reliability, economic competitiveness, electricity markets, fuel infrastructure, or the ability of needed capacity to be built. The RGGI program relies upon the region being able to support a substantial increase in its reliance on natural gas fired generation. The Draft Model Rule should include provisions that require the states to monitor whether the fuel delivery infrastructure, such as pipelines or liquefied natural gas terminals, is being added at a rate that is sufficient to provide reliably for the demand of the projected growth in natural gas fired generation.

Allowance Auction Alternative: The proposed requirement for generators to purchase a significant amount of their allowances will negatively impact the reliability of New York's electricity system by reducing our fuel diversity – one of the cornerstones of our reliable system. The RGGI region is projected to need generating capacity and increased fuel diversity in order to avoid reliability risks, at the same point at which the RGGI is contemplated to start. The RGGI should abandon the auction approach for allocating allowances and should instead allocate all allowances to generators. Because an auction approach is largely untested, the RGGI will not serve as a successful template for a potential national program. As an alternative to the allocation of allowances for various public benefit purposes or supporting these programs via the auction of allowances (many of which already have programs implemented to address them, such as the System Benefits Charge Program in New York), the RGGI should allow public benefit programs to be eligible offset categories, thereby securing the environmental and consumer benefits of these programs, still allowing all allowances to be allocated to generators, and avoiding detrimental impacts to fuel diversity and reliability.

Offsets: Considering the difficulty of controlling CO2 emissions and the limited availability of viable compliance tools, the ability and flexibility to invest in offset projects should be encouraged without any limits. Given the wide acknowledgment of greenhouse gases as a global issue, it should not matter where offsets come from or what form projects take, as long as the level of emission reductions can be quantified and verified. Restricting offsets only would reduce compliance options for facilities potentially

subject to the Draft Model Rule, create higher consumer costs, potentially increase leakage, and encourage higher CO2 emissions elsewhere. The RGGI should expeditiously develop offset protocols for additional project categories and allow sooner use of CDM credits and EU allowances.

Cap: In considerations on how to apportion the cap among states, New York should get credit for its significant emission reductions prior to 2000 and the hundreds of millions of dollars in investments that energy producers and consumers made since 1990, especially given that, during that period, other potential RGGI states and those outside of the region increased their emissions and that New York's electric rates continue to be so much higher than those states. Furthermore, the RGGI potential cap structure should be limited to a cap that stabilizes emissions through 2015.

Program Review and Sunset: The RGGI should be reviewed sooner than 2015, such as in 2012 after the RGGI's proposed first compliance period ends. By 2015, the RGGI should be terminated, having been eclipsed by a potential national program. Under no circumstance should any potential implementation of the RGGI continue beyond 2015, in the event that a national program becomes available, because of the resulting severe economic disadvantages and market disparities. If a potential national program is not in place by 2015, then the reasonableness of continuing a regional-only program is questionable, and the RGGI should not be escalated by implementing a 10 percent reduction, given the risks to economic competitiveness, electricity markets, and reliability.

Leakage: A "Blue Ribbon" Panel should evaluate the issue of leakage, to avoid economic disadvantages for New York's power producers and energy consumers. Emissions data for SO2, NOx and Hg, both within and outside of RGGI, should be provided, so that emissions leakage can be assessed. Electricity imports and the issue of leakage need to be monitored continuously before 2015 to determine any needed program modifications. Furthermore, an unfettered offsets program can help reduce the potential impacts of leakage.

Modeling: Any perceived lack of funding for additional modeling should not dictate that RGGI policy should be based upon the current modeling results. The modeling assumptions need to be updated, because they appear to be significantly lagging the real world conditions, such as rising international oil demand and national natural gas demand giving rise to significantly higher fuel prices. An inadequate gas supply infrastructure will make achievement of the RGGI targets nearly impossible. Also, it is unclear why generating capacity is being added at a rate that significantly exceeds the load growth and why this additional capacity does not result in a significant decline in capacity prices. Additionally, it is a leap of faith to assume that load growth will decline as assumed in the base case assumptions and that the pursuit of conservation programs will be able to further reduce the load growth to approximately 0.6 percent per year. Additionally, RGGI stakeholders need to have the opportunity to review and comment on EPRI's modeling results on the role of nuclear power in the RGGI, and the RGGI should take these results into account, in terms of potential emissions, needed generating capacity, allowance prices, and changes in power imports.

Improved Coordination: The DEC, PSC, NYSERDA, NYISO, NYS Reliability Council, and the Empire State Development Corporation need to improve their coordination on the development of the RGGI program design and to ensure that any potential program does not impair electric system reliability, the competitive operation of electricity markets, and economic and job competitiveness.

3. The Pace of the RGGI and Needed Next Steps

Decisions Should Not Be Rushed

To help get the structure of the RGGI right, RGGI decision-makers adjusted the original timeline for program development, in order to ensure that important aspects of the modeling can be completed and that stakeholders have an adequate opportunity to review and provide comments on the results. This work has not been completed. The development of the RGGI should continue to proceed at a pace that

allows stakeholders to carefully review and comment upon modeling results upon which decision-making is based. The RGGI team should not rush to complete the design of the RGGI, given that the IPM energy modeling has been updated for the reference case and policy scenarios and only recently have spreadsheet results been provided for stakeholder review and comment. Although some detailed spreadsheets results have been made available, other modeling results have been communicated only as PowerPoint presentations, without adequate opportunity to review and comment upon the underlying assumptions and detailed results.

Individual state agency heads should not be rushed in deciding whether or not to support the RGGI proposal and to sign-on to the Memorandum of Understanding (MOU) by which the states are contemplating the potential implementation of the RGGI. Stakeholders need to have time to review and evaluate the implications revealed by the necessary reliability studies (as described in the next section) in order to advise state governments regarding the RGGI and the MOU. Indeed, stakeholders must have the opportunity to review and comment on the MOU and the actual wording of the Draft Model Rule, as well as the updated assumptions which support the Draft Model Rule, before any documents are endorsed by the states for potential implementation.

Costs and Benefits Need Review

Furthermore, the RGGI has yet to complete the economic modeling and cost-benefit analysis for the program and has yet to conduct an analysis of the potential impacts the proposal may have on the reliability of the electric system and the fuel diversity upon which that reliability is based. Economic modeling results presented to date have shifted the potential impact of the RGGI on the economy from a slight negative impact to a slight positive impact, in part based upon the estimated economic benefits of a likely over-reliance on energy efficiency measures. These economic results are overly optimistic, and the RGGI team should evaluate potential economic impacts of the highest emissions modeling case, in order to better understand what potential worst case consequences might be.

The cost-benefit analysis should evaluate the overall price impacts of the RGGI on energy consumers and the overall cost-effectiveness of the program, taking into account current and rapidly changing energy costs. The economy has never before been more impacted by energy costs, and the RGGI should take care not to add to that burden. This analysis should be repeated periodically and as needed before overall program review in 2015.

4. Reliability Study Needed

Maintaining energy reliability is central to the RGGI Program Goal. The RGGI must evaluate, with stakeholder review and comment, whether the RGGI proposal impacts electric system reliability. The New York State Reliability Council (NYSRC) and IPPNY have underscored the need for a two-phase reliability study of the RGGI. Until these reliability studies are completed and reviewed, the RGGI team cannot know the appropriate structure of key program components. Remarkably, some groups already are calling for changes to the RGGI proposal that would require deeper and faster emission reductions with decreased program implementation flexibility, when this reliability analysis on the current proposal has not been conducted and reviewed.

The first phase of the study must analyze zonal level outputs of the Integrated Planning Model (IPM) for New York for the reference case and a number of potential RGGI policy scenarios. This analysis is expected to provide an assessment of the reliability of the New York system criteria identified by the New York Department of Public Service as indicators of reliability (*e.g.*, energy and capacity pricing, plant retirements, build schedules and energy flows between zones). The first phase analysis also must determine the potential impact of the RGGI program on any generating units that may be critical to the bulk transmission system or distribution level individual load pockets, and the costs that may need to be incurred to mitigate those impacts.

The second phase analysis must involve more extensive modeling to determine more precisely the impact of expected or potential retirements and generating unit additions, which could result from any potential implementation of the RGGI, on the reliability of the bulk power system. A power flow analysis needs to be conducted to identify potential violations of thermal and voltage criteria under pre-and post-contingency conditions. Stability studies need to be conducted to evaluate the impact of those system changes on system reliability. Studies need to be performed to verify whether the minimum installed reserve margins, such as those assumed for the IPM, are reasonable, considering the modifications to the bulk power system configuration. Subsequent studies need to be required to re-evaluate the costs associated with implementation of the final cap-and-trade program.

In particular, the second phase of the reliability study must precede state agency sign-on to the Draft Model Rule, in order to identify any reliability issues at the regional level that may affect transactions between the NYISO, ISO New England, and PJM. These three ISOs need to work together with their Reliability Council-type entities and energy agencies responsible for reliability. The regional reliability analysis must be completed in order to inform the reliability considerations of each ISO area and each state, as the individual state processes examine whether and how they might implement the Draft Model Rule. Stakeholders need to be informed how the models to be used work and to have input upon the underlying assumptions.

Any potential program operation must be monitored continuously to ensure that reliability impacts do not occur, and the RGGI should decide how the program may be modified to avoid compromising reliability. The RGGI design must not lead to and must avoid creating the need for Reliability-Must-Run (RMR) contracts; use of these contracts would indicate that a reliability problem exists in contravention of the RGGI Program Goal and that an electricity market problem has arisen in contravention of state and federal actions to foster competition in the electric industry.

5. RGGI Needs "Fail-Safe Provision" and Monitoring/ Review Prior to 2015

The RGGI could come at a time of great uncertainty in the energy industry, with escalating fuel prices, rising demand, and the need for power plants to be built throughout the potential RGGI region for reliability purposes and to increase needed fuel diversity. According to the key finding of its "Draft 2005 Regional System Plan," New England will need to add generating capacity as early as 2008 and no later than 2010 and will need to increase the dual-fuel capability of gas-fired facilities to reduce system reliability risks. Similarly, in its recent *Power Trends 2005* report, the New York ISO strongly recommended that New York needs to add significant generation resources starting now to meet its reliability needs between the years 2008 and 2011. Additionally, the NYISO has stated that the Northeast must develop a more effective fuel diversity strategy. Furthermore, PJM has indicated that it requires additional capacity by 2008 to maintain its minimum reliability requirement.

The RGGI Draft Model Rule should include a "fail-safe provision" as a stop-gap to prevent adverse impacts on both energy producers and consumers. Due to uncertainties and what many believe may be significant optimism in assumptions used in the IPM energy modeling, the modeling projections may be significantly underestimating the potential impacts of the program. A fail-safe provision, otherwise known as a "safety valve," would stop further implementation of the potential program, in order for a "reality-check" assessment to be accomplished. The fail-safe provision should be triggered when allowance cost levels exceed twice the estimated allowance cost of the final modeling package case on a year-by-year basis. When the fail-safe provision is triggered, the RGGI team should perform automatically a review of the root causes of any difference between reality and the projected modeling results and make any needed adjustments to the program, including relaxing or suspending the cap.

Additionally, the Draft Model Rule should include provisions that require states to monitor potential impacts during the emission stabilization phase prior to 2015 and to take action to modify, slow, or stop the program, if there is any indication that any potential implementation of the program is having, or potentially could have, negative impacts on reliability, economic competitiveness, electricity markets, fuel

infrastructure, or the ability of needed capacity to be built. The RGGI program relies upon the region being able to support a substantial increase in its reliance on natural gas fired generation. The Draft Model Rule should require the states to monitor whether the fuel delivery infrastructure, such as pipelines or liquefied natural gas terminals, is being added at a rate that is sufficient to provide reliably for the demand of the projected growth in natural gas fired generation. A template for a successful potential national program would not run past any of these energy security danger signs.

6. Allowance Allocations Must Avoid Reliability and Fuel Diversity Impacts

To the extent that any RGGI program may be ultimately determined to be appropriate for implementation, the RGGI structure needs to be as flexible as possible in its potential implementation. There is no existing CO2 control equipment with which to retrofit power plants, and increasing demand and fuel prices make it less practical to switch fuels or reduce operations. As a result, the ability to obtain sufficient allowances is a primary compliance tool with any potential program requirements.

It is unclear how a cap and trade program will work, if there is an overly restricted supply of allowances available to meet the requirements of any potential cap. Remarkably, the RGGI Proposal includes major restrictions on the ability of states to decide how allowances should best be allocated. The proposal would allocate, via auction, at least 20 percent of allowances to public benefits programs and 5 percent of allowances to a Strategic Carbon Fund.

<u>Allowance Auction Jeopardizes Reliability</u>

IPPNY strongly opposes the provision of the current draft RGGI proposal to significantly limit the number of allowances that are directly allocated to generation sources. The requirement that generators purchase a significant amount of their allowances will negatively impact the reliability of New York's electricity system by reducing our fuel diversity – one of the cornerstones of our reliable system. The RGGI should abandon the auction approach for allocating allowances and should instead allocate all allowances to generators. Failure to allocate all allowances to generation resources will threaten reliability, since some units will face instantaneous financial impacts as a result of this policy.

A primary purpose of the RGGI is to serve as a template for a successful potential national program. This laudable and widely accepted goal will be unattainable, if an auction approach for allocating allowances is selected. Indeed, the use of an auction approach is largely untested. Given that all past successful national and European power plant emission cap and trade programs have not relied on an auction approach to allocate allowances, it is unlikely that a potential national CO2 program would adopt an auction approach.

Considering the difficulty of controlling CO2 emissions, allowances need to be available for use by generators in order to ensure the continued reliable operation of New York's electric system. The NYISO, ISO New England, and PJM each project the need for the RGGI region to add generating capacity and increase fuel diversity in order to avoid reliability risks, at the same point at which the RGGI is contemplated to start. Auctioning allowances will unnecessarily restrict the ability of power plant owners to comply with any potential program. In addition, the auction of CO2 allowances will have the most significant adverse impact on the very resources essential to maintaining New York's fuel diversity and reliability – coal and dual-fueled generators.

In order to maintain its electric system reliability, New England has resorted to using RMR contracts, which will allow power plant owners to recover allowance costs. New York has not needed to use these contracts and has avoided their anti-competitive implications. The RGGI must be designed so as to allow New York to continue to avoid creating the need for these contracts.

Facilities owned by generators have many operating limitations in wholesale day-ahead and real-time electricity markets, such as minimum generation levels, minimum run times and minimum down times. In

some instances, generators are required to use a minimum amount of fuel oil for reliability reasons, such as under the requirements of the NYS Reliability Council's Reliability Rule I-R3. Also, a significant number of existing generating facilities are subject to long-term contracts. Because these facilities have no way to recoup the additional costs of the auction approach, the resulting financial consequences could be severe, causing units which are essential to New York's fuel diversity and reliability to face shut-down decisions. In addition, the Northeast will be disadvantaged within capital markets, because any policy that ultimately forces a generation resource off-line will increase future capital rates, erode bond ratings and increase market risk profiles, resulting in increased costs for consumers in energy markets. These financial impacts and increased market risks will result in less investment in the electricity system, at the very time when the RGGI region will need to add additional generating capacity to preserve electric system reliability and increase fuel diversity. Failure to allocate all allowances to generation resources will create a credit and cash management shortfall that will affect the ability of generators to enter into longer-term facility investments, forcing the electricity market to rely on short-term financial arrangements and undercutting the generators' ability to make long term capital improvements with the assurance of revenues to support those investments. As a result, the assumed consumer benefit of the allowance auction approach would be lost.

Public Benefit Programs Should Be Treated as Offsets

As an alternative to the allocation of allowances for various public benefit purposes or supporting these programs via the auction of allowances, the RGGI should allow public benefit programs to be eligible offset categories. In this way, entities which are willing to make investments in these programs can work with those who wish to develop these programs. Similar to the types of programs noted in the RGGI proposal, these offset categories should include projects that achieve greenhouse gas emissions reductions from any sector and projects that stimulate or reward investment in technologies that will reduce these emissions from any sector. By treating these types of programs as offset categories, the RGGI will be able to secure the environmental and consumer benefits of these programs and still to allocate all allowances to generators, thereby avoiding the detrimental impacts to fuel diversity and reliability described above.

7. Offsets Must Be Available Without Limits

IPPNY appreciates that offsets are part of the RGGI Proposal; however, we still have concerns about how they are proposed to be implemented. Considering the difficulty of controlling CO2 emissions and the limited availability of viable compliance tools, the ability and flexibility to invest in offset projects should be encouraged without any limits. Indeed, the RGGI would be setting a precedent by limiting offset projects, since other greenhouse gas programs do not contain limits. Remarkably, the RGGI proposal includes limits on the availability, type and potentially even the location of offset projects; these restrictions result in an untenable program design. The RGGI should provide a detailed description of the offsets market analysis that was performed to assess the availability and cost of offsets in the RGGI region. Given the wide acknowledgment of greenhouse gases as a global issue, it should not matter where offsets come from or what form projects take, as long as the level of emission reductions can be quantified and verified.

Attempts to keep eligible offset projects inside the RGGI region for supposed economic reasons are neither practical nor necessary. As far as climate change is concerned, a ton of power plant CO2 emission reduction within the RGGI region is no better than a ton of CO2 sequestered in South America. Reducing global CO2 emissions should not be restricted to the efforts of the electricity generation sector or other sources in the RGGI region. Restricting offsets only would reduce compliance options for facilities potentially subject to the Draft Model Rule, create higher consumer costs, potentially increase leakage, and encourage higher CO2 emissions elsewhere. These restrictions would completely negate any reductions made in the region with a negative net impact globally. As a result, as early as possible during any potential implementation of the RGGI, the program should include a wide variety of offset options, not a restrictive few, since this course of action makes more sense economically and environmentally.

The RGGI should expeditiously develop offset protocols for additional project categories and allow sooner use of CDM credits and EU allowances; also, all offset categories that are eligible under the EU and CDM programs should be included in the RGGI offsets program. Furthermore, the RGGI team should include the numerous projects several companies have undertaken under the EPA Gas STAR program and continue to do with specific Best Management Practices (BMPs) and Inspection and Maintenance (I&M) programs. These sources of offset projects provide for robust offsets. Additionally, the RGGI structure should include offset projects, such as (1) natural gas transmission, distribution and storage, (2) investments in facilities, in addition to landfill gas generating facilities, which avoid emissions of methane from landfills, (3) projects that achieve greenhouse gas emissions reductions from any sector, and (4) projects that stimulate or reward investment in technologies that will reduce these emissions from any sector.

8. Cap / Review before 2015

IPPNY appreciates that the RGGI has chosen an initial cap which seeks to stabilize emissions. However, IPPNY is concerned about the starting point which would determine the level of emissions from which emissions would be stabilized into the future. In the early stages of RGGI discussions, the Inter-State RGGI Staff Working Group had indicated an intention to use 1990 as the beginning point to determine the starting level of emissions.

Despite any difficulties that the RGGI may be experiencing with getting data for all of the states going back to 1990, New York should not abdicate getting credit for its significant emission reductions prior to 2000 and the hundreds of millions of dollars in investments that energy producers and consumers made since 1990 through a variety of public policies (e.g., 6 cent law, system benefit charges), especially when other potential RGGI states and those outside of the region increased their emissions. Starting emissions reductions from 2000-2004 levels, without otherwise providing New York with the benefit of the reductions the State already achieved, does a disservice to the State's energy consumers and producers which made investments in New York and contributed revenues to enhance the State's economic well-being. As a result, New York is deprived of what rightfully would be a larger share of the budget, in its attempt to reach agreement with other states potentially participating in the program. New York must be given consideration for these prior investments and emission reductions in RGGI decisions on apportioning the cap, especially given the fact that New York's electric rates are so much higher than other RGGI states.

To help ensure a more successful template for a potential national program, the structure of the RGGI should not include a firm provision to implement the cap in two steps, that is stabilization and then a ten percent reduction after 2015. First, the RGGI should set any potential cap at a level that stabilizes emissions, monitor any impacts of potential implementation in relation to any need for a fail-safe provision, as described above, prior to 2015, and then fully evaluate the impacts of a stabilization cap before 2015. Remarkably, some groups already are calling for changes to the RGGI proposal that would require a regional stabilization cap that is lower than the proposed 150 million tons; indeed, according the modeling of the highest emissions case to date, it could be argued that the regional cap should be around 180 million tons.

IPPNY appreciates that the RGGI program will be reviewed and suggests that the review should occur before 2015. IPPNY also appreciates that the RGGI proposal includes a multi-year compliance period. IPPNY suggests that the RGGI program be reviewed in 2012, for example, after the RGGI's proposed first compliance period ends.

If the RGGI has succeeded in achieving its main purpose of being a template for a successful national program (in the event that such a program is pursued), then the RGGI should be terminated in 2015, having been eclipsed by a national program. If a national program is not in place by 2015, then the review of the program, with substantial input from electricity market participants and other stakeholders, should evaluate carefully whether it makes sense to escalate a regional-only program by implementing a 10 percent reduction, given the risks to economic competitiveness, electricity markets, and reliability.

Also, the RGGI may determine the program to be untenable, if it has not precipitated a potential national program by 2015. The RGGI should keep in mind that, before any potential RGGI program started, the region already achieved the emission reductions which would have been required by participation in the Kyoto Protocol.

9. Sunset and Linkage to Potential National Program

Under no circumstance should any potential implementation of the RGGI continue beyond 2015, in the event that a potential national program becomes available. The RGGI would need to defer to any potential national program for market and trading benefit purposes. A more aggressive RGGI program possibly operating in parallel to a potential national program would be extremely problematic, because of the severe economic disadvantages and market disparities that would result. Indeed, the Northeast region, which might undertake the Initiative to aid the rest of the nation in developing a program, would then be penalized for having taken that bold step.

10. Leakage

Issues of leakage need to be evaluated by an independent and market-knowledgeable "Blue Ribbon" Panel, in order to ensure that New York's power producers, business, and residents are not economically disadvantaged from any potential implementation of the RGGI in relation to those states which do not participate in the program. This evaluation is especially important, since the modeling indicates that economic expansion may occur outside of the region. Electricity imports and the issue of leakage need to be monitored continuously and well before the anticipated review of the program in 2015, in order to determine how the program should be modified to avoid negative impacts. Furthermore, an unfettered offsets program can help reduce the potential impacts of leakage.

Emissions data for SO2, NOx and Hg, both within and outside of RGGI, should be provided so that emissions leakage can be assessed. Due to the fact that power plant SO2, NOx and Hg emissions rates from RGGI states are generally much cleaner than surrounding areas, reduced generation within the RGGI states as a result of the regional power plant CO2 program could actually result in overall increase or shift of SO2, NOx and Hg emissions within the entire Eastern Interconnect Region, with a significant amount of these emissions being transported into the RGGI region with potential resulting air quality degradation. Due to different emission characteristics between different plants and fuels, it is not possible to extrapolate SO2, NOx and Hg emissions leakage from what has been projected for CO2.

Other air pollution control programs will help assure that SO2, NOx and Hg emissions will be controlled; however, the nature of cap and trade programs does not ensure that leakage will not be a problem for the RGGI region. The Clean Air Interstate Rule (CAIR) caps SO2 and NOx emissions over most of the Eastern U.S. but does not require that emissions will be controlled in any specific state or region (e.g., the Northeast) – only that, overall, reductions will occur within the Eastern U.S. Under SO2, NOx or Hg cap and trade programs, it is probable that some sources in states immediately upwind of the RGGI states will increase their emissions (while achieving compliance by purchasing allowances) as a consequence of generation leakage resulting from the RGGI. Similarly, the Clean Air Mercury Rule implements emission reductions through a cap over the entire nation. While the cap and trade provisions of this rule are being challenged, the fact is that at the current time nothing in the promulgated rule assures that mercury emissions will not increase in surrounding states as a result of generation leakage resulting from the RGGI. Finally, it is understood that the Ozone Transport Commission is evaluating "CAIR Plus" emission reduction requirements throughout the Northeast. However, no details have been developed, and there is no assurance that this initiative will protect against emissions leakage that may result from the RGGI. We understand that the IPM modeling of the RGGI has shown leakage may be a problem from the PJM system; however, it is many of those same sources in the PJM system that may increase emissions above their own states' emissions budgets under CAIR or similar other programs.

11. Modeling

Fuel Prices

The modeling assumptions need to be updated, because they appear to be significantly lagging the real world conditions, such as rising international oil demand and national natural gas demand giving rise to significantly higher fuel prices. The natural gas prices used in the modeling are well below current levels, and the downward sliding slope of gas prices over time continues to seem unrealistic as a base-case assumption. Any perceived lack of funding for additional modeling should not dictate that RGGI policy should be based upon the current flawed modeling results.

Capacity / Generation

The generation mix needs to be examined, especially in terms of the increase of natural gas facilities projected to be added in New York in relation to the relatively flat resource acquisition of other states. Additionally, it is unclear why generating capacity is being added at a rate that significantly exceeds the load growth and why this additional capacity does not result in a significant decline in capacity prices. Generation exceeding load growth by such a large amount makes the modeling results for both generation additions and retirements quite suspect. Also, the manner in which the RGGI proposes to treat capacity should be reconciled with any approach that the NYISO and the NYPSC take with regards to requirements for the retirement of facilities, especially in terms of impacts on reliability, energy prices, and fuel diversity.

Nuclear Relicensing

EPRI has recently released modeling results to help the RGGI better understand the impact on CO_2, if nuclear energy is not available. EPRI developed the results through a contract with ICF Consulting to run a limited set of modeling scenarios in conjunction with and using modeling assumptions defined through the RGGI. EPRI sponsored this project in the region, since funding was not available for these reduced nuclear capacity runs through the RGGI.

RGGI stakeholders need to have the opportunity to review and comment on these new results, and the RGGI should take these results into account, in terms of potential emissions, needed generating capacity, allowance prices, and changes in power imports. These modeling results indicate that the RGGI region will need to increase reliance on fossil-fueled base load generating facilities to replace the power generated by nuclear facilities, if those facilities are not relicensed.

Fuel Infrastructure

Concern remains regarding the ability of the natural gas infrastructure to support the assumed increase in natural gas demand, even before any potential RGGI requirements are imposed. An inadequate gas supply infrastructure will make achievement of the RGGI targets nearly impossible. In addition, a lack of infrastructure will put pressure on oil supply, especially as oil storage capacity also is declining, at the same time that greater reductions in coal-generated electricity could be required in an effort to meet the potential RGGI limits. The combination of these factors could increase concerns about reliability and fuel diversity, to the extent that dual-fueled facilities need both gas and oil and must compete for limited supply with other sectors at a time when the price of both fuels is escalating.

Demand / Energy Efficiency

RGGI stakeholders need to have the opportunity to review the assumptions and detailed spreadsheet results for the energy efficiency modeling; this modeling effort has been largely a “black box.” IPPNY recognizes the importance of energy efficiency in addressing energy demand, but the RGGI modeling results are premised on our ability to rely on achieving energy efficiency that goes well beyond what has

been achieved previously. It is a leap of faith to assume that load growth will decline as assumed in the base case assumptions and that the pursuit of conservation programs will be able to further reduce the load growth to approximately 0.6 percent per year.

12. Improved Energy and Environmental Entity Coordination

September 12, 2005 was a great day in terms of improved coordination on the RGGI by energy and environmental entities, to the extent that the Albany RGGI Stakeholder Meeting was attended for the first time by representatives of the DEC, PSC, NYSERDA, NYISO, and the NYS Reliability Council. However, the course of the discussion showed that these entities need to continue to improve their coordination on the development of the RGGI program design and to ensure that any potential program does not impair electric system reliability and the competitive operation of electricity markets. In particular, RGGI decision-makers need to be more involved at the top levels with the NYISO and the NYS Reliability Council, and these entities should continue to formally weigh-in on any potential market and reliability impacts. This coordination also should be expanded to include the Empire State Development Corporation, in order for the potential economic and job impacts of the RGGI to be evaluated appropriately.

Thank you for the opportunity to provide these comments on the RGGI Proposal.