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REGIONAL GREENHOUSE GAS INITIATIVE

COMMENTS ON THE MODEL RULE

May 22, 2006

Consumer Power Advocates (CPA) is pleased to offer these comments on the Model Rule proposed in the Regional Greenhouse Gas Initiative. CPA is a member organization of leading academic and health care institutions all of which are purchasers of large amounts of energy in New York City.

CPA supports global greenhouse gas (GHG) reduction, and recognizes that the electric industry serving the States participating in RGGI is a significant source of GHG. However, RGGI alone is not sufficient to resolving this important issue. RGGI will ultimately be successful only if its major provisions are extended nationally and even internationally. To that end, it is vitally important that the final rules mitigate impacts on energy users, and minimize any economic harm caused by higher energy prices attributable to RGGI.

To CPA, the most important issue left open by the Model Rule is the distribution of emission allowances among generators. In the Model Rule, up to 75% of these allowances could be distributed at no cost to the recipients, with the remaining 25% sold to generators through public auction. CPA believes that all allowances should be auctioned for public benefit, and that rate relief is the highest priority among the possible benefits. Auction of all allowances serves the goals of RGGI by providing a correct allocation of costs to those generators which emit the greatest amount of GHG, and by providing a source of revenue to mitigate the burden on energy consumers, whose continued support is essential for the success and expansion of the program.

The objection that the public benefit auction of all allowances will lead to higher energy prices is specious. In the NYISO markets, energy prices are set by the highest accepted bid into the hourly energy auctions. All generators receive this same price, regardless of their bids. Bids are limited to reference prices based on "costs," but these costs include opportunity costs. For example, if a generator had an inventory of fuel oil purchased at $1 per gallon, but the current market price of that oil increased to $2, the opportunity cost of $2 would be included in the reference price. Similarly, the market price of carbon allowances would be opportunity costs allowable in reference prices, regardless of the cost at which the generator receives them. There is virtually no dispute on this point: regardless of the method of allocation of carbon allowances, electricity prices will increase by the market value of those allowances.

CPA is concerned that this increase in the price of electricity will undermine public support for RGGI, and lead to the rejection of similar GHG control programs nationwide. To avoid this, it is essential that all emission allowances be auctioned, and the proceeds retained for public benefit. CPA believes that the most important public benefit in this context is rate relief for consumers, including large energy users. That will avoid the worst outcome in which industry leaves the region to chase low priced but dirty power, and RGGI becomes the policy to be avoided, rather than an example to be followed.

CPA suspects that some RGGI supporters welcome increased costs to consumers because they believe it will cause increased conservation and reduction in demand which in turn will benefit the environment, but this enthusiasm is misplaced here. It is undoubtedly true the high prices will encourage conservation, but that is only true when high prices exist universally. While the price impact of RGGI is uncertain, if that impact is large, the possible migration of industry to low cost States would not only defeat the purpose of reducing GHG emission, it would crystallize public opposition to further GHG control. The use of the revenue from the public benefit audition of all allowances would provide the funds to offset the increase in energy costs and avoid those unfortunate consequences.

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We expect some parties to cite the example of the SO2 trade and cap program which was successfully implemented several years ago. In that program, emission allowances were provided to existing sources at no cost. At that time, those sources were almost exclusively regulated utilities, whose rate were determined cost of service principles. Unlike the current market system, regulatory practice has never allowed the inclusion of opportunity costs in rates, and the value derived for those free allowances was retained for ratepayers, either through lower initial rates or through credits funded by the sale unused allowances. For example, in its current steam rate case, the Con Edison has proposed to refund over $2 million annually of unused SO2 allowances, and this is only a fraction of the total credits ultimately available for the Company's ratepayers.

CPA urges that all emission allowances created under RGGI be auctioned for public benefit.