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Mr. Franz Litz
NYS Dept. of Environmental Conservation
625 Broadway
Albany, NY 12233

Dear Mr. Litz,

As a significant regional stakeholder, NRG Energy, Inc. has provided its input on all aspects of the Regional Greenhouse Gas Initiative (RGGI) as the Memorandum of Understanding (MOU) was being developed. We very much appreciate the opportunity, on an ongoing basis, to continue to give you our comments and contribute to the comprehensive and constructive processes that implementing states will seek to follow in further defining RGGI. This letter contains our key concerns with four areas of the MOU as signed in December 2005.

NRG is a leading wholesale power generation company, primarily engaged in the ownership and operation of power generation facilities and the sale of energy, capacity and related products in the United States and internationally. In the RGGI applicable states, NRG owns just over 7,700 MW or a little over 8% of the installed fossil-fired generation. As you know, NRG is a strong advocate of a national program for dealing with greenhouse gas (GHG) and climate change issues in the United States. We believe that there are serious economic, efficiency and effectiveness shortcomings to having fragmented regulation on these issues; failing to serve our shared interests in reliable and affordable electricity supply that meaningfully balances environmental quality issues. Notwithstanding this position, as the RGGI states develop the model rule (ideally as a model to be pushed for implementation on a national basis), NRG would like to suggest that the following issues be seriously considered:

1. **Strategic Energy Set-Aside**

   A major concern with the components of the MOU is the consumer benefit allowance allocation or strategic energy set-aside. Although the MOU is silent on how these allowances will be administered, the popular view is that these allowances are going to be auctioned. The model rule must specifically propose how these allowances will be managed including, for example, any procedure for an allowance auction. Although, there are as yet no specifics available on details of any auction proposal, we note that auction design will fundamentally drive the resulting impacts. If this component is included in the model rule, we strongly recommend that a working group be established as soon as possible to develop the process so that any auction may be practically, efficiently and fairly administered.

- In our view, any allowance auction should be characterized and regarded as an experiment (compared to existing precedent) because, for example, the percentage of the allowance pool is potentially much larger than the allowances set aside in the Acid Rain Program auction. Also, individual states have the right to place more than the MOU minimum level of 25% of the state's allocation into an auction. Even if all states set aside just the minimum 25%, it is likely that most sources will have to participate in any sale process to get the allowances needed for operation and compliance, because there are not yet any commercially available control technologies to directly reduce CO2. Other options to reduce CO2 in response to incentives established in RGGI (by, for example, fuel switching to more expensive and volatile natural gas generation) will significantly affect fuel diversity in the participating states and potentially seriously undermine energy reliability.
- The issue of whether any proposed auction is open to everyone or limited to just affected sources will affect the market price of the allowances. An analogous situation is the recent price increases in SO2 allowances (primarily reflective of large financial institutions participating in the market). This has precipitated a shift in the SO2 allowance market and directly contributes to higher electricity prices for businesses and consumers, since emissions costs are directly factored in to market clearing prices for electricity. We see the potential for similar activities in a limited RGGI market to increase uncertainty for any RGGI CO2 auctions, with resultant higher CO2 allowance prices flowing through to participating states' householders on their monthly utility bills.
- Even after any auction implementation plan has been developed, the proposed auction participants need as much information as possible about the market to determine bid prices. Therefore, RGGI should aim to develop and apply an allowance tracking system well before the auction date. Developing a tracking system is a major effort and we believe the model rule should address this and get the implementation process started as soon as possible.

2. Leakage

The implication from comments made by members of the Staff Working at the last RGGI stakeholder meeting was that the leakage workgroup would be doing more modeling. NRG believes that the group should concentrate on developing a tracking mechanism to confirm the extent to which leakage "undermines the integrity of the program". That would necessitate defining what results would be regarded as undermining the program, and the means that will be used to determine if any increase in imports is due to increased demand or to RGGI costs imposed on the affected sources. For example, if a number of traditional coal plants are constructed just outside the RGGI region, or existing plants outside RGGI have the incentive to export more power into the RGGI region in response to rising power within RGGI states (already having some of the highest power prices in the country), then that would signal the existence of counterproductive incentives created by the program. However, we see this area as needing detailed attention, because it is unlikely that leakage signals will be so obvious.

3. Early Reduction Allocations

Comments by various stakeholders have suggested that the early reduction allocations should be included in the cap rather than in addition to the cap. NRG believes that this would be a mistake. All past cap-and-trade programs have permitted early reduction credits as a supplement to any established cap. Not only does this tried and tested approach reward companies for their early efforts to meet future targets, but it also facilitates compliance in the critical first years of a program. Contrary to the beliefs of the opponents of this approach, there are significant uncertainties related to how affected sources will meet the cap, suggesting that it would be prudent to follow successful past practices and award early reduction allocations on top of the cap. Further, one of the main assertions that such supplementary allocation is inappropriate has been that the CO2 cap is somehow intrinsically more important than the caps set for other programs. We view this as spurious at best, because the caps for SO2 and NOX have always been based on direct and immediate health-based goals.

4. Compliance Agents

Finally, NRG strongly recommends that the model rule explicitly address the issue of certifying agents for data and compliance submittals. Compliance with RGGI standards will be based on the CEMS data currently gathered, reviewed and certified by a site. These actions are typically performed by an agent, as defined in the CEMS regulations (40 CFR Part 75). RGGI should allow the use of those same agents for any RGGI submittals and compliance certifications.

If you have any questions concerning the information in this letter or require additional information, please feel free to contact Roger Caiazza 315-349-1361 or me at 609-524-4645.

Very Truly Yours,

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