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David J. Manning
Executive Vice President Corporate Affairs
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Ms Denise Sheehan, Acting Commissioner
NYS Department of Environmental Conservation
625 Broadway
Albany, NY 12233

Mr William M Flynn, Chairman
NYS Public Service Commission
3 Empire State Plaza
Albany, NY 12233-1350

Mr Peter Smith, President
NYSERDA
17 Columbia Circle
Albany, NY 12203-6399

Re: RGGI Program Proposal

Dear Commissioner Sheehan, Chairman Flynn and President Smith

KeySpan would like to commend the State's efforts and Governor Pataki's leadership in developing the recently announced RGGI Program Proposal. Mr Robert Teetz and Ms Cathy Waxman of my staff have been intimately involved in the stakeholder process conducted over the last two years by your team and they have advised me on a number of occasions that the work done by your Franz Litz and Karl Michaels in leading this effort for NY has been outstanding. They have made every effort to be fair to all stake holders, be they industry representatives or from the environmental community. They have listened intently, solicited and reviewed input and comments, incorporated suggestions and weathered a fair amount of criticism at times. Throughout, they have done so with professionalism and a clear desire to balance environmental objectives and economic impacts. We appreciate having had the opportunity to participate as invited stake holders thus far. We endorse the broad concepts of the RGGI Program Proposal as outlined by the NY representatives of the Staff Working Group and we offer the following comments which we hope will be constructive in adding detail to the proposal.

Level and Timing of the Cap

As you probably know, KeySpan has long advocated that mandatory greenhouse gas reduction initiatives be enacted at the national level. We, along with our industry colleagues on the Clean Energy Group, have supported federal CO2 legislation introduced by Senator Carper. With little movement nationally, KeySpan agrees that it falls to the region to demonstrate that a rational first effort in stabilizing the growth of CO2 emissions can be developed and implemented. We believe that the level of the cap, first achieving stabilization and then a modest, though, significant, 10% reduction by 2020, comprise a measured approach that might serve as a template for a national program. We recognize that some in the environmental community would prefer steeper reductions than what has been proposed and sooner, but with the Northeast already having the lowest CO2 profile in the country we do not believe that consumers in the Northeast should bear a further disproportionate burden of the energy costs to achieve reductions beyond those proposed. In fact, we hope that the State will proceed very cautiously as the program is implemented to ensure that the predicted modest costs of the program (as forecast by the modeling) are never exceeded.

We know that there has been much debate over the modeling assumptions. Some of them give us pause as well including the apparently low forecasted natural gas prices and the optimistic development of significant wind and other renewable capacity. Nevertheless, we recognize that the team employed the best available estimates in this regard. If these assumptions materialize, the modeling suggests that cost impacts should be relatively modest and compliance will be reasonably achievable. To assure this outcome we understand that the Staff Working Group (SWG) and the Agency Heads, as it moves forward, have built into the program, a review point in 2015 to determine whether the model results and forecasted impacts are actually materializing. We suggest that this review be sooner and more frequent, perhaps beginning no later than 2012, following the first true-up period ending in 2011. This will provide an opportunity for the regulators to make adjustments to the timing and or level of the cap so as to preserve the anticipated modest cost of the program. Mechanisms to accomplish this could include circuit breakers and/or safety valve concepts which would be triggered if model assumptions don't materialize or implementation costs rise above model predictions. Most importantly, regardless of the mechanism, the agencies, presumably with the PSC in the lead, should carefully and regularly measure program costs to assure they do not exceed expectations or further reduce the region's energy price competitiveness.

Leakage and Divergent State Policies

KeySpan is concerned that the desired benefits of the program could be diminished by increased emissions from sources outside the RGGI region that may occur through generation shifts to lower cost, higher emitting, energy in PJM. While model predictions

suggest that such leakage will be tolerable, KeySpan is aware that NY's own state power authorities are actively evaluating the development of over 1500 MWs of new transmission capacity designed to tap the PJM market. We believe this could be perceived as contrary to the environmental objectives of RGGI and could set an inappropriate example by the State. Energy from PJM, if comprised of the average mix of energy sources in PA, NJ, and Md, would be environmentally inferior to the alternative (new in-state capacity additions) also under consideration. For example, a 500MW line tapping average PJM energy sources could result in CO2 emissions 38% percent above the in-state alternative namely a new state-of-the-art, gas fired, combined cycle facility. Even more dramatic, Nox and SO2 emissions would be 50 times and 2000 times higher, respectively, not to mention the additional mercury! The following table exemplifies the concern.

Total Emission Comparison		
New Combined Cycle Gas vs. Average PJM Energy		
	500 MW Combined Cycle Gas (tons)	500 MW Transmission Line to PJM (tons)
Nox	85	4205
SO2	9	17,892
CO2	1,843,980	2,553,540
Hg	0	172 (lbs)

Higher emissions from upwind sources will only hamper NY's efforts to curb acid rain in the Adirondacks and achieve ozone and fine particulate attainment. RGGI implementation will only heighten the existing incentives toward leakage which could in-turn have a chilling effect on the development of clean, efficient generation in NY. We encourage the State to assure the adoption of a consistent and uniform energy policy approach across all of its agencies which is compatible with RGGI objectives and avoids the possibility of increased leakage particularly induced by its own agencies. Broadly speaking, we urge the agencies to add specific elements to the model rule, beyond the 5% Strategic Carbon Fund (which does not even address leakage related Nox, Sox and Hg emissions) to curb leakage that will cause increased emissions in non-participating upwind states as well as the exodus of rate payer dollars and possibly jobs from NY.

Offsets

KeySpan is encouraged by the proposed eligibility of natural gas efficiency projects for the creation of offsets. KeySpan believes that fuel switching of commercial, residential and fleet entities from coal, oil or gasoline to more carbon efficient natural gas fuel can significantly contribute to lower emissions in the region and increase the availability of offsets for compliance. We believe that fuel switching should explicitly qualify under the proposed offset eligibility program and encourage the SWG, and the State in its regulation, to specifically codify fuel switching to natural gas as eligible in the first phase of the offset program. Natural gas is 28% more carbon efficient than fuel oil and the economic incentive created by a RGGI induced carbon price signal will help stimulate the fuel conversion process. In addition, just as reductions in SF6 fugitive emissions have been listed as eligible in the first offset phase, we believe that reductions in fugitive methane emissions from natural gas distribution systems should be eligible as well. KeySpan would be happy to discuss the specific mechanisms for creation of fuel switching and fugitive gas emission reduction offsets at your convenience.

Public Benefit Allowances and Strategic Carbon Fund

While KeySpan prefers that all allowances, with the possible exception of a new source set aside, be directly allocated to affected sources, we understand the consumer cost mitigation rationale for withholding up to 20% for distribution via an auction process. Since this would be one of the first attempts to administer a cap and trade program including an auction process, we urge caution and perhaps a smaller percentage, beginning with 5-10%, on a trial basis. We are concerned that the proceeds from such auctions may not be utilized in a manner that most efficiently and effectively achieves further CO2 emission reductions. Accordingly, we propose that funds accrued through any auction process be made available not only to demand side efficiency and conservation programs but also to carbon efficiency improvement projects by generators. A mechanism which would channel the funding to the carbon efficiency improvement projects achieving the greatest CO2 reductions per dollar invested would be the most appropriate means of utilizing the proceeds. We would envision that such funds could be used to promote in-plant carbon efficiency improvements including lower carbon fuel utilization and repowering.

Allocation to Sources

While the program proposal does not contain specifics with regard to allocation, other than the suggestion that each state must consider the use of 20% of the allowances for public benefit, KeySpan strongly believes that the ultimate allocation formula adopted by NY should ensure that the cleaner fossil units receive sufficient allowances to cover their needs. The burden of any dearth of allowances resulting from the cap should be

experienced by the higher emitting sources, forcing them to be buyers in the auction rather than the cleaner units. Conventional oil and gas fired units have CO2 emission rates some 20% to 44% lower than coal units yet they operate primarily as the marginal units in the ISO market place. Gas fired combined cycle units have CO2 emission rates 60% below coal fired units and can also be the marginal units. Thus, the allocation formula developed should not add additional cost risk to these cleaner units. Such cost risk should be borne by the higher emitting, lower cost units. An allocation formula that covers the needs of cleaner units will help to narrow the price gap and make cleaner units more competitive.

Again, we commend the efforts of the NY team to fashion a well-reasoned and balanced RGGI Program Proposal. We endorse the program outlined as a reasonable approach and trust that the suggestions offered within this letter will help to add the detail that will be required as the process moves forward. Please feel free to contact me or Bob Teetz at (516) 545-2577 should you wish to discuss the concepts we've offered in further detail. KeySpan looks forward to continuing to work with you to address the climate change challenge and hope that our combined efforts will result in RGGI leading the way to a national program.

Sincerely,



David J. Manning
Executive Vice President and
Chief Environmental Officer

cc C Fox (Governor's Office)
F Litz (NYSDEC)
J Gallagher (DPS)
K Michael (NYSERDA)
M Lennon
R D Teetz
C Waxman