# Con Edison and O&R Comments on Issues Raised in November 2012 RGGI Stakeholder Meetings

December 20, 2012

Consolidated Edison Company of New York, Inc. and Orange and Rockland Utilities, Inc. (together, "the Companies"), respectfully submit the following comments in response to the issues raised in the November 20, 2012 and November 28, 2012 webinars hosted by RGGI, Inc. as part of the 2012 Program Review of the Regional Greenhouse Gas Initiative (RGGI).

*Introduction*

The Companies are committed to carbon emissions reduction and have supported RGGI since its inception. We believe that economy-wide carbon price signals are the most economically-efficient means of achieving carbon reduction goals, especially in Northeast, which already has one of the cleanest power generation fleets in the nation. However, we also recognize that regional programs like RGGI are an important step in the country's ongoing search for an effective mechanism to reduce carbon emissions. Accordingly, we value the opportunity to participate in the RGGI Program Review to provide input that considers the interests of the New York City/Downstate areas that we represent.

Now that the 2012 Program Review has reached its final stages, the Companies urge the States participating in RGGI ("the RGGI States") to carefully select program changes that foster a transparent and predictable market for carbon dioxide (CO2) emissions allowances that is not subject to adjustment, revision, or uncertainty regarding the regional emissions cap or the future supply of allowances in quarterly auctions. The Companies support changes to RGGI investment strategies that result in programs that facilitate the ability for customers to manage their energy usage, or for electric sector emissions to be reduced as a result of proper investment of allowance proceeds. Also, we support the use of a circuit breaker mechanism for allowance prices, similar to the cost containment reserve mechanism that was included in the final policy scenarios presented in the stakeholder webinars on November 20 and 28, 2012. At this time the Companies are not able to offer a position on the policy scenarios both because RGGI, Inc. has yet to release information on the impact each scenario would have on wholesale power prices and, by extension, customers' bills, and because the RGGI States have not made a formal commitment to invest auction proceeds in programs that directly benefit electric customers.

*Incomplete Information on Impact of Lower Cap Levels*

As of December 20th, RGGI, Inc. has not released any data that quantifies the potential cost impacts of the final RGGI policy scenarios. Previous RGGI modeling results included estimates of wholesale price impacts, but that information is absent from the final data. Additionally, stakeholders have not seen the complete results of a macroeconomic scenario analysis commissioned by the RGGI States as part of the 2012 Program Review. Several times during the Program Review process, RGGI, Inc. indicated that this information would be available to stakeholders. While the RGGI States may have access to the fully integrated modeling results – including bill impact analysis conducted as part of the macroeconomic study – RGGI stakeholders do not, and are consequently unable to offer the States an informed perspective on the future of the program. Without a concrete understanding of how changes to the regional cap and other program design elements will impact our customers, the Companies are not prepared to weigh in on the policy scenarios presented in the November webinars. We strongly encourage the RGGI States to make the complete package of modeling results – including Integrated Planning Model (IPM) results, wholesale price impacts, customer bill impacts, and Regional Economic Modeling, Inc. (REMI) modeling results – available on the RGGI, Inc. website as soon as possible.

*Transparency is Essential for RGGI's Future Success*

In order for the RGGI market to function efficiently after program changes are implemented, it must be transparent. RGGI's rules and parameters should be clear and consistent so that the impacts of the program can be forecasted and factored into future business and policy decisions for participants. Any changes to the regional cap, adjustments of future allowance supply, and decisions regarding retirement of unsold allowances should be clear and predictable. This has not always been the case, for example when New York State made the decision to retire its unsold allowances from the first compliance period without warning, depriving stakeholders an opportunity to comment. As previously noted in comments following the October 18, 2012 stakeholder session, the Companies support a one-time and irrevocable decision from the RGGI States about how they will manage unsold allowances and account for banked allowances for the duration of the program.

Furthermore, the Companies support making these changes known to market participants sufficiently in advance of the first auction subject to the RGGI program changes so that participants can appropriately plan for the changes, including any changes to the treatment of unsold and/or banked allowances from the initial RGGI program years. Making such an announcement will avoid a situation in which the States retire allowances on an inconsistent basis, or reduce the supply of allowances in future auctions and arbitrarily drive the RGGI market toward scarcity. Such non-market decision-making will only serve to introduce uncertainty and price volatility that would result in unnecessarily higher bills for our customers. Furthermore, it will penalize market participants, causing winners and losers not based on clear rules, but rather on arbitrary rule changes; such arbitrary wealth transfer would cause additional harm to customers across the RGGI region.

The Companies note that the States have not described, as part of the revised Model Rule, how they will treat unsold allowances. In the interests of transparency and to allow the market to function as intended, a clear approach to managing unsold allowances should be included in the final Model Rule when it is circulated for final public comment and prior to the initiation of any state-based rulemaking process. Additionally, the Companies request that the RGGI States commit to hold stakeholder proceedings to address any future program design questions, including, but not limited to, linkage with other sub-national cap-and-trade programs.

*Annual Cap Decline*

On October 12, 2012 PACE Energy and Climate Center submitted final modeling recommendations to RGGI, Inc. on behalf of a diverse group of RGGI stakeholders, including environmental advocates, generators, and utilities.[1] Among other things, the letter suggested that the RGGI States consider modeling scenarios where the annual cap reduction was both lower (1.5 percent) and higher (3.5 percent) than the current 2.5 percent decline rate. Having signed on to the PACE letter, the Companies were disappointed to learn that all of RGGI's final policy scenarios are structured around a cap declining by 2.5 percent per year. This original rate of decline was established because the initial RGGI cap of 188 million tons was seen as a moderate goal, whereas a decline rate of 2.5 percent per year from 2015 to 2018 would achieve the substantial CO2 reductions envisioned by the RGGI States at the program's inception. However, in subsequent years the region has seen large actual CO2 reductions – annual reductions have averaged about 9 percent since 2005 – due to unforeseen circumstances; these reductions have far exceeded the 2.5% reduction rate initially envisioned. The Companies are concerned that if the RGGI States shift the cap to a significantly lower level midway through the second compliance period, continuing a 2.5 percent rate of reduction may no longer be necessary or even feasible given changes in the RGGI region's generation portfolio, and for that reason, the comments submitted requested modeling of both a higher and lower rates of change.

It is important to recall that the generating fleet of the northeastern U.S. is already among the lowest-emitting in the country and now even more heavily dependent on gas-fired generation than expected when the RGGI program was initially conceived; nuclear and hydroelectric generation are also a large part of the current fuel mix. Such a fuel mix leaves only limited opportunities to use fuel-switching

[1] *Joint Modeling Recommendations to the RGGI States*, October 12, 2012.

to further reduce $CO_2$ emissions, as there is not yet a cost-effective means of reducing carbon emissions in these efficient, high-performing plants. If, as the States intend, the revised cap is set at a level that will be surpassed by actual emissions in a very short period of time, the Companies believe it is critical that the rate at which the cap decreases does not exceed the speed at which emissions control technology can be researched, developed and installed. Furthermore the cap decrease should not exceed the ability to achieve further energy efficiency, particularly in light of an economy that appears to be showing signs of growth once again. Absent new technology, an overly-ambitious cap reduction scheme could result in prohibitively high emission allowance costs, resulting in unnecessarily large rate increases for the Companies' customers. The Companies therefore reiterate their earlier recommendation for the States to analyze the relative benefits of a cap reduction rate at no more than 1.5 percent through 2020.

*Limit Cost Increases for Electricity Customers*

As noted in previous comments, the Companies support the concept of, and the proposed design for, cost containment reserves which release additional allowances into RGGI allowance auctions when specific price triggers are reached.[2] While there has been a great deal of RGGI stakeholder input on where the cost containment reserve (CCR) allowances should come from (i.e. 'under the cap' or 'above the cap'), the Companies propose that all reserve allowances come from outside the cap so as to avoid unnecessarily volatile allowance prices.

Presuming for a moment that allowance prices will reach the reserve trigger price as a result of a real or perceived shortage of available allowances, borrowing allowance supplies from future years to populate the CCR – reserves that come from 'under the cap,' in RGGI parlance – will only serve to exacerbate the scarcity of allowances, leading to further upward pressure on prices. Allowance market participants will base their bidding strategies on an established cap, expectations about future allowance supply under the cap, existing prices in the secondary market, and their compliance needs. On the other hand, injecting allowances from a CCR that is populated by new allowances 'above the cap', serves as an appropriate circuit breaker to mitigate extreme price impacts.

*RGGI Proceeds*

One aspect of the RGGI program's functionality that has been conspicuously absent during Program Review discussions is the RGGI States' strategies for investment of auction proceeds. While the Companies understand that this is an issue decided at the state level, it is difficult to make judgments

[2] *Con Edison and O&R Comments on Items Raised in the October 18, 2012 RGGI Webinar*, October 26, 2012.

regarding changes to the RGGI cap or flexibility mechanisms if the use of RGGI auction proceeds is not accompanied by a clear rationale and commitment to use the funds in an appropriate manner to further the goals of the RGGI program – to reduce carbon emissions in the electricity sector. At the inception of the RGGI program, the RGGI States assured stakeholders that auction proceeds would be reinvested in the states in ways that lowered the overall cost of compliance borne by electric customers. However, this reinvestment loop has not taken shape in all states, leaving electric customers with higher energy costs and no benefits to help reduce emissions and lower the impact of RGGI on their bills. Indeed, New York State has used the funds for general budget purposes, heating oil efficiency programs and cultivation of New York's clean technology sector. While several of these programs contribute to emissions reductions, they deny electric customers the opportunity to control their supply costs and achieve RGGI's goals, and instead act more like a tax in that they collect revenue and then invest in other sectors of the economy.

In other words, if left unaddressed, this break in the reinvestment loop would reduce the RGGI States' anticipated cap adjustment to little more than an energy tax hike collected through utilities' bills. The RGGI States could do more to improve the functionality of their cap-and-trade system if they consistently invested RGGI proceeds in end-use electric energy efficiency programs, or used RGGI proceeds to offset collections for other social benefit programs funded by surcharges on electric bills. The Companies therefore urge the RGGI States to carefully consider the importance of the proper investment of allowance proceeds as they fine-tune their proposal for RGGI program adjustments.

*Conclusion*

The Companies respectfully request that the RGGI States take these comments into consideration as they prepare a final proposal for revisions to the Model Rule. On behalf of our customers, who ultimately bear both the compliance costs of the RGGI program and the added cost of higher electricity prices, the Companies encourage the States to carefully weigh the impacts that changes to the RGGI program would have on our customers. We also continue to advocate for the release of additional modeling results as described herein. Overall, we believe that these recommendations would balance the benefits of RGGI's carbon price signals with reasonable results for customers.