

The State of New Hampshire
Department of Environmental Services

Thomas S. Burack, Commissioner

*Celebrating 25 years of protecting
New Hampshire's environment.*



April 19, 2012

The Honorable Bob Odell, Chairman
Senate Energy and Natural Resources Committee
Legislative Office Building, Room 102
Concord, NH 03301

Re: HB 1490-FN relative to Repealing New Hampshire's Regional Greenhouse Gas Initiative (RGGI) Cap and Trade Program for Controlling Carbon Dioxide (CO₂) Emissions

Dear Chairman Odell and Members of the Committee:

Thank you for the opportunity to comment on behalf of the Department of Environmental Services (DES) regarding House Bill 1490-FN, which seeks to revise and then (effective January 1, 2015) repeal New Hampshire's Regional Greenhouse Gas Initiative (RGGI¹) cap and trade program for controlling carbon dioxide (CO₂) emissions. In the interest of long-term regulatory and market certainty, DES believes that any contemplation of revisions to the state's RGGI program would best be considered in the larger context of the statutorily required 2012 comprehensive review of New Hampshire's RGGI program (pursuant to RSA 125-O:27). Therefore, DES does not support the bill and recommends that action be deferred pending completion of the 2012 review.

It is important to take this opportunity to clarify certain misconceptions about New Hampshire's participation in RGGI, and to focus on the fiscal impacts of which your committee should be aware.

First, and foremost, New Hampshire is economically better off participating in RGGI than not. Approximately half of the state's power consumption is purchased from the 6-state New England regional grid and the costs of RGGI implementation in the other states is reflected in the regional electricity rate. Were New Hampshire to withdraw from RGGI, DES and the Public Utilities Commission (PUC) estimate that this ongoing additional cost would be approximately \$6.7 million to New Hampshire ratepayers.² However, if New Hampshire continues its participation, the state would realize an estimated \$13 million from the sale of

¹ RGGI Fact Sheet, RGGI, Inc. website http://www.rggi.org/docs/RGGI_Fact_Sheet.pdf

² RGGI RATEPAYER COSTS DES and PUC 2-page handout

RGGI allowances allocated to New Hampshire to offset this additional cost, and would reinvest the proceeds in energy efficiency measures.³

A short-term (pre-2015) proposal under the bill would require direct (free) allowance allocation of nearly all of the allowances, rather than auctions (a small amount would continue to be auctioned to cover administrative expenses). Auctions have not been found by experts to have any greater impact on program costs than allocating allowances for free. These market experts assert that in competitive wholesale electricity markets, CO₂ allowances are treated as assets by electricity generators, regardless of how they are obtained. Therefore, the market value of CO₂ allowances is passed through in the price of wholesale electricity, regardless of whether CO₂ allowances are auctioned or distributed for free. As noted in a Congressional Budget Office report⁴,

“A common misconception is that freely distributing emission allowances to producers would prevent consumer prices from rising as a result of the cap. Although producers would not bear out-of-pocket costs for allowances they were given, using those allowances would create an “opportunity cost” for them because it would mean forgoing the income that they could earn by selling the allowances. Producers would pass that opportunity cost on to their customers in the same way that they would pass along actual expenses. That result was borne out in the cap-and-trade programs for sulfur dioxide in the United States and for CO₂ in Europe, where consumer prices rose even though producers were given allowances for free. Thus, giving away allowances could yield windfall profits for the producers that received them by effectively transferring income from consumers to firms’ owners and shareholders. The study of the hypothetical 23 percent cut in CO₂ emissions concluded, for example, that if all of the allowances were distributed for free to producers in the oil, natural gas, and coal sectors, stock values would double for oil and gas producers and increase more than sevenfold for coal producers, compared with projected values in the absence of a cap.”

Cap-and-trade programs with CO₂ allowance auctions benefit consumers by harnessing the value of the CO₂ allowances for investment in programs that reduce energy demand, create jobs, and enhance consumers’ control over their energy use and costs.⁵ In May 2007, the National Commission on Energy Policy recommended that not more than 50% of the total allowances should be allocated for free under a federal program, and the free portion should be

³ *Economic Impact in New Hampshire of the Regional Greenhouse Gas Initiative (RGGI): An Independent Assessment*,— University of New Hampshire (Gittell and Magnusson January, 2008) website http://des.nh.gov/organization/divisions/air/tsb/tps/climate/rggi/documents/unh_rggi_study.doc

⁴ *Trade-Offs in Allocating Allowances for CO₂ Emissions*, CBO, April 25, 2007

⁵ *RGGI Fact Sheet: RGGI CO₂ Allowance Auctions*, RGGI, Inc. website http://www.rrgi.org/docs/RGGI_Auctions_in_Brief.pdf

phased out over time, as the percentage auctioned increases.⁶ A February 2008 report by the Sightline Institute further explains the impact in its title: *"Why Free Allocation of Carbon Allowances Means Windfall Profits for Energy Companies at the Expense of Consumers"*.⁷

Although RGGI is clearly intended to reduce CO₂ emissions in order to address climate change, it is important to understand that it was only after significant study and debate that New Hampshire opted into RGGI as a "no regrets" policy that directly benefits the state both economically and from an energy independence perspective. These conclusions remain fundamentally sound today, whether one believes that climate change induced by emissions of greenhouse gases from human activity is occurring or not. While both the DES and the PUC participated in the development of RGGI, we did not endorse enactment of a New Hampshire statute until we were certain that the program would meet our state's needs and would not impose economic hardship on New Hampshire's citizens and ratepayers.

New Hampshire was one of the last states to become a participant in RGGI, and we did so only after a University of New Hampshire economic study confirmed that New Hampshire would be better off participating in RGGI than not, and that RGGI would have a net positive impact on New Hampshire's economy as well as help to stabilize and, over the longer term, reduce the state's electricity costs. Even then, New Hampshire's enabling legislation includes several safeguards to additionally protect the state from potential unintended consequences of any significant market volatility.

There are several additional significant benefits⁸ to implementing RGGI in New Hampshire. RGGI is an economic and environmental "win-win," a pro-business strategy that:

- helps to mitigate and ultimately reduce long-term energy costs via greater investment in energy efficiency;
- creates a market signal that encourages development of cleaner and, in many cases, more local energy sources;
- increases our energy independence with more local energy sources, thus keeping more energy dollars local;
- is a flexible, market-driven policy that begins to address the issue of climate change by capping and then modestly reducing regional CO₂ emissions from large fossil-fueled power plants;
- starts to reduce greenhouse gas (GHG) emissions to avoid the most deleterious projections of climate change impacts;
- increases economic opportunities for New Hampshire businesses for development of clean energy technologies; and

⁶ NCEP presentation dated May 1, 2007
<http://www.pnucc.org/documents/NCEPAllocatingAllowancesMay2007.pdf>

⁷ Sightline Institute report February 2008 <http://www.greencollar.org/UserFiles/ads-media/12681875174b97017d48ff9.pdf>

⁸ RGGI Benefits report February 2011 http://www.rggi.org/rggi_benefits

- places New Hampshire's generators in an advantaged position to respond to future federal policies and better manage carbon-constrained energy markets.

Market-based implementation results in competition, efficiency, and innovation that deliver emissions reductions at the lowest possible cost. New Hampshire's participation has allowed the state to mitigate the electricity cost impact of RGGI implementation throughout the rest of the region, as compliance costs have been reflected in the regional wholesale price of electricity. This has been accomplished through the creation of a state fund to increase energy efficiency from the sale of RGGI allowances.

One criticism heard during last year's House debate was that investments of state proceeds from RGGI allowance auctions are somehow perceived as beneficial only to those individuals, municipalities, and businesses directly receiving RGGI grants. To the contrary, any investment of RGGI proceeds toward energy efficiency directly benefits *all* New Hampshire citizens and ratepayers by reducing the overall demand for electricity, which in turn reduces the additional capital investment needed by electricity providers to meet increased demand. In particular, the high cost of "peaking" plants to meet demands on the hottest days of the year are reduced or avoided. All of these costs are ultimately passed on to all New Hampshire consumers, so keeping them low is in the best interests of all citizens, businesses and municipalities. Thus, investments in energy efficiency ultimately reduce costs for everybody.

It is important to remember that in any grant award process there will always be direct "winners" and "losers", and those not receiving grants may question the evaluation process. While DES believes that PUC staff have done an excellent job administering the Greenhouse Gas Emissions Reduction Fund (GHGERF) proceeds, there is always a legitimate conversation to be had over the statutory requirements for investment of the funds and oversight of the process used to award grants. It must be recognized that, in addition to the PUC's internal process, the Governor and Executive Council have and must still approve all grant awards recommended by the PUC. While there has been some criticism leveled at the grant awards process recently, DES staff have participated in this process, and based on our observations during this participation we believe the legislature can be assured that the funds have been administered in the full spirit of the statute and have been awarded to those recipients who demonstrated that they could get the "best bang for the buck" in terms of realized and demonstrable efficiency savings. This process was open to anyone who applied and met the criteria. DES stands ready and willing to discuss any suggestions for improving this process.

As noted above, the bill provides that 215,512 allowances would still be auctioned, presumably to cover administrative expenses of the program. It is estimated that revenues from the sale of 215,512 allowances would be \$416,000. This would not be sufficient to cover currently estimated administrative expenses of \$473,000. Furthermore, this bill, as amended, would prohibit the PUC from using GHGERF funds to contract with outside consultants after January 1, 2013. This would preclude the PUC from continuing to monitor, measure, and verify the results of its GHGERF grant program. Monitoring, measurement, and verification are critical components of the grant program, and DES requests that if this bill is to move forward in any

fashion, that it be further amended to ensure sufficient funding for all administrative costs, including the potential shortfall identified above.

It should also be noted that New Hampshire was one of the first states to get RGGI dollars flowing into its economy, and the results are already beginning to show significant energy savings and job creation according to a UNH analysis commissioned by the PUC. Specifically, grant programs in the first round of the RGGI Fund analyzed by UNH generated a savings of \$1.5 million to state businesses, communities, and residents. The lifetime cost reductions from the \$17.7 million awarded for this first round of grants are projected to be \$60.0 million, based on current energy costs. While necessarily some of the initial grants were awarded for certain "foundational" purposes (e.g., providing job training, benchmarking the energy performance of municipal buildings), subsequent grant rounds created far-reaching programs that will result in actual energy reductions across all sectors in New Hampshire. The so-called foundational grants totaled \$3,363,742, while direct impact grants totaled \$14.3 million in the first grant round. A summary of the UNH analysis⁹ and the 2011 Annual Report¹⁰ to the Legislature by DES and PUC further explain the economic and energy impacts of the initial RGGI grants.

Criticism was also expressed over the use of \$3.1 million from the GHGERF to help balance the Fiscal Year 2010 state budget. While we at DES also had concerns, we recognized that difficult budget decisions had to be made. It is important to put into perspective that, of \$34.72 million in RGGI allowance auction revenues generated during the period December 2008 through December 2011, nearly 90% has been spent on the intended use, namely energy efficiency. This is well in excess of the minimum 25% figure anticipated by the RGGI states' Memorandum of Understanding signed by Governor Lynch in 2005. Again, DES would welcome the opportunity to hear suggestions for better ensuring that the GHGERF is better protected to ensure the revenues are used solely for energy efficiency investments.

Lastly, many expressed concern that there is little that New Hampshire alone could do to reduce carbon emissions that would have any significant impact on climate change. This is exactly why RGGI was conceived. The RGGI states represent the 7th largest economy in the world when considered as a region, and our joint efforts under this initiative will reduce regional emissions of 165 million tons of CO₂ from the power generation sector by 10% or 16.5 million tons. This is a significant reduction and, in conjunction with other measures, will help the region achieve our joint climate goals while helping to secure energy independence and promote the transition to a new energy economy with associated job creation.

Implementing RGGI for New Hampshire is good policy, as it makes sense both economically and environmentally. New Hampshire does not operate in a vacuum, but rather is directly affected by the decisions made by other states. If New Hampshire alone were to

⁹ UNH report Executive Summary

http://puc.nh.gov/Sustainable%20Energy/GHGERF/Evaluations/GHGERF_Year%201_Executive%20Summary.pdf

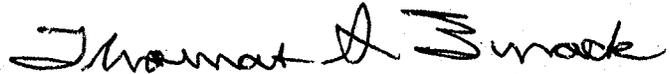
¹⁰ 2011 Annual Report to the Legislature by DES and PUC

<http://puc.nh.gov/Sustainable%20Energy/GHGERF/RGGI%20Annual%20Reports/2011%20RGGI%20Annual%20Report%20to%20NH%20Legislature%20102511.pdf>

discontinue its participation in RGGI, it would still incur the costs of the RGGI program without receiving any financial benefit. The RGGI program well positions the state onto the road to energy independence and a cleaner environment.

DES looks forward to working with all who share an interest in addressing climate change in an economically beneficial manner. Thank you for the opportunity to provide testimony. Should you have further questions or need additional information please feel free to contact Michael Fitzgerald, Air Resources Division (271-6390, michael.fitzgerald@des.nh.gov).

Sincerely,



Thomas S. Burack
Commissioner

cc: HB 1490-FN sponsors