

# The Regional Greenhouse Gas Initiative Comes to New Jersey

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AS WE ENTERED 2008, CRUDE OIL PRICES hovered close to \$100 per barrel, double-digit electric price increases were on the horizon, and the New Jersey Legislature, having completed the Global Warming Response Act, was busy working on additional climate and carbon legislation. Not a surprise. After all, oil pricing is unpredictable at best, electric costs are apparently uncontrollable, and, since other legislative business includes tasks such as balancing the budget, the politically responsible legislator is bound to focus efforts on climate change.

While climate-related issues (global warming, greenhouse gas emissions, carbon constraints, renewable energy, etc.) have been talked about for some time, the issues are steadily moving from theory into practice. Of the many climate and energy programs being proposed for New Jersey, one of the most ambitious is the Regional Greenhouse Gas Initiative (RGGI; read: "Reggie;" Assembly Bill 4559 (P.L. 2007 c. 340)).

Broadly, RGGI is the process through which 10 northeastern states have agreed to reduce and tax greenhouse gas emissions within their respective states. As proposed, each participating state will develop a similar regulatory program that will establish total emission caps, create "allowances" that append a dollar cost to the allowable emissions, and implement a process to auction those emission allowances to both the generators who need the allowances and to third-party speculators. Though the regulatory RGGI program will not manage a secondary emission allowance market, it is expected that the allowances will be tradable, and will be traded after the initial auction.

This concept might make the more skeptical of you, or even those of you who pay an electric bill, just a bit nervous. Justifiably so—a confederacy of state regulators setting out to save polar ice by taxing generating capacity and allowing financiers to profit from that tax does indeed sound like a recipe for bigger electric bills—after all, someone has to pay and it's unlikely to be Wall Street.

It has been argued that RGGI in fact misses the target: the bulk of energy consumed in New Jersey is related to transportation, not electric generation (of the total 2546.7 trillion BTUs of energy consumed in New Jersey in 2001, 49 percent was petroleum (i.e., transportation) while only 10 percent was electricity)—making vehicle traffic a major source of greenhouse gas emissions in New Jersey. Less traffic would then result in less of the unwanted emissions. Of course, with the state having identified toll increases as a means to offset budget shortfalls, there may be less incentive to remove the vehicle emission source.

Nevertheless, New Jersey's RGGI program was authorized and is scheduled to begin in January 2009. More importantly, RGGI and its progeny offer an opportunity for commercial and industrial electric users to gain control of their electric costs while proactively adapting to the impending carbon-constrained world.

Who will be affected by RGGI? First, RGGI will directly affect "compliance entities"—owners or operators of electric-generating units with a nameplate capacity of 25 megawatts or more and which hold an operating permit issued under the Air Pollution Control Act (an air permit). Owners of onsite cogeneration or combined heat/power units—onsite generators—are not considered "compliance entities," as long as they do not sell 10 percent of their annual gross generation. For onsite generators who do happen to sell more than 10 percent of their generation, there is an allowance price-control mechanism built into the legislation. If you are a compliance entity, or a seller of greater than 10 percent of onsite generation, it's time to gear up for January 2009.

Second, RGGI indirectly affects users (ratepayers) because it will increase the cost of generating and transmitting electricity. By requiring generators to purchase the right to emit greenhouse gases, RGGI will increase the overall cost of generation. Under existing conditions, that cost will likely be realized in the wholesale, and eventually retail, price of electricity. Power purchasers

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might seek to avoid the higher cost by purchasing from generators in non-RGGI states—the so-called “leakage” problem. “Leakage” refers to an increase in emissions from power plants located in non-RGGI states, which increase generation to make up for a reduction in generation within RGGI states; if RGGI makes a local plant less efficient, the power will be supplied from elsewhere.

However, there would be an increased transmission cost associated with that power. Moreover, the RGGI tax will theoretically allow non-RGGI state generators to increase their prices to just below the RGGI generator’s cost and still be competitive. Thus, even with alternative purchase options, RGGI could effectively add an additional rate increase on top of the increases that are now in the queue.

And the good news? The good news for commercial, institutional and industrial ratepayers is how the income from the initial allowances will be used.

The initial baseline CO<sub>2</sub> emissions for New Jersey under RGGI are expected to be just under 23 million tons. With a RGGI “allowance” being authorization to emit one ton of carbon dioxide or its equivalent, and initial (conservative) expectations putting allowance values at \$2 to \$3, it is expected that the auction of allowances will provide the state with a significant cash pool. That revenue will be held by the state in the ambitiously named Global Warming Solutions Fund. Three state entities will use fund monies for various energy and carbon-control projects in the state.

The New Jersey Economic Development Authority, which will receive 60 percent of the fund net, is of particular interest, because it is tasked with providing financial assistance to commercial, industrial and institutional entities to support end-user energy efficiency and emission reduction/efficient generation projects.

By feeding the power generation tax back to the end user to develop efficiency and alternative generation projects, RGGI provides a mechanism for commercial, institutional and industrial ratepayers to develop valuable capital assets that result in decreased electricity costs. Thus, though RGGI may cause the kilowatt hour cost of electricity to rise, implementing these projects should allow a reduction in kilowatt hours used, resulting in a reduced total energy cost. But keep in mind that expenditures from the fund must be appropriated by the legislature each year, and project planning will need to keep that contingency in mind.

Additional opportunities for the proactive ratepayer may become available: the Global Warming Response Act requires that by 2020, the state reduce greenhouse gas emissions to the 1990 statewide level; Renewable Portfolio Standards will require power generators to market power created by renewable sources; and under RGGI, generators will be able to use “offsets” in lieu of allowances to achieve compliance. These conditions will create opportunity in one form or another.

Regardless of whether you subscribe to the politics or policies, the carbon-constrained world is here—and with it—new opportunities for proactive entities to develop projects that will help control electric costs, increase use and generation efficiency, and reduce overall carbon footprints. ■

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