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Statement
Of the
AMERICAN PUBLIC POWER ASSOCIATION (APPA)
For the
HOUSE ENERGY AND COMMERCE COMMITTEE'S
Hearing to Review the Discussion Draft Entitled the "American Clean Energy and Security Act of 2009"
April 23, 2009

The American Public Power Association (APPA) appreciates the opportunity to provide the following testimony for the House Energy and Commerce Committee's hearing to review the discussion draft entitled the "American Clean Energy and Security Act of 2009." APPA represents the interests of more than 2,000 publicly-owned electric utility systems across the country, serving approximately 45 million Americans. APPA member utilities include state public power agencies and municipal electric utilities that serve some of the nation's largest cities. However, the vast majority of these publicly-owned electric utilities serve small and medium-sized communities in 49 states, all but Hawaii. In fact, 70 percent of our member systems serve communities with populations of 10,000 people or less.

Overall, public power systems' primary purpose is to provide reliable, efficient service to their local customers at the lowest possible cost, consistent with good environmental stewardship. Public power systems are locally created governmental institutions that address a basic community need: they operate on a not-for-profit basis to provide an essential public service, reliably and efficiently, at a reasonable price.

While APPA's oral testimony will focus on a few key issues addressed in the Waxman-Markey Discussion Draft ("Discussion Draft"), the written testimony will provide an overview of APPA's position on the entire draft bill given that much of the bill would substantially impact our members if passed as drafted.

Overall, APPA is concerned that the bill as drafted presents a substantial paradigm shift – electric utilities would be subject to more federal authority than ever before with regard to their decision-making and operation in a number of areas. This additional authority would range from how much renewable energy they will need to produce or purchase to the amount of mandatory energy efficiency that they will need to undertake to the greenhouse gas (GHG) emissions reductions that will be instituted. Therefore, the flexibility that has enabled electric utilities to keep costs relatively low for customers and provide a diversified portfolio of fuels would be substantially eroded by federal fiat, as envisioned by the draft bill.

We are also concerned that the Discussion Draft seeks to do too much at once, by addressing both climate change and other energy policy issues in the same legislative vehicle. We want to make clear that APPA supports federal legislation to address greenhouse gas emissions. We also support a federal renewable electricity standard if the standard does not exceed 15 percent for

electric utilities that sell over 4 million MWHs (megawatt hours) of electricity at retail annually, and if the additional provisions described below are included. However, we are concerned about both mandates applying simultaneously to the electric utility industry. Given the Discussion Draft's contemplation of a cap-and-trade regime to reduce GHG emissions, we believe that the electric utility industry should be given the maximum flexibility possible to meet the goals of such a mandate. Instead, the Discussion Draft contemplates three overlapping mandates on the utility sector at once – a cap-and-trade regime on GHGs, a federal RES of 25 percent by 2025, and an energy efficiency resource standard of 15 percent by 2020. This "straightjacketing" of the electric utility industry by Congress is likely to result in higher than necessary electricity prices.

Key questions for the Committee are: what are the public policy goals it would like to achieve and what would be the most efficient ways of achieving such goals? If the answer is that the Committee wants to promote development of renewable energy, energy efficiency and low-carbon resources, why is anything beyond a mandate to reduce GHG emissions necessary? Conversely, if Congress mandates high levels of renewable energy production and energy efficiency savings with the concomitant reductions in GHG emissions, what is the need for a complex, multi-decade cap-and-trade program? We would urge the Committee to consider addressing the extremely complex and potentially costly climate change title separate from the other provisions contemplated by the draft.

While APPA supports congressional action to reduce GHG emissions, we have not yet taken a position on the exact type of mechanism to be employed to achieve this goal. However, APPA has adopted a set of principles related to a cap-and-trade approach that appropriately conveys our concerns about the costs and complexity of such a regime if it does not include a strong cost containment mechanism such as a safety valve and if it auctions rather than allocates allowances, among other things. Our policy states that any federal cap and trade program should:

- Include a safety valve (which sets a maximum allowance price) or other stringent cost control mechanisms that mitigate price volatility and protect consumers.

- Minimize the initial auction amount to no more than five percent of total allowances to allow time for efficient markets to develop, to protect consumers and ensure continuing reliable operation of the electric system.

- Require the federal government to conduct regular reviews of allocations and auction of allowances in order to ensure they do not create windfall profits.

- Provide for effective market oversight, including strong enforcement and penalties, to prevent market manipulation

- Allow auction revenue to only be used for targeted R&D, energy efficiency, and mitigation of cost impacts on consumers.

- Provide for allowances sufficient to maintain reliability and to allow time to adapt. Generating units of 25 MW or less should be exempted from mandatory participation in the program.

- Allow credit for early action.

- Allow for regular reviews of the program to determine if changes are warranted to prevent the transfer of wealth and jobs to other countries that have not implemented climate legislation.

- Ensure that offsets are additional, permanent, independently verified, enforceable, and measurable. In addition, offset allowances should be available from an expansive set of sectors and activities without arbitrary geographic or quantity limits on the use of qualified offsets to meet cap requirements.

Our testimony below will provide our views on the Discussion Draft in its totality based on the provisions of direct impact to APPA's members.

Title I – Clean Energy

Renewable Electricity Standard. While there are many important and controversial questions facing the 111th Congress, one of the most important to the electric utility industry is potential passage of a federal renewable electricity standard (RES). APPA supports a workable federal RES mandate of no more than 15 percent by 2020 that includes provisions to: minimize costs to consumers; address grid reliability; provide for Congress to review the need for such legislation once a federal mandate to reduce greenhouse gas emissions is enacted; and allows for the deployment of energy efficiency measures to meet the standard, among other important issues. We believe such an RES would provide significant environmental and energy security benefits. At the same time, we believe an RES of 15 percent by 2020 is the maximum that this economy, electricity consumers, and the electric transmission grid can accommodate in the next 10 years.

In addition, a key concern for public power entities that would be subject to the RES is ensuring that federal financial incentives for renewable electricity – such as Clean Renewable Energy Bonds (CREBs) and the Renewable Energy Production Incentive (REPI) – are not subject to caps or funding shortfalls that make them largely unavailable to us in practice.

Any federal RES should include the broadest range of renewable energy resources to be used to comply with the standard, including those allowed under state renewable energy requirements such as animal waste biomass, incremental hydropower, and new hydropower added at existing hydro and non-hydro dams. In addition, a federal RES should allow a significant portion of the requirement to be met through energy efficiency measures, both utility system efficiencies and customer-based programs, including any such measures allowed under similar state requirements. Federal legislation should permit banking of excess credits to meet future year requirements and at a minimum, existing hydropower and municipal solid waste resources, including those owned by the federal government, should be excluded from the calculation of the baseline against which the renewable energy requirement is applied.

Any federal RES also needs to ensure that any credits that accrue to federally-owned generation marketed by the power marketing administrations (PMAs), including both existing generation and additions, either are provided directly to the PMA customers affected by federal or state RES standards commensurate with their allocations of federally-generated power or sold with proceeds going to repayment of affected projects as determined by federal power costumers in such marketing areas.

The draft legislation before the Committee proposes an extremely aggressive requirement of 25 percent by 2025 for utilities with retail sales of 1 million MWH or more annually. Proponents of this proposal claim that a 25 percent RES will actually lower electricity bills, as well as create

thousands of new jobs and somehow resolve the unavailability of substantial amounts of renewable resources in certain regions of the country. Such arguments are counter intuitive and should be considered carefully and with great skepticism. The fact is that most renewable energy resources are simply more expensive to develop than other alternatives, and will be for the foreseeable future, no matter what the scale of such development. That is precisely why Congress is considering mandating them and why Congress has provided significant financial incentives (mostly to private entities) for their development over the past several years: so that development will actually occur despite their higher cost.

Cost increases associated with an RES will pose special challenges for low-and moderate- income households as these consumers tend to spend a larger share of their budgets on energy related products and services. Electricity consumers in regions where wholesale electricity markets are operated by regional transmission organizations or independent system operators under the supervision of the Federal Energy Regulatory Commission – regions where many consumers are already facing electricity bills that look more like mortgage payments – will pay even more due to the flawed design and operation of those markets. And increased costs will be even more of a problem if an RES is combined with, or soon followed by, climate change legislation, which will have yet additional costs for the consumer. Finally, the intermittent nature of some renewable resources (such as wind and solar) poses challenges to transmission grid reliability as a higher proportion of this type of generation come online. Electricity must be generated and transmitted instantaneously to meet customer demand, which requires a majority of electric generating facilities to be available 24/7. Because the wind doesn't always blow and the sun doesn't always shine, even as forecasted, other types of generation – most often natural gas - must be available to back up these resources.

The engineers operating transmission systems report that, given existing technology and capacity constraints, 15 percent of the grid relying on these resources is more manageable from an operational standpoint than a higher number and will ensure greater stability of the grid in the future. We understand that Congress is also considering new policies designed to spur grid expansion and enhancements, but those proposals are still in the developmental stages and, even if enacted, it will take many years to site, design and construct the actual facilities.

The current draft legislation does not include a waiver provision from the federal RES. APPA believes it is important that the Secretary of Energy is authorized to provide waivers of compliance or penalties on a case-by-case basis. Such waivers potentially would be available, but not limited to, the effects of natural disasters, the recognition of utilities in "negative load growth" circumstances and other economic, operational and contractual impacts, and delays in relevant federal permitting approvals, among other situations to be determined.

Of significant concern to APPA is that the draft RES legislation currently before the Committee would apply to utilities with annual retail sales of 1 million MWH or more annually. APPA opposes this low threshold and supports a more reasonable level of 4 million MWH or more of annual retail sales. The Small Business Administration defines electric utilities of 4 million MWHs or less as "small businesses." This definition has been retained in a variety of statutes, including the Small Business Regulatory Flexibility Act (SBRFA), which codify the widespread recognition that federal regulation is more burdensome on small businesses. The 1 million MWH threshold set in the Discussion Draft ignores the well-defined government definition of an electric utility small business. This threshold would capture 61% of public power customers while the 4 million MWH threshold would capture 43% of public power customers. It is also important to note that public power utilities' ratepayers will experience the full impact of increased costs from implementing an RES since private companies may be able to absorb some of the additional costs

by reducing dividends paid to their shareholders. Not-for-profit public power utilities have no choice but to pass on increased costs to their customers in the form of higher rates.

For these reasons and those set forth in the attached policy resolution, APPA believes our support for a workable 15 percent federal RES by 2020 for utilities with annual retail sales of 4 million MWH or more annually and which include the other provisions described above would strike an appropriate balance to allow Congress to move forward on this important issue. We would support such an RES if it moved on a stand-alone basis.

Carbon Capture and Storage. APPA supports additional and expanded federal support for research, development, and deployment (RD&D) of cost-effective technologies to reduce, capture, transform, transport, or sequester greenhouse gases from emissions sources throughout the economy; and for legislative emission reduction targets to be consistent with commercially available technologies. APPA believes that aggressive research and development must be conducted in the short-term to prudently evaluate the feasibility for future commercial deployment of carbon capture and sequestration (CCS) technologies for reducing carbon dioxide (CO_2) emissions from fossil fuel-fired electric generation. At present, there is not commercially proven and demonstrated CO_2 capture technology or geologic sequestration for reducing CO_2 emissions from utility scale power plants that generate electricity from either coal or natural gas. There are several small power plant CO_2 separation demonstration projects in the U.S., but current technologies in development are prohibitively expensive and require inordinate amounts of energy to operate. It is unclear at this point how long it will take to advance and scale up this technology for widespread application in the electric utility sector.

Given this situation, APPA supports congressional efforts to accelerate RD&D of CCS technologies, including Section 115 of the draft legislation, which mirrors H.R. 1689, the Carbon Capture and Storage Early Deployment Act, bipartisan legislation that was introduced earlier this year by Congressman Boucher (D-VA) and others. During the 110th Congress, APPA worked with Congressman Boucher and other utility industry stakeholders to make significant improvements to similar legislation (H.R. 6258) that were encompassed in the bill introduced this year. The legislation would establish a $1-1.1 billion annual fund, derived from fees on the generation of electricity from coal, oil and natural gas. Grants from the fund would be awarded to large-scale projects advancing the commercial availability of CCS technology. The financing mechanism laid out in the CCS Early Deployment Act provides an important and appropriate bridge to accelerate much needed funding prior to the availability of revenues from a national cap on emissions.

APPA believes that the RD&D efforts should include assessment of legal liabilities associated with CO_2 sequestration, because the ability to secure financing for long-term sequestration projects will depend on who is legally responsible for the sequestered CO_2 during and after the sequestration period. Resolution of the liability issue will be necessary to obtain financing and insurance for new generating units with CCS once the technology becomes available. Additionally, Congress must allow for the testing and verification of the viability of geologic storage in different regions of the country, and in multiple types of geologic formations, before requiring actions that assume the widespread practicality of geologic storage.

New Source Performance Standards. The Discussion Draft contains language in Section 116 which, if enacted, would establish a new source performance standard (NSPS) under the Clean Air Act's NSPS for CO_2 for new coal-fired power plants including possibly some which have received valid permits from state environmental regulatory agencies. We recognize that implementation of these standards is tied to certain commercial demonstration goals.

As proposed, the performance standards, as of Jan. 1, 2009, would require new coal-fired power plants in the future -- at a time when carbon capture and sequestration become feasible -- to operate at a CO_2 emissions limit feasible for only natural gas (combined cycle) plants, thus requiring significant use of capture and geologic sequestration for the majority of CO_2 emissions. As the discussion draft is currently written, these standards arguably could apply retroactively to some plants permitted prior to January 1, 2009, where any group has sought administrative review for <u>any</u> reason, and such review has not been resolved by January 1, 2009.

APPA opposes these provisions because several of our members have these facilities coming online over the next few years in various stages of permitting and building. We also believe, as mentioned below, that there should be a "bright line" between CO2 regulation and the existing Clean Air Act, as the Discussion Draft acknowledges for other parts of the Clean Air Act (CAA). In addition, this language would effectively create a moratorium on coal in a post-2015 world, and raise some significant challenges for facilities yet to be permitted between 2009 and 2015. As of 2009, there is no regulatory permitting system for Class VI (Safe Drinking Water Act) underground storage at power plants. Nor are there regulatory systems in most states to review subsurface geologic permit applications. Most importantly, there is no commercially deployable coal generation technology in the United States which can achieve the 1100 lb/MWH. (See chart below.)

APPA commends the R&D projects enabled under the CCS provisions in the bill as mentioned above, but regards the technology as still in a demonstration stage. It is critical for our nation to explore ways to achieve geologic sequestration of CO_2 under the right circumstances, but it is also important to realize that none of the many necessary component technologies have been linked together to date to operate as a power plant. Until they have functioned as a cohesive set of technologies at a power plant, we are really speculating on the performance, cost, and reliability of the component technologies. At this time there are still many unknown issues which need to be resolved before presuming that an 1100 lb/MWh (or the retrofitted target level of 800 lb/MWh) can be met.

APPA believes that the goal of encouraging new carbon capture and geologic sequestration (or perhaps carbon transformation or beneficial use adaptation) is laudable. However, the NSPS provision in the Discussion Draft would have the perverse consequence of halting state of the art coal plants that have received permitting approval, and are intended to both replace older, dirtier facilities and adapt carbon capture and sequestration technologies in the future. Such new generation coal plants are necessary to continue to promote the transition to cleaner, more efficient, and state of the art power production infrastructure for the nation.

An additional problem with the NSPS is that it would make it impossible to demonstrate coal CCS plants. CCS technology is not yet proven, and no guarantees are available for carbon removal performance or geologic sequestration. Requiring all coal CCS plants to remove carbon to levels of 1100 or 800 lbs/MWh means that there will be no CCS demonstration plants. There is too much risk in constructing a demonstration technology when it is unknown if the technology will meet the mandatory emission limit. The bill should provide separate permitting provisions with sufficient flexibility to allow construction of CCS demonstration plants.

It is also important to note that, once contracted, a power plant owner/operator cannot simply cancel the project with vendors because Congress passes a law with a new plant NSPS or retrofit technology performance standard equal to a natural gas emission limit. These communities would not only have to pay for such facilities, but would also have to buy or build additional generation

to meet their load (customer demand) requirements. This concern is particularly acute for public power utilities since they, unlike some other utilities, have a legal obligation to serve all of their customers.

Waxman-Markey Discussion Draft's NSPS Is Impossible For Current Coal Generation Technology to Meet

Steam Cycle	Thermal Efficiency (%)	Heat Rate (Btu/kWh)	CO2 Production (lbs/MWh Gross)
Sub-critical	36-38	9,000-9,500	1,850-2,050
Super-critical	40-42	8,500-8,200	1,670-1,750
Ultra-critical	43-46	8,000-7,450	1,525-1,625
Advanced Ultra-Critical	46-48	7,450-7,100	1,450-1,525

Achievable

Waxman Markey NSPS Limit 1100 → 800 lb/MWh ← Not Achievable

Additional Comments on Section 116:

The draft does not specify whether the pounds of CO2 per MWH requirement is in **gross or net** MWH limit. The current NOx NSPS for post-1997 Subpart D units (which refers to the Clean Air Act's treatment of certain types of utility boilers) is in pounds per MWH, with gross as the measure for MWH. APPA believes that this provision should be consistent with the manner in which Subpart D units are covered in the Clean Air Act.

The Discussion Draft appears to exempt GHGs from NAAQS, HAPs, PSD, and Title V of the Clean Air Act, which APPA supports. APPA would like the additional clarification that GHGs, especially CO_2, would be exempt from the Section 112(d) of the Clean Air Act.

Clean Energy -- Low Carbon Fuel Standard. While APPA has no position on a Low Carbon Fuel Standard, it is worth noting that this section of the draft makes reference to the term "Electricity" and notes that the Administrator of EPA may, at his discretion, issue regulations providing for—''(A) the generation of credits for electricity used as a transportation fuel and that these credits will be given to the manufacturers or importers of such vehicles." While APPA supports the development of plug-in hybrid electric vehicles (PHEVs), the policy trade-off involved in shifting emissions from the transportation to the electricity sector will put additional burden on utilities to reduce emissions, despite significant net societal (cross sector) greenhouse gas emission reduction benefits. Utilities, as the provider of the electricity fuel through retail electricity service, should be credited for providing this significant net greenhouse gas emissions reduction and should not be penalized or subjected to limitations in supporting this new transportation-related electricity load. Allowing utilities to receive partial or full value through, for example, carbon credits, for the net emission reductions associated with electricity as a transportation fuel, would provide certainty and incentives for utilities to further support the transportation sector in helping to address climate change, achieve energy security, and build stronger local and domestic economies.

Plug-In Hybrid Electric Vehicle and Electric Vehicle Infrastructure. APPA is a strong supporter of PHEVs, but we believe this section is not necessary for public power utilities as we

have already taken steps to advance the requirements of this section. In addition, the Energy Independence and Security Act of 2007 (EISA 2007) authorized funding for plug-in hybrid demonstration programs, consumer incentives, fleet purchasing requirements and manufacturing incentives for the both the vehicles themselves and supporting battery technologies. Based upon this success and support, multiple major automakers have announced plans to commercialize battery electric and plug-in hybrid vehicles as early as 2010.

Large – Scale Vehicle Electrification Program. As a member of the Electric Drive Transportation Association, APPA supports this section.

Plug-In Electric Drive Vehicle Manufacturing. Under this provision, DOE is required to provide financial assistance to domestic auto manufacturers to "facilitate the manufacture of plug-in electric drive vehicles as defined in section 131(a)(5) of the Energy Independence and Security Act of 2007." APPA supports this section and believes DOE is the best agency to carry it out.

Transmission Planning. APPA believes that several features of this subtitle are superior to comparable provisions in other transmission-related legislation that APPA has reviewed in recent weeks. First, the federal transmission policy set out in proposed Section 216A(a)(1) is relatively balanced. While deployment of renewable and other low-carbon energy sources is indeed an important policy objective, it is not the only objective that transmission policy needs to meet. APPA supports the inclusion of the other noted objectives, such as ensuring reliability, reducing congestion, ensuring cyber-security and providing for cost-effective electricity services. Similarly, proposed Section 216A(a)(2) accounts for both supply-side and demand-side options in regional electric grid planning.

Second, the transmission planning regime set out in proposed Section 216A(b) builds on existing transmission planning efforts and expertise, by allowing entities that wish to conduct planning under the principles developed by the Federal Energy Regulatory Commission (FERC) to come forward and identify themselves, and then proceed to work in coordination to develop a "bottom up" regional transmission plan, with the FERC's assistance. This approach is superior to the approach outlined in other bills APPA has reviewed, where one or a very few entities are selected to produce a "top down," interconnection-wide transmission "overlay." Many APPA members that rely on the transmission systems of other utilities to obtain the electric power they need to serve their own customers report that their "local" transmission needs have gone unaddressed for some years. Spending billions of dollars on an extra high voltage transmission overlay to move low-carbon energy sources across entire regions makes little sense if that power cannot make it the last leg of the transmission journey to local distribution systems where it is to be consumed. Doing this would be like building a new freeway without an accompanying network of secondary roads to move the traffic to its ultimate destination. APPA members, both transmission owning and transmission dependent, have expended considerable resources to develop and participate in the new regional transmission planning processes required by the FERC's 2007 Order No. 890. Those processes should be built upon, not bypassed.

Third, the Discussion Draft is also significant for what it does not contain. Unlike other transmission-related legislation now pending, it does not provide the FERC with additional transmission siting authorities. APPA supported the "federal back-stop" transmission siting provisions contained in the Energy Policy Act of 2005 (which added new FPA Section 216). While APPA has been disappointed that these provisions have come under attack both in Congress and in the courts, we remain hopeful that a reasonable balance between the use of state and federal transmission siting authorities can be struck, and that a federal backstop regime can be made to work. Nor does Subtitle F contain any provisions "hardwiring" particular

transmission cost allocation methods to recover the costs of new transmission facilities. Transmission facilities cost allocation and cost recovery is a very difficult subject upon which to legislate, because of the cross-cutting arguments surrounding who benefits from each transmission project (and hence who should pay for it), the number of different customer classes that have to be considered (which can give rise to cross-subsidization concerns), and the possibility of changing transmission system flows over time (which means that potential beneficiaries can change over time). For these reasons, APPA supports leaving such transmission cost allocation decisions to the FERC, as the regulatory agency with substantial expertise in these matters. (Attached is APPA's recently passed resolution on transmission policy that underscores the issues delineated above.)

Smart Grid Advancement. APPA is concerned that this subtitle (in particular, Section 143), rather than dealing with "Smart Grid" issues, duplicates efforts already being undertaken by the electric utility industry to implement energy efficiency, demand response, use of distributed generation and similar measures at the retail level. Congress has, through an extensive series of amendments to the Public Utilities Regulatory Policies Act of 1978 (PURPA), has already required electric utilities (including many public power utilities) to review their own retail rate structures and service offerings and to consider how to facilitate such increased demand response, energy efficiency, and use of distributed generation. Many APPA members are already implementing such measures, to reduce their need for new generation investment and to prepare for potential future climate regulation. It is therefore unnecessary, onerous and duplicative for Congress to instruct electric utilities to now come up with "goals" and accompanying "peak load reduction plans," as envisioned in Section 143.

Title II – Energy Efficiency

Building Energy Efficiency Programs. APPA recognizes the need for public power systems to deploy a wide array of energy efficiency programs at the local level in order to reduce greenhouse gas emissions. APPA supports funding of current federal energy efficiency programs such as the Weatherization Assistance Program and encourages the creation of other fully funded voluntary energy efficiency programs to make homes more energy efficient.

Utilities Energy Efficiency. APPA does not support a federal Energy Efficiency Resource Standard (EERS), but instead believes utilities should be able to use energy efficiency measures to meet any renewable electricity standard. The EERS sets nationwide minimum levels of electricity and natural gas savings to be achieved through utility efficiency programs, building energy codes, appliance standards, and related efficiency measures. The EERS in this bill would require electric utilities to save 15% of energy by 2020.

As an Energy Star Partner, APPA supports and strongly encourages energy efficiency programs. Through APPA's Energy Efficiency Resource Central: Public Power's Initiative for Energy Efficiency, APPA offers a wide variety of education, policy and advocacy resources and services to help utilities promote energy efficiency. Many APPA members are already making great strides in the area of energy efficiency. APPA currently has 31 "Energy Efficiency Partners," which are state and regional public power associations and joint action agencies that are disseminating information on the energy efficiency programs they offer to their member public power utilities. In addition, a new group has formed recently, the Clean and Efficient Energy Program (CEEP), which is a collaborative effort between public power and the Alliance to Save Energy to provide educational materials and training on energy efficiency for public power managers.

We are concerned that our members, who are already aggressively implementing energy efficient measures, would be greatly disadvantaged under this provision. Utilities are rated on their progress based on the average annual electricity delivered to retail customers during the two previous calendar years. Utilities that have already implemented energy efficiency programs would have to find new ways to save additional energy or face steep penalties, while other utilities would be able to take advantage of "low-hanging fruit" efficiency measures to meet the requirements under an EERS.

As mentioned above, instead of creating a separate "one-size-fits-all" federal standard for energy efficiency, APPA supports allowing a significant portion of a renewable electricity standard (RES) to be met using energy efficiency. This will be especially important for our members in regions lacking traditional sources of renewable energy. Providing this kind of flexibility in an RES would help utilities meet the goals of both an RES and an EERS in one standard and help them actually reduce carbon emissions and comply with standards instead of just paying civil penalties when they are unable to meet various benchmarks.

Public Institutions. APPA supports this provision which increases the authorization for the amount available for grants for energy efficiency improvement and energy sustainability for public institutions including municipal utilities.

Title III – Safe Climate Act

APPA supports congressional action on legislation to reduce greenhouse gas (GHG) emissions. However, as mentioned above, any credible program must include cost containment provisions that protect consumers. The program must also maintain the reliability of electricity to consumers by including a transition period that provides time for the development and commercialization of low-carbon generation technologies. The Discussion Draft does not meet these two important goals.

The Discussion Draft relies on three provisions to control costs of its GHG cap-and-trade program: banking and borrowing of allowances; a strategic reserve of allowances; and offsets. These are inadequate to protect electricity consumers from potentially high and volatile prices.

APPA supports the draft's banking and borrowing provisions because they give utilities some flexibility in complying with annual requirements to submit allowances. Since utilities cannot accurately predict how many allowances will be needed in any given year, the flexibility to bank allowances or borrow from the next year without penalty is a very practical tool. However, the provision permitting borrowing with interest from allowance vintages of up to five years in the future will do little to contain allowance costs. Since the emissions cap declines each year, it is likely that allowances for future years will cost more than current-year allowances.

APPA supports the draft's provisions that limit the strategic reserve auction to covered entities and limit the amount any entity can purchase. However, APPA believes that strategic reserve allowances will be of little use to covered entities because the minimum price requirements are so high: 100 percent above a rolling 36-month average market price. This price could only be attractive if the current market prices were exceptionally high compared to their 36-month average. In other words, the strategic reserve would only help when the allowance price more than doubled in a short period of time.

APPA supports the draft's provisions allowing the use of alternative compliance mechanisms – such as domestic and international offsets and international emissions allowances – but believes

that the provisions governing the establishment and use of offsets are inadequate for cost containment purposes. The draft allows EPA up to two years to promulgate regulations governing which type of offset projects can be used. Investment in offset projects will be delayed until EPA has completed its regulations, and consequently, there will be few offset projects available when the 2012 compliance period begins. This is just the opposite of what is needed to control costs in the early compliance years. The use of offsets is crucial for cost containment in the transition period when technological solutions, like carbon capture and storage, are not yet generally available.

In addition, the draft sets detailed requirements for EPA's processes to regulate and enforce the establishment and use of offsets. This will significantly increase EPA's workload, raising the question of whether EPA can realistically meet the time limits established in the bill for approving offset project requests and issuing offset credits. Instead of requiring EPA to specifically approve and verify each project, consideration should be given to building on the work accomplished by existing offset regimes. For example, legislation could establish a list of types of offset projects that would be presumed eligible, subject to meeting verification requirements, and require EPA to accept verification protocols used on major offset trading exchanges, such as the Chicago Climate Exchange.

Given the draft's stringent requirements for the approval and verification of offsets, APPA can see no reason for the discount applied to offsets: five offsets equal four emission allowances. The discount will only impede investment in offset projects by reducing their value.

APPA believes that a credible cap-and-trade program for GHG emissions must include either a safety valve that sets a maximum allowance price or other equally stringent cost control mechanisms that mitigate price volatility and protect consumers. The Discussion Draft does not meet this standard. This is of particular concern because a GHG cap-and-trade program covers more sectors and potentially will have a much broader economic effect than previous emissions trading programs (such as the U.S. program for SO_2 emissions). Thus, high allowance prices and allowance price volatility can affect the entire economy by significantly increasing consumer prices, substantially adding to the cost of doing business, and impeding business investments – including investments in technology and infrastructure that can reduce GHG emissions. A safety valve setting a price ceiling for allowances would provide businesses with some certainty on future costs and keep consumer price increases to a reasonable level.

Electric utilities will have difficulty complying with greenhouse gas emissions caps in the transition years before technological solutions are commercially available. Therefore, caps in the early years of the program should be high enough to give utilities time to implement changes in their power supply portfolios, where prudent, and to get significant benefits from energy efficiency and demand reduction programs. APPA supports the approach taken in the Dingell-Boucher 2008 Discussion Draft, which provides higher caps than the Discussion Draft in the first 10 to 15 years of the program, but still ends up with essentially the same cap by the year 2029.

The Waxman-Markey Discussion Draft does not yet include provisions covering how allowances will be distributed, that is, by allocation or by auction. APPA supports a program that provides electric utilities with allowances sufficient to maintain reliability and to allow time to adapt. Allocating allowances to the utility sector during a transition period will give utilities time to make investments to reduce emissions without unduly burdening end-use customers with exorbitant rate increases. As discussed above, APPA's position does allow for a no more than 5 percent auction at the outset of any cap and trade GHG reduction program, but that is conditioned

on the inclusion of a safety valve or equally stringent cost containment mechanism. Since such a cost containment mechanism is not included in the Discussion Draft, we therefore support allocating all of the allowances with no auction.

In the early years of a cap-and-trade program, the electric utility sector should receive an allowance allocation proportionate to its share of emissions. Allowances should go to load-serving entities because they are in the best position to ensure that allowance revenues are used to reduce costs to electric consumers. In addition, one of the rationales for relying heavily on auctions rather than allocating allowances is to avoid giving industry a "windfall profit" at the expense of consumers. This concern arose from experience with the European cap-and-trade system where many generators included the market cost of allowances in their electricity prices even though they were allocated allowances and did not pay for them. Allocating allowances to load-serving entities, rather than fossil fuel-fired generators, eliminates this concern.

This is particularly important in regions of the country where wholesale electricity markets are run by a Regional Transmission Organization or Independent System Operator (RTO-run markets). Allocating allowances to independent generators selling into RTO-run markets will simply further increase the already artificially high wholesale power prices these markets are producing. That is because fossil fuel-fired generating units set the "clearing price" in most hours of the day in these markets. In the mid-Atlantic region served by PJM, for example, coal-fired units set the clearing price 70 percent of the time. These coal generators will naturally add the value of any carbon allowances to their bids (and most probably an additional premium since these markets do not require generator bids to be cost-based). Then, when these coal units do set the clearing price, all other generators dispatched in that hour (including much lower cost nuclear and other sources) will receive the same price. That price, including the windfall profits accruing to the non-coal generators that were also paid for the coal unit's carbon allowances, will be paid by all electricity consumers in the region.

As a result, two related problems will emerge: 1) the cost to consumers will be far in excess of what is needed for the actual reduction of carbon emissions, and 2) the program will not provide clear price incentives for a shift to cleaner sources of energy. The attached fact sheet provides more information on this issue. The best way to protect consumers and the environment from these adverse results is for the Federal Energy Regulatory Commission to address the serious flaws in the design and operation of the RTO/ISO markets. Trying to address these problems through provisions in a cap and trade program will be unsuccessful.

The annual emissions cap will ensure reductions in emissions regardless of whether allowances are auctioned or allocated. Some parties are concerned that customers will not alter their behavior to reduce consumption unless their cost of energy increases substantially (through the addition of allowance prices). However, utilities and their regulators can agree to substantial investments in energy-efficiency programs to achieve the same goal of reduced electricity consumption.

Given the electric industry's experiences with certain auctions, including those in electricity markets run by a Regional Transmission Organization or Independent System Operator, APPA has serious concerns about auctioning allowances. Any auction (if one is implemented) should proceed cautiously and prevent unintended harm. Thus, APPA strongly supports minimizing the initial auction amount to no more than five percent of total allowances. This will allow time for efficient allowance markets to develop, provide some protection to consumers from the risks of unpredictable cost increases, and ensure continuing reliable operation of the electric system.

An auction disadvantages small, not-for-profit entities like public power systems and favors large, for-profit national and multi-national corporations. Large companies will generally have enough financial clout to purchase the amount of allowances that they want – either for compliance purposes or simply on speculation. Since the amount of available allowances decreases each year, a prudent company that needs allowances will buy more allowances in the early years when the price is expected to be lower. Thus small entities – such as many public power utilities – that need allowances, but do not have access to large financial resources could have difficulty competing for the pool of available allowances. Provisions that limit participation in auctions to covered entities and set purchase limits – for example, limiting purchases to a 110% of an entity's compliance obligation – should be considered. (There would be no restrictions on participation in allowance trading markets.)

The Discussion Draft also does not yet include provisions for the use of revenues generated by allowance auctions. APPA believes that all net proceeds from auctions should be used only for targeted research and development, energy efficiency, and mitigation of cost impacts on consumers.

Any GHG cap-and-trade program must provide for effective market oversight, including strong enforcement and penalties. Oversight is needed to prevent market manipulation so that costs to consumers are minimized, market participants retain confidence in the market, and the market produces the desired environmental benefits in the most efficient and cost-effective manner. APPA supports many of the Discussion Draft's provisions on carbon market oversight. These include setting substantial civil and felony penalties for market manipulation and fraud; requiring position limits and margin requirements for each class of allowances; and ensuring market transparency.

APPA believes that effective market oversight of allowances in futures and other derivatives markets must include measures to identify and address excessive speculation. There is already significant interest in carbon markets, and the potential size of the market, combined with the likely price volatility, should make it attractive to investors. While some argue that promoting commodities as an investment provides market liquidity, the run-up – and subsequent collapse – in natural gas and oil prices in 2008 illustrates the potential for investors with large speculative positions to drive market prices. This 2008 experience resulted in calls for serious reform of the Commodity Futures Trading Commission (CFTC) regulatory authority, but any effective reform would have to include not just the CFTC-regulated exchanges but also unregulated over-the-counter (OTC) markets, which typically are much larger than the exchanges. Regulation of the derivatives markets for emissions allowances must ensure that all trading activities are subject to meaningful oversight.

Finally, APPA notes that for most sectors subject to the cap-and-trade program, the Discussion Draft provides an exemption for small emitters. APPA recommends that the electricity sector be granted the same 25,000 tons or less exemption available to most other sectors covered by the program. In addition, the draft requires entities to report GHG emissions and compliance data to the EPA Administrator as part of a GHG registry. The definition of "reporting entity" includes "a covered entity," and the definition of "covered entity" includes "any electricity source." Thus, a utility that generates power only from non-emitting sources, such as nuclear or hydro generating facilities, would be required to submit reports. In order to eliminate an unnecessary administrative burden, the definitions should be modified so that only electricity sources that produce emissions are required to report.

Title IV – Transitioning to a Clean Energy Economy

APPA supports Section 421 on Clean Energy Curriculum Development Grants that authorizes the Secretary of Education to award grants in order to develop educational programs focused on careers and jobs in renewable energy, energy efficiency and climate change mitigation. Also, we are supportive of Section 422 which will enable the Department of Labor to implement a sustainability and workforce training and education program for green jobs. We look forward to the Committee's proposals for Worker Transition as training for green jobs will provide a dual benefit of creating much needed jobs for our nation's workforce and encourage additional entrants into the labor market for the energy industry.

Consumer Assistance. While this is a "placeholder" in the draft pending a decision on the methodology for allocating allowances, it is important to note that, while APPA supports providing assistance to low-income consumers for additional electricity costs for complying with a cap-and-trade climate change bill, we believe that the appropriate cost-containment measures in such a bill will serve to provide the best cushion against the possibility of volatile electricity prices.

Thank you again for the invitation to testify before the House Energy and Commerce Committee on the Discussion Draft. We look forward to working with the Committee as the process continues.