

May 18, 2009

The Honorable Henry A. Waxman  
Chair  
Energy and Commerce Committee  
U.S. House of Representatives  
Washington, D.C. 20515

The Honorable Edward J. Markey  
Chair  
Energy and Environment Subcommittee  
U.S. House of Representatives  
Washington, D.C. 20515

Dear Chairmen Waxman and Markey:

We are writing to express our strong concerns with the proposal in the American Clean Energy and Security Act of 2009 that would allocate greenhouse gas emission allowances directly to owners of unregulated merchant electric generation units. Because these generators are not owned by a regulated utility, the state commissions would have no way to ensure that consumers would receive the benefits of these free allowances. Moreover, there is no pressure from competition from other countries-- merchant generators are not "trade-exposed" since they don't compete in overseas markets. Finally, any electric sector allowances given to generators would not be available to help soften the impact of pricing carbon on consumers, through their LDCs.

The arguments made by the generators to support their request for allowances cannot be substantiated. These companies say they need allowances to cover their "net compliance costs," but there is no commercial technology available to remove CO<sub>2</sub> emissions from an existing generator. Free allowances won't help to keep generators with high carbon emissions in operation – even if that were desirable. If carbon prices are too high, the company could simply retire its generator and keep the value of the allowance stream for its shareholders – as sort of a "golden parachute."

Regardless of whether the allowances are allocated or auctioned to generation owners in deregulated markets, consumers will see no benefit. Under a free allocation, generators will just add to their electricity price the opportunity cost of holding, rather than selling, the allowance. Coal and natural gas plants will therefore simply add an estimated market price of the allowance to their price charged for electricity.

Because these generators sell into the organized wholesale electricity markets, the structure of these markets will further exacerbate the increase in the cost of achieving carbon reduction goals by raising the price of all electricity sold in these markets – including renewable and nuclear generation which emit no carbon – and severely distort the market price signals for carbon that are integral to the success of any cap and trade program.

In the deregulated Regional Transmission Organization markets covering much of the country, electricity is sold in spot markets priced by a single clearing price auction or under relatively short contractual arrangements greatly influenced by those spot market prices. Fossil fuel-fired electric generating units (natural gas or coal) set the market clearing price for virtually every time period. For example, in the largest RTO, PJM, coal plants are the marginal units 70% of the time. The result is that all of the electricity dispatched in those hours receives the price set by the

coal units, even though the cost of generating electricity from other units, such as nuclear units, is much lower. Nuclear power plants, which operate whenever available, emit no carbon, but very rarely set the clearing price, will be paid this extra cost of the allowance—receiving excess revenues while continuing to operate as always.

At a time when consumers are facing extreme hardships from increasing energy costs and shut-offs of utility service, implementation of a carbon mitigation policy must be done in a manner that achieves needed emission reductions at the least cost to consumers. Allocation of allowances to generators in the deregulated wholesale electricity markets will only raise the cost for consumers without guaranteeing any corresponding reduction in carbon emissions.

Sincerely,

American Public Power Association

Citizen Power

Consumer Federation of America

Electricity Consumers Resource Council (ELCON)

National Association of Regulatory Utility Commissioners

National Association of State Utility Consumer Advocates

National Consumer Law Center, on behalf of our low-income clients

National Rural Electric Cooperative Association

Public Citizen

Virginia Citizens Consumer Council

cc: Members of the House Energy and Commerce Committee