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Seven Northeast States Sign on to Regional Greenhouse Gas Initiative (RGGI)

On December 20, 2005, the governors of Connecticut, Delaware, Maine, New Hampshire, New Jersey, New York and Vermont signed a Memorandum of Understanding (MOU) to address climate change and CO₂ emissions from power plants, known as the Regional Greenhouse Gas Initiative (RGGI). Pursuant to RGGI, the states have agreed to propose rules to establish a program under which CO₂ emissions would be stabilized and then reduced, and the country's first market-based cap and trade program for CO₂ emissions would be established. The MOU contemplates that the seven states will each propose a legislative/regulatory scheme pursuant to a Model Rule (the details of which are yet to be announced), to provide consistency among the seven states.

Which sources and pollutants would be affected within the seven states?

RGGI will regulate CO₂ emissions from fossil fuel-fired electric generating units having a rated capacity equal to or greater than 25 megawatts and combusting more than 50% fossil fuel.

How will the cap and trade program work?

The states have agreed to each propose rules to establish a cap on the total emissions to be allowed from all of the affected power plants (known as the regional base annual CO₂ emissions budget) which would be 121,253,550 short tons of CO₂. The initial base annual CO₂ emissions budget for each state is as follows:

- Connecticut: 10,695,036 short tons
- Delaware: 7,559,787 short tons
- Maine: 5,948,902 short tons
- New Hampshire: 8,620,460 short tons
- New Jersey: 22,892,730 short tons
- New York: 64,310,805 short tons
- Vermont: 1,225,830 short tons



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If ultimately established, the cap would take effect on January 1, 2009. From 2009-2014, each state's base annual CO₂ emissions budget would be the number listed above. Beginning in 2015, each state's base annual CO₂ emissions budget would decrease by 2.5% per year so that by 2018, the base annual emissions budget will be 10% below its initial base annual CO₂ emissions budget.

The second step in implementing the cap and trade program is that each state would issue one allowance for each ton of CO₂ emissions within the budget, and these allowances would be distributed to the power plants and the marketplace. The seven states agreed in the MOU that 25% of the allowances will be allocated for a consumer benefit or strategic energy purpose, which means that at least 25% of the emissions allowances will be auctioned and the revenues used to support energy efficiency, renewable energy, innovative energy technologies or consumer rebates.

Finally, every affected power plant would be required to have enough allowances to cover its emissions at the end of each compliance period. If a source does not have enough emissions, it can reduce its emissions, buy allowances on the market or generate credits through an emissions offset project (discussed in more detail, below). Power plants with more than enough allowances may bank them or sell them to others.

The MOU contemplates compliance periods that last for a minimum of three years, to allow for fluctuations in weather and other conditions to average out over time.

Are there any safety valves for affected power plants?

Yes. If, after the first 14 months of any compliance period, the average regional spot price for CO₂ allowances equals or exceeds \$10.00 (in 2005 dollars, as adjusted for inflation) for at least one year, then the compliance period may be extended by up to three one-year periods.

What are offsets?

If an affected power plant reduces CO₂ emissions on or after December 20, 2005 (the date of the MOU) through an approved offset CO₂ project, it will be awarded offset allowances that it may use to comply with the future cap and trade requirements. The use of offsets is not unlimited; in each compliance period, an affected power plant may cover only up to 3.3% of its reported emissions (approximately 50% of a source's average compliance obligation) with offset allowances. Therefore, a significant portion of the required reductions must occur at the power plants. Since there is no technology to control CO₂, this would mean that power plants will reduce electric output or switch to a lower CO₂-generating fossil fuel.

The MOU lists the following approved offset projects: landfill gas (methane) capture and combustion; sulfur hexafluoride (SF₆) capture and recycling; afforestation (transition of land from non-forested to forested state); end-use efficiency for natural gas, propane and heating oil; methane capture from farming operations; and projects to reduce fugitive methane emissions from natural gas transmission and distribution. The seven states agree that additional offset projects may be added in the future.

An offset project located within one of the seven states would receive one allowance for each CO₂-equivalent ton of certified reduction. An offset project located outside of the seven states would receive one allowance for every two CO₂-equivalent tons of certified reduction.

If after the initial 14 months of any compliance period, the cost of CO₂ allowances exceeds \$7.00 (in 2005 dollars, as adjusted for inflation) for at least one year, offset allowances may be awarded to projects located anywhere in North America, the ratio awarded will be one allowance for each CO₂-equivalent ton of certified reduction, and sources will be permitted to cover up to 5% of their emissions with offset allowances. If the cost of CO₂ allowances exceeds \$10.00 (in 2005 dollars, as adjusted for inflation) for a sustained period, then offset allowances may be awarded to projects located anywhere in North America or from international trading programs, the ratio awarded will be one allowance for each CO₂-equivalent ton of certified reduction, and sources may cover between 5-20% of their emissions with offset allowances, depending upon the length of the compliance period.

What are early reduction credits?

Each state may award early reduction credits for projects undertaken between December 20, 2005 and January 1, 2009 that reduce emissions from the affected power plant by (i) absolutely reducing emissions through emission rate improvements; or (ii) permanently reducing utilization of one or more units at the power plant.

Early reduction credits, allowances and offset allowances may be banked without any limitation.

What happened to Massachusetts and Rhode Island? Can other states join? Can existing states drop out?

Massachusetts and Rhode Island participated in the development of RGGI until they withdrew from the pact in mid-December 2005. Governor Romney of Massachusetts stated that he could not endorse a plan that did not include an overall limit or safety valve on the amount power plants would have to pay if they exceeded CO₂ emissions limits¹. According to the MOU, Massachusetts and Rhode Island may become part of RGGI without any amendment to the MOU at any time prior to January 1, 2008. If Massachusetts or Rhode Island wish to join, the applicable CO₂ emissions budgets that will be added to the overall cap are:

¹ Massachusetts is requesting comment on proposed regulations to implement the CO₂ provisions of state regulations governing power plants. The existing regulations place an annual cap and emissions rate on CO₂ emissions from the six largest and oldest power plants in the Commonwealth. The proposed amendments detail procedures enabling the affected power plants to demonstrate compliance by using emission reductions, avoided emissions and/or sequestered emissions. In addition, the draft regulations contain protections against excessive price increases for businesses and consumers.

With respect to off-site projects, the proposed regulations would create a two-tiered system of triggers and safety valves. The first tier allows power plants to perform offset projects in the northeast region, which keeps technology development and environmental benefits closer to home. If the price of available offsets reaches \$6.50/ton of emissions for 12 months, however, sources would then be able to purchase offsets from anywhere in the world, thereby protecting ratepayers while providing the same environmental benefit. If the price of offsets climbs to a point with unacceptable economic impacts, or \$10.00/ton, the power plants can then satisfy the emissions obligations by paying into a Greenhouse Gas Expendable Trust. The Trust will be used by the Commonwealth to purchase new offsets or invest in the development of technology to reduce greenhouse gas emissions. Comments on the proposed regulations are due by January 31, 2006.

- Massachusetts: 26,660,204 short tons
- Rhode Island: 2,659,239 short tons

Additional states may join RGGI by an amendment to the MOU. Any state participating in RGGI may withdraw upon 30 days written notice.

What's next?

By March 20, 2006, the states intend to release a draft Model Rule for public comment. After a 60-day comment period, the Model Rule will be finalized. The MOU states that each of the seven states will "seek to establish" legislation and/or regulations to implement RGGI as soon as practicable but no later than December 31, 2008. As stated above, the program launch is scheduled for January 1, 2009. A comprehensive review of the program will occur in 2012.

For More Information

For the full text of the MOU and other materials relating to RGGI, please see the RGGI Website: <http://www.rggi.org>.

Our environmental attorneys and in-house technical professionals have the experience necessary to guide you through all environmental matters. If you have any questions or require further information regarding these or any other matters, please contact any member of the Nixon Peabody Environmental team or your regular Nixon Peabody contact.

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