# NYSERDA

Regulatory Impact Statement

21 NYCRR Part 507, $CO_2$ Allowance Auction Program

BACKGROUND

On December 20, 2005, New York State entered into a historic regional agreement to reduce greenhouse gas (GHG) emissions from power plants, an important step to protect our environment and meet the significant challenge of climate change. Under the agreement, the governors of ten Northeast and Mid-Atlantic States have committed to propose the Regional Greenhouse Gas Initiative (RGGI), a program to cap and reduce carbon dioxide ($CO_2$) emissions from power plants in the region by 10 percent by 2019, for adoption in their states.[1] In order to carry out the State's commitment, the Department of Environmental Conservation (the Department) has proposed to establish the $CO_2$ Budget Trading Program by promulgating 6 NYCRR Part 242.

The $CO_2$ Budget Trading Program is designed to allocate $CO_2$ emissions allowances ("Allowances") to an Energy Efficiency and Clean Energy Technology Account ("Account"), which will be established and administered by the New York State Energy Research and Development Authority ("Authority") under this Part 507. The $CO_2$ Allowance Auction Program as set forth at Part 507 is designed to complement the provisions of the $CO_2$ Budget Trading Program and to effectuate the purposes thereof.

As stated in Section 242-5.3 of the proposed $CO_2$ Budget Trading Program rule, the Account will be established to promote and reward investments in energy efficiency, renewable or non-carbon emitting technologies, and/or innovative carbon emissions abatement technologies with significant carbon reduction potential. The Authority will conduct auctions, pursuant to the process provided in Part 507, through which the allowances will be made available for sale. The proceeds of the auction(s) will be used to promote the above-stated purposes of the Account, and for administrative and implementation expenses incurred.

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[1] In addition to New York, the other states participating in RGGI are: Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, Rhode Island, and Vermont.

1. STATUTORY AUTHORITY

The Authority currently administers energy efficiency and clean energy technology programs that are similar to the programs and/or projects that will be funded by the proceeds raised by the auction of allowances from the Account. The stated purposes of the Account are consistent with the Authority's statutory authority, which directs the Authority to conduct, sponsor and assist programs related to new energy technologies and to provide services related to their development. The Authority has the statutory authority to sell the allowances and enter into any contracts and to execute all instruments necessary to develop, research, promote and reward investments related to energy efficiency, renewable or non-carbon-emitting technologies.

The Authority's statutory authority springs from Title 9 of Article 8 of the Public Authorities Law (PAL). In enacting Title 9 of Article 8, the legislature declared, in relevant part, that the purpose of the Authority is, among other things, to promote the development and utilization of "safe, dependable, renewable and economic energy sources and the conservation of energy and energy resources." PAL Section 1850-a. The statute directs the Authority to develop and implement [these] "new energy technologies" and "energy conservation technologies" as such terms are broadly defined by the statute, in a manner consistent with economic, social and environmental objectives. PAL Sections 1851(10), (11); 1854. Taken together, the "new energy technologies" and "energy conservation technologies" that the statute directs the Authority to promote closely match the "energy efficiency, renewable or non-carbon-emitting technologies" that are to be promoted through Part 507. In exercising its statutory powers, the Authority is directed to cooperate and act in conjunction with various entities, including State agencies, in exercising its powers, and is authorized to provide services to State agencies in furtherance of its corporate purposes. PAL Section 1854(2). The Authority is empowered to make rules and regulations governing the exercise of its corporate powers and in fulfillment of its corporate purposes by PAL Section 1855(4).

Pursuant to PAL Section 1855, the Authority is specifically empowered to accept from any State agency the grant of any aid in any form and to comply, subject to the relevant provisions of the Authority's enabling legislation, with the terms and conditions of the grant of the aid. Public Authorities Law Section 1855 also provides that the Authority may receive, acquire, sell, and dispose of any personal property, and may "enter into any contracts and to execute all instruments necessary or convenient for the exercise of its corporate powers and the fulfillment of its corporate purposes." PAL Sections 1855(5), (10). Finally, the statute provides the Authority with the statutory authority "to do all things necessary or convenient to carry out its corporate purposes and exercise the powers given and granted by this title." PAL Section 1855(17).

Given the numerous references and express emphasis in the Authority's enabling statute on the development of energy conservation and renewable energy resources, as central to the Authority's purpose, the Authority's establishment of the Account, auction of the allowances, and use of allowance sale revenues for the purposes stated in the Account definition clearly fall within the authority granted to NYSERDA by Title 9 of Article 8 of the PAL.

2. LEGISLATIVE OBJECTIVES

The legislative history reinforces the plain import of the statutory language. The Governor's Memoranda approving the Authority's creation states that "the primary purpose of this bill is to accelerate the development and use within the State of new energy technologies." L.1975, c. 864. Upon amendment in 1980, the Governor stated that it is the Authority's statutory mandate to "foster, sponsor and assist development and demonstration of new energy generation and conservation technologies." L.1980, c. 558.

3. NEEDS AND BENEFITS

The Department has determined that the burning of fossil fuels to generate electricity is a major contributor to a warming climate, and that a warming climate poses a serious threat to environmental resources and public health of New York State. In response, the Department has proposed to establish the $CO_2$ Budget Trading Program by promulgating 6 NYCRR Part 242. Under that Part 242, proceeds from the sale of allowances to affected generators of $CO_2$ will be used by the Authority to fund programs promoting energy efficiency, renewable or non carbon-emitting technologies, and innovative carbon-emissions abatement technologies with significant carbon reduction potential. The $CO_2$ Allowance Auction Program will thereby effectuate the purposes of the $CO_2$ Budget Trading Program by producing significant environmental co-benefits in the form of improved local air quality, forest preservation, improved agricultural manure handling practices leading to better water and air quality in rural areas of the State, and a more robust, diverse and clean energy supply in the State.

In support of these goals, the auctions will be designed to achieve the following objectives: achieve fully transparent and efficient pricing of allowances; promote a liquid allowance market by making entry and trading as easy and low-cost as possible; be open to participation by the categories of bidders determined to be eligible by the Authority or its designee in consultation with the Auction Advisory Committee; monitor for and guard against the exercise of market power and market manipulation; be held as frequently as is needed to achieve design objectives; avoid interference with existing allowance markets; align well with wholesale energy and capacity markets; and to not act as a barrier to efficient investment in relatively clean existing or new electricity generating sources.

An Auction Advisory Committee ("Committee") comprised of the President and Chief Executive Officer of the Authority, the Commissioner of the Department and the Chairperson of the New York State Public Service Commission, or their respective designees, shall advise the Authority on procedures relevant to conducting the auctions described in Part 507. Beginning in 2008, $CO_2$ Allowance auctions will be held at least annually, but may be held as often as necessary to effectuate the objectives of the $CO_2$ Budget Trading Program, as determined by the Authority in consultation with the Committee.

Prior to each auction, the Authority or its designee, in consultation with the Committee, shall select the category or categories of bidders eligible to participate in each auction. Eligible bidders for an auction may include owners of $CO_2$ budget units located in New York, owners of $CO_2$ budget units located outside of New York but within the RGGI participating States that have final $CO_2$ Budget Trading rules in place at the time of the auction, and other market participants including but not limited to owners of fossil fuel-fired generation units located outside of the RGGI participating State, brokers, environmental groups and financial and investment institutions. All otherwise eligible bidders wishing to participate in an auction will be required to open and maintain a compliance or a general $CO_2$ allowance account pursuant to Part 242.

A detailed description of each auction, including details regarding participation, will be set forth in a Notice of $CO_2$ Allowance Auction ("Notice"), which will be published on a $CO_2$ allowance auction website and in the Department's Environmental Notice Bulletin at least 45 days prior to each auction. The Notice will include but will not be limited to the following information: date and time of auction, type of auction, eligible categories of bidders, number of $CO_2$ Allowances to be auctioned, location and/or electronic address of auction, format of bids, surety or security mechanism to certify eligibility to participate, and the Authority's information contact person. The Notice may also include a "reserve" or minimum price to be accepted for $CO_2$ Allowances.

Auctions will be implemented through a two-step process, consisting of (1) a pre-qualification application step that will pre-qualify bidders, and (2) a competitive bidding step. Only those bidders found pre-qualified through the step one application process will be permitted to submit bid(s) in the auctions. The prequalification application will include a detailed description of the bidder and its corporate background, and will be accompanied by the bidder's surety. The surety required may be a letter of credit, bond, or other surety instrument deemed acceptable to the Authority or its designee that guarantees payment of the stated surety amount in the event the bidder's offer is accepted and the bidder fails to complete the transaction.

The Authority will review each pre-qualification application and make determinations as to qualification for participation in bidding. Failure to provide any information required by the Notice may result in the pre-qualification application being declared incomplete or otherwise deficient. All prospective bidders will be notified in writing of such determinations no later than 15 days prior to the date upon which the auction may be conducted. If a pre-qualification application is determined to be incomplete or otherwise deficient, the Authority shall notify the bidder and state the reasons therefore. Prospective bidders whose pre-qualification applications have been determined to be incomplete or deficient will be given a reasonable opportunity to provide additional information and to cure such deficiencies.

In conducting auctions, the Authority or its designee may employ any one of the following auction formats, or an auction format consisting of any or all of the components thereof:

(a) Sealed Bid, Discriminatory Price. A single or multiple round sealed-bid auction in which the bidders may submit multiple bids at different prices. Allowances are allocated to the highest bidders at their own bid prices.

(b) Sealed Bid, Uniform Price. A single or multiple round sealed-bid auction in which bidders may submit multiple bids at different prices; the price paid by all awarded bidders will be uniform.

(c) Ascending price, multiple round. A multiple round auction starting with an opening price with increases each round by predetermined increments. In each round, bidders offer the quantity they are willing to purchase at the posted price. Rounds continue so long as demand exceeds the quantity offered for sale. At the completion of the final round, the Authority may allocate allowances: (i) at the final price to remaining bidders and withhold unsold allowances for a future auction, (ii) at the penultimate price, first to final round bidders and then in order of bid during the penultimate round for all remaining allowances, or (iii) according to an alternative mechanism designed to effectuate the objectives of this Part.

(d) Descending price, multiple round. A multi-round auction starting with a high provisional price, which falls in each round by predetermined increments. In each round, the bidder can “lock in” some purchases at the current provisional price and/or the bidder can wait for the price to fall. The auction rounds cease when the number of allowances locked in is greater than or equal to the quantity of allowances being offered.

Upon closure of bidding, the Authority or its designee will rank all bids and all $CO_2$ Allowances will be sold at the amounts specified in the accepted bids until there are no remaining $CO_2$ Allowances available for the specified auction. In the event that there is more than one winning bidder submitting the same price and the total number of $CO_2$ allowances requested in all such winning bids exceeds the number of $CO_2$ allowances remaining, the Authority or its designee will award the remaining $CO_2$ allowances based on the pro rata share of the number of $CO_2$ allowances bid on by each winning bidder, in chronological order based on the time that the winning bids were submitted, or such other method as designed by the Authority. At such time as the transactions are complete, the Authority will notify the Department or its designee to transfer the corresponding $CO_2$ allowances from the energy efficiency clean energy technology account to the bidder's compliance or general account. All unsuccessful bidders may submit a written request for return of all financial securities or payments following the conclusion of each auction. After the auction is completed, any $CO_2$ Allowances left unsold shall be made available for sale in a subsequent auction or group of auctions, which will be determined by the Authority in consultation with the Auction Advisory Committee.

As noted above, proceeds of such auctions will be deposited into a designated Authority account and will be used to promote or reward investments in energy efficiency, renewable or non-carbon-emitting technologies, innovative carbon emissions abatement technologies with significant carbon reduction potential, and for the administration of the $CO_2$ Budget Trading Program and the Account.

4. COSTS

The costs to regulated parties and other bidders of participation in the $CO_2$ Allowance Auction Program are expected to be minimal.2 The auction process will provide regulated sources with an opportunity to acquire $CO_2$ allowances for compliance with the $CO_2$ Budget Trading Program. It has been designed to provide a user-friendly, web-based auction platform, and participation will not require qualifications or expertise not

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already available to regulated parties. The requirement that regulated sources, consisting of fossil fuel-fired electric generating units, reduce their greenhouse gas emissions and otherwise comply with the $CO_2$ cap and trade program is imposed by the $CO_2$ Budget Trading Program. A detailed analysis of the costs of the $CO_2$ Budget Trading Program, as promulgated by the Department at Part 242, which this Part 507 is designed to complement, is included in the Regulatory Impact Statement for that program.

The Authority will incur costs associated with the design, administration and implementation of the $CO_2$ Allowance Auction program and associated with administration and implementation of the Account and the programs that will be funded thereby.

With regard to the administration and implementation of the auctions, the Authority will need sufficient staff to: administer the auction process on an ongoing basis, including the preparation of notices to the public and other documents required under the process, to review applications submitted by prospective bidders, to conduct and/or supervise the conduct of each auction, to complete the transactions reached under each auction, and to coordinate the administration of the $CO_2$ Allowance Auction Program with the Department. The Authority estimates that between two and three person years (the full time equivalent of working 100 percent on the project for a full work year expressed as 220 days) will be required to administer and implement the $CO_2$ Allowance Auctions, at a cost of $110,000 per person per year, inclusive of employee benefits, or up to $330,000 annually. The Authority also expects to contract for the services of an auction service provider and an independent auditor, who will assist in the actual conduct of each auction.

The costs incurred by the Authority and the number of staff needed to administer and implement the programs that are to be funded through auction proceeds are difficult to quantify at this time, as those costs will depend in large part on the size and scope of those programs, which in turn will be determined by the amount of funds realized through the auctions.

The Authority currently administers application-based offerings and implements programs, under the System Benefits Charge (SBC) program, that are similar to the energy efficiency and clean energy technology programs that the Authority expects to administer and implement, through the use of auction proceeds, under the $CO_2$ Allowance Auction Program. Under the SBC program, the Authority's administration and evaluation expenditures are capped at 10% of the funds available. Based on the similarity between the current SBC programs and those that the Authority expects to initiate under the CO2 Allowance Auction Program, the Authority expects that administration and evaluation costs under the CO2 Allowance Auction Program will approximate 10% of the funds available to the Authority through auction proceeds. The Authority expects that all costs will be recovered from the auction proceeds.

5. LOCAL GOVERNMENT MANDATES

The Jamestown Board of Public Utilities ("JBPU"), a municipally owned utility, owns and operates the S.A. Carlson Generating Station, and will need to comply with the provisions of the $CO_2$ Budget Trading Program. In addition to the purchase of allowances through the $CO_2$ Allowance Auction Program, various strategies are available for JBPU to comply with the $CO_2$ Budget Trading Program, including increasing the efficiency of the natural gas-fired turbine, co-firing with biofuel, or the purchase of offsets. Should the JBPU decide to participate in the $CO_2$ Allowance Auction Program for compliance purposes, the JBPU will be required to comply with the provisions of Part 507.

No other additional record keeping, reporting, or other requirements will be imposed on local governments under this rulemaking.

6. PAPERWORK

Bidders in the $CO_2$ Allowance Auction Program will be required to submit a pre-qualification application and associated supporting documentation as outlined in Part 507. The process has been designed to minimize the amount of paperwork associated with each application, and allows for the continuing qualification of bidders, absent changes, for subsequent auctions.

7. DUPLICATION

The $CO_2$ Allowance Auction Program is designed to complement the provisions of the $CO_2$ Budget

Trading Program.  It does not duplicate any current regulation or rule.

8. ALTERNATIVES

The $CO_2$ Allowance Auction Program is designed to complement the provisions of the $CO_2$ Budget Trading Program, which provides for the auction of $CO_2$ allowances that are allocated to the Account.  The Authority will design and implement auctions in accordance with the requirements of the $CO_2$ Budget Trading Program.  As is provided by the rule, NYSERDA has identified a range of alternative auction formats that may be employed for individual auctions over the course of the program, including:

(1) Sealed Bid, Discriminatory Price; a single or multiple round sealed-bid auction in which the bidders may submit multiple bids at different prices; allowances are allocated to the highest bidders at their own bid prices.

(2) Sealed Bid, Uniform Price.  A single or multiple round sealed-bid auction in which bidders may submit multiple bids at different prices; the price paid by all awarded bidders will be uniform.

(3) Ascending price, multiple round.  A multiple round auction starting with an opening price with increases each round by predetermined increments.  In each round, bidders offer the quantity they are willing to purchase at the posted price. Rounds continue so long as demand exceeds the quantity offered for sale.  At the completion of the final round, the Authority may allocate allowances: (i) at the final price to remaining bidders and withhold unsold allowances for a future auction, (ii) at the penultimate price, first to final round bidders and then to bidders in the penultimate round in chronological order of bid during the penultimate round for all remaining allowances, or (iii) according to an alternative mechanism designed to effectuate the objectives of this Part.

(4) Descending price, multiple round.  A multi-round auction starting with a high provisional price, which falls in each round by predetermined increments.  In each round, the bidder can lock in some purchases at the current provisional price and/or the bidder can wait for the price to fall.  The auction rounds cease when the number of allowances locked in is greater than or equal to the quantity of allowances being offered.

NYSERDA may also employ an auction format consisting of a combination of the components of the various formats described above. NYSERDA has hired a consultant to provide information useful in selecting the auction format to be employed. The consultants will provide information about the advantages disadvantages of each format. The consultants will also provide guidance about how frequently to hold auctions, whether and how to sell allowances from future compliance periods in advance of their associated compliance period, and whether and how to use a reserve price. NYSERDA and the Auction Advisory Committee will use this information to weigh these alternatives and make decisions about what auction features should be used in each auction.

## 9. FEDERAL STANDARDS

The $CO_2$ Allowance Auction Program is an administrative program, and does not exceed any current federal standard.

## 10. COMPLIANCE SCHEDULE

The $CO_2$ Allowance Auction Program will be administered in such a manner as to ensure that regulated parties have the opportunity to comply with the requirements of the $CO_2$ Budget Trading Program in a timely manner.