

RGGI Reform Principles

Program Revisions to Increase Environmental and Economic Benefits

May 2015

The Regional Greenhouse Gas Initiative (RGGI) is a groundbreaking, first-in-the-nation state partnership that demonstrates the effectiveness of carefully designed and implemented market-based climate policy. RGGI also provides an effective and proven pathway for current and new member states to comply with EPA's greenhouse gas reduction requirements under the Clean Power Plan (CPP). As member states of RGGI initiate the 2016 Program Review, the undersigned stakeholders highlight reforms that will build on the success of RGGI to date, deliver greater environmental and economic benefits, and enable RGGI to meet the requirements of the CPP.

We urge RGGI states to adopt the following three key reforms, which are discussed in greater detail below:

- 1) Extend the RGGI cap to at least 2030 in order to provide additional clarity to the market and match EPA's timeline for achievement of CPP targets;
- 2) Correct the cap reduction trajectory to deliver necessary long term emissions reductions; and
- 3) Revise or remove the Cost Containment Reserve to ensure achievement of emissions reduction targets.

Background

RGGI's successful track record ranges from demonstrating the viability of a market-based policy to address power plant greenhouse gas emissions to raising hundreds of millions of dollars for investments in energy efficiency, clean energy, and other consumer-benefit programs. Carbon pollution has fallen so significantly since RGGI's development that the states reduced the emissions cap by 45% during the 2012 Program Review, and emissions continue to decline.¹ The decision by member states to auction the vast majority of emissions allowances has created a level playing field for regulated entities and has raised revenue for investments in programs that benefit consumers, state economies, and the environment. The majority of auction proceeds to date have been directed to energy efficiency programs that lower consumers' energy bills and regional emissions. Efficiency investments also reduce fossil fuel imports and keep money in the local economy, creating significant benefits. Independent analysis of RGGI's first 2.5 years of operation found that investment in efficiency programs will result in savings that flow into local economies to boost output by \$1.6 billion and create 16,000 job years of employment.² Through 2013, over \$630 million of RGGI proceeds have been invested in energy efficiency, leading to \$2.3 billion in lifetime energy bill savings.³ Careful design of emissions tracking and market oversight have created an administratively streamlined program free of collusion and manipulation of emissions allowance markets.⁴

¹ 2014 emissions totaled 86.4 million tons, 5% below the new cap. See annual emissions reports at: <https://rggi-coats.org/eats/rggi/>.

² *The Economic Impacts of the Regional Greenhouse Gas Initiative on Ten Northeast and Mid-Atlantic States*, Analysis Group, 2011. <http://www.analysisgroup.com/RGGI.aspx>

³ *Investment of RGGI Proceeds Through 2013*, RGGI, Inc., April 2015: <http://rggi.org/docs/ProceedsReport/Investment-RGGI-Proceeds-Through-2013.pdf>

⁴ Market monitor Potomac Economics has found all RGGI auctions and secondary market activity free of manipulation, see: http://rggi.org/market/market_monitor

The RGGI states have put a great deal of work into creating this successful program, and that success is a product of many carefully conceived programmatic details. Though this document outlines three necessary modifications, it is important to acknowledge and preserve the many elements of the RGGI program that have been proven to work. This includes fundamental design elements, like auctioning the vast majority of allowances and reinvesting that revenue in energy efficiency, to more nuanced details that keep the program running smoothly and transparently.

One example of this sound policy design is the voluntary renewables set aside, which ensures the integrity of voluntary purchases of renewable energy credits through the retirement of a corresponding amount of RGGI allowances. This system, which has been independently implemented by all but one of the RGGI states,⁵ provides one possible solution for consideration in the context of recent CPP discussions regarding the best treatment of renewables attribute purchases from a region with a mass-based emissions cap.

Another well-constructed element of the RGGI program is the set of stringent and thoroughly reviewed standards for the use of CO₂ offsets.⁶ If offsets are not allowed to contribute to meeting CPP requirements, RGGI states should preserve the existing offsets standards for use outside of the 111(d) framework. RGGI states could 1) continue to allow the use of offsets in the RGGI program so long as the states demonstrate that this will neither contribute to nor prevent compliance with the CPP, or 2) preserve the offsets standards for use outside of RGGI to help meet long-term state GHG reductions and for future programs covering emissions from other sectors.

Sharing this successful model should also be a priority during the 2016 Program Review. The RGGI states should develop a streamlined pathway to expedite participation for new member states. Given the deadline for states to submit CPP compliance plans, any measures that the RGGI states can take to facilitate swift adoption will be valuable. It is critical that allowance budgets and other provisions for new states entering the program be determined such that strong program design and rigorous environmental outcomes are maintained for the RGGI program as a whole. One way to achieve this goal would be to determine new state allowance budgets just as the RGGI states determined the current RGGI cap: using 2012 emissions levels to determine a 2014 budget, and declining each year from 2014 until the first year of participation for a new state. This will ensure that the program's overall stringency is maintained and that CPP targets are met or exceeded.

Necessary Modifications

RGGI's successes to date are impressive, and states deserve credit for significantly strengthening the program in the 2012 Program Review. RGGI is a model program for additional states to participate in or emulate, and additional reforms will ensure that RGGI helps current states to achieve their own pollution reduction targets, to meet or exceed requirements of the CPP, and to further strengthen a model program for addressing the threat of climate change. Beyond the priority reforms identified below, an additional reduction in the cap level may merit consideration if emissions continue to decline along current trends through 2015 and 2016. Emissions in the RGGI region have decreased in each of the last four years, with 2014 emissions dropping to 86.4 million tons of CO₂.

⁵ *RGGI State Set-Aside Provisions for Voluntary Renewable Energy (VRE)*, 2009.

http://www.epa.gov/greenpower/documents/events/rggi_status_table.pdf

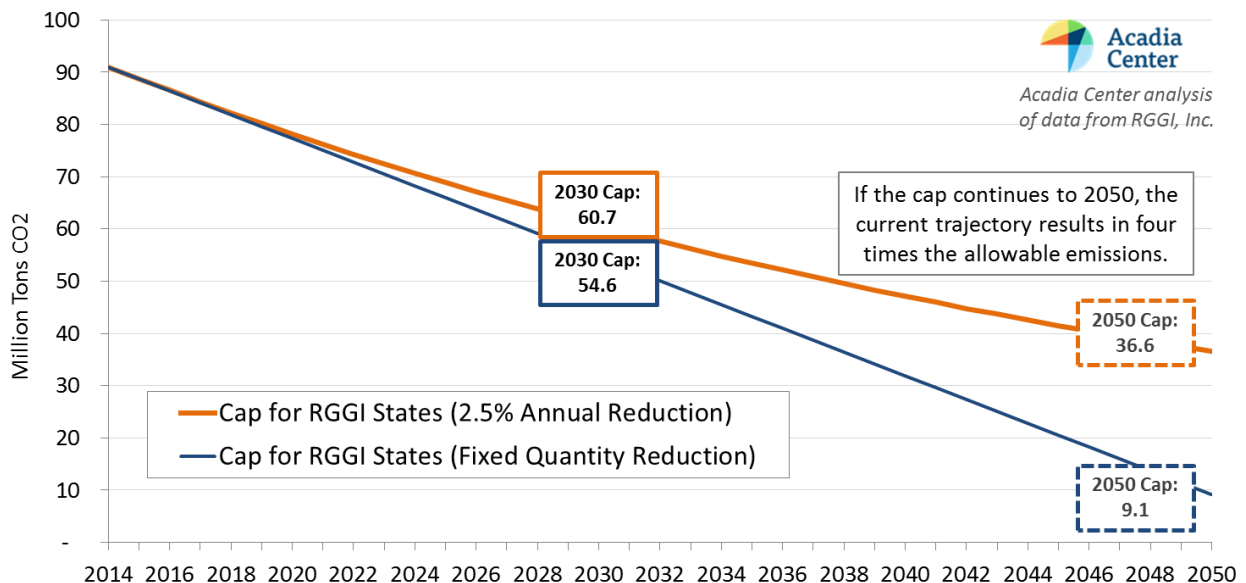
⁶ For more information on CO₂ offsets in the RGGI program, see: <http://www.rggi.org/market/offsets>

RGGI Cap Extension

The RGGI cap currently extends to 2020, and the RGGI states must extend the cap to at least 2030 in order to provide ongoing market certainty to unlock clean energy investments and to be consistent with EPA’s proposed 2030 mass-based targets under the Clean Power Plan.⁷ The RGGI cap was restructured as part of the 2012 Program Review to reflect actual regional CO₂ emissions, with allowances apportioned to each participating state consistent with the proportion of allowances that each state received at the start of the program. We assume that the states will agree to preserve these proportions of the total RGGI budget, but apportionment of the RGGI cap among states could be modified so long as the total cap does not increase.

Trajectory of the Cap Decline

The manner in which RGGI’s cap declines must be revised to ensure achievement of long-term emissions reduction objectives. The cap established in the 2012 Program Review declines by 2.5% annually, but instead of declining by a *fixed quantity of allowances*, the yearly step-down is based on a *percentage of the prior year’s cap*. By 2030 the difference between the fixed quantity and percentage-based reduction is significant. The proper, fixed quantity approach leads to a regional cap of 54.6 million tons while the current, percentage-based approach leads to a regional cap of 60.7 million tons. By 2050 the fixed quantity approach would reduce the cap by 90%, versus 60% when reducing the cap by a percentage-based quantity of allowances each year. Stated differently, unless states correct the cap trajectory, they will be allowing four times as much climate pollution in 2050 as they would under the more universally accepted fixed quantity approach. RGGI’s initial cap required a fixed quantity reduction from the baseline year, so returning to this approach would be consistent with RGGI’s intent, and would support states’ efforts to achieve deep emissions reduction targets by 2050.⁸ For these reasons, the “2030 Projected RGGI Cap” in the figure below is based on the annual fixed quantity reduction approach.



⁷ EPA has yet to release its Final Rule, and therefore these targets are not yet finalized. EPA TSD: *Translation of the Clean Power Plan Emission Rate-Based CO₂ Goals to Mass-Based Equivalents*, November 2014:

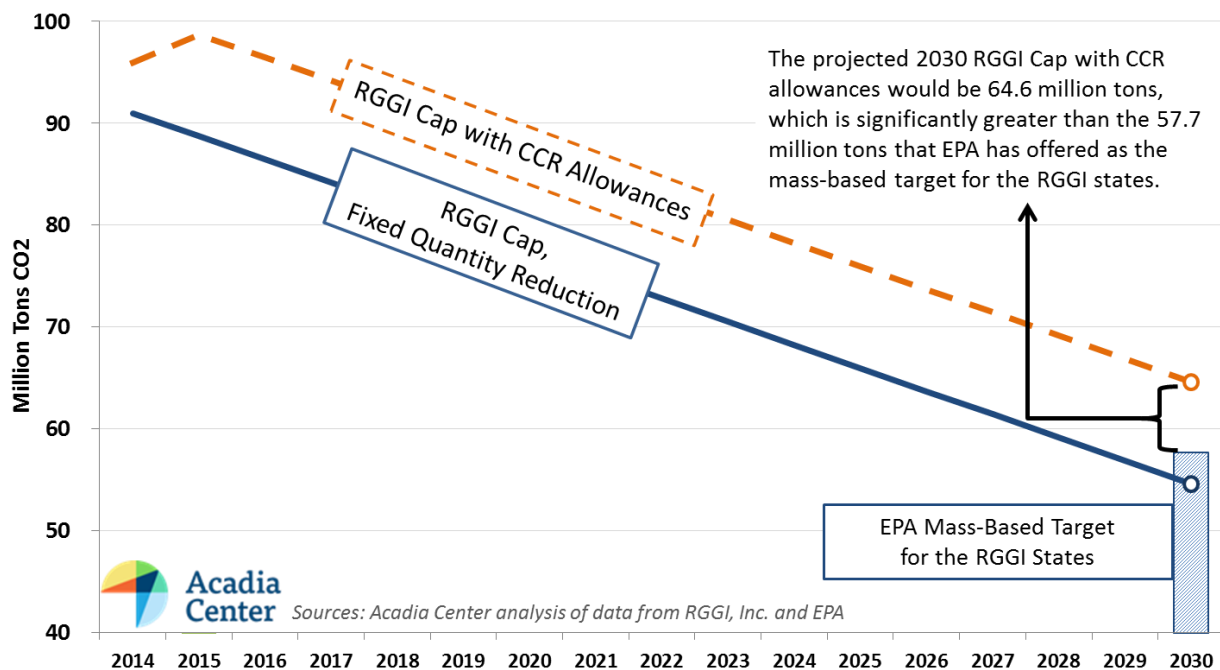
<http://www2.epa.gov/sites/production/files/2014-11/documents/20141106tsd-rate-to-mass.pdf>

⁸ All RGGI states, with the exception of Delaware, have mandated GHG emissions reduction targets. For additional details on state emissions reduction targets see: http://www.c2es.org/what_s_being_done/targets

Cost Containment Reserve

In order to mitigate price volatility, the RGGI states established a Cost Containment Reserve (CCR) that creates additional allowances when price thresholds are reached. That price threshold was reached in the first RGGI allowance auction of 2014, and all five million available CCR allowances were purchased, thus increasing the effective 2014 cap by five million tons of CO₂. In each year from 2015 to 2020, ten million additional CCR allowances will be available if price thresholds are met, thereby increasing the potential cap by ten million tons of CO₂ each year. From 2014-2020, the CCR allowances could permit 65 million tons of CO₂ emissions in addition to the nominal cap—almost a whole year’s worth of emissions.

As the following figure shows, these CCR allowances could increase the cap to the point that the RGGI program would not be stringent enough to achieve EPA’s proposed targets in 2030.



RGGI states should consider removing the CCR entirely, but if it is retained, it should be modified to draw allowances from under the cap. This would ensure that aggregate emissions limits are not exceeded, while preserving a mechanism to mitigate price volatility. This approach is currently being used in California’s emissions trading program where prices have been stable.⁹ Like the RGGI CCR, in California’s program additional allowances become available for purchase when price thresholds are met. Unlike the RGGI CCR, about 4% of CA’s original number of allowances from the capped budget is held back in the allowance price containment reserve. If this reserve of allowances is exhausted, there is limited “borrowing” allowed from the latest program years, and therefore the cumulative supply of allowances – and permissible emissions – is not increased.¹⁰ In addition to

⁹ EDF, *Carbon Market California: A Comprehensive Analysis of the Golden State’s Cap-and-Trade Program*, <http://www.edf.org/sites/default/files/content/carbon-market-california-year-two.pdf>

¹⁰ Explanation of California’s Allowance Price Containment Reserve: <http://www.arb.ca.gov/regact/2010/capandtrade10/capv3appg.pdf>

adopting this approach to cost containment, the RGGI states should consider raising the CCR trigger prices as part of the 2016 Program Review process in order to better ensure emissions reductions and avoid flooding the market with emissions allowances.

As states move forward with the 2016 Program Review we look forward to continuing engagement on these and other steps to build on RGGI's success and to strengthen the program.

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