

**STATE OF CONNECTICUT
DEPARTMENT OF ENVIRONMENTAL PROTECTION**

**COMMENTS OF THE CONNECTICUT INDUSTRIAL
ENERGY CONSUMERS ON THE REGIONAL GREENHOUSE
GAS INITIATIVE PRE-PROPOSAL REGULATIONS**

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COUCH WHITE, LLP
540 BROADWAY
ALBANY, NEW YORK 12207
Telephone: (518) 320-3420
Telecopier: (518) 320-3492
E-Mail: jking@couchwhite.com

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PRELIMINARY STATEMENT

The Connecticut Industrial Energy Consumers (“CIEC”) hereby files its comments on Connecticut’s Pre-Proposal Regional Greenhouse Gas Initiative (“RGGI”) Regulations (“Pre-Proposal Regulations”). CIEC is an *ad hoc* coalition of industrial end-users that collectively employ over 30,000 Connecticut workers at numerous plant locations throughout the State. These industrial end-users consume a substantial part of all electricity consumed in Connecticut.

For the reasons set forth below, CIEC urges the Staff of the Connecticut Department of Environmental Protection (“DEP”) to: (i) amend the Pre-Proposal Regulations to exempt customer-side distributed generation (“DG”) resources up to 65 MW and all other on-site resources that sell less than 20 percent of their net output into the grid; (ii) refrain from issuing the Final Regulations until sufficient modeling and cost impact analyses are conducted on the auction allowance process; (iii) amend the Pre-Proposal Regulations to protect electric consumers by including a price cap at \$0.75 per ton and a sunset provision; and (iv) amend the Pre-Proposal Regulations to allocate all or a significant portion of auction proceeds to customers in the form of a per kilowatt-hour credit.

SUMMARY OF POSITION

In December 2005, the governors of seven Northeast states signed the RGGI Memorandum of Understanding. RGGI is a cooperative effort by the seven states to implement a regional carbon dioxide (“CO₂”) cap-and-trade program. The Memorandum of Understanding recognizes that the signatory states will need legislative and/or regulatory

approval for the RGGI program. The Memorandum of Understanding provides that the signatory states will collectively develop a Model Rule “to serve as the framework for the creation of necessary statutory and/or regulatory authority to establish the Program.”¹

Accordingly, on March 23, 2006, the states that are participating in the RGGI effort, including Connecticut, issued a “Draft Model Rule.” On May 22, 2006, CIEC and 105 other parties submitted comments regarding various issues raised by the Draft Model Rule. The RGGI states through a “RGGI Staff Working Group” evaluated the various parties’ comments. In August, 2006, the RGGI Staff Working Group released its “Final Model Rule,” with a corrected Final Model Rule released in January, 2007. Thereafter, the RGGI states initiated individual regulatory or legislative proceedings necessary to adopt the Final Model Rule in a manner that complies with their specific regulatory requirements. On April 25, 2007, the Connecticut DEP issued its Pre-Proposal Regulations for the implementation and enforcement of the RGGI program in Connecticut.

As set forth in more detail below, the State of Connecticut, its Legislature and/or its regulators must implement the RGGI program in accordance with Connecticut’s policies, laws and regulations. Consistent with Connecticut state law and policy, which encourages investments in DG resources, all customer-side DG resources up to 65 MW, as that term is defined by Section 16-1(a)(40) of the Conn. Gen. Stats.,² should be exempt from

¹ RGGI Memorandum of Understanding, Section 3(A).

² "Customer-side distributed resources" means “(A) the generation of electricity from a unit with a rating of not more than sixty-five megawatts on the premises of a retail end user within the transmission and distribution system including, but not limited to, fuel cells, photovoltaic systems or small wind turbines, or (B) a reduction in the demand for electricity

the RGGI program. Moreover, the Pre-Proposal Regulations should be amended to exclude on-site generators that sell up to 20 percent of their net output into the grid. These amendments will benefit Connecticut's electric customers by providing additional, much-needed capacity while providing end-users with an option to reduce their energy prices. It would be contrary to state policy if these on-site generators are required to meet the economic demands of the Pre-Proposal Regulations.

Moreover, prior to issuing Final Regulations, the DEP must conduct sufficient modeling and cost impact analyses on the RGGI auction allowance process. Pursuant to Section 22a-174-31(f)(3)(C) of the Pre-Proposal Regulations, the DEP Commissioner is directed "to allocate up to one hundred percent" of the required CO₂ allowance allocations to the consumer benefit account "by no later than the end of the second compliance period."³ However, upon information and belief, the DEP has not issued any significant reliability analyses that support an auction process. In light of the potential dramatic adverse impact of the Pre-Proposal Regulations on economic development within Connecticut, it is essential that the DEP conduct such studies and provide sufficient notice and a comment period to allow the public and independent experts to comment on the reliability analyses prior to issuing the Final Regulations.

on the premises of a retail end user in the distribution system through methods of conservation and load management, including, but not limited to, peak reduction systems and demand response systems." Conn. Gen. Stats. § 16-1(a)(40).

³ Pre-Proposal Regulations § 22a-174-31(f)(3).

In addition, the Pre-Proposal Regulations must be amended substantially to more adequately protect Connecticut's electric consumers. The impact of the Final Regulations on Connecticut's consumers may be significant. Therefore, the DEP should modify the Pre-Proposal Regulations to include the following consumer protections: (i) a price cap of \$0.75 percent per ton; and (ii) a sunset provision. A price cap is necessary until there is a commercially-available, cost-effective technology alternative in order to ensure reliability and price certainty without interfering in the allocation of credit proceeds. Moreover, given the likelihood of a national policy aimed at reducing greenhouse gas emissions in the near future, a sunset provision on the Final Regulations is important to allow Connecticut to timely transition to such national greenhouse gas emissions reduction policies.

Finally, the State should mitigate the impact of RGGI on the price of electricity by allocating all or a significant portion of auction proceeds to customers. As discussed below, the price of electricity in Connecticut remains well above the national average. These high electricity prices have contributed to the significant decline in Connecticut's manufacturing sector. Although CIEC members remain supportive of energy efficiency measures for the reduction of demand and RGGI's goal of emission reductions, in Connecticut's flawed energy markets, reduced demand does not necessarily lead to reduced electricity prices. Because end-use customers in Connecticut must bear the costs to implement RGGI, it is essential that such customers' costs will be mitigated to the extent possible without any uncertainty.

POINT I

CONSISTENT WITH STATE POLICY, THE PRE-PROPOSAL REGULATIONS SHOULD EXEMPT CUSTOMER-SIDE DG RESOURCES UP TO 65 MW AND ALL OTHER ON-SITE RESOURCES THAT SELL LESS THAN 20 PERCENT OF THEIR NET OUTPUT INTO THE GRID

The Pre-Proposal Regulations are applicable to any unit that “serves an electricity generator with a nameplate capacity equal to or greater than 25 MWe.”⁴ However, as discussed below, such broad applicability is inconsistent with both Connecticut law and policies that promote the use and development of customer-side DG resources, as well as the Final Model Rule’s exemption of certain customer-side resources. Accordingly, as discussed below, the DEP should modify the applicability of the Pre-Proposal Regulations to exclude all customer-side DG resources up to 65 MW and all other on-site resources that sell less than 20 percent of their net output into the grid.

Connecticut has a strong state policy of encouraging customer-side investment in DG resources. Through Public Act No. 05-01, *An Act Concerning Energy Independent* (the “Act”), the state established a goal “to provide Connecticut with additional means of addressing rising electric prices faced by the state’s citizens and businesses.”⁵ In furtherance of this objective, the Act required that Connecticut develop a program to encourage the use

⁴ Pre-Proposal Regulations at § 22a-174-31 (b)(1).

⁵ Docket 05-07-17, *DPUC Review of the Development of a Program to Provide Monetary Grants for Capital Costs of Customer-Side Distributed Resources*, Decision (March 27, 2006) at 2.

of customer-side DG in order to reduce peak system usage in the state.⁶ Specifically, pursuant to Section 8(a) of the Act, the Connecticut Department of Public Utility Control (“DPUC”) was required to, “no later than January 1, 2006, establish a program to grant awards to retail end use customers of electric distribution companies to fund the capital costs of obtaining projects of customer-side distributed resources....”⁷ Moreover, Section 8(b) of the Act allowed the DPUC to provide awards to electric distribution companies for education, assistance and promotion of investments in customer-side DG resources.⁸

The DPUC has conducted several proceedings to implements the requirements of the Act with respect to the encouragement of customer-side DG resources.⁹ In addition, the electric distribution companies have developed and implemented plans to facilitate the installation of customer-side DG resources.

Moreover, in reliance upon this state policy encouraging the growth of DG resources and its accompanying incentives, many Connecticut customers have devoted considerable time and economic resources, collectively incurring millions of dollars in expenses, to evaluate the practicality of customer-side DG. As of May 4, 2007,

⁶ *Id.* at 10.

⁷ Public Act 05-01, *An Act Concerning Energy Independence* § 8(a) (2005).

⁸ *Id.* § 8(b).

⁹ *See, e.g.*, Docket 05-07-17, *supra*, Decision (March 27, 2006) (developing a program to provide monetary grants for investments in customer-side DG resources); Docket 05-07-16, *DPUC Review of the Development of a Program to Provide Various Incentives for Customer-Side Distributed Generation Resources*, Decision (March 27, 2006); Docket 05-07-21, *Development of Program to Provide Long-Term Financing for Customer-Side Distribution Resources*, Decision (April 7, 2006).

approximately 300 MW of new customer-side DG resources have been proposed, half of which are already in the construction phase. These proposed DG units, which efficiently utilize thermal waste, are especially effective at assisting customers in meeting conservation goals. However, in order to achieve the state's DG goals it is critical that the DG programs remain stable and consistent.

As noted earlier, CIEC members are supportive of RGGI's goal of emission reductions. In fact, CIEC members have found that building/using DG has the potential to reduce the overall carbon footprint of an industrial site. However, in order to remain consistent with Connecticut's policy of encouraging DG resources, the State should exempt all customer-side DG up to 65 MW from the RGGI auctions. Such a modification would conform with the strong public policy and laws favoring such DG resources in Connecticut. Moreover, the exemption of such resources will help promote DG and reduce the strain on the bulk power system by providing increased energy, capacity or ancillary services to the grid. In addition, an exemption would produce significant environmental benefits through the reduction of emissions and the potential displacement of older, less efficient units. Conversely, if an exemption is not granted for DG resources up to 65 MW, the Final Regulations will have the unintended effect of stifling the growth and implementation of DG resources by imposing potentially hundreds of thousands of dollars in additional operating costs.

In addition, generators that sell up to 20 percent of their output to the grid based on the generators' net nameplate capacity should be exempted from the Final

Regulations.¹⁰ The Final Model Rule recognizes the importance of customer-side DG both environmentally and economically by allowing industrial generators that sell less than 10 percent of their output to the grid to exclude themselves from participation in RGGI by applying for a binding permit restriction prior to January 1, 2008.¹¹ Connecticut should take this initiative a step further in order to further promote the benefits of DG. As stated above, an increase in the sale of energy generated by DG resources will provide critical energy, capacity or ancillary services to the grid while potentially displacing less efficient generating units. Thus, the Final Regulations should perpetually exclude on-site generators that sell not more than 20 percent of their output to the grid. In the event an industrial generator wishes to contract to sell more than 20 percent into the grid, the Final Regulations may contain a provision that automatically brings the generator into the program for that amount sold over the 20 percent threshold.¹²

¹⁰ Net output should include an offset for utility provided electricity.

¹¹ Final Model Rule § XX-1.4(b)(1) (January 5, 2007).

¹² Such an exemption would be consistent with other federal and state programs. For example, under the Federal Acid Rain regulations, certain cogeneration units that supply on an annual basis an amount equal to or less than one-third its Potential Electrical Output Capacity or equal to or less than 219,000 MWh are exempt from regulation. 40 C.F.R. 72.6(b)(4)(ii).

POINT II

THE FINAL REGULATIONS SHOULD NOT BE ISSUED UNTIL SUFFICIENT MODELING AND COST IMPACT ANALYSES ARE CONDUCTED ON THE AUCTION ALLOWANCE PROCESS

Pursuant to Section 22a-174-31(f)(3)(C) of the Pre-Proposal Regulations, the DEP Commissioner is directed “to allocate up to one hundred percent” of the required CO₂ allowance allocations to the consumer benefit account (“Consumer Benefit Account”) “by no later than the end of the second compliance period.”¹³ By October 1 of each allocation year, the DEP Commissioner or selected trustee shall then auction the allowances held in the Consumer Benefit Account.¹⁴ This proposed allocation of a specific percentage of CO₂ allowance allocations, however, is not supported by any independent analysis of RGGI’s impact on energy prices paid by Connecticut energy customers. Moreover, upon information and belief, the DEP has not issued any significant reliability analyses that support the Pre-Proposal Regulations. Therefore, in the absence of the requisite studies and proper evaluation of such, the DEP should not issue Proposed Regulations requiring the auction of a specific percentage of CO₂ allowance allocations.

Significantly, the DEP has not referenced or provided any modeling or analyses used to draft the Pre-Proposal Regulations that evaluates the impacts of the 100 percent allowance auction approach by the second compliance period. In fact, at the April

¹³ Pre-Proposal Regulations § 22a-174-31(f)(3).

¹⁴ *Id.*

26, 2007 RGGI Workshop meeting, many of the stakeholders expressed concerns over the reference to an allowance auction without any specifics on the process that will ultimately be used. On May 31, 2007, the RGGI states, including Connecticut, released several auction method alternatives under consideration, one of which would be eventually be incorporated into the RGGI program.¹⁵ However, to date, the DEP itself still has not provided such information nor any modeling reports or analysis of various auction models considered.

Moreover, in the absence of future analyses, any reliance upon the RGGI modeling used in developing the Final Model Rule would be misplaced. Notably, the factual assumptions that underlie this RGGI modeling, as well as the application of these factual assumption to the economic modeling formulas, have not been subjected to any credible, rigorous review by an independent entity.

Given the potential dramatic adverse impact of the Pre-Proposal Regulations on economic development within Connecticut, at a minimum, the economic modeling and conclusions that underlie the Pre-Proposal Regulations should be subjected to rigorous independent review. Specifically, the DEP should perform the following analyses prior to issuing Final Regulations:

1. Generate modeling reports on the various auction models under consideration;
2. Obtain an independent evaluation of such modeling reports; and
3. Develop a detailed auction process.

¹⁵ In October, 2007, the RGGI states are scheduled to run simulations on the various auction methods.

In addition, the supporting documentation must be made available to the public so that it may be examined by independent experts and commented upon by the stakeholders prior to issuance of the Final Regulations.

POINT III

THE PRE-PROPOSAL REGULATIONS MUST BE AMENDED SUBSTANTIALLY TO PROTECT ELECTRIC CONSUMERS

As discussed above, the Pre-Proposal Regulations are not adequately supported by independent analyses. Nevertheless, if, despite this lack of support, the Pre-Proposal Regulations are issued as the Final Regulations, they must first be amended to protect consumers. Accordingly, as discussed below, the following amendments to the Pre-Proposal Regulations should be made: (i) adopt a price cap that will predictably and timely limit auction allocation prices; and (ii) include a sunset provision for termination of the state RGGI program.

A. The Pre-Proposal Regulations Need To Be Modified To Include A Price Cap

The Pre-Proposal Regulations as proposed have the potential to significantly increase prices to Connecticut consumers. Thus, in order to protect consumers, the Pre-Proposal Regulations should incorporate a price cap of \$0.75 per ton until there is a commercially-available, cost-effective technology alternative to capture and sequester

carbon. Such a price cap will help ensure reliability and price certainty without interfering in the allocation of credit proceeds.

In the absence of a price cap, the Pre-Proposal Regulations could impose tremendous costs and uncertainty on the energy industry and its consumers. This risk is associated with the lack of any restriction upon auction prices, which would allow them to increase without limitation, subject only to the dynamics of the market. This risk is further exacerbated by participation of traders in the auction market, who will likely charge a premium for any allocations obtained. Given the current economic conditions that challenge the ability of Connecticut businesses to maintain operations, as well as the identified critical need for additional energy infrastructure, especially in Southwest Connecticut, Connecticut should not implement a RGGI program with the significant energy cost uncertainties and unquantifiable risks inherent in the Pre-Proposal Regulations.

Conversely, including a price cap at \$0.75 per ton in the Final Regulations will protect energy customers while still satisfying the RGGI's objectives. To illustrate this point, the Final RGGI Model Rule specified an allowance structure which allocates 25 percent of revenues to energy efficiency measures and 75 percent to budget source.¹⁶ The Final RGGI Model Rule was based on forecasted CO₂ allowance prices ranging from \$1.00/ton to \$2.20/ton.¹⁷ In its Pre-Proposal Regulations, the DEP proposes to use up to a 100 percent allowance auction structure. Thus, the revenues generated from the proposed

¹⁶ Final Model Rule § XX-5.3(a) (January 5, 2007).

¹⁷ ICF Consulting, *RGGI Electricity Sector Modeling Results, Updated Reference, RGGI Package and Sensitivities* (September 21, 2005) at 12.

\$0.75/ton price cap under a 100 percent allowance auction structure is expected to generate, or even exceed, the auction revenues anticipated from the Final RGGI Model Rule.

A price cap is critical to ensure that the risks associated with the implementation of RGGI are reduced. Connecticut consumers cannot afford the risk of unconstrained price increases that is inherent in the Pre-Proposal Regulations. Accordingly, CIEC requests that the DEP revise the Pre-Proposal Regulations to incorporate a price cap so that the allowance auction price shall not exceed \$0.75 per ton until there is a commercially available and cost effective technology alternative to capture and sequester carbon.

B. The Pre-Proposal Regulations Should Include A Sunset Provision

By July, 2007, the United States House of Representatives is scheduled to vote on federal legislation aimed at reducing greenhouse gas emissions.¹⁸ A national policy could very well be ready for implementation by 2009, the year Connecticut's RGGI rule is designated for its implementation.¹⁹ Connecticut businesses already struggle to compete with facilities in other states. This competitive disadvantage cannot be exacerbated. Thus, it is imperative that the playing field be leveled once a national policy is in place. RGGI must not be allowed to compete with a national policy. Accordingly, the Final Regulations should

¹⁸ See San Francisco Chronicle, *Pelosi creates committee to deal with global warming* (January 19, 2007).

¹⁹ See Pre-Proposal Regulations § 22A-174-31(b)(5)(C) (April 25, 2007).

contain a sunset clause that allows for the timely transition to national greenhouse gas emissions reduction policies.

POINT IV

ALL OR A SIGNIFICANT PORTION OF ALL AUCTION PROCEEDS SHOULD BE PASSED BACK DIRECTLY TO CUSTOMERS

The DEP advocates utilizing all of the auction proceeds to fund a Consumer Benefit Account with the stated purpose of promoting and rewarding investments in energy efficiency, renewable technologies or innovative greenhouse gas emissions abatement technologies.²⁰ Moreover, as stated in the Pre-Proposal Regulations, the Consumer Benefit Account also is to be used for the “direct mitigation of electricity ratepayer impacts attributable to the implementation of the CO₂ Budget Trading Program.”²¹ Given that the electricity prices in Connecticut have increased over 200 percent in recent years for some service classifications, the Pre-Proposal Regulations should allocate all or a significant portion of auction proceeds to customers in order to alleviate the impact of RGGI on electric rates.

The price of electricity in Connecticut remains well above the national average, and is higher than prices paid in other states that compete with Connecticut in

²⁰ *Id.* § 22a-174-31(f)(3)(B).

²¹ *Id.* § 22a-174-31(a)(32).

retaining and attracting business.²² For example, the electricity prices paid by industrial customers in Connecticut for the period ending February 2007 were approximately 112 percent above the national average.²³ In stark contrast, electricity prices paid by comparable customers in Pennsylvania were approximately 7.7 percent above the national average.²⁴ Moreover, as the Department has stated, “[e]ven more disturbing is that the gap between electric rates in Connecticut and those in other regions have increased on a cents per kilowatt hour basis as the cost generation increased from \$.04 in 2002 to over \$.10 in 2006 for CL&P customers.”²⁵

These high energy costs are a significant factor in the decline in Connecticut’s manufacturing sector. Significantly, in the last ten years, the manufacturing sector in Connecticut lost 16 percent of its employment – more than 37,600 jobs.²⁶ Consequently, in order to ensure that the State does not lose more jobs to states or nations where the cost of doing business is lower, it is imperative that the price of electricity decrease, not increase. The additional rate increases RGGI potentially will generate will create new hardship for customers and will impact the decisions of businesses to locate or expand in Connecticut.

²² United States Department of Energy, *Average Retail Price of Electricity to Ultimate Customers by End-Use Sector, by State* (May 24, 2007).

²³ *Id.*

²⁴ *Id.*

²⁵ Docket 06-03-02, *DPUC Investigation Into Electric Retention Tariffs*, Decision (October 25, 2006) at 8.

²⁶ Connecticut Department of Labor, *Labor Market Information*.

Thus, Connecticut should allocate a substantial percentage of the allowance proceeds directly to end-users in the form of a per kilowatt-hour credit. This will reduce the rate impact of RGGI to the maximum extent possible and will help Connecticut to be a more competitive state.

CIEC members remain supportive of energy efficiency and RGGI's goal of emission reductions. In fact, electricity consumers in Connecticut already fund numerous energy efficiency and environmental benefit programs (*e.g.*, the Systems Benefits Charge and the Renewable Portfolio Standard conservation charge, contributing approximately \$71 million to the Connecticut Energy Efficiency Fund in 2006²⁷). In addition, many other energy efficiency and environmental initiatives exist, or are pending, as a result of separate state and federal programs. In fact, the Energy Conservation Management Board ("ECMB") has been recognized nationally for its electric energy efficiency programs.²⁸ And, in 2006, the ECMB programs achieved lifetime energy savings of over 4.6 billion kWh.²⁹

However, despite these demand reductions, in Connecticut's flawed energy markets, reduced demand does not lead to reduced electricity prices. For example, in 1998

²⁷ Energy Conservation Management Board, *Energy Efficiency Investing in Connecticut's Future: Report of the Energy Conservation Management Board Year 2006 Programs and Operations* (March 1, 2007) at 2.

²⁸ *Id.* at 6 ("In 2006, the ECMB and the electric companies continued to develop and implement a variety of award-winning programs that received national recognition for their quality and performance. In 2006, NEEP and its sponsors, including CL&P and UI, were recognized by the EPA with the ENERGY STAR Sustained Excellence 2006 Award for continued leadership in protecting the environment.")

²⁹ *Id.* at 14.

the industrial demand for electricity was 5,837,522 MWh and the average annual price was 7.70 cents/kWh.³⁰ In 2006, the industrial demand was 4,916,862 MWh, yet the average annual price was 11.97 cents/kWh.³¹ Thus, increased spending on energy efficiency programs will not necessarily offset the impact of RGGI by reducing electricity prices.

By diverting all of the proceeds that may be realized from auctioning the RGGI emissions allowances to fund additional spending on energy efficiency and renewables programs, the RGGI program in Connecticut would deprive consumers of an effective offset to the increased costs of RGGI implementation. The bottom line is that because end-use electric consumers in Connecticut must bear the costs to implement RGGI, all or a significant portion of the proceeds that result from the RGGI emissions allowances auctions should be applied directly to mitigate retail electric rates for consumers. It is of tantamount importance to make sure the customers that bear the costs of the State's Final RGGI Regulations will be mitigated to the maximum extent possible without any uncertainties. The only certain way to ensure that customers receive an offset for RGGI's costs is to use all or a significant portion of the auction proceeds to provide a direct per-kWh credit to retail electric distribution rates.

³⁰ United States Department of Energy, Energy Information Administration, *Current and Historical Monthly Retail Sales, Revenues, and Average Retail Price by State and by Sector*.

³¹ *Id.*

CONCLUSION

For the reasons stated herein, the Connecticut Industrial Energy Consumers urge the Connecticut Department of Environmental Protection to: (i) amend the Pre-Proposal Regulations to exempt customer-side distributed generation resources up to 65 MW and all other on-site resources that sell less than 20 percent of their net output into the grid; (ii) refrain from issuing the Final Regulations until sufficient modeling and cost impact analyses are conducted on the auction allowance process; (iii) amend the Pre-Proposal Regulations to protect electric consumers by including a price cap at \$0.75 per ton and a sunset provision; and (iv) amend the Pre-Proposal Regulations to allocate all or a significant portion of auction proceeds to customers in the form of a per kilowatt-hour credit.

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Albany, New York

Respectfully submitted,

James S. King

James S. King
Thais M. Trieby
COUCH WHITE, LLP
Representatives of Connecticut Industrial
Energy Consumers
540 Broadway
P.O. Box 22222
Albany, New York 12207
Telephone: (518) 320-3420
Telecopier: (518) 320-3492
E-Mail: jking@couchwhite.com