

STATE OF IOWA

BEFORE THE IOWA UTILITIES BOARD

IN RE:)	
THE AMERICAN CLEAN ENERGY)	DOCKET NO. NOI-2009-0002
AND SECURITY ACT OF 2009)	
)	

Second Round Comments of the Department of Natural Resources

The Department of Natural Resources (DNR) reiterates its strong support for the American Clean Energy and Security Act of 2009 (“the bill”) and provides the following comments in order to clarify areas of agreement and disagreement with other parties who submitted first round comments.

Q2e.

The DNR’s initial response made the point that it is improper to attribute the cost of wholesale emissions to retail customers as MidAmerican Energy Company (MEC) does in their cost calculations. The DNR asserted that the appropriate method of accounting for allowance value is to assume that the value of wholesale allowances will be recovered from the middleman local distribution companies (LDCs) that directly receive them, by charging higher prices for the wholesale electricity.¹ The Department notes that Interstate Power and Light Company (IPL), in calculating their own allowance allocation in their first round submission, agrees with us in principle:

“IPL sells a relatively small amount of the energy supplied by IPL covered sources or purchased in the wholesale bulk power market to wholesale requirements customers. These customers would compensate IPL, either financially or through transfer of allowances to IPL, for the emissions associated with the energy sold to them.”²

As noted in the DNR’s previous submission, properly attributing wholesale allowance value reduces MEC’s cost from \$276 million to \$150 million (using MEC’s estimate of \$25/allowance). Using EPA’s \$13 allowance price gives a cost of \$78 million.

Q2f.

As the Office of the Consumer Advocate has encouraged the interested parties to acknowledge common ground wherever it can be found in this process, the DNR joins MEC and the Sierra Club in opposing the allocation of free allowances to merchant coal units.

¹ Comments of the Iowa Department of Natural Resources 7 (filed August 27, 2009).

² Comments of Interstate Power and Light Company 14 (filed August 27, 2009).

Regardless of whether one agrees with the current allocation formula, it is clear that giving allowances to merchant coal represents an unfair exception to the basic principles of the formula. In this departure from the general rule, allowances are given to an entity that is not the retail seller, and is not positioned to use the allowance value for the benefit of the customer. By directly receiving allowances for wholesale sales, merchant coal is given an unjustified advantage over other wholesale sellers such as MEC. Merchant coal, because it has been given free allowances, will not need to purchase them and will not need to recover this cost by raising electricity prices. In this way, the merchant coal operator is no longer paying the price of carbon when it burns its coal, while its wholesale market competitors are forced to do so. Entities that produce electricity from low carbon technologies may justifiably make MEC's wholesale coal electricity sales less profitable, however merchant coal should not be put in the position to do so. This flaw in the allocation program should be corrected.

While finding points of agreement is desirable, the DNR must disagree with MEC on several issues raised under Q2f in its response document.

1. MEC's point 3, "Retail Sales", claims that the retail delivery component of the formula "...disadvantages medium-sized utilities that have fewer sales than their larger counterparts that support the bill – many of whom have larger percentages of nuclear and hydro energy in their generation portfolio."³ The final clause of this quote reflects the truth of the situation. The formula does not always favor large utilities and disfavor smaller ones. A large utility that generates its electricity from coal is more poorly positioned in this instance than an equal sized utility that generates solely from nuclear. And a small hydroelectric utility could be positioned more advantageously than a medium sized coal utility. Size is only beneficial if the larger amount of generation comes from low carbon sources. Being large as opposed to medium sized provides no advantage if the additional retail delivery allowances must be dedicated to covering a larger amount of CO₂ emissions.
2. MEC's point 4, "Early Adopters of Renewables"⁴ is in direct contradiction with their argument regarding retail sales. MEC points out that by owning significant wind resources, they will receive fewer emissions-based allowances due to their lowered carbon intensity. They portray this as a "penalty". Under the current 50/50 formula, MEC's wind electricity receives allowances through the retail delivery half of the formula. While wind decreases the emissions allowances, it *increases* the delivery allowances. MEC has benefitted, and continues to benefit, by selling wind electricity, yet it has no emissions from it that it must use its free allowances to cover.

In addition, to avoid having their wind assets reduce their carbon intensity, MEC has the ability to choose the period 1999-2001 as their base period for purposes of allowance allocation.⁵

³ Comments of MidAmerican Energy Company 14 (filed August 27, 2009).

⁴ *Id* at 14-15.

⁵ American Clean Energy and Security Act of 2009, H.R. 2454, 111th Cong. § 783 (2009).

In its points 3 and 4, MEC states that predominately low-carbon utilities gain an unfair advantage by being compensated for low-carbon generation, then objects that MEC is not being sufficiently compensated for their low-carbon generation. The issue is not being penalized, but rather that MEC's percentage of low-carbon generation is not high enough to provide them with that type of surplus.

3. In MEC's point 5, "Load Growth", they state:

"The bill established 2005 as the baseline year against which the emission reduction targets are established. From 2005 through 2008, MidAmerican's retail load grew by an average of 3.2 percent per year. Correspondingly, over this same time period, MidAmerican's carbon dioxide emissions increased by approximately 4 million metric tons. As a result, the bill penalizes those economies that have grown since the baseline year."⁶

It is necessary to pick a baseline year to work from and it is unclear what could be used as an alternative. Virtually every year that could have been chosen as the baseline would be open to this argument, and the cap's reduction targets would need to have been adjusted as well.

More importantly, the fundamental premise of MEC's statement—that economic growth, load growth, and increased emissions are synonymous—is factually incorrect, as California, among others, have demonstrated. Economic growth without emissions growth is not only possible, but is absolutely necessary. It is only Iowa's current dependence on using coal for its electricity that results in increased emissions when economic activity increases.

Q2g.

Various respondents' comments on the "Prohibition Against Excess Distributions" section of the bill reveal strongly divergent opinions. The DNR believes that MEC and IPL have disregarded the intent of this important provision. It is useful to remember that the bill still must pass the Senate, and that this provision will be subject to agency rulemaking. The level of detail that would be necessary to address all of the utilities' points is more appropriately dealt with during the rulemaking process. However, let us be clear that this provision was inserted into the bill for the benefit of coal-heavy utilities in order to alleviate their concerns about coastal utilities receiving windfall profits from excess allowance allocations with Midwestern utilities experiencing significant shortfalls. The provision's specific purpose is to fix a problem that Iowa utilities have repeatedly pointed to as a reason for opposing the bill.

Q9b-c.

While it is understandable that an inquiry of the Iowa Utilities Board (IUB) would primarily focus on the bill's effects on Iowa utilities and their customers, taking too narrow a view of

⁶ Comments of MidAmerican Energy Company 15 (filed August 27, 2009).

this bill can result in misplaced priorities and disastrous results. The DNR notes that many of the first round submissions focus on perceived costs or disadvantages that might result from the bill, without weighing them against the enormous cost of delaying action, doing too little, or simply doing nothing at all.

The Union of Concerned Scientists correctly points out in their filing that:

“[a]ll major scientific institutions and professional societies around the world, including the National Academy of Sciences, the National Aeronautic and Space Administration and the Nobel-Prize-winning U.N. Intergovernmental Panel on Climate Change, have concluded that human activity is driving global warming. **We must immediately begin to reduce global warming emissions in order to avoid catastrophic climate change impact**”⁷ (emphasis added).

The U.S. Global Change Research Program’s 2009 Report, *Global Climate Change Impacts in the United States*, previously submitted by the DNR, the Environmental Law & Policy Center Iowa Office, the Iowa Environmental Council, and the Iowa Policy Project, finds that the average U.S. temperature is predicted to increase 4–6.5° F under its lower emissions scenario and 7–11° F under its higher emissions scenario by the end of the century.⁸ A new Nature Conservancy analysis shows that by 2100, Iowa is facing an average annual temperature increase of a stunning 10°+ F, the third highest of any state.⁹ Effects of this temperature increase in Iowa may include new invasive species, reduced air quality, more intense rain events, and increased heat waves, among others.¹⁰

While keeping electricity bills and other economic impacts low is an important goal, we must not lose sight of the big picture. The top priority must be reducing greenhouse gas emissions substantially and quickly. Economics will always be an important consideration; however we cannot forget that if we fail to act now, we may find ourselves attempting to keep houses cool, and electric bills flat, in a future where the “normal” Iowa summer is ten degrees hotter.

Fortunately, an assessment of effective and cost-effective mitigation strategies for Iowa has already been completed. Last December the Iowa Climate Change Advisory Council released its final report, detailing fifty-six policies that could be implemented in Iowa. Collectively, they could reduce greenhouse gas emissions by up to 105 million metric tons of carbon dioxide equivalent (MMtCO₂e) in 2020. Nineteen of these policies would collectively result in a cost savings of \$1.1 billion by 2020.¹¹ The ICCAC final report can serve as a roadmap for climate change policy in Iowa. Together with the bill, the ICCAC final report will be key pieces of Iowa’s climate change mitigation strategy.

⁷ Comments of the Union of Concerned Scientists 1 (filed August 27, 2009).

⁸ *Global Climate Change Impacts in the United States* 29 (Thomas R. Karl, Jerry M. Melillo, & Thomas C. Peterson eds., Cambridge University Press) (2009).

⁹ http://www.nature.org/initiatives/climatechange/files/climate_wizard_analysis.pdf (last visited 9/8/09).

¹⁰ *Global Climate Change Impacts in the United States* 117-122 (Thomas R. Karl, Jerry M. Melillo, & Thomas C. Peterson eds., Cambridge University Press) (2009).

¹¹ Iowa Climate Change Advisory Council, Final Report, December 23, 2008, available at: <http://www.iaclimatechange.us/capag.cfm>

The DNR notes that few submissions discussed the effects of climate change or the bill on Iowa's agriculture industry. Agriculture provides an excellent example of how Iowa will either suffer or succeed depending on how well we deal with climate change. On a business as usual trajectory, Iowa's climate will become less than optimal for corn and soybeans. Blistering hot summers with extended dry spells, punctuated by infrequent but destructive rain events and flooding, are not ideal conditions for growing crops. On the other hand, a successful mitigation scenario would mean continued successful crop production under only moderately different conditions, with any increased energy costs being offset by offset opportunities. Iowa's agricultural and forestry industries are positioned to benefit from the offsets, carbon sequestration, and clean energy provisions of the bill while being exempted from the emissions cap. The DNR recommends that the Board carefully review Secretary of Agriculture Thomas Vilsack's testimony before the House Agriculture Committee¹² as well as the United States Department of Agriculture's (USDA) preliminary analysis¹³, both of which were submitted during the first round of comments. USDA estimates that, under the bill, farmers will net approximately \$1-2 billion per year from 2012 – 2018, increasing to \$20 billion annually in 2050.¹⁴

Summary

As discussed above, there is much about the bill to consider beyond electricity rates. This bill is enormously important for many reasons, but the main one is that it would represent the first substantial step that the United States has taken toward addressing climate change after ignoring the problem for far too long. Much of the rest of world is looking to see what the U.S. will do before committing to greenhouse gas reductions. The U.S. should become the leader on this issue as it has been the largest contributor to the problem. It would be hard to overstate the benefits of successful greenhouse gas reduction legislation, yet we risk failing to do what is desperately needed due to concerns over the program's costs to utilities.

On an issue of such importance, the DNR believes that honest and transparent discussion is crucial. This bill is not perfect as all parties would agree, and the DNR supports seeking changes to the bill during the Senate process that would benefit the citizens of Iowa. However, the DNR believes that it is absolutely crucial for this bill to pass and for the nation to begin serious greenhouse gas reduction efforts as soon as possible.

¹² *Hearing Before the House Agriculture Committee*, 111th Cong. 2 (2009) (statement of Tom Vilsack, Secretary, U.S. Department of Agriculture).

¹³ Office of the Chief Economist, U.S. Dep't of Agriculture, *A Preliminary Analysis of the Effects of HR 2454 on U.S. Agriculture* 11 (2009).

¹⁴ *Id.*