DEVELOPING NEW YORK'S ECONOMYWIDE CAP-AND-INVEST (NYCI) REGULATIONS: YOUR INPUT IS REQUESTED

New York is undertaking one of the most ambitious efforts in the U.S. to address climate change by reducing greenhouse gas (GHG) emissions from every sector of the economy as required by the 2019 Climate Leadership and Community Protection Act. As part of that effort, the Department of Environmental Conservation (DEC) and the New York State Energy Research and Development Authority (NYSERDA) are designing a New York Cap-and Invest program (NYCI) that will set a declining cap on the amount of GHG emissions in the state. It is anticipated that large-scale GHG emissions sources and distributors of heating and transportation fuels will be required to purchase or obtain allowances for the emissions associated with their activities. With the stated goal of NYCI to incentivize consumers, businesses and other entities to transition to lower-carbon alternatives, applying a price to the amount of GHG emissions is the route to achieve this.

In its initial pre-proposal outreach DEC and NYSERDA hosted webinars in June 2023 and solicited written comments from interested stakeholders on a number of questions related to development of three regulations – the Cap-and-Invest Rule, Mandatory Reporting Rule and Auction Rule - that will form the basis of the NYCI program. On December 20, 2023, DEC and NYSERDA issued a ***New York Cap-and-Invest Pre-Proposal Outline*** and ***New York State Climate Affordability Study*** on which they are currently soliciting feedback as part of a Second Stage of Pre-Proposal Outreach. DEC and NYSERDA hosted webinars on January 23, 25 and 26, 2024 addressing this effort. Video recordings and slide decks associated with these webinars are available on the **NYCI website**.

DEC and NYSERDA have requested feedback on the Second Stage of Pre-Proposal no later than **March 1, 2024** so that they can evaluate the feedback as they develop the regulatory proposal that will be the subject of an upcoming formal rulemaking process. Comments can be submitted via the **NYCI website**. The final NYCI process is expected to take effect in 2025.

Key design elements of the NYCI program are listed on the following pages, along with positions associated with those elements that National Fuel believes are necessary to avoid affordability and related challenges for New York residents and businesses that have resulted from overly aggressive design elements in similar programs in the western part of the country. In addition, NYCI must be designed so that its application is equitable across all sectors and regions of the state, including appropriately obligating the electric sector so regions with a higher utilization of natural gas are not disproportionately impacted, and to allow linkage with existing cap-and-trade programs to enable more cost-effective pathways to compliance.

Applicability & Thresholds: Which sources are covered by the regulations, and at what emissions thresholds.

Some suggested language that National Fuel supports:

- Obligated and Non-Obligated sources should be determined equitably and consistently across sectors. The electricity sector should be deemed an Obligated source to avoid creating an unfair advantage for that sector in comparison to other energy sectors or sources. When obligating the electricity sector coordination must occur with the Regional Greenhouse Gas Initiative (RGGI) to ensure there is no double-counting. Obligating the electricity sector also ensures an accurate determination of emissions intensity for the industrial sector, making it more likely that participants in that sector will be deemed "emissions intensive" and qualify for no-cost allowances to help mitigate the risks of leakage and negative competitive outcomes.
- If upstream out of state emissions associated with energy/products used in New York will be included in NYCI analyses then they should be captured for all energy sources, including electricity, and emission factors should be based on actual, not estimated, data whenever possible. This analysis should include the use of fuels derived from low-GHG intensity basins, certified natural gas and renewable natural gas (RNG). Biofuels like RNG should not be considered Obligated sources, and their emissions should be determined via a full life-cycle analysis with credit for avoided emissions.
- To avoid impeding what promises to be a complex and challenging program, emissions standards and reporting developed by DEC should align with similar standards and reporting being developed by the New York Public Service Commission (PSC) in its CLCPA Implementation proceeding (Case 22-M-0149), and New York's GHG accounting should be modified to be consistent with other jurisdictions. Failure to align New York's emissions accounting and reporting could isolate and disadvantage New York and its residents and businesses in a way that results in higher cost and economic and emissions leakage.

Allowance Allocation: How allowances are made available.

Some suggested language that National Fuel supports:

- Similar to the proposed electric utility consignment mechanism, allowances should also be allocated to natural gas utilities to advance affordability for both natural gas and electric utility customers who will be responsible for NYCI costs necessarily passed through to them in their utility bills. This is particularly important for regions like Western New York where there is higher usage of natural gas by residents and businesses.
- An Obligated source that is an owner and transporter of fuels should only be required to purchase allowances for fuel that they own. For example, natural gas utilities should not have a compliance obligation for gas they transport on behalf of other fuel suppliers (e.g., energy services companies (ESCOs)).
- Allowance allocations for emissions intensive and trade exposed industries (EITEs) are important to lessen the risk of economic and GHG leakage from the state. However, the consignment approach proposed by DEC and NYSERDA differs from the more straightforward and less constraining approach offered in other established North American carbon markets where allowances can be used for compliance purposes and should be carefully evaluated to ensure that it offers the most benefit for EITEs.

Ambition: The economywide emissions cap, and allowance budget.

Some suggested language that National Fuel supports:

- This program needs to be affordable for those paying for it, and clearly described on utility bills and related documentation so the public has a full understanding of the nature and source of these costs. A poorly designed, overly aggressive cap-and-invest program could impose unsustainable cost burdens on residents and businesses and disproportionately burden certain regions of the state, including Western New York. Establishing such a program to generate monies to fund the state's energy transformation would hardly be worth it if an imprudently designed program resulted in leakage - emissions or economic - and disproportionate negative impacts on certain individuals, sectors and/or regions of the state. Consistent with the Climate Action Council's final Scoping Plan, which "recommends gradually phasing in the program with cost containment mechanisms," the program should be implemented in a careful, measured manner with sufficient flexibility.
- DEC and NYSERDA offer two potential methods to set the initial emissions cap for 2025, the historical and projection methods.Due to uncertainties and lack of detail around the projection method, and because it seems likely that the historical method will yield more transparent results, the historical method is preferred. Ideally, DEC and NYSERDA would engage with relevant stakeholders on the technical details associated with this calculation so that a more accurate cap calculation can be achieved.
- Calculation of the emissions cap should err on the high end to facilitate flexibility and, at least initially, reductions in the cap should not be fixed or automatic. Any changes to the cap should follow a thorough review and evaluation of the program's progress and impacts. These reviews should occur at regular intervals of sufficient frequency to ensure that any negative economic impacts are identified promptly. If negative impacts are detected, the program should have built in off-rams that are activated. If no negative impacts are detected, reductions in the cap should be conservatively instituted.
- If reductions in the cap are fixed they should be gradual and should not be tied to the 2030 and 2050 targets until monitoring demonstrates that the program is working appropriately and without negative economic impacts on state residents and businesses. The cap trajectory outlined in the DEC and NYSERDA proposal that calls for a "slower reduction" in 2026 – 2027 and "accelerating reductions" thereafter is far from "slow" and will place unrealistic burdens on residents and businesses when it is unclear whether adequate renewable energy will be available and unlikely that hard-to-electrify manufacturing will be able to pursue alternative decarbonization technologies such as RNG under the current NYCI proposal.
- Facility specific GHG emissions and co-pollutant caps for Obligated entities located "in or near" disadvantaged communities (DACs) are too vague, would inhibit the flexibility of entities to find the most cost-effective means of reducing total emissions over time and should be rejected. Co-pollutants are more appropriately addressed via other regulations, not NYCI. A better way to ensure that NYCI benefits DACs is through the distribution of NYCI revenues.

Program Stability: The automatic and planned program adjustments to moderate costs and sustain program ambition of emissions are higher or lower than anticipated.

Some suggested language that National Fuel supports:

- A low price ceiling should be adopted at the outset to facilitate affordability of the NYCI program. Higher ceilings should not be adopted unless careful monitoring confirms that the program is not having unintended negative economic consequences for residents and businesses. If the program adopts phased-in price escalations, they should be moderate increases over extended periods of time. NYSERDA & DEC's initial modeling shows that even at the lowest price ceiling of $14 (Scenario C) NYCI helps substantially accelerate emissions reductions. The availability of price ceiling units (PCUs) offers additional program flexibility.
- In addition to focusing on affordability impacts for low-income households, NYCI must also be sensitive to middle-income households, particularly in upstate New York where initial modeling shows higher net monthly cost impacts because of increased fuel use for heating and transportation but among the lowest per capita health benefits from NYCI in the state.
- Program stability mechanisms should be employed to moderate costs, avoid economic harm and increase flexibility. For example, cost containment reserves (CCR) should be adopted and designed to respond to higher than anticipated prices. Initially, a low trigger price for the CCR should be adopted to ensure the maximum compliance cost relief at the outset of the program.
- There should be no restrictions on allowance banking, even in the first compliance period (as proposed by DEC and NYSERDA).Banking adjustments that would result in a reduced allowance budget should not be included in NYCI because they would inhibit the flexibility of the program that will be critical in its early stages.
- NYCI should be designed to link with established markets like California and Washington to enable more cost-effective pathways to compliance and to give New Yorkers access to a larger more liquid market. To facilitate compliance with NYCI and encourage greater emissions reductions, an offset program should be designed and implemented in New York. California, Washington and Quebec all utilize offset credits as an important mechanism for cost containment and compliance flexibility for entities participating in their cap-and-trade programs. California's offset program prioritizes DACs and California and Quebec's offset programs are linked such that offset credits purchased in each jurisdiction are interchangeable. These initiatives are consistent with the Governor's articulated goals that cap-and-invest should "prioritize the frontline disadvantaged communities in our state" and should be designed "with the capacity to link with other current and future programs to further catalyze a nationwide movement towards carbon pricing, which can lower the price of the transition overall." Alignment of GHG accounting methodologies will also be necessary to permit linkage across jurisdictions, as noted below.

Compliance, Enforcement & Penalties: Compliance periods and types of enforcement mechanisms.

Some suggested language that National Fuel supports:

- Multi-year compliance periods and related techniques should be adopted at the outset of the program to give Obligated sources maximum flexibility as they begin and continue compliance with the program. A three-year compliance period, or a longer period, should be utilized for the program to ensure the greatest flexibility.
- While it is important to include measures in NYCI to ensure market integrity and prevent market manipulation, these measures should be carefully constructed so that they do not impose unnecessary limitations on or inappropriately inhibit the flexibility and liquidity of legitimate market activities.
- Enforcement should consider the newness of the cap-and-invest program in New York (indeed, only two other similar economywide programs have been adopted in the US) and the inevitable learning curve for participants. Consideration should be given to institution of a safe harbor from penalties for a period of time following program commencement.

Reporting and Verification: The start and frequency of reporting, how reporting should be verified, and how to leverage existing reporting programs.

Some suggested language that National Fuel supports:

- Reporting should be developed that leverages existing emissions reports that are currently being filed in the state and, as noted above, should align with similar standards and reporting being developed by the PSC in its CLCPA Implementation proceeding (Case 22-M-0149).
- NYCI should be designed to include all viable emissions reduction technologies in the compliance market and should utilize the best scientific standards for lifecycle accounting of GHG emissions so that all emissions reduction technologies can compete on a level playing field to deliver the greatest cost-effective emissions abatement. Accordingly, New York's GHG accounting framework should be modified to be consistent with other jurisdictions; a necessity if the Governor wants to link with current and future cap-and-invest/trade programs in these jurisdictions and help address affordability concerns.

Auction Rules: The structure and mechanics of allowance auctions.

Some suggested language that National Fuel supports:

- Auction and market rules should be implemented that are easy to understand and effectuate, and that ensure flexibility. For example, the program should be designed to allow robust trading of allowances and should consider authorizing trading of allowances with other/linked jurisdictions.