

OGE Energy Corp. PO Box 321
Oklahoma City, Oklahoma 73101-0321
405-553-3000
www.oge.com



Statement of Donald R. Rowlett
Director of Regulatory Policy and Compliance
OGE Energy Corp.

Hearing Before the Senate Environment and Public Works Committee
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Re: America's Climate Security Act of 2007 (S. 2191)

My name is Donald R. Rowlett. I am the Director of Regulatory Policy and Compliance for OGE Energy Corp., which is an electric utility and natural gas pipeline company headquartered in Oklahoma City. Our electric utility, which is called OG&E, serves approximately 780,000 customers in Oklahoma and western Arkansas. Our fossil-fuel generation mix is approximately 60% natural gas-fired, 40% coal-fired, and we currently have wind power capacity of 170 megawatts or roughly 3% of our total generation.

My company and I appreciate the opportunity to come before you today to provide our perspective and recommendations regarding what perhaps may be the most important environmental and economic legislation the Congress has ever considered—America's Climate Security Act of 2007 (S. 2191). I characterize S. 2191 in that historic manner because, consistent with its stated purpose in attempting to avoid catastrophic global environmental disaster, the bill's implications may very well result in the most far-reaching re-engineering of modern society ever attempted by Congress. The sheer complexity and enormity of that undertaking underscores the need to take special care to avoid approaches that would wreak serious and broad damage to the nation's economy, a goal which we believe everyone shares.

I. OG&E's experience providing low cost, reliable and environmentally responsible electricity informs our perspective on S 2191:

All utilities are not alike. They vary in many important ways: in terms of size, weather demands, financial resources, generation mix, renewable resources, and of course their state regulatory and political environment in which they operate. OG&E is a medium sized investor owned utility and lacks the resources that many of the much larger utilities that have appeared before this Committee possess. These differences can explain why larger utilities, especially those with nuclear generation, may have a substantially different perspective on S. 2192 than OG&E does. To understand our specific views on S. 2191 more fully, it may be helpful to the Committee to first have a sense of OG&E's individual persona as a utility and our particular experience and perspective in providing low cost, reliable and environmentally responsible electric service to our customer.

As a regulated utility, OG&E bears the responsibility of its "obligation to serve" all electricity customers in its service area and we take this obligation extremely seriously. This obligation to serve carries with it the requirement to provide reliable electric power at the lowest reasonable cost to our customers. But beyond that obligation to serve, OGE strongly believes that it is incumbent on us as a good corporate citizen to produce reliable and low cost power for our customers in an environmentally responsible manner. Our company's response in adopting cleaner sources of power generation is therefore motivated not necessarily by a legal compulsion but by a belief that it is simply the right thing to do. Producing electricity with fewer emissions is a prudent, rational and worthy objective unto itself, independent of global climate change concerns. Our customers want their electricity to be inexpensive and reliable, but also as cleanly generated as we can make it. It makes good business sense to respond to our customers in that regard. It also makes good business sense in our line of work to diversify our generation mix to reduce dependency on any one fuel choice option.

OG&E and Wind Power:

I can report firsthand to you from Oklahoma that the interest in environmentally friendly energy and energy related consumer behavior certainly exists in our state. In the western part of our state wind farms seem to be popping up everywhere. Oklahoma has

gone from virtually no wind power just a few years ago to being ranked 6th nationally in existing installed wind power generation capacity today. And, more is on the way. On October 30, 2007, OGE Energy announced that, in response to market demand, OG&E plans to quadruple its wind power generation capacity. We also announced plans to build new transmission lines running between western and central Oklahoma to allow renewable power being developed in sparsely populated western Oklahoma to reach customers where it can be used. Under this expanded renewable energy initiative, OG&E could increase its wind power capacity from its current 170 megawatts to about 770 megawatts, and move Oklahoma up the ranking of states in terms of wind generation from its current sixth ranking to as high as third. And I might emphasize that all of this is happening without state or federal mandates.

As proud as we are of this wind initiative, we certainly recognize that it is very aggressive for a utility our size. Building this wind generation capacity and the transmission lines needed to make it useful is very expensive and creates difficult operational issues involving dispatch and reliability which increase in scale to the extent even more wind capacity might be added to address obligations created by S. 2191.

OG&E and Efficiency:

In addition to wind power, we are renewing our interest and focus on demand side management (“DSM”) programs aimed at reducing energy use. Through programs like time of use rates, weatherization programs, highly efficient lighting and appliance incentive programs, commercial and industrial load curtailment programs and consumer education we are already reducing our system’s demand for power by approximately 200 megawatts. With additional customer education, better technology such as smart meters, and other programs, we believe that there is another 100 or so megawatts of additional energy savings to be obtained.

OG&E is envied in the industry as a low cost utility and we have some of the lowest electricity rates in the nation. What is important for the Committee to understand though is that as a very low cost electricity provider, it is far more difficult for OG&E to use efficiency to shift demand for power—meaning, for us to lower the volume of electricity our customers use--than it is for high cost utilities.

OG&E and Clean Coal:

OG&E's low electricity rates are primarily attributable to the favorable cost implications of our coal burning generation. Often 70 % of our baseload generation will be from our coal generation, with natural gas largely used for the balance of baseload generation and for peaking demand. We use low sulfur Powder River Basin coal which has kept both our emissions and our electricity rates to our customers low, which in turn has contributed very significantly to Oklahoma's economic viability and competitiveness, as well as our enviable standard of living enjoyed by our citizens.

Obviously, a primary purpose of S. 2191 is to make coal a significantly more expensive fuel to mitigate its traditional use and thereby mitigate its uncontrolled greenhouse gas emissions. We note that S. 2191 also has provisions to spur development of clean coal technologies, including carbon capture and sequestration (CCS) technology, that will allow the nation to continue to use "clean" coal for electric generation. OG&E strongly supports the development of such clean coal initiatives. But our very recent experience in responsibly trying to get state regulatory approval for the *cleanest* of existing state of the art clean coal technologies—an *ultra*-super critical coal plant—provides a very cautionary tale that makes us question the ability to construct any new coal plant in Oklahoma for the foreseeable future even if it is the cleanest available coal technology. I believe the Committee would benefit from an understanding of our recent experience in that regard.

Along with our sister utilities in the state, Public Service Company of Oklahoma and the Oklahoma Municipal Power Authority, we are experiencing the need for more baseload generating capacity in the 2012 timeframe. We partnered with those two utilities to propose building one 950 megawatt *ultra*-super critical coal-fired power plant together rather than each of us individually building, smaller, less efficient plants scattered across the state. An *ultra*-supercritical plant represents the very latest in proven state-of-the-art technology and offers major efficiency and environmental performance advantages over older technology and even compared to modern super critical coal plants. **With the addition of this plant, we projected OG&E's carbon footprint could be as much as 3% lower than today.** This would be accomplished by being able to reduce the use of our less efficient coal plants and through increased use of wind power.

In reaching the decision of what type of plant to build, we quickly discounted wind power because it is not suitable for base load generation. We also discounted nuclear because our need for power is in 2012 which would be impossible to meet with the timeframes associated with nuclear plant construction. In addition the financial costs and regulatory risks associated with building new nuclear plants exceed the resource profile that OG&E can afford. We have no appreciable untapped hydro power to speak of in Oklahoma and it was apparent we could not conserve our way out of the need for base load power. So that left gas and coal as our effective options.

Both those fossil fuel options come with pros and cons. Natural gas is certainly a cleaner burning fuel, but comes with higher prices and enormous price volatility. We have low electric rates in Oklahoma but because the summers are so hot and so long, electric bills can be quite high since our customers tend to use a lot of electricity for air conditioning. By the same token, just 2 winters ago we were in emergency meetings trying to determine how we could supplement the funding of public and private low income assistance programs that were not going to be able to meet the projected heating needs of those customers that winter due to gas prices that had spiked over \$10. During this time I appeared before the Oklahoma Corporation Commission in a hearing it convened to understand the reasons for these high prices and to find out what utility companies were doing to mitigate these costs. Consequently, summer or winter, we very much understand from our customers and our state regulator how much importance they attach to the price of their power.

In recent years, we in Oklahoma, like many other states, have had our share of manufacturing plant closings. Just in the Oklahoma City area alone we have had a large tire plant and an automobile plant close, taking with them in excess of 4,000 jobs. In each case, we were called upon by many, including the Governor of our state, to see if there was anything we could do to lower the energy costs of these plants. We did as much as we could at the time, but were unable to do enough on our own to convince the manufacturers to preserve the local plants and the associated jobs. In every one of our state regulatory proceedings our industrial customers constantly remind the regulators that they compete in a global marketplace and any cost disadvantage may be the difference between staying in Oklahoma or not. So given the high price and high

volatility of generating electricity by natural gas, you can understand why that is a significantly disfavored option from the perspective of its impact on customers.

Coal on the other hand is both abundant domestically and significantly cheaper than natural gas—even with the uncertainties of future environmental regulation factored in—and it still handily beats the price of natural gas by many multiples. Clearly, however, the downside to coal is the environmental cost concern. Consequently, in proposing to build an *ultra*-super critical coal plant, we believed we had combined a very significant emission reduction strategy with \$5.5 billion in demonstrable cost savings for consumers—a tremendous value proposition for both Oklahoma’s environment and economy.

After an extensive and thorough public review and comment process at the Oklahoma Corporation Commission, last August an administrative law judge issued a lengthy and detailed recommendation strongly in favor of approval of our proposed ultra-super critical plant, citing the \$5.5 billion in customer savings compared to deployment of a gas-fired base load alternative. Nonetheless, in September our application was denied in a 2-1 vote by the Oklahoma Corporation Commissioners. The Commission’s majority cited concerns about process, the evidence of the need for the power, and cost recovery. Of special interest to this Committee, environmental concerns per se were not identified as reasons for denial of the application.

II. OGE’s views and recommendations on S. 2191

A. We cannot yet sufficiently determine the economic impact of S. 2191 on our customers or our operations:

In our view, as serious as this legislation is for the entire nation, we would assume that before the Committee would turn to marking up S. 2191 it would be able to articulate in a reasonably confident way the macro-economic impact of the bill and understand how the constituencies in each Senator’s state would be affected by the bill. But we understand that such economic analysis has yet to be done. The many witnesses at prior hearings, both supporting and criticizing the legislation, have made a compelling case that the costs of a cap and trade regime such as that contained in S. 2191 will be

enormous. We would observe that Section 2605 of the bill requires the Congressional Budget Office to estimate the price range at which emission allowances will trade during the two year period of the initial greenhouse gas emission market and the impact of allowance trading on the US economy no later than July 14, 2014, which is two years after the implementation of the bill's allowance regime in 2012. It appears to us that this kind of analysis is needed *now* even more than in 2014. Given the unprecedented stakes for this legislation in terms of environmental and economic impacts, we urge the Committee to demand a credible "macro-economic" assessment at the earliest moment and certainly before enactment.

But we are also in need of more information to perform a detailed assessment of the bill's "micro-economic" impact on our own OG&E operations, our credible range of compliance options, and the consequent impact on our customers. We would draw the Committee's attention to Section 3901 et seq., which provides for distribution of "free" allowances to "incumbent utilities". Section 3903 uses several variables including an upfront reservation of a portion of the "free" pool for "new entrants" and rural cooperatively-owned utilities that reduces the overall number of such allowances available to the balance of the utility sector, which includes us, on a pro-rated basis. We cannot estimate the number of allowances that will be reserved for new entrants and the co-ops, and therefore cannot determine what is left to be prorated among the rest of the power sector. But even then we cannot determine how much of that residuum of the "free" allowances that we might receive on a pro-rated basis since to do so requires that we know the ratio of our CO₂ equivalents emissions during the 3 years prior to the bill's enactment to the annual average of the aggregate quantity of CO₂ equivalents from all of the nation's covered power plants during those same three years. While we can estimate our OG&E CO₂ equivalents over any three years from our recent actual experience, it is necessary to know what the national emissions denominator is in that ratio, and different data bases can give different answers that can materially change the result. Without knowing what are the values that the Committee is using for those variables no utility can determine with even reasonable accuracy the number of allowance that it may actually stand to receive under that section. And therefore we cannot confidently deduce the number of allowances that we will need to secure through the auction process or by

purchase from groups favored with allowances that they receive from other provisions under the bill or through offsets. We would note that, as recommended in Subsection J below, a carbon tax provides far greater certainty as to the carbon price signal and allows for more reliable estimations of costs and compliance options.

We presume that the Committee is working with a set of assumed values for those variables and for the purpose of being able to work along with the Committee on an equal factual footing, regardless of whether there is consensus on the particular values the Committee might be assuming, we would urge that the Committee publish its assumptions in that regard so that estimates and comparisons can all be made by all interested parties on an “apples to apples” basis. In similar vein, we do not know what dollar value the Committee is assuming for allowances in the auction market in any particular year or even in the first year (2012), or the estimated value that allowances will demand when sold by sponsors of offsets. In our view, no Senator on the Committee can expect to understand the actual impact of the bill on their respective state’s constituents without such information. By the same token, no utility can fairly evaluate compliance options and the cost thereof without such information. Certainly, the residential, commercial and industrial electric customers, and the public utility commissions in each state will want to know such information. So, we would recommend that such information be made available immediately and that the Committee allow the affected public a suitable period of time to reflect on that and similar information before a full Committee markup so that any further legislative action is properly informed.

Notwithstanding the limitation on our ability to estimate with the desired degree of accuracy the cost and compliance implications of S. 2191, our best analysis thus far produces a sobering conceptualization of the challenge presented by the bill for both OG&E and our customers. We estimate that OG&E’s CO₂ emissions represent approximately 0.9 percent of the total annual average CO₂ emissions of the electric power industry in the United States. Thus, under Section 3903’s allocation methodology for “incumbent” utilities such as us, OG&E would receive approximately 9.5 million allowances in 2012. These credits are only about thirty-six (36) percent of the allowances needed by OG&E in 2012. OG&E would still need approximately 16.5 million *additional* allowances in 2012. This is a conservative estimate, as it is unclear

how many allowances will be available to investor-owned utilities when all other allocations are made for “new entrants”, “cooperatively owned utilities” and others before investor-owned utilities (IOUs) such as us receive their shares of the “free” allowance pool in 2012.

While it not clear what the market costs will be for the allowances that OG&E will need (*i.e.*, possibly 16.5 million allowances in 2012), OG&E believes that these costs will be significant. For example, if allowances are priced at \$30 when OG&E needs to purchase them in 2012 and we opt to buy them, OG&E will have to spend nearly \$500 million that year. (This illustration’s cost is scalable in accord with one’s assumption of the allowance price.) It is unclear how OG&E will recover these costs since assumptions about retail rates and customers’ ability to pay are all unknowns at this time.

Since the purpose of S. 2191 is to provide incentives for companies to change their operations to reduce greenhouse gas emissions rather than simply buy allowances to cover an unchanged emission rate, OG&E would likely have to do more to comply than simply buy allowances. For example, OG&E could retire all of its coal-fired generating units and switch to 100 percent natural gas generation. If OG&E pursued this option, OG&E would face the following costs:

- \$2 billion in capital cost to construct the gas-fired generation.
Note: **This option is not possible for 2012.**
- An **increase** of over \$1.1 billion in fuel costs per year. ***This is more than double OG&E’s current annual fuel costs.***
- **Even if OG&E eliminated coal from its generation portfolio, OG&E would still need to buy 7.8 million allowances which could cost \$234 million in 2012 (if allowances are priced at \$30 per allowance).**
- OG&E could mitigate part of the increase in fuel costs and the cost of purchasing allowances if it installed significant amounts of additional wind generation. However, OG&E believes that 1000 MW of wind generation would only reduce the increased fuel costs and allowance costs by **forty to fifty percent**. The capital cost associated with 1000 MW of additional wind generation would be approximately \$2 billion.

- It is unclear who would pay for the very significant stranded costs associated with the retired coal-fired generating units.

Employing this full switch from coal to natural gas would increase the average monthly bill for a 1000 kWh OG&E customer by approximately forty percent ---representing an increase of \$40 over the current \$100 per month bill. And as noted above, even after this fuel cost impact, OG&E would still need to spend perhaps hundreds of millions of dollars on allowances in order to comply. The costs of these allowances would also presumably be passed on to OG&E's customers, if permitted by our state regulator, thus making the estimated \$40 per month price increase to customers from full fuel switching very conservative and not all-inclusive.

B. S. 2191 fails to provide coal-based generation with sufficient transition support needed to protect customers from adverse cost and reliability impacts:

We understand the bill's objective of injecting a so-called "price signal" into the utility market to induce changes for cleaner electricity generation. However, OG&E is the type of utility that will be seriously challenged in the early years of S. 2191's regime because we do not sense that it provides adequate transitional support for us to protect our customers from adverse cost and reliability impacts.

The objective of reducing national CO2 emissions by 15% compared to 2005 levels by 2020 will be very aggressive for us primarily due to two factors: first, our high use of coal-based generation and second, the few lower-emission alternatives available to us in what we view as the initial, transitional term of the bill, i.e. 2012 through 2020.¹

Nuclear generation opportunities have much longer lead times than S. 2191's implementation date of 2012 would allow. As suggested in the narrative in Section I above, based on the Oklahoma Corporation Commission's decision not to allow construction of an ultra-super critical coal plant that would have saved Oklahoma rate

¹ While we appreciate that S. 2191 projects a 65% emissions reduction from 1990 levels by 2050, we view whatever may occur beyond the general 2020 timeframe to be sufficiently uncertain and speculative that it is unrealistic to predict with much confidence what our situation will be then, especially if we cannot successfully navigate the early transition years leading up to 2020.

payers \$5.5 billion compared to a gas plant, we have serious doubts about the ability to build any new coal plant in Oklahoma in the near future. Beyond Oklahoma, we observe that other clean coal plants are also encountering significant difficulty in being approved by state regulators, with their difficulties often largely attributable to the opposition of environmentalists and the advocacy by natural gas sellers who see economic opportunity for themselves in the demise of any new coal plant. We also note efforts to push EPA to prevent by regulation the construction of any new coal plants that are not equipped with CCS technology. The needed CCS technology that will allow the cleaner, continued use of coal is a decade or more away, and perhaps will not be commercially available until 2025. Renewable resources such as wind, solar and geothermal are not reliable for base load purposes.

We therefore view the distribution of what are referred to colloquially as “free” allowances under Section 3901 et seq. to be critically important to our ability to transition during the early years of the legislation’s cap and trade regime. If anything, we view the current provisions of Section 3903 as likely not providing enough allowances to mitigate what we believe will be the economic cost of this program and to relieve the compulsion to engage in significant fuel switching to natural gas.

In addition, while there are certainly advocates of auctioning all the allowances who will criticize the number of allowances distributed through Section 3903 as excessive or as a “windfall”, we strongly disagree. We envision no realistic scenario where we do not need to continue to rely substantially on our coal generation fleet during the transition period to meet base load demand, notwithstanding the pressure for increased use of wind and natural gas generation. Any “free” allowances will mitigate the suite of new increased cost factors we will encounter from (i) our continued use of coal and increased use of more wind and natural gas generation and (ii) the expense of buying needed additional allowances through auction or offset projects.

C. S. 2191 unfairly discriminates between co-operatively owned utilities and investor-owned utilities.

Section 3903 differentiates in its distribution of “free” allowances between co-operatively owned utilities and the balance of the electric power sector. Under Section 3903, co-ops get a distribution of allowances to cover *all* of their 2006 CO₂ equivalent emissions, whereas what remains in the “free” pool after the co-ops are fully satisfied gets distributed pro-rata to the rest of the utility sector based on their ratio of emissions to the total national emissions of the utility sector. To us this appears to be a political accommodation that is unjustified and unfair. If there truly is an impending environmental catastrophe the ownership structure of the source of the green house gases does not change the impact on the environment. From a financial perspective, we are not necessarily better situated to absorb the cost of compliance any more than a co-operative is. Moreover, most of the co-operative utilities have a generation mix that tilts heavily toward coal-burning just like ours does. Our need for allowance relief is no different than theirs. S. 2191 should treat all utilities the same with regard to the distribution of Section 3903 allowances.

D. S.2191 overly restricts the use of domestic offsets:

Section 2402 generally restricts the amount of allowances that a utility can use from domestic offsets to 15% of its annual obligation. A utility of OG&E’s size and resource capability likely will not be engaging in international offset activity, ergo what is available from domestic offsets is of far more interest and potential usefulness. While it remains to be seen how expensive and available such offset projects may be, it is not lost on us that Oklahoma is an agricultural state where presumably agricultural offset opportunities as envisioned by the bill may exist for us. We believe that a ton of CO₂ equivalent offset is the same as a ton of CO₂ reduction at our own plants. While we cannot realistically determine so now, potentially offsets could provide a cost-effective tool for us, especially in the transition period before clean coal technology is both commercially available and politically acceptable to state regulators. We would recommend significantly increasing the percentage of offset-based allowances that a

utility could use during the period prior to 2020, or, even better, completely eliminating any limit on the use of verifiable domestic offsets.

E. In the absence of available alternatives in the immediate future, S. 2191 will compel massive fuel switching from coal to natural gas by utilities:

Even without being able to quantify the cost of possibly alternative compliance strategies, it is evident beyond any doubt that S. 2191 will compel coal-burning utilities to engage in massive fuel switching to natural gas. The dramatic mismatch between the allowances that will be distributed to utilities under Section 3901 et seq. compared to their historic emission profiles, and the absence of new alternative technology such as clean coal/CCS to accomplish compliance while still using coal, will drive utilities into the allowance auction market and to the offset allowance market, the cost of neither of which can be reliably estimated initially or controlled over time. In the absence of new coal plants and other good, reliable technological choices for the indefinite future, and given the onset of the cap and trade regime in 2012—just four short years from now---no serious coal-burning utility company's board of directors, knowing that state utility regulators are watching and need to approve every significant resource supply decision, will passively leave their company's or their customers' fate to the unknown and uncontrollable allowance auction market. Instead they will be compelled to adopt a compliance policy that has elements over which they exercise the maximum amount of control. We assume this is exactly the behavior the bill is intended to motivate. And for OG&E and other utilities that meet our profile, by far the most accessible and dependable such policy option is to switch from burning coal to burning natural gas. The Committee must recognize in its legislative deliberations this stark and unavoidable reality; to do otherwise is not to anchor the legislation in reality.

Not surprisingly, the EU's recent experience shows that such fuel switching apparently accounts for the bulk of emission reductions in the EU cap and trade regime. Too many credible and expert witnesses before this Committee have warned about the similar overwhelming and compelling incentive our US coal burning utilities will experience to switch from coal to natural gas. They have warned that utilities, with their laudable obligation to serve their customers, will do all that is necessary to serve their

customers reliably, economically and with environmental responsibility. Even if the utilities themselves did not feel compelled to do so, their state regulatory commissions would certainly insist on it. Moreover, assuming the usual ability to pass-through the cost of fuel used to generate electricity, utilities will have the economic incentive to do what will be universally viewed as the “right thing” for their customers. And no one should expect otherwise. Nor should anyone expect that increasing utilities’ incentive to switch to natural gas will have anything other than a dramatic upward pressure on the price of natural gas, the supply of which is not increasing sufficiently to meet this demand.

While an increased price for natural gas is most certainly good news for many in Oklahoma’s robust natural gas production industry, it imposes predictable and unavoidable adverse consequences on everyone else who either uses electricity or natural gas. Numerous experts have already testified that, with the supply of natural gas effectively not increasing, the massive increase in demand for natural gas represented in coal burning utilities switching away from coal-burning will significantly increase the price of natural gas all across this country. The adverse impact of the increased costs of natural gas to residential, commercial and industrial customers will be enormous. This will result in major economic challenges for residential, commercial and industrial users of natural gas in every state in the Union. For example, hospitals and other health care facilities are large energy consumers. These significant increases will place even greater cost burdens on an already overwhelming health care dilemma. But the bottom line is that utilities will get the natural gas they need to generate cleaner electricity for their customers and in so doing other gas users will either have to pay the higher price or do without natural gas, which raises a host of issues about demand destruction, job loss and other adverse economic consequences that have already been well established in prior testimony before the Committee by a spectrum of witnesses extending from the AFL-CIO to the Industrial Energy Consumers of America.

F. S. 2191 does not address the issue of stranded costs that may be caused by compliance with the bill's cap and trade obligations.

If we are correct that significant fuel switching to natural gas will occur, leaving coal-burning facilities idled, we have a very big question as to who will deal with the stranded costs associated with those idled coal plants. The bill is silent in that regard, but we are confident that state utility commissions and electric customers will be very concerned with those stranded costs. This issue is an enormous concern. It would appear to us that in the event of such stranded costs the bill should accommodate the impact it causes by providing allowances or other compensation to the adversely affected utilities.

G. Load Serving Entities should be permitted to apply Section 3501 allowances against their cap and trade obligation.

OG&E qualifies as a "load serving entity" under Section 4(18). Section 3501 distributes allowances to load serving entities, including utilities like OG&E, for the purpose of defraying the cost impact of the cap and trade regime on low and middle income electricity customers. The provision appears to require the load serving entity (perhaps envisioning entities having no electric generation-related emission obligations) to sell these distributed allowances for cash, and then use that revenue to reduce the rates that their low- and middle-income customers pay. In our view, while the distribution of allowances to load serving entities is justified in recognition of their obligation to serve customers, requiring utilities that both generate electricity and qualify as load serving entities such as OG&E to sell those allowances for cash rather than simply to apply them directly to meet their basic allowance obligation is inefficient. Load serving/generating utilities are going to need every allowance they can acquire to meet those basic obligations and in so applying their share of the load serving entity allowance distribution in that manner they will directly benefit all their customers, including their low and middle income customers.

H. S. 2191 too severely limits allowances for carbon capture and sequestration development:

If one is concerned about the impacts of fuel switching in the transition period before 2020 as we are, you can understand why we prioritize the expeditious development of clean coal technologies including carbon capture and sequestration that will facilitate the continued use of coal or the resumption of the use of coal if there is switching to natural gas. The entire cap and trade regime envisioned by S. 2191 benefits by the most rapid implementation of clean coal technologies and CCS by reducing pressure to switch fuels to natural gas.

However, Section 3601 only allocates 4% of the allowances to CCS development projects. In our view this is well below the value of CCS development to the goal of cutting CO₂ emissions and well below the amount of interest coal burning utilities and their customers have in expeditiously incorporating CCS into their existing and possibly future coal-generation fleets.

It is also counter-productive that the allowances for CCS decline over time after 2017 (see Section 3603) when in our view they should increase since we do not expect CCS to be available until well beyond the 2020-2025 timeframe. Nor is it good policy to limit the allowances for CCS projects to 10 years (see Section 3604) or limit and prorate the pool of CCS allowances (see Section 3605). In addition, Section 3602(2) seems to limit allowances to *geological* sequestration, thus excluding other types of sequestration opportunities which can offer similarly favorable and beneficial results. If CCS is so critical to allowing an emission free use of coal, which will provide low cost electricity and mitigate fuel switching, we view allocating more allowances to incentivize that objective to be a far greater national priority than S. 2191 currently does.

I. The Carbon Market Efficiency Board is less desirable than a “Safety Valve” to protect the economy from extreme adverse economic impact;

We are aware of the vibrant difference of opinion between advocates of the safety valve limit on the price of an allowance and the advocates of the Carbon Market Efficiency Board approach. Between those two options, OG&E supports the notion of the safety valve as a more effective and efficient means of preventing undesirable

economic adversity. The safety valve provides far more predictability and legal certainty to affected parties. The powers of the Carbon Board are inherently restricted—ultimately the Board cannot increase the number of allowances—and any relief it grants in terms of increasing allowances in a year must be effectively “made up” by similar reductions in available allowances in future years. The Board is placed in a very rigid constraint and we simply do not agree that that level of inflexibility is either wise or needed.

J. A Carbon Tax may well be more efficient and effective in the early years of any global climate control regime:

While we cannot sufficiently quantify the compliance options and their costs as we need to do, we are impressed that the cap and trade regime in S. 2191 imposes substantial energy cost, but also significant transactional costs in the early years. The bill appears intended to drive utilities and industrial entities into a frenzy of activity—including but not limited to amassing information, recordkeeping, reporting, negotiating for fuels and technologies, finding available and affordable allowances-- all requiring lawyers and accountants, reminiscent of the overhead impressed on American business in Sarbanes-Oxley. We have observed that most economists who have opined on the matter emphasize that imposition of a carbon tax has far greater transactional efficiencies and operational attributes than any cap and trade regime. A carbon tax needs no bureaucracy to monitor and administer it in the way a cap and trade regime does; plus a carbon tax can be readily adjusted up or down to ease economic adversity or provide enhanced incentive to reduce emissions. In addition, a carbon tax permits more confidence and predictability in making the significant investment decisions that utilities like OG&E are going to be faced with.

For all these reasons, it may be more efficient and effective in sending a price signal to change behavior that will produce environmental/climate benefits to impose a carbon tax than a cap and trade regime with its transactional costs and economic dislocations. We would suggest that the Committee evaluate whether it would be more effective and efficient to amend S.2191 to initially impose a carbon tax and delay implementation of any cap and trade regime to a date when the technologies such as clean coal and CCS are actually politically and commercially available so that coal

remains a vibrant contributor to the solution and not a reason to drive natural gas markets out of control.

Conclusion:

OGE Energy Corp. wants to thank the Committee for allowing us to present our views. We respect the earnest desire of the Committee members to wrestle with the global climate issue in a responsible manner and would hope that the Committee members understand that OGE Energy has a tradition and overriding sense of obligation to do the right thing for our customers.