Testimony of

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On Behalf of the
American Gas Association

U.S. House Committee on Energy and Commerce
Subcommittee on Energy and Environment

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Executive Summary

- Natural gas is America's clean, secure, efficient, and abundant fossil fuel
- Residential natural gas consumers, who use the fuel for essential human needs, have a 30-year record of reducing consumption and greenhouse gas emissions
- History demonstrates that programmatic measures, such as appliance efficiency standards and building codes and standards, will lead to more certain emissions reductions than a cap-and-trade system
- If subjected to cap and trade, natural gas utilities should be allocated adequate allowances
- Congress should assure natural gas utilities of cost pass-through for allowances
- A climate change program should consider the unique benefits of renewable natural gas
- Natural gas, because it has the smallest carbon footprint of any fossil fuel is part of the climate change solution
- AGA endorses carbon footprint labeling for appliances
- AGA suggests requiring carbon labeling for buildings
- DOE should be required to consider carbon emissions in its appliance standards
- EERS seeks to reach a laudable goal, but the mechanism is less than perfect
- Utilities do not control their customers' consumption
- EERS does not take into account economic growth
- EERS does not take into account carbon-driven fuel switching
- The mechanism of EERS is potentially troublesome

Introduction

Thank you for the opportunity to testify before the subcommittee. My name is John W. Somerhalder II, and I am the Chairman, Chief Executive Officer, and President of AGL Resources, Inc., located in Atlanta, Georgia. AGL provides natural gas service through six natural gas utilities to more than 2.2 million households, commercial, industrial, and power generation customers in Georgia, New Jersey, Virginia, Florida, Tennessee, and Maryland.

I am testifying today on behalf of the American Gas Association (AGA), which represents 202 local energy utility companies that deliver natural gas to more than 65 million homes, small businesses, and industries throughout the United States. AGA member companies deliver gas to approximately 170 million Americans in all fifty states.

Natural gas meets one-fourth of the United States' energy needs. I am the 2009 Vice-Chairman of AGA.

Natural Gas is America's Clean, Secure, Efficient, and Abundant Fossil Fuel

Natural gas is America's cleanest and most secure fossil fuel. Natural gas is essentially methane, a naturally-occurring substance that contains only one carbon atom. When burned, natural gas is the most environmentally-friendly fuel because it produces low levels of unwanted byproducts (SO_x, particulate matter, and NO_x) and less carbon dioxide (CO_2) than other fuels. Upon combustion natural gas produces 43% less CO_2 than coal and 28% less than fuel oil. Moreover, almost all of the natural gas that is consumed in America is produced in North America, either in the United States or Canada, with the vast majority of that being produced in the United States. Only a small portion—1 to 2%— is imported from abroad as liquefied natural gas.

Natural gas is also the most efficient of the fossil fuels. Approximately 90% of the energy value of natural gas is delivered to consumers. In contrast less than 30% of the primary energy involved in producing electricity reaches the consumer. Additionally, natural gas is an abundant fuel. Recent prodigious discoveries of shale gas have significantly added to this abundant resource base. Changes in economics and technology will continue to increase our resource base estimates in the future, as they have consistently done in the past.

Natural gas is an essential fuel for America. The natural gas delivered by AGA members to residential customers is consumed almost entirely to meet essential human needs—space heating, water heating, and cooking.

AGA and its members would like to highlight two important facts about natural gas that are little known and often overlooked:

- **America's residential natural gas customers have led the nation in reducing the emission of greenhouse gases over the last 30 years and can continue, with appropriate policies, to reduce those emissions. It takes less natural gas to serve 65 million homes today than it took to serve about half that number in 1970.**

- **Natural gas is not part of the climate change problem; rather, it is part of the climate change solution because it offers an immediate answer with existing technology and has the smallest carbon footprint of all fossil fuels.**

We hope that the subcommittee will be mindful of these two critical pieces of information as it crafts climate change legislation. They are important facts that bear upon formulating the best policies for achieving the nation's carbon-regulation goals.

Residential Gas Consumers Have an Unrivaled Record in Reducing Greenhouse Gases

Residential natural gas customers have consistently reduced their per-household consumption of this fuel—and the carbon emissions resulting from its use—for more than 30 years. On a national basis, residential customers have reduced their average natural gas consumption by approximately 30% over these years. Both research and anecdotal evidence make clear that there are proven drivers for reducing natural gas consumption and the carbon emissions associated with natural gas consumption—increased appliance efficiency and increased building efficiency, supplemented by a variety of education and incentive programs.

AGA believes that pursuing appliance efficiency and building efficiency policies is the preferable, indeed optimal, means to achieve further carbon reduction in this sector. AGA remains of the view that it would be counter-productive to make natural gas residential and commercial customers subject to cap-and-trade regulation. Instead, we believe that this sector can continue its admirable record of reducing carbon emissions by continuing an intensive focus upon energy efficiency and building codes and standards measures, which for three decades have led to dramatically reduced natural gas consumption (and emissions).

The costs, direct or indirect, of a cap-and-trade system will simply add to already high energy costs and will have only a modest impact in achieving the desired end result—reducing carbon emissions. Unlike electricity, where there are a number of options for reducing consumption in the relatively near term, almost all natural gas in the home is consumed by furnaces, water heaters, and stoves—durable appliances with relatively long lives. In addition, electricity generators can alter their generating sources, which is not an option for natural gas. While "dialing down" is certainly an option, it has its limits, and consumers have already dialed down dramatically with the natural gas price increases of this decade.

AGA and its members believe, of course, that both natural gas utilities and their customers should contribute to reducing greenhouse gas emissions in order to meet the nation's goals. Our collective experience with energy efficiency, however, informs our view that natural gas residential and commercial customers should not be included under the cap-and-trade aspects of a climate-change program. Instead, there are other ways, which are almost certain to be more productive, that can, and should, be applied to these sectors. Further, a cap-and-trade program can penalize those who have previously and most aggressively pursued efficiency gains and carbon reductions.

The success of residential and commercial natural gas consumers is illustrated by the fact that they have reduced their per-household consumption so dramatically that there has been virtually no growth in sectoral emissions in nearly four decades despite an increase in natural gas households of over 70%. An allowance program based on 2005 emission levels penalizes those consumers and natural gas utilities that implemented early programmatic actions—from appliance and building standards to consumer education and rebate programs.

In light of the above factors, we maintain that a national programmatic-focused effort, rather than a cap-and-trade effort for these customers, is the best way to ensure equity while not subjecting consumers to unnecessary and unpredictable allowance costs. We do not want to see our customers competing with electricity generators and large industrials for the allowances necessary to heat their homes and cook their food. We believe, and history proves, that programmatic measures uniformly applied can accomplish what we want without the undue costs and complexities of a cap-and-trade system. This approach would not penalize those who acted early, and it is focused on the only things these residential and commercial customers can do—tighten their homes, install efficient appliances and use less wherever possible.

Treatment of Residential and Commercial Natural Gas Customers in a Cap-and-Trade Program

Although we believe programmatic measures are much more appropriate for our customers than cap-and-trade, the following comments are directed at the program proposed in the Waxman/Markey discussion draft.

AGA supports excluding the natural gas residential and commercial sectors from the scope of the cap-and-trade system until 2016 as proposed in the discussion draft bill released March 31, 2009 by Chairmen Waxman and Markey. Between 2012 and 2016 progress toward reducing carbon emissions will continue to be made through efficiency measures without subjecting these consumers to the costs associated with emissions credits for the natural gas that they consume. Such consumer costs would be unlikely to induce significant additional changes in behavior as some might hope.

AGA continues to believe that a sound policy balance on this issue was reflected in the Committee's October 7, 2008, discussion draft bill. Under that proposal residential and commercial natural gas customers would not have been subject to an emissions cap at the outset of the program. Rather, up to the year 2016 these sectors could be covered through aggressive promotion and implementation of various greenhouse gas reduction programs, including, but not limited to, state- or utility-sponsored conservation and efficiency programs, tightened building codes and standards, and appliance efficiency standards. If the residential and commercial natural gas sectors had continued with their historic downward trend in consumption and emissions, under the October discussion draft, they would have remained out of the cap-and-trade system until 2020.

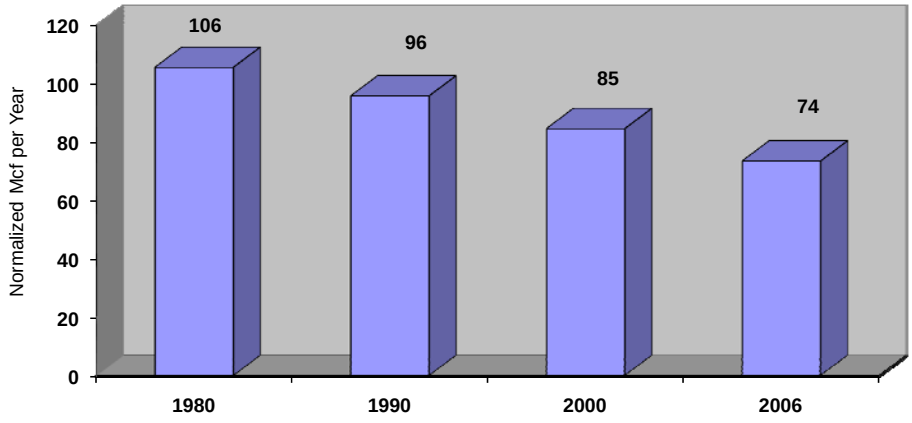
The specific attributes of residential and commercial natural gas customers that warrant this treatment in the context of a greenhouse gas regulation proposal, are enumerated below:

Natural gas is used to meet essential human needs for small-volume customers. The majority of the homes in this country use natural gas, and in this sector 98% of all gas is used for space heating, water heating and cooking, while the remaining 2% is used for clothes drying and other purposes. This fuel is, therefore, used for essential human needs rather than for luxuries.

Residential and commercial natural gas consumption accounts for less than 6% of total U.S. greenhouse gas emissions. Natural gas provides approximately 40% of all energy consumed in the residential and commercial sectors. As noted previously (and discussed more fully below), it is the most efficient and lowest carbon-emitting fossil fuel.

Carbon emissions from residential use of natural gas are already at 1970s levels. While the number of natural gas customers has grown substantially, greenhouse gas emissions have been reduced. In fact, total annual residential natural gas consumption is lower today than it was in the 1970s, despite the fact that the number of natural gas households has increased more than 70% from 38 million to more than 64 million. Customers of natural gas utilities continue to lead the nation in reducing energy consumption and the accompanying greenhouse gas emissions. AGA believes that few, if any, sectors of the economy can claim a comparable record of achievement. Consumption of natural gas in the residential sector, on a national average basis, is shown in the following graph:

NATURAL GAS USE PER RESIDENTIAL CUSTOMER IS DECLINING



The greenhouse gas emission reductions per household experienced during the past four decades are largely attributable to tighter homes and more efficient natural gas appliances. These factors will undoubtedly provide the foundation for continued future reductions in greenhouse gas emissions. Placing small-volume natural gas customers under a cap-and-trade system would make these homes, businesses, schools and hospitals compete (directly or indirectly) with electricity generators and industrial facilities for a limited number of allowances, thereby significantly increasing the energy costs of these consumers.

Natural gas utilities are aggressively promoting decoupled rate structures that allow them to promote conservation and efficiency consistent with shareholder interests. Nearly 40% of all residential natural gas customers are served by gas utilities that have decoupled rates or that are engaged in state proceedings that are presently considering decoupled rates. Rate decoupling is important to energy efficiency and greenhouse gas emissions because it breaks the link between utility revenue recovery and customers' energy consumption.

Natural Gas Utilities Should Receive Adequate Allowances if They are Subject To a Cap

Under the March 31, 2009, discussion draft bill, residential and commercial customers would be placed under cap and trade (with the point of regulation being natural distribution companies) in 2016. The discussion draft is silent for the moment as to the disposition of emissions allowances. AGA believes that most allowances required for residential and commercial natural gas customers should be allocated rather than auctioned, as allocating allowances is the best way to ensure that price impacts on our customers will be minimized. It should be pointed out that local natural gas utilities, as regulated by state public utility commissions, make no profit on natural gas prices when they rise. Similarly they would not make any profit on allocated allowances—allocated allowances would only serve to reduce the price of natural gas to our ultimate customers. The allocation of allowances to local gas utilities should be proportional to their base-year greenhouse gas emissions.

Natural Gas Utilities Should Receive Assurances of Cost Pass-through

Depending upon what Congress ultimately determines as to coverage of natural gas residential and commercial customers and an allocation of allowances for the benefit of these customers, natural gas utilities will at some point be required to purchase allowances for their customers. In functional terms, this will essentially amount to a specific federal charge for the right to consume natural gas, almost entirely for essential human needs as discussed above. AGA believes that the climate change bill should provide that natural gas utilities will be permitted ratemaking treatment to pass on the costs of these credits to their customers.

To the extent that carbon emissions from the use of natural gas by residential and commercial customers of gas distribution utilities are covered under a cap-and-trade program, gas utilities may be required to incur costs (e.g., purchase allowances) to comply with the legislation. Absent a specific directive in the federal legislation, natural gas utilities would only be able to recover from their customers the costs that their state commissions would allow as prudent. In order to ensure that customers bear the environmental compliance costs that were incurred on their behalf, Congress should exercise its authority over interstate commerce and provide in any legislation that costs incurred by a gas utility on behalf of retail customers to comply with this legislation are to be considered prudent and reasonable operating expenses of the gas utility for retail ratemaking purposes and recoverable on a full and current basis, and that state action refusing to permit the pass-through of those costs to retail customers would conflict with federal law.

Any Bill Should Treat Renewable Natural Gas Appropriately

One exciting development in the natural gas industry is the growing production of biogas, also known as renewable gas, which can be produced from landfill and livestock waste. Methane that would otherwise be released from these sources is more than 20 times as potent as CO_2 as a greenhouse gas. To the extent this methane is captured and burned, greenhouse gases are reduced by 95 percent. We are uncertain how the use of renewable gas is treated under the bill, and we do not believe it should be treated as other hydrocarbon fuels. (The same point applies with regard to the treatment of renewable natural gas under the Energy Efficiency Resource Standard, which is discussed below.)

Using Natural Gas in Homes and Businesses is Part of the Climate Change Solution

Many misguidedly believe that because natural gas is a fossil fuel it is one of the causes of greenhouse gas emissions and, as result, a contributing factor to climate change. In fact, however, natural gas is part of the climate change solution. As mentioned previously, natural gas is a fuel that emits low levels of traditional pollutants such as NO_x and SO_x. With regard to greenhouse gas emissions, natural gas, because it has only one carbon atom, emits less carbon when consumed than any other fossil fuel. As a result, natural gas has the potential to be a vehicle to move the nation toward its greenhouse gas reduction goals.

There are significant differences in emissions between natural gas and electricity that fundamentally result from vastly different levels of efficiency. Approximately 90 percent of the energy value in natural gas is delivered to the home. With electricity less than 30 percent of the primary energy value reaches the customer. The largest difference in efficiency for electricity is lost as waste heat at the generating station, as well as line losses in transmission and distribution. These radically different efficiencies produce the significant differences in carbon emissions between electric and natural gas appliances.

The full potential for natural gas efficiencies in the climate change arena is demonstrated most dramatically by the natural gas water heater. The average natural gas water heater emits approximately 1.7 tons of CO_2 per year. In contrast, the average electric water heater results in more than twice as much—3.8 tons per year. The difference between the two could not be more dramatic, and it becomes a multiple of three when the comparison is made between a high-efficiency natural gas water heater and a high-efficiency electric water heater. These numbers are based on national averages, and, as a result, actual differences will vary from area to area.

The same differences in efficiency and emissions follow when comparing an all-electric home with a natural gas home. A typical all-electric home on average produces 10.8 tons of CO_2 per year, while an all-natural gas home produces 7.2 tons of CO_2 per year. Again, these numbers reflect national averages, and actual experience will necessarily differ, but the order of magnitude of difference remains.

The plain consequence is that the nation can reduce its carbon footprint by opting for appliances that use natural gas in direct applications (*i.e.*, where the natural gas is used to heat air, water, or food). There is the opportunity, on a national basis, to reduce carbon emissions by millions upon millions of tons if we utilize more natural gas directly in homes and businesses as the fuel for the future.

Converting small-volume customers to high-efficiency natural gas applications is one of the best ways available today to reduce greenhouse gas emissions. As the example above demonstrates, converting electric resistance water heaters to natural gas can reduce greenhouse gas emissions by one-half to two-thirds. Doing so would have the added benefit of reducing overall energy consumption, costs, and the need to construct new electricity generating plants—a critical problem in a carbon-constrained environment—and electric transmission lines.

AGA Applauds the Inclusion of Carbon Footprint Labeling in Section 213(h)

AGA commends the committee for having recognized the carbon benefits of natural gas and having taken action on it in the discussion draft bill. Section 213(h) of the discussion draft (pages 247-251) would expand the existing Federal Trade Commission EnergyGuide labeling program for home appliances to include carbon footprint information. The current program displays on an appliance label the expected annual operating costs for the appliance (and the range of costs for comparable equipment). The discussion draft would expand this to include expected carbon output associated with use of the appliance.

AGA applauds the inclusion of this provision in the draft bill. As America heads down the path where drastic reductions in carbon output will be a top national priority, giving consumers this carbon output information will provide them with essential information for playing their part in achieving this national priority. Moreover, implementing this step is virtually cost free. The new program would apply to appliances covered by the existing program. The data for calculating carbon footprint is available. No additional manufacturing cost is involved. Labels are already required, so the additional labeling cost will be nominal for appliance manufacturers. Thus, this provision offers an opportunity to provide consumers with important information to factor into their purchasing decisions with virtually no additional cost for doing so.

A national requirement for carbon-footprint labeling would lead to a uniform standard for providing this information to consumers. It would also avert the possibility of individual manufacturers establishing their own methodologies for doing so, the result of which would be conflicting information and potentially misleading claims as to a carbon footprint.

Making carbon footprint information available to consumers will assist them in determining which appliance option has the lowest total environmental impact. The information currently included on the EnergyGuide label does not provide a means for finding the most carbon-efficient appliance. In particular, when consumers are empowered to make more efficient choices, manufacturers – and all energy industry actors – will feel increased pressure and competition to provide more efficient supply.

Section 213(h) Should Be Expanded To Include Carbon Labeling for Buildings

As mentioned above, energy efficiency in the residential and commercial sector has, over the last 30 years, been driven primarily by improvements in appliance efficiency and improvements in building envelopes. Further carbon reductions in this sector, at least over the next several decades, will continue to come principally from these types of activities. The carbon footprint labeling for appliances called for in Section 213(h) of the discussion draft bill is a step in the right direction as to appliances.

AGA believes that it would be appropriate and productive to expand the scope of Section 213(h) to include buildings as well. As noted, building efficiency is a principal driver in energy efficiency. Approximately 40 percent of all energy is consumed with regard to buildings. As we go forward, building efficiency will have a similar role with regard to reducing carbon. As with appliances, requiring carbon footprint labels with respect to buildings would be a very low-cost means to provide consumers with important information for making the choices that will ultimately determine whether the United States will reduce its carbon footprint to the degree scientists believe will be necessary to avert global warming.

AGA is presently crafting a legislative proposal to require carbon footprint labeling for buildings. We expect to be in contact in the very near future with committee staff to discuss this.

Appliance Minimum Efficiency Rules Should Include Carbon Information and Impacts

AGA believes that, as the nation tackles the goal of reducing carbon, additional changes to the way in which we have addressed energy efficiency are necessary. While the Department of Energy (DOE) acknowledges the carbon impact of its appliance efficiency standards, it should also be directly considering CO_2 emissions associated with appliances as a part of the rulemaking process in which it establishes minimum efficiency standards. Integrating CO_2 emissions into the decision making process would provide DOE with more complete information with which to consider the full range of appliance efficiency options. Current federal law covering appliance efficiency does not direct DOE to this end, mainly because the appliance efficiency rulemaking process is restricted, by statute, to consideration of a narrow set of energy measurements or "descriptors."

AGA is in the process of crafting a legislative proposal to this end—that would expand the currently used energy descriptors to include CO_2 emissions in the rating of appliance efficiency. The addition of CO_2 in the rating of appliances coupled with new standard levels would provide more direct consideration of carbon impacts in the analysis of appliance energy use. This additional authority given to the DOE could provide immediate benefits in assisting federal energy policies toward a lower carbon economy.

The Energy Efficiency Resource Standard Provision Seeks to Reach a Laudable Goal but by a Very Imperfect Route

AGA and its member companies are committed to continuing to press for energy efficiency, in order to save our customers money, to maximize the utility of our natural resources, and to reduce the carbon emissions of our nation. As noted above, there is a growing, and accelerating, trend toward decoupled natural gas utility rates. Such approaches, by breaking the link between customer energy consumption and utility revenues help utilities become full partners in the quest for energy efficiency. Moreover, most natural gas utilities today participate in, or even operate, energy efficiency programs. On a national scale they collectively deployed $500 million in 2007 for this purpose—an amount that we expect to double in the next several years.

Furthermore, as discussed above, natural gas residential and commercial customers have led the way in efficiency and carbon-reduction over the last thirty years. These customers have reduced their annual consumption by 1% or more annually from 1980 to 2000 and about 2% annually since 2000. AGA member companies will continue to work with their customers to ensure a continuation of this trend, although it will become increasingly difficult to do so as the least costly measures have, in many cases, already been taken. Again, the goals of this program, similar to the goals of the climate change program, would be best met through universally applied building codes and appliance standards, supplemented by a variety of education and incentive programs. This approach, as stated previously, would not unduly penalize the early actions of more aggressive companies.

In contrast to the preferred programmatic approach noted above, Section 231 of the discussion draft bill proposes to establish an "energy efficiency resource standard" (EERS) for both electric utilities and natural gas utilities. As it would apply to natural gas utilities, the EERS would, in the most essential terms, require the customers of a natural gas utility to reduce their consumption of natural gas by 10% between 2012 and 2020 or the utility will be require to pay a penalty of $5 per MMBtu for each MMBtu by which they fall short of the target.

While the end is a laudable one, the construct and means are fraught with problems. Unfortunately the conversation on this topic has, to this point, largely occurred among proponents of the idea. A serious and thorough vetting of such a dramatic proposal will be necessary by all parties interested in advancing energy efficiency. Such a program can only be workable, if at all, with significant input from the natural gas utilities involved. If adequate federal and state funding is available, local gas utilities are positioned to work with the states and their customers to develop and implement effective energy saving programs. However, for this approach to be successful, utilities must be allowed to earn a return for their contribution, not merely be subject to penalties.

AGA suggests that the proposed means outlined in Section 231 to the desired end is a minefield for both utilities and their customers. While we will not enumerate all the difficulties with Section 231, we will outline below a few that should suffice to illustrate that this concept still needs further in-depth analysis before becoming a policy pillar that can be relied upon in the quest to increase energy efficiency and reduce carbon

emissions. Additionally, the discussion above should make clear that, from 30 years of experience, we have a wealth of knowledge as to the programmatic measures that can be employed to reach the desired end of increased energy efficiency.

Utilities Can Influence, But Do Not Control, the Consumption of Their Customers

The fundamental scheme of the EERS is that customers must reduce their consumption, and natural gas utilities must pay the penalty if they do not. Without question there are many actions that natural gas utilities can take—and do take—to encourage energy efficiency. But they cannot adjust customers' thermostats, close open windows, or unilaterally install additional insulation or new appliances in their homes. While utilities can influence the conduct of their customers through education and publicity campaigns, appliance rebate and weatherization programs, incentives for efficient appliances, and the like, they cannot control the actions of their customers, which is what is ultimately measured by the EERS mechanism. AGA believes that sound policy argues instead for a program that provides carrots, not sticks, for the entities whose behavior is to be influenced. If the goal is to reduce energy consumption, the policy mechanisms to be employed should focus on the efficiency drivers that have proven successful in the past and are likely to be so in the future. This lack of control is further exacerbated in the industrial market, where most customers are sophisticated energy consumers who do not purchase their gas supplies from the utility and are thus transport-only customers.

The EERS Fails to Account for the Needs of Economic Growth and Development

One of our national goals is certainly to facilitate a growing and vibrant economy and the jobs that necessarily follow from that. A growing economy requires that America's energy industries expand to meet the needs of the growing economy—both businesses and citizens. Moreover, as a matter of national policy we should be seeking to attract new industry to the United States, both for the jobs it provides as well as for the stimulative effect on the economy as a whole. The concept of the EERS, as well as the construct used for it here, runs contrary to these overarching national goals.

As drafted, the EERS provision in the discussion draft calls for a 10% decrease in consumption by natural gas utility customers by the year 2020. The reduction is to be achieved by all customers taken as a group (although excluding electric generation customers). In a number of areas of the United States, population is growing and the economy has been expanding over the last decade or so. More importantly, new applications such as natural gas vehicles in commercial fleets, which provide a clean and domestic alternative to gasoline, would be much less likely to grow. As now framed, the EERS provision would appear to place these utilities in a very difficult position in terms of achieving the goal of the 10% reduction.

AGA recognizes that the EERS mechanism attempts to utilize some sort of comparative mechanism, analyzing a base case against actual experience. This is troublesome in its own right, but even if it were to be employed, the practical difficulty is that a utility will be faced with ensuring the accuracy of its base case as to projected

customer growth or face an *ex post facto* penalty. This hardly seems fair, and it is does not appear to be a wise grounding for what will ultimately be an important efficiency policy.

The EERS Fails to Account for Carbon-Driven Fuel Switching

One of the core issues with the EERS is that it is proposed to be overlaid on a cap-and-trade scheme. This is something of a two-fisted approach with a definite potential for conflict and unintended consequences. AGA urges the committee to give careful thought to whether an EERS together with a cap-and-trade scheme will result in conflicting goals.

One particular instance greatly concerns AGA. If we assume that the nation adopts a cap-and-trade (or some other) carbon regulation system in the near future, the result, when implemented, will be to place a price on carbon. When carbon markets are functioning efficiently, at least in the relatively near term, residential customers will begin to recognize that by shifting their water heating, space heating, and cooking to natural gas (where such service is available). They will save money and reduce CO_2 emissions. This will result from the fact that natural gas will have a lower carbon output and price than electricity in most areas. Moreover, we expect that states, for a variety of reasons (state carbon footprint, the job development aspects of reasonable energy prices, and the need to minimize new, expensive electric capacity), will encourage customers to migrate toward natural gas, direct application appliances. In any event, for whatever reason undertaken, we believe that these trends are likely and that the result will be a good one: lower overall energy consumption, energy costs, and carbon emissions for the United States.

Under the EERS, however, the natural gas utility would pay the $5 per MMBtu penalty because its customers will have increased their usage of natural gas instead of reducing it in order to achieve greater overall energy efficiency, lower energy bills, and reduced carbon emissions. This hardly seems like the outcome we should be seeking to achieve. It is, moreover, a plausible—indeed likely—that scenario where the goals of a cap-and-trade system and EERS overlap they will produce conflicting results. Given the complexity of the two regulatory schemes, we do not think that this is the only scenario in which the two systems may collide.

The Mechanics of the EERS are Problematic

The EERS seems to be grounded in a concept of energy savings that are the "result" of specific actions of one kind or another. This approach is problematic in that it is unduly vague and susceptible to widely differing interpretation and application. For example, assume a home owner reduces consumption of natural gas. Was this caused by a utility program for weatherization or the fact that children grew up and left home for school? These types of imponderables are numerous within the scheme of this provision. It must be understood and appreciated that natural gas utilities have limited knowledge about what goes on "behind the meter" – we do not have the ability or the right to obtain perfect information inside the home or business.

The provision has at its core a comparison between a "business-as-usual" projection and measures implemented after the bill becomes law that "cause" natural gas savings. Projecting a "business-as-usual scenario into the future, especially when a new scheme of carbon regulation has been implemented, could be dicey to say the least. Will DOE issue regulations providing detailed guidance as to how this should be done? How will projections of economic growth and development be factored into this "business-as-usual" scenario? How will natural gas utilities predict the degree of fuel switching to natural gas resulting from pricing the externality of carbon? What will be the factors to determine whether "savings" resulted from utility actions?

At its core, these aspects of this proposed mechanism are troublesome and, frankly, strike fear in the hearts of AGA member companies when the risk of error, misjudgment, or interpretation is a penalty (or stick) of $5 per MMBtu. In the end, predictions can only be correct as a matter of accident. Given this truism, it is fundamentally unfair to have the Damocles sword of this penalty provision hanging over head, perhaps with the penalty determination ultimately made, long after the fact, by an individual in the depths of a federal agency. Again, we think sounder policy is to identify the goal and provide incentives to reach it rather than *ex post facto* penalties for failing to achieve it.

For years after 2020 DOE may set future years standards that turn on "cost-effective energy efficiency potential." Yet "cost-effective" is defined so broadly as to be nearly meaningless.

We could go on in enumerating concerns with the EERS methodology employed in the bill. The examples given above, however, amply demonstrate that this is a thicket into which we should not wander. As AGA has stated in many forums, if the goal is to achieve greenhouse gas reductions—and surely it is—then we have an ample record on how to reach that end. And the end sought by the EERS provision is a laudable one and, with the correct complementary policies, in all likelihood an achievable one.

AGA undertakes to work with the committee to develop a suite of policies that can achieve the goals sought by this provision.

AGA and its members appreciate the opportunity to present their views on these important subjects. We look forward to working with the committee and its staff to be a constructive voice in this important national conversation.